

PharMerica CORP  
Form 10-Q  
August 02, 2013  
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**UNITED STATES**  
**SECURITIES AND EXCHANGE COMMISSION**

Washington, DC 20549

**FORM 10-Q**

(Mark One)

**QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**  
For the quarterly period ended June 30, 2013

or

**TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**  
For the transition period from \_\_\_\_\_ to \_\_\_\_\_.

Commission File Number: 001-33380

**PHARMERICA CORPORATION**

(Exact name of registrant as specified in its charter)

**Delaware**  
(State or Other Jurisdiction of

Incorporation or Organization)

1901 Campus Place

**87-0792558**  
(I.R.S. Employer

Identification No.)

40299

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**Louisville, KY**  
(Address of Principal Executive Offices)

(Zip Code)

**(502) 627-7000**

**(Registrant's Telephone Number, Including Area Code)**

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

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

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

Large accelerated filer  Accelerated filer  Non-accelerated filer  Smaller reporting company   
(Do not check if a 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

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

**Class of Common Stock**  
Common stock, \$0.01 par value

**Outstanding at July 26, 2013**  
29,772,037 shares

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**PHARMERICA CORPORATION**

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## PHARMERICA CORPORATION

## CONDENSED CONSOLIDATED INCOME STATEMENTS

For the Three and Six Months Ended June 30, 2012 and 2013

(Unaudited)

(In millions, except share and per share amounts)

	Three Months Ended June 30		Six Months Ended June 30	
	2012	2013	2012	2013
Revenues	\$ 458.5	\$ 430.8	\$ 957.4	\$ 870.6
Cost of goods sold	382.6	348.2	808.9	703.7
Gross profit	75.9	82.6	148.5	166.9
Selling, general and administrative expenses	54.9	55.5	107.3	112.2
Amortization expense	3.0	3.9	5.8	8.0
Merger, acquisition, integration costs and other charges	2.8	2.8	8.2	5.7
Hurricane Sandy disaster costs		(0.9)		(0.3)
Operating income	15.2	21.3	27.2	41.3
Interest expense, net	2.5	2.9	5.2	5.5
Income before income taxes	12.7	18.4	22.0	35.8
Provision for income taxes	5.1	8.2	8.8	15.1
Net income	\$ 7.6	\$ 10.2	\$ 13.2	\$ 20.7
Earnings per common share:				
Basic	\$ 0.26	\$ 0.34	\$ 0.45	\$ 0.70
Diluted	\$ 0.26	\$ 0.34	\$ 0.44	\$ 0.69
Shares used in computing earnings per common share:				
Basic	29,489,766	29,713,010	29,459,978	29,640,388
Diluted	29,720,403	30,134,944	29,735,489	30,141,730

See accompanying Notes to Condensed Consolidated Financial Statements

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**PHARMERICA CORPORATION**  
**CONDENSED CONSOLIDATED BALANCE SHEETS**

As of December 31, 2012 and June 30, 2013

(Unaudited)

(In millions, except share and per share amounts)

	(As Adjusted) December 31, 2012	June 30, 2013
<b>ASSETS</b>		
Current assets:		
Cash and cash equivalents	\$ 12.3	\$ 12.3
Accounts receivable, net	206.6	195.3
Inventory	135.7	113.2
Deferred tax assets, net	36.7	35.4
Prepays and other assets	38.8	40.8
	430.1	397.0
Equipment and leasehold improvements	158.8	169.7
Accumulated depreciation	(105.7)	(112.4)
	53.1	57.3
Goodwill	268.5	268.5
Intangible assets, net	121.9	116.3
Other	12.7	11.2
	\$ 886.3	\$ 850.3
<b>LIABILITIES AND STOCKHOLDERS EQUITY</b>		
Current liabilities:		
Accounts payable	\$ 49.7	\$ 41.4
Salaries, wages and other compensation	35.8	35.5
Current portion of long-term debt	12.5	12.5
Income taxes payable	1.5	7.4
Other accrued liabilities	7.6	7.7
	107.1	104.5
Long-term debt	303.0	244.6
Other long-term liabilities	22.5	23.1
Deferred tax liabilities	11.1	12.7
Commitments and contingencies (See Note 6)		
Stockholders' equity:		
Preferred stock, \$0.01 par value per share; 1,000,000 shares authorized and no shares issued, December 31, 2012 and June 30, 2013		
Common stock, \$0.01 par value per share; 175,000,000 shares authorized; 30,943,748 and 31,355,900 shares issued as of December 31, 2012 and June 30, 2013, respectively	0.3	0.3

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Capital in excess of par value	363.0	367.0
Retained earnings	91.3	112.0
Treasury stock at cost, 1,456,293 and 1,585,366 shares at December 31, 2012 and June 30, 2013, respectively	(12.0)	(13.9)
	442.6	465.4
	\$ 886.3	\$ 850.3

See accompanying Notes to Condensed Consolidated Financial Statements

**Table of Contents****PHARMERICA CORPORATION****CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS****For the Three and Six Months Ended June 30, 2012 and 2013****(Unaudited)****(In millions)**

	<b>Three Months Ended June 30</b>		<b>Six Months Ended June 30</b>	
	<b>2012</b>	<b>2013</b>	<b>2012</b>	<b>2013</b>
<b>Cash flows provided by (used in) operating activities:</b>				
Net income	\$ 7.6	\$ 10.2	\$ 13.2	\$ 20.7
<b>Adjustments to reconcile net income to net cash provided by (used in) operating activities:</b>				
Depreciation	4.5	4.8	9.3	9.6
Amortization	3.0	3.9	5.8	8.0
Merger, acquisition, integration costs and other charges	0.3		1.9	
Hurricane Sandy disaster costs		(1.0)		(1.6)
Stock-based compensation and deferred compensation	1.2	1.8	3.0	4.0
Amortization of deferred financing fees	0.2	0.7	0.4	1.0
Deferred income taxes	3.4	(0.7)	6.0	2.9
Gain on disposition of equipment		(0.1)	(0.1)	(0.1)
Other	0.2	0.2		0.3
<b>Change in operating assets and liabilities:</b>				
Accounts receivable, net	25.0	11.5	12.9	10.3
Inventory	(4.9)	(13.0)	21.6	22.5
Prepays and other assets	(2.3)	(2.4)	(2.8)	1.0
Accounts payable	(11.0)	4.7	(18.0)	(7.9)
Salaries, wages and other compensation	1.9	2.1	(4.6)	(2.7)
Other accrued liabilities	2.8	3.9	3.2	6.3
<b>Net cash provided by operating activities</b>	<b>31.9</b>	<b>26.6</b>	<b>51.8</b>	<b>74.3</b>
<b>Cash flows provided by (used in) investing activities:</b>				
Purchase of equipment and leasehold improvements	(4.4)	(7.3)	(6.9)	(14.0)
Acquisitions, net of cash acquired	(0.4)		(0.4)	(0.5)
Cash proceeds from the sale of assets	0.2	0.1	0.3	0.1
<b>Net cash used in investing activities</b>	<b>(4.6)</b>	<b>(7.2)</b>	<b>(7.0)</b>	<b>(14.4)</b>
<b>Cash flows provided by (used in) financing activities:</b>				
Repayments of long-term debt		(3.2)		(6.3)
Net activity of long-term revolving credit facility	(22.1)	(11.6)	(50.0)	(52.1)
Repayments of capital lease obligations			(0.1)	
Issuance of common stock	0.1	0.3	0.1	0.4
Treasury stock at cost		(0.1)	(0.2)	(1.9)
Excess tax benefit from stock-based compensation		0.2		0.4
Other		(0.5)		(0.4)
<b>Net cash used in financing activities</b>	<b>(22.0)</b>	<b>(14.9)</b>	<b>(50.2)</b>	<b>(59.9)</b>
<b>Change in cash and cash equivalents</b>	<b>5.3</b>	<b>4.5</b>	<b>(5.4)</b>	

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Cash and cash equivalents at beginning of period	6.7	7.8	17.4	12.3
Cash and cash equivalents at end of period	\$ 12.0	\$ 12.3	\$ 12.0	\$ 12.3
Supplemental information:				
Cash paid for interest	\$ 2.2	\$ 2.3	\$ 5.0	\$ 4.6
Cash paid for taxes	\$ 0.9	\$ 5.9	\$ 2.2	\$ 6.4

See accompanying Notes to Condensed Consolidated Financial Statements



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**PHARMERICA CORPORATION**  
**CONDENSED CONSOLIDATED STATEMENT OF STOCKHOLDERS' EQUITY**

**For the Six Months Ended June 30, 2013**

**(Unaudited)**

**(In millions, except share amounts)**

	Common Stock Shares	Common Stock Amount	Capital in Excess of Par Value	Retained Earnings	Treasury Stock	Total
Balance at December 31, 2012	29,487,455	\$ 0.3	\$ 363.0	\$ 91.3	\$ (12.0)	\$ 442.6
Net income				20.7		20.7
Exercise of stock options and tax components of stock-based awards, net	33,266		0.4			0.4
Vested restricted stock units	316,339					
Vested performance stock units	62,547					
Treasury stock at cost	(129,073)				(1.9)	(1.9)
Stock-based compensation - non-vested restricted stock			3.0			3.0
Stock-based compensation - stock options			0.6			0.6
Balance at June 30, 2013	29,770,534	\$ 0.3	\$ 367.0	\$ 112.0	\$ (13.9)	\$ 465.4

See accompanying Notes to Condensed Consolidated Financial Statements

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**PHARMERICA CORPORATION**

**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**

**(Unaudited)**

**NOTE 1 ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**

*Nature of Business*

PharMerica Corporation (together with its subsidiaries, the Corporation) is an institutional pharmacy services company that services healthcare facilities, provides pharmacy management services to hospitals and also provides specialty infusion services to patients outside a hospital setting. The Corporation is the second largest institutional pharmacy services company in the United States based on revenues, operating 90 institutional pharmacies and 12 specialty infusion pharmacies in 45 states. The Corporation's customers are typically institutional healthcare providers, such as skilled nursing facilities, nursing centers, assisted living facilities, hospitals, individuals receiving in-home care and other long-term alternative care settings. The Corporation is generally the primary source of supply of pharmaceuticals to its customers. The Corporation also provides pharmacy management services to 89 hospitals in the United States.

*Operating Segments*

The Corporation consists of two operating segments: pharmacy and specialty infusion services. For financial reporting purposes, management considers these two operating segments to be similar and, therefore, has aggregated them into a single reportable segment.

*Principles of Consolidation*

All intercompany transactions have been eliminated.

*Basis of Presentation*

The accompanying condensed consolidated financial statements have been prepared in accordance with the instructions to Form 10-Q and Article 10 of Regulation S-X and do not include all of the information and disclosures required by generally accepted accounting principles in the United States (U.S. GAAP) for complete financial statements. Accordingly, the accompanying condensed consolidated financial statements should be read in conjunction with the consolidated financial statements of the Corporation and related footnotes for the year ended December 31, 2012, included in the Corporation's Annual Report on Form 10-K. The balance sheet as of December 31, 2012 has been derived from the audited consolidated financial statements adjusted for acquisition related measurement period adjustments as of that date but does not include all of the information and footnotes required by U.S. GAAP for complete financial statements.

The results of operations for the interim periods are not necessarily indicative of results of operations for a full year. It is the opinion of management that all necessary adjustments for a fair presentation of the condensed consolidated financial statements for the interim periods have been made and are of a normal recurring nature.

*Use of Estimates*

The accompanying condensed consolidated financial statements have been prepared in accordance with U.S. GAAP which requires management to make estimates and assumptions that affect the reported amounts of assets, liabilities and disclosure of contingent liabilities as of the date of the condensed consolidated financial statements and the reported amounts of revenues and expenses during the reporting periods. Significant estimates are involved in collectability of accounts receivable, revenue recognition, inventory valuation, supplier rebates, the valuation of long-lived assets and goodwill and accounting for income taxes. Actual amounts may differ from these estimates.

*Cash and Cash Equivalents*

Cash and cash equivalents consist of cash on hand and cash equivalents with original maturities of three months or less. As of December 31, 2012 and June 30, 2013, the Corporation did not hold a material amount of funds in cash equivalent money market accounts. Management believes it effectively safeguards cash assets.



**Table of Contents****PHARMERICA CORPORATION****NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)****(Unaudited)****NOTE 1 ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)***Fair Value of Financial Instruments*

Fair value is an exit price, representing the amount that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants. As such, fair value is a market-based measurement that should be determined based upon assumptions that market participants would use in pricing an asset or liability. As a basis for considering such assumptions, the Corporation follows a three-tier fair value hierarchy, which prioritizes the inputs used in measuring fair value as follows:

Level 1: Observable inputs such as quoted prices in active markets;

Level 2: Inputs, other than quoted prices in active markets, that are observable either directly or indirectly; and

Level 3: Unobservable inputs in which there is little or no market data, which require the Corporation to develop its own assumptions.

Assets and liabilities measured at fair value are based on one or more of the following three valuation techniques:

- A. *Market approach*: Prices and other relevant information generated by market transactions involving identical or comparable assets or liabilities.
- B. *Cost approach*: Amount that would be required to replace the service capacity of an asset (replacement cost).
- C. *Income approach*: Techniques to convert future amounts to a single present amount based upon market expectations (including present value techniques, option-pricing and excess earnings models).

The financial liability recorded at fair value at December 31, 2012 and June 30, 2013 is set forth in the tables below (dollars in millions):

<b>As of December 31, 2012</b>	<b>Liability</b>	<b>Level 1</b>	<b>Level 2</b>	<b>Level 3</b>	<b>Valuation Technique</b>
<i>Financial Liability</i>					
Deferred Compensation Plan	\$ 4.8	\$	\$ 4.8	\$	A
<b>As of June 30, 2013</b>					
<i>Financial Liability</i>					
Deferred Compensation Plan	\$ 5.8	\$	\$ 5.8	\$	A

The deferred compensation plan liability represents an unfunded obligation associated with the deferred compensation plan offered to eligible employees and members of the Board of Directors of the Corporation and is recorded in other long-term liabilities in the condensed consolidated balance sheets. The fair value of the liability associated with the deferred compensation plan is derived using pricing and other relevant

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information for similar assets or liabilities generated by market transactions.

The carrying amounts reported in the accompanying condensed consolidated balance sheets for cash and cash equivalents, accounts receivable, inventory and accounts payable approximate fair value because of the short-term maturity of these assets and liability. The Corporation's debt approximates fair value due to the terms of the interest being set at variable market interest rates (Level 2).

### *Accounts Receivable and Allowance for Doubtful Accounts*

Accounts receivable primarily consist of amounts due from Prescription Drug Plans ( PDPs ) under Medicare Part D, institutional healthcare providers, the respective state Medicaid programs, third party insurance companies, and private payers. The Corporation's ability to collect outstanding receivables is critical to its results of operations and cash flows. To provide for accounts receivable that could become uncollectible in the future, the Corporation establishes an allowance for doubtful accounts to reduce the carrying value of such receivables to the extent it is probable that a portion or all of a particular account will not be collected.

**Table of Contents****PHARMERICA CORPORATION****NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)****(Unaudited)****NOTE 1 ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)**

The Corporation has an established process to determine the adequacy of the allowance for doubtful accounts, which relies on analytical tools, specific identification, and benchmarks to arrive at a reasonable allowance. No single statistic or measurement determines the adequacy of the allowance for doubtful accounts. The Corporation monitors and reviews trends by payer classification along with the composition of the Corporation's aging accounts receivable. This review is focused primarily on trends in private and other payers, PDP's, dual eligible co-payments, historic payment patterns of long-term care institutions, and monitoring respective credit risks. In addition, the Corporation analyzes other factors such as revenue days in accounts receivable, denial trends by payer types, payment patterns by payer types, subsequent cash collections, and current events that may impact payment patterns of the Corporation's long-term care institution customers. Accounts receivable are written off after collection efforts have been completed in accordance with the Corporation's policies.

The Corporation's accounts receivable and summarized aging categories are as follows (dollars in millions):

	(As Adjusted) December 31, 2012	June 30, 2013
Institutional healthcare providers	\$ 158.1	\$ 155.7
Medicare Part D	41.6	33.9
Private payer and other	28.4	29.1
Insured	16.8	15.7
Medicaid	16.1	14.7
Medicare	2.0	1.8
Allowance for doubtful accounts	(56.4)	(54.8)
	\$ 206.6	\$ 196.1*
0 to 60 days	58.8%	58.0%
61 to 120 days	17.1%	18.2%
Over 120 days	24.1%	23.8%
	100.0%	100.0%

\* Includes \$0.8 million of notes receivable for Institutional healthcare providers which is included in other long term assets on the condensed consolidated balance sheets.

The following is a summary of activity in the Corporation's allowance for doubtful accounts (dollars in millions):

Beginning Balance	Charges to Costs and Expenses	Write-offs	Ending Balance
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Allowance for doubtful accounts:				
Year ended December 31, 2012	\$ 48.6	\$ 25.9	\$ (18.1)	\$ 56.4
Six months ended June 30, 2013	56.4	10.7	(12.3)	54.8

### *Concentration of Credit Risk*

For the three months ended June 30, 2012 and 2013, the Corporation derived approximately 14.2% and 12.7%, respectively, of its revenues from a single customer, including all payer sources of the Corporation. For the six months ended June 30, 2012 and 2013, the Corporation derived approximately 14.0% and 13.6%, respectively, of its revenues from a single customer, including all payer sources of the Corporation.

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The Corporation capitalizes financing fees related to acquiring or issuing new debt instruments. These expenditures include bank fees and premiums, legal costs, and filing fees. The Corporation amortizes these deferred financing fees using the effective interest method on fees associated with the term debt and the straight-line method for fees associated with the revolving credit facility.

*Inventory*

Inventory is primarily located at the Corporation's pharmacy locations. Inventory consists solely of finished products (primarily prescription drugs) and is valued at the lower of first-in, first-out cost ( FIFO ) or market. Physical inventories are performed on a quarterly basis at the end of the quarter at all pharmacy sites. Cost of goods sold is adjusted based upon the results of the physical inventory counts.

*Equipment and Leasehold Improvements*

Equipment and leasehold improvements are recorded at cost on the acquisition date and are depreciated using the straight-line method over their estimated useful lives or lease term, if shorter, as follows (in years):

	<b>Estimated Useful Lives</b>
Leasehold improvements	1-7
Equipment and software	3-10

Expenditures for maintenance, repairs and renewals of minor items are expensed as incurred. Major rebuilds and improvements are capitalized. For the three months ended June 30, 2012 and 2013, maintenance and repairs were \$1.9 million and \$2.3 million, respectively. For the six months ended June 30, 2012 and 2013, maintenance and repairs were \$3.9 million and \$5.0 million, respectively.

Long-lived assets are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset or asset group may not be recoverable. Recoverability of long-lived assets is assessed by a comparison of the carrying amount of the asset or asset group to the estimated future undiscounted net cash flows expected to be generated by the asset or group of assets. If estimated future undiscounted net cash flows are less than the carrying amount of the asset or group of assets, the asset is considered impaired and an expense is recorded in an amount required to reduce the carrying amount of the asset or asset group to its then fair value. The Corporation did not record impairment charges on equipment and leasehold improvements for the six months ended June 30, 2012 or 2013.

The Corporation's equipment and leasehold improvements are further described in Note 3.

*Capitalization of Internal Software Costs*

The Corporation capitalizes the costs incurred during the application development stage, which includes costs to design the software configuration and interfaces, coding, installation, and testing. Costs incurred during the preliminary project stage along with post-implementation stages of internal use computer software are expensed as incurred. Capitalized development costs are amortized generally over three years and are subject to impairment evaluations. Costs incurred to maintain existing software development are expensed as incurred. The capitalization and ongoing assessment of recoverability of development costs requires judgment by management with respect to certain



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external factors, including, but not limited to, technological and economic feasibility and estimated economic life. For the three months ended June 30, 2012 and 2013, the Corporation capitalized internally developed software costs of \$1.5 million and \$3.6 million, respectively. For the six months ended June 30, 2012 and 2013, the Corporation capitalized internally developed software costs of \$2.4 million and \$6.5 million, respectively. As of December 31, 2012 and June 30, 2013, net capitalized software costs, including acquired assets and amounts for projects which have not been completed, totaled \$16.6 million and \$15.6 million, respectively.

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**Table of Contents****PHARMERICA CORPORATION****NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)****(Unaudited)****NOTE 1 ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)***Goodwill and Other Intangibles*

Goodwill represents the excess purchase price of an acquired entity over the net amounts assigned to assets acquired and liabilities assumed. The Corporation's policy is to perform a qualitative assessment on goodwill impairment to determine whether it is more likely than not (defined as having a likelihood of more than 50 percent) that the fair value of a reporting unit is less than its carrying amount as a basis for determining whether it is necessary to perform the two-step goodwill impairment test. The Corporation performed a qualitative assessment as of December 31, 2012 and did not find it necessary to perform the first step of the two-step impairment test based on that analysis. In addition, as a result of the Corporation being notified during May 2013 that it will be losing its largest customer effective December 31, 2013, the Corporation performed the first step of the two step analysis for the pharmacy segment during the quarter ended June 30, 2013 and determined that an impairment of goodwill did not occur as a result of this triggering event. The Corporation's discounted cash flows as calculated for the step one analysis were approximately 26% greater than current book value.

The Corporation's finite-lived intangible assets are comprised primarily of trade names, customer relationship assets and non-compete agreements primarily originating from business acquisitions. Finite-lived intangible assets are amortized on a straight-line basis over the course of their lives ranging from 5 to 20 years. For impairment reviews, intangible assets are reviewed on a specific pharmacy basis or as a group of pharmacies depending on the intangible assets under review. The Corporation's goodwill and intangible assets are further described in Note 4.

*Self-Insured Employee Health Benefits*

The Corporation is self-insured for the majority of its employee health benefits. The Corporation's self-insurance for employee health benefits includes a stop-loss policy to limit the maximum potential liability of the Corporation for both individual and aggregate claims per year. The Corporation records a monthly expense for self-insurance based on historical claims data and inputs from third-party administrators. For the three months ended June 30, 2012 and 2013, the expense for employee health benefits was \$6.0 million and \$5.6 million, respectively, and for the six months ended June 30, 2012 and 2013 the expense for employee health benefits was \$11.5 million and \$11.1 million, respectively, the majority of which was related to its self-insured plans. As of December 31, 2012 and June 30, 2013, the Corporation had \$3.3 million and \$3.4 million, respectively, recorded as a liability for self-insured employee health benefits.

*Supplier Rebates*

The Corporation receives rebates on purchases from its vendors and suppliers for achieving market share or purchase volumes. Rebates for brand name products are generally based upon achieving a defined market share tier within a therapeutic class and can be based on either purchasing volumes or actual prescriptions dispensed. Rebates for generic products are primarily based on achieving purchasing volume requirements. The Corporation generally accounts for these rebates and other incentives received from its vendors and suppliers, relating to the purchase or distribution of inventory, on an accrual basis as a reduction of cost of goods sold and inventory. The estimated accrual is adjusted, if necessary, after the third party validates the appropriate data and notifies the Corporation of its agreement under the terms of the contract. The Corporation considers these rebates to represent product discounts, and as a result, the rebates are allocated as a reduction of product cost and relieved through cost of goods sold upon the sale of the related inventory or as a reduction of inventory for drugs which have not yet been sold.

*Delivery Expenses*

The Corporation incurred delivery expenses of \$15.8 million and \$15.2 million for the three months ended June 30, 2012 and 2013, respectively, and \$32.1 million and \$30.9 million for the six months ended June 30, 2012 and 2013, respectively, to deliver products sold to its customers. Delivery expenses are reported as a component of cost of goods sold in the accompanying condensed consolidated income statements.

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### *Stock Option Accounting*

The Corporation recognizes stock-based compensation expense in its condensed consolidated financial statements using the Black-Scholes-Merton option valuation model (see Note 10).

**Table of Contents****PHARMERICA CORPORATION****NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)****(Unaudited)****NOTE 1 ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)***Income Taxes*

Deferred tax assets and liabilities are recognized for the future tax consequences attributable to temporary differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax basis. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. The Corporation accrues for tax obligations, as appropriate, based on facts and circumstances in the various regulatory environments. Deferred tax assets and liabilities are more fully described in Note 11.

*Measurement Period Adjustments*

For the six months ended June 30, 2013, the Corporation has adjusted certain amounts on the condensed consolidated balance sheet as of December 31, 2012 as a result of measurement period adjustments related to the Amerita acquisition (See Note 2).

**NOTE 2 ACQUISITIONS***2012 Acquisitions**Amerita Acquisition*

On December 13, 2012 the Corporation, through a wholly-owned subsidiary, acquired all of the outstanding stock of Amerita, Inc., a Delaware corporation ( Amerita ), for \$84.5 million, net of cash acquired of \$1.0 million, including the working capital adjustment in the first quarter of 2013. During the six months ended June 30, 2013, the final working capital adjustment was completed for the Amerita acquisition resulting in additional purchase price paid of \$0.5 million. The Corporation's primary purpose in acquiring Amerita, Inc. was to complement existing pharmacy services through the provision of additional infusion services. The total purchase price of Amerita was allocated to the net tangible and identifiable intangible assets based upon their fair values on December 13, 2012. The excess of the purchase price over the fair values of the net tangible and identifiable intangible assets was recorded as goodwill. The Corporation believes the resulting amount of goodwill reflects its expectation of the synergistic benefits of the acquisition. For tax purposes, the transaction was considered a stock acquisition. Approximately \$15.9 million of goodwill related to previous acquisitions made by Amerita will be tax deductible by the Corporation.

The preliminary allocation of the purchase price was based upon the fair value of net tangible and identifiable intangible assets as of December 13, 2012. The preliminary purchase price allocation was as follows (dollars in millions):

	Amounts Previously Recognized as of Acquisition		Measurement Period Adjustments	Amounts Recognized as of Acquisition Date (As Adjusted)		
	Date (1)					
Accounts receivable	\$	11.1	\$	0.1	\$	11.2
Inventory		1.6				1.6
Other current assets		0.6		0.2		0.8

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Equipment and leasehold improvements	0.8		0.8
Other long-term assets	0.2		0.2
Deferred tax assets	1.2		1.2
Identifiable intangibles	30.8		30.8
Goodwill	53.3	0.3	53.6
<b>Total Assets</b>	<b>99.6</b>	<b>0.6</b>	<b>100.2</b>
Current liabilities	(5.6)	(0.1)	(5.7)
Deferred tax liabilities - long-term	(9.9)		(9.9)
Other long-term liabilities	(0.1)		(0.1)
<b>Total Liabilities</b>	<b>(15.6)</b>	<b>(0.1)</b>	<b>(15.7)</b>
Total purchase price, less cash acquired	\$ 84.0	\$ 0.5	\$ 84.5

(1) As previously reported in the Corporation's 2012 Annual Report on Form 10-K

**Table of Contents****PHARMERICA CORPORATION****NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)****(Unaudited)****NOTE 2 ACQUISITIONS (Continued)**

The following is the fair value of the equipment and leasehold improvements of the Amerita acquisition at the date of acquisition (dollars in millions):

	Fair-Value	Weighted Average Useful Life (Yr)
<b>Equipment and leasehold improvements</b>		
Leasehold improvements	\$ 0.1	1.8
Equipment and software	0.7	4.9
	<b>\$ 0.8</b>	

The following are the fair values of the identifiable intangible assets of the Amerita acquisition at the date of acquisition (dollars in millions):

	Fair-Value	Weighted Average Useful Life (Yr)
<b>Identifiable intangibles</b>		
Trade name	\$ 27.0	13.0
Customer (payer) relationships	2.4	10.0
Non-compete agreements	1.4	5.0
	<b>\$ 30.8</b>	

*Other*

For the three months ended June 30, 2012 and June 30, 2013, the Corporation incurred \$2.3 million and \$0.6 million, respectively, and \$4.8 million and \$2.0 million for the six months ended June 30, 2012 and 2013, respectively, of acquisition-related costs, which have been classified as a component of merger, acquisition, integration costs and other charges.

*Pro Forma*

The following unaudited pro forma condensed consolidated financial information is not intended to represent or be indicative of the condensed consolidated results of operations or financial condition of the Corporation that would have been reported had the acquisitions been completed as of the date or for the periods presented, and should not be taken as representative of the future consolidated results of operations or financial condition of the Corporation.

The unaudited pro forma effect of the acquisitions assuming the acquisitions occurred on January 1, 2012, excluding the merger, acquisition, integration costs and other charges, stock-based compensation and deferred compensation, and assuming an effective tax rate exclusive of

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discrete items for the three and six months ended June 30, 2012, would be as follows (dollars in millions, except per share amounts):

	<b>Three Months Ended June 30, 2012</b>	<b>Six Months Ended June 30, 2012</b>
Revenues	\$ 476.1	\$ 995.5
Net income	\$ 10.5	\$ 20.5
Earnings per common share:		
Basic	\$ 0.36	\$ 0.69
Diluted	\$ 0.35	\$ 0.69

**Table of Contents****PHARMERICA CORPORATION****NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)****(Unaudited)****NOTE 3 EQUIPMENT AND LEASEHOLD IMPROVEMENTS**

Equipment and leasehold improvements consist of the following (dollars in millions):

	December 31, 2012	June 30, 2013
Leasehold improvements	\$ 14.7	\$ 16.7
Equipment and software	139.0	141.8
Construction in progress	5.1	11.2
	158.8	169.7
Accumulated depreciation	(105.7)	(112.4)
Total equipment and leasehold improvements	\$ 53.1	\$ 57.3

Depreciation expense totaled \$4.5 million and \$4.8 million for the three months ended June 30, 2012 and 2013, respectively. Depreciation expense totaled \$9.3 million and \$9.6 million for the six months ended June 30, 2012 and 2013, respectively.

**NOTE 4 GOODWILL AND INTANGIBLES**

As of December 31, 2012, as adjusted, and June 30, 2013 the carrying amount of goodwill was \$268.5 million.

The following table presents the components of the Corporation's intangible assets (dollars in millions):

Finite Lived Intangible Assets	Balance at December 31, 2012	Additions	Balance at June 30, 2013
Customer relationships	\$ 98.8	\$	\$ 98.8
Trade name	57.0		57.0
Non-compete agreements	12.6	2.4	15.0
Sub Total	168.4	2.4	170.8
Accumulated amortization	(46.5)	(8.0)	(54.5)
Net intangible assets	\$ 121.9	\$ (5.6)	\$ 116.3

Amortization expense relating to finite-lived intangible assets was \$3.0 million and \$3.9 million for the three months ended June 30, 2012 and 2013, respectively. Amortization expense relating to finite-lived intangible assets was \$5.8 million and \$8.0 million for the six months ended June 30, 2012 and 2013, respectively.

**NOTE 5 CREDIT AGREEMENT**



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On May 2, 2011, the Corporation entered into a long-term credit agreement (the Credit Agreement ) among the Corporation, the Lenders named therein, and Citibank, N.A. ( Citibank ), as Administrative Agent. The Credit Agreement consists of a \$250.0 million term loan facility and a \$200.0 million revolving credit facility. The terms and conditions of the Credit Agreement are customary to facilities of this nature.

As of June 30, 2013, \$237.5 million was outstanding under the term loan facility and \$19.6 million was outstanding under the revolving credit facility. Indebtedness under the Credit Agreement matures on June 30, 2016, at which time the commitments of the Lenders to make revolving loans also expire.

**Table of Contents****PHARMERICA CORPORATION****NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)****(Unaudited)****NOTE 5 CREDIT AGREEMENT (continued)**

The table below summarizes the term debt and revolving credit facility of the Corporation (dollars in millions):

<i>Credit Agreement:</i>	<b>December 31, 2012</b>	<b>June 30, 2013</b>
Term Debt - payable to lenders at LIBOR plus applicable margin (2.95% as of June 30, 2013), matures June 30, 2016	\$ 243.8	\$ 237.5
Revolving Credit Facility payable to lenders, interest plus applicable margin (3.95% as of June 30, 2013), matures June 30, 2016	71.7	19.6
<b>Total debt</b>	<b>315.5</b>	<b>257.1</b>
Less: Current portion of long-term debt	12.5	12.5
<b>Total long-term debt</b>	<b>\$ 303.0</b>	<b>\$ 244.6</b>

The Corporation's indebtedness has the following maturities for the current year and the next three years (dollars in millions):

<b>Year Ending December 31,</b>	<b>Term Debt</b>	<b>Revolving Credit Facility</b>	<b>Total Maturities</b>
2013	\$ 6.3	\$	\$ 6.3
2014	12.5		12.5
2015	112.5		112.5
2016	106.2	19.6	125.8
	<b>\$ 237.5</b>	<b>\$ 19.6</b>	<b>\$ 257.1</b>

The Credit Agreement provides for the issuance of letters of credit which, when issued, reduce availability under the revolving credit facility. The aggregate amount of letters of credit outstanding as of June 30, 2013 was \$2.0 million. After giving effect to the letters of credit, total availability under the revolving credit facility was \$178.4 million as of June 30, 2013. The revolving credit facility contains a \$100.0 million accordion feature, which permits the Corporation to increase the total debt capacity, up to an aggregate of \$537.5 million, subject to securing additional commitments from existing or new lenders.

The Corporation was compliant with all debt covenant requirements at June 30, 2013.

*Deferred Financing Fees*

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The Corporation capitalized a total of \$9.8 million in deferred financing fees associated with the Credit Agreement and recorded them as other assets in the accompanying condensed consolidated balance sheets. As of June 30, 2013, the Corporation had \$7.3 million of unamortized deferred financing fees.

### **NOTE 6 COMMITMENTS AND CONTINGENCIES**

#### *Legal Action and Regulatory*

The Corporation is responding to investigations by the U.S. Attorneys and by the Drug Enforcement Agency into the Corporation's alleged failure to comply with various laws and regulations relating to the control and dispensing of certain controlled substances as well as the potential filing of false claims for payments of certain controlled substances that the Corporation dispensed to nursing home residents. The Corporation has been informed that the government believes that the claims at issue were not eligible for payment due to the alleged non-compliance with various Medicare, Medicaid and other laws and regulations relating to the dispensing, control, sale, billing and reimbursement for such controlled substances. The Corporation denies the allegations made by the government and will defend itself in the event any actions are brought by the government. At this time, we are unable to estimate the outcome of the investigations. If the government brings claims and the Corporation is not successful in defending them, it could result in material fines and recoupment of government claims which could result in a material adverse effect to our consolidated financial condition, results of operations, or liquidity. As a part of these investigations, on April 15, 2013, the U.S. Department of Justice, through the U.S. Attorney's Office for the Eastern District of Virginia, filed a complaint in the United States District Court for the Eastern District of Virginia against the Corporation's two pharmacies in Virginia Beach, Virginia and Fredericksburg, Virginia alleging that these two pharmacies failed to comply with the Controlled Substances Act by dispensing Schedule II drugs without a proper prescription. The Corporation is evaluating the complaint and intends to defend itself against these allegations.

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**PHARMERICA CORPORATION**

**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

**(Unaudited)**

**NOTE 6 COMMITMENTS AND CONTINGENCIES (Continued)**

On March 4, 2011, a relator, Mark Silver, on behalf of the U.S. Government and various state governments, filed a complaint in the United States District for the District of New Jersey against the Corporation alleging that the Corporation violated the False Claims Act and Anti-Kickback Statute through its agreements to provide prescription drugs to nursing homes under certain Medicare and Medicaid programs. On February 19, 2013, the U.S. Government declined to intervene in the case. The Corporation believes that it has complied with applicable laws and regulations with respect to these matters and intends to defend itself against these allegations.

The U.S. Department of Justice, through the U.S. Attorney's Office for the District of South Carolina and the Western District of Virginia, are investigating whether the Corporation's activities in connection with agreements it had with the manufacturers of the pharmaceutical Aranesp and Depakote, respectively, violated the False Claims Act or the Anti-Kickback Statute. The Corporation is cooperating with these investigations and believes that it has complied with applicable laws and regulations with respect to these matters. At this time, we are unable to estimate the outcome of the investigations. If the government brings claims and the Corporation is not successful in defending them, it could result in material fines and recoupment of government claims which could result in a material adverse effect to our consolidated financial condition, results of operations, or liquidity.

In addition, the Corporation is involved in certain legal actions and regulatory investigations, including those related to pharmaceuticals sold by the Corporation arising in the ordinary course of business. At this time, the Corporation is unable to determine the impact of these investigations on its consolidated financial condition, results of operations, or liquidity.

*FUL and AMP Changes*

The reimbursement rates for pharmacy services under Medicaid are determined on a state-by-state basis subject to review by CMS and applicable federal law. Although Medicaid programs vary from state to state, they generally provide for the payment of certain pharmacy services, up to the established limits, at rates determined in accordance with each state's regulations. Federal regulations and the regulations of certain states establish upper limits for reimbursement of certain prescription drugs under Medicaid (these upper limits being the FUL).

The 2010 Health Care Reform Legislation amended the Deficit Reduction Act of 2005 (DRA) to change the definition of the FUL by requiring the calculation of the FUL as no less than 175% of the weighted average, based on utilization, of the most recently reported monthly Average Manufacturer's Price (AMP) for pharmaceutically and therapeutically equivalent multi-source drugs available through retail community pharmacies nationally. In addition, the definition of AMP changed to reflect net sales only to drug wholesalers that distribute to retail community pharmacies and to retail community pharmacies that directly purchase from drug manufacturers. Further, the 2010 Health Care Reform Legislation continues the current statutory exclusion of prompt pay discounts offered to wholesalers and adds three other exclusions to the AMP definition: i) bona fide services fees; ii) reimbursement for unsalable returned goods (recalled, expired, damaged, etc.); and iii) payments from and rebates/discounts to certain entities not conducting business as a wholesaler or retail community pharmacy. In addition to reporting monthly, the manufacturers are required to report the total number of units used to calculate each monthly AMP. Centers for Medicare and Medicaid Services (CMS) will use this information when it establishes FULs as a result of the new volume-weighted requirements pursuant to the 2010 Health Care Reform Legislation.

In September 2011, CMS issued the first draft FUL reimbursement files for multiple source drugs, including the draft methodology used to calculate the FULs in accordance with the Health Care Legislation. These draft FUL prices are based on the manufacturer reported and certified July 2011 monthly AMP and AMP unit data. CMS continues to release this data monthly and is expected to do so going forward. CMS has not posted monthly AMPs for individual drugs, but only posted the weighted average of monthly AMPs in a FUL group and the calculation methodology.

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CMS has issued proposed regulations further clarifying the AMP and FUL changes described above and has indicated that the final rule will be issued on January 1, 2014.

Until CMS provides final guidance and the industry adapts to this now public available pricing information, the Corporation is unable to fully evaluate the impact of the changes in FUL and AMP to its business.

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**PHARMERICA CORPORATION**

**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

**(Unaudited)**

**NOTE 6 COMMITMENTS AND CONTINGENCIES (Continued)**

*Acquisitions*

The Corporation has historically acquired the stock or assets of businesses with prior operating histories. Acquired companies may have unknown or contingent liabilities, including liabilities for failure to comply with healthcare laws and regulations, medical and general professional liabilities, workers' compensation liabilities, previous tax liabilities, and unacceptable business practices.

Although the Corporation institutes policies designed to conform practices to its standards following completion of acquisitions, there can be no assurance the Corporation will not become liable for past activities that may later be asserted to be improper by private plaintiffs or government agencies. Although the Corporation generally seeks to obtain indemnification from prospective sellers covering such matters, there can be no assurance that any such matter will be covered by indemnification, or if covered, that such indemnification will be adequate to cover potential losses and fines. In the ordinary course of business, the Corporation enters into contracts containing standard indemnification provisions and indemnifications specific to a transaction such as business acquisitions and disposals of an operating facility. These indemnifications may cover claims against employment-related matters, governmental regulations, environmental issues, tax matters, as well as customer, third party payer, supplier, and contractual relationships. Obligations under these indemnities generally would be initiated by a breach of the terms of the contract or by a third party claim or event.

*Prime Vendor Agreement*

On January 25, 2013 the Corporation renegotiated its Amended Prime Vendor Agreement with AmerisourceBergen Drug Corporation ( ABDC ) effective January 1, 2013. The First Amendment to the Amended Prime Vendor Agreement (the First Amendment ) modifies the previous agreement, which was set to expire September 30, 2013 and extends its term until September 30, 2016.

The First Amendment requires the Corporation to purchase certain levels of brand and non-injectable generic drugs from ABDC. The First Amendment does provide the flexibility for the Corporation to contract with other suppliers. If the Corporation fails to adhere to the contractual purchase provisions, ABDC has the ability to increase the Corporation's drug pricing under the terms of the First Amendment.

*Employment Agreements*

The Corporation has entered into employment agreements with certain of its executive officers. During the employment period, certain executive officers will be eligible to (i) participate in any short-term and long-term incentive programs established or maintained by the Corporation, (ii) participate in all incentive, savings and retirement plans and programs of the Corporation, (iii) participate, along with their dependents, in all welfare benefit plans and programs provided by the Corporation, and (iv) receive four weeks of paid vacation per calendar year.

The type of compensation due to each of the executive officers in the event of the termination of their employment period varies depending on the nature of the termination. The employment agreements generally do not entitle the executive officers to any additional payment or benefits solely upon the occurrence of a change in control but do provide additional payments or benefits or both upon a termination of employment in connection with a change in control. Additionally, the vesting of certain equity based grants made to certain executive officers accelerate upon the occurrence of a change in control.

*Leases*

The Corporation leases real estate properties, buildings, vehicles, and equipment under cancelable and non-cancelable leases. The leases expire at various times and have various renewal options. Interest rates used in computing the net present value of the lease payments are based on the

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Corporation's incremental borrowing rate at the inception of the lease. The Corporation recorded the following lease expense for the periods presented (dollars in millions):

	Three Months Ended June 30,		Six Months Ended June 30,	
	2012	2013	2012	2013
Pharmacy locations and administrative offices lease expense	\$ 3.6	\$ 3.8	\$ 7.1	\$ 7.7
Office equipment lease expense	0.6	0.5	1.2	1.2
<b>Total lease expense</b>	<b>\$ 4.2</b>	<b>\$ 4.3</b>	<b>\$ 8.3</b>	<b>\$ 8.9</b>

**Table of Contents****PHARMERICA CORPORATION****NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)****(Unaudited)****NOTE 6 COMMITMENTS AND CONTINGENCIES (Continued)**

Future minimum lease payments for those leases having an initial or remaining non-cancelable lease term in excess of one year are as follows for the years indicated (dollars in millions):

Year Ending December 31,	Operating Leases
2013	\$ 15.8*
2014	11.8
2015	9.4
2016	7.0
2017	4.8
Thereafter	9.4
<b>Total</b>	<b>\$ 58.2</b>

\* The 2013 amount shown includes lease expense for the six months ended June 30, 2013 of \$7.7 million.

**NOTE 7 REVENUES**

The Corporation recognizes revenues at the time services are provided or products are delivered. A significant portion of these revenues are billed to PDPs under Medicare Part D, the state Medicaid programs, long-term care institutions, third party insurance companies, and private payers. Some claims are electronically adjudicated through online processing at the point the prescription is dispensed such that the Corporation's operating system is automatically updated with the actual amount to be reimbursed. As a result, revenues and the associated receivables are based upon the actual reimbursement to be received by the Corporation. For claims that are adjudicated on-line and are rejected or otherwise denied upon submission, the Corporation provides contractual allowances based upon historical trends, contractual reimbursement terms and other factors which may impact ultimate reimbursement. Amounts are adjusted to actual reimbursed amounts upon cash receipts.

The Corporation's specialty infusion services revenues are recognized on the date that services and related products are provided to patients and are recorded at amounts estimated to be received under reimbursement arrangements with payers. Substantially all the Corporation's specialty infusion services revenues are derived from fees charged for patient care under fee-for-service arrangements.

The Corporation's hospital pharmacy management revenues represent contractually defined management fees and the reimbursement of costs associated with the direct operations of hospital pharmacies, which are primarily comprised of personnel costs.

Under the Medicare Part D benefit, payment is determined in accordance with the agreements the Corporation has negotiated with the Medicare Part D Plans. The remainder of the Corporation's billings are paid or reimbursed by individual residents, long-term care facilities (including revenues for residents funded under Medicare Part A), and other third party payers, including Medicaid and private insurers.

The Medicare and Medicaid programs are highly regulated. The failure, even if inadvertent, of the Corporation and/or client facilities to comply with applicable reimbursement regulations could adversely affect the Corporation's reimbursement under these programs and the Corporation's ability to continue to participate in these programs. In addition, failure to comply with these regulations could subject the Corporation to other



penalties.

As noted, the Corporation obtains reimbursement for drugs it provides to enrollees of a given Medicare Part D Plan in accordance with the terms of the agreement negotiated between it and that Medicare Part D Plan. The Corporation has entered into such agreements with all known Medicare Part D Plan sponsors under which it will provide drugs and associated services to their enrollees. The Corporation in the ordinary course of business has ongoing discussions with Medicare Part D Plans and may, as appropriate, renegotiate agreements.

**Table of Contents****PHARMERICA CORPORATION****NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)****(Unaudited)****NOTE 7 REVENUES (Continued)**

A summary of revenues by payer type follows (dollars in millions):

	Three Months Ended June 30,				Six Months Ended June 30,			
	2012		2013		2012		2013	
	Amount	% of Revenues	Amount	% of Revenues	Amount	% of Revenues	Amount	% of Revenues
Medicare Part D	\$ 220.3	48.1%	\$ 202.5	47.0%	\$ 460.6	48.1%	\$ 396.5	45.6%
Institutional healthcare providers	138.7	30.2	128.7	29.9	288.5	30.1	266.1	30.6
Medicaid	42.4	9.2	38.0	8.8	90.0	9.4	79.7	9.2
Private and other	21.6	4.7	16.7	3.9	45.1	4.7	37.8	4.3
Insured	18.4	4.1	25.1	5.8	39.1	4.1	50.9	5.8
Medicare	0.9	0.2	3.8	0.9	1.8	0.2	7.4	0.8
Hospital management fees	16.2	3.5	16.0	3.7	32.3	3.4	32.2	3.7
Total	\$ 458.5	100.0%	\$ 430.8	100.0%	\$ 957.4	100.0%	\$ 870.6	100.0%

Co-payments for the Corporation's services can be applicable under Medicare Part D, the state Medicaid programs, and certain third party payers and are typically not collected at the time products are delivered or services are provided. Co-payments under the Medicaid programs and third party plans are generally billed to the responsible party as part of the Corporation's normal billing procedures and are subject to the Corporation's normal collection procedures.

Under Medicare Part D, co-payments related to institutional residents who are both Medicare and Medicaid eligible (dual eligible) are due from the responsible party for up to the first thirty days of a beneficiary's stay in a skilled nursing facility, subsequent to which the PDPs are responsible for reimbursement.

Under certain circumstances, including state-mandated return policies, the Corporation accepts returns of medications and issues a credit memorandum to the applicable payer. Product returns are processed in the period in which the return is accepted by the Corporation. A reserve has been established for such returns based on historical trends.

**NOTE 8 MERGER, ACQUISITION, INTEGRATION COSTS AND OTHER CHARGES**

Merger, acquisition, integration costs and other charges were \$2.8 million for both the three months ended June 30, 2012 and 2013 and \$8.2 million and \$5.7 million for the six months ended June 30, 2012 and 2013, respectively.

Integration costs and other charges were \$0.5 million and \$2.2 million for the three months ended June 30, 2012 and 2013, respectively. The increase is primarily attributable to a former executive officer related to a separation agreement. Integration costs and other charges were \$3.4 million and \$3.7 million for the six months ended June 30, 2012 and 2013, respectively. The six months ended June 30, 2012 included \$1.9 million incurred during the first quarter of 2012 related to an unsolicited tender offer.

Acquisition costs were \$2.3 million and \$0.6 million for the three months ended June 30, 2012 and 2013, respectively, and \$4.8 million and \$2.0 million for the six months ended June 30, 2012 and 2013, respectively. Acquisition costs decreased due to decreases in professional fees for

potential acquisitions and employee, severance and facility costs associated with prior acquisitions.

**NOTE 9 HURRICANE SANDY DISASTER COSTS**

In October 2012, Hurricane Sandy caused significant damage on Long Island, New York and surrounding areas. The financial impacts of the storm to the Corporation's Long Beach facility, as well as damage and disruption at the Corporation's customers' facilities, have been recorded as a separate component in the condensed consolidated income statements.

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**PHARMERICA CORPORATION**

**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

**(Unaudited)**

**NOTE 9 HURRICANE SANDY DISASTER COSTS (continued)**

The Corporation expects a portion of the cost associated with Hurricane Sandy to be covered by insurance. While the exact amount has not been determined, the Corporation's current estimate of covered losses, net of its less than \$0.1 million deductible, is approximately \$4.1 million. After consideration of a \$4.0 million advance by the insurance carrier, the Corporation has recorded a receivable for \$0.1 million which is included in prepaids and other assets in the condensed consolidated balance sheets. The actual recovery will vary depending on the outcome of the insurance loss adjustment process. Accordingly, no offsetting benefit for insurance recoveries above the amount of the loss shown was recorded. For the six months ended June 30, 2013, Hurricane Sandy disaster costs were \$(0.3) million.

**NOTE 10 COMMON STOCK, PREFERRED STOCK, TREASURY STOCK, STOCK-BASED COMPENSATION AND OTHER BENEFITS**

*Common Stock*

Holders of the Corporation's common stock are entitled to one vote for each share held of record on all matters on which stockholders may vote. There are no preemptive, conversion, redemption or sinking fund provisions applicable to the Corporation's common stock. In the event of liquidation, dissolution or winding up, holders of common stock are entitled to share ratably in the assets available for distribution, subject to any prior rights of any holders of preferred stock then outstanding. In addition, the Corporation's Credit Agreement imposes restrictions on its ability to pay cash dividends.

*Preferred Stock*

The certificate of incorporation authorizes the issuance of an aggregate of 1.0 million shares of preferred stock. As of June 30, 2013, there were no shares of preferred stock outstanding.

The Corporation's Board of Directors may, from time to time, direct the issuance of shares of preferred stock in series and may, at the time of issuance, determine the designation, powers, rights, preferences and limitations of each series. Satisfaction of any dividend preferences of outstanding preferred stock would reduce the amount of funds available for the payment of dividends on the Corporation's shares of common stock. Holders of preferred stock may be entitled to receive a preference payment in the event of any liquidation, dissolution or winding-up of the Corporation before any payment is made to the holders of the Corporation's common stock. Under certain circumstances, the issuance of preferred stock may render more difficult or tend to discourage a merger, tender offer or proxy contest, the assumption of control by a holder of a large block of the Corporation's securities or the removal of incumbent management. The Board of Directors may issue shares of preferred stock with voting and conversion rights that could adversely affect the holders of common stock. Specifically, the Corporation's certificate of incorporation authorizes the Corporation's Board of Directors to adopt a rights plan without stockholder approval. This could delay or prevent a change in control of the Corporation or the removal of existing management.

*Treasury Stock Purchases*

In August 2010, the Board of Directors authorized a share repurchase of up to \$25.0 million of the Corporation's common stock, of which \$10.5 million was used. On July 2, 2012 the Board of Directors authorized an increase to the remaining portion of the existing stock repurchase program that will allow the Corporation to again repurchase up to a maximum of \$25.0 million of the Corporation's common stock. Approximately \$24.0 million remains available under the program as of June 30, 2013. Share repurchases under this authorization may be made in the open market through unsolicited or solicited privately negotiated transactions, or in such other appropriate manner, and will be funded from available cash. The amount and timing of the repurchases, if any, will be determined by the Corporation's management and will depend on a variety of factors including price, corporate and regulatory requirements, capital availability and other market conditions. Common stock acquired through the share repurchase program will be held as treasury shares and may be used for general corporate purposes, including

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reissuance in connection with acquisitions, employee stock option exercises or other employee stock plans. The share repurchase program does not have an expiration date and may be limited, terminated or extended at any time without prior notice. During the six months ended June 30, 2013, the Corporation did not repurchase shares of common stock under the share repurchase program.

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**PHARMERICA CORPORATION**

**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

**(Unaudited)**

**NOTE 10 COMMON STOCK, PREFERRED STOCK, TREASURY STOCK, STOCK-BASED COMPENSATION AND OTHER BENEFITS (Continued)**

The Corporation may redeem shares from employees upon the vesting of the Corporation's stock awards for minimum statutory tax withholding purposes. The Corporation redeemed 129,073 shares of certain vested awards for an aggregate price of approximately \$1.9 million during six months ended June 30, 2013. These shares have also been designated by the Corporation as treasury stock.

As of June 30, 2013, the Corporation had a total of 1,585,366 shares held as treasury stock.

*Amended and Restated 2007 Omnibus Incentive Plan*

The Corporation has adopted the Amended and Restated PharMerica Corporation 2007 Omnibus Incentive Plan (as amended and restated, the Omnibus Plan) under which the Corporation is authorized to grant equity-based and other awards to its employees, officers, directors, and consultants.

The Corporation has reserved 7,237,000 shares of its common stock for awards to be granted under the Omnibus Plan plus 534,642 shares reserved for substitute equity awards. Under the fungible share pool, one share of stock will be subtracted from the share limit for each share of stock covered by a stock option or stock appreciation right award and 1.65 shares of stock will be subtracted from the share limit for each share of stock covered by any full-value award, including restricted share awards, restricted stock units and performance share awards at target. The following shares are not available for re-grant under the Omnibus Plan: (i) shares tendered by a participant or withheld by the Corporation to pay the purchase price of a stock option award or to satisfy taxes owed with respect to an award, (ii) shares subject to a stock appreciation right that are not issued in connection with such award's settlement upon the exercise thereof, and (iii) shares reacquired by the Corporation using cash proceeds received by the Corporation from the exercise of stock options. Effective January 1, 2010, shares subject to an award that is forfeited, expired or settled for cash, are available for re-grant under the Omnibus Plan as one share of stock for each share of stock covered by a stock option or appreciation right and 1.65 shares of stock for each share of stock covered by any other type of award.

As of June 30, 2013, total shares available for grants of stock-based awards pursuant to the Omnibus Plan were 3,192,342 shares. The 3,192,342 shares do not take into consideration the dilution of 1.65 shares of stock for any full-value award, including restricted stock awards, restricted stock units and performance share awards at target. The number of shares remaining available for future issuance calculated under the fungible share pool would be 2,305,944.

*Stock Appreciation Rights Plan*

The wholly-owned subsidiary of the Corporation, Amerita, Inc., has adopted the 2013 Stock Appreciation Rights Plan (SAR Plan) effective March 26, 2013 under which Amerita's Board of Directors is authorized to grant Stock Appreciation Rights (SAR) to certain employees of the Corporation. Each SAR shall vest, generally in full after three years, and become exercisable, in one or more installments and shall be subject to the achievement of specified performance goals or objectives established with respect to one or more performance criteria. The SAR awards are exercisable for two years after the vesting period is complete, but no SAR may be exercised more than ten years after the grant date. Final settlement of the SAR awards is to be provided to the employees in cash; as a result, the Corporation has recognized a liability on the condensed consolidated balance sheet associated with the awards.

**Table of Contents****PHARMERICA CORPORATION****NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)****(Unaudited)****NOTE 10 COMMON STOCK, PREFERRED STOCK, TREASURY STOCK, STOCK-BASED COMPENSATION AND OTHER BENEFITS (Continued)***Stock-Based Compensation Expense*

The following is a summary of stock-based compensation incurred by the Corporation (dollars in millions, except per share amounts):

	Three Months Ended June 30,		Six Months Ended June 30,	
	2012	2013	2012	2013
Stock option compensation expense	\$ 0.5	\$ 0.2	\$ 1.0	\$ 0.6
Nonvested stock compensation expense	0.8	1.4	1.9	3.0
<b>Total Stock Compensation Expense</b>	<b>\$ 1.3</b>	<b>\$ 1.6</b>	<b>\$ 2.9</b>	<b>\$ 3.6</b>
Negative effect on diluted earnings per share	\$ (0.03)	\$ (0.03)	\$ (0.06)	\$ (0.07)

As of June 30, 2013, there was \$11.4 million of total unrecognized compensation cost related to the Corporation's stock compensation arrangements. Total unrecognized compensation cost will be adjusted for future changes in estimated forfeitures.

Total estimated stock-based compensation expense for the Corporation's stock options and nonvested stock awards for the current and the next four years and thereafter are as follows (dollars in millions):

Year Ending December 31,	Stock Options	Nonvested Restricted Stock Units	Performance Share Units	Total
2013	\$ 1.1	\$ 3.9	\$ 1.9	\$ 6.9*
2014	0.6	2.7	1.6	4.9
2015	0.1	1.2	0.9	2.2
2016		0.3	0.7	1.0
2017				
Thereafter				
<b>Total</b>	<b>\$ 1.8</b>	<b>\$ 8.1</b>	<b>\$ 5.1</b>	<b>\$ 15.0</b>

\* The 2013 amount shown includes stock-based compensation expense for the six months ended June 30, 2013 of \$3.6 million.  
*SAR Compensation Expense*

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The Corporation incurred expense during the three months ended June 30, 2013 of less than \$0.1 million related to the SAR awards which also represents the amount of the cumulative liability.



**Table of Contents****PHARMERICA CORPORATION****NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)****(Unaudited)****NOTE 10 COMMON STOCK, PREFERRED STOCK, TREASURY STOCK, STOCK-BASED COMPENSATION AND OTHER BENEFITS (Continued)***Stock Option Activity*

Stock options were not granted to officers and employees during 2012 or 2013. The following table summarizes option activity for the periods presented:

	Number of Shares	Weighted- Average Exercise Price Per Share	Weighted- Average Remaining Term	Aggregate Intrinsic Value (in millions)
Outstanding shares at December 31, 2012	2,424,285	\$ 15.14	3.2 years	\$ 1.8
Exercised	(33,266)	11.53		
Canceled	(61,632)	13.15		
Expired	(429,767)	15.70		
Outstanding shares at June 30, 2013	1,899,620	\$ 15.14	2.8 years	\$ 1.3
Exercisable shares at June 30, 2013	1,594,690	\$ 15.55	2.4 years	\$ 0.7

The total intrinsic value of stock options exercised for both the six months ended June 30, 2012 and June 30, 2013 was less than \$0.1 million. Cash received from stock option exercises during the six months ended June 30, 2013 was \$0.4 million. The total fair value of options vested for the six months ended June 30, 2012 and 2013 was \$2.0 million and \$1.6 million, respectively. The Corporation expects to recognize stock-based compensation expense for stock options over a remaining weighted average period of 1.07 years.

*Nonvested Shares*

The following table summarizes nonvested share activity for the periods presented:

	Number of Shares	Weighted- Average Grant Date Fair Value
Outstanding shares at December 31, 2012	1,133,335	\$ 13.00
Granted - Restricted Stock Units	285,824	14.75
Granted - Performance Share Units	234,376	14.48
Forfeited	(208,993)	15.03
Vested	(378,886)	13.04

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Outstanding shares at June 30, 2013	1,065,656	\$	13.38
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The total fair value of shares vested for the six months ended June 30, 2012 and 2013 was \$1.2 million and \$4.9 million, respectively. The aggregate intrinsic value of shares vested for the six months ended June 30, 2013 and 2012 was \$5.6 million and \$1.2 million, respectively. The Corporation expects to recognize stock based compensation expense for nonvested shares over a weighted average period of 1.54 years. The aggregate intrinsic value of the outstanding shares at June 30, 2013 was \$14.8 million with a vesting term of three years or less.

Based upon the achievement of the performance criteria at the end of the performance cycle for the performance share units issued to date, the Corporation may issue no shares or a maximum of 791,355 shares.

**Table of Contents****PHARMERICA CORPORATION****NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)****(Unaudited)****NOTE 11 INCOME TAXES**

The provision for income taxes is based upon the Corporation's estimate of annual taxable income or loss for each respective accounting period. The following table summarizes our provision for income taxes for the periods presented (dollars in millions):

	Three Months Ended June 30,		Six Months Ended June 30,	
	2012	2013	2012	2013
Provision for income taxes	\$ 5.1	\$ 8.2	\$ 8.8	\$ 15.1
Total provision as a percentage of pre-tax income	40.1%	44.2%	40.1%	42.1%

The increase in the provision for income taxes as a percentage of pre-tax income for the six months ended June 30, 2013 compared to the six months ended June 30, 2012 was primarily due to an increase in discrete items associated with the Corporation's stock-based compensation plan and its effect on the provision for income taxes upon the separation of a former executive officer during the second quarter of 2013. Excluding the impact of the discrete items, the provision for income taxes as a percentage of pre-tax income would have been 40.1%. The effective tax rates in 2013 and 2012 are higher than the federal statutory rate largely as a result of the combined impact of state and local taxes and various non-deductible expenses.

The Corporation derives a current federal and state income tax benefit from the impact of deductions associated with the amortization of tax deductible goodwill acquired through business combinations. The tax basis of the Corporation's tax deductible goodwill was approximately \$123.3 million and \$116.8 million at December 31, 2012 and June 30, 2013, respectively. The future tax benefits of the tax-deductible goodwill are included in the Corporation's deferred tax assets.

The Corporation recognizes an asset or liability for the deferred tax consequences of temporary differences between the tax basis of assets and liabilities and their reported amounts in the financial statements. These temporary differences will result in taxable or deductible amounts in future years when the reported amounts of the assets are recovered or liabilities are settled. The Corporation also recognizes as deferred tax assets the future tax benefits from net operating and capital loss carryforwards. As of June 30, 2013, the Corporation has no tax benefits from federal net operating loss carryforwards and tax benefits from state net operating loss carryforwards of \$7.3 million, net of federal benefit. The net operating losses have carryforward periods ranging from 1 to 20 years depending on the taxing jurisdiction.

A valuation allowance is provided for the Corporation's deferred tax assets if it is more likely than not that some portion or all of the net deferred tax assets will not be realized. The Corporation recognized deferred tax assets totaling \$25.6 million at December 31, 2012 and \$22.7 million at June 30, 2013, net of state valuation allowances of \$1.0 million.

As of December 31, 2012 and June 30, 2013, the Corporation had no reserves recorded for unrecognized tax benefits for U.S. federal and state tax jurisdictions.

**Table of Contents****PHARMERICA CORPORATION****NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)****(Unaudited)****NOTE 12 EARNINGS PER SHARE**

The following table sets forth the computation of basic and diluted earnings per share (dollars in millions, except per share amounts):

	Three months ended June 30,		Six months ended June 30,	
	2012	2013	2012	2013
<b>Numerator:</b>				
Numerator for basic and earnings per diluted share - net income	\$ 7.6	\$ 10.2	\$ 13.2	\$ 20.7
<b>Denominator:</b>				
Denominator for basic earnings per share - weighted average shares	29,489,766	29,713,010	29,459,978	29,640,388
Effective of dilutive securities (stock options, restricted stock units and performance share units)	230,637	421,934	275,511	501,342
Denominator for earnings per diluted share - adjusted weighted average shares	29,720,403	30,134,944	29,735,489	30,141,730
Basic earnings per share	\$ 0.26	\$ 0.34	\$ 0.45	\$ 0.70
Earnings per diluted share	\$ 0.26	\$ 0.34	\$ 0.44	\$ 0.69
Unexercised employee stock options and unvested restricted shares excluded from the effect of dilutive securities above (a)	3,164,242	1,546,348	3,142,971	1,706,682

(a) These unexercised employee stock options and nonvested restricted shares were not included in the computation of diluted earnings per share because to do so would have been anti-dilutive for the periods presented.

Stock options and restricted shares and units granted by the Corporation are treated as potential common shares outstanding in computing earnings per diluted share. Performance share units are treated as potential common shares outstanding in computing earnings per diluted share only when the performance conditions are met.

Common shares repurchased by the Corporation reduce the number of basic shares used in the denominator for basic and diluted earnings per share.

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**Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations**

**CAUTIONARY STATEMENT REGARDING FORWARD-LOOKING STATEMENTS**

This Quarterly Report on Form 10-Q contains 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, which reflect the Corporation's current estimates, expectations and projections about the Corporation's future results, performance, prospects and opportunities. Forward looking statements include, among other things, the information concerning the Corporation's possible future results of operations including revenues, costs of goods sold, and gross margin, business and growth strategies, financing plans, the Corporation's competitive position and the effects of competition, the projected growth of the industries in which we operate, and the Corporation's ability to consummate strategic acquisitions. Forward-looking statements include statements that are not historical facts and can be identified by forward-looking words such as anticipate, believe, could, estimate, expect, intend, plan, may, should, will, would, project, and similar expressions. These forward-looking statements are based upon information currently available to the Corporation and are subject to a number of risks, uncertainties and other factors that could cause the Corporation's actual results, performance, prospects or opportunities to differ materially from those expressed in, or implied by, these forward-looking statements. Important factors that could cause the Corporation's actual results to differ materially from the results referred to in the forward-looking statements the Corporation makes in this report include:

the Corporation's access to capital, credit ratings, indebtedness, and ability to raise additional financings and operate under the terms of the Corporation's debt obligations;

anti-takeover provisions of the Delaware General Corporation Law, which in concert with our certificate of incorporation and our by-laws could delay or deter a change in control;

the effects of adverse economic trends or intense competition in the markets in which we operate;

the Corporation's risk of loss of revenues due to a customer or owner of skilled nursing facility entering the institutional pharmacy business;

the demand for the Corporation's products and services;

the risk of retaining existing customers and service contracts and the Corporation's ability to attract new customers for growth of the Corporation's business;

the effects of renegotiating contract pricing relating to significant customers and suppliers, including the hospital pharmacy business which is substantially dependent on service provided to one customer;

the impacts of cyber security risks and/or incidents;

the effects of a failure in the security or stability of our technology infrastructure, or the infrastructure of one or more of our key vendors, or a significant failure or disruption in service;

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the effects of an increase in credit risk, loss or bankruptcy of or default by any significant customer, supplier, or other entity relevant to the Corporation's operations;

the Corporation's ability to successfully pursue the Corporation's development and acquisition activities and successfully integrate new operations and systems, including the realization of anticipated revenues, economies of scale, cost savings, and productivity gains associated with such operations;

the Corporation's ability to control costs, particularly labor and employee benefit costs, rising pharmaceutical costs, and regulatory compliance costs;

the effects of healthcare reform and government regulations, including, interpretation of regulations and changes in the nature and enforcement of regulations governing the healthcare and institutional pharmacy services industries, including, the dispensing of antipsychotic prescriptions;

changes in the reimbursement rates or methods of payment from Medicare and Medicaid and other third party payers to both us and our customers;

the potential impact of state government budget shortfalls and their ability to pay the Corporation and its customers for services provided;

the Corporation's ability, and the ability of the Corporation's customers, to comply with Medicare or Medicaid reimbursement regulations or other applicable laws;

the effects of the sequestration order issued by the Federal government in March 2013, mandating pending reductions impacting most federal programs, including Medicare;

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the effects of changes in the interest rate on the Corporation's outstanding floating rate debt instrument and the increases in interest expense, including increases in interest rate terms on any new debt financing;

further consolidation of managed care organizations and other third party payers;

political and economic conditions nationally, regionally, and in the markets in which the Corporation operates;

natural disasters, war, civil unrest, terrorism, fire, floods, tornadoes, earthquakes, hurricanes, epidemic, pandemic, catastrophic event or other matters beyond the Corporation's control;

increases in energy costs, including state and federal taxes, and the impact on the costs of delivery expenses and utility expenses;

elimination of, changes in, or the Corporation's failure to satisfy pharmaceutical manufacturers' rebate programs;

the Corporation's ability to attract and retain key executives, pharmacists, and other healthcare personnel;

the Corporation's risk of loss not covered by insurance;

the outcome of litigation to which the Corporation is a party from time to time, including adverse results in material litigation or governmental inquiries;

changes in accounting rules and standards, audits, compliance with the Sarbanes-Oxley Act, and regulatory investigations;

changes in market conditions that would result in the impairment of goodwill or other assets of the Corporation;

changes in market conditions in which we operate that would influence the value of the Corporation's stock;

the uncertainty as to the long-term value of the Corporation's common stock;

the Corporation's ability to anticipate a shift in demand for generic drug equivalents and the impact on the financial results including the negative impact on brand drug rebates;

the effect on prescription volumes and the Corporation's net revenues and profitability if the safety risk profiles of drugs increase or if drugs are withdrawn from the market, including as a result of manufacturing issues, or if prescription drugs transition to over-the-counter products;

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the effects on the Corporation's results of operations related to interpretations of accounting principles by the SEC staff that may differ from those of management;

changes in tax laws and regulations;

the effects of changes to critical accounting estimates; and

other factors, risks and uncertainties referenced in the Corporation's filings with the Commission, including the Risk Factors set forth in the Corporation's Annual Report on Form 10-K for the year ended December 31, 2012.

**YOU ARE CAUTIONED NOT TO PLACE UNDUE RELIANCE ON ANY FORWARD-LOOKING STATEMENTS, ALL OF WHICH SPEAK ONLY AS OF THE DATE OF THIS QUARTERLY REPORT. EXCEPT AS REQUIRED BY LAW, WE UNDERTAKE NO OBLIGATION TO PUBLICLY UPDATE OR RELEASE ANY REVISIONS TO THESE FORWARD-LOOKING STATEMENTS TO REFLECT ANY EVENTS OR CIRCUMSTANCES AFTER THE DATE OF THIS QUARTERLY REPORT OR TO REFLECT THE OCCURRENCE OF UNANTICIPATED EVENTS. ALL SUBSEQUENT WRITTEN AND ORAL FORWARD-LOOKING STATEMENTS ATTRIBUTABLE TO US OR ANY PERSON ACTING ON THE CORPORATION'S BEHALF ARE EXPRESSLY QUALIFIED IN THEIR ENTIRETY BY THE CAUTIONARY STATEMENTS CONTAINED OR REFERRED TO IN THIS SECTION AND IN OUR RISK FACTORS SET FORTH IN PART I, ITEM 1A OF THE CORPORATION'S ANNUAL REPORT ON FORM 10-K FOR THE YEAR ENDED DECEMBER 31, 2012 AND IN OTHER REPORTS FILED WITH THE SEC BY THE CORPORATION.**

### General

The condensed consolidated financial statements and Management's Discussion and Analysis of Financial Condition and Results of Operations included in this quarterly report on Form 10-Q as of and for the three and six months ended June 30, 2013, reflect the financial position, results of operations, and cash flows of the Corporation.

Unless the context otherwise requires, all references to we, us, our, and Corporation refer to PharMerica Corporation and its subsidiaries.



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### **The Corporation's Business and Industry Trends**

#### *Pharmacy Business*

Our core business provides pharmacy products and services to residents and patients in skilled nursing facilities, nursing centers, assisted living facilities, hospitals, and other long-term alternative care settings. We purchase, repackage, and dispense prescription and non-prescription pharmaceuticals in accordance with physician orders and deliver such medication to healthcare facilities for administration to individual patients and residents. Depending on the specific location, we service healthcare facilities typically within a radius of 120 miles or less of our pharmacy locations at least once each day. We provide 24-hour, seven-day per week on-call pharmacist services for emergency dispensing, delivery, and/or consultation with the facility's staff or the resident's attending physician. We also provide various supplemental healthcare services that complement our institutional pharmacy services.

We offer prescription and non-prescription pharmaceuticals to our customers through unit dose or modified unit dose packaging, dispensing, and delivery systems, typically in a 14 to 30 day supply. Unit dose medications are packaged for dispensing in individual doses as compared to bulk packaging used by most retail pharmacies. The customers we serve prefer the unit dose delivery system over the bulk delivery system employed by retail pharmacies because it improves control over the storage and ordering of drugs and reduces errors in drug administration in healthcare facilities. Nursing staff in our customers' facilities administer the pharmaceuticals to individual patients and residents. The Corporation also utilizes an on-site dispensing system, with real time data transfer between the system and the Corporation, which provides timely medication administration in emergency and first dose situations. We also offer clinical pharmacy programs that encompass a wide range of drug therapy and disease management protocols, including protocols for anemia treatment, infectious diseases, wound care, nutritional support, renal dosing, and therapeutic substitution.

Our computerized dispensing and delivery systems are designed to improve efficiency and control over distribution of medications to patients and residents. We provide computerized physician orders and medication administration records for patients or residents on a monthly basis as requested. Data from these records are formulated into monthly management reports on patient and resident care and quality assurance. This system improves efficiencies in nursing time, reduces drug waste, and helps to improve patient outcomes.

#### *Hospital Pharmacy Management Services*

We also provide hospital pharmacy management services. These services generally entail the overall management of the hospital pharmacy operations, including the ordering, receipt, storage, and dispensing of pharmaceuticals to the hospital's patients pursuant to the clinical guidelines established by the hospital. We offer the hospitals a wide range of regulatory and financial management services, including inventory control, budgetary analysis, staffing optimization, and assistance with obtaining and maintaining applicable regulatory licenses, certifications, and accreditations. We work with the hospitals to develop and implement pharmacy policies and procedures, including drug formulary development and utilization management. We also offer clinical pharmacy programs that encompass a wide range of drug therapy and disease management protocols, including protocols for anemia treatment, infectious diseases, wound care, nutritional support, renal dosing, and therapeutic substitution. The hospital pharmacy management services segment is comprised of a few customers, of which, our largest service is to the majority of the Kindred hospitals.

#### *Consultant Pharmacist Services*

Federal and state regulations mandate that long-term care facilities, in addition to providing a source of pharmaceuticals, retain consultant pharmacist services to monitor and report on prescription drug therapy in order to maintain and improve the quality of resident care. On September 30, 2008, the United States Department of Health and Human Services Office of Inspector General (OIG) published OIG Supplemental Compliance Program Guidance for Nursing Homes. With quality of care being the first risk area identified, the supplemental guidance is part of a series of recent government efforts focused on improving quality of care at skilled nursing and long-term care facilities. The guidance contains compliance recommendations and an expanded discussion of risk areas. The guidance stressed that facilities must provide pharmaceutical services to meet the needs of each resident and should be mindful of potential quality of care problems when implementing policies and procedures on proper medication management. It further stated that facilities can reduce risk by educating staff on medication management and improper pharmacy kickbacks for consultant pharmacists and that facilities should review the total compensation paid to consultant pharmacists to ensure it is not structured in a way that reflects the volume or value of particular drugs prescribed or administered to residents.

We provide consultant pharmacist services to 67% of our patients serviced. The services offered by our consultant pharmacists include:

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Monthly reviews of each resident's drug regimen to assess the appropriateness and efficiency of drug therapies, including the review of medical records, monitoring drug interactions with other drugs or food, monitoring laboratory test results, and recommending alternative therapies;

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Participation on quality assurance and other committees of our customers, as required or requested by such customers;

Monitoring and reporting on facility-wide drug utilization;

Development and maintenance of pharmaceutical policy and procedure manuals; and

Assistance with federal and state regulatory compliance pertaining to resident care.

### *Medical Records*

The Corporation provides medical records services, which includes the completion and maintenance of medical record information for patients in the Corporation's customer's facilities. The medical records services include:

Real-time access to medication and treatment administration records, physician order sheets and psychotropic drug monitoring sheets;

Online ordering to save time and resources;

A customized database with the medication profiles of each resident's medication safety, efficiency and regulatory compliance;

Web-based individual patient records detailing each prescribed medicine; and

Electronic medical records to improve information to make it more legible and instantaneous.

### *Specialty Infusion Services*

The Corporation provides specialty infusion services focused on providing complex pharmaceutical products and clinical services to patients in client facilities, hospice, and outside of hospital or nursing home settings. We offer high-touch clinical services to patients with acute or chronic conditions. The delivery of home infusion therapy requires comprehensive planning and monitoring which is provided through our registered nursing staff. Our nursing staff performs an initial patient assessment, provides therapy specific training and education, administers therapy and monitors for potential side effects. We also provide extensive clinical monitoring and patient follow-up to ensure patient therapy adherence and proactively manage patients' conditions. An in-network strategy facilitates easier decision-making for referral sources and provides us with the ability to pre-authorize patients, auto adjudicate, and bill electronically, enabling faster prescription turnaround.

### *Customers*

*Institutional Care Settings.* Our customers are typically institutional healthcare providers, such as skilled nursing facilities, nursing centers, assisted living facilities and other long-term alternative care settings. We are generally the primary source of pharmaceuticals for our customers.

Our customers depend on institutional pharmacies like us to provide the necessary pharmacy products and services and to play an integral role in monitoring patient medication regimens and safety. We dispense pharmaceuticals in patient specific packaging in accordance with physician instructions.

We have significant customer concentrations with facilities operated by Kindred. For the six months ended June 30, 2013, revenues from Kindred's nursing facilities and hospitals represented approximately 13.6% of the Corporation's total revenues. The Corporation has been informed by Kindred that it is not renewing the Corporation's contract for skilled nursing pharmacy services, which accounts for approximately

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10.2% of revenues in the six months ended June 30, 2013, when the current contract expires on December 31, 2013. The Corporation provides hospital management services to this customer's hospitals, which account for approximately 3.4% of revenues in the six months ended June 30, 2013, under a separate contract that continues through 2014.

*Specialty Infusion Services.* At June 30, 2013, the Corporation provided specialty infusion services to patients in 14 states with acute or chronic conditions in a setting outside of a hospital or nursing home.

### ***Suppliers/Inventory***

We obtain pharmaceutical and other products from ABDC and other contracts negotiated directly with pharmaceutical manufacturers for discounted prices. While the loss of a supplier could adversely affect our business if alternate sources of supply are unavailable, numerous sources of supply are generally available to us.

We seek to maintain an on-site inventory of pharmaceuticals and supplies to ensure prompt delivery to our customers. ABDC maintains local distribution facilities in most major geographic markets in which we operate.

**Table of Contents****Brand versus Generic**

The pharmaceutical industry has been experiencing a higher level of brand-to-generic drug conversions. The following table summarizes the Corporation's generic drug dispensing rate:

	2012	2013
March 31,	80.9%	83.3%
June 30,	83.2	83.3
September 30,	84.4	
December 31,	84.8	

The following table summarizes the material brand-to-generic conversions expected to occur in 2013 through 2017:

2013	2014	2015	2016	2017
Lidoderm Patch (3Q)	Detrol LA (1Q)	Namenda (1Q)	Crestor (3Q)	Seroquel XR (4Q)
Diovan (4Q)	Nexium (1Q)	Abilify (2Q)		
Cymbalta (4Q)	Renvela (1Q)	Procrit (2Q)		
	Excelon (1Q)	Travatan Z (2Q)		
	Celebrex (2Q)	Zyvox (2Q)		
	Restasis (2Q)	Aggrenox (3Q)		
	Copaxone (4Q)	Combivent (4Q)		

(Number in parentheses refers to the expected quarter of conversion)

When a branded drug shifts to a generic, initial pricing of the generic drug in the market will vary depending on the number of manufacturers launching their generic version of the drug. Historically a shift from brand-to-generic decreased our revenue and improved our gross margin from sales of these classes of drugs during the initial time period a brand drug has a generic alternative. However, recent experience has indicated that the third-party payers may reduce their reimbursements to the Corporation faster than previously experienced. In addition, the number of generic manufacturers entering the market impacts the overall cost and reimbursement of generic drugs. This acceleration in the reimbursement reduction and the number of generic manufacturers have resulted in margin compression much earlier than we have historically experienced. Due to the unique nature of the brand-to-generic conversion, management cannot estimate the future financial impact of the brand-to-generic conversions on the Corporation's results of operations.

**Supplier and Manufacturer Rebates**

We currently receive rebates from certain manufacturers and distributors of pharmaceutical products for achieving targets of market share or purchase volumes. Rebates are designed to prefer, protect, or maintain a manufacturer's products that are dispensed by the pharmacy under its formulary. Rebates for brand name products are generally based upon achieving a defined market share tier within a therapeutic class and can be based on either purchasing volumes or actual prescriptions dispensed. Rebates for generic products are more likely to be based on achieving purchasing volume requirements.

**Information Technology**

Computerized medical records and documentation are an integral part of our distribution system. We primarily utilize a proprietary information technology infrastructure that automates order entry of medications, dispensing of medications, invoicing, and payment processing. These systems provide consulting drug review, electronic medication management, medical records, and regulatory compliance information to help ensure patient safety. These systems also support verification of eligibility and electronic billing capabilities for the Corporation's pharmacies. They also provide order entry, shipment, billing, reimbursement and collection of service fees for medications, specialty services and other services rendered.

Based upon our electronic records, we are able to provide reports to our customers and management on patient care and quality assurance. These reports help to improve efficiency in patient care, reduce drug waste, and improve patient outcomes. We expect to continue to invest in technologies that help critical information access and system availability.

**Competition**

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We face a highly competitive environment in the institutional pharmacy market. In each geographic market, there are national, regional and local institutional pharmacies that provide services comparable to those offered by our pharmacies which may have greater financial and other resources than we do and may be more established in the markets they serve than we are. In addition, owners of skilled nursing facilities are also entering the institutional pharmacy market, particularly in areas of their geographic concentration. On a nationwide basis, there is one large competitor in the institutional pharmacy industry, Omnicare, Inc.

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We believe that the competitive factors most important to our business are pricing, quality and the range of services offered, clinical expertise, ease of doing business with the provider and the ability to develop and maintain relationships with customers. Because relatively few barriers to entry exist in the local markets we serve, we have encountered and will continue to encounter substantial competition from local market entrants.

### ***2010 Health Care Reform Legislation***

The Patient Protection and Affordable Care Act and the reconciliation law known as Health Care and Education Affordability Reconciliation Act (combined we refer to both Acts as the 2010 Health Care Reform Legislation ) were enacted in March 2010. State participation in the expansion of Medicaid under the 2010 Health Care Reform Legislation is voluntary. Three key provisions of the 2010 Health Care Reform Legislation that are relevant to the Corporation are: (i) the gradual modification to the calculation of the Federal Upper Limit ( FUL ) for drug prices and the definition of Average Manufacturer s Price ( AMP ), (ii) the closure, over time, of the Medicare Part D coverage gap, which is otherwise known as the Donut Hole, and (iii) short cycle dispensing. Regulations under the 2010 Health Care Reform Legislation are expected to continue being drafted, released, and finalized throughout the next several years. Pending the promulgation of these regulations, the Corporation is unable to fully evaluate the impact of the 2010 Health Care Reform Legislation.

### ***FUL and AMP Changes***

The reimbursement rates for pharmacy services under Medicaid are determined on a state-by-state basis subject to review by CMS and applicable federal law. Although Medicaid programs vary from state to state, they generally provide for the payment of certain pharmacy services, up to the established limits, at rates determined in accordance with each state s regulations. Federal regulations and the regulations of certain states establish upper limits for reimbursement of certain prescription drugs under Medicaid (these upper limits being the FUL ).

The 2010 Health Care Reform Legislation amended the Deficit Reduction Act of 2005 (the DRA ) to change the definition of FUL by requiring the calculation of the FUL as no less than 175% of the weighted average, based on utilization, of the most recently reported monthly AMP for pharmaceutically and therapeutically equivalent multi-source drugs available through retail community pharmacies nationally.

In addition, the definition of AMP changed to reflect net sales only to drug wholesalers that distribute to retail community pharmacies and to retail community pharmacies that directly purchase from drug manufacturers. Further, the 2010 Health Care Reform Legislation continues the current statutory exclusion of prompt pay discounts offered to wholesalers and adds three other exclusions to the AMP definition: i) bona fide services fees; ii) reimbursement for unsalable returned goods (recalled, expired, damaged, etc.); and iii) payments from and rebates/discounts to certain entities not conducting business as a wholesaler or retail community pharmacy. In addition to reporting monthly, the manufacturers are required to report the total number of units used to calculate each monthly AMP. Centers for Medicare and Medicaid Services ( CMS ) will use this information when it establishes FULs as a result of the new volume-weighted requirements pursuant to the 2010 Health Care Reform Legislation.

In September 2011, CMS issued the first draft FUL reimbursement files for multiple source drugs, including the draft methodology used to calculate the FULs in accordance with the Health Care Legislation. These draft FUL prices are based on the manufacturer reported and certified July 2011 monthly AMP and AMP unit data. CMS continues to release this data monthly and is expected to do so going forward. CMS has not posted monthly AMPs for individual drugs, but only posted the weighted average of monthly AMPs in a FUL group and the calculation methodology.

CMS has issued proposed regulations further clarifying the AMP and FUL changes described above and has indicated that the final rule will be issued on January 1, 2014.

Until CMS provides final guidance and the industry adapts to this now public available pricing information, the Corporation is unable to fully evaluate the impact of the changes in FUL and AMP to its business.

### ***Part D Coverage Gap***

Starting on January 1, 2011, the Medicare Coverage Gap Discount Program (the Program ) requires drug manufacturers to provide a 50% discount on the negotiated ingredient cost to certain Medicare Part D beneficiaries for certain drugs and biologics purchased during the coverage gap (this is exclusive of the pharmacy dispensing fee). In addition, the 2010 Health Care Reform Legislation requires Medicare to close or eliminate the coverage gap entirely by fiscal year 2020 by gradually reducing the coinsurance percentage for both drugs covered and not covered by the Program for each applicable beneficiary.





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At this time, the Corporation is unable to fully evaluate the impact of the changes to the coverage gap to its business.

### ***Short Cycle Dispensing***

Pursuant to the 2010 Health Care Reform Legislation, Prescription Drug Plans ( PDPs ) are required, under Medicare Part D and Medicare Advantage prescription drug plans ( Medicare Advantage or MAPDs ) to utilize specific, uniform dispensing techniques, such as weekly, daily, or automated dose dispensing, when dispensing covered Medicare Part D drugs to beneficiaries who reside in a long-term care facility to reduce waste associated with 30 to 90 day prescriptions for such beneficiaries. Beginning January 1, 2013, CMS required pharmacies dispensing to long-term care facilities to dispense no more than 14-day supplies of brand-name oral solid medications covered by Medicare Part D. The Corporation fully implemented short cycle dispensing on January 1, 2013. The impact of short cycle dispensing is not expected to have a material adverse impact on the Corporation's results of operations.

### ***Overview of Reimbursement***

Medicare is a federal program that provides certain hospital and medical insurance benefits to persons age 65 and over and to certain disabled persons. Medicaid is a medical assistance program administered by each state that provides healthcare benefits to certain indigent patients. Within the Medicare and Medicaid statutory framework, there are substantial areas subject to administrative rulings, interpretations, and discretion that may affect payments made under Medicare and Medicaid.

We receive payment for our services from institutional healthcare providers, commercial Medicare Part D Plans, third party payer government reimbursement programs such as Medicare and Medicaid, and other non-government sources such as commercial insurance companies, health maintenance organizations, preferred provider organizations, and contracted providers. With respect to our skilled nursing facilities customers, their residents are covered by Medicare Part A, Part B and Part D Plans, Medicaid, insurance, and other private payers (including managed care).

### ***Medicare***

The Medicare program consists of four parts: (i) Medicare Part A, which covers, among other things, in-patient hospital, skilled nursing facilities, home healthcare, and certain other types of healthcare services; (ii) Medicare Part B, which covers physicians' services, outpatient services, and certain items and services provided by medical suppliers such as intravenous therapy; (iii) Medicare Part C or Medicare Advantage, a managed care option for beneficiaries who are entitled to Medicare Part A and enrolled in Medicare Part B, and (iv) Medicare Part D, which provides coverage for prescription drugs that are not otherwise covered under Medicare Part A or Part B for those beneficiaries that enroll.

### ***Part A***

The Balanced Budget Act of 1997 (the BBA ) mandated the Prospective Payment System ( PPS ) for Medicare-eligible enrolled residents in skilled nursing facilities. Under PPS, Medicare pays skilled nursing facilities a fixed fee per patient per day for extended care services to patients, covering substantially all items and services furnished during such enrollee's stay. Such services and items include pharmacy services and prescription drugs. We bill skilled nursing facilities based upon a negotiated fee schedule and are paid based on those contractual relationships. We do not receive direct payment from Medicare for patients covered under the Medicare Part A benefit. We classify the revenues recognized from these payers as Institutional Healthcare Providers.

Federal legislation continues to focus on reducing Medicare and Medicaid program expenditures. Such decreases may directly impact the Corporation's customers and their Medicare reimbursement. Given the changing nature of these rules, we are unable at this time to fully evaluate the impact on our business. Any evaluation of budgeting, cost-cutting, and financing of health care must also consider the new federal administration and the impact its proposed health care policies could have on any future cost considerations.

### ***Part B***

The Medicare Modernization Act also changed the Medicare payment methodology and conditions for coverage of certain items of durable medical equipment, prosthetics, orthotics, and supplies ( DMEPOS ) under Medicare Part B. The Corporation provides some of these products to its customers. The changes include, among other things, a new competitive bidding program. Beginning on January 1, 2011 in selected areas and for selected supplies, only suppliers that were winning bidders are eligible to provide services, at prices established as a result of the competitive bids, to Medicare beneficiaries. Enteral nutrients, equipment and supplies, oxygen equipment, hospital beds, walkers, negative pressure wound therapy pumps and supplies are among the 10 categories of DMEPOS included in the first round of the competitive bidding process. The Corporation submitted bids in all geographic areas for the enteral nutrient category prior to the March 3, 2012 deadline set by CMS. The bidding

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and selection process has been completed and implementation of the contracts and pricing was effective July 1, 2013. Medicare Part B is not material to the Corporation, representing 0.08% of revenues.

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***Part D***

Medicare Part D provides coverage for prescription drugs that are not otherwise covered under Medicare Part A or Part B for those beneficiaries that enroll. Under Medicare Part D, beneficiaries may enroll in prescription drug plans offered by private commercial insurers who contract with CMS (or in a fallback plan offered on behalf of the government through a contractor, to the extent private entities fail to offer a plan in a given area), which provide coverage of outpatient prescription drugs (collectively, Part D Plans). Part D Plans include both plans providing the drug benefit on a standalone basis and Medicare Advantage plans providing drug coverage as a supplement to an existing medical benefit under that Medicare Advantage plan. Medicare beneficiaries generally have to pay a premium to enroll in a Part D Plan, with the premium amount varying from one Part D Plan to another, although CMS provides various federal subsidies to Part D Plans to reduce the cost to beneficiaries.

Part D Plans are required to make available certain drugs on their formularies. Dually-eligible residents in nursing centers generally are entitled to have their prescription drug costs covered by a Part D Plan, provided that the prescription drugs which they are taking are either on the Part D Plan's formulary or an exception to the Part D Plan's formulary is granted. CMS reviews the formularies of Part D Plans and requires these formularies to include the types of drugs most commonly used by Medicare beneficiaries. CMS also reviews the formulary exceptions criteria of the Part D Plans that provide for coverage of drugs determined by the Part D Plan to be medically appropriate for the enrollee; however there currently is not a separate formulary for long-term care residents.

We obtain reimbursement for drugs provided to enrollees of the given Part D Plan in accordance with the terms of agreements negotiated between us and the Part D Plan. The Medicare Part D final rule prohibits Part D plans from paying for drugs and services not specifically called for by the BBA.

Medicare Part D does not alter federal reimbursement for residents of nursing centers whose stay at the nursing center is covered under Medicare Part A. Accordingly, Medicare's fixed per diem payments to nursing centers under PPS will continue to include a portion attributable to the expected cost of drugs provided to such residents. We will, therefore, continue to receive reimbursement for drugs provided to such residents from the nursing center in accordance with the terms of our agreements with each nursing center.

In addition, we receive rebates from pharmaceutical manufacturers for undertaking certain activities that the manufacturers believe may increase the likelihood that we will dispense their products. CMS continues to question whether institutional pharmacies should be permitted to receive these access/performance rebates from manufacturers with respect to prescriptions covered under Medicare Part D, but has not prohibited the receipt of such rebates. CMS defines these as rebates a manufacturer provides to long-term care pharmacies that are designed to prefer, protect, or maintain that manufacturer's product selection by the long-term care pharmacy or to increase the volume of that manufacturer's products that are dispensed by the pharmacy under its formulary. CMS, in 2007, required PDPs to have policies and systems in place as part of their drug utilization management programs to protect beneficiaries and reduce costs when long-term care pharmacies receive incentives to move market share through access/performance rebates. The elimination or substantial reduction of manufacturer rebates, if not offset by other reimbursement, would have an adverse effect on our business.

***Medicaid***

The reimbursement rate for pharmacy services under Medicaid is determined on a state-by-state basis subject to review by CMS and applicable federal law. Although Medicaid programs vary from state to state, they generally provide for the payment of certain pharmacy services, up to established limits, at rates determined in accordance with each state's regulations. The federal Medicaid statute specifies a variety of requirements that a state plan must meet, including the requirements related to eligibility, coverage for services, payment, and admissions. For residents that are eligible for Medicaid only, and are not dual eligible covered under Medicare Part D, we bill the individual state Medicaid program or in certain circumstances the state's designated managed care or other similar organizations. Federal regulations and the regulations of certain states establish upper limits for reimbursement of certain prescription drugs under Medicaid. In most states, pharmacy services are priced at the lower of usual and customary charges or cost, which generally is defined as a function of average wholesale price and may include a profit percentage plus a dispensing fee. Most states establish a fixed dispensing fee per prescription that is adjusted to reflect associated cost. Over the last several years, state Medicaid programs have lowered reimbursement through a variety of mechanisms, principally higher discounts off average wholesale price levels, expansion of the number of medications subject to federal upper limit pricing, and general reductions in contract payment methodology to pharmacies.

**Table of Contents****Critical Accounting Estimates**

The preparation of financial statements in accordance with accounting principles generally accepted in the U.S. requires us to make estimates and assumptions that affect reported amounts and related disclosures. Management considers an accounting estimate to be critical if:

It requires assumptions to be made that were uncertain at the time the estimate was made; and

Changes in the estimate or different estimates could have a material impact on our condensed consolidated results of operations or financial condition.

The critical accounting estimates discussed below are not intended to be a comprehensive list of all of the Corporation's accounting policies that require estimates. Management believes that of the significant accounting policies, as discussed in Note 1 of the condensed consolidated financial statements included elsewhere in this report, the estimates discussed below involve a higher degree of judgment and complexity. Management believes the current assumptions and other considerations used to estimate amounts reflected in the condensed consolidated financial statements are appropriate. However, if actual experience differs from the assumptions and other considerations used in estimating amounts reflected in the condensed consolidated financial statements, the resulting changes could have a material adverse effect on the condensed consolidated results of operations and financial condition of the Corporation.

***Allowance for doubtful accounts and provision for doubtful accounts***

Accounts receivable primarily consist of amounts due from PDP's under Medicaid Part D, long-term care institutions, the respective state Medicaid programs, private payers and third party insurance companies. Our ability to collect outstanding receivables is critical to our results of operations and cash flows. We establish an allowance for doubtful accounts to reduce the carrying value of our receivables to their estimated net realizable value. In addition, certain drugs dispensed are subject to being returned and the responsible paying party is due a credit for such returns.

Our allowance for doubtful accounts, included in our condensed consolidated balance sheets at December 31, 2012 and June 30, 2013, were \$56.4 million and \$54.8 million, respectively.

Our quarterly provision for doubtful accounts included in our condensed consolidated income statements was as follows (dollars in millions):

	Amount	% of Revenues		Amount	% of Revenues
<b>2012</b>			<b>2013</b>		
First Quarter	\$ 6.2	1.2%	First Quarter*	\$ 5.3	1.2%
Second Quarter	6.2	1.4	Second Quarter	5.2	1.2
Third Quarter	7.3	1.7			
Fourth Quarter*	5.5	1.3			

\* Excludes a \$0.7 million and \$0.2 million expense related to Hurricane Sandy for the Fourth Quarter of 2012 and the First Quarter of 2013, respectively. See further discussion in Note 9.

The largest components of bad debts in our accounts receivable relate to the accounts for which private payers are responsible (which we refer to as private and other), accounts for which our customers from long-term care institutions are responsible for under Medicare Part A and owe us for the drug component of their patients stay at their respective institution and third party, Medicare Part D, and Medicaid accounts that have been denied.

The Corporation has an established process to determine the adequacy of the allowance for doubtful accounts, which relies on analytical tools, specific identification, and benchmarks to arrive at a reasonable allowance. No single statistic or measurement alone determines the allowance for doubtful accounts.

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We monitor and review trends by payer classification along with the composition of our aging accounts receivable. This review is focused primarily on trends in private and other payers, PDP s, dual eligible co-payments, historic payment patterns of long-term care institutions, and monitoring respective credit risks.

In addition, we analyze other factors such as revenue days in accounts receivables, denial trends by payer types, payment patterns by payer types, subsequent cash collections, and current events that may impact payment patterns of our long-term care institution customers.

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The following table shows our pharmacy revenue days outstanding reflected in our pharmacy net accounts receivable as of the quarters indicated:

	2012	2013
First Quarter	42.8	41.8
Second Quarter	45.4	41.9
Third Quarter	44.1	
Fourth Quarter	44.1	

The following table shows our summarized aging categories by quarter:

	2012				2013	
	First	Second	Third	Fourth	First	Second
0 to 60 days	61.5%	58.0%	58.6%	58.8%	58.0%	58.0%
61 to 120 days	17.3	17.7	15.7	17.1	15.8	18.2
Over 120 Days	21.2	24.3	25.7	24.1	26.2	23.8

The following table shows our allowance for doubtful accounts as a percent of gross accounts receivable:

	2012			2013			
	Allowance	Gross Accounts Receivable	% of Gross Accounts Receivable	Allowance	Gross Accounts Receivable	% of Gross Accounts Receivable	
2012				2013			
First Quarter	\$ 52.1	\$ 296.4	17.6%	First Quarter	\$ 55.8	\$ 263.5	21.2%
Second Quarter	52.8	272.1	19.4	Second Quarter	54.8	250.9	21.8
Third Quarter	56.1	266.0	21.1				
Fourth Quarter	56.4	263.0	21.4				

We recognize revenues at the time services are provided or products are delivered. A significant portion of our revenues are billed to PDPs under Medicare Part D, the state Medicaid programs, long-term care institutions, third party insurance companies, and private payers. Some claims are electronically adjudicated through online processing at the point the prescription is dispensed such that our operating system is automatically updated with the actual amount to be reimbursed. As a result, our revenues and the associated receivables are based upon the actual reimbursement to be received. For claims that are adjudicated on-line and are rejected or otherwise denied upon submission, the Corporation provides contractual allowances based upon historical trends, contractual reimbursement terms and other factors which may impact ultimate reimbursement. Amounts are adjusted to actual reimbursed amounts based upon cash receipts.

The Corporation's specialty infusion services revenues are recognized on the date that services and related products are provided to patients and are recorded at amounts estimated to be received under reimbursement arrangements with payers. Substantially all the Corporation's specialty infusion services revenues are derived from fees charged for patient care under fee-for-service arrangements.

Our hospital pharmacy management revenues represent contractually defined management fees and the reimbursement of costs associated with the direct operations of hospital pharmacies, and are primarily comprised of personnel costs.

Co-payments for our services can be applicable under Medicare Part D, the state Medicaid programs, and certain third party payers and are typically not collected at the time products are delivered or services are provided. Co-payments under the Medicaid programs and third party plans are generally billed to the responsible party as part of our normal billing procedures which are subject to normal collection procedures.

Under Medicare Part D, institutional residents who are dual eligible have co-payments due from the responsible party for up to the first thirty days of a beneficiary's stay in a skilled nursing facility subsequent to which the PDP's are responsible for reimbursement.

Under certain circumstances, including state-mandated return policies under various Medicaid programs, we accept returns of medications and issue credit memorandums to the applicable payer. Product returns are processed in the period returned. We estimate an amount for expected returns based on historical trends. Please refer to Note 7 to our accompanying condensed consolidated financial statements and footnotes

included elsewhere in this quarterly report for a further discussion of our revenue recognition policies.

**Table of Contents*****Inventory and cost of drugs dispensed***

We have inventory located at each of our pharmacy locations. Our inventory is valued at the lower of first-in, first-out cost or market. The inventory consists of prescription drugs, over the counter products and intravenous solutions. Our inventory relating to controlled substances is maintained on a manually prepared perpetual system to the extent required by the Drug Enforcement Agency and state board of pharmacies. All other inventory is maintained on a periodic system, through the performance of physical inventories at the end of each quarter. All inventory counts are reconciled to the balance sheet account and differences are adjusted through cost of goods sold. In addition, we record an amount of potential returns of prescription drugs based on historical rates of returns.

As of December 31, 2012 and June 30, 2013, our inventories on our accompanying condensed consolidated balance sheets were \$135.7 million and \$113.2 million, respectively.

Our inventory turns were as follows for the periods presented:

	2012	2013
First Quarter	11.0	8.6
Second Quarter	10.6	9.4
Third Quarter	10.3	
Fourth Quarter	8.9	

We account for rebates and other incentives received from vendors and suppliers, relating to the purchase or distribution of inventory, as a reduction to cost of goods sold and inventory. We consider these rebates to represent product discounts, and as a result, the rebates are allocated as a reduction of product cost and relieved through cost of goods sold upon the sale of the related inventory.

***Goodwill, other intangible assets and accounting for business combinations***

Goodwill represents the excess of the purchase price over the fair value of the net assets of acquired companies. Our intangible assets are comprised primarily of trade names, customer relationship assets, and non-compete agreements.

Our goodwill included in our accompanying condensed consolidated balance sheets as of December 31, 2012 and June 30, 2013 was \$268.5 million.

Our net intangible assets included in our accompanying condensed consolidated balance sheets as of December 31, 2012 and June 30, 2013 were \$121.9 million and \$116.3 million, respectively. The amount of accumulated amortization of intangible assets as of December 31, 2012 and June 30, 2013 was \$46.5 million and \$54.5 million, respectively.

The Corporation performs an annual, and more frequent if necessary, qualitative assessment of its reporting units to determine if it is necessary to proceed to the first step of the two-step goodwill impairment test. The Corporation is not required to do so unless, based on the qualitative assessment, it is determined that it is more likely than not that the fair value of the reporting unit is less than its carrying amount. The qualitative analysis requires the Corporation to examine a wide range of factors, including macro economic factors, industry and market considerations, overall financial performance of the Corporation, and other relevant entity specific factors affecting a reporting unit such as a change in the composition or carrying amount of its net assets and changes in share price. If the Corporation must continue to step one, then we determine fair value using widely accepted valuation techniques, including discounted cash flow and market multiple analyses. These types of analyses require us to make assumptions and estimates regarding future cash flows, industry economic factors and the profitability of future business strategies.

The Corporation performed a qualitative assessment as of December 31, 2012, and did not find it necessary to perform the first step of the two-step impairment test based on that analysis. In addition, as a result of the Corporation being notified during May 2013 that it will be losing its largest customer effective December 31, 2013, the Corporation performed the first step of the two step analysis for the pharmacy segment during the second quarter of 2013 and determined that an impairment of goodwill did not occur as a result of this triggering event. The Corporation's discounted cash flows as calculated for the step one analysis were approximately 26% greater than current book value.

The purchase prices of acquisitions are allocated to the assets acquired and liabilities assumed based upon their respective fair values. Such valuations require us to make significant estimates and assumptions, including projections of future events and operating performance.



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Fair value estimates are determined by management based upon and derived from appraisals, established market values of comparable assets, or internal calculations of estimated future net cash flows. Our estimate of future cash flows is based on assumptions and projections we believe to be currently reasonable and supportable. The ultimate decision regarding purchase price allocation is that of management.

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We assess for the potential impairment of intangible assets and finite-lived assets recorded on the Corporation's balance sheet whenever events or changes in circumstances indicate that their carrying amounts may not be recoverable.

*Accounting for income taxes*

The provision for income taxes is based upon the Corporation's annual taxable income or loss for each respective accounting period. The Corporation recognizes an asset or liability for the deferred tax consequences of temporary differences between the tax basis of assets and liabilities and their reported amounts in the condensed consolidated financial statements. Deferred tax assets generally represent items that will result in a tax deduction in future years for which we have already recorded the tax benefit in the accompanying condensed consolidated income statements. The Corporation also recognizes as deferred tax assets the future tax benefits from net operating and capital loss carryforwards. Conversely deferred tax liabilities represent a temporary difference which will be taxed in a future period.

We assess the likelihood that deferred tax assets will be recovered as an offset to future taxable income. A valuation allowance is provided for deferred tax assets if it is more-likely-than-not that some portion or all of the net deferred tax assets will not be realized. Our deferred tax asset balances in our condensed consolidated balance sheets as of December 31, 2012 and June 30, 2013, were \$25.6 million and \$22.7 million, respectively, including the impact of valuation allowances. Our valuation allowances for state deferred tax assets in our condensed consolidated balance sheets as of December 31, 2012 and June 30, 2013 were \$1.0 million.

Please refer to Note 11 to our condensed consolidated financial statements included elsewhere in this report for further discussion of our accounting for income taxes.

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### **Key Financial Statement Components**

#### ***Consolidated Income Statements***

Our revenues are comprised primarily of product and infusion service revenues and are derived from the sale of prescription drugs through our pharmacies. The majority of our product and service revenues are derived on a fee-for-service basis. Our revenues are recorded net of certain discounts and estimates for returns.

Cost of goods sold is comprised primarily of the cost of product. Our cost of product relating to drugs dispensed by our pharmacies consists primarily of the cost of inventory dispensed and our costs incurred to process and dispense the prescriptions. Cost of goods sold also includes direct labor, delivery costs, rent, utilities, depreciation, travel costs, professional fees and other costs attributable to the dispensing of medications. In addition, cost of product includes a credit for rebates earned directly or indirectly from pharmaceutical manufacturers whose drugs are included in our formularies. These rebates generally take the form of formulary rebates, which are earned based on the volume of a specific drug dispensed, or market share rebates, which are earned based on the achievement of contractually specified market share levels. The Corporation receives rebates on brand and generic drugs dispensed and other administrative rebates.

Selling, general and administrative expenses reflect the costs of operations dedicated to executive management, the generation of new sales, maintenance of existing client relationships, management of clinical programs, enhancement of technology capabilities, direction of pharmacy operations, human resources and performance of reimbursement and collection activities, in addition to finance, legal and other staff activities.

Merger, acquisition, integration costs and other charges represent the costs associated with integrating our operations, as well as costs related to acquisitions. Also included in this category are costs related to the unsolicited tender offer by Omnicare and costs related to the transition of the information technology services being provided by the Corporation's current vendor to another vendor (IT Transition).

Hurricane Sandy disaster costs reflect costs associated with damages caused by Hurricane Sandy in October 2012 and the related insurance recovery from the effects of the storm to the Corporation's operations.

Interest expense, net, primarily includes interest expense relating to our senior secured credit facility, partially offset by interest income generated by cash and cash equivalents.

#### ***Consolidated Balance Sheets***

Our assets include cash and cash equivalent investments, accounts receivable, inventory, fixed assets, deferred tax assets, goodwill and intangibles.

Cash reflects the accumulation of positive cash flows from our operations and financing activities, and primarily includes deposits with banks or other financial institutions. Our cash balances are at the highest on Thursday nights and at the lowest on Friday nights. Friday is usually our largest cash disbursement day as a result of payments for our drug costs and our payrolls.

Accounts receivable primarily consist of amounts due from PDPs under Medicare Part D, the respective state Medicaid programs, long-term care institutions, third party insurance companies, and private payers, net of allowances for doubtful accounts, as well as contractual allowances.

Inventory reflects the cost of prescription products held for dispensing by our pharmacies, net of allocated rebates, and is valued at the lower of first-in, first-out cost or market. We perform quarterly inventory counts and record our inventory and cost of goods sold based on such quarterly inventories. We also include an estimate for returns on inventory.

Deferred tax assets and liabilities primarily represent temporary differences between the financial statement basis and the tax basis of certain assets or liabilities.

Fixed assets include investments in our pharmacies and information technology, including capitalized software development. Goodwill and intangible assets are comprised primarily of goodwill and intangibles related to our previous acquisitions.

Our primary liabilities include accounts payable, accrued salaries and wages, other current liabilities, debt, and deferred tax liabilities. Accounts payable primarily consist of amounts payable for prescription inventory purchases under our Amended Prime Vendor Agreement and other purchases made in the normal course of business. The balances in accounts payable and accrued salaries and wages are at the highest on

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Thursday nights and at the lowest on Friday nights, as a result of payments for drug costs and payroll being funded on Friday. Accrued expenses and other current liabilities primarily consist of employee and facility-related cost accruals incurred in the normal course of business, as well as income taxes payable.

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Our debt is primarily comprised of loans under our senior secured credit facility as well as our revolving credit facility. Deferred tax liabilities primarily represent temporary differences between the financial statement basis and tax basis of fixed assets and tax deductible goodwill. We do not have any off-balance sheet arrangements, other than purchase commitments and lease obligations.

### ***Consolidated Statements of Cash Flows***

Important elements of our operating cash flows are the timing of billing cycles, subsequent cash collections and payments for drug costs and labor. Due to the nature of the Corporation's cash cycle, cash flows from operations can fluctuate significantly depending on the day of the week of the respective close process. We pay for our prescription drug inventory in accordance with payment terms offered under the First Amendment of the Amended Prime Vendor Agreement. Outgoing cash flows include inventory purchases, employee payroll and benefits, facility operating expenses, capital expenditures including technology investments, interest and principal payments on our outstanding debt, and income taxes. The cost of acquisitions will also result in cash outflows.

### **Definitions**

Listed below are definitions of terms used by the Corporation in managing the business. The definitions are necessary to the understanding of the Management's Discussion and Analysis section of this document.

*Gross profit per prescription dispensed:* Represents the gross profit divided by the total prescriptions dispensed.

*Gross profit margin:* Represents the gross profit per prescription dispensed divided by the revenue per prescription dispensed.

*Prescriptions dispensed:* Represents a prescription filled for an individual patient. A prescription will usually be for a 14 or 30 day period and will include only one drug type.

*Revenues per prescription dispensed:* Represents the revenues divided by the total prescriptions dispensed.

**Table of Contents****Results of Operations**

The following table presents selected consolidated comparative results of operations and statistical information for the periods presented (dollars in millions, except per prescription, and prescriptions dispensed in thousands):

	Three Months Ended June 30,					Six Months Ended June 30,						
	2012		Increase (Decrease)		2013	2012		Increase (Decrease)		2013		
	Amount	% of Total Revenues		%	Amount	% of Total Revenues	Amount	% of Total Revenues		%	Amount	% of Total Revenues
Revenues	\$ 458.5	100.0%	\$ (27.7)	(6.0)%	\$ 430.8	100.0%	\$ 957.4	100.0%	\$ (86.8)	(9.1)%	\$ 870.6	100.0%
Cost of goods sold	382.6	83.4	(34.4)	(9.0)	348.2	80.8	808.9	84.5	(105.2)	(13.0)	703.7	80.8
Gross profit	\$ 75.9	16.6%	\$ 6.7	8.8%	\$ 82.6	19.2%	\$ 148.5	15.5%	\$ 18.4	12.4%	\$ 166.9	19.2%

*Pharmacy (in whole numbers except where indicated)*

**Financial data**

Prescriptions dispensed (in thousands)	9,879	(459)	(4.6)%	9,420	19,964	(832)	(4.2)%	19,132
Revenue per prescription dispensed	\$ 46.41	\$ (0.68)	(1.5)%	\$ 45.73	\$ 47.96	\$ (2.46)	(5.1)%	\$ 45.50
Gross profit per prescription dispensed	\$ 7.68	\$ 1.09	14.1%	\$ 8.77	\$ 7.44	\$ 1.28	17.2%	\$ 8.72
Gross profit margin	16.6%	2.6%	15.7%	19.2%	15.5%	3.7%	23.6%	19.2%
Generic dispensing rate	83.2%	0.1%	0.1%	83.3%	82.1%	1.2%	1.5%	83.3%

**Revenues**

Revenues decreased \$27.7 million for the three months ended June 30, 2013 compared to the three months ended June 30, 2012 due to the net decline in prescriptions dispensed, resulting from the decrease in the number of customer licensed beds serviced. The decline was partially offset by the acquisition of Amerita in the fourth quarter of 2012. The decrease of \$27.7 million is comprised of an unfavorable volume variance of approximately \$21.3 million or 459,000 less prescriptions dispensed and an unfavorable rate variance of approximately \$6.4 million or \$0.68 decrease per prescription dispensed.

Revenues decreased \$86.8 million for the six months ended June 30, 2013 compared to the six months ended June 30, 2012 due to the net decline in prescriptions dispensed and an increase in the generic dispensing rate which lowers revenues, along with one less workday in the six months ended June 30, 2013. The decline was partially offset by the acquisition of Amerita in the fourth quarter of 2012. The decrease of \$86.8 million is comprised of an unfavorable volume variance of approximately \$39.9 million or 832,000 less prescriptions dispensed and an unfavorable rate variance of approximately \$46.9 million or \$2.46 decrease per prescription dispensed.

**Gross Profit**

Gross profit for the three months ended June 30, 2013 was \$82.6 million or \$8.77 per prescription dispensed compared to \$75.9 million or \$7.68 per prescription dispensed for the three months ended June 30, 2012. Gross profit margin for the three months ended June 30, 2013 was 19.2% compared to 16.6% for the three months ended June 30, 2012. Gross profit margin was positively impacted by the effects of the Corporation's purchasing strategies and the slight increase in the generic dispensing rate.

Gross profit for the six months ended June 30, 2013 was \$166.9 million or \$8.72 per prescription dispensed compared to \$148.5 million or \$7.44 per prescription dispensed for the six months ended June 30, 2012. Gross profit margin for the six months ended June 30, 2013 was 19.2% compared to 15.5% for the six months ended June 30, 2012. Gross profit margin was positively impacted by the effects of the Corporation's purchasing strategies and the increase in the generic dispensing rate.

**Selling, General and Administrative Expenses**

Selling, general and administrative expenses were \$55.5 million for the three months ended June 30, 2013 compared to \$54.9 million for the three months ended June 30, 2012. The increase of \$0.6 million is due primarily to an increase of \$2.3 million in labor costs, of which \$3.0 million is related to the Amerita acquisition, partially offset by a decrease of \$0.7 million in labor costs for the remainder of the Corporation. The increase in labor is partially offset by a \$1.7 million decrease in contracted services and \$1.0 million decrease in bad debt expense. All other costs included in selling, general and administrative expenses increased approximately \$1.0 million.

Selling, general and administrative expenses were \$112.2 million for the six months ended June 30, 2013 compared to \$107.3 million for the six months ended June 30, 2012. The increase of \$4.9 million is due primarily to an increase of \$6.1 million in labor costs, which is related to the Amerita acquisition partially offset by a decrease of \$3.1 million in contracted services and \$1.9 million decrease in bad debt expense. All other costs included in selling, general and administrative expenses increased approximately \$3.8 million.

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### **Depreciation and Amortization**

Depreciation expense was \$4.8 million for the three months ended June 30, 2013 compared to \$4.5 million for the three months ended June 30, 2012. The increase of \$0.3 million is due primarily to depreciation expense recognized on assets acquired with Amerita and computer hardware additions purchased in the fourth quarter 2012 related to the IT Transition.

Depreciation expense was \$9.6 million for the six months ended June 30, 2013 compared to \$9.3 million for the six months ended June 30, 2012. The increase of \$0.3 million is due primarily to depreciation expense recognized on assets acquired with Amerita and computer hardware additions purchased in the fourth quarter 2012 related to the IT Transition.

Amortization expense was \$3.9 million for the three months ended June 30, 2013 compared to \$3.0 million for the three months ended June 30, 2012. The increase of \$0.9 million is due primarily to the amortization expense recognized on intangibles acquired through the Amerita acquisition on December 13, 2012.

Amortization expense was \$8.0 million for the six months ended June 30, 2013 compared to \$5.8 million for the six months ended June 30, 2012. The increase of \$2.2 million is due primarily to the amortization expense recognized on intangibles acquired through the Amerita acquisition on December 13, 2012.

### **Merger, Acquisition, Integration Costs and Other Charges**

Merger, acquisition, integration costs and other charges were \$2.8 million for both the three months ended June 30, 2013 and June 30, 2012 and were \$5.7 million and \$8.2 million for the six months ended June 30, 2013 and June 30, 2012, respectively.

Integration costs and other charges were \$2.2 million and \$0.5 million for the three months ended June 30, 2013 and 2012, respectively. The increase is primarily attributable to a former executive officer related to a separation agreement. Integration costs and other charges were \$3.7 million and \$3.4 million for the six months ended June 30, 2013 and 2012, respectively. The six months ended June 30, 2012 included \$1.9 million incurred during the first quarter of 2012 related to an unsolicited tender offer.

Acquisition costs were \$0.6 million for the three months ended June 30, 2013 compared to \$2.3 million for the three months ended June 30, 2012 and were \$2.0 million for the six months ended June 30, 2013 compared to \$4.8 million for the six months ended June 30, 2012. Acquisition costs decreased due to decreases in professional fees for potential acquisitions and employee, severance and facility costs associated with prior acquisitions.

### **Interest Expense**

Interest expense was \$2.9 million and \$2.5 million for the three months ended June 30, 2013 and June 30, 2012, respectively. Interest expense was \$5.5 million for the six months ended June 30, 2013 compared to \$5.2 million for the six months ended June 30, 2012. The increase was primarily due to a higher outstanding balance on long-term debt. Long-term debt, including the current portion, was \$257.1 million and \$250.0 million as of June 30, 2013 and June 30, 2012, respectively.

### **Tax Provision**

The provision for income taxes as a percentage of pre-tax income was 44.2% and 40.1% for the three months ended June 30, 2013 and June 30, 2012, respectively. The provision for income taxes as a percentage of pre-tax income was 42.1% and 40.1% for the six months ended June 30, 2013 and June 30, 2012, respectively. The increase in the provision is due to an increase in discrete items associated with the Corporation's stock-based compensation plan and its effect on the provision upon the separation of an executive officer. Excluding the impact of the discrete items, the provision for income taxes as percentage of pre-tax income would have been 40.1%. The effective tax rates in 2013 and 2012 are higher than the federal statutory rate largely as a result of the combined impact of state and local taxes and various non-deductible expenses.



**Table of Contents****Liquidity and Capital Resources**

**Cash Flows** - The following table presents selected data from our condensed consolidated statements of cash flows for the periods presented (dollars in millions):

	Three Months Ended June 30,		Six Months Ended June 30,	
	2012	2013	2012	2013
Net cash provided by operating activities	\$ 31.9	\$ 26.6	\$ 51.8	\$ 74.3
Net cash used in investing activities	(4.6)	(7.2)	(7.0)	(14.4)
Net cash used in financing activities	(22.0)	(14.9)	(50.2)	(59.9)
Net change in cash and cash equivalents	5.3	4.5	(5.4)	
Cash and cash equivalents at beginning of period	6.7	7.8	17.4	12.3
Cash and cash equivalents at end of period	\$ 12.0	\$ 12.3	\$ 12.0	\$ 12.3

**Operating Activities** Cash provided by operating activities aggregated \$26.6 million and \$74.3 million for the three and six months ended June 30, 2013, respectively, compared to \$31.9 million and \$51.8 million for the three and six months ended June 30, 2012, respectively. The decrease in cash provided by operating activities for the three months June 30, 2013 compared to the prior period is a result of a decrease in cash collections on accounts receivable and an increase in inventory purchases resulting from the Corporation's purchasing strategies partially offset by a decrease in cash used for accounts payable. The increase in cash provided by operating activities for the six months ended June 30, 2013 compared to the prior period is due to the increase in net income along with decreases in cash paid for employee compensation and accounts payable.

**Investing Activities** Cash used in investing activities aggregated \$7.2 million and \$14.4 million for the three and six months ended June 30, 2013, respectively, compared to \$4.6 million and \$7.0 million for the three and six months ended June 30, 2012, respectively. The increase in investing activities compared to the prior periods is due primarily to the increase in capital expenditures necessary for the IT Transition and to re-invest in assets lost as a result of Hurricane Sandy in the fourth quarter 2012.

**Financing Activities** Cash used in financing activities aggregated \$14.9 million and \$59.9 million for the three and six months ended June 30, 2013, respectively, compared to \$22.0 million and \$50.2 million for the three and six months ended June 30, 2012, respectively. The decrease in the three months ended June 30, 2013 compared to the prior period is due primarily to a decrease in repayments on the revolving credit facility, partially offset by an increase in term loan debt payments. The increase in the six months ended June 30, 2013 compared to the prior period is due primarily to an increase in term loan debt and revolving credit facility repayments during 2013 along with an increase in treasury stock repurchases.

**Credit Agreement**

On May 2, 2011, the Corporation entered into a long-term credit agreement (the **Credit Agreement**) among the Corporation, the Lenders named therein, and Citibank, N.A. ( **Citibank** ), as Administrative Agent. The Credit Agreement consists of a \$250.0 million term loan facility and a \$200.0 million revolving credit facility. The terms and conditions of the Credit Agreement are customary to facilities of this nature. Indebtedness under the Credit Agreement matures on June 30, 2016, at which time the commitments of the Lenders to make revolving loans also expire.

The Credit Agreement requires term loan principal payments by the Corporation in an amount of \$3.1 million on the last business day of each quarter beginning September 2012 through June 2015 and \$53.1 million on the last business day of each quarter beginning September 2015 through June 2016. The final principal repayment installment of term loans shall be repaid on the term maturity date, June 30, 2016. In addition, the term loan is subject to certain prepayment obligations relating to certain asset sales, certain casualty losses and the incurrence by the Corporation of certain indebtedness.

The Corporation had a total of \$237.5 million outstanding of term debt under the Credit Agreement and a \$19.6 million outstanding balance under the revolving portion of the Credit Agreement as of June 30, 2013. The Credit Agreement provides for the issuance of letters of credit which, when issued, constitute usage and reduce availability on the revolving portion of the Credit Agreement. The amount of letters of credit outstanding as of June 30, 2013 was \$2.0 million. After giving effect to the letters of credit and amounts outstanding under the revolving credit agreement, total availability under the revolving credit facility was \$178.4 million as of June 30, 2013. The revolving credit facility contains a

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\$100.0 million accordion feature, which permits the Corporation to increase the total debt capacity, up to an aggregate of \$537.5 million, subject to securing additional commitments from existing or new lenders.

The Corporation was compliant with all debt covenant requirements at June 30, 2013.

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### **Prime Vendor Agreement**

On January 25, 2013 the Corporation renegotiated its prime vendor agreement with ABDC effective January 1, 2013. The First Amendment modifies the previous agreement, which was set to expire September 30, 2013 and extends its term until September 30, 2016. The First Amendment requires the Corporation to purchase certain levels of brand and non-injectable generic drugs from ABDC. The First Amendment does provide the flexibility for the Corporation to contract with other suppliers. If the Corporation fails to adhere to the contractual purchase provisions ABDC has the ability to increase the Corporation's drug pricing under the terms of the First Amendment.

We also obtain pharmaceutical and other products from contracts negotiated directly with pharmaceutical manufacturers for discounted prices. While the loss of a supplier could adversely affect our business if alternate sources of supply are unavailable, numerous sources of supply are generally available to us.

We seek to maintain an on-site inventory of pharmaceuticals and supplies to ensure prompt delivery to our customers. ABDC maintains local distribution facilities in most major geographic markets in which we operate.

### **Treasury Stock**

During the six months ended June 30, 2013, the Corporation did not repurchase shares of common stock under the share repurchase program.

The Corporation may redeem shares from employees upon the vesting of the Corporation's stock awards for minimum statutory tax withholding purposes. The Corporation redeemed 129,073 shares of certain vested awards for an aggregate price of approximately \$1.9 million during six months ended June 30, 2013. These shares have been designated by the Corporation as treasury stock.

As of June 30, 2013, the Corporation had a total of 1,585,366 shares held as treasury stock.

**Table of Contents****Supplemental Quarterly Information**

The following tables represent the results of the Corporation's quarterly operations for the year ended December 31, 2012 and for the first and second quarters of 2013 (in millions, except where indicated):

	2012 Quarters				2013 Quarters	
	First	Second	Third	Fourth	First	Second
Revenues	\$ 498.9	\$ 458.5	\$ 442.0	\$ 433.2	\$ 439.8	\$ 430.8
Cost of goods sold	426.3	382.6	365.9	357.6	355.5	348.2
Gross profit	72.6	75.9	76.1	75.6	84.3	82.6
Selling, general and administrative	52.4	54.9	54.5	52.9	56.7	55.5
Amortization expense	2.8	3.0	3.2	3.3	4.1	3.9
Merger, acquisition, integration costs, and other charges	5.4	2.8	6.1	5.6	2.9	2.8
Hurricane Sandy disaster costs				4.5	0.6	(0.9)
Operating income	12.0	15.2	12.3	9.3	20.0	21.3
Interest expense, net	2.7	2.5	2.4	2.4	2.6	2.9
Income before income taxes	9.3	12.7	9.9	6.9	17.4	18.4
Provision for income taxes	3.7	5.1	3.9	3.2	6.9	8.2
Net income	\$ 5.6	\$ 7.6	\$ 6.0	\$ 3.7	\$ 10.5	\$ 10.2
<b>Earnings per share (1):</b>						
Basic	\$ 0.19	\$ 0.26	\$ 0.20	\$ 0.13	\$ 0.36	\$ 0.34
Diluted	\$ 0.19	\$ 0.26	\$ 0.20	\$ 0.12	\$ 0.35	\$ 0.34
<b>Adjusted diluted earnings per diluted share (1)(2):</b>	\$ 0.33	\$ 0.35	\$ 0.39	\$ 0.36	\$ 0.46	\$ 0.44
<b>Shares used in computing earnings per share:</b>						
Basic	29.4	29.5	29.5	29.5	29.6	29.7
Diluted	29.7	29.7	29.8	30.0	30.1	30.1
<b>Balance sheet data:</b>						
Cash and cash equivalents	\$ 6.7	\$ 12.0	\$ 49.5	\$ 12.3	\$ 7.8	\$ 12.3
Working capital (3)	\$ 330.0	\$ 316.6	\$ 323.2	\$ 323.0	\$ 292.9	\$ 292.5
Goodwill (3)	\$ 214.9	\$ 214.9	\$ 214.9	\$ 268.5	\$ 268.5	\$ 268.5
Intangible assets, net	\$ 97.8	\$ 95.7	\$ 94.0	\$ 121.9	\$ 120.1	\$ 116.3
Total assets (3)	\$ 800.7	\$ 782.3	\$ 798.2	\$ 886.3	\$ 840.9	\$ 850.3
Long-term debt	\$ 272.1	\$ 250.0	\$ 243.8	\$ 315.5	\$ 271.7	\$ 257.1
Total stockholders' equity	\$ 420.8	\$ 429.7	\$ 437.3	\$ 442.6	\$ 453.6	\$ 465.4
<b>Supplemental information:</b>						
Adjusted EBITDA(2)	\$ 26.8	\$ 26.7	\$ 28.8	\$ 28.9	\$ 34.6	\$ 33.7
Adjusted EBITDA Margin (2)	5.4%	5.8%	6.5%	6.7%	7.9%	7.8%
Adjusted EBITDA per prescription dispensed (2)	\$ 2.66	\$ 2.70	\$ 2.97	\$ 3.03	\$ 3.56	\$ 3.58
Net cash provided by (used in) operating activities	\$ 19.9	\$ 31.9	\$ 51.4	\$ (17.5)	\$ 47.7	\$ 26.6
Net cash used in investing activities	\$ (2.4)	\$ (4.6)	\$ (7.0)	\$ (91.3)	\$ (7.2)	\$ (7.2)
Net cash (used in) provided by financing activities	\$ (28.2)	\$ (22.0)	\$ (6.9)	\$ 71.6	\$ (45.0)	\$ (14.9)
<b>Statistical information (in whole numbers except where indicated)</b>						
<b>Volume information</b>						
Prescriptions dispensed (in thousands)	10,085	9,879	9,711	9,546	9,711	9,420
Revenue per prescription dispensed	\$ 49.47	\$ 46.41	\$ 45.52	\$ 45.38	\$ 45.29	\$ 45.73
Gross profit per prescription dispensed	\$ 7.20	\$ 7.68	\$ 7.84	\$ 7.92	\$ 8.68	\$ 8.77
Gross profit margin	14.6%	16.6%	17.2%	17.5%	19.2%	19.2%
Generic drug dispensing rate	80.9%	83.2%	84.4%	84.8%	83.3%	83.3%

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- (1) The Corporation has never declared a cash dividend. Earnings per common share in actual cents.
- (2) See [Use of Non-GAAP Measures for Measuring Quarterly Results](#) for a definition and Reconciliation of Adjusted Earnings Per Diluted Common Share to Earnings Per Diluted Common Share, and for Reconciliation of Net Income to Adjusted EBITDA and Margin.
- (3) As adjusted, see Note 2 [Acquisitions](#) in the Condensed Consolidated Financial Statements.

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**Table of Contents*****Use of Non-GAAP Measures for Measuring Quarterly Results***

The Corporation calculates Adjusted EBITDA as provided in the reconciliation below and calculates Adjusted EBITDA Margin by taking Adjusted EBITDA and dividing it by revenues. The Corporation calculates and uses Adjusted EBITDA as an indicator of its ability to generate cash from reported operating results. The measurement is used in concert with net income and cash flows from operating activities, which measure actual cash generated in the period. In addition, the Corporation believes that Adjusted EBITDA and Adjusted EBITDA Margin are supplemental measurement tools used by analysts and investors to help evaluate overall operating performance and the ability to incur and service debt and make capital expenditures. In addition, Adjusted EBITDA, as defined in the Credit Agreement, is used in conjunction with the Corporation's debt leverage ratio and this calculation sets the applicable margin for the quarterly interest charge. Adjusted EBITDA, as defined in the Credit Agreement, is not the same calculation as this Adjusted EBITDA table. Adjusted EBITDA does not represent funds available for the Corporation's discretionary use and is not intended to represent or to be used as a substitute for net income or cash flows from operating activities data as measured under U.S. generally accepted accounting principles (GAAP). The items excluded from Adjusted EBITDA but included in the calculation of the Corporation's reported net income and cash flows from operating activities are significant components of the accompanying consolidated income statements and cash flows and must be considered in performing a comprehensive assessment of overall financial performance. The Corporation's calculation of Adjusted EBITDA may not be consistent with calculations of EBITDA used by other companies. The following are reconciliations of Adjusted EBITDA to the Corporation's net income and net operating cash flows for the periods presented.

The Corporation calculates and uses adjusted diluted earnings per share, which is exclusive of the impact of merger, acquisition, integration costs and other charges, Hurricane Sandy disaster costs, stock-based compensation and deferred compensation and impact of discrete items on tax provisions as an indicator of its core operating results. The measurement is used in concert with net income and diluted earnings per share, which measure actual earnings per share generated in the period. The Corporation believes the exclusion of these charges in expressing earnings per share provides management with a useful measure to assess period to period comparability and is useful to investors in evaluating the Corporation's operating results from period to period. Adjusted diluted earnings per share, which is exclusive of the impact of merger, acquisition, integration costs and other charges, Hurricane Sandy disaster costs, stock-based compensation and deferred compensation and impact of discrete items on tax provisions does not represent the amount that effectively accrues directly to stockholders (i.e., such costs are a reduction in earnings and stockholders' equity) and is not intended to represent or to be used as a substitute for earnings per diluted common share as measured under GAAP. The impact of merger, acquisition, integration costs and other charges, Hurricane Sandy disaster costs, stock-based compensation and deferred compensation and impact of discrete items on tax provisions excluded from the earnings per diluted share are significant components of the accompanying consolidated income statements and must be considered in performing a comprehensive assessment of overall financial performance. The following is a reconciliation of adjusted diluted earnings per share to the Corporation's GAAP earnings per diluted common share for the periods presented.

**Table of Contents****Unaudited Reconciliation of Net Income to Adjusted EBITDA**

	2012 Quarters				2013 Quarters	
	First	Second	Third	Fourth	First	Second
Net income	\$ 5.6	\$ 7.6	\$ 6.0	\$ 3.7	\$ 10.5	\$ 10.2
Add:						
Interest expense, net	2.7	2.5	2.4	2.4	2.6	2.9
Merger, acquisition, integration costs and other charges	5.4	2.8	6.1	5.6	2.9	2.8
Hurricane Sandy disaster costs				4.5	0.6	(0.9)
Stock-based compensation and deferred compensation	1.8	1.2	2.6	1.5	2.2	1.8
Provision for income taxes	3.7	5.1	3.9	3.2	6.9	8.2
Depreciation and amortization expense	7.6	7.5	7.8	8.0	8.9	8.7
<b>Adjusted EBITDA</b>	<b>\$ 26.8</b>	<b>\$ 26.7</b>	<b>\$ 28.8</b>	<b>\$ 28.9</b>	<b>\$ 34.6</b>	<b>\$ 33.7</b>
Adjusted EBITDA Margin	5.4%	5.8%	6.5%	6.7%	7.9%	7.8%

**Unaudited Reconciliation of Adjusted EBITDA to Net Operating Cash Flows**

	2012 Quarters				2013 Quarters	
	First	Second	Third	Fourth	First	Second
Adjusted EBITDA	\$ 26.8	\$ 26.7	\$ 28.8	\$ 28.9	\$ 34.6	\$ 33.7
Interest expense, net	(2.7)	(2.5)	(2.4)	(2.4)	(2.6)	(2.9)
Merger, acquisition, integration costs and other charges	(3.8)	(2.5)	(5.8)	(6.5)	(2.9)	(2.8)
Hurricane Sandy disaster costs				(3.0)	(1.2)	(0.1)
Provision for bad debt	6.2	6.2	7.3	5.5	5.3	5.2
Amortization of deferred financing fees	0.2	0.2	0.3	0.3	0.3	0.7
Loss (gain) on disposition of equipment	(0.1)			0.2		(0.1)
Provision for income taxes	(3.7)	(5.1)	(3.9)	(3.2)	(6.9)	(8.2)
Deferred income taxes	2.6	3.4	(2.1)	(1.1)	3.6	(0.7)
Changes in federal and state income tax payable	(0.2)	1.0	4.4	(4.1)	2.8	3.2
Changes in assets and liabilities	(5.2)	4.3	24.7	(32.2)	14.6	(1.6)
Other	(0.2)	0.2	0.1	0.1	0.1	0.2
<b>Net Cash Flows Provided by (Used in) Operating Activities</b>	<b>\$ 19.9</b>	<b>\$ 31.9</b>	<b>\$ 51.4</b>	<b>\$ (17.5)</b>	<b>\$ 47.7</b>	<b>\$ 26.6</b>

**Unaudited Reconciliation of Diluted Earnings Per Share to Adjusted Diluted Earnings Per Share**

	2012 Quarters				2013 Quarters	
	First	Second	Third	Fourth	First	Second
Diluted earnings per share	\$ 0.19	\$ 0.26	\$ 0.20	\$ 0.12	\$ 0.35	\$ 0.34
Add:						
Diluted earnings per share impact of:						
Merger, acquisition, integration costs and other charges	0.11	0.06	0.13	0.11	0.06	0.06
Hurricane Sandy disaster costs				0.09	0.01	(0.02)
Stock-based compensation and deferred compensation	0.03	0.03	0.06	0.03	0.04	0.03
Impact of discrete items on tax provision				0.01		0.03
<b>Adjusted diluted earnings per share</b>	<b>\$ 0.33</b>	<b>\$ 0.35</b>	<b>\$ 0.39</b>	<b>\$ 0.36</b>	<b>\$ 0.46</b>	<b>\$ 0.44</b>





**Table of Contents****Second Quarter 2013 compared to the First Quarter 2013****Results of Operations**

The following table presents selected consolidated comparative results of operations and statistical information for the periods presented (dollars in millions, except per prescription, and prescriptions dispensed in thousands):

	March 31, 2013		Quarter Ended Increase (Decrease)		June 30, 2013	
	Amount	% of Revenues			Amount	% of Revenues
	Revenues	\$ 439.8	100.0%	\$ (9.0)	(2.0)%	\$ 430.8
Cost of goods sold	355.5	80.8	(7.3)	(2.1)	348.2	80.8
Gross profit	\$ 84.3	19.2%	\$ (1.7)	(2.0)%	\$ 82.6	19.2%

**Pharmacy (in whole numbers except where indicated)****Financial data**

Prescriptions dispensed (in thousands)	9,711	(291)	(3.0)%	9,420
Revenue per prescription dispensed	\$ 45.29	\$ 0.44	1.0 %	\$ 45.73
Gross profit per prescription dispensed	\$ 8.68	\$ 0.09	1.0 %	\$ 8.77
Gross profit margin	19.2%	%	%	19.2%
Generic dispensing rate	83.3%	%	%	83.3%

**Revenues**

Revenues decreased \$9.0 million for the three months ended June 30, 2013 compared to the three months ended March 31, 2013 due to the decrease in prescriptions dispensed of 291,000 resulting from a decrease in customer licensed beds. The decrease is comprised of an unfavorable volume variance of \$13.2 million and a favorable rate variance of \$4.2 million.

**Gross Profit and Operating Expenses**

Gross profit for the three months ended June 30, 2013 was \$82.6 million or \$8.77 per prescription dispensed compared to \$84.3 million or \$8.68 per prescription dispensed for the three months ended March 31, 2013. Gross profit margin for the three months ended June 30, 2013 and March 31, 2013 was 19.2% for both periods. Gross profit margin continues to be positively impacted by the effects of the Corporation's purchasing strategies.

**Selling, General and Administrative Expenses**

Selling, general and administrative expenses were \$55.5 million for the three months ended June 30, 2013 compared to \$56.7 million for the three months ended March 31, 2013. The decrease of \$1.2 million is due primarily to a decrease in labor costs.

**Depreciation and Amortization**

Depreciation expense was \$4.8 million for both the three months ended June 30, 2013 and March 31, 2013.

Amortization expense was \$3.9 million for the three months ended June 30, 2013 compared to \$4.1 million for the three months ended March 31, 2013. The decrease of \$0.2 million is due to the reduction of expense related to non-compete agreements associated with former employees.

**Merger, Acquisition, Integration Costs and Other Charges**

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Merger, acquisition, integration costs and other charges decreased to \$2.8 million for the three months ended June 30, 2013 compared to \$2.9 million for the three months ended March 31, 2013.

Integration costs and other charges were \$2.2 million for the three months ended June 30, 2013 compared to \$1.5 million for the three months ended March 31, 2013. The increase is primarily due to severance costs related to former executives and employees of the Corporation.

Acquisition costs were \$0.6 million for the three months ended June 30, 2013 compared to \$1.4 million for the three months ended March 31, 2013. The decrease is primarily due to a decrease in professional fees associated with current or potential acquisitions.

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**Interest Expense**

Interest expense was \$2.9 million for the three months ended June 30, 2013 compared to \$2.6 million for the three months ended March 31, 2013. The increase was primarily due to non-cash amortization of deferred financing costs, partially offset by a lower average balance on the revolving credit facility.

**Tax Provision**

The provision for income taxes as a percentage of pre-tax income was 44.2% and 39.9% for the three months ended June 30, 2013 and March 31, 2013, respectively. The increase in the effective rate is due to an increase in discrete items associated with the Corporation's stock-based compensation plans and its effect on the provision upon the separation of a former executive officer. Excluding the impact of the discrete items, the provision for income taxes as a percentage of pre-tax income would have been 40.1%.

**Table of Contents****Liquidity and Capital Resources**

The following compares the Corporation's Condensed Consolidated Statements of Cash Flows for the three months ended March 31, 2013 and June 30, 2013 (dollars in millions):

	Quarter Ended	
	March 31, 2013	June 30, 2013
Cash flows provided by (used in) operating activities:		
Net income	\$ 10.5	\$ 10.2
Adjustments to reconcile net income to net cash provided by (used in) operating activities:		
Depreciation	4.8	4.8
Amortization	4.1	3.9
Merger, acquisition, integration costs and other charges		
Hurricane Sandy disaster costs	(0.6)	(1.0)
Stock-based compensation and deferred compensation	2.2	1.8
Amortization of deferred financing fees	0.3	0.7
Deferred income taxes	3.6	(0.7)
Gain on disposition of equipment		(0.1)
Other	0.1	0.2
Change in operating assets and liabilities:		
Accounts receivable, net	(1.2)	11.5
Inventory	35.5	(13.0)
Prepays and other assets	3.4	(2.4)
Accounts payable	(12.6)	4.7
Salaries, wages and other compensation	(4.8)	2.1
Other accrued liabilities	2.4	3.9
Net cash provided by operating activities	47.7	26.6
Cash flows provided by (used in) investing activities:		
Purchase of equipment and leasehold improvements	(6.7)	(7.3)
Acquisitions, net of cash acquired	(0.5)	
Cash proceeds from the sale of assets		0.1
Net cash used in investing activities	(7.2)	(7.2)
Cash flows provided by (used in) financing activities:		
Repayments of long-term debt	(3.1)	(3.2)
Net activity of long-term revolving credit facility	(40.5)	(11.6)
Issuance of common stock	0.1	0.3
Treasury stock at cost	(1.8)	(0.1)
Excess tax benefit from stock-based compensation	0.2	0.2
Other	0.1	(0.5)
Net cash used in financing activities	(45.0)	(14.9)
Change in cash and cash equivalents	(4.5)	4.5
Cash and cash equivalents at beginning of period	12.3	7.8
Cash and cash equivalents at end of period	\$ 7.8	\$ 12.3
Supplemental information:		
Cash paid for interest	\$ 2.3	\$ 2.3

Cash paid for taxes	\$ 0.5	\$ 5.9
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**Item 3. Quantitative and Qualitative Disclosures about Market Risk**

During the reporting period, there have been no material changes in the disclosures set forth in Part II, Item 7a in our Form 10-K for the year ended December 31, 2012.

**Item 4. Controls and Procedures**

**Evaluation of Disclosure Controls and Procedures**

The Corporation has carried out an evaluation under the supervision and with the participation of management, including the Corporation's Chief Executive Officer and Chief Financial Officer, of the effectiveness of the design and operation of the Corporation's disclosure controls and procedures as defined in Rule 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934, as amended (the Exchange Act) as of the end of the period covered by this report. The Corporation's disclosure controls and procedures are designed so that information required to be disclosed in the Corporation's reports filed under the Exchange Act, such as this Quarterly Report on Form 10-Q, is recorded, processed, summarized and reported within the time periods specified in the Commission's rules and forms. The Corporation's disclosure controls and procedures are also intended to ensure that such information is accumulated and communicated to the Corporation's management, including the Chief Executive Officer and Chief Financial Officer, as appropriate to allow timely decisions regarding required disclosure. There are inherent limitations to the effectiveness of any system of disclosure controls and procedures, including the possibility of human error and the circumvention or overriding of the controls and procedures. Accordingly, even effective disclosure controls and procedures can only provide reasonable assurance of achieving their control objectives, and management necessarily is required to use its judgment in evaluating the cost-benefit relationship of possible disclosure controls and procedures. Based upon this evaluation, the Chief Executive Officer and Chief Financial Officer have concluded that, as of June 30, 2013, the Corporation's disclosure controls and procedures are effective to provide reasonable assurance that information required to be disclosed in the reports that the Corporation files and submits under the Exchange Act is recorded, processed, summarized and reported as and when required and such information is accumulated and communicated as appropriate to allow timely decisions regarding required disclosures.

**Changes in Internal Control Over Financial Reporting**

There have been no changes in the Corporation's internal control over financial reporting during the quarter ended June 30, 2013, that have materially affected, or are reasonably likely to materially affect, the Corporation's internal control over financial reporting.

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**PART II. OTHER INFORMATION**

**Item 1. Legal Proceedings**

On March 4, 2011, a relator, Mark Silver, on behalf of the U.S. Government and various state governments, filed a complaint in the United States District for the District of New Jersey against the Corporation alleging that the Corporation violated the False Claims Act and Anti-Kickback Statute through its agreements to provide prescription drugs to nursing homes under certain Medicare and Medicaid programs. On February 19, 2013, the U.S. Government declined to intervene in the case. The Corporation believes that it has complied with applicable laws and regulations with respect to these matters and intends to defend itself against these allegations.

See Note 6 to the Corporation's Condensed Consolidated Financial Statements set forth in Part I of this report.

**Item 1A. Risk Factors**

There have been no material changes in our risk factors from those disclosed in the Corporation's Annual Report on Form 10-K for the year ended December 31, 2012. We encourage you to read these risk factors in their entirety.

**Item 2. Unregistered Sales of Equity and Use of Proceeds**

In August 2010, the Board of Directors authorized a stock repurchase program of up to \$25.0 million of the Corporation's common stock, of which \$10.5 million was used. On July 2, 2012 the Board of Directors authorized an increase to the remaining portion of the existing stock repurchase program that will allow the Corporation to again repurchase up to a maximum of \$25.0 million of the Corporation's common stock. The Corporation did not repurchase shares under this program during the three months ended June 30, 2013.

Additionally, the Corporation may redeem shares from employees upon vesting of the Corporation's stock awards for minimum statutory tax withholding purposes. The Corporation redeemed 10,584 shares of certain vested awards for an aggregate price of \$0.1 million during the three months ended June 30, 2013. These shares have been designated by the Corporation as treasury stock.

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The following table summarizes our share repurchase activity by month for the three months ended June 30, 2013:

<b>Period</b>	<b>Total Number of Shares Purchased</b>	<b>Weighted Average Price Paid per Share</b>	<b>Total Number of Shares Purchased as Part of a Publicly Announced Plans or Program (2)</b>	<b>Approximate Dollar Value of Shares that may yet be Purchased under the Plans or Programs (in millions)</b>
April 1, 2013 - April 30, 2013	6,066 (1)	\$ 14.03		\$ 24.0
May 1, 2013 - May 31, 2013	239 (1)	14.12		24.0
June 1, 2013 - June 30, 2013	4,279 (1)	15.28		24.0

(1) The Corporation repurchased 10,584 shares of common stock in connection with the vesting of certain stock awards to cover minimum statutory withholding taxes.

(2) The Corporation did not repurchase shares under this program for the three months ended June 30, 2013.

**Item 4. Mine Safety Disclosures**

Not Applicable



**Table of Contents****Item 6. Exhibits**

<b>Exhibit No.</b>	<b>Description</b>
31.1*	Certification of Chief Executive Officer required by Rule 13a-14(a) or Rule 15d-14(a) of the Securities Exchange Act of 1934, as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
31.2*	Certification of Chief Financial Officer required by Rule 13a-14(a) or Rule 15d-14(a) of the Securities Exchange Act of 1934, as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
32.1*	Certification of Chief Executive Officer, pursuant to 18 U.S.C. 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002
32.2*	Certification of Chief Financial Officer pursuant to 18 U.S.C. 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002
101.INS**	XBRL Instance Document.
101.SCH**	XBRL Taxonomy Extension Schema Document.
101.CAL**	XBRL Taxonomy Extension Calculation Linkbase Document.
101.DEF**	XBRL Taxonomy Extension Definition Linkbase Document.
101.LAB**	XBRL Taxonomy Extension Label Linkbase Document.
101.PRE**	XBRL Taxonomy Extension Presentation Linkbase Document.

\* Furnished herewith.

\*\* As provided in Rule 406T of Regulation S-T, this information is furnished herewith and not filed for purposes of sections 11 and 12 of the Securities Act of 1933 or section 18 of the Securities Exchange Act of 1934.

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**SIGNATURES**

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

Date: August 2, 2013

PHARMERICA CORPORATION

/s/ GREGORY S. WEISHAR  
**Gregory S. Weishar**  
**Chief Executive Officer and**

**Director**

Date: August 2, 2013

/s/ DAVID W. FROESEL, JR.  
**David W. Froesel, Jr.**  
**Executive Vice President, Chief**

**Financial Officer and Treasurer**

Date: August 2, 2013

/s/ BERARD E. TOMASSETTI  
**Berard E. Tomassetti**  
**Senior Vice President and**

**Chief Accounting Officer**

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