

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

Form 10-K

(Mark One)

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

FOR THE FISCAL YEAR ENDED DECEMBER 31, 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 1-11151

U.S. PHYSICAL THERAPY, INC.
(EXACT NAME OF REGISTRANT AS SPECIFIED IN ITS CHARTER)

NEVADA
(STATE OR OTHER JURISDICTION OF
INCORPORATION OR ORGANIZATION)

76-0364866
(I.R.S. EMPLOYER
IDENTIFICATION NO.)

1300 WEST SAM HOUSTON PARKWAY SOUTH,
SUITE 300,
HOUSTON, TEXAS
(ADDRESS OF PRINCIPAL EXECUTIVE OFFICES)

77042
(ZIP CODE)

REGISTRANT'S TELEPHONE NUMBER, INCLUDING AREA CODE: (713) 297-7000
SECURITIES REGISTERED PURSUANT TO SECTION 12(b) OF THE EXCHANGE ACT:

Title of Each Class

Name of Each Exchange on Which Registered

Common Stock, \$.01 par value

New York Stock Exchange

SECURITIES REGISTERED PURSUANT TO SECTION 12(g) OF THE EXCHANGE ACT: NONE

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes No

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or 15(d) of the Act. Yes No

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Exchange Act 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 Website, 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 if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K.

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 (Do not check if a smaller reporting company)

Smaller reporting company

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

The aggregate market value of the shares of the registrant's common stock held by non-affiliates of the registrant at June 30, 2013 was \$250,528,000 based on the closing sale price reported on the NYSE for the registrant's common stock on June 28, 2013, the last business day of the registrant's most recently completed second fiscal quarter. For purposes of this computation, all executive officers, directors and 5% or greater beneficial owners of the registrant were deemed to be affiliates. Such determination should not be deemed an admission that such executive officers, directors and beneficial owners are, in fact, affiliates of the registrant.

As of March 11, 2014, the number of shares outstanding of the registrant's common stock, par value \$.01 per share, was: 12,198,365.

DOCUMENTS INCORPORATED BY REFERENCE

DOCUMENT

PART OF FORM 10-K

Portions of Definitive Proxy Statement for the 2014 Annual Meeting of Shareholders

PART III

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FORWARD-LOOKING STATEMENTS

We make statements in this report that are considered to be forward-looking statements within the meaning given such term under Section 21E of the Securities Exchange Act of 1934, as amended (the “Exchange Act”). These statements contain forward-looking information relating to the financial condition, results of operations, plans, objectives, future performance and business of our Company. These statements (often using words such as “believes”, “expects”, “intends”, “plans”, “appear”, “should” and similar words) involve risks and uncertainties that could cause actual results to differ materially from those we project. Included among such statements are those relating to opening new clinics, availability of personnel and the reimbursement environment. The forward-looking statements are based on our current views and assumptions and actual results could differ materially from those anticipated in such forward-looking statements as a result of certain risks, uncertainties, and factors, which include, but are not limited to:

- changes as the result of government enacted national healthcare reform;
- changes in Medicare guidelines and reimbursement or failure of our clinics to maintain their Medicare certification status;
- business and regulatory conditions including federal and state regulations;
- changes in reimbursement rates or payment methods from third party payors including government agencies and deductibles and co-pays owed by patients;
- revenue and earnings expectations;
- general economic conditions;
- availability and cost of qualified physical therapists;
- personnel productivity;
- competitive, economic or reimbursement conditions in our markets which may require us to reorganize or close certain clinics and thereby incur losses and/or closure costs including the possible write-down or write-off of goodwill and other intangible assets;
- maintaining adequate internal controls;
- availability, terms, and use of capital;
- acquisitions and the successful integration of the operations of the acquired businesses; and
- weather and other seasonal factors.

Many factors are beyond our control. Given these uncertainties, you should not place undue reliance on our forward-looking statements. Please see the other sections of this report and our other periodic reports filed with the Securities and Exchange Commission (the “SEC”) for more information on these factors. Our forward-looking statements represent our estimates and assumptions only as of the date of this report. Except as required by law, we are under no obligation to update any forward-looking statement, regardless of the reason the statement is no longer accurate.

PART I

ITEM 1. BUSINESS.

GENERAL

Our company, U.S. Physical Therapy, Inc. (the “Company”), through its subsidiaries, operates outpatient physical therapy clinics that provide pre-and post-operative care and treatment for orthopedic-related disorders, sports-related injuries, preventative care, rehabilitation of injured workers and neurological-related injuries. We primarily operate through subsidiary clinic partnerships in which we generally own a 1% general partnership interest and a 64% limited partnership interest and the managing therapist(s) of the clinics owns the remaining limited partnership interest in the majority of the clinics (hereinafter referred to as “Clinic Partnerships”). To a lesser extent, we operate some clinics through wholly-owned subsidiaries under profit sharing arrangements with therapists (hereinafter referred to as “Wholly-Owned Facilities”). Unless the context otherwise requires, references in this Annual Report on Form 10-K to “we”, “our” or “us” includes the Company and all of its subsidiaries.

Our strategy is to develop outpatient physical therapy clinics and acquire single and multi-clinic outpatient physical therapy practices on a national basis. At December 31, 2013, we operated 472 clinics in 43 states. The average age of the 472 clinics in operation at December 31, 2013 was 8.5 years. There were 367 clinics operated under Clinic Partnerships and 105 were operated as Wholly-Owned Facilities. Of the 472 clinics, we developed 298 and acquired 174. Our highest concentration of clinics are in the following states—Tennessee, Texas, Michigan, Maryland, Georgia, Washington, Pennsylvania, Wisconsin, New Jersey, Indiana, Oklahoma, Virginia, Missouri and Arizona. In addition to our 472 clinics, at December 31, 2013, we also managed 18 physical therapy practices for third parties, primarily physicians.

During the last three years, we completed the following multi-clinic acquisitions:

| <u>Acquisition</u> | <u>Date</u> | <u>% Interest Acquired</u> | <u>Number of Clinics</u> |
|-------------------------------|-------------|----------------------------|--------------------------|
| | <u>2013</u> | | |
| February 2013 Acquisition | February 28 | 72% | 9 |
| April 2013 Acquisition | April 30 | 50% | 5 |
| May 2013 Acquisition | May 24 | 80% | 5 |
| December 9, 2013 Acquisition | December 9 | 60% | 12 |
| December 13, 2013 Acquisition | December 13 | 90% | 11 |
| | <u>2012</u> | | |
| May 2012 Acquisition | May 22 | 70% | 7 |
| | <u>2011</u> | | |
| July 2011 Acquisition | July 25 | 51% | 20 |

In addition to the five multi-clinic acquisitions detailed above, in 2013, we acquired three individual clinics in separate transactions. In addition to the May 2012 Acquisition, in 2012, we acquired seven individual clinics in separate transactions. Two of the acquired clinic practices operate in two separate partnerships and the remaining five operate as satellites of existing partnerships.

We continue to seek to attract physical therapists who have established relationships with physicians and other referral sources by offering therapists a competitive salary and a share of the profits or an ownership interest in the clinic operated by that therapist. In addition, we have developed satellite clinic facilities of existing clinics, with the result that a substantial number of clinic groups operate more than one clinic location. In 2014, we intend to acquire clinic practices and continue to focus on developing new clinics and on opening satellite clinics where appropriate along with increasing our patient volume through marketing and new programs.

Therapists at our clinics initially perform a comprehensive evaluation of each patient, which is then followed by a treatment plan specific to the injury as prescribed by the patient's physician. The treatment plan may include a number of procedures, including therapeutic exercise, manual therapy techniques, ultrasound, electrical stimulation, hot packs, iontophoresis, education on management of daily life skills and home exercise programs. A clinic's business primarily comes from referrals by local physicians. The principal sources of payment for the clinics' services are managed care programs, commercial health insurance, Medicare/Medicaid and workers' compensation insurance.

Our Company was re-incorporated in April 1992 under the laws of the State of Nevada and has operating subsidiaries organized in various states in the form of limited partnerships and wholly-owned corporations. This description of our business should be read in conjunction with our financial statements and the related notes contained elsewhere in this Annual Report on Form 10-K. Our principal executive offices are located at 1300 West Sam Houston Parkway South, Suite 300, Houston, Texas 77042. Our telephone number is (713) 297-7000. Our website is www.usph.com.

OUR CLINICS

Most of our clinics are Clinic Partnerships in which we own the general partnership interest and a majority of the limited partnership interests. The managing healthcare practitioner of the clinics usually owns a portion of the limited partnership interests. Generally, the therapist partners have no interest in the net losses of Clinic Partnerships, except to the extent of their capital accounts. Since we also develop satellite clinic facilities of existing clinics, Clinic Partnerships may consist of more than one clinic location. As of December 31, 2013, through wholly-owned subsidiaries, we owned a 1% general partnership interest in all the Clinic Partnerships, except for one partnership in which we own a 6% general partnership interest. Our limited partnership interests range from 49% to 99% in the Clinic Partnerships, but with respect to the majority of our Clinic Partnerships, we own a limited partnership interest of 64%. For the vast majority of the Clinic Partnerships, the managing healthcare practitioner is a physical therapist who owns the remaining limited partnership interest in the Clinic Partnership.

In the majority of the Clinic Partnership agreements, the therapist partner began with a 20% interest in their Clinic Partnership earnings which increased by 3% at the end of each year thereafter up to a maximum interest of 35%.

Typically each therapist partner or director enters into an employment agreement for a term of up to three years with their Clinic Partnership. Each agreement typically provides for a covenant not to compete during the period of his or her employment and for up to two years thereafter. Under each employment agreement, the therapist partner receives a base salary and may receive a bonus based on the net revenues or profits generated by their Clinic Partnership. In the case of Clinic Partnerships, the therapist partner receives earnings distributions based upon their ownership interest. Upon termination of employment, the Company typically has the right, but is not obligated, to purchase the therapist's partnership interest in Clinic Partnerships. In connection with several of our acquired clinics, in the event that a limited minority partner's employment ceases at any time after three years from the acquisition date, we have agreed to repurchase that individual's non-controlling interest at a predetermined multiple of earnings before interest and taxes.

Each Clinic Partnership maintains an independent local identity, while at the same time enjoying the benefits of national purchasing, negotiated third-party payor contracts, centralized support services and management practices. Under a management agreement, one of our subsidiaries provides a variety of support services to each clinic, including supervision of site selection, construction, clinic design and equipment selection, establishment of accounting systems and billing procedures and training of office support personnel, processing of accounts payable, operational direction, auditing of regulatory compliance, payroll, benefits administration, accounting services, quality assurance and marketing support.

Our typical clinic occupies approximately 1,500 to 3,000 square feet of leased space in an office building or shopping center. We attempt to lease ground level space for patient ease of access to our clinics. We also attempt to make the decor in our clinics less institutional and more aesthetically pleasing than traditional hospital clinics. Typical minimum staff at a clinic consists of a licensed physical therapist and an office manager, as well as, if appropriate, a medical advisor. As patient visits grow, staffing may also include additional physical therapists, occupational therapists, therapy assistants, aides, exercise physiologists, athletic trainers and office personnel. Therapy services are performed under the supervision of a licensed therapist.

We provide services at our clinics on an outpatient basis. Patients are usually treated for approximately one hour per day, two to three times a week, typically for two to six weeks. We generally charge for treatment on a per procedure basis. Medicare patients are charged based on prescribed time increments and Medicare billing standards. In addition, our clinics will develop, when appropriate, individual maintenance and self-management exercise programs to be continued after treatment. We continually assess the potential for developing new services and expanding the methods of providing our existing services in the most efficient manner while providing high quality patient care.

FACTORS INFLUENCING DEMAND FOR THERAPY SERVICES

We believe that the following factors, among others, influence the growth of outpatient physical therapy services:

Economic Benefits of Therapy Services. Purchasers and providers of healthcare services, such as insurance companies, health maintenance organizations, businesses and industries, continuously seek cost savings for traditional healthcare services. We believe that our therapy services provide a cost-effective way to prevent short-term disabilities from becoming chronic conditions and to speed recovery from surgery and musculoskeletal injuries.

Earlier Hospital Discharge. Changes in health insurance reimbursement, both public and private, have encouraged the earlier discharge of patients to reduce costs. We believe that early hospital discharge practices foster greater demand for outpatient physical therapy services.

Aging Population. In general, the elderly population has a greater incidence of disability compared to the population as a whole. As this segment of the population grows, we believe that demand for rehabilitation services will expand.

MARKETING

We focus our marketing efforts primarily on physicians, including orthopedic surgeons, neurosurgeons, physiatrists, internal medicine physicians, podiatrists, occupational medicine physicians and general practitioners. In marketing to the physician community, we emphasize our commitment to quality patient care and regular communication with physicians regarding patient progress. We employ personnel to assist clinic directors in developing and implementing marketing plans for the physician community and to assist in establishing relationships with health maintenance organizations, preferred provider organizations, industry and case managers and insurance companies.

SOURCES OF REVENUE

Payor sources for clinic services are primarily managed care programs, commercial health insurance, Medicare/Medicaid and workers' compensation insurance. Commercial health insurance, Medicare and managed care programs generally provide coverage to patients utilizing our clinics after payment by the patients of normal deductibles and co-insurance payments. Workers' compensation laws generally require employers to provide, directly or indirectly through insurance, costs of medical rehabilitation for their employees from work-related injuries and disabilities and, in some jurisdictions, mandatory vocational rehabilitation, usually without any

deductibles, co-payments or cost sharing. Treatments for patients who are parties to personal injury cases are generally paid from the proceeds of settlements with insurance companies or from favorable judgments. If an unfavorable judgment is received, collection efforts are generally not pursued against the patient and the patient's account is written-off against established reserves. Bad debt reserves relating to all receivable types are regularly reviewed and adjusted as appropriate.

The following table shows our payor mix for the years ended:

| Payor | December 31, 2013 | | December 31, 2012 | | December 31, 2011 | |
|---|-------------------------------------|---------------|---------------------|---------------|---------------------|---------------|
| | Net Patient Revenue | Percentage | Net Patient Revenue | Percentage | Net Patient Revenue | Percentage |
| | (Net Patient Revenues in Thousands) | | | | | |
| Managed Care Program | \$ 58,680 | 22.8% | \$ 73,244 | 30.0% | \$ 65,799 | 29.1% |
| Commercial Health Insurance | 79,148 | 30.6% | 57,066 | 23.4% | 52,517 | 23.3% |
| Medicare/Medicaid | 60,697 | 23.5% | 58,730 | 24.1% | 56,095 | 24.8% |
| Workers' Compensation Insurance | 45,221 | 17.5% | 42,086 | 17.2% | 39,203 | 17.4% |
| Other | 14,537 | 5.6% | 12,974 | 5.3% | 12,190 | 5.4% |
| Total | <u>\$258,283</u> | <u>100.0%</u> | <u>\$244,100</u> | <u>100.0%</u> | <u>\$225,804</u> | <u>100.0%</u> |

Our business depends to a significant extent on our relationships with commercial health insurers, health maintenance organizations, preferred provider organizations and workers' compensation insurers. In some geographical areas, our clinics must be approved as providers by key health maintenance organizations and preferred provider plans to obtain payments. Failure to obtain or maintain these approvals would adversely affect financial results.

During the year ended December 31, 2013, approximately 25.0% of our visits and 21.7% of our net patient revenues were from patients with Medicare program coverage. To receive Medicare reimbursement, a facility (Medicare Certified Rehabilitation Agency) or the individual therapist (Physical/Occupational Therapist in Private Practice) must meet applicable participation conditions set by the Department of Health and Human Services ("HHS") relating to the type of facility, equipment, record keeping, personnel and standards of medical care, and also must comply with all state and local laws. HHS, through Centers for Medicare & Medicaid Services ("CMS") and designated agencies, periodically inspects or surveys clinics/providers for approval and/or compliance. We anticipate that our newly developed clinics will generally become certified as Medicare providers or will be enrolled as a group of physical/occupation therapists in a private practice. However, we cannot assure you that newly developed clinics will be successful in becoming eligible as Medicare providers.

The Medicare program reimburses outpatient rehabilitation providers based on the Medicare Physician Fee Schedule ("MPFS"). The MPFS rates are automatically updated annually based on a formula, called the sustainable growth rate ("SGR") formula. The use of the SGR formula would have resulted in calculated automatic reductions in rates in every year since 2002; however, for each year through March 31, 2014, Centers for Medicare & Medicaid Services ("CMS") or Congress has taken action to prevent the implementation of SGR formula reductions. The Bipartisan Budget Act of 2013 froze the Medicare physician fee schedule rates at 2013 levels through March 31, 2014, averting a scheduled 20.1% cut in the MPFS as a result of the SGR formula that would have taken effect on January 1, 2014. Unless Congress again takes legislative action to prevent the SGR formula reductions from going into effect automatic reductions in the MPFS will commence on April 1, 2014.

The Budget Control Act of 2011 increased the federal debt ceiling in connection with deficit reductions over the next ten years, and requires automatic reductions in federal spending by approximately \$1.2 trillion. Payments to Medicare providers are subject to these automatic spending reductions, subject to a 2% cap. On April 1, 2013, a 2% reduction to Medicare payments was implemented.

As a result of the Balanced Budget Act of 1997, the formula for determining the total amount paid by Medicare in any one year for outpatient physical therapy, occupational therapy, and/or speech-language pathology services provided to any Medicare beneficiary (*i.e.*, the “Therapy Cap” or “Limit”) was established. Based on the statutory definitions which constrained how the Therapy Cap would be applied, there is one Limit for Physical Therapy and Speech Language Pathology Services combined, and one Limit for Occupational Therapy. During 2013, the annual Limit on outpatient therapy services was \$1,900 for Physical Therapy and Speech Language Pathology Services combined and \$1,900 for Occupational Therapy Services. Effective January 1, 2014, the annual Limit on outpatient therapy services is \$1,920 for Physical and Speech Language Pathology Services combined and \$1,920 for Occupational Therapy Services. Historically, these Therapy Caps applied to outpatient therapy services provided in all settings, except for services provided in departments of hospitals. However, the American Taxpayer Relief Act of 2012 and the Bipartisan Budget Act of 2013 extended the annual limits on therapy expenses to services furnished in hospital outpatient department settings through March 31, 2014. Unless Congress enacts legislation to extend the application of these limits to therapy provided in hospital outpatient settings, the Therapy Caps will no longer apply to such services starting as of April 1, 2014.

In the Deficit Reduction Act of 2005, Congress implemented an exceptions process to the annual Limit for therapy expenses for therapy services above the annual Limit. The Bipartisan Budget Act of 2013 extended the exceptions process for outpatient Therapy Caps through March 31, 2014. Therapy services above the annual Limit that are medically necessary satisfy an exception to the annual Limit and such claims are payable by the Medicare program. Unless Congress extends the exceptions process, the Therapy Caps will apply to all claims regardless of medical necessity beginning April 1, 2014. For any claim above the annual Limit, the claim must contain a modifier indicating that the services are medically necessary and justified by appropriate documentation in the medical record.

Furthermore, under the Middle Class Tax Relief and Job Creation Act of 2012 (“MCTRA”), since October 1, 2012, patients who met or exceeded \$3,700 in therapy expenditures during a calendar year have been subject to a manual medical review to determine whether applicable payment criteria are satisfied. The \$3,700 threshold is applied to Physical Therapy and Speech Language Pathology Services; a separate \$3,700 threshold is applied to the Occupational Therapy. The Bipartisan Budget Relief Act of 2013 extended through March 31, 2014 the requirement that Medicare perform manual medical review of therapy services beyond the \$3,700 threshold. In addition, as of January 1, 2013, CMS implemented a claims based data collection strategy that is designed to assist in reforming the Medicare payment system for outpatient therapy. Since January 1, 2013, all therapy claims must include additional codes and modifiers providing information about the beneficiary’s functional status at the outset of the therapy episode of care, specified points during treatment, and at the time of discharge. Effective July 1, 2013, claims submitted without the appropriate codes and modifiers are returned unpaid.

CMS adopted a multiple procedure payment reduction (“MPPR”) for therapy services in the final update to the MPFS for calendar year 2011. During 2011, the MPPR applied to all outpatient therapy services paid under Medicare Part B — occupational therapy, physical therapy and speech-language pathology. Under the policy, the Medicare program pays 100% of the practice expense component of the Relative Value Unit (“RVU”) for the therapy procedure with the highest practice expense RVU, then reduces the payment for the practice expense component for the second and subsequent therapy procedures or units of service furnished during the same day for the same patient, regardless of whether those therapy services are furnished in separate sessions. In 2011 and 2012, the practice expense component for the second and subsequent therapy service furnished during the same day for the same patient was reduced by 20% in office and other non-institutional settings and by 25% in institutional settings. The American Taxpayer Relief Act of 2012 increased the payment reduction of the practice expense component to 50%, on subsequent therapy procedures in either setting, effective April 1, 2013.

In addition, the Middle Class Tax Relief and Job Creation Act of 2012 (“MCTRA”) directed CMS to implement a claims-based data collection program to gather additional data on patient function during the course of therapy in order to better understand patient conditions and outcomes. All practice settings that provide outpatient therapy services are required to include this data on the claim form. Since July 1, 2013, therapists have

been required to report new codes and modifiers on the claim form that reflect a patient's functional limitations and goals at initial evaluation, periodically throughout care, and at discharge. Since July 1, 2013, CMS has rejected claims if the required data is not included in the claim.

The Physician Quality Reporting System, or "PQRS," is a CMS reporting program that uses a combination of incentive payments and payment reductions to promote reporting of quality information by "eligible professionals." Although physical therapists, occupational therapists and qualified speech-language therapists are generally able to participate in the PQRS program, therapy professionals for whose services we bill through our rehab agencies cannot participate because the Medicare claims processing systems currently cannot accommodate institutional providers such as rehab agencies. Eligible professionals, such as those of our therapy professionals for whose services we bill using their individual Medicare provider numbers, who do not satisfactorily report data on quality measures will be subject to a 2% reduction in their Medicare payment in 2016.

Statutes, regulations, and payment rules governing the delivery of therapy services to Medicare beneficiaries are complex and subject to interpretation. We believe that we are in substantial compliance in all material respects with all applicable laws and regulations and are not aware of any pending or threatened investigations involving allegations of potential wrongdoing that would have a material effect on our financial statements as of December 31, 2013. Compliance with such laws and regulations can be subject to future government review and interpretation, as well as significant regulatory action including fines, penalties, and exclusion from the Medicare program.

Medicare regulations require that a physician or non-physician practitioner certify the need for skilled therapy services for each patient and that these services be provided under an established plan of treatment, which is periodically revised.

Medicaid has not been a material payor for us, constituting less than 2% of historical revenue.

REGULATION AND HEALTHCARE REFORM

Numerous federal, state and local regulations regulate healthcare services and those who provide them. Some states into which we may expand have laws requiring facilities employing health professionals and providing health-related services to be licensed and, in some cases, to obtain a certificate of need (that is, demonstrating to a state regulatory authority the need for, and financial feasibility of, new facilities or the commencement of new healthcare services). Only one of the states in which we currently operate requires a certificate of need for the operation of our physical therapy business functions. Our therapists and/or clinics, however, are required to be licensed, as determined by the state in which they provide services. Failure to obtain or maintain any required certificates, approvals or licenses could have a material adverse effect on our business, financial condition and results of operations.

Regulations Controlling Fraud and Abuse. Various federal and state laws regulate financial relationships involving providers of healthcare services. These laws include Section 1128B(b) of the Social Security Act (42 U.S.C. § 1320a-7b[b]) (the "Fraud and Abuse Law"), under which civil and criminal penalties can be imposed upon persons who, among other things, offer, solicit, pay or receive remuneration in return for (i) the referral of patients for the rendering of any item or service for which payment may be made, in whole or in part, by a Federal health care program (including Medicare and Medicaid); or (ii) purchasing, leasing, ordering, or arranging for or recommending purchasing, leasing, ordering any good, facility, service, or item for which payment may be made, in whole or in part, by a Federal health care program (including Medicare and Medicaid). We believe that our business procedures and business arrangements are in compliance with these provisions. However, the provisions are broadly written and the full extent of their specific application to specific facts and arrangements to which the Company is a party is uncertain and difficult to predict. In addition, several states have enacted state laws similar to the Fraud and Abuse Law, which may be more restrictive than the federal Fraud and Abuse Law.

In 1991, the Office of the Inspector General (“OIG”) of the HHS issued the first of its regulations describing compensation financial arrangements that fall within a “Safe Harbor” and, therefore, are not viewed as illegal remuneration under the Fraud and Abuse Law. Failure to fall within a Safe Harbor does not mean that the Fraud and Abuse Law has been violated; however, the OIG has indicated that failure to fall within a Safe Harbor may subject an arrangement to increased scrutiny under a “facts and circumstances” test.

Our business of managing physician-owned physical therapy facilities is regulated by the Fraud and Abuse Law. However, the manner in which we contract with such facilities often falls outside the complete scope of available Safe Harbors. We believe our arrangements comply with the Fraud and Abuse Law, even though federal courts provide limited guidance as to the application of the Fraud and Abuse Law to these arrangements. If our management contracts are held to violate the Fraud and Abuse Law, it could have an adverse effect on our business, financial condition and results of operations.

In February 2000, the OIG issued a special fraud alert regarding the rental of space in physician offices by persons or entities to which the physicians refer patients. The OIG’s stated concern in these arrangements is that rental payments may be disguised kickbacks to the physician-landlords to induce referrals. We rent clinic space for a few of our clinics from referring physicians and have taken the steps that we believe are necessary to ensure that all leases comply to the extent possible and applicable with the space rental Safe Harbor to the Fraud and Abuse Law.

In April 2003, the OIG issued a special advisory bulletin addressing certain complex contractual arrangements for the provision of items and services that were previously identified as suspect in a 1989 special fraud alert. This special advisory bulletin identified several characteristics commonly exhibited by suspect arrangements, the existence of one or more of which could indicate a prohibited arrangement to the OIG. Generally, the indicia of a suspect contractual joint venture as identified by the special advisory bulletin and the associated OIG advisory opinion include the following:

- *New Line of Business.* A provider in one line of business (“Owner”) expands into a new line of business that can be provided to the Owner’s existing patients, with another party who currently provides the same or similar item or service as the new business (“Manager/Supplier”).
- *Captive Referral Base.* The arrangement predominantly or exclusively serves the Owner’s existing patient base (or patients under the control or influence of the Owner).
- *Little or No Bona Fide Business Risk.* The Owner’s primary contribution to the venture is referrals; it makes little or no financial or other investment in the business, delegating the entire operation to the Manager/Supplier, while retaining profits generated from its captive referral base.
- *Status of the Manager/Supplier.* The Manager/Supplier is a would-be competitor of the Owner’s new line of business and would normally compete for the captive referrals. It has the capacity to provide virtually identical services in its own right and bill insurers and patients for them in its own name.
- *Scope of Services Provided by the Manager/Supplier.* The Manager/Supplier provides all, or many, of the new business’ key services.
- *Remuneration.* The practical effect of the arrangement, viewed in its entirety, is to provide the Owner the opportunity to bill insurers and patients for business otherwise provided by the Manager/Supplier. The remuneration from the venture to the Owner (i.e., the profits of the venture) takes into account the value and volume of business the Owner generates.
- *Exclusivity.* The arrangement bars the Owner from providing items or services to any patients other than those coming from Owner and/or bars the Manager/Supplier from providing services in its own right to the Owner’s patients.

Due to the nature of our business operations, many of our management service arrangements exhibit one or more of these characteristics. However, the Company believes it has taken steps regarding the structure of such

arrangements as necessary to sufficiently distinguish them from these suspect ventures, and to comply with the requirements of the Fraud and Abuse Law. However, if the OIG believes the Company has entered into a prohibited contractual joint venture, it could have an adverse effect on our business, financial condition and results of operations.

Stark Law. Provisions of the Omnibus Budget Reconciliation Act of 1993 (42 U.S.C. § 1395nn) (the “Stark Law”) prohibit referrals by a physician of “designated health services” which are payable, in whole or in part, by Medicare or Medicaid, to an entity in which the physician or the physician’s immediate family member has an investment interest or other financial relationship, subject to several exceptions. Unlike the Fraud and Abuse Law, the Stark Law is a strict liability statute. Proof of intent to violate the Stark Law is not required. Physical therapy services are among the “designated health services”. Further, the Stark Law has application to the Company’s management contracts with individual physicians and physician groups, as well as, any other financial relationship between us and referring physicians, including any financial transaction resulting from a clinic acquisition. The Stark Law also prohibits billing for services rendered pursuant to a prohibited referral. Several states have enacted laws similar to the Stark Law. These state laws may cover all (not just Medicare and Medicaid) patients. Many federal healthcare reform proposals in the past few years have attempted to expand the Stark Law to cover all patients as well. As with the Fraud and Abuse Law, we consider the Stark Law in planning our clinics, marketing and other activities, and believe that our operations are in compliance with the Stark Law. If we violate the Stark Law, our financial results and operations could be adversely affected. Penalties for violations include denial of payment for the services, significant civil monetary penalties, and exclusion from the Medicare and Medicaid programs.

HIPAA. In an effort to further combat healthcare fraud and protect patient confidentiality, Congress included several anti-fraud measures in the Health Insurance Portability and Accountability Act of 1996 (“HIPAA”). HIPAA created a source of funding for fraud control to coordinate federal, state and local healthcare law enforcement programs, conduct investigations, provide guidance to the healthcare industry concerning fraudulent healthcare practices, and establish a national data bank to receive and report final adverse actions. HIPAA also criminalized certain forms of health fraud against all public and private payors. Additionally, HIPAA mandates the adoption of standards regarding the exchange of healthcare information in an effort to ensure the privacy and electronic security of patient information and standards relating to the privacy of health information. Sanctions for failing to comply with HIPAA include criminal penalties and civil sanctions. In February of 2009, the American Recovery and Reinvestment Act of 2009 (“ARRA”) was signed into law. Title XIII of ARRA, the Health Information Technology for Economic and Clinical Health Act (“HITECH”), provided for substantial Medicare and Medicaid incentives for providers to adopt electronic health records (“EHRs”) and grants for the development of health information exchange (“HIE”). Recognizing that HIE and EHR systems will not be implemented unless the public can be assured that the privacy and security of patient information in such systems is protected, HITECH also significantly expanded the scope of the privacy and security requirements under HIPAA. Most notable are the new mandatory breach notification requirements and a heightened enforcement scheme that includes increased penalties, and which now apply to business associates as well as to covered entities. In addition to HIPAA, a number of states have adopted laws and/or regulations applicable in the use and disclosure of individually identifiable health information that can be more stringent than comparable provisions under HIPAA.

We believe that our operations substantially comply with applicable standards for privacy and security of protected healthcare information. We cannot predict what negative effect, if any, HIPAA/HITECH or any applicable state law or regulation will have on our business.

Other Regulatory Factors. Political, economic and regulatory influences are fundamentally changing the healthcare industry in the United States. Congress, state legislatures and the private sector continue to review and assess alternative healthcare delivery and payment systems. Potential alternative approaches could include mandated basic healthcare benefits, controls on healthcare spending through limitations on the growth of private health insurance premiums and Medicare and Medicaid spending, the creation of large insurance purchasing groups, and price controls. Legislative debate is expected to continue in the future and market forces are expected

to demand only modest increases or reduced costs. For instance, managed care entities are demanding lower reimbursement rates from healthcare providers and, in some cases, are requiring or encouraging providers to accept capitated payments that may not allow providers to cover their full costs or realize traditional levels of profitability. We cannot reasonably predict what impact the adoption of federal or state healthcare reform measures or future private sector reform may have on our business.

COMPETITION

The healthcare industry, including the physical therapy business, is highly competitive. The physical therapy business is highly fragmented with no company having as much as six percent of the market share nationally. We believe that our Company is the third largest national outpatient rehabilitation provider.

Competitive factors affecting our business include quality of care, cost, treatment outcomes, convenience of location, and relationships with, and ability to meet the needs of, referral and payor sources. Our clinics compete, directly or indirectly, with many types of healthcare providers including the physical therapy departments of hospitals, private therapy clinics, physician-owned therapy clinics, and chiropractors. We may face more intense competition if consolidation of the therapy industry continues.

We believe that our strategy of providing key therapists in a community with an opportunity to participate in ownership or clinic profitability provides us with a competitive advantage by helping to ensure the commitment of local management to the success of the clinic.

We also believe that our competitive position is enhanced by our strategy of locating our clinics, when possible, on the ground floor of buildings and shopping centers with nearby parking, thereby making the clinics more easily accessible to patients. We offer convenient hours. We also attempt to make the decor in our clinics less institutional and more aesthetically pleasing than traditional hospital clinics.

ENFORCEMENT ENVIRONMENT

In recent years, federal and state governments have launched several initiatives aimed at uncovering behavior that violates the federal civil and criminal laws regarding false claims and fraudulent billing and coding practices. Such laws require providers to adhere to complex reimbursement requirements regarding proper billing and coding in order to be compensated for their services by government payors. Our compliance program requires adherence to applicable law and promotes reimbursement education and training; however, a determination that our clinics' billing and coding practices are false or fraudulent could have a material adverse effect on us.

We and our clinics are subject to federal and state laws prohibiting entities and individuals from knowingly and willfully making claims to Medicare, Medicaid and other governmental programs and third party payors that contain false or fraudulent information. The federal False Claims Act encourages private individuals to file suits on behalf of the government against healthcare providers such as us. As such suits are generally filed under seal with a court to allow the government adequate time to investigate and determine whether it will intervene in the action, the implicated healthcare providers often are unaware of the suit until the government has made its determination and the seal is lifted. Violations or alleged violations of such laws, and any related lawsuits, could result in (i) exclusion from participation in Medicare, Medicaid and other federal healthcare programs, or (ii) significant financial or criminal sanctions, resulting in the possibility of substantial financial penalties for small billing errors that are replicated in a large number of claims, as each individual claim could be deemed a separate violation. In addition, many states also have enacted similar statutes, which may include criminal penalties, substantial fines, and treble damages.

COMPLIANCE PROGRAM

Our Compliance Program. The ongoing success of our Company depends upon our reputation for quality service and ethical business practices. Our Company operates in a highly regulated environment with many federal, state and local laws and regulations. We take a proactive interest in understanding and complying with the laws and regulations that apply to our business.

Our Board of Directors (the “Board”) has adopted a Code of Business Conduct and Ethics to clarify the ethical standards under which the Board and management carry out their duties. In addition, the Board has created a Corporate Compliance Sub-Committee of the Board’s Audit Committee (“Compliance Committee”) whose purpose is to assist the Board and its Audit Committee (“Audit Committee”) in discharging their oversight responsibilities with respect to compliance with federal and state laws and regulations relating to healthcare.

We have issued an Ethics and Compliance Manual and created a compliance DVD, hand-outs and an on-line testing program. These tools were prepared to ensure that each clinic as well as every employee of our Company and subsidiaries has a clear understanding of our mutual commitment to high standards of professionalism, honesty, fairness and compliance with the law in conducting business. These standards are administered by our Compliance Officer (“CO”), who has the responsibility for the day-to-day oversight, administration and development of our compliance program. The CO, internal and external counsel, management and the Compliance Committee review our policies and procedures for our compliance program from time to time in an effort to improve operations and to ensure compliance with requirements of standards, laws and regulations and to reflect the on-going compliance focus areas which have been identified by the Compliance Committee. We also have established systems for reporting potential violations, educating our employees, monitoring and auditing compliance and handling enforcement and discipline.

Committees. Our Compliance Committee, appointed by the Board, consists of four independent directors. The Compliance Committee has general oversight of our Company’s compliance with the legal and regulatory requirements regarding healthcare operations. The Compliance Committee relies on the expertise and knowledge of management, the CO and other compliance and legal personnel. The CO regularly communicates with the Chairman of the Compliance Committee. The Compliance Committee meets at least four times a year or more frequently as necessary to carry out its responsibilities and reports regularly to the Board regarding its actions and recommendations.

In addition, management has appointed a team to address our Company’s compliance with HIPAA. The HIPAA team consists of a security officer and employees from our legal, information systems, finance, operations, compliance, business services and human resources departments. The team prepares assessments and makes recommendations regarding operational changes and/or new systems, if needed, to comply with HIPAA.

Each clinic certified as a Medicare Rehabilitation Agency has a formally appointed governing body composed of a member of management of the Company and the director/administrator of the clinic. The governing body retains legal responsibility for the overall conduct of the clinic. The members confer regularly and discuss, among other issues, clinic compliance with applicable laws and regulations. In addition, there are Professional Advisory Committees which serve as Infection Control Committees. These committees meet in the facilities and function as advisors.

The Company has in place a Risk Management Committee consisting of the CO, the Corporate in-house Legal Counsel and the Corporate Vice President of Administration. This committee reviews and monitors all employee and patient incident reports and provides clinic personnel with actions to be taken in response to the reports.

Reporting Violations. In order to facilitate our employees’ ability to report in confidence, anonymously and without retaliation any perceived improper work-related activities, accounting irregularities and other violations of our compliance program, we have set up an independent national compliance hotline. The compliance hotline is available to receive confidential reports of wrongdoing Monday through Friday (excluding holidays), 24 hours a day. The compliance hotline is staffed by experienced third party professionals trained to utilize utmost care and discretion in handling sensitive issues and confidential information. The information received is documented and forwarded timely to the CO, who, together with the Compliance Committee, has the power and resources to investigate and resolve matters of improper conduct.

Educating Our Employees. We utilize numerous methods to train our employees in compliance related issues. The directors/administrators of each clinic are responsible to conduct the initial training sessions on

compliance with existing employees. Training is based on our Ethics and Compliance Manual, inclusive of HIPAA information, and our compliance DVD. The directors/administrators also provide periodic “refresher” training for existing employees and one-on-one comprehensive training with new hires. The corporate compliance group responds to questions from clinic personnel and will conduct frequent teleconference meetings on topics as deemed necessary.

When a clinic opens, the CO provides a package of compliance materials containing manuals and detailed instructions for meeting Medicare Conditions of Participation Standards and other compliance requirements. During follow up training with the director/administrator of the clinic, the CO explains various details regarding requirements and compliance standards. The CO and the compliance staff will remain in contact with the director/administrator while the clinic is implementing compliance standards and will provide any assistance required. All new office managers receive training (including Medicare, regulatory and corporate compliance, insurance billing, charge entry and transaction posting and coding, daily, weekly and monthly accounting reports) from the training staff at the corporate office. The corporate compliance group will assist in continued compliance, including guidance to the clinic staff with regard to Medicare certifications, state survey requirements and responses to any inquiries from regulatory agencies.

Monitoring and Auditing Clinic Operational Compliance. Our Company has in place audit programs and other procedures to monitor and audit clinic operational compliance with applicable policies and procedures. We employ internal auditors who, as part of their job responsibilities, conduct periodic audits of each clinic. Most clinics are audited at least once every 18 months and additional focused audits are performed as deemed necessary. During these audits, particular attention is given to compliance with Medicare and internal policies, Federal and state laws and regulations, third party payor requirements, and patient chart documentation, billing, reporting, record keeping, collections and contract procedures. The audits are conducted on site and include interviews with the employees involved in management, operations, billing and accounts receivable. Formal audit reports are prepared and reviewed with corporate management and the Compliance Committee. Each clinic director/administrator receives a letter instructing them of any corrective measures required. Each clinic director/administrator then works with the compliance team and operations to ensure such corrective measures are achieved.

Handling Enforcement and Discipline. It is our policy that any employee who fails to comply with compliance program requirements or who negligently or deliberately fails to comply with known laws or regulations specifically addressed in our compliance program should be subject to disciplinary action up to and including discharge from employment. The Compliance Committee, compliance staff, human resources staff and management investigate violations of our compliance program and impose disciplinary action as considered appropriate.

EMPLOYEES

At December 31, 2013, we employed 2,805 people, of which 1,886 were full-time employees. At that date, no Company employees were governed by collective bargaining agreements or were members of a union. We consider our relations with our employees to be good.

In the states in which our current clinics are located, persons performing designated physical therapy services are required to be licensed by the state. Based on standard employee screening systems in place, all persons currently employed by us who are required to be licensed are licensed. We are not aware of any federal licensing requirements applicable to our employees.

AVAILABLE INFORMATION

Our annual reports on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K and amendments to those reports filed or furnished pursuant to Section 13(a) or 15(d) of the Exchange Act are made available free of charge on our internet website at www.usph.com as soon as reasonably practicable after we electronically file such material with, or furnish it to, the SEC.

ITEM 1A.—RISK FACTORS.

Our business, operations and financial condition are subject to various risks. Some of these risks are described below, and readers of this Annual Report on Form 10-K should take such risks into account in evaluating our Company or making any decision to invest in us. This section does not describe all risks applicable to our Company, our industry or our business, and it is intended only as a summary of material factors affecting our business.

Risks related to our business and operations

Healthcare reform legislation may affect our business.

In recent years, many legislative proposals have been introduced or proposed in Congress and in some state legislatures that would affect major changes in the healthcare system, either nationally or at the state level. At the federal level, Congress has continued to propose or consider healthcare budgets that substantially reduce payments under the Medicare programs. See “Business- Sources of Revenue” in Item 1 for more information. The ultimate content, timing or effect of any healthcare reform legislation and the impact of potential legislation on us is uncertain and difficult, if not impossible, to predict. That impact may be material to our business, financial condition or results of operations.

Our operations are subject to extensive regulation.

The healthcare industry is subject to extensive federal, state and local laws and regulations relating to:

- facility and professional licensure/permits, including certificates of need;
- conduct of operations, including financial relationships among healthcare providers, Medicare fraud and abuse, and physician self-referral;
- addition of facilities and services; and
- billing and payment for services.

In recent years, there have been heightened coordinated civil and criminal enforcement efforts by both federal and state government agencies relating to the healthcare industry. We believe we are in substantial compliance with all laws, but differing interpretations or enforcement of these laws and regulations could subject our current practices to allegations of impropriety or illegality or could require us to make changes in our methods of operations, facilities, equipment, personnel, services and capital expenditure programs and increase our operating expenses. If we fail to comply with these extensive laws and government regulations, we could become ineligible to receive government program reimbursement, suffer civil or criminal penalties or be required to make significant changes to our operations. In addition, we could be forced to expend considerable resources responding to an investigation or other enforcement action under these laws or regulations. For a more complete description of certain of these laws and regulations, see “Business—Regulation and Healthcare Reform” in Item 1.

The healthcare industry is subject to extensive federal, state and local laws and regulations relating to (1) facility and professional licensure, including certificates of need, (2) conduct of operations, including financial relationships among healthcare providers, Medicare fraud and abuse and physician self-referral, (3) addition of facilities and services and enrollment of newly developed facilities in the Medicare program, (4) payment for services and (5) safeguarding protected health information.

Both federal and state regulatory agencies inspect, survey and audit our facilities to review our compliance with these laws and regulations. While our facilities intend to comply with the existing licensing, Medicare certification requirements and accreditation standards, there can be no assurance that these regulatory authorities will determine that all applicable requirements are fully met at any given time. A determination by any of these

regulatory authorities that a facility is not in compliance with these requirements could lead to the imposition of requirements that the facility takes corrective action, assessment of fines and penalties, or loss of licensure, Medicare certification or accreditation. These consequences could have an adverse effect on our company.

Decreases in Medicare reimbursement rates, implementation of annual caps, and payment reductions applied to the second and subsequent therapy services will adversely affect our financial results.

The Medicare program reimburses outpatient rehabilitation providers based on the MPFS. The MPFS rates are automatically updated annually based on a formula, called the SGR formula. The use of the SGR formula would have resulted in calculated automatic reductions in rates in every year since 2002; however, for each year through March 31, 2014, CMS or Congress has taken action to prevent the implementation of SGR formula reductions. The Bipartisan Budget Act of 2013 froze the Medicare physician fee schedule rates at 2013 levels through March 31, 2014, averting a scheduled 20.1% cut in the MPFS as a result of the SGR formula that would have taken effect on January 1, 2014. Unless Congress again takes legislative action to prevent the SGR formula reductions from going into effect automatic reductions in the MPFS will commence on April 1, 2014.

The Budget Control Act of 2011 increased the federal debt ceiling in connection with deficit reductions over the next ten years, and requires automatic reductions in federal spending by approximately \$1.2 trillion. Payments to Medicare providers are subject to these automatic spending reductions, subject to a 2% cap. On April 1, 2013, a 2% reduction to Medicare payments was implemented.

As a result of the Balanced Budget Act of 1997, the formula for determining the total amount paid by Medicare in any one year for outpatient physical therapy, occupational therapy, and/or speech-language pathology services provided to any Medicare beneficiary (*i.e.*, the “Therapy Cap” or “Limit”) was established. Based on the statutory definitions which constrained how the Therapy Cap would be applied, there is one Limit for Physical Therapy and Speech Language Pathology Services combined, and one Limit for Occupational Therapy. During 2013, the annual Limit on outpatient therapy services was \$1,900 for Physical Therapy and Speech Language Pathology Services combined and \$1,900 for Occupational Therapy Services. Effective January 1, 2014, the annual Limit on outpatient services is \$1,920 for Physical and Speech Language Pathology Services combined and \$1,920 for Occupational Therapy Services. Historically, these Therapy Caps applied to outpatient therapy services provided in all settings, except for services provided in departments of hospitals. However, the American Taxpayer Relief Act of 2012 and the Bipartisan Budget Act of 2013 extended the annual limits on therapy expenses to services furnished in hospital outpatient department settings through March 31, 2014. Unless Congress enacts legislation to extend the application of these limits to therapy provided in hospital outpatient settings, the Therapy Caps will no longer apply to such services starting as of April 1, 2014.

In the Deficit Reduction Act of 2005, Congress implemented an exceptions process to the annual Limit for therapy expenses for therapy services above the annual Limit. The Bipartisan Budget Act of 2013 extended the exceptions process for outpatient Therapy Caps through March 31, 2014. Therapy services above the annual Limit that are medically necessary satisfy an exception to the annual Limit and such claims are payable by the Medicare program. Unless Congress extends the exceptions process, the Therapy Caps will apply to all claims regardless of medical necessity beginning April 1, 2014. For any claim above the annual Limit, the claim must contain a modifier indicating that the services are medically necessary and justified by appropriate documentation in the medical record.

Furthermore, under the MCTRA, since October 1, 2012, patients who met or exceeded \$3,700 in therapy expenditures during a calendar year have been subject to a manual medical review to determine whether applicable payment criteria are satisfied. The \$3,700 threshold is applied to Physical Therapy and Speech Language Pathology Services; a separate \$3,700 threshold is applied to the Occupational Therapy. The Bipartisan Budget Relief Act of 2013 extended through March 31, 2014 the requirement that Medicare perform manual medical review of therapy services beyond the \$3,700 threshold. In addition, as of January 1, 2013, CMS implemented a claims based data collection strategy that is designed to assist in reforming the Medicare payment system for outpatient therapy. Since January 1, 2013, all therapy claims must include additional codes and

modifiers providing information about the beneficiary’s functional status at the outset of the therapy episode of care, specified points during treatment, and at the time of discharge. Effective July 1, 2013, claims submitted without the appropriate codes and modifiers are returned unpaid.

CMS adopted a MPPR for therapy services in the final update to the MPFS for calendar year 2011. During 2011, the MPPR applied to all outpatient therapy services paid under Medicare Part B — occupational therapy, physical therapy and speech-language pathology. Under the policy, the Medicare program pays 100% of the practice expense component of the RVU for the therapy procedure with the highest practice expense RVU, then reduces the payment for the practice expense component for the second and subsequent therapy procedures or units of service furnished during the same day for the same patient, regardless of whether those therapy services are furnished in separate sessions. In 2011 and 2012, the practice expense component for the second and subsequent therapy service furnished during the same day for the same patient was reduced by 20% in office and other non-institutional settings and by 25% in institutional settings. The American Taxpayer Relief Act of 2012 increased the payment reduction of the practice expense component to 50%, on subsequent therapy procedures in either setting, effective April 1, 2013.

In addition, the MCTRA directed CMS to implement a claims-based data collection program to gather additional data on patient function during the course of therapy in order to better understand patient conditions and outcomes. All practice settings that provide outpatient therapy services are required to include this data on the claim form. Since July 1, 2013, therapists have been required to report new codes and modifiers on the claim form that reflect a patient’s functional limitations and goals at initial evaluation, periodically throughout care, and at discharge. Since July 1, 2013, CMS has rejected claims if the required data is not included in the claim.

The PQRS is a CMS reporting program that uses a combination of incentive payments and payment reductions to promote reporting of quality information by “eligible professionals.” Although physical therapists, occupational therapists and qualified speech-language therapists are generally able to participate in the PQRS program, therapy professionals for whose services we bill through our rehab agencies cannot participate because the Medicare claims processing systems currently cannot accommodate institutional providers such as rehab agencies. Eligible professionals, such as those of our therapy professionals for whose services we bill using their individual Medicare provider numbers, who do not satisfactorily report data on quality measures will be subject to a 2% reduction in their Medicare payment in 2016.

Statutes, regulations, and payment rules governing the delivery of therapy services to Medicare beneficiaries are complex and subject to interpretation. We believe that we are in substantial compliance in all material respects with all applicable laws and regulations and are not aware of any pending or threatened investigations involving allegations of potential wrongdoing that would have a material effect on our financial statements as of December 31, 2013. Compliance with such laws and regulations can be subject to future government review and interpretation, as well as significant regulatory action including fines, penalties, and exclusion from the Medicare program.

As a result of increased post-payment reviews of claims we submit to Medicare for our services, we may incur additional costs and may be required to repay amounts already paid to us.

We are subject to regular post-payment inquiries, investigations and audits of the claims we submit to Medicare for payment for our services. These post-payment reviews are increasing as a result of new government cost-containment initiatives. These additional post-payment reviews may require us to incur additional costs to respond to requests for records and to pursue the reversal of payment denials, and ultimately may require us to refund amounts paid to us by Medicare that are determined to have been overpaid.

For a further description of this and other laws and regulations involving governmental reimbursements, see “Business—Sources of Revenue” and “—Regulation and Healthcare Reform” in Item 1.

If we fail to effectively and timely transition to the ICD-10 coding system, our operations could be adversely affected.

Health plans and providers are required to transition to the new ICD-10 coding system, which greatly expands the number and detail of billing codes used for third-party claims. Use of the ICD-10 system is required beginning October 1, 2014. Transition to the new ICD-10 system requires significant investment in coding technology and software as well as the training of staff involved in the coding and billing process. In addition to these upfront costs of transition to ICD-10, it is possible that we could experience disruption or delays in payment due to technical or coding errors or other implementation issues involving our systems or the systems and implementation efforts of health plans and their business partners.

The uncertain economic conditions and the historically high unemployment rate may have material adverse impacts on our business and financial condition that we currently cannot predict.

Unemployment in the United States has remained high while business and consumer confidence is relatively low. Although it is difficult to predict with any degree of certainty the impact on our business, these factors could materially and adversely affect our business and financial condition.

We depend upon reimbursement by third-party payors.

Substantially all of our revenues are derived from private and governmental third-party payors. In 2013, approximately 76.5% of our revenues were derived collectively from managed care plans, commercial health insurers, workers' compensation payors, and other private pay revenue sources and approximately 23.5% of our revenues were derived from Medicare and Medicaid. Initiatives undertaken by industry and government to contain healthcare costs affect the profitability of our clinics. These payors attempt to control healthcare costs by contracting with healthcare providers to obtain services on a discounted basis. We believe that this trend will continue and may limit reimbursement for healthcare services. If insurers or managed care companies from whom we receive substantial payments were to reduce the amounts they pay for services, our profit margins may decline, or we may lose patients if we choose not to renew our contracts with these insurers at lower rates. In addition, in certain geographical areas, our clinics must be approved as providers by key health maintenance organizations and preferred provider plans. Failure to obtain or maintain these approvals would adversely affect our financial results.

In recent years, through legislative and regulatory actions, the federal government has made substantial changes to various payment systems under the Medicare program. See "Business- Sources of Revenue" in Item 1 for more information. President Obama signed into law comprehensive reforms to the healthcare system, including changes to Medicare reimbursement. Additional reforms or other changes to these payment systems may be proposed or adopted, either by the U.S. Congress or by CMS. If revised regulations are adopted, the availability, methods and rates of Medicare reimbursements for services of the type furnished at our facilities could change. Some of these changes and proposed changes could adversely affect our business strategy, operations and financial results.

Our facilities are subject to extensive federal and state laws and regulations relating to the privacy of individually identifiable information.

HIPAA required the HHS to adopt standards to protect the privacy and security of individually identifiable health-related information. The department released final regulations containing privacy standards in December 2000 and published revisions to the final regulations in August 2002. The privacy regulations extensively regulate the use and disclosure of individually identifiable health-related information. The regulations also provide patients with significant rights related to understanding and controlling how their health information is used or disclosed. The security regulations require healthcare providers to implement administrative, physical and technical practices to protect the security of individually identifiable health information that is maintained or transmitted electronically. HITECH, which was signed into law in February of 2009, enhanced the privacy,

security and enforcement provisions of HIPAA by, among other things establishing security breach notification requirements, allowing enforcement of HIPAA by state attorneys general, and increasing penalties for HIPAA violations. Violations of HIPAA or HITECH could result in civil or criminal penalties.

In addition to HIPAA, there are numerous federal and state laws and regulations addressing patient and consumer privacy concerns, including unauthorized access or theft of personal information. State statutes and regulations vary from state to state. Lawsuits, including class actions and action by state attorneys general, directed at companies that have experienced a privacy or security breach also can occur.

The Company and its clinics have established policies and procedures in an effort to ensure compliance with these privacy related requirements. However, if there is a breach, we may be subject to various penalties and damages and may be required to incur costs to mitigate the impact of the breach on affected individuals.

We depend upon the cultivation and maintenance of relationships with the physicians in our markets.

Our success is dependent upon referrals from physicians in the communities our clinics serve and our ability to maintain good relations with these physicians and other referral sources. Physicians referring patients to our clinics are free to refer their patients to other therapy providers or to their own physician owned therapy practice. If we are unable to successfully cultivate and maintain strong relationships with physicians and other referral sources, our business may decrease and our net operating revenues may decline.

We also depend upon our ability to recruit and retain experienced physical therapists.

Our revenue generation is dependent upon referrals from physicians in the communities our clinics serve, and our ability to maintain good relations with these physicians. Our therapists are the front line for generating these referrals and we are dependent on their talents and skills to successfully cultivate and maintain strong relationships with these physicians. If we cannot recruit and retain our base of experienced and clinically skilled therapists, our business may decrease and our net operating revenues may decline. Periodically, we have clinics in isolated communities that are temporarily unable to operate due to the unavailability of a therapist who satisfies our standards.

Our revenues may fluctuate due to weather.

We have a significant number of clinics in states that normally experience snow and ice during the winter months. Also, a significant number of our clinics are located in states along the Gulf Coast and Atlantic Coast which are subject to periodic winter storms, hurricanes and other severe storm systems. Periods of severe weather may cause physical damage to our facilities or prevent our staff or patients from traveling to our clinics, which may cause a decrease in our net operating revenues.

We operate in a highly competitive industry.

We encounter competition from local, regional or national entities, some of which have superior resources or other competitive advantages. Intense competition may adversely affect our business, financial condition or results of operations. For a more complete description of this competitive environment, see “Business—Competition” in Item 1. An adverse effect on our business, financial condition or results of operations may require us to write-down goodwill.

We may incur closure costs and losses.

The competitive, economic or reimbursement conditions in our markets in which we operate may require us to reorganize or to close certain clinics. In the event a clinic is reorganized or closed, we may incur losses and closure costs. The closure costs and losses may include, but are not limited to, lease obligations, severance, and write-down or write-off of goodwill and other intangible assets.

Future acquisitions may use significant resources, may be unsuccessful and could expose us to unforeseen liabilities.

As part of our growth strategy, we intend to continue pursuing acquisitions of outpatient physical therapy clinics. Acquisitions may involve significant cash expenditures, potential debt incurrence and operational losses, dilutive issuances of equity securities and expenses that could have an adverse effect on our financial condition and results of operations. Acquisitions involve numerous risks, including:

- the difficulty and expense of integrating acquired personnel into our business;
- the diversion of management's time from existing operations;
- the potential loss of key employees of acquired companies;
- the difficulty of assignment and/or procurement of managed care contractual arrangements; and
- the assumption of the liabilities and exposure to unforeseen liabilities of acquired companies, including liabilities for failure to comply with healthcare regulations.

We may not be successful in obtaining financing for acquisitions at a reasonable cost, or such financing may contain restrictive covenants that limit our operating flexibility. We also may be unable to acquire outpatient physical therapy clinics or successfully operate such clinics following the acquisition.

Certain of our internal controls, particularly as they relate to billings and cash collections, are largely decentralized at our clinic locations.

Our clinic operations are largely decentralized and certain of our internal controls, particularly the processing of billings and cash collections, occur at the clinic level. Taken as a whole, we believe our internal controls for these functions at our clinics are adequate. Our controls for billing and cash collections largely depend on compliance with our written policies and procedures and separation of functions among clinic personnel. We also maintain corporate level controls, including an audit compliance program, that are intended to mitigate and detect any potential deficiencies in internal controls at the clinic level. The effectiveness of these controls to future periods are subject to the risk that controls may become inadequate because of changes in conditions or the level of compliance with our policies and procedures deteriorates.

We may not be able to generate sufficient cash to service all of our indebtedness and may not be able to refinance our indebtedness on favorable terms. If we are unable to do so, we may be forced to take other actions to satisfy our obligations under our indebtedness, which may not be successful.

Our ability to make scheduled payments on or to refinance our debt obligations depends on our financial condition and operating performance, which are subject to prevailing economic and competitive conditions and to certain financial, business and other factors beyond our control. We cannot assure you we will maintain a level of cash flows from operating activities sufficient to permit us to pay the principal, premium, if any, and interest on our indebtedness.

In addition, we conduct our operations through our subsidiaries. Accordingly, repayment of our indebtedness is dependent on the generation of cash flow by our subsidiaries and their ability to make such cash available to us by dividend, debt repayment or otherwise. Our subsidiaries may not be able to, or may not be permitted to, make distributions to enable us to make payments in respect of our indebtedness. Each subsidiary is a distinct legal entity, and, under certain circumstances, legal and contractual restrictions may limit our ability to obtain cash from our subsidiaries. We may find it necessary or prudent to refinance our outstanding indebtedness with longer-maturity debt at a higher interest rate. Our ability to refinance our indebtedness on favorable terms, or at all, is directly affected by the current global economic and financial conditions. In addition, our ability to incur secured indebtedness (which would generally enable us to achieve better pricing than the incurrence of unsecured indebtedness) depends in part on the value of our assets, which depends, in turn, on the strength of our cash flows and results of operations, and on economic and market conditions and other factors.

If our cash flows and capital resources are insufficient to fund our debt service obligations or we are unable to refinance our indebtedness, we may be forced to reduce or delay investments and capital expenditures, or to sell assets, seek additional capital or restructure our indebtedness. These alternative measures may not be successful and may not permit us to meet our scheduled debt service obligations. If our operating results and available cash are insufficient to meet our debt service obligations, we could face substantial liquidity problems and might be required to dispose of material assets or operations to meet our debt service and other obligations. We may not be able to consummate those dispositions, or the proceeds from the dispositions may not be adequate to meet any debt service obligations then due.

Our Credit Agreement contains restrictions that limit our flexibility in operating our business.

Our Credit Agreement contains various covenants that limit our ability to engage in specified types of transactions. These covenants limit our and our subsidiaries' ability to, among other things: incur additional indebtedness; pay dividends on, repurchase or make distributions in respect of our capital stock or make other restricted payments; make certain investments; sell or transfer assets; create liens; consolidate, merge, sell or otherwise dispose of all or substantially all of our assets; and enter into certain transactions with our affiliates.

Under our Credit Agreement, we are required to satisfy and maintain specified financial ratios. Our ability to meet those financial ratios can be affected by events beyond our control, and there can be no assurance we will continue to meet those ratios. A breach of any of these covenants could result in a default under our Credit Agreement. Upon the occurrence of an event of default under the Credit Agreement, the lenders thereunder could elect to declare all amounts outstanding under the Credit Agreement to be immediately due and payable and terminate all commitments to extend further credit.

Risks Relating to Our Outstanding Common Stock

Our stock price could be volatile, which could cause you to lose part or all of your investment.

The stock market has from time to time experienced significant price and volume fluctuations that may be unrelated to the operating performance of particular companies. In particular, the market price of our common stock has been and may continue to be highly volatile. During 2013, our stock price ranged from a low of \$22.80 per share (on March 11, 2013) to a high of \$35.84 per share (on December 31, 2013). Factors, such as announcements concerning changes in revenues and earnings expectations, regulatory conditions, including federal and state regulations, and economic and other external factors, as well as period-to-period fluctuations and financial results, may have a significant effect on the market price of our common stock.

From time to time, there has been limited trading volume in our common stock. In addition, there can be no assurance that there will continue to be a trading market or that any securities research analysts will continue to provide research coverage with respect to our common stock. It is possible that such factors will adversely affect the market for our common stock.

Issuance of shares in connection with financing transactions or under stock incentive plans will dilute current stockholders.

Pursuant to our stock incentive plans, our Compensation Committee of the Board of Directors, consisting solely of independent directors, is authorized to grant stock awards to our employees, directors and consultants. Shareholders will incur dilution upon the exercise of any outstanding stock awards or the grant of any restricted stock. In addition, if we raise additional funds by issuing additional common stock, or securities convertible into or exchangeable or exercisable for common stock, further dilution to our existing stockholders will result, and new investors could have rights superior to existing stockholders.

The number of shares of our common stock eligible for future sale could adversely affect the market price of our stock.

At December 31, 2013, we had reserved approximately 38,700 shares of common stock for issuance under outstanding options and 648,000 shares for future equity grants. Of these shares, 148,000 of common stock are registered for sale or resale on currently effective registration statements and 500,000 have been approved by stockholders and will be registered for sale or resale in early 2014. We may issue additional restricted securities or register additional shares of common stock under the Securities Act of 1933, as amended (the "Securities Act") in the future. The issuance of a significant number of shares of common stock upon the exercise of stock options or the availability for sale, or sale, of a substantial number of the shares of common stock eligible for future sale under effective registration statements, under Rule 144 or otherwise, could adversely affect the market price of the common stock.

Provisions in our articles of incorporation and bylaws could delay or prevent a change in control of our company, even if that change would be beneficial to our stockholders.

Certain provisions of our articles of incorporation and bylaws may delay, discourage, prevent or render more difficult an attempt to obtain control of our company, whether through a tender offer, business combination, proxy contest or otherwise. These provisions include the charter authorization of "blank check" preferred stock and a restriction on the ability of stockholders to call a special meeting.

ITEM 1B. UNRESOLVED STAFF COMMENTS.

Not Applicable.

ITEM 2. PROPERTIES.

We lease the properties used for our clinics under non-cancelable operating leases with terms ranging from one to five years, with the exception of the property for one clinic which we own. We intend to lease the premises for any new clinic locations except in rare instances where leasing is not a cost-effective alternative. Our typical clinic occupies 1,500 to 3,000 square feet.

We also lease our executive offices located in Houston, Texas, under a non-cancelable operating lease expiring in April 2017. We currently occupy approximately 37,537 square feet of space (including allocations for common areas) at our executive offices.

ITEM 3. LEGAL PROCEEDINGS.

We are involved in litigation and other proceedings arising in the ordinary course of business. While the ultimate outcome of lawsuits or other proceedings cannot be predicted with certainty, we do not believe the impact of existing lawsuits or other proceedings will have a material impact on our business, financial condition or results of operations.

ITEM 4. MINE SAFETY DISCLOSURES.

Not Applicable.

PART II

ITEM 5. *MARKET FOR REGISTRANT'S COMMON EQUITY, RELATED STOCKHOLDER MATTERS AND ISSUER PURCHASES OF EQUITY SECURITIES.*

PRICE QUOTATIONS

Our common stock has traded on the New York Stock Exchange ("NYSE") since August 14, 2012 under the symbol "USPH." Prior to that, our common stock was traded on the Nasdaq Global Select Market under the symbol "USPH". As of March 10, 2014, there were 64 holders of record of our outstanding common stock. The table below indicates the high and low sales prices of our common stock reported for the periods presented.

| Quarter | 2013 | | 2012 | |
|--------------|---------|---------|---------|---------|
| | High | Low | High | Low |
| First | \$28.24 | \$22.80 | \$23.39 | \$18.51 |
| Second | 31.56 | 22.84 | 25.46 | 22.52 |
| Third | 32.15 | 26.91 | 28.40 | 23.75 |
| Fourth | 35.84 | 29.55 | 28.24 | 22.69 |

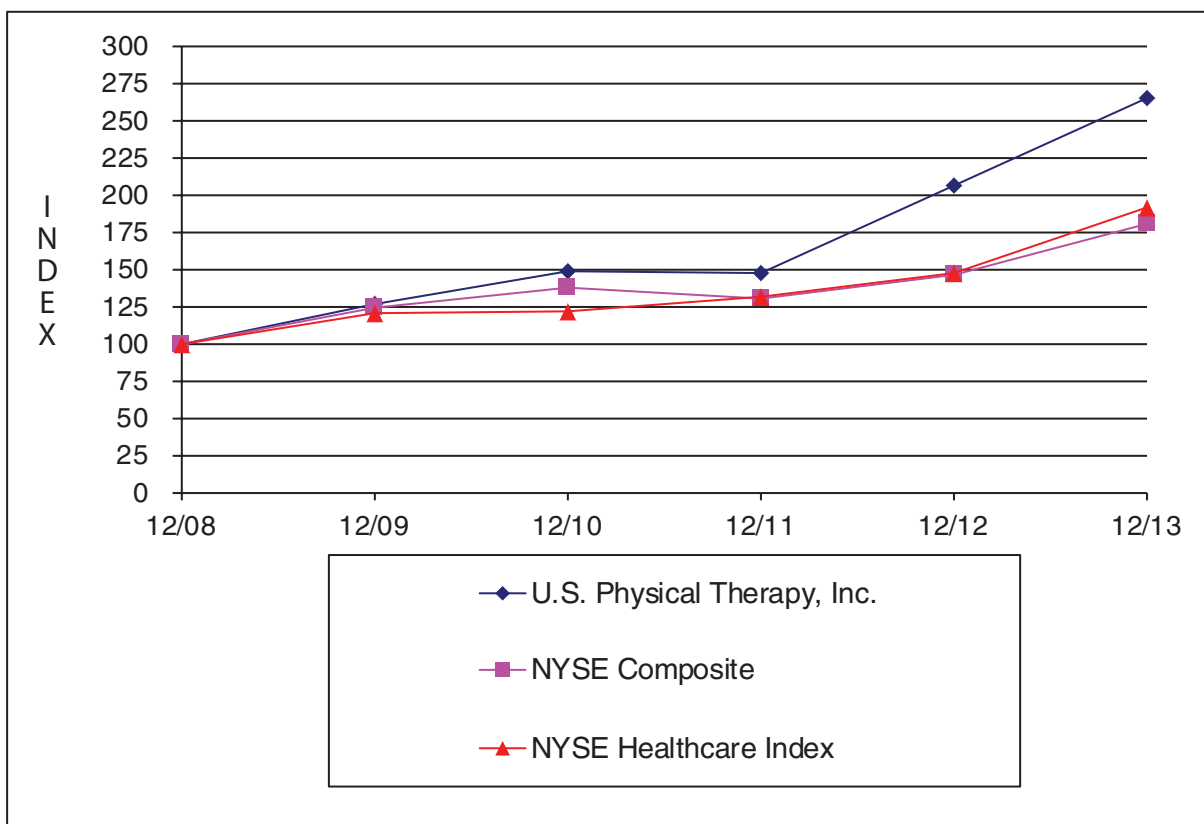
During 2013, we paid a quarterly dividend of \$0.10 per share totaling \$0.40 per share for 2013, which amounted to a total of aggregate cash payments of dividends to holders of our common stock in 2013 of approximately \$4.8 million. During 2012, we paid a quarterly dividend of \$0.09 per share and a special dividend in December 2012 of \$0.40 per share, totaling \$0.76 per share for 2012, which amounted to a total of aggregate cash payments of dividends to holders of our common stock in 2012 of approximately \$9.0 million. In 2014, our Board of Directors declared a quarterly dividend of \$0.12 per share payable to shareholders of record on March 19, 2014 to be paid on April 4, 2014. We are currently restricted from paying dividends in excess of \$7,500,000 in any fiscal year on our common stock under the Credit Agreement.

FIVE YEAR PERFORMANCE GRAPH

The performance graph and related description shall not be deemed incorporated by reference into any filing under the Securities Act or under the Exchange Act, except to the extent that the Company specifically incorporates this information by reference. In addition, the performance graph and the related description shall not be deemed “soliciting material” or “filed” with the SEC or subject to Regulation 14A or 14C.

Prior to August 14, 2012, our common stock traded on the NASDAQ Stock Market. On August 14, 2012, our common stock began trading on the New York Stock Exchange (“NYSE”). The following performance graph compares the cumulative total stockholder return of our common stock to The NYSE Composite Index and the NYSE Health Care Index for the period from December 31, 2008 through December 31, 2013. The graph assumes that \$100 was invested in our common stock and the common stock of each of the companies listed on The NYSE Composite Index and The NYSE Health Care Index on December 31, 2008 and that any dividends were reinvested.

Comparison of Five Years Cumulative Total Return for the Year Ended December 31, 2013



| | 12/08 | 12/09 | 12/10 | 12/11 | 12/12 | 12/13 |
|-----------------------------------|-------|-------|-------|-------|-------|-------|
| U. S. Physical Therapy, Inc. | 100 | 127 | 149 | 148 | 207 | 265 |
| NYSE Composite | 100 | 125 | 138 | 130 | 147 | 181 |
| NYSE Healthcare Index | 100 | 120 | 122 | 132 | 148 | 192 |

ITEM 6. SELECTED FINANCIAL DATA.

The following selected financial data from continuing operations should be read in conjunction with the description of our critical accounting policies set forth in “Management’s Discussion and Analysis of Results of Operations and Financial Condition”.

| | 2013 | For the Years Ended December 31, | | | 2009 |
|--|-----------|--|-----------|-----------|-----------|
| | | 2012 | 2011 | 2010 | |
| | | (\$ in thousands, except per share data) | | | |
| Net revenues | \$264,058 | \$249,651 | \$231,523 | \$208,646 | \$199,458 |
| Income from continuing operations including noncontrolling interests, net of tax | \$ 26,003 | \$ 26,640 | \$ 26,679 | \$ 24,083 | \$ 19,732 |
| Net income including noncontrolling interests | \$ 20,996 | \$ 26,217 | \$ 29,783 | \$ 24,700 | \$ 19,974 |
| Net income attributable to common shareholders | \$ 17,492 | \$ 18,212 | \$ 18,812 | \$ 15,305 | \$ 11,380 |
| Basic earnings per share attributable to common shareholders: | \$ 1.45 | \$ 1.54 | \$ 1.60 | \$ 1.32 | \$ 0.97 |
| Diluted earnings per share attributable to common shareholders: | \$ 1.45 | \$ 1.53 | \$ 1.57 | \$ 1.30 | \$ 0.95 |
| Dividends declared and paid per common share | \$ 0.40 | \$ 0.76 | \$ 0.32 | \$ — | \$ — |

| | 2013 | 2012 | On December 31, | | 2009 |
|--|-------------------|-----------|-----------------|-----------|-----------|
| | | | 2011 | 2010 | |
| | (\$ in thousands) | | | | |
| Total assets | \$224,135 | \$171,714 | \$163,252 | \$140,861 | \$111,429 |
| Long-term debt, less current portion | \$ 40,650 | \$ 17,575 | \$ 23,784 | \$ 5,750 | \$ 400 |
| Working capital | \$ 26,488 | \$ 29,015 | \$ 29,343 | \$ 25,053 | \$ 18,255 |
| Current ratio | 2.14 | 2.78 | 2.80 | 2.76 | 2.24 |
| Total long-term debt to total capitalization | 0.27 | 0.13 | 0.20 | 0.05 | — |

ITEM 7. MANAGEMENT’S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS.

EXECUTIVE SUMMARY

Our Business. We operate outpatient physical therapy clinics that provide pre- and post-operative care and treatment for a variety of orthopedic-related disorders and sports-related injuries, neurologically-related injuries and rehabilitation of injured workers.

During 2013, 2012 and 2011, we completed the following multi-clinic acquisitions:

| <u>Acquisition</u> | <u>Date</u> | <u>% Interest Acquired</u> | <u>Number of Clinics</u> |
|-------------------------------|-------------|----------------------------|--------------------------|
| | <u>2013</u> | | |
| February 2013 Acquisition | February 28 | 72% | 9 |
| April 2013 Acquisition | April 30 | 50% | 5 |
| May 2013 Acquisition | May 24 | 80% | 5 |
| December 9, 2013 Acquisition | December 9 | 60% | 12 |
| December 13, 2013 Acquisition | December 13 | 90% | 11 |
| | <u>2012</u> | | |
| May 2012 Acquisition | May 22 | 70% | 7 |
| | <u>2011</u> | | |
| July 2011 Acquisition | July 25 | 51% | 20 |

In addition to the five multi-clinic acquisitions detailed above, in 2013, we acquired three individual clinics in separate transactions. In addition to the May 2012 Acquisition, in 2012, we acquired seven individual clinics in separate transactions. Two of the acquired clinic practices operate in two separate partnerships and the remaining five operate as satellites of existing partnerships.

The results of operations of the acquired clinics have been included in our consolidated financial statements since the date of their acquisition.

On September 30, 2013, we sold the remainder of our physician services business. Previously, the Company closed its two physician services facilities – one in August 2013 and the other in December 2012. As previously disclosed in the Company’s public filings, the physician services business incurred negative gross margins in 2012 and through the first nine months of 2013. Revenues from physician services were generated by patient visits, franchise arrangements and fees from third parties. The results of operations and the loss on the sale of the physician services business have been reclassified to discontinued operations for all periods presented.

The following table details the losses from discontinued operations reported for the physician services business (in thousands):

| | <u>For the Year Ended December 31,</u> | | |
|---|--|------------------------|------------------------|
| | <u>2013</u> | <u>2012</u> | <u>2011</u> |
| Net revenues | \$ 864 | \$2,435 | \$ 5,483 |
| Operating costs | <u>1,537</u> | <u>2,761</u> | <u>702</u> |
| Gross margin | (673) | (326) | 4,781 |
| Direct general and administrative expenses less proceeds .. | 1,176 | 278 | 278 |
| Write off of goodwill and other intangible assets | <u>6,338</u> | <u>—</u> | <u>—</u> |
| | (8,187) | (604) | 4,503 |
| Tax benefit | <u>3,180</u> | <u>181</u> | <u>(1,399)</u> |
| (Loss) income from discontinued operations | <u><u>\$(5,007)</u></u> | <u><u>\$ (423)</u></u> | <u><u>\$ 3,104</u></u> |

At December 31, 2013, we operated 472 clinics in 43 states. The average age of our clinics at December 31, 2013 was 8.5 years.

In addition to our owned clinics, we also manage physical therapy facilities for third parties, primarily physicians, with 18 third-party facilities under management as of December 31, 2013.

CRITICAL ACCOUNTING POLICIES

Critical accounting policies are those that have a significant impact on our results of operations and financial position involving significant estimates requiring our judgment. Our critical accounting policies are:

Revenue Recognition. Revenues are recognized in the period in which services are rendered. Net patient revenues (patient revenues less estimated contractual adjustments) are reported at the estimated net realizable amounts from insurance companies, third-party payors, patients and others for services rendered. The Company has agreements with third-party payors that provide for payments to the Company at contracted amounts different from its established rates. The allowance for estimated contractual adjustments is based on terms of payor contracts and historical collection and write-off experience.

Revenues from physician services, sold primarily through franchisee arrangements, are considered multiple deliverables—training and ongoing services. Each component can be purchased separately. Revenue is recognized over the period the respective services are provided.

Contractual Allowances. Contractual allowances result from the differences between the rates charged for services performed and expected reimbursements by both insurance companies and government sponsored

healthcare programs for such services. Medicare regulations and the various third party payors and managed care contracts are often complex and may include multiple reimbursement mechanisms payable for the services provided in our clinics. We estimate contractual allowances based on our interpretation of the applicable regulations, payor contracts and historical calculations. Each month the Company estimates its contractual allowance for each clinic based on payor contracts and the historical collection experience of the clinic and applies an appropriate contractual allowance reserve percentage to the gross accounts receivable balances for each payor of the clinic. Based on our historical experience, calculating the contractual allowance reserve percentage at the payor level is sufficient to allow us to provide the necessary detail and accuracy with our collectibility estimates. However, the services authorized and provided and related reimbursement are subject to interpretation that could result in payments that differ from our estimates. Payor terms are periodically revised necessitating continual review and assessment of the estimates made by management. Our billing system may not capture the exact change in our contractual allowance reserve estimate from period to period. Therefore, in order to assess the accuracy of our revenues and hence our contractual allowance reserves, our management regularly compares its cash collections to corresponding net revenues measured both in the aggregate and on a clinic-by-clinic basis. In the aggregate, the historical difference between net revenues and corresponding cash collections has generally reflected a difference within approximately 1% of net revenues. Additionally, analysis of subsequent period's contractual write-offs on a payor basis reflects a difference within approximately 1% between the actual aggregate contractual reserve percentage as compared to the estimated contractual allowance reserve percentage associated with the same period end balance. As a result, we believe that a reasonable likely change in the contractual allowance reserve estimate would not be more than 1% at December 31, 2013. For purposes of demonstrating the sensitivity of this estimate on the Company's financial condition, a one percent increase or decrease in our aggregate contractual allowance reserve percentage would decrease or increase, respectively, net patient revenue by approximately \$736,000 for the year ended December 31, 2013. Management believes the changes in the estimate of the contractual allowance reserve for the periods ended December 31, 2013, 2012 and 2011 have not been material to the statement of operations.

The following table sets forth information regarding our patient accounts receivable as of the dates indicated (in thousands):

| | December 31, | |
|--|-----------------|-----------------|
| | 2013 | 2012 |
| Gross patient accounts receivable | \$73,636 | \$64,101 |
| Less contractual allowances | 41,386 | 36,533 |
| Subtotal - accounts receivable | 32,250 | 27,568 |
| Less allowance for doubtful accounts | 1,430 | 1,595 |
| Net patient accounts receivable | <u>\$30,820</u> | <u>\$25,973</u> |

The following table presents our patient accounts receivable aging by payor class as of the dates indicated (in thousands):

| Payor | December 31, 2013 | | | December 31, 2012 | | |
|--------------------------------------|---------------------|----------------|-----------------|---------------------|----------------|-----------------|
| | Current to 120 Days | 120+ Days | Total | Current to 120 Days | 120+ Days | Total |
| Managed Care/ Commercial Plans | \$10,762 | \$1,336 | \$12,098 | \$ 9,308 | \$1,648 | \$10,956 |
| Medicare/Medicaid | 6,943 | 996 | 7,939 | 5,451 | 1,089 | 6,540 |
| Workers Compensation* | 6,883 | 1,009 | 7,892 | 5,425 | 1,027 | 6,452 |
| Self-pay | 1,236 | 1,347 | 2,583 | 878 | 1,307 | 2,185 |
| Other** | 1,137 | 601 | 1,738 | 793 | 642 | 1,435 |
| Totals | <u>\$26,961</u> | <u>\$5,289</u> | <u>\$32,250</u> | <u>\$21,855</u> | <u>\$5,713</u> | <u>\$27,568</u> |

* Workers compensation is paid by state administrators or their designated agents.

** Other includes primarily litigation claims and, to a lesser extent, vehicular insurance claims.

Reimbursement for Medicare beneficiaries is based upon a fee schedule published by HHS. For a more complete description of our third party revenue sources, see “Business—Sources of Revenue” in Item 1.

Provision for Doubtful Accounts. We determine our provision for doubtful accounts based on the specific agings and payor classifications at each clinic. We review the accounts receivable aging and rely on prior experience with particular payors to determine an appropriate reserve for doubtful accounts. Historically, clinics that have a large number of aged accounts generally have less favorable collection experience, and thus, require a higher allowance. Accounts that are ultimately determined to be uncollectible are written off against our bad debt allowance. The amount of our aggregate allowance for doubtful accounts is regularly reviewed for adequacy in light of current and historical experience.

Accounting for Income Taxes. We account for income taxes under the asset and liability method. Deferred tax assets and liabilities are recognized for the future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases and operating loss and tax credit carryforwards. 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 effect on deferred tax assets and liabilities of a change in tax rates is recognized in income in the period that includes the enactment date. The Company recognizes the financial statement benefit of a tax position only after determining that the relevant tax authority would more likely than not sustain the position following an audit. For tax positions meeting the more-likely-than-not threshold, the amount to be recognized in the financial statements is the largest benefit that has a greater than 50 percent likelihood of being realized upon ultimate settlement with the relevant tax authority.

We do not believe that we have any significant uncertain tax positions at December 31, 2013, nor is this expected to change within the next twelve months due to the settlement and expiration of statutes of limitation.

We did not have any accrued interest or penalties associated with any unrecognized tax benefits nor was any interest expense recognized during the twelve months ended December 31, 2013 and 2012.

Carrying Value of Long-Lived Assets. Our property and equipment, intangible assets and goodwill (collectively, our “long-lived assets”) comprise a significant portion of our total assets. The accounting standards require that we periodically, and upon the occurrence of certain events, assess the recoverability of our long-lived assets. If the carrying value of our property and equipment exceeds their undiscounted cash flows, we are required to write the carrying value down to estimated fair value.

Goodwill. The fair value of goodwill and other intangible assets with indefinite lives are tested for impairment annually and upon the occurrence of certain events, and are written down to fair value if considered impaired. The Company evaluates goodwill for impairment on at least an annual basis (in its third quarter) by comparing the fair value of its reporting units to the carrying value of each reporting unit including related goodwill. We operate a one segment business which is made up of various clinics within partnerships. The partnerships are components of regions and are aggregated to the operating segment level for the purpose of determining our reporting units when performing our annual goodwill impairment test.

An impairment loss generally would be recognized when the carrying amount of the net assets of a reporting unit, inclusive of goodwill and other intangible assets, exceeds the estimated fair value of the reporting unit. The estimated fair value of a reporting unit is determined using two factors: (i) earnings prior to taxes, depreciation and amortization for the reporting unit multiplied by a price/earnings ratio used in the industry and (ii) a discounted cash flow analysis. A weight is assigned to each factor and the sum of each weight times the factor is considered the estimated fair value. For 2013, the factors (i.e., price/earnings ratio, discount rate and residual capitalization rate) were updated to reflect current market conditions. The evaluation of goodwill in 2013, 2012 and 2011 did not result in any goodwill amounts that were deemed impaired.

SELECTED OPERATING AND FINANCIAL DATA

The following table and discussion relates to continuing operations unless otherwise noted. The defined terms with their respective description used in the following discussion are listed below:

| | |
|-------------------------------|--|
| 2013 | Year ended December 31, 2013 |
| 2012 | Year ended December 31, 2012 |
| 2011 | Year ended December 31, 2011 |
| New Clinics | Clinics opened or acquired during the year ended December 31, 2013 |
| Mature Clinics | Clinics opened or acquired prior to January 1, 2013 |
| 2012 New Clinics | Clinics opened or acquired during the year ended December 31, 2012 |
| 2012 Mature Clinics | Clinics opened or acquired prior to January 1, 2012 |
| 2011 New Clinics | Clinics opened or acquired during the year ended December 31, 2011 |
| 2011 Mature Clinics | Clinics opened or acquired prior to January 1, 2011 |

The following table presents selected operating and financial data, used by management as key indicators of our operating performance:

| | For the Years Ended December 31, | | |
|---|----------------------------------|-----------|-----------|
| | 2013 | 2012 | 2011 |
| Number of clinics, at the end of period | 472 | 431 | 416 |
| Working Days | 255 | 255 | 255 |
| Average visits per day per clinic | 21.5 | 21.7 | 20.9 |
| Total patient visits | 2,440,590 | 2,313,814 | 2,161,012 |
| Net patient revenue per visit | \$ 105.83 | \$ 105.50 | \$ 104.49 |

RESULTS OF OPERATIONS

FISCAL YEAR 2013 COMPARED TO FISCAL 2012

- Net revenues rose 5.8 % to \$264.1 million for 2013 from \$249.7 million for 2012 primarily due to increases in net patient revenues which is discussed in detail below.
- Reported net income attributable to common shareholders for 2013 decreased 4.0% to \$17.5 million from \$18.2 million in 2012. Diluted earnings per share were \$1.45 for 2013 and \$1.53 for 2012.

Net Patient Revenues

- Net patient revenues increased to \$258.3 million for 2013 from \$244.1 million for 2012, an increase of \$14.2 million, or 5.8%. The increase in net patient revenues of \$14.2 million consisted of an increase of \$12.4 million from New Clinics and \$1.8 million from Mature Clinics. During 2013, we acquired five multi-clinic groups for a total of 42 clinics. The average net patient revenue per visit increased to \$105.83 in 2013 from \$105.50 in 2012. The net patient revenues are included in our results since the respective date of their acquisition. See above table.
- Total patient visits increased to 2,441,000 for 2013 from 2,314,000 for 2012. The growth in patient visits was attributable to 110,000 visits in New Clinics primarily due to the acquisitions in 2013 and an increase of 17,000 visits for Mature Clinics.

Net patient revenues are based on established billing rates less allowances and discounts for patients covered by contractual programs and workers' compensation. Net patient revenues reflect contractual and other adjustments, which we evaluate monthly, relating to patient discounts from certain payors. Payments received under these programs are based on predetermined rates and are generally less than the established billing rates of the clinics.

Other Revenues

Other revenues, consisting primarily of management fees, increased by \$224,000 from \$5.6 million to \$5.8 million. This increase was primarily due to an increase in the number of management contracts. On December 31, 2013, we managed 18 third-party physical therapy facilities versus 15 on December 31, 2012.

Clinic Operating Costs

Clinic operating costs were \$199.4 million, or 75.5% of net revenues, for 2013 and \$186.7 million, or 74.8% of net revenues, for 2012. The increase was primarily attributable to \$10.2 million in operating costs of New Clinics and an increase in operating costs of \$6.3 million for 2012 New Clinics offset by a decrease in operating costs of \$3.8 million for 2012 Mature Clinics. Included in the 2013 results is a pre-tax charge of \$0.9 million related to an estimated refund due to a payor for overpayments to a partnership clinic group over several years. Without this charge, operating costs for 2012 Mature Clinics would have been reduced by \$4.7 million. Each component of clinic operating costs is discussed below:

Clinic Operating Costs—Salaries and Related Costs

Salaries and related costs increased to \$141.8 million for 2013 from \$131.6 million for 2012, an increase of \$10.2 million, or 7.8%. Approximately \$7.5 million of the increase was attributable to New Clinics. The remaining \$2.7 million of the increase was due to \$4.4 million in higher costs at various 2012 New Clinics offset by a decrease of \$1.7 million in costs at 2012 Mature Clinics. Salaries and related costs as a percentage of net revenues was 53.7% for 2013 and 52.7% for 2012.

Clinic Operating Costs—Rent, Clinic Supplies and Other

Rent, clinic supplies and other costs increased to \$52.9 million for 2013 from \$50.1 million for 2012, an increase of \$2.8 million, or 5.6%. For 2013, New Clinics accounted for approximately \$2.8 million of the increase and 2012 New Clinics accounted for approximately \$1.6 million of the increase due to a full year of activity for clinics developed or acquired in 2012. Rent, clinic supplies and other costs for 2012 Mature Clinics decreased \$1.6 million in 2013 as compared to 2012 due to cost containment efforts. Included in the rent, clinic supplies and other costs for 2012 Mature Clinics is a pre-tax charge of \$850,000 related to an estimated refund due to a payor for overpayments to a partnership clinic group over several years. Without this charge, rent, clinic supplies and other costs for 2012 Mature Clinics would have decreased by \$2.5 million. Rent, clinic supplies and other costs as a percent of net revenues was 20.0% for 2013 and 20.1% for 2012.

Clinic Operating Costs—Provision for Doubtful Accounts

The provision for doubtful accounts for net patient receivables of \$4.4 million as a percentage of net patient revenues was 1.7% for 2013. The provision for doubtful accounts for net patient receivables of \$4.7 million as a percentage of net patient revenues was 1.9% for 2012. During 2012, we recorded a reserve for a receivable from a management contract of \$0.1 million.

Our provision for doubtful accounts as a percentage of total patient accounts receivable was 4.4% at December 31, 2013 and 5.8% at December 31, 2012. Without the effects of the receivables related to the clinics acquired in December 2013, which are initially recorded at net realizable value, our allowance for bad debts as a percentage of patient accounts receivable was 4.79%. The provision for doubtful accounts at the end of each period is based on a detailed, clinic-by-clinic review of overdue accounts and is regularly reviewed in the aggregate in light of historical experience.

The accounts receivable days outstanding were 39 days at December 31, 2013 and 42 days at December 31, 2012. Net patient receivables in the amount of \$4.4 million and \$4.9 million were written-off in 2013 and 2012, respectively.

Closure Costs

For 2013, closure costs amounted to \$246,000. In 2012, closure costs amounted to \$211,000.

Gross Margin

In 2013, the gross margin increased by \$1.8 million, or 2.8%, as compared to 2012. The gross margin percentage for 2013 was 24.5% as compared to 25.2% for 2012.

Corporate Office Costs

Corporate office costs, consisting primarily of salaries, benefits and equity based compensation of corporate office personnel and directors, rent, insurance costs, depreciation and amortization, travel, legal, compliance, professional, marketing and recruiting fees, were \$25.9 million for 2013 and \$24.5 million for 2012. Corporate office costs as a percentage of net revenues was 9.8% for both 2013 and 2012.

Interest Expense

Interest expense decreased to \$538,000 for 2013 from \$557,000 for 2012 primarily due to lower average borrowings throughout the year. At December 31, 2013, \$40.0 million was outstanding under our revolving credit facility, however, \$36.0 million was drawn on December 13, 2013 resulting in a minimal effect on interest expense and average borrowings for 2013. See "Liquidity and Capital Resources" below for a discussion of the terms of our new revolving credit facility.

Provision for Income Taxes

The provision for income taxes was \$12.2 million for 2013 and \$11.2 million for 2012. For 2013, we accrued state and federal income taxes at an effective tax rate (provision for taxes divided by the difference between income from operations and net income attributable to non-controlling interest) of 41.1%. For 2013, the provision for income taxes for the 2013 period includes an adjustment of \$393,000 related to the true-up of our 2012 tax provision based on a detailed reconciliation of our federal and state taxes payable and receivable accounts along with our federal and state deferred tax asset and liability accounts. The provision for income taxes as a percentage of income before taxes less net income attributable to non-controlling interests is 40% for 2013 and we expect it to be at a comparable tax rate in 2014. In 2012, the income tax provision was reduced by \$350,000 related to a taxable deduction charged to additional-paid-in-capital for the reduction of a subsidiary intercompany loan and included a charge of \$162,000 for a true-up of our 2011 tax provision.

Net Income Attributable to Non-controlling Interests

Net income attributable to non-controlling interests was \$8.5 million in 2013 and \$8.4 million in 2012. As a percentage of operating income before corporate office costs, net income attributable to non-controlling interests was 13.2% in 2013 compared to 13.4% in 2012. The reduction is attributable to the Company's increased ownership interest in certain physical therapy partnerships.

FISCAL YEAR 2012 COMPARED TO FISCAL 2011

- Net revenues rose 7.8 % to \$249.7 million for 2012 from \$231.5 million for 2011 due to increases in net patient revenues offset partially by a \$168,000 decrease in other revenues. The 2012 results includes seven months of operations of the May 2012 Acquisition. The 2011 results include five months of operations of the July 2011 Acquisition.
- Reported net income attributable to common shareholders for 2012 decreased 3.2% to \$18.2 million from \$18.8 million in 2011. Diluted earnings per share were \$1.53 for 2012 and \$1.57 for 2011. Included in the 2011 results is a pretax gain of \$5.4 million related to a purchase price settlement on the

February 2010 Acquisition that occurred beyond our purchase price measurement date. Excluding this 2011 gain, diluted earnings per share from operations would have been \$1.17 for 2011. In comparison to adjusted diluted earnings per share of \$1.17 for 2011, the 2012 diluted earnings per share of \$1.53 represents an increase of 30.7% in 2012 from 2011. See table below (in thousands).

| | Year Ended December 31, | |
|---|----------------------------|-----------------|
| | 2012 | 2011 |
| Net income attributable to common shareholders from continuing operations | \$18,212 | \$18,812 |
| Gain on purchase price settlement of \$5,434 less tax effect of \$629 | — | (4,805) |
| Adjusted net income attributable to common shareholders | <u>\$18,212</u> | <u>\$14,007</u> |
| Adjusted net income attributable to common shareholders per diluted share | \$ 1.53 | \$ 1.17 |

Net Patient Revenues

- Net patient revenues increased to \$244.1 million for 2012 from \$225.8 million for 2011, an increase of \$18.3 million, or 8.1%, primarily due to an increase in patient visits from 2.2 million to 2.3 million. The increase in net patient revenues of \$18.3 million consisted of an increase of \$12.7 million from Mature Clinics and \$5.6 million from New Clinics. The \$12.7 million from Mature Clinics is primarily due to the July 2011 Acquisition. The 2012 results include 12 months of operations of the July 2011 Acquisition and the 2011 results include five months of operations.
- Total patient visits increased to 2,314,000 for 2012 from 2,161,000 for 2011. The growth in patient visits was attributable to 51,000 visits in New Clinics, primarily due to the May 2012 Acquisition, and an increase of 102,000 visits for Mature Clinics, primarily due to the July 2011 Acquisition.

Net patient revenues are based on established billing rates less allowances and discounts for patients covered by contractual programs and workers' compensation. Net patient revenues reflect contractual and other adjustments, which we evaluate monthly, relating to patient discounts from certain payors. Payments received under these programs are based on predetermined rates and are generally less than the established billing rates of the clinics.

Other Revenues

Other revenues decreased by \$168,000 from \$5.7 million to \$5.6 million due to a management contract termination in December 2011.

Clinic Operating Costs

Clinic operating costs were 74.8% of net revenues for 2012 and 75.9% of net revenues for 2011. Each component of clinic operating costs is discussed below:

Clinic Operating Costs—Salaries and Related Costs

Salaries and related costs increased to \$131.6 million for 2012 from \$124.8 million for 2011, an increase of \$6.8 million, or 5.4%. Approximately \$3.7 million of the increase was attributable to New Clinics. The remaining \$3.1 million of the increase was due to \$5.9 million in higher costs at various 2011 New Clinics offset by a decrease of \$2.8 million in costs at 2011 Mature Clinics. Salaries and related costs as a percentage of net revenues was 52.7% for 2012 and 53.9% for 2011.

Clinic Operating Costs—Rent, Clinic Supplies and Other

Rent, clinic supplies and other costs increased to \$50.1 million for 2012 from \$47.0 million for 2011, an increase of \$3.1 million, or 6.6%. For 2012, New Clinics accounted for approximately \$1.7 million of the

increase and 2011 New Clinics accounted for approximately \$4.0 million of the increase due to a full year of activity for clinics developed or acquired in 2011. Rent, clinic supplies and other costs for 2011 Mature Clinics decreased \$2.6 million in 2012 as compared to 2011 due to cost containment efforts. Rent, clinic supplies and other costs as a percent of net revenues was 20.1% for 2012 and 20.3% for 2011.

Clinic Operating Costs—Provision for Doubtful Accounts

The provision for doubtful accounts for net patient receivables of \$4.7 million as a percentage of net patient revenues was 1.9% for 2012. The provision for doubtful accounts for net patient receivables of \$3.8 million was 1.6% for 2011. During 2012, we recorded a reserve for a receivable from a management contract of \$0.1 million.

Our allowance for bad debts as a percentage of total patient accounts receivable was 5.8% at December 31, 2012 and 7.0% at December 31, 2011. The allowance for doubtful accounts at the end of each period is based on a detailed, clinic-by-clinic review of overdue accounts and is regularly reviewed in the aggregate in light of historical experience.

The accounts receivable days outstanding were 42 days at December 31, 2012 and 48 days at December 31, 2011. Net patient receivables in the amount of \$4.9 million and \$3.0 million were written-off in 2012 and 2011, respectively.

Closure Costs

For 2012, closure costs amounted to \$211,000. In 2011, closure costs amounted to \$59,000.

Gross Margin

In 2012, the gross margin increased by \$7.0 million, or 12.6%, as compared to 2011 due to increased visits and net patient revenue per visit. The gross margin percentage for 2012 was 25.2% as compared to 24.1% for 2011.

Corporate Office Costs

Corporate office costs, consisting primarily of salaries, benefits and equity based compensation of corporate office personnel and directors, rent, insurance costs, depreciation and amortization, travel, legal, compliance, professional, marketing and recruiting fees, were \$24.5 million for 2012 and \$24.4 million for 2011. Corporate office costs were reduced as a percentage of net revenues to 9.8% for 2012 from 10.6% for 2011.

Interest and Other Income, net

Interest and other income, net for 2011 included a pretax gain of \$5.4 million related to a purchase price settlement on the February 2010 Acquisition that occurred beyond our purchase price measurement date. The settlement included \$1.5 million in cash, \$0.1 million in debt forgiveness and \$3.8 million in exchange of the remaining non-controlling interest.

Interest Expense

Interest expense increased to \$557,000 for 2012 from \$496,000 for 2011 primarily due to higher average borrowings. At December 31, 2012, \$17.4 million was outstanding under our revolving credit facility. See “Liquidity and Capital Resources” below for a discussion of the terms of our revolving credit facility.

Provision for Income Taxes

The provision for income taxes was \$11.2 million for 2012 and \$9.7 million for 2011. For 2012, we accrued state and federal income taxes at an effective tax rate (provision for taxes divided by the difference between

income from operations and net income attributable to non-controlling interest) of 38.1%. In 2012, the income tax provision was reduced by \$350,000 related to a taxable deduction charged to additional-paid-in-capital for the reduction of a subsidiary intercompany loan and included a charge of \$162,000 for a true-up of our 2011 tax provision based on a detailed reconciliation of our federal and state taxes payable and receivable accounts along with our federal and state deferred tax asset and liability accounts. For 2011, we accrued state and federal income taxes at an effective tax rate (provision for taxes divided by the difference between income from operations and net income attributable to non-controlling interest) of 34.6%. Of the \$5.4 million gain mentioned above, \$3.8 million was non taxable.

Net Income Attributable to Non-controlling Interests

Net income attributable to non-controlling interests was \$8.5 million in 2012 compared to \$7.8 million in 2011. As a percentage of operating income before corporate office costs, net income attributable to non-controlling interests was 13.4% in 2012 compared to 14.1% in 2011. The reduction is attributable to the Company's increased ownership interest in certain physical therapy partnerships.

LIQUIDITY AND CAPITAL RESOURCES

We believe that our business is generating sufficient cash flow from operating activities to allow us to meet our short-term and long-term cash requirements, other than those with respect to future significant acquisitions. At December 31, 2013, we had \$12.9 million in cash and cash equivalents compared to \$11.7 million at December 31, 2012. Although the start-up costs associated with opening new clinics and our planned capital expenditures are significant, we believe that our cash and cash equivalents and availability under our revolving credit facility are sufficient to fund the working capital needs of our operating subsidiaries, future clinic development and single practice acquisitions and investments through at least December 2014. The amount outstanding under our revolving credit facility was \$40.0 million at December 31, 2013 compared to \$17.4 million at December 31, 2012. At December 31, 2013, we had \$85 million available under our revolving credit facility. Significant acquisitions would likely require financing under our revolving credit facility.

The increase in cash and cash equivalents of \$1.2 million from December 31, 2012 to December 31, 2013 was due primarily to \$44.8 million provided by operations, \$22.6 million net proceeds on our revolving line of credit, \$0.7 million from the tax benefit of stock options exercised, \$0.7 million from the sale of business, non-controlling interests and fixed assets. The major uses of cash for investing and financing activities included: purchase of businesses (\$46.6 million), distributions to non-controlling interests (\$9.2 million), payments of cash dividends to our shareholders (\$4.8 million), purchases of fixed assets (\$4.6 million), acquisitions of non-controlling interests (\$1.9 million), and payments on notes payable (\$0.5 million).

Effective December 5, 2013, we entered into an Amended and Restated Credit Agreement with a commitment for a \$125.0 million revolving credit facility with a maturity date of November 30, 2018 ("Credit Agreement"). The Credit Agreement is unsecured and has loan covenants, including requirements that the Company comply with a consolidated fixed charge coverage ratio and consolidated leverage ratio. Proceeds from the Credit Agreement may be used for working capital, acquisitions, purchases of the Company's common stock, dividend payments to the Company's common stockholders, capital expenditures and other corporate purposes. The pricing grid which is based on the Company's consolidated leverage ratio with the applicable spread over LIBOR ranging from 1.5% to 2.5% or the applicable spread over the Base Rate ranging from 0.1% to 1%. Fees under the Credit Agreement include an unused commitment fee ranging from 0.1% to 0.25% depending on the Company's consolidated leverage ratio and the amount of funds outstanding under the Credit Agreement. On December 31, 2013, \$40.0 million was outstanding on the revolving credit facility resulting in \$85.0 million of availability, and we were in compliance with all of the covenants thereunder.

The purchase price for the 72% interest in the February 2013 Acquisition was \$4.3 million in cash and \$400,000 in a seller note, that is payable in two principal installments totaling \$200,000 each, plus accrued interest, in February 2014 and 2015. The purchase price for the 50% interest in the April 2013 Acquisition was

\$2.4 million in cash and \$200,000 in a seller note, that is payable in two principal installments totaling \$100,000 each, plus accrued interest, in April of 2014 and 2015. The purchase price for the 80% interest in the May 2013 Acquisition was \$3.6 million in cash and \$200,000 in a seller note, that is payable in two principal installments totaling \$100,000 each, plus accrued interest, in May of 2014 and 2015. The purchase price for the 60% interest in the December 9, 2013 Acquisition was \$1.7 million in cash. The purchase price for the 90% interest in the December 13, 2013 Acquisition was \$35.5 million in cash and \$500,000 in a seller note, that is payable in two principal installments totaling \$250,000 each, plus accrued interest, in December 2014 and 2015. The aggregate purchase price for the three individual clinics acquired in 2013 was \$238,000. Through 15 separate transactions during 2013, the Company purchased partnership interests in 10 partnerships and sold interests in five partnerships. The interests in the partnerships purchased and sold ranged from less than 1% to 35%. The aggregate of the purchase prices paid, was \$1.9 million and the proceeds for the sales was \$0.8 million, which included cash of \$0.2 million and notes receivable of \$0.6 million.

The purchase price for the 70% interest in the May 2012 Acquisition was \$6,090,000 in cash and \$250,000 in seller notes, that are payable in two principal installments totaling \$125,000 each, plus any accrued interest, in May 2013 and 2014. The seller notes accrue interest at 3.25% per annum. In addition to the May 2012 Acquisition, in 2012, the Company, through its subsidiaries, purchased seven outpatient therapy practices in seven transactions for aggregate cash consideration of \$1,938,000 and, in one transaction a \$100,000 note payable. In addition, in 15 separate transactions during 2012, we purchased partnership interests in 15 partnerships in which we had an existing controlling interest. The interests in the partnerships purchased ranged from 10% to 35%. The aggregate of the purchase prices paid was \$2.2 million, which included \$0.2 million of undistributed earnings. The remaining purchase price of \$2.0 million, less future tax benefits of \$0.8 million, was recognized as an adjustment to additional paid-in capital. During 2012, we sold interests in the range of 0.64% to 1% in three partnerships for an aggregate price of \$239,000. This amount less related undistributed earnings of \$5,000 was credited to additional paid-in capital.

The purchase price for the 51% interest in the July 2011 Acquisition was \$8,426,000, which consisted of \$8,226,000 in cash and a \$200,000 seller note, that is payable in two principal installments totaling \$100,000 each, plus any accrued interest, in July 2012 and 2013. The seller note accrues interest at 3.25% per annum. In addition, in six separate transactions during 2011, we purchased a total of 22.2% of the 30% non-controlling interest in STAR Physical Therapy, LP, a subsidiary of the Company (“STAR”). The aggregate purchase price paid for the 22.2% interest was \$16.9 million, which included \$0.8 million of undistributed earnings. The remaining purchase price of \$16.1 million, less future tax benefits of \$6.3 million, was recognized as an adjustment to additional paid-in capital. After these transactions, we owned 92.2% and the non-controlling interest limited partners in aggregate owned the remaining 7.8% in the partnership.

Effective June 30, 2011, we purchased the 35% non-controlling interest in one of our Texas partnerships. The aggregate purchase price for the 35% interest was \$3.9 million, of which \$3.5 million was paid in cash and \$367,272 was paid in the form of a note to the seller. The purchase price included \$0.2 million of undistributed earnings and \$0.2 million in invested capital. The remaining purchase price of \$3.5 million, less future tax benefits of \$1.4 million, was recognized as an adjustment to additional paid-in capital. After this transaction, we own 100% of the partnership.

In addition, during 2011, we purchased the non-controlling interests of several other partners for \$142,000, which included \$48,000 of undistributed earnings and sold an additional interest to an existing partner for \$58,000. The net purchase price of approximately \$36,000, less future tax benefits of \$23,000, was recognized as an adjustment to additional paid-in capital.

Historically, we have generated sufficient cash from operations to fund our development activities and to cover operational needs. We plan to continue developing new clinics and making additional acquisitions in selected markets. We have from time to time purchased the non-controlling interests of limited partners in our Clinic Partnerships. We may purchase additional non-controlling interests in the future. Generally, any acquisition or purchase of non-controlling interests is expected to be accomplished using a combination of cash and financing. Any large acquisition would likely require financing.

We make reasonable and appropriate efforts to collect accounts receivable, including applicable deductible and co-payment amounts. Claims are submitted to payors daily, weekly or monthly in accordance with our policy or payor's requirements. When possible, we submit our claims electronically. The collection process is time consuming and typically involves the submission of claims to multiple payors whose payment of claims may be dependent upon the payment of another payor. Claims under litigation and vehicular incidents can take a year or longer to collect. Medicare and other payor claims relating to new clinics awaiting Medicare Rehab Agency status approval initially may not be submitted for six months or more. When all reasonable internal collection efforts have been exhausted, accounts are written off prior to sending them to outside collection firms. With managed care, commercial health plans and self-pay payor type receivables, the write-off generally occurs after the account receivable has been outstanding for 120 days or longer.

We have future obligations for debt repayments, employment agreements and future minimum rentals under operating leases. The obligations as of December 31, 2013 are summarized as follows (in thousands):

| Contractual Obligation | Total | 2014 | 2015 | 2016 | 2017 | 2018 | Thereafter |
|-------------------------------|------------------|-----------------|-----------------|-----------------|----------------|-----------------|----------------|
| Credit Agreement and Notes | | | | | | | |
| Payable | \$ 41,475 | \$ 825 | \$ 650 | \$ — | \$ — | \$40,000 | \$ — |
| Interest Payable | \$ 69 | 48 | 21 | — | — | — | — |
| Employee Agreements | \$ 22,636 | 18,148 | 3,748 | 701 | 39 | — | — |
| Operating Leases | \$ 67,622 | 22,563 | 18,263 | 12,761 | 7,859 | 4,274 | 1,902 |
| | <u>\$131,802</u> | <u>\$41,584</u> | <u>\$22,682</u> | <u>\$13,462</u> | <u>\$7,898</u> | <u>\$44,274</u> | <u>\$1,902</u> |

We generally enter into various notes payable as a means of financing our acquisitions. Our present outstanding notes payable relate only to certain of the acquisitions of businesses and non-controlling interests that occurred in 2013 and 2012. For those acquisitions, we entered into several notes payables aggregating \$1.7 million. The notes are payable in equal annual installments of principal over two years plus any accrued and unpaid interest. Interest accrues at various interest rates ranging from 3.25% to 4.0% per annum, subject to adjustment. In addition, we assumed leases with remaining terms of 1 month to 6 years for the operating facilities. At December 31, 2013, the balance on these notes payable was \$1.5 million.

In conjunction with the above mentioned acquisitions, in the event that a limited minority partner's employment ceases at any time after three years from the acquisition date, we have agreed to repurchase that individual's non-controlling interest at a predetermined multiple of earnings before interest and taxes.

As of December 31, 2013, we have accrued \$2.4 million related to credit balances and overpayments due to patients and payors. This amount is expected to be paid in 2014.

The purchase agreement related to an acquisition that occurred in 2008 provided for possible contingent consideration of up to \$3,781,000 based on the achievement of a designated level of operating results within a three-year period following the acquisition. In 2009, 2010 and 2011, we paid \$1,179,000, \$1,080,000 and \$1,522,000, respectively, of additional consideration related to the operating results of such acquired business. Those amounts were recorded as additional goodwill.

From September 2001 through December 31, 2008, the Board authorized us to purchase, in the open market or in privately negotiated transactions, up to 2,250,000 shares of our common stock. In March 2009, the Board authorized the repurchase of up to 10% or approximately 1,200,000 shares of our common stock ("March 2009 Authorization"). In connection with the March 2009 Authorization, we amended our prior credit agreement to permit share repurchases of up to \$15,000,000. We are required to retire shares purchased under the March 2009 Authorization. Under the March 2009 Authorization, we have purchased a total of 859,499 shares. There is no expiration date for the share repurchase program. The Credit Agreement permits the Company to purchase, commencing on October 24, 2012 and at all times thereafter, up to \$15,000,000 of its common stock subject to

compliance with covenants. There are currently an additional estimated 340,501 shares that may be purchased from time to time in the open market or private transactions depending on price, availability and our cash position. We did not purchase any shares of our common stock during 2012 or 2013.

Off Balance Sheet Arrangements

With the exception of operating leases for our executive offices and clinic facilities discussed in Note 14 to our consolidated financial statements included in Item 8, we have no off-balance sheet debt or other off-balance sheet financing arrangements.

FACTORS AFFECTING FUTURE RESULTS

The risks related to our business and operations include:

- changes as the result of government enacted national healthcare reform;
- changes in Medicare guidelines and reimbursement or failure of our clinics to maintain their Medicare certification status;
- business and regulatory conditions including federal and state regulations;
- changes in reimbursement rates or payment methods from third party payors including government agencies and deductibles and co-pays owed by patients;
- revenue and earnings expectations;
- general economic conditions;
- availability and cost of qualified physical therapists;
- personnel productivity;
- competitive, economic or reimbursement conditions in our markets which may require us to reorganize or close certain clinics and thereby incur losses and/or closure costs including the possible write-down or write-off of goodwill and other intangible assets;
- maintaining adequate internal controls;
- availability, terms, and use of capital;
- acquisitions and the successful integration of the operations of the acquired businesses; and
- weather and other seasonal factors.

See Risk Factors in Item 1A of this Annual Report on Form 10-K.

ITEM 7A. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

We do not maintain any derivative instruments such as interest rate swap arrangements, hedging contracts, futures contracts or the like. Our only indebtedness as of December 31, 2013 was seller notes of \$1.5 million and an outstanding balance on our Credit Agreement of \$40.0 million. The outstanding balance under our Credit Agreement is subject to fluctuating interest rates. A 1% change in the interest rate would yield an additional \$400,000 of interest expense. See Note 8 to our consolidated financial statements included in Item 8.

ITEM 8. FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA.

U.S. PHYSICAL THERAPY, INC. AND SUBSIDIARIES

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REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

Board of Directors and Shareholders
U.S. Physical Therapy, Inc.

We have audited the accompanying consolidated balance sheets of U.S Physical Therapy, Inc. (a Nevada Corporation) and subsidiaries (the “Company”) as of December 31, 2013 and 2012, and the related consolidated statements of net income, changes in shareholders’ equity, and cash flows for each of the three years in the period ended December 31, 2013. These financial statements are the responsibility of the Company’s management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of U.S. Physical Therapy, Inc. and subsidiaries as of December 31, 2013 and 2012, and the results of their consolidated operations and their cash flows for each of the three years in the period ended December 31, 2013 in conformity with accounting principles generally accepted in the United States of America.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the Company’s internal control over financial reporting as of December 31, 2013, based on criteria established in the 1992 *Internal Control—Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO), and our report dated March 10, 2014 expressed an unqualified opinion.

/s/ GRANT THORNTON LLP

Houston, Texas
March 11, 2014

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

Board of Directors and Shareholders
U.S. Physical Therapy, Inc.

We have audited the internal control over financial reporting of U.S. Physical Therapy, Inc. (a Nevada Corporation) and subsidiaries (the “Company”) as of December 31, 2013, based on criteria established in the 1992 *Internal Control—Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). The Company’s management is responsible for maintaining effective internal control over financial reporting and for its assessment of the effectiveness of internal control over financial reporting, included in the accompanying Management’s Report appearing under Item 9A on Internal Control over Financial Reporting. Our responsibility is to express an opinion on the Company’s internal control over financial reporting based on our audit. Our audit of, and opinion on, the Company’s internal control over financial reporting does not include the internal control over financial reporting of ARC Rehabilitation Services, LLC, a 90% owned subsidiary, whose financial statements reflect total assets and revenues constituting 1.1% and 0.2%, respectively, of the related consolidated financial statement amounts as of and for the year ended December 31, 2013. As indicated in Management’s Report, ARC Rehabilitation Services, LLC was acquired during 2013. Management’s assertion on the effectiveness of the Company’s internal control over financial reporting excluded internal control over financial reporting of ARC Rehabilitation Services, LLC.

We conducted our audit in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether effective internal control over financial reporting was maintained in all material respects. Our audit included obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, testing and evaluating the design and operating effectiveness of internal control based on the assessed risk, and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion.

A company’s internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company’s internal control over financial reporting includes those policies and procedures that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company’s assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

In our opinion, the Company maintained, in all material respects, effective internal control over financial reporting as of December 31, 2013, based on criteria established in the 1992 *Internal Control—Integrated Framework* issued by COSO.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the consolidated financial statements of the Company as of and for the year ended December 31, 2013, and our report dated March 10, 2014 expressed an unqualified opinion on those financial statements.

/s/ GRANT THORNTON LLP

Houston, Texas
March 11, 2014

U.S. PHYSICAL THERAPY, INC. AND SUBSIDIARIES
CONSOLIDATED BALANCE SHEETS

| | December 31, 2013 | December 31, 2012 |
|--|---------------------------------------|----------------------|
| | (In thousands, except per share data) | |
| ASSETS | | |
| Current assets: | | |
| Cash and cash equivalents | \$ 12,898 | \$ 11,671 |
| Patient accounts receivable, less allowance for doubtful accounts of \$1,430 and \$1,595, respectively | 30,820 | 25,973 |
| Accounts receivable - other, less allowance for doubtful accounts of \$198 and \$514, respectively | 1,844 | 1,703 |
| Other current assets | 4,098 | 5,975 |
| Total current assets | 49,660 | 45,322 |
| Fixed assets: | | |
| Furniture and equipment | 38,965 | 36,316 |
| Leasehold improvements | 21,891 | 20,858 |
| | 60,856 | 57,174 |
| Less accumulated depreciation and amortization | 45,896 | 44,158 |
| | 14,960 | 13,016 |
| Goodwill | 143,955 | 100,188 |
| Other intangible assets, net | 14,479 | 12,146 |
| Other assets | 1,081 | 1,042 |
| | <u>\$224,135</u> | <u>\$171,714</u> |
| LIABILITIES AND SHAREHOLDERS' EQUITY | | |
| Current liabilities: | | |
| Accounts payable - trade | \$ 1,722 | \$ 1,732 |
| Accrued expenses | 20,625 | 14,116 |
| Current portion of notes payable | 825 | 459 |
| Total current liabilities | 23,172 | 16,307 |
| Notes payable | 650 | 175 |
| Revolving line of credit | 40,000 | 17,400 |
| Deferred rent | 996 | 894 |
| Other long-term liabilities | 4,196 | 2,279 |
| Total liabilities | 69,014 | 37,055 |
| Commitments and contingencies | | |
| Redeemable non-controlling interests | 4,104 | — |
| Shareholders' equity: | | |
| U. S. Physical Therapy, Inc. shareholders' equity: | | |
| Preferred stock, \$.01 par value, 500,000 shares authorized, no shares issued and outstanding | — | — |
| Common stock, \$.01 par value, 20,000,000 shares authorized, 14,315,882 and 14,129,651 shares issued, respectively | 143 | 141 |
| Additional paid-in capital | 40,569 | 37,489 |
| Retained earnings | 119,206 | 111,321 |
| Treasury stock at cost, 2,214,737 shares | (31,628) | (31,628) |
| Total U. S. Physical Therapy, Inc. shareholders' equity | 128,290 | 117,323 |
| Noncontrolling interests | 22,727 | 17,336 |
| Total equity | 151,017 | 134,659 |
| | <u>\$224,135</u> | <u>\$171,714</u> |

See notes to consolidated financial statements.

U.S. PHYSICAL THERAPY, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF NET INCOME

| | Year Ended December 31, | | |
|--|---------------------------------------|------------------|------------------|
| | 2013 | 2012 | 2011 |
| | (In thousands, except per share data) | | |
| Net patient revenues | \$258,283 | \$244,100 | \$225,804 |
| Other revenues | 5,775 | 5,551 | 5,719 |
| Net revenues | <u>264,058</u> | <u>249,651</u> | <u>231,523</u> |
| Clinic operating costs: | | | |
| Salaries and related costs | 141,840 | 131,604 | 124,820 |
| Rent, clinic supplies, contract labor and other | 52,887 | 50,102 | 46,998 |
| Provision for doubtful accounts | 4,384 | 4,824 | 3,778 |
| Closure costs | 246 | 211 | 59 |
| Total clinic operating costs | <u>199,357</u> | <u>186,741</u> | <u>175,655</u> |
| Gross margin | <u>64,701</u> | <u>62,910</u> | <u>55,868</u> |
| Corporate office costs | 25,931 | 24,504 | 24,440 |
| Operating income from continuing operations | <u>38,770</u> | <u>38,406</u> | <u>31,428</u> |
| Interest and other income, net | 7 | 6 | 5,445 |
| Interest expense | (538) | (557) | (496) |
| Income before taxes from continuing operations | <u>38,239</u> | <u>37,855</u> | <u>36,377</u> |
| Provision for income taxes | 12,236 | 11,215 | 9,698 |
| Net income from continuing operations including non-controlling interests .. | <u>26,003</u> | <u>26,640</u> | <u>26,679</u> |
| Discontinued operations, net of tax benefit of \$3,180 and \$181 and provision of \$1,399 | (5,007) | (423) | 3,104 |
| Net income including non-controlling interests | <u>20,996</u> | <u>26,217</u> | <u>29,783</u> |
| Less: net income attributable to non-controlling interests | (8,273) | (8,284) | (8,809) |
| Net income attributable to common shareholders | <u>\$ 12,723</u> | <u>\$ 17,933</u> | <u>\$ 20,974</u> |
| Basic earnings per share attributable to common shareholders: | | | |
| From continuing operations | \$ 1.45 | \$ 1.54 | \$ 1.60 |
| From discontinued operations | (0.40) | (0.02) | 0.18 |
| Basic | <u>\$ 1.05</u> | <u>\$ 1.52</u> | <u>\$ 1.78</u> |
| Diluted earnings per share attributable to common shareholders: | | | |
| From continuing operations | \$ 1.45 | \$ 1.53 | \$ 1.57 |
| From discontinued operations | (0.40) | (0.02) | 0.18 |
| Diluted | <u>\$ 1.05</u> | <u>\$ 1.51</u> | <u>\$ 1.75</u> |
| Shares used in computation: | | | |
| Basic | <u>12,063</u> | <u>11,804</u> | <u>11,814</u> |
| Diluted | <u>12,082</u> | <u>11,904</u> | <u>11,977</u> |
| Dividends declared per common share | <u>\$ 0.40</u> | <u>\$ 0.76</u> | <u>\$ 0.32</u> |
| Earnings attributable to common shareholders: | | | |
| From continuing operations | \$ 17,492 | \$ 18,212 | \$ 18,812 |
| From discontinued operations | (4,769) | (279) | 2,162 |
| | <u>\$ 12,723</u> | <u>\$ 17,933</u> | <u>\$ 20,974</u> |

See notes to consolidated financial statements.

U.S. PHYSICAL THERAPY, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF SHAREHOLDERS' EQUITY

| | U. S. Physical Therapy, Inc. | | | | | | | | |
|---|------------------------------|--------------|----------------------------------|----------------------|----------------|-------------------|----------------------------------|-----------------------------|------------------|
| | Common Stock | | Additional Paid-In Capital | Retained Earnings | Treasury Stock | | Total Shareholders' Equity | Noncontrolling Interests | Total |
| | Shares | Amount | | | Shares | Amount | | | |
| | (In thousands) | | | | | | | | |
| Balance December 31, 2010 | 13,893 | \$139 | \$ 45,570 | \$ 89,876 | (2,215) | \$(31,628) | \$103,957 | \$12,426 | \$116,383 |
| Proceeds from exercise of stock options | 139 | — | — | — | — | — | — | — | — |
| Net tax benefit from exercise of stock options | — | — | 217 | — | — | — | 217 | — | 217 |
| Issuance of restricted stock | 160 | — | — | — | — | — | — | — | — |
| Cancellation of restricted stock | (18) | — | — | — | — | — | — | — | — |
| Compensation expense - restricted stock | — | — | 2,032 | — | — | — | 2,032 | — | 2,032 |
| Transfer of compensation liability for certain stock issued pursuant to long-term incentive plans | — | — | 199 | — | — | — | 199 | — | 199 |
| Purchase of business | — | — | — | — | — | — | — | 8,096 | 8,096 |
| Acquisition of noncontrolling interests | — | — | (11,885) | — | — | — | (11,885) | (1,198) | (13,083) |
| Settlement of purchase price | — | — | — | — | — | — | — | (3,835) | (3,835) |
| Purchase and retirement of treasury stock | (255) | — | — | (4,656) | — | — | (4,656) | — | (4,656) |
| Distributions to noncontrolling interest partners | — | — | — | — | — | — | — | (9,767) | (9,767) |
| Cash dividends to shareholders | — | — | — | (3,789) | — | — | (3,789) | — | (3,789) |
| Net income | — | — | — | 20,974 | — | — | 20,974 | 8,809 | 29,783 |
| Balance December 31, 2011 | <u>13,919</u> | <u>\$139</u> | <u>\$ 36,133</u> | <u>\$102,405</u> | <u>(2,215)</u> | <u>\$(31,628)</u> | <u>\$107,049</u> | <u>\$14,531</u> | <u>\$121,580</u> |
| Proceeds from exercise of stock options | 130 | 2 | 20 | — | — | — | 22 | — | 22 |
| Net tax benefit from exercise of stock options | — | — | 1,209 | — | — | — | 1,209 | — | 1,209 |
| Issuance of restricted stock | 81 | — | — | — | — | — | — | — | — |
| Compensation expense - restricted stock | — | — | 2,102 | — | — | — | 2,102 | — | 2,102 |
| Transfer of compensation liability for certain stock issued pursuant to long-term incentive plans | — | — | 135 | — | — | — | 135 | — | 135 |
| Purchase of business | — | — | — | — | — | — | — | 2,892 | 2,892 |
| Acquisitions and sales of noncontrolling interests, net | — | — | (955) | — | — | — | (955) | (244) | (1,199) |
| Contribution of noncontrolling interest partners | — | — | — | — | — | — | — | 49 | 49 |
| Transfer of losses from noncontrolling interests | — | — | (1,155) | — | — | — | (1,155) | 1,155 | — |
| Distributions to noncontrolling interest partners | — | — | — | — | — | — | — | (9,332) | (9,332) |
| Cash dividends to shareholders | — | — | — | (9,017) | — | — | (9,017) | — | (9,017) |
| Net income | — | — | — | 17,933 | — | — | 17,933 | 8,285 | 26,218 |
| Balance December 31, 2012 | <u>14,130</u> | <u>\$141</u> | <u>\$ 37,489</u> | <u>\$111,321</u> | <u>(2,215)</u> | <u>\$(31,628)</u> | <u>\$117,323</u> | <u>\$17,336</u> | <u>\$134,659</u> |
| Proceeds from exercise of stock options | 17 | 2 | 45 | — | — | — | 47 | — | 47 |
| Net tax benefit from exercise of stock options | — | — | 695 | — | — | — | 695 | — | 695 |
| Issuance of restricted stock | 175 | — | — | — | — | — | — | — | — |
| Cancellation of restricted stock | (6) | — | — | — | — | — | — | — | — |
| Compensation expense - restricted stock | — | — | 2,743 | — | — | — | 2,743 | — | 2,743 |
| Transfer of compensation liability for certain stock issued pursuant to long-term incentive plans | — | — | 248 | — | — | — | 248 | — | 248 |
| Purchase of business | — | — | — | — | — | — | — | 10,541 | 10,541 |
| Acquisitions and sales of noncontrolling interests, net | — | — | (651) | — | — | — | (651) | (155) | (806) |
| Reclass to redeemable non-controlling interests | — | — | — | — | — | — | — | (4,104) | (4,104) |
| Distributions to noncontrolling interest partners | — | — | — | — | — | — | — | (9,164) | (9,164) |
| Cash dividends to shareholders | — | — | — | (4,838) | — | — | (4,838) | — | (4,838) |
| Net income | — | — | — | 12,723 | — | — | 12,723 | 8,273 | 20,996 |
| Balance December 31, 2013 | <u>14,316</u> | <u>\$143</u> | <u>\$ 40,569</u> | <u>\$119,206</u> | <u>(2,215)</u> | <u>\$(31,628)</u> | <u>\$128,290</u> | <u>\$22,727</u> | <u>\$151,017</u> |

See notes to consolidated financial statements.

U.S. PHYSICAL THERAPY, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CASH FLOWS

| | Year Ended December 31, | | |
|--|-------------------------|------------------|-----------------|
| | 2013 | 2012 | 2011 |
| | (In thousands) | | |
| OPERATING ACTIVITIES | | | |
| Net income including noncontrolling interests | \$ 20,996 | \$ 26,218 | \$ 29,783 |
| Adjustments to reconcile net income including noncontrolling interests to net cash provided by operating activities: | | | |
| Depreciation and amortization | 5,562 | 5,287 | 5,449 |
| Provision for doubtful accounts | 4,384 | 4,848 | 3,785 |
| Gain on purchase price settlement | — | — | (5,435) |
| Equity-based awards compensation expense | 2,743 | 2,102 | 2,032 |
| Loss (gain) on sale of business and fixed assets | 7,335 | 175 | 182 |
| Excess tax benefit from exercise of stock options | (695) | (1,351) | (217) |
| Deferred income tax | 2,369 | 3,738 | 3,833 |
| Other | — | — | 437 |
| Changes in operating assets and liabilities: | | | |
| Increase in patient accounts receivable | (5,389) | (1,663) | (5,147) |
| Increase in accounts receivable - other | (5) | (561) | (990) |
| (Increase) decrease in other assets | 1,803 | (585) | (1,972) |
| (Decrease) increase in accounts payable and accrued expenses | 4,833 | (340) | 1,190 |
| (Decrease) increase in other liabilities | 859 | 1,381 | (275) |
| Net cash provided by operating activities | 44,795 | 39,249 | 32,655 |
| INVESTING ACTIVITIES | | | |
| Purchase of fixed assets | (4,637) | (4,234) | (3,222) |
| Purchase of businesses, net of cash acquired | (46,628) | (7,929) | (9,451) |
| Acquisitions of noncontrolling interests | (1,876) | (2,244) | (20,439) |
| Sale of noncontrolling interests | 233 | 239 | — |
| Settlement of purchase price | — | — | 1,500 |
| Proceeds on sale of business and fixed assets, net | 459 | 64 | 6 |
| Net cash used in investing activities | (52,449) | (14,104) | (31,606) |
| FINANCING ACTIVITIES | | | |
| Distributions to noncontrolling interests | (9,164) | (9,332) | (9,767) |
| Cash dividends to shareholders | (4,838) | (9,017) | (3,789) |
| Purchase and retire of common stock | — | — | (4,656) |
| Proceeds from revolving line of credit | 150,800 | 79,900 | 118,900 |
| Payments on revolving line of credit | (128,200) | (86,000) | (100,900) |
| Payment of notes payable | (459) | (434) | (250) |
| Tax benefit from stock options exercised | 695 | 1,351 | 217 |
| Other | 47 | 75 | — |
| Net cash provided by (used in) financing activities | 8,881 | (23,457) | (245) |
| Net increase in cash and cash equivalents | 1,227 | 1,688 | 804 |
| Cash and cash equivalents - beginning of period | 11,671 | 9,983 | 9,179 |
| Cash and cash equivalents - end of period | <u>\$ 12,898</u> | <u>\$ 11,671</u> | <u>\$ 9,983</u> |
| SUPPLEMENTAL DISCLOSURES OF CASH FLOW INFORMATION | | | |
| Cash paid during the period for: | | | |
| Income taxes | \$ 4,111 | \$ 6,361 | \$ 9,037 |
| Interest | \$ 352 | \$ 639 | \$ 325 |
| Non-cash investing and financing transactions during the period: | | | |
| Purchase of business - seller financing portion | \$ 1,300 | \$ 350 | \$ 200 |
| Acquisition of noncontrolling interest - seller financing portion | \$ — | \$ — | \$ 367 |

See notes to consolidated financial statements.

U.S. PHYSICAL THERAPY, INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
DECEMBER 31, 2013

1. Organization, Nature of Operations and Basis of Presentation

U.S. Physical Therapy, Inc. and its subsidiaries (together, the “Company”) operate outpatient physical therapy clinics that provide pre-and post-operative care and treatment for orthopedic-related disorders, sports-related injuries, preventative care, rehabilitation of injured workers and neurological-related injuries. As of December 31, 2013 the Company owned and operated 472 clinics in 43 states. The clinics’ business primarily originates from physician referrals. The principal sources of payment for the clinics’ services are managed care programs, commercial health insurance, Medicare/Medicaid, workers’ compensation insurance and proceeds from personal injury cases. In addition to the Company’s ownership of outpatient physical therapy clinics, it also manages physical therapy facilities for third parties, primarily physicians, with 18 such third-party facilities under management as of December 31, 2013.

The consolidated financial statements include the accounts of U.S. Physical Therapy, Inc. and its subsidiaries. All significant intercompany transactions and balances have been eliminated. The Company primarily operates through subsidiary clinic partnerships, in which the Company generally owns a 1% general partnership interest and a 64% limited partnership interest. The managing therapist of each clinic owns the remaining limited partnership interest in the majority of the clinics (hereinafter referred to as “Clinic Partnership”). To a lesser extent, the Company operates some clinics through wholly-owned subsidiaries under profit sharing arrangements with therapists (hereinafter referred to as “Wholly-Owned Facilities”).

During the last three years, the Company completed the following multi-clinic acquisitions:

| <u>Acquisition</u> | <u>Date</u> | <u>% Interest Acquired</u> | <u>Number of Clinics</u> |
|-------------------------------|-------------|--------------------------------|------------------------------|
| | <u>2013</u> | | |
| February 2013 Acquisition | February 28 | 72% | 9 |
| April 2013 Acquisition | April 30 | 50% | 5 |
| May 2013 Acquisition | May 24 | 80% | 5 |
| December 9, 2013 Acquisition | December 9 | 60% | 12 |
| December 13, 2013 Acquisition | December 13 | 90% | 11 |
| | <u>2012</u> | | |
| May 2012 Acquisition | May 22 | 70% | 7 |
| | <u>2011</u> | | |
| July 2011 Acquisition | July 25 | 51% | 20 |

In addition to the five multi-clinic acquisitions detailed above, in 2013, the Company acquired three individual clinics in separate transactions. In addition to the May 2012 Acquisition, in 2012, the Company acquired seven individual clinics in separate transactions. Two of the acquired clinic practices operate in two separate partnerships and the remaining five operate as satellites of existing partnerships.

Clinic Partnerships

For Clinic Partnerships, the earnings and liabilities attributable to the non-controlling interest, typically owned by the managing therapist, directly or indirectly, are recorded within the statements of net income and balance sheets as non-controlling interests.

Wholly-Owned Facilities

For Wholly-Owned Facilities with profit sharing arrangements, an appropriate accrual is recorded for the amount of profit sharing due the clinic partners/directors. The amount is expensed as compensation and included in clinic operating costs—salaries and related costs. The respective liability is included in current liabilities—accrued expenses on the balance sheet.

2. Significant Accounting Policies

Cash Equivalents

The Company maintains its cash and cash equivalents at financial institutions. The combined account balances at several institutions typically exceed Federal Deposit Insurance Corporation (“FDIC”) insurance coverage and, as a result, there is a concentration of credit risk related to amounts on deposit in excess of FDIC insurance coverage. Management believes that this risk is not significant.

Long-Lived Assets

Fixed assets are stated at cost. Depreciation is computed on the straight-line method over the estimated useful lives of the related assets. Estimated useful lives for furniture and equipment range from three to eight years and for software purchased from three to seven years. Leasehold improvements are amortized over the shorter of the related lease term or estimated useful lives of the assets, which is generally three to five years.

Impairment of Long-Lived Assets and Long-Lived Assets to Be Disposed Of

The Company reviews property and equipment and intangible assets with finite lives for impairment upon the occurrence of certain events or circumstances that indicate the related amounts may be impaired. Assets to be disposed of are reported at the lower of the carrying amount or fair value less costs to sell.

Goodwill

Goodwill represents the excess of the amount paid and fair value of the non-controlling interests over the fair value of the acquired business assets, which include certain intangible assets. Historically, goodwill has been derived from acquisitions and, prior to 2009, from the purchase of some or all of a particular local management’s equity interest in an existing clinic. Effective January 1, 2009, if the purchase price of a non-controlling interest by the Company exceeds or is less than the book value at the time of purchase, any excess or shortfall is recognized as an adjustment to additional paid-in capital.

The fair value of goodwill and other intangible assets with indefinite lives are tested for impairment annually and upon the occurrence of certain events, and are written down to fair value if considered impaired. The Company evaluates goodwill for impairment on at least an annual basis (in its third quarter) by comparing the fair value of its reporting units to the carrying value of each reporting unit including related goodwill. The Company operates a one segment business which is made up of various clinics within partnerships. The partnerships are components of regions and are aggregated to the operating segment level for the purpose of determining the Company’s reporting units when performing its annual goodwill impairment test.

An impairment loss generally would be recognized when the carrying amount of the net assets of a reporting unit, inclusive of goodwill and other intangible assets, exceeds the estimated fair value of the reporting unit. The estimated fair value of a reporting unit is determined using two factors: (i) earnings prior to taxes, depreciation and amortization for the reporting unit multiplied by a price/earnings ratio used in the industry and (ii) a discounted cash flow analysis. A weight is assigned to each factor and the sum of each weight times the factor is considered the estimated fair value. For 2013, the factors (i.e., price/earnings ratio, discount rate and residual capitalization rate) were updated to reflect current market conditions. The evaluation of goodwill in 2013, 2012 and 2011 did not result in any goodwill amounts that were deemed impaired.

The Company has not identified any triggering events occurring after the testing date that would impact the impairment testing results obtained. Factors which could result in future impairment charges include but are not limited to:

- changes as the result of government enacted national healthcare reform;
- changes in Medicare guidelines and reimbursement or failure of our clinics to maintain their Medicare certification status;
- business and regulatory conditions including federal and state regulations;
- changes in reimbursement rates or payment methods from third party payors including government agencies and deductibles and co-pays owed by patients;
- revenue and earnings expectations;
- general economic conditions;
- availability and cost of qualified physical and occupational therapists;
- personnel productivity;
- competitive, economic or reimbursement conditions in our markets which may require us to reorganize or close certain operations and thereby incur losses and/or closure costs including the possible write-down or write-off of goodwill and other intangible assets;
- maintaining adequate internal controls;
- availability, terms, and use of capital;
- acquisitions, purchase of non-controlling interests (minority interests) and the successful integration of the operations of the acquired businesses; and
- weather and other seasonal factors.

The Company will continue to monitor for any triggering events or other indicators of impairment.

Non-controlling Interests

The Company recognizes non-controlling interests as equity in the consolidated financial statements separate from the parent entity's equity. The amount of net income attributable to non-controlling interests is included in consolidated net income on the face of the income statement. Changes in a parent entity's ownership interest in a subsidiary that do not result in deconsolidation are treated as equity transactions if the parent entity retains its controlling financial interest. The Company recognizes a gain or loss in net income when a subsidiary is deconsolidated. Such gain or loss is measured using the fair value of the non-controlling equity investment on the deconsolidation date.

When the purchase price of a non-controlling interest by the Company exceeds the book value at the time of purchase, any excess or shortfall is recognized as an adjustment to additional paid-in capital. Additionally, operating losses are allocated to non-controlling interests even when such allocation creates a deficit balance for the non-controlling interest partner.

The non-controlling interests that are reflected as redeemable non-controlling interests in the consolidated financial statements consist of those outside owners that have certain put rights that are currently exercisable, and that, if exercised, require that the Company purchases the non-controlling interest of the particular limited partner. The redeemable non-controlling interests reflect the book value of the respective non-controlling interests. The redeemable non-controlling interests will be adjusted to the fair value in the reporting period in which the Company deems it probable that the limited partner will assert the put rights. Typically, for

acquisitions, the Company agrees to purchase the individual's non-controlling interest at a predetermined multiple of earnings before interest and taxes. As of December 31, 2012, there were no non-controlling interests with put rights that were exercisable.

Revenue Recognition

Revenues are recognized in the period in which services are rendered. Net patient revenues (patient revenues less estimated contractual adjustments) are reported at the estimated net realizable amounts from third-party payors, patients and others for services rendered. The Company has agreements with third-party payors that provide for payments to the Company at amounts different from its established rates. The allowance for estimated contractual adjustments is based on terms of payor contracts and historical collection and write-off experience.

The Company determines allowances for doubtful accounts based on the specific agings and payor classifications at each clinic. The provision for doubtful accounts is included in clinic operating costs in the statement of net income. Net accounts receivable, which are stated at the historical carrying amount net of contractual allowances, write-offs and allowance for doubtful accounts, includes only those amounts the Company estimates to be collectible.

Medicare Reimbursement

The Medicare program reimburses outpatient rehabilitation providers based on the Medicare Physician Fee Schedule ("MPFS"). The MPFS rates are automatically updated annually based on a formula, called the sustainable growth rate ("SGR") formula. The use of the SGR formula would have resulted in calculated automatic reductions in rates in every year since 2002; however, for each year through March 31, 2014, Centers for Medicare & Medicaid Services ("CMS") or Congress has taken action to prevent the implementation of SGR formula reductions. The Bipartisan Budget Act of 2013 froze the Medicare physician fee schedule rates at 2013 levels through March 31, 2014, averting a scheduled 20.1% cut in the MPFS as a result of the SGR formula that would have taken effect on January 1, 2014. Unless Congress again takes legislative action to prevent the SGR formula reductions from going into effect automatic reductions in the MPFS will commence on April 1, 2014.

The Budget Control Act of 2011 increased the federal debt ceiling in connection with deficit reductions over the next ten years, and requires automatic reductions in federal spending by approximately \$1.2 trillion. Payments to Medicare providers are subject to these automatic spending reductions, subject to a 2% cap. On April 1, 2013, a 2% reduction to Medicare payments was implemented.

As a result of the Balanced Budget Act of 1997, the formula for determining the total amount paid by Medicare in any one year for outpatient physical therapy, occupational therapy, and/or speech-language pathology services provided to any Medicare beneficiary (*i.e.*, the "Therapy Cap" or "Limit") was established. Based on the statutory definitions which constrained how the Therapy Cap would be applied, there is one Limit for Physical Therapy and Speech Language Pathology Services combined, and one Limit for Occupational Therapy. During 2013, the annual Limit on outpatient therapy services was \$1,900 for Physical Therapy and Speech Language Pathology Services combined and \$1,900 for Occupational Therapy Services. Effective January 1, 2014, the annual Limit on outpatient therapy services is \$1,920 for Physical and Speech Language Pathology Services combined and \$1,920 for Occupational Therapy Services. Historically, these Therapy Caps applied to outpatient therapy services provided in all settings, except for services provided in departments of hospitals. However, the American Taxpayer Relief Act of 2012 and the Bipartisan Budget Act of 2013 extended the annual limits on therapy expenses to services furnished in hospital outpatient department settings through March 31, 2014. Unless Congress enacts legislation to extend the application of these limits to therapy provided in hospital outpatient settings, the Therapy Caps will no longer apply to such services starting as of April 1, 2014.

In the Deficit Reduction Act of 2005, Congress implemented an exceptions process to the annual Limit for therapy expenses for therapy services above the annual Limit. The Bipartisan Budget Act of 2013 extended the exceptions process for outpatient Therapy Caps through March 31, 2014. Therapy services above the annual Limit that are medically necessary satisfy an exception to the annual Limit and such claims are payable by the Medicare program. Unless Congress extends the exceptions process, the Therapy Caps will apply to all claims regardless of medical necessity beginning April 1, 2014. For any claim above the annual Limit, the claim must contain a modifier indicating that the services are medically necessary and justified by appropriate documentation in the medical record.

Furthermore, under the Middle Class Tax Relief and Job Creation Act of 2012 (“MCTRA”), since October 1, 2012, patients who met or exceeded \$3,700 in therapy expenditures during a calendar year have been subject to a manual medical review to determine whether applicable payment criteria are satisfied. The \$3,700 threshold is applied to Physical Therapy and Speech Language Pathology Services; a separate \$3,700 threshold is applied to the Occupational Therapy. The Bipartisan Budget Relief Act of 2013 extended through March 31, 2014 the requirement that Medicare perform manual medical review of therapy services beyond the \$3,700 threshold. In addition, as of January 1, 2013, CMS implemented a claims based data collection strategy that is designed to assist in reforming the Medicare payment system for outpatient therapy. Since January 1, 2013, all therapy claims must include additional codes and modifiers providing information about the beneficiary’s functional status at the outset of the therapy episode of care, specified points during treatment, and at the time of discharge. Effective July 1, 2013, claims submitted without the appropriate codes and modifiers are returned unpaid.

CMS adopted a multiple procedure payment reduction (“MPPR”) for therapy services in the final update to the MPFS for calendar year 2011. During 2011, the MPPR applied to all outpatient therapy services paid under Medicare Part B — occupational therapy, physical therapy and speech-language pathology. Under the policy, the Medicare program pays 100% of the practice expense component of the Relative Value Unit (“RVU”) for the therapy procedure with the highest practice expense RVU, then reduces the payment for the practice expense component for the second and subsequent therapy procedures or units of service furnished during the same day for the same patient, regardless of whether those therapy services are furnished in separate sessions. In 2011 and 2012, the practice expense component for the second and subsequent therapy service furnished during the same day for the same patient was reduced by 20% in office and other non-institutional settings and by 25% in institutional settings. The American Taxpayer Relief Act of 2012 increased the payment reduction of the practice expense component to 50%, on subsequent therapy procedures in either setting, effective April 1, 2013. In addition, the Middle Class Tax Relief and Job Creation Act of 2012 (“MCTRA”) directed CMS to implement a claims-based data collection program to gather additional data on patient function during the course of therapy in order to better understand patient conditions and outcomes. All practice settings that provide outpatient therapy services are required to include this data on the claim form. Since July 1, 2013, therapists have been required to report new codes and modifiers on the claim form that reflect a patient’s functional limitations and goals at initial evaluation, periodically throughout care, and at discharge. Since July 1, 2013, CMS has rejected claims if the required data is not included in the claim.

The Physician Quality Reporting System, or “PQRS,” is a CMS reporting program that uses a combination of incentive payments and payment reductions to promote reporting of quality information by “eligible professionals.” Although physical therapists, occupational therapists and qualified speech-language therapists are generally able to participate in the PQRS program, therapy professionals for whose services we bill through our rehab agencies cannot participate because the Medicare claims processing systems currently cannot accommodate institutional providers such as rehab agencies. Eligible professionals, such as those of our therapy professionals for whose services we bill using their individual Medicare provider numbers, who do not satisfactorily report data on quality measures will be subject to a 2% reduction in their Medicare payment in 2016.

Statutes, regulations, and payment rules governing the delivery of therapy services to Medicare beneficiaries are complex and subject to interpretation. The Company believes that it is in substantial compliance in all material respects with all applicable laws and regulations and is not aware of any pending or threatened

investigations involving allegations of potential wrongdoing that would have a material effect on the Company's financial statements as of December 31, 2013. Compliance with such laws and regulations can be subject to future government review and interpretation, as well as significant regulatory action including fines, penalties, and exclusion from the Medicare program.

Management Contract Revenues

Management contract revenues are derived from contractual arrangements whereby the Company manages a clinic for third party owners. The Company does not have any ownership interest in these clinics. Typically, revenues are determined based on the number of visits conducted at the clinic and recognized when services are performed. Costs, typically salaries for the Company's employees, are recorded when incurred. Management contract revenues are included in "other revenues" in the accompanying Consolidated Statements of Net Income.

Contractual Allowances

Contractual allowances result from the differences between the rates charged for services performed and expected reimbursements by both insurance companies and government sponsored healthcare programs for such services. Medicare regulations and the various third party payors and managed care contracts are often complex and may include multiple reimbursement mechanisms payable for the services provided in Company clinics. The Company estimates contractual allowances based on its interpretation of the applicable regulations, payor contracts and historical calculations. Each month the Company estimates its contractual allowance for each clinic based on payor contracts and the historical collection experience of the clinic and applies an appropriate contractual allowance reserve percentage to the gross accounts receivable balances for each payor of the clinic. Based on the Company's historical experience, calculating the contractual allowance reserve percentage at the payor level is sufficient to allow the Company to provide the necessary detail and accuracy with its collectibility estimates. However, the services authorized and provided and related reimbursement are subject to interpretation that could result in payments that differ from the Company's estimates. Payor terms are periodically revised necessitating continual review and assessment of the estimates made by management. The Company's billing system does not capture the exact change in its contractual allowance reserve estimate from period to period in order to assess the accuracy of its revenues and hence its contractual allowance reserves. Management regularly compares its cash collections to corresponding net revenues measured both in the aggregate and on a clinic-by-clinic basis. In the aggregate, historically the difference between net revenues and corresponding cash collections has generally reflected a difference within approximately 1% of net revenues. Additionally, analysis of subsequent period's contractual write-offs on a payor basis reflects a difference within approximately 1% between the actual aggregate contractual reserve percentage as compared to the estimated contractual allowance reserve percentage associated with the same period end balance. As a result, the Company believes that a change in the contractual allowance reserve estimate would not likely be more than 1% at December 31, 2013.

Income Taxes

Income taxes are accounted for under the asset and liability method. Deferred tax assets and liabilities are recognized for the future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases and operating loss and tax credit carryforwards. 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 effect on deferred tax assets and liabilities of a change in tax rates is recognized in income in the period that includes the enactment date.

The Company recognizes the financial statement benefit of a tax position only after determining that the relevant tax authority would more likely than not sustain the position following an audit. For tax positions meeting the more-likely-than-not threshold, the amount to be recognized in the financial statements is the largest benefit that has a greater than 50 percent likelihood of being realized upon ultimate settlement with the relevant tax authority.

The Company did not have any accrued interest or penalties associated with any unrecognized tax benefits nor was any interest expense recognized during the twelve months ended December 31, 2013 and 2012. The Company will book any interest or penalties, if required, in interest and/or other income/expense as appropriate.

Fair Values of Financial Instruments

The carrying amounts reported in the balance sheet for cash and cash equivalents, accounts receivable, accounts payable and notes payable approximate their fair values due to the short-term maturity of these financial instruments. The carrying amount of the revolving credit facility approximates its fair value. The interest rate on the Credit Agreement, which is tied to the Eurodollar Rate, is set at various short-term intervals, as detailed in the credit agreement.

Segment Reporting

Operating segments are components of an enterprise for which separate financial information is available that is evaluated regularly by chief operating decision makers in deciding how to allocate resources and in assessing performance. The Company identifies operating segments based on management responsibility and believes it meets the criteria for aggregating its operating segments into a single reporting segment.

Use of Estimates

In preparing the Company's consolidated financial statements, management makes certain estimates and assumptions, especially in relation to, but not limited to, goodwill impairment, allowance for receivables, tax provision and contractual allowances, that affect the amounts reported in the consolidated financial statements and related disclosures. Actual results may differ from these estimates.

Self-Insurance Program

The Company utilizes a self insurance plan for its employee group health insurance coverage administered by a third party. Predetermined loss limits have been arranged with the insurance company to minimize the Company's maximum liability and cash outlay. Accrued expenses include the estimated incurred but unreported costs to settle unpaid claims and estimated future claims. Management believes that the current accrued amounts are sufficient to pay claims arising from self insurance claims incurred through December 31, 2013.

Stock Options

The Company measures and recognizes compensation expense for all stock-based payments at fair value. Compensation cost recognized includes compensation for all stock-based payments granted prior to, but not yet vested on January 1, 2006, based on the grant-date fair value estimated at the time of grant and compensation cost for the stock-based payments granted subsequent to January 1, 2006, based on the grant-date fair value. There was no stock option compensation in the years ended December 31, 2013, 2012 and 2011. No stock options were granted during the years ended December 31, 2013, 2012 and 2011. As of December 31, 2013, there were no non vested stock options.

Restricted Stock

Restricted stock issued to employees and directors is subject to continued employment or continued service on the board, respectively. Typically, the transfer restrictions for shares granted to employees lapse in equal installments on the following four or five annual anniversaries of the date of grant. Compensation expense for grants of restricted stock is recognized based on the fair value per share on the date of grant amortized over the vesting period. The restricted stock issued is included in basic and diluted shares for the earnings per share computation.

Reclassifications

Reclassification has been made to prior period amounts to conform to the current period presentation of the physician services business, which was sold in 2013, as discontinued operations.

Subsequent Event

The Company has evaluated events occurring after the balance sheet date for possible disclosure as a subsequent event through the date that these financial statements were issued.

3. Acquisitions of Businesses and Non-controlling Interests

Acquisition of Businesses

During 2013, 2012 and 2011, the Company completed the following multi-clinic acquisitions of physical therapy practices:

| <u>Acquisition</u> | <u>Date</u> | <u>% Interest Acquired</u> | <u>Number of Clinics</u> |
|-------------------------------|-------------|----------------------------|--------------------------|
| | <u>2013</u> | | |
| February 2013 Acquisition | February 28 | 72% | 9 |
| April 2013 Acquisition | April 30 | 50% | 5 |
| May 2013 Acquisition | May 24 | 80% | 5 |
| December 9, 2013 Acquisition | December 9 | 60% | 12 |
| December 13, 2013 Acquisition | December 13 | 90% | 11 |
| | <u>2012</u> | | |
| May 2012 Acquisition | May 22 | 70% | 7 |
| | <u>2011</u> | | |
| July 2011 Acquisition | July 25 | 51% | 20 |

In addition to the five multi-clinic acquisitions detailed above, in 2013, the Company acquired three individual clinics in separate transactions. In addition to the May 2012 Acquisition, in 2012, the Company acquired seven individual clinic in separate transactions. Two of the acquired clinic practices operate in two separate partnerships and the remaining five operate as satellites of existing partnerships.

The purchase price for the 72% interest in the February 2013 Acquisition was \$4.3 million in cash and \$400,000 in a seller note, that is payable in two principal installments totaling \$200,000 each, plus accrued interest, in February 2014 and 2015. The purchase price for the 50% interest in the April 2013 Acquisition was \$2.4 million in cash and \$200,000 in a seller note, that is payable in two principal installments totaling \$100,000 each, plus accrued interest, in April of 2014 and 2015. The purchase price for the 80% interest in the May 2013 Acquisition was \$3.6 million in cash and \$200,000 in a seller note, that is payable in two principal installments totaling \$100,000 each, plus accrued interest, in May of 2014 and 2015. The purchase price for the 60% interest in the December 9, 2013 Acquisition was \$1.7 million in cash.

The purchase price for the 90% interest in the December 13, 2013 Acquisition was \$35.5 million in cash and \$500,000 in a seller note, that is payable in two principal installments totaling \$250,000 each, plus accrued interest, in December 2014 and 2015. On December 13, 2013, U.S. Physical Therapy, Ltd. (“USPT Ltd.” and “Purchaser”), a wholly-owned subsidiary of the Company, entered into a Reorganization and Purchase Agreement (the “Purchase Agreement”) with ARC Rehabilitation Services, LLC, Athletic & Rehabilitation Center, LLC, Matthew J. Condon and Kevin O’Rourke (collectively referred to as “Sellers”). Prior to, and in

connection with the transaction contemplated by the Purchase Agreement, the Sellers and Purchaser, formed or caused to be formed ARC Physical Therapy Plus, Limited Partnership, a Texas limited partnership (“ARC PT”) and ARC PT Management GP, LLC, a Texas limited liability company (“ARC GP”). ARC GP, which owns a 1% interest in ARC PT, is the sole general partner of ARC PT. ARC PT owns and operates 11 outpatient physical and occupational therapy clinics and has three on site industrial client locations it serves. As a result of the closing under the Purchase Agreement, USPT Ltd. owns 89% of the limited partnership interests of ARC PT and 100% of the membership interests in ARC GP (the “Acquired Interests”). The business acquired complements the Company’s business since it focuses on developing programs for traditional physical and occupational therapy, work hardening, corporate wellness, as well as pre and post offer employment testing and functional capacity testing. The results of operations are included in the consolidated results of the Company since December 13, 2013 which includes \$505,000 of net revenues and \$119,000 of earnings from the December 13, 2013 Acquisition.

Unaudited proforma net revenue and net income from continuing operations for the Company as if the December 13, 2013 Acquisition occurred as of January 1, 2012 is as follows (in thousands, except per share data):

| | For the Year Ended December 31, | |
|---|---------------------------------|-----------|
| | 2013 | 2012 |
| Net revenues | \$275,511 | \$261,231 |
| Net income attributable to common shareholders from continuing operations | \$ 19,231 | \$ 19,894 |
| Earnings per share: | | |
| Basic - net income attributable to common shareholders from continuing operations | \$ 1.60 | \$ 1.69 |
| Diluted - net income attributable to common shareholders from continuing operations | \$ 1.59 | \$ 1.67 |
| Shares used in computation: | | |
| Basic - net income attributable to common shareholders from continuing operations | 12,050 | 11,804 |
| Diluted - net income attributable to common shareholders from continuing operations | 12,069 | 11,904 |

The aggregate purchase price for the three clinic practices acquired in 2013 was \$238,000.

The purchase prices for the acquisitions in 2013 have been preliminarily allocated as follows (in thousands):

| | |
|---|------------------|
| Cash paid, net of cash acquired | \$ 46,628 |
| Seller notes | 1,300 |
| Total consideration | <u>\$ 47,928</u> |
| Estimated fair value of net tangible assets acquired: | |
| Total current assets | \$ 3,895 |
| Total non-current assets | 2,283 |
| Total liabilities | <u>(1,082)</u> |
| Net tangible assets acquired | \$ 5,096 |
| Referral relationships | 400 |
| Non compete | 160 |
| Tradename | 600 |
| Goodwill | 52,213 |
| Fair value of noncontrolling interest | <u>(10,541)</u> |
| | <u>\$ 47,928</u> |

The purchase price for the 70% interest in the May 2012 Acquisition was \$6,090,000 in cash and \$250,000 in seller notes, that are payable in two principal installments totaling \$125,000 each, plus any accrued interest, in May 2013 and 2014. The seller notes accrue interest at 3.25% per annum. For the Company, 70% of the goodwill for the May 2012 Acquisition is tax deductible. In addition to the above multi-clinic acquisitions, in 2012, the Company, through its subsidiaries, purchased seven outpatient therapy practices in seven transactions for aggregate cash consideration of \$1,938,000 and, in one transaction, a \$100,000 note payable. For the Company, approximately 67% of the goodwill for the acquisitions in 2012 is tax deductible.

The purchase prices for the acquisitions in 2012 were allocated as follows (in thousands):

| | |
|---|-----------------|
| Cash paid, net of cash acquired | \$ 7,929 |
| Seller notes | 350 |
| Total consideration | <u>\$ 8,279</u> |
| Estimated fair value of net tangible assets acquired: | |
| Total current assets | \$ 410 |
| Total non-current assets | 525 |
| Total liabilities | <u>(333)</u> |
| Net tangible assets acquired | \$ 602 |
| Referral relationships | 857 |
| Non compete | 265 |
| Tradename | 1,300 |
| Goodwill | 8,147 |
| Fair value of noncontrolling interest | <u>(2,892)</u> |
| | <u>\$ 8,279</u> |

The purchase price for the 51% interest in the July 2011 Acquisition was \$8,426,000, which consisted of \$8,226,000 in cash and a \$200,000 seller note, that is payable in two principal installments totaling \$100,000 each, plus any accrued interest, in July 2012 and 2013. The seller note accrues interest at 3.25% per annum. For the Company 51% of the goodwill for the July 2011 Acquisition is tax deductible.

The purchase price for the July 2011 Acquisition was allocated as follows (in thousands):

| | |
|---|-----------------|
| Cash paid, net of cash acquired | \$ 7,930 |
| Seller notes | 200 |
| Total consideration | <u>\$ 8,130</u> |
| Estimated fair value of net tangible assets acquired: | |
| Total current assets | \$ 1,341 |
| Total non-current assets | 902 |
| Total liabilities | <u>(581)</u> |
| Net tangible assets acquired | \$ 1,662 |
| Tradename | 1,900 |
| Referral relationships | 1,100 |
| Non compete | 300 |
| Goodwill | 11,263 |
| Fair value of noncontrolling interest | <u>(8,095)</u> |
| | <u>\$ 8,130</u> |

The purchase prices plus the fair value of the non-controlling interests for the February 2013 Acquisition and the acquisitions in 2012 and 2011 were allocated to the fair value of the assets acquired, inclusive of

identifiable intangible assets, i.e. tradenames, referral relationships and non compete agreements, and liabilities assumed based on the fair values at the acquisition date, with the amount exceeding the fair values being recorded as goodwill. For the remaining acquisitions in 2013, the purchase prices plus the fair value of the non-controlling interests were allocated to the fair value of the assets acquired, exclusive of identifiable intangible assets and liabilities assumed based on the preliminary estimates of the fair values at the acquisition date, with the amount exceeding the estimated fair values being recorded as goodwill.

For the remaining acquisitions in 2013, the Company is in the process of completing its formal valuation analysis to identify and determine the fair value of tangible and intangible assets acquired and the liabilities assumed. Thus, the final allocation of the purchase price may differ from the preliminary estimates used at December 31, 2013 based on additional information obtained and completion of the valuation of the identifiable intangible assets. Changes in the estimated valuation of the tangible assets acquired, the completion of the valuation of identifiable intangible assets and the completion by the Company of the identification of any unrecorded pre-acquisition contingencies, where the liability is probable and the amount can be reasonably estimated, will likely result in adjustments to goodwill.

For the February 2013 Acquisition and for the acquisitions in 2012 and 2011, the values assigned to the referral relationships and non compete agreements are being amortized to expense equally over the respective estimated lives. For referral relationships, the range of the estimated lives was 12 to 13 years, and for non compete agreements the estimated lives was six years. The values assigned to goodwill and tradenames are tested annually for impairment.

In April 2012, the Company sold 1% of its interest in the July 2011 Acquisition to the limited partners. The Company now owns a 50% interest in the July 2011 Acquisition, 1% as a general partner and 49% as a limited partner.

For the 2013, 2012 and 2011 acquisitions, total current assets primarily represent primarily patient accounts receivable. Total non current assets are fixed assets, primarily equipment, used in the practices.

The consideration paid for each of the acquisitions was derived through arm's length negotiations. Funding for the cash portions was derived from proceeds from the Company's previous revolving credit facility. The results of operations of the acquisitions have been included in the Company's consolidated financial statements since their respective date of acquisition. Unaudited proforma consolidated financial information for the acquisitions in 2013, with the exception of the December 13, 2013 Acquisition, 2012 and 2011 acquisitions have not been included as the results, individually and in the aggregate, were not material to current operations.

In November 2011, the Company and the seller of an acquisition in 2010 reached an agreement regarding an adjustment to purchase price. The Company received \$1.5 million cash, the forgiveness of the balance of \$0.1 million on the notes payable as well as the 30% partnership interest originally held by the seller which had a book value of \$3.8 million.

Acquisitions of Non-controlling Interests

In 15 separate transactions during 2013, the Company purchased partnership interests in 10 partnerships and sold interests in five partnerships . The interests in the partnerships purchased and sold ranged from less than 1% to 35%. The aggregate of the purchase prices paid, was \$1.9 million and the proceeds for the sales was \$0.8 million, which included cash of \$0.2 million and notes receivable of \$0.6 million. The purchase prices paid included a net of \$0.1 million of undistributed earnings. The remaining \$1.0 million, less future tax benefits of \$0.4 million, was recognized as an adjustment to additional paid-in capital.

In 15 separate transactions during 2012, the Company purchased partnership interests in 15 partnerships. The interests in the partnerships purchased ranged from 10% to 35%. The aggregate of the purchase prices paid

was \$2.2 million, which included \$0.2 million of undistributed earnings. The remaining purchase price of \$2.0 million, less future tax benefits of \$0.8 million, was recognized as an adjustment to additional paid-in capital. During 2012, the Company sold interests in the range of 0.64% to 1% in three partnerships for an aggregate price of \$239,000. This amount less related undistributed earnings of \$5,000 was credited to additional paid-in capital.

In six separate transactions during 2011, the Company purchased a total of 22.2% of the 30% non-controlling interest in STAR Physical Therapy, LP, a subsidiary of the Company (“STAR”). The aggregate purchase price paid for the 22.2% interest was \$16.9 million, which included \$0.8 million of undistributed earnings. The remaining purchase price of \$16.1 million, less future tax benefits of \$6.3 million, was recognized as an adjustment to additional paid-in capital. After these transactions, the Company owned 92.2% and the non-controlling interest limited partners in aggregate owned the remaining 7.8% in the partnership. Of the 22.2% aggregate non-controlling interests purchased, 17% was held by Regg Swanson, the Managing Director and a founder of STAR and a member of the Company’s Board of Directors (“Swanson”). The purchase prices were determined based on the contractual terms in the Reorganization of Securities Purchase Agreement dated as of September 6, 2007 among the Company, STAR, the limited partners of STAR and Regg Swanson as Seller Representative and in his individual capacity, which was filed as Exhibit 10.1 to the Company’s Current Report on Form 8-K filed with the SEC on September 7, 2007. After the sale of his 17.0% interest, Swanson owned 2.0% of STAR (“Swanson Interest”).

Effective June 30, 2011, the Company purchased the 35% non-controlling interest in one of its Texas partnerships. The aggregate purchase price for the 35% interest was \$3.9 million, of which \$3.5 million was paid in cash and \$367,272 was paid in the form of a note to the seller, which is payable in two equal annual installments of principal plus any accrued and unpaid interest. Interest accrues at 3.25% per annum. The purchase price included \$0.2 million of undistributed earnings and \$0.2 million in invested capital. The remaining purchase price of \$3.5 million, less future tax benefits of \$1.4 million, was recognized as an adjustment to additional paid-in capital. After this transaction, the Company owns 100% of the partnership.

In addition, during 2011, the Company purchased the non-controlling interests of several other partners for \$142,000, which included \$48,000 of undistributed earnings and sold additional interest to an existing partner for \$58,000. The net purchase price of approximately \$36,000, less future tax benefits of \$23,000, was recognized as an adjustment to additional paid-in capital.

The results of operations of the acquired non-controlling interests are included in the accompanying financial statements from the dates of purchase in the net income attributable to common shareholders.

4. Divestiture of Business

On September 30, 2013, the Company sold the remainder of its physician services business. Previously, the Company closed its two physician services facilities – one in August 2013 and the other in December 2012. As previously disclosed in the Company’s public filings, the physician services business incurred negative gross margins in 2012 and through the first nine months of 2013. Revenues from physician services were generated by patient visits, franchise arrangements and fees from third parties. The results of operations and the loss on the sale of the physician services business have been reclassified to discontinued operations for all periods presented.

The Company received \$400,000 cash and a note receivable of \$500,000. The sale less the write-off of assets, primarily of goodwill and other intangible assets, and recording of appropriate accruals resulted in an after-tax loss of \$4.4 million.

The following table details the losses, including the operating results, from discontinued operations reported for the physician services business (in thousands):

| | For the Year Ended December 31, | | |
|---|---------------------------------|-----------------|-----------------|
| | 2013 | 2012 | 2011 |
| Net revenues | \$ 864 | \$2,435 | \$ 5,483 |
| Operating costs | 1,537 | 2,761 | 702 |
| Gross margin | (673) | (326) | 4,781 |
| Direct general and administrative expenses less proceeds .. | 1,176 | 278 | 278 |
| Write off of goodwill and other intangible assets | 6,338 | — | — |
| | (8,187) | (604) | 4,503 |
| Tax benefit (provision) | 3,180 | 181 | (1,399) |
| (Loss) income from discontinued operations | <u>\$ (5,007)</u> | <u>\$ (423)</u> | <u>\$ 3,104</u> |

The cash flow impact of the sale and closures is deemed immaterial for the consolidated statements of cash flows. The reclassifications on the consolidated balance sheet as of December 31, 2012 are also deemed immaterial.

5. Goodwill

The changes in the carrying amount of goodwill as of December 31, 2013 and 2012 consisted of the following (in thousands):

| | Year Ended December 31 | |
|--|---------------------------|------------------|
| | 2013 | 2012 |
| Beginning balance | \$100,188 | \$ 92,750 |
| Goodwill acquired during the year | 52,213 | 10,538 |
| Goodwill allocated to specific assets for businesses acquired in 2011 | — | (3,300) |
| Goodwill allocated to specific assets for businesses acquired in 2012 | (2,340) | — |
| Goodwill adjustments for purchase price allocation of businesses acquired | (48) | 200 |
| Goodwill written off - sale of physician services business | (6,058) | — |
| Ending balance | <u>\$143,955</u> | <u>\$100,188</u> |

6. Intangible Assets, net

Intangible assets, net as of December 31, 2013 and 2012 consisted of the following (in thousands):

| | December 31, | |
|---|-----------------|-----------------|
| | 2013 | 2012 |
| Tradenames | \$ 9,814 | \$ 7,973 |
| Referral relationships, net of accumulated amortization of \$1,582 and \$1,217, respectively | 3,959 | 3,501 |
| Non compete agreements, net of accumulated amortization of \$1,950 and \$1,848, respectively | 706 | 672 |
| | <u>\$14,479</u> | <u>\$12,146</u> |

Tradenames, referral relationships and non compete agreements are related to the businesses acquired. The value assigned to tradenames has an indefinite life and is tested at least annually for impairment using the relief from royalty method in conjunction with the Company's annual goodwill impairment test. The value assigned to referral relationships is being amortized over their respective estimated useful lives which range from six to 16 years. Non compete agreements are amortized over the respective term of the agreements which range from five to six years.

The following table details the amount of amortization expense recorded for intangible assets for the years ended December 31, 2013, 2012 and 2011 (in thousands):

| | Year Ended December 31, | | |
|------------------------|-------------------------|--------------|--------------|
| | 2013 | 2012 | 2011 |
| Referral relationships | \$521 | \$433 | \$305 |
| Non compete agreements | 372 | 405 | 390 |
| | <u>\$893</u> | <u>\$838</u> | <u>\$695</u> |

During 2013, in conjunction with the sale of the physician services business, the Company wrote-off the referral relationships and non compete agreements related to this business which included accumulated amortization of \$156,000 and \$270,000, respectively.

The remaining balance of referral relationships and non compete agreements is expected to be amortized as follows (in thousands):

| Referral Relationships | | Non Compete Agreements | |
|------------------------|---------------|------------------------|---------------|
| Years | Annual Amount | Years | Annual Amount |
| 2014 | 461 | 2014 | 207 |
| 2015 | 440 | 2015 | 207 |
| 2016 | 440 | 2016 | 144 |
| 2017 | 440 | 2017 | 100 |
| 2018 | 404 | 2018 | 43 |
| 2019 | 367 | 2019 | 4 |
| 2020 | 367 | | |
| 2021 | 367 | | |
| 2022 | 318 | | |
| 2023 | 211 | | |
| 2024 | 108 | | |
| 2025 | 31 | | |
| 2026 | 5 | | |

7. Accrued Expenses

Accrued expenses as of December 31, 2013 and 2012 consisted of the following (in thousands):

| | 2013 | 2012 |
|---|-----------------|-----------------|
| Salaries and related costs | \$11,686 | \$ 8,941 |
| Group health insurance claims | 2,023 | 991 |
| Credit balances and overpayments due to patients and payors | 2,371 | 1,513 |
| Other | 4,545 | 2,671 |
| Total | <u>\$20,625</u> | <u>\$14,116</u> |

8. Notes Payable

Notes payable as of December 31, 2013 and 2012 consisted of the following (dollars in thousands):

| | <u>2013</u> | <u>2012</u> |
|---|-----------------|-----------------|
| Credit Agreement average effective interest rate of 2.9% inclusive of unused fee | \$40,000 | \$17,400 |
| Various notes payable with \$825 plus accrued interest due in the next year interest accrues at 3.25% per annum | <u>1,475</u> | <u>634</u> |
| | 41,475 | 18,034 |
| Less current portion | <u>(825)</u> | <u>(459)</u> |
| | <u>\$40,650</u> | <u>\$17,575</u> |

Effective December 5, 2013, the Company entered into an Amended and Restated Credit Agreement with a commitment for a \$125.0 million revolving credit facility with a maturity date of November 30, 2018 (“Credit Agreement”). The Credit Agreement is unsecured and has loan covenants, including requirements that the Company comply with a consolidated fixed charge coverage ratio and consolidated leverage ratio. Proceeds from the Credit Agreement may be used for working capital, acquisitions, purchases of the Company’s common stock, dividend payments to the Company’s common stockholders, capital expenditures and other corporate purposes. The pricing grid is based on the Company’s consolidated leverage ratio with the applicable spread over LIBOR ranging from 1.5% to 2.5% or the applicable spread over the Base Rate ranging from 0.1% to 1%. Fees under the Credit Agreement include an unused commitment fee ranging from 0.1% to 0.25% depending on the Company’s consolidated leverage ratio and the amount of funds outstanding under the Credit Agreement.

On December 31, 2013, \$40.0 million was outstanding on the Credit Agreement resulting in \$85.0 million of availability. As of December 30, 2013, the Company was in compliance with all of the covenants thereunder.

The Company generally enters into various notes payable as a means of financing a portion of its acquisitions and purchases of non-controlling interests. In conjunction with the acquisitions in 2013, the Company entered into notes payable in the aggregate amount of \$1.3 million, each payable in two equal annual installments totaling \$650,000 plus any accrued and unpaid interest. Interest accrues at 3.25% per annum, subject to adjustment. In conjunction with the acquisitions in 2012, the Company entered into notes payable in the aggregate amount of \$350,000, each payable in two equal annual installments totaling \$175,000 plus any accrued and unpaid interest. Interest accrues at 3.25% per annum. In conjunction with the July 2011 Acquisition, the Company entered into a note payable in the amount of \$200,000 payable in two equal annual installments of \$100,000 plus any accrued and unpaid interest. Interest accrues at 3.25% per annum. In June 2011, the Company, in conjunction with the purchase of a non-controlling interest, entered into a note payable in the amount of \$367,272 payable in two equal annual installments of \$183,636 plus any accrued and unpaid interest. Interest accrued at 3.25% per annum.

Aggregate annual payments of principal required pursuant to the Credit Agreement and the above notes payable subsequent to December 31, 2013 are as follows (in thousands):

| | |
|--|-----------------|
| During the twelve months ended December 30, 2014 | \$ 825 |
| During the twelve months ended December 30, 2015 | 650 |
| During the twelve months ended December 30, 2018 | <u>40,000</u> |
| | <u>\$41,475</u> |

9. Income Taxes

Significant components of deferred tax assets included in the consolidated balance sheets at December 31, 2013 and 2012 were as follows (in thousands):

| | <u>2013</u> | <u>2012</u> |
|---|-------------------------|-------------------------|
| Deferred tax assets: | | |
| Compensation | \$ 1,280 | \$ 1,059 |
| Allowance for doubtful accounts | 449 | 607 |
| Lease obligations - closed clinics | 77 | 39 |
| Other | — | 22 |
| Deferred tax assets | <u>\$ 1,806</u> | <u>\$ 1,727</u> |
| Deferred tax liabilities: | | |
| Depreciation and amortization | \$(4,237) | \$(2,166) |
| Other | (546) | (575) |
| Deferred tax liabilities | <u>(4,783)</u> | <u>(2,741)</u> |
| Net deferred tax assets (liabilities) | <u><u>\$(2,977)</u></u> | <u><u>\$(1,014)</u></u> |
| Amount included in: | | |
| Other current assets | \$ 482 | \$ 590 |
| Long term liabilities | \$(3,459) | \$(1,604) |

During 2013 and 2012, the Company recorded deferred tax assets of \$0.4 million and \$0.8 million, respectively, related to acquisitions of non-controlling interests. At December 31, 2013 and 2012, the Company had a tax receivable of \$2.2 million and \$4.2 million, respectively, included in other current assets on the accompanying consolidated balance sheets.

The differences between the federal tax rate and the Company's effective tax rate for results of continuing operations for the years ended December 31, 2013, 2012 and 2011 were as follows (in thousands):

| | <u>2013</u> | | <u>2012</u> | | <u>2011</u> | |
|--|------------------------|---------------------|------------------------|---------------------|------------------------|---------------------|
| U. S. tax at statutory rate | \$10,415 | 35.0% | \$10,299 | 35.0% | \$ 9,979 | 35.0% |
| State income taxes, net of federal benefit | 1,814 | 6.1% | 1,219 | 4.2% | 963 | 3.4% |
| Deductible losses | (98) | -0.3% | (404) | -1.4% | — | 0.0% |
| Nontaxable gain | — | | — | | (1,342) | -4.7% |
| Nondeductible expenses | 105 | 0.3% | 101 | 0.3% | 98 | 0.3% |
| | <u><u>\$12,236</u></u> | <u><u>41.1%</u></u> | <u><u>\$11,215</u></u> | <u><u>38.1%</u></u> | <u><u>\$ 9,698</u></u> | <u><u>34.0%</u></u> |

Significant components of the provision for income taxes for continuing operations for the years ended December 31, 2013, 2012 and 2011 were as follows (in thousands):

| | <u>2013</u> | <u>2012</u> | <u>2011</u> |
|--|------------------------|------------------------|-----------------------|
| Current: | | | |
| Federal | \$ 8,445 | \$ 7,117 | \$6,376 |
| State | 1,422 | 360 | (511) |
| Total current | <u>9,867</u> | <u>7,477</u> | <u>5,865</u> |
| Deferred: | | | |
| Federal | 1,970 | 3,183 | 3,603 |
| State | 399 | 555 | 230 |
| Total deferred | <u>2,369</u> | <u>3,738</u> | <u>3,833</u> |
| Total income tax provision for continuing operations | <u><u>\$12,236</u></u> | <u><u>\$11,215</u></u> | <u><u>\$9,698</u></u> |

For 2012, 2011 and 2010, the Company performed a detailed reconciliation of its federal and state taxes payable and receivable accounts along with its federal and state deferred tax asset and liability accounts. As a result of this detailed analysis, the Company recorded an increase in the 2013 state income tax provision of \$393,000, for the 2012 reconciliation, and \$162,000 additional provision in 2012 for the 2011 reconciliation. No adjustment was necessary for the 2010 reconciliation. The Company considers this reconciliation process to be an annual control.

The Company is required to establish a valuation allowance for deferred tax assets if, based on the weight of available evidence, it is more likely than not that some portion or all of the deferred tax assets will not be realized. The ultimate realization of deferred tax assets is dependent upon the generation of future taxable income during the periods in which those temporary differences become deductible. Management considers the projected future taxable income and tax planning strategies in making this assessment. Based upon the level of historical taxable income and projections for future taxable income in the periods which the deferred tax assets are deductible, management believes that a valuation allowance is not required, as it is more likely than not that the results of future operations will generate sufficient taxable income to realize the deferred tax assets.

The Company's U.S. federal returns remain open to examination for 2010 through 2012 and U.S. state jurisdictions are open for periods ranging from 2009 through 2012.

The Company does not believe that it has any significant uncertain tax positions at December 31, 2013, nor is this expected to change within the next twelve months due to the settlement and expiration of statutes of limitation.

The Company did not have any accrued interest or penalties associated with any unrecognized tax benefits nor was any interest expense recognized during the years ended December 31, 2013, 2012 and 2011.

10. Equity Based Plans

The Company has the following equity based plans with outstanding equity grants:

The Amended and Restated 1999 Employee Stock Option Plan (the "Amended 1999 Plan") permits the Company to grant to non-employee directors and employees of the Company up to 600,000 non-qualified options to purchase shares of common stock and restricted stock (subject to proportionate adjustments in the event of stock dividends, splits, and similar corporate transactions). The exercise prices of options granted under the Amended 1999 Plan are determined by the Compensation Committee. The period within which each option will be exercisable is determined by the Compensation Committee. The Amended 1999 Plan was approved by the shareholders of the Company at the 2008 Shareholders Meeting on May 20, 2008.

The Amended and Restated 2003 Stock Option Plan (the "Amended 2003 Plan") permits the Company to grant to key employees and outside directors of the Company incentive and non-qualified options and shares of restricted stock covering up to 1,750,000 shares of common stock (subject to proportionate adjustments in the event of stock dividends, splits, and similar corporate transactions). The Amended 2003 Plan was approved by the shareholders of the Company at the 2013 Shareholders Meeting on May 14, 2013.

A cumulative summary of equity plans as of December 31, 2013 follows:

| Equity Plans | Authorized | Restricted Stock Issued | Outstanding Stock Options | Stock Options Exercised | Stock Options Exercisable | Shares Available for Grant |
|-----------------------------|------------------|-------------------------|---------------------------|-------------------------|---------------------------|----------------------------|
| Amended 1999 Plan | 600,000 | 360,900 | 8,700 | 131,091 | 8,700 | 99,309 |
| Amended 2003 Plan | 1,750,000 | 422,663 | 30,000 | 748,300 | 30,000 | 549,037 |
| | <u>2,350,000</u> | <u>783,563</u> | <u>38,700</u> | <u>879,391</u> | <u>38,700</u> | <u>648,346</u> |

A summary of the status of the Company's stock options granted under the plans as of December 31, 2013, 2012 and 2011 and the changes during the years then ended is presented below:

| | Number of Shares | Weighted Average Exercise Price | Weighted Average Remaining Contractual Term | Aggregate Intrinsic Value (000's) |
|--|---------------------|--|---|--|
| Outstanding at December 31, 2010 | 723,890 | 14.30 | 3.6 Years | |
| Granted | — | — | | |
| Exercised | (375,080) | 13.92 | | |
| Cancelled | — | — | | |
| Forfeited | — | — | | |
| Outstanding at December 31, 2011 | 348,810 | 14.30 | 2.6 Years | |
| Granted | — | — | | |
| Exercised | (272,750) | 14.12 | | |
| Cancelled | (220) | 17.89 | | |
| Forfeited | — | — | | |
| Outstanding at December 31, 2012 | 75,840 | 14.71 | 2.2 Years | |
| Granted | — | — | | |
| Exercised | (37,140) | 15.25 | | |
| Cancelled | — | — | | |
| Forfeited | — | — | | |
| Outstanding at December 31, 2013 | 38,700 | 18.36 | 1.6 Years | |
| Exercisable at December 31, 2013 | 38,700 | — | 1.6 Years | \$654 |

All shares pursuant to stock options were fully vested at December 31, 2013 and 2012.

A summary of the intrinsic value of stock options exercised during the years ended December 31, 2013, 2012 and 2011 is as follows:

| | Number of Shares | Aggregate Intrinsic Value (000') |
|------------|---------------------|---|
| 2011 | 375,080 | \$3,160 |
| 2012 | 272,750 | \$3,459 |
| 2013 | 37,140 | \$ 402 |

The following tables summarize information about the Company's stock options outstanding as of December 31, 2013, 2012 and 2011, respectively:

| | Outstanding Options as of December 31, 2013 | Exercise Price | Weighted Average Remaining Contractual Life | Exercisable | Exercise Price |
|-----------------|---|-------------------|---|---------------|-------------------|
| 1999 Plan | 8,700 | \$12.60 - \$18.42 | 1.6 Years | 8,700 | \$12.60 - \$18.42 |
| 2003 Plan | <u>30,000</u> | \$18.42 | 1.6 Years | <u>30,000</u> | \$18.42 |
| | <u>38,700</u> | \$12.60 - \$18.42 | 1.6 Years | <u>38,700</u> | \$12.60 - \$18.42 |

| | Outstanding Options as of December 31, 2012 | Exercise Price | Weighted Average Remaining Contractual Life | Exercisable | Exercise Price |
|-----------------|---|-------------------|---|---------------|-------------------|
| 1999 Plan | 15,840 | \$12.60 - \$18.42 | 2.2 Years | 15,840 | \$12.60 - \$18.42 |
| 2003 Plan | <u>60,000</u> | \$12.51 - \$18.80 | 2.2 Years | <u>60,000</u> | \$12.51 - \$18.80 |
| | <u>75,840</u> | \$12.51 - \$18.80 | 2.2 Years | <u>75,840</u> | \$12.51 - \$18.80 |

| | Outstanding Options as of December 31, 2011 | Exercise Price | Weighted Average Remaining Contractual Life | Exercisable | Exercise Price |
|-------------------|---|-------------------|---|----------------|-------------------|
| 1999 Plan | 17,310 | \$12.60 - \$18.42 | 3.2 Years | 17,310 | \$12.60 - \$18.42 |
| 2003 Plan | 251,500 | \$12.51 - \$18.80 | 2.9 Years | 251,500 | \$12.51 - \$18.80 |
| Inducements | <u>80,000</u> | \$12.75 - \$14.32 | 1.7 Years | <u>80,000</u> | \$12.75 - \$14.32 |
| | <u>348,810</u> | \$12.51 - \$18.80 | 2.6 Years | <u>348,810</u> | \$12.51 - \$18.80 |

During 2003, the Board of Directors of the Company granted inducement options ("Inducements") to five individuals in connection with their offers of employment. In 2012, the remaining options were exercised.

The following table summarizes information about the Company's stock options outstanding and those options that are exercisable as of December 31, 2013:

| Exercise Prices | Outstanding Options | Exercisable Options |
|-----------------|------------------------|------------------------|
| \$12.60 | 400 | 400 |
| \$18.42 | <u>38,300</u> | <u>38,300</u> |
| | <u>38,700</u> | <u>38,700</u> |

During 2013, 2012 and 2011, the Company granted the following shares (net of those shares cancelled in their respective grant year due to employee terminations prior to restrictions lapsing) of restricted stock to directors, officers and employees pursuant to its equity plans as follows:

| <u>Year Granted</u> | <u>Number of Shares</u> | <u>Weighted Average Fair Value Per Share</u> |
|-------------------------|-----------------------------|--|
| 2011 | 156,750 | \$19.94 |
| 2012 | 80,650 | \$21.65 |
| 2013 | 174,938 | \$23.52 |

Generally, restrictions on the stock granted to employees lapse in equal annual installments on the following four or five anniversaries of the date of grant. For those shares granted to directors, the restrictions will lapse in equal quarterly installments during the first year after the date of grant. For those granted to executive officers, the restriction will lapse in equal quarterly installments during the three to four years following the date of grant.

As of December 31, 2013, there were 244,018 shares outstanding for which restrictions had not lapsed. The restrictions will lapse in 2014 through 2017.

Compensation expense for grants of restricted stock will be recognized based on the fair value on the date of grant. Compensation expense for restricted stock grants was \$2,743,000, \$2,102,000 and \$2,032,000, respectively, for 2013, 2012 and 2011. As of December 31, 2013, the remaining \$4.2 million of compensation expense will be recognized from 2014 through 2017.

11. Preferred Stock

The Board is empowered, without approval of the shareholders, to cause shares of preferred stock to be issued in one or more series and to establish the number of shares to be included in each such series and the rights, powers, preferences and limitations of each series. There are no provisions in the Company's Articles of Incorporation specifying the vote required by the holders of preferred stock to take action. All such provisions would be set out in the designation of any series of preferred stock established by the Board. The bylaws of the Company specify that, when a quorum is present at any meeting, the vote of the holders of at least a majority of the outstanding shares entitled to vote who are present, in person or by proxy, shall decide any question brought before the meeting, unless a different vote is required by law or the Company's Articles of Incorporation. Because the Board has the power to establish the preferences and rights of each series, it may afford the holders of any series of preferred stock, preferences, powers, and rights, voting or otherwise, senior to the right of holders of common stock. The issuance of the preferred stock could have the effect of delaying or preventing a change in control of the Company.

12. Common Stock

From September 2001 through December 31, 2008, the Board authorized the Company to purchase, in the open market or in privately negotiated transactions, up to 2,250,000 shares of the Company's common stock. In March 2009, the Board authorized the repurchase of up to 10% or approximately 1,200,000 shares of its common stock ("March 2009 Authorization"). In connection with the March 2009 Authorization, the Company amended the Credit Agreement to permit share repurchases of up to \$15,000,000. The Company is required to retire shares purchased under the March 2009 Authorization.

Under the March 2009 Authorization, the Company has purchased a total of 859,499 shares. There is no expiration date for the share repurchase program. The Credit Agreement was further amended to permit the Company to purchase, commencing on October 24, 2012 and at all times thereafter, up to \$15,000,000 of its common stock subject to compliance with covenants. There are currently an additional estimated 340,501 shares

that may be purchased from time to time in the open market or private transactions depending on price, availability and the Company's cash position. The Company did not purchase any shares of its common stock during 2012 or 2013.

13. Defined Contribution Plan

The Company has a 401(k) profit sharing plan covering all employees with three months of service. The Company may make discretionary contributions of up to 50% of employee contributions. The Company did not make any discretionary contributions and recognized no contribution expense for the years ended December 31, 2013, 2012 and 2011.

14. Commitments and Contingencies

Operating Leases

The Company has entered into operating leases for its executive offices and clinic facilities. In connection with these agreements, the Company incurred rent expense of \$22.0 million, \$20.8 million and \$19.4 million for the years ended December 31, 2013, 2012 and 2011, respectively. Several of the leases provide for an annual increase in the rental payment based upon the Consumer Price Index. The majority of the leases provide for renewal periods ranging from one to five years. The agreements to extend the leases specify that rental rates would be adjusted to market rates as of each renewal date.

The future minimum operating lease commitments for each of the next five years and thereafter and in the aggregate as of December 31, 2013 are as follows (in thousands):

| | |
|------------------|-----------------|
| 2014 | \$22,563 |
| 2015 | 18,263 |
| 2016 | 12,761 |
| 2017 | 7,859 |
| 2018 | 4,274 |
| Thereafter | <u>1,902</u> |
| | <u>\$67,622</u> |

Employment Agreements

At December 31, 2013, the Company had outstanding employment agreements with three of its executive officers. These agreements, which presently expire on December 31, 2015, provide for automatic one year renewals if not terminated on at least 12 month notice. All of the agreements contain a provision for annual adjustment of salaries.

In addition, the Company has outstanding employment agreements with most of the managing physical therapist partners of the Company's physical therapy clinics and with certain other clinic employees which obligate subsidiaries of the Company to pay compensation of \$18.1 million in 2014 and \$4.5 million in the aggregate from 2015 through 2018. In addition, most of the employment agreements with the managing physical therapists provide for monthly bonus payments calculated as a percentage of each clinic's net revenues (not in excess of operating profits) or operating profits.

15. Earnings Per Share

The computations of basic and diluted earnings per share for the years ended December 31, 2013, 2012 and 2011 are as follows (in thousands, except per share data):

| | <u>2013</u> | <u>2012</u> | <u>2011</u> |
|---|-----------------|-----------------|-----------------|
| Earnings attributable to common shareholders: | | | |
| From continuing operations | \$17,492 | \$18,212 | \$18,812 |
| From discontinued operations | <u>(4,769)</u> | <u>(279)</u> | <u>2,162</u> |
| | <u>\$12,723</u> | <u>\$17,933</u> | <u>\$20,974</u> |
| Basic earnings per share attributable to common shareholders: | | | |
| From continuing operations | \$ 1.45 | \$ 1.54 | \$ 1.60 |
| From discontinued operations | <u>(0.40)</u> | <u>(0.02)</u> | <u>0.18</u> |
| Basic | <u>\$ 1.05</u> | <u>\$ 1.52</u> | <u>\$ 1.78</u> |
| Diluted earnings per share attributable to common shareholders: | | | |
| From continuing operations | \$ 1.45 | \$ 1.53 | \$ 1.57 |
| From discontinued operations | <u>(0.40)</u> | <u>(0.02)</u> | <u>0.18</u> |
| Diluted | <u>\$ 1.05</u> | <u>\$ 1.51</u> | <u>\$ 1.75</u> |
| Shares used in computation: | | | |
| Basic earnings per share - weighted-average shares | 12,063 | 11,804 | 11,814 |
| Effect of dilutive securities - Stock options | <u>19</u> | <u>100</u> | <u>163</u> |
| Denominator for diluted earnings per share - adjusted weighted-average shares | <u>12,082</u> | <u>11,904</u> | <u>11,977</u> |

All options to purchase shares for the year ended December 31, 2013, 2012 and 2011 were included in the diluted earnings per share calculation as the average market price for those years exceeded the options' exercise price.

16. Selected Quarterly Financial Data (Unaudited)

| | 2013 | | | |
|---|---------------------------------------|----------------|----------------|----------------|
| | Q1 | Q2 | Q3 | Q4 |
| | (In thousands, except per share data) | | | |
| Net patient revenues from continuing operations | \$61,432 | \$65,227 | \$64,368 | \$67,256 |
| Net revenues from continuing operations | \$62,756 | \$66,868 | \$65,829 | \$68,605 |
| Operating income from continuing operations | \$ 8,435 | \$11,059 | \$ 9,904 | \$ 9,372 |
| Net income from continuing operations including noncontrolling interests | \$ 5,809 | \$ 7,642 | \$ 6,756 | \$ 5,796 |
| Net income from continuing operations attributable to common shareholders | \$ 3,851 | \$ 5,079 | \$ 4,659 | \$ 3,903 |
| Net losses from discontinued operations attributable to common shareholders | \$ (130) | \$ (165) | \$ (4,432) | \$ (42) |
| Net income attributable to common shareholders. | \$ 3,721 | \$ 4,914 | \$ 227 | \$ 3,861 |
| Basic earnings per share attributable to common shareholders: | | | | |
| From continuing operations. | \$ 0.32 | \$ 0.42 | \$ 0.38 | \$ 0.32 |
| From discontinued operations | (0.01) | (0.01) | (0.36) | — |
| Basic | <u>\$ 0.31</u> | <u>\$ 0.41</u> | <u>\$ 0.02</u> | <u>\$ 0.32</u> |
| Diluted earnings per share attributable to common shareholders: | | | | |
| From continuing operations. | \$ 0.32 | \$ 0.42 | \$ 0.38 | \$ 0.32 |
| From discontinued operations | (0.01) | (0.01) | (0.36) | — |
| Diluted | <u>\$ 0.31</u> | <u>\$ 0.41</u> | <u>\$ 0.02</u> | <u>\$ 0.32</u> |
| Shares used in computation: | | | | |
| Basic. | 11,955 | 12,089 | 12,106 | 12,103 |
| Diluted | 11,979 | 12,110 | 12,120 | 12,117 |
| | 2012 | | | |
| | Q1 | Q2 | Q3 | Q4 |
| | (In thousands, except per share data) | | | |
| Net patient revenues from continuing operations | \$60,366 | \$61,963 | \$60,719 | \$61,052 |
| Net revenues from continuing operations | \$61,771 | \$63,397 | \$62,102 | \$62,381 |
| Operating income from continuing operations | \$ 9,765 | \$10,806 | \$ 9,534 | \$ 8,301 |
| Net income from continuing operations including noncontrolling interests | \$ 6,733 | \$ 7,452 | \$ 6,423 | \$ 6,032 |
| Net income from continuing operations attributable to common shareholders | \$ 4,436 | \$ 4,958 | \$ 4,588 | \$ 4,230 |
| Net income (losses) from discontinued operations attributable to common shareholders | \$ 42 | \$ (109) | \$ (25) | \$ (187) |
| Net income attributable to common shareholders | \$ 4,478 | \$ 4,849 | \$ 4,563 | \$ 4,043 |
| Basic earnings per share attributable to common shareholders: | | | | |
| From continuing operations. | \$ 0.37 | \$ 0.41 | \$ 0.39 | \$ 0.35 |
| From discontinued operations | — | (0.01) | — | (0.02) |
| Basic | <u>\$ 0.37</u> | <u>\$ 0.40</u> | <u>\$ 0.39</u> | <u>\$ 0.33</u> |
| Diluted earnings per share attributable to common shareholders: | | | | |
| From continuing operations. | \$ 0.37 | \$ 0.41 | \$ 0.38 | \$ 0.35 |
| From discontinued operations | — | (0.01) | — | (0.02) |
| Diluted. | <u>\$ 0.37</u> | <u>\$ 0.40</u> | <u>\$ 0.38</u> | <u>\$ 0.33</u> |
| Shares used in computation: | | | | |
| Basic | 11,955 | 12,089 | 12,106 | 12,103 |
| Diluted. | 11,979 | 12,110 | 12,120 | 12,117 |

ITEM 9. CHANGES IN AND DISAGREEMENTS WITH ACCOUNTANTS ON ACCOUNTING AND FINANCIAL DISCLOSURE.

Not applicable.

ITEM 9A. CONTROLS AND PROCEDURES.

Evaluation of Disclosure Controls and Procedures

Our management, including our Chief Executive Officer and Chief Financial Officer, has conducted an evaluation of the effectiveness of our disclosure controls and procedures (as defined in Rule 13a-15(e) promulgated under the Exchange Act) as of the end of the fiscal period covered by this report. Based upon that evaluation, our Chief Executive Officer and Chief Financial Officer have concluded that our disclosure controls and procedures are effective in ensuring that the information required to be disclosed in the reports we file or submit under the Exchange Act is recorded, processed, summarized and reported, within the time periods specified in the rules and forms of the SEC and that such information is accumulated and communicated to our management, including our Chief Executive Officer and Chief Financial Officer, as appropriate to allow timely decisions regarding disclosure.

Changes in Internal Control Over Financial Reporting

There have been no changes in our internal control over financial reporting during the quarter ended December 31, 2013 that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

MANAGEMENT'S REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING

Management is responsible for establishing and maintaining adequate internal control over financial reporting, as such term is defined in Rule 13a-15(f) under Exchange Act. U.S. Physical Therapy, Inc and subsidiaries' (the "Company") internal control over financial reporting is designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles.

Internal control over financial reporting includes those policies and procedures that:

- Pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the Company;
- Provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that our receipts and expenditures are being made only in accordance with authorizations of the Company's management and directors; and
- Provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use or disposition of the Company's assets that could have a material effect on the financial statements.

Internal control over financial reporting cannot provide absolute assurance of achieving financial reporting objectives because of its inherent limitations. Internal control over financial reporting is a process that involves human diligence and compliance and is subject to lapses in judgment and breakdowns resulting from human failures. Internal control over financial reporting can also be circumvented by collusion or improper management override. Because of such limitations, there is a risk that material misstatements may not be prevented or detected on a timely basis by internal control over financial reporting. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate. However, these inherent limitations are known features of the financial reporting process. Therefore, it is possible to design into the process safeguards to reduce, though not eliminate, the risk.

Management conducted an assessment of the effectiveness of our internal control over financial reporting as of December 31, 2013. In making this assessment, management used the criteria described in Internal Control — Integrated *Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission. Based on this assessment, management concluded that our internal control over financial reporting was effective as of December 31, 2013.

The Company's internal control over financial reporting has been audited by Grant Thornton LLP, an independent registered public accounting firm, as stated in their report included on page 39.

ITEM 9B. OTHER INFORMATION

Not applicable.

PART III

ITEM 10. *DIRECTORS, EXECUTIVE OFFICERS AND CORPORATE GOVERNANCE.*

The information required in response to this Item 10 is incorporated herein by reference to our definitive proxy statement relating to our 2014 Annual Meeting of Stockholders to be filed with the SEC pursuant to Regulation 14A, not later than 120 days after the end of our fiscal year covered by this report.

ITEM 11. *EXECUTIVE COMPENSATION.*

The information required in response to this Item 11 is incorporated herein by reference to our definitive proxy statement relating to our 2014 Annual Meeting of Stockholders to be filed with the SEC pursuant to Regulation 14A, not later than 120 days after the end of our fiscal year covered by this report.

ITEM 12. *SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT AND RELATED STOCKHOLDER MATTERS.*

The information required in response to this Item 12 is incorporated herein by reference to our definitive proxy statement relating to our 2014 Annual Meeting of Stockholders to be filed with the SEC pursuant to Regulation 14A, not later than 120 days after the end of our fiscal year covered by this report.

ITEM 13. *CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS, AND DIRECTOR INDEPENDENCE.*

The information required in response to this Item 13 is incorporated herein by reference to our definitive proxy statement relating to our 2014 Annual Meeting of Stockholders to be filed with the SEC pursuant to Regulation 14A, not later than 120 days after the end of our fiscal year covered by this report.

ITEM 14. *PRINCIPAL ACCOUNTANT FEES AND SERVICES.*

The information required in response to this Item 14 is incorporated herein by reference to our definitive proxy statement relating to our 2014 Annual Meeting of Stockholders to be filed with the SEC pursuant to Regulation 14A, not later than 120 days after the end of our fiscal year covered by this report.

PART IV

ITEM 15. *EXHIBITS AND FINANCIAL STATEMENT SCHEDULES.*

(a) Documents filed as a part of this report:

1. *Financial Statements.* Reference is made to the Index to Financial Statements and Related Information under Item 8 in Part II hereof, where these documents are listed.

2. *Financial Statement Schedules.* See page 73 for Schedule II — Valuation and Qualifying Accounts. All other schedules are omitted because of the absence of conditions under which they are required or because the required information is shown in the financial statements or notes thereto.

3. *Exhibits.* The exhibits listed in List of Exhibits on the next page are filed or incorporated by reference as part of this report.

EXHIBIT INDEX

LIST OF EXHIBITS

| <u>Number</u> | <u>Description</u> |
|---------------|---|
| 3.1 | Articles of Incorporation of the Company [filed as an exhibit to the Company's Form 10-Q for the quarterly period ended June 30, 2001 and incorporated herein by reference]. |
| 3.2 | Amendment to the Articles of Incorporation of the Company [filed as an exhibit to the Company's Form 10-Q for the quarterly period ended June 30, 2001 and incorporated herein by reference]. |
| 3.3 | Bylaws of the Company, as amended [filed as an exhibit to the Company's Form 10-KSB for the year ended December 31, 1993 and incorporated herein by reference—Commission File Number—1-11151]. |
| 10.1+ | 1992 Stock Option Plan, as amended [filed as an exhibit to the Company's Form 10-Q for the quarterly period ended June 30, 2001 and incorporated herein by reference]. |
| 10.2+ | Executive Option Plan [filed as an exhibit to the Company's Registration Statement on Form S-8 (Reg. No. 33-63444) and incorporated herein by reference]. |
| 10.3+ | 1999 Employee Stock Option Plan (as amended and restated May 20, 2008) [incorporated by reference to Appendix A to the Company's Definitive Proxy Statement on Schedule 14A, filed with the SEC on April 17, 2008]. |
| 10.4+ | U. S. Physical Therapy, Inc. 2003 Stock Incentive Plan, as amended and restated March 26, 2010 [incorporated by reference to Appendix A to the Company's proxy statement on Schedule 14A filed with the SEC on April 9, 2010]. |
| 10.5+ | First Amendment to the Amended and Restated 2003 Stock Incentive Plan [incorporated by reference to Appendix A to the Company's proxy statement on Schedule 14A filed with the SEC on April 8, 2013]. |
| 10.6+ | Consulting agreement between the Company and J. Livingston Kosberg [filed as an exhibit to the Company's Form 10-Q for the quarterly period ended June 30, 2001 and incorporated herein by reference]. |
| 10.7+ | First Amendment to the Consulting Agreement between the Company and J. Livingston—Kosberg [filed as an exhibit to the Company's Form 10-K for the year ended December 31, 2002 and incorporated herein by reference.] |
| 10.8+ | Amended and Restated Employment Agreement dated May 24, 2007, between U.S. Physical Therapy, Inc. and Christopher J. Reading [incorporated by reference to Exhibit 10.3 to the Company's Current Report on Form 8-K filed with the SEC on May 25, 2007]. |
| 10.9+ | Amendment to Amended and Restated Employment Agreement dated December 2, 2008 between U.S. Physical Therapy, Inc. and Christopher J. Reading [incorporated by reference to Exhibit 10.1 to the Company's Current Report on Form 8-K, filed with the SEC on December 5, 2008]. |
| 10.10+ | Amended and Restated Employment Agreement dated May 24, 2007, between U.S. Physical Therapy, Inc. and Lawrance W. McAfee [incorporated by reference to Exhibit 10.4 to the Company's Current Report on Form 8-K filed with the SEC on May 25, 2007]. |
| 10.11+ | Amendment to Amended and Restated Employment Agreement dated December 2, 2008 between U.S. Physical Therapy, Inc. and Lawrance W. McAfee [incorporated by reference to Exhibit 10.2 to the Company's Current Report on Form 8-K, filed with the SEC on December 5, 2008]. |
| 10.12+ | Form of Restricted Stock Agreement [incorporated by reference to Exhibit 10.17 to the Company's Annual Report on Form 10-K filed with the SEC on March 12, 2013]. |

| <u>Number</u> | <u>Description</u> |
|---------------|--|
| 10.13+ | Employment Agreement dated May 24, 2007, between U. S. Physical Therapy, Inc. and Glenn D. McDowell [incorporated by reference to Exhibit 10.2 to the Company's Current Report on Form 8-K filed with the SEC on May 25, 2007]. |
| 10.14+ | Amendment to Employment Agreement dated December 2, 2008 between U.S. Physical Therapy, Inc. and Glenn D. McDowell [incorporated by reference to Exhibit 10.3 to the Company's Current Report on Form 8-K, filed with the SEC on December 5, 2008]. |
| 10.15+ | USPH Executive Long-Term Incentive Plan, as Amended [incorporated by reference to Exhibit 10.1 to the Company's Current Report on Form 8-K, filed with the SEC on December 31, 2008]. |
| 10.16 | USPH 2009 Executive Bonus Plan (incorporated by reference to Exhibit 99.1 to the Company's Current Report on Form 8-K filed with the SEC on May 19, 2009). |
| 10.17+ | U. S. Physical Therapy, Inc. Objective Long-Term Incentive Plan for Senior Management, effective March 31, 2011 [incorporated by reference to Exhibit 99.1 to the Company's Current Report on Form 8-K filed with the SEC on April 6, 2011]. |
| 10.18+ | U. S. Physical Therapy, Inc. Discretionary Long-Term Incentive Plan for Senior Management for 2011, effective March 31, 2011 [incorporated by reference to Exhibit 99.2 to the Company's Current Report on Form 8-K filed with the SEC on April 6, 2011]. |
| 10.19+ | U. S. Physical Therapy, Inc. Objective Cash Bonus Plan for 2011, effective March 31, 2011 [incorporated by reference to Exhibit 99.3 to the Company's Current Report on Form 8-K filed with the SEC on April 6, 2011]. |
| 10.20+ | U. S. Physical Therapy, Inc. Discretionary Cash Bonus Plan for 2011, effective March 31, 2011 [incorporated by reference to Exhibit 99.4 to the Company's Current Report on Form 8-K filed with the SEC on April 6, 2011]. |
| 10.21+ | U. S. Physical Therapy, Inc. Objective Long-Term Incentive Plan for Senior Management, effective March 27, 2012 (incorporated by reference to Exhibit 99.1 to the Company's Current Report on Form 8-K filed with the SEC on March 28, 2012). |
| 10.22+ | U. S. Physical Therapy, Inc. Discretionary Long-Term Incentive Plan for Senior Management for 2012, effective March 27, 2012 (incorporated by reference to Exhibit 99.2 to the Company's Current Report on Form 8-K filed with the SEC on March 28, 2012). |
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| 10.29 | Credit Agreement, dated as of August 27, 2007 among U. S. Physical Therapy, Inc., as the Borrower, Bank of America, N. A., as Administrative Agent, Swing Line Lender and L/C Issuer, and The Other Lenders Party Hereto [incorporated by reference to Exhibit 10.2 to the Company’s Current Report on Form 8-K/A filed with the SEC on September 5, 2007]. |
| 10.30 | First Amendment to Credit Agreement dated as of June 4, 2008 by and among U.S. Physical Therapy, Inc., a Nevada Corporation, the Lenders party hereto, and Bank of America, N. A., as Administrative Agent [incorporated by reference to Exhibit 10.1 to the Company’s Quarterly Report on Form 10-Q for the quarterly period ended June 30, 2008, filed with the SEC on August 11, 2008]. |
| 10.31 | Second Amendment to Credit Agreement and Consent by and among the Company and the Lenders party hereto, and Bank of America, N. A., as Administrative Agent (incorporated by reference to Exhibit 99.1 to the Company Current Report on Form 8-K filed with the SEC on March 18, 2010). |
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| <u>Number</u> | <u>Description</u> |
|---------------|---|
| 21.1* | Subsidiaries of the Registrant |
| 23.1* | Consent of Independent Registered Public Accounting Firm—Grant Thornton LLP |
| 31.1* | Certification of Chief Executive Officer pursuant to Rule 13a-14(a) of the Securities Exchange Act of 1934, as amended |
| 31.2* | Certification of Chief Financial Officer pursuant to Rule 13a-14(a) of the Securities Exchange Act of 1934, as amended |
| 31.3* | Certification of Controller pursuant to Rule 13a-14(a) of the Securities Exchange Act of 1934, as amended |
| 32.1* | Certification of Periodic Report of the Chief Executive Officer, Chief Financial Officer and Controller pursuant to Rule 13a-14(b) of the Securities Exchange Act of 1934, as amended, and 18 U.S.C. Section 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 |

* Filed herewith

+ Management contract or compensatory plan or arrangement.

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

Board of Directors and Shareholders
U.S. Physical Therapy, Inc.

We have audited in accordance with the standards of the Public Company Accounting Oversight Board (United States) the consolidated financial statements of U.S. Physical Therapy, Inc. (a Nevada Corporation) and subsidiaries (the “Company”) referred to in our report dated March 11, 2014, which is included in the annual report to security holders and included in Part II of this form. Our audits of the basic consolidated financial statements included the financial statement schedule listed in the index appearing under item 15, which is the responsibility of the Company’s management. In our opinion, this financial statement schedule, when considered in relation to the basic consolidated financial statements taken as a whole, presents fairly, in all material respects, the information set forth therein.

/s/ GRANT THORNTON LLP

Houston, Texas
March 11, 2014

FINANCIAL STATEMENT SCHEDULE*

**SCHEDULE II — VALUATION AND QUALIFYING ACCOUNTS
U.S. PHYSICAL THERAPY, INC. AND SUBSIDIARIES**

| <u>COL. A</u> | <u>COL B</u> | <u>COL C</u> | <u>COL D</u> | <u>COL E</u> |
|---|---------------------------------------|--------------------------------------|----------------------------------|---------------------------------|
| <u>Description</u> | <u>Balance at Beginning of Period</u> | <u>Charged to Costs and Expenses</u> | <u>Charged to Other Accounts</u> | <u>Balance at End of Period</u> |
| | | <u>Additions</u> | | |
| | | <u>Charged to Costs and Expenses</u> | <u>Charged to Other Accounts</u> | <u>Deductions</u> |
| | | | | <u>Balance at End of Period</u> |
| | | <u>(Amounts in Thousands)</u> | | |
| YEAR ENDED DECEMBER 31, 2013: | | | | |
| Reserves and allowances deducted from asset accounts: | | | | |
| Allowance for doubtful accounts(1) | \$2,109 | \$4,370 | — | \$4,851(2) \$1,628 |
| YEAR ENDED DECEMBER 31, 2012: | | | | |
| Reserves and allowances deducted from asset accounts: | | | | |
| Allowance for doubtful accounts | \$3,037 | \$4,848 | — | \$5,776(2) \$2,109 |
| YEAR ENDED DECEMBER 31, 2011: | | | | |
| Reserves and allowances deducted from asset accounts: | | | | |
| Allowance for doubtful accounts | \$2,273 | \$3,785 | — | \$3,021(2) \$3,037 |

(1) Related to patient accounts receivable and accounts receivable—other.

(2) Uncollectible accounts written off, net of recoveries.

* All other schedules are omitted because of the absence of conditions under which they are required or because the required information is shown in the financial statements or notes thereto.

SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) 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.

U.S. PHYSICAL THERAPY, INC.
(Registrant)

By: /s/ LAWRENCE W. MCAFEE
Lawrance W. McAfee
Chief Financial Officer

By: /s/ JON C. BATES
Jon C. Bates
Vice President/Controller

Date: March 11, 2014

Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed below by the following persons on behalf of the registrant and in the capacities indicated as of the date indicated above.

| | |
|--|---|
| By: <u> /s/ CHRISTOPHER J. READING </u> Christopher J. Reading | President, Chief Executive Officer and Director (principal executive officer) |
| By: <u> /s/ LAWRENCE W. MCAFEE </u> Lawrance W. McAfee | Executive Vice President, Chief Financial Officer and Director (principal financial and accounting officer) |
| By: <u> /s/ JERALD PULLINS </u> Jerald Pullins | Chairman of the Board |
| By: <u> /s/ DANIEL C. ARNOLD </u> Daniel C. Arnold | Vice Chairman of the Board |
| By: <u> /s/ MARK J. BROOKNER </u> Mark J. Brookner | Director |
| By: <u> /s/ HARRY S. CHAPMAN </u> Harry S. Chapman | Director |
| By: <u> /s/ BERNARD A. HARRIS, JR. </u> Bernard A. Harris, Jr. | Director |
| By: <u> /s/ MARLIN W. JOHNSTON </u> Marlin W. Johnston | Director |
| By: <u> /s/ REGG SWANSON </u> Regg Swanson | Director |
| By: <u> /s/ CLAYTON TRIER </u> Clayton Trier | Director |

EXHIBIT INDEX

LIST OF EXHIBITS

| <u>Number</u> | <u>Description</u> |
|---------------|---|
| 3.1 | Articles of Incorporation of the Company [filed as an exhibit to the Company's Form 10-Q for the quarterly period ended June 30, 2001 and incorporated herein by reference]. |
| 3.2 | Amendment to the Articles of Incorporation of the Company [filed as an exhibit to the Company's Form 10-Q for the quarterly period ended June 30, 2001 and incorporated herein by reference]. |
| 3.3 | Bylaws of the Company, as amended [filed as an exhibit to the Company's Form 10-KSB for the year ended December 31, 1993 and incorporated herein by reference—Commission File Number—1-11151]. |
| 10.1+ | 1992 Stock Option Plan, as amended [filed as an exhibit to the Company's Form 10-Q for the quarterly period ended June 30, 2001 and incorporated herein by reference]. |
| 10.2+ | Executive Option Plan [filed as an exhibit to the Company's Registration Statement on Form S-8 (Reg. No. 33-63444) and incorporated herein by reference]. |
| 10.3+ | 1999 Employee Stock Option Plan (as amended and restated May 20, 2008) [incorporated by reference to Appendix A to the Company's Definitive Proxy Statement on Schedule 14A, filed with the SEC on April 17, 2008]. |
| 10.4+ | U. S. Physical Therapy, Inc. 2003 Stock Incentive Plan, as amended and restated March 26, 2010 [incorporated by reference to Appendix A to the Company's proxy statement on Schedule 14A filed with the SEC on April 9, 2010]. |
| 10.5+ | First Amendment to the Amended and Restated 2003 Stock Incentive Plan [incorporated by reference to Appendix A to the Company's proxy statement on Schedule 14A filed with the SEC on April 8, 2013]. |
| 10.6+ | Consulting agreement between the Company and J. Livingston Kosberg [filed as an exhibit to the Company's Form 10-Q for the quarterly period ended June 30, 2001 and incorporated herein by reference]. |
| 10.7+ | First Amendment to the Consulting Agreement between the Company and J. Livingston—Kosberg [filed as an exhibit to the Company's Form 10-K for the year ended December 31, 2002 and incorporated herein by reference.] |
| 10.8+ | Amended and Restated Employment Agreement dated May 24, 2007, between U.S. Physical Therapy, Inc. and Christopher J. Reading [incorporated by reference to Exhibit 10.3 to the Company's Current Report on Form 8-K filed with the SEC on May 25, 2007]. |
| 10.9+ | Amendment to Amended and Restated Employment Agreement dated December 2, 2008 between U.S. Physical Therapy, Inc. and Christopher J. Reading [incorporated by reference to Exhibit 10.1 to the Company's Current Report on Form 8-K, filed with the SEC on December 5, 2008]. |
| 10.10+ | Amended and Restated Employment Agreement dated May 24, 2007, between U.S. Physical Therapy, Inc. and Lawrance W. McAfee [incorporated by reference to Exhibit 10.4 to the Company's Current Report on Form 8-K filed with the SEC on May 25, 2007]. |
| 10.11+ | Amendment to Amended and Restated Employment Agreement dated December 2, 2008 between U.S. Physical Therapy, Inc. and Lawrance W. McAfee [incorporated by reference to Exhibit 10.2 to the Company's Current Report on Form 8-K, filed with the SEC on December 5, 2008]. |
| 10.12+ | Form of Restricted Stock Agreement [incorporated by reference to Exhibit 10.17 to the Company's Annual Report on Form 10-K filed with the SEC on March 12, 2013]. |

| <u>Number</u> | <u>Description</u> |
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| 10.13+ | Employment Agreement dated May 24, 2007, between U. S. Physical Therapy, Inc. and Glenn D. McDowell [incorporated by reference to Exhibit 10.2 to the Company's Current Report on Form 8-K filed with the SEC on May 25, 2007]. |
| 10.14+ | Amendment to Employment Agreement dated December 2, 2008 between U.S. Physical Therapy, Inc. and Glenn D. McDowell [incorporated by reference to Exhibit 10.3 to the Company's Current Report on Form 8-K, filed with the SEC on December 5, 2008]. |
| 10.15+ | USPH Executive Long-Term Incentive Plan, as Amended [incorporated by reference to Exhibit 10.1 to the Company's Current Report on Form 8-K, filed with the SEC on December 31, 2008]. |
| 10.16 | USPH 2009 Executive Bonus Plan (incorporated by reference to Exhibit 99.1 to the Company's Current Report on Form 8-K filed with the SEC on May 19, 2009). |
| 10.17+ | U. S. Physical Therapy, Inc. Objective Long-Term Incentive Plan for Senior Management, effective March 31, 2011 [incorporated by reference to Exhibit 99.1 to the Company's Current Report on Form 8-K filed with the SEC on April 6, 2011]. |
| 10.18+ | U. S. Physical Therapy, Inc. Discretionary Long-Term Incentive Plan for Senior Management for 2011, effective March 31, 2011 [incorporated by reference to Exhibit 99.2 to the Company's Current Report on Form 8-K filed with the SEC on April 6, 2011]. |
| 10.19+ | U. S. Physical Therapy, Inc. Objective Cash Bonus Plan for 2011, effective March 31, 2011 [incorporated by reference to Exhibit 99.3 to the Company's Current Report on Form 8-K filed with the SEC on April 6, 2011]. |
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| 101.LAB* | XBRL Taxonomy Extension Label Linkbase Document |
| 101.PRE* | XBRL Taxonomy Extension Presentation Linkbase Document |

* Filed herewith

+ Management contract or compensatory plan or arrangement.

EXHIBIT 21.1

SUBSIDIARIES OF THE REGISTRANT

| <u>NAME OF SUBSIDIARY</u> | <u>TYPE OF ENTITY</u> | <u>STATE OF INCORPORATION OR FORMATION</u> |
|--|---------------------------|--|
| U.S. PT – Delaware, Inc. dba The Facilities Group | Corporation | Delaware |
| U.S. Therapy, Inc. dba First Choice Physical Therapy | Corporation | Texas |
| National Rehab GP, Inc. | Corporation | Texas |
| National Rehab Delaware, Inc. | Corporation | Delaware |
| U.S. PT – Michigan, Inc. | Corporation | Delaware |
| HH Rehab Associates, Inc. dba Genesee Valley Physical Therapy dba Theramax Physical Therapy | Corporation | Michigan |
| Professional Rehab Services, Inc. | Corporation | Michigan |
| U.S. Physical Therapy, Ltd. | Limited Partnership | Texas |
| U.S. PT Management, Ltd. | Limited Partnership | Texas |
| National Rehab Management GP, Inc. | Corporation | Texas |
| Rehab Partners #1, Inc. | Corporation | Texas |
| Rehab Partners #2, Inc. | Corporation | Texas |
| Rehab Partners #3, Inc. | Corporation | Texas |
| Rehab Partners #4, Inc. | Corporation | Texas |
| Rehab Partners #5, Inc. | Corporation | Texas |
| Rehab Partners #6, Inc. | Corporation | Texas |
| U.S. PT Payroll, Inc. (formerly Rehab Partners #7, Inc.) | Corporation | Texas |
| Rehab Partners Acquisition #1, Inc. | Corporation | Texas |
| U.S. PT Therapy Services, Inc. (formerly U.S. Surgical Partners, Inc.) dba Capstone Physical Therapy dba Carolina Hand and Wellness Center dba Hand Therapy Specialists of North Texas dba Innovative Physical Therapy dba Kinetix Physical Therapy dba Lake City Hand Therapy dba Life Sport Physical Therapy dba Metro Hand Rehabilitation dba Missouri City Physical Therapy dba Mountain View Physical Therapy of Medford dba Mountain View Physical Therapy of Talent dba Northern Illinois Therapy Services dba ProCare Sports Medicine dba Propel Physical Therapy dba Reaction Physical Therapy dba Therapeutic Concepts dba Tulsa Hand Therapy dba Waco Sports Medicine & Rehabilitation | Corporation | Delaware |
| U.S. PT Contract Management, Inc. | Corporation | Texas |

| <u>NAME OF SUBSIDIARY</u> | <u>TYPE OF ENTITY</u> | <u>STATE OF INCORPORATION OR FORMATION</u> |
|--|---------------------------|--|
| U.S. PT Turnkey Services, Inc. (formerly Surgical Management GP, Inc. dba The Hand & Orthopedic Rehab Clinic | Corporation | Texas |
| Southeastern Hand Rehabilitation, Inc. dba Reist Hand Therapy dba Achieve Physical Therapy | Corporation | Florida |
| Action Therapy Centers, Limited Partnership dba Action Physical Therapy dba Houston Hand Therapy | Limited Partnership | Texas |
| Star Therapy Centers, Limited Partnership dba Star Therapy Services of Cinco Ranch dba Star Therapy Services of Cy-Fair dba Star Therapy Services of Copperfield dba Star Therapy Services of Katy dba Star Therapy Services of Magnolia dba Star Therapy Services of Spring Cypress | Limited Partnership | Texas |
| Progressive Physical Therapy Clinic, Ltd. Dba Progressive Hand and Physical Therapy | Limited Partnership | Texas |
| Virginia Parc Physical Therapy, Ltd. dba McKinney Physical Therapy Associates | Limited Partnership | Texas |
| Dearborn Physical Therapy, Ltd. dba Advanced Physical Therapy | Limited Partnership | Texas |
| Saline Physical Therapy of Michigan, Ltd. dba Physical Therapy in Motion | Limited Partnership | Texas |
| Roepeke Physical Therapy, Limited Partnership dba Elite Hand & Upper Extremity Clinic | Limited Partnership | Texas |
| Merrill Physical Therapy, Limited Partnership | Limited Partnership | Texas |
| Joan Ostermeier Physical Therapy, Limited Partnership dba Sport & Spine Clinic of Wittenberg | Limited Partnership | Texas |
| Crossroads Physical Therapy, Limited Partnership dba Green Oaks Physical Therapy dba Green Oaks Physical Therapy – Fort Worth | Limited Partnership | Texas |
| Kelly Lynch Physical Therapy, Limited Partnership | Limited Partnership | Texas |
| U.S. PT Michigan #1, Limited Partnership | Limited Partnership | Texas |
| Spracklen Physical Therapy, Limited Partnership | Limited Partnership | Texas |
| Bosque River Physical Therapy and Rehabilitation, Limited Partnership | Limited Partnership | Texas |
| Frisco Physical Therapy, Limited Partnership | Limited Partnership | Texas |
| Sport & Spine Clinic of Fort Atkinson, Limited Partnership dba Sport & Spine Clinic of Sauk City dba Sport & Spine Clinic of Madison dba Sport & Spine Clinic of Edgerton dba Sport & Spine Clinic of Jefferson | Limited Partnership | Texas |
| Sport & Spine Clinic of Auburndale, Limited Partnership | Limited Partnership | Texas |

| <u>NAME OF SUBSIDIARY</u> | <u>TYPE OF ENTITY</u> | <u>STATE OF INCORPORATION OR FORMATION</u> |
|---|---------------------------|--|
| Kingwood Physical Therapy, Ltd. | | |
| dba Spring-Klein Physical Therapy | | |
| dba West Woodlands Physical Therapy | Limited Partnership | Texas |
| Enid Therapy Center, Limited Partnership | Limited Partnership | Texas |
| Active Physical Therapy, Limited Partnership | Limited Partnership | Texas |
| Cleveland Physical Therapy, Ltd. | Limited Partnership | Texas |
| Aquatic and Orthopedic Rehab Specialists, Limited Partnership | | |
| dba Horizon Physical Therapy | Limited Partnership | Texas |
| Vileno Therapy of Treasure Coast, Limited Partnership | | |
| dba Treasure Coast Hand & Physical Therapy | Limited Partnership | Texas |
| Comprehensive Hand & Physical Therapy, Limited Partnership | Limited Partnership | Texas |
| Safety Harbor Physical Therapy, Limited Partnership | | |
| dba Apex Physical Therapy | Limited Partnership | Texas |
| South Tulsa Physical Therapy, Limited Partnership | | |
| dba Jenks Physical Therapy | Limited Partnership | Texas |
| Hands On Therapy, Limited Partnership | Limited Partnership | Texas |
| U.S. PT Michigan #2, Limited Partnership | Limited Partnership | Texas |
| Tupelo Hand Rehabilitation, Limited Partnership | Limited Partnership | Texas |
| The Hale Hand Center, Limited Partnership | Limited Partnership | Texas |
| Sooner Physical Therapy, Limited Partnership | Limited Partnership | Texas |
| Arrow Physical Therapy, Limited Partnership | | |
| dba Broken Arrow Physical Therapy | Limited Partnership | Texas |
| Achieve Physical Therapy, Limited Partnership | Limited Partnership | Texas |
| Melbourne Physical Therapy Specialists, Limited Partnership | Limited Partnership | Texas |
| Maine Physical Therapy, Limited Partnership | Limited Partnership | Texas |
| Saginaw Valley Sport and Spine, Limited Partnership | | |
| dba Sport & Spine Physical Therapy and Rehab | Limited Partnership | Texas |
| Brazos Valley Physical Therapy, Limited Partnership | Limited Partnership | Texas |
| Plymouth Physical Therapy Specialists, Limited Partnership | Limited Partnership | Texas |
| Brick Hand & Rehabilitative Services, Limited Partnership | Limited Partnership | Texas |
| Heartland Physical Therapy, Limited Partnership | Limited Partnership | Texas |
| Bay View Physical Therapy, Ltd. | | |
| dba Pine State Physical Therapy | | |
| dba Bay View Physical Therapy of Newport | Limited Partnership | Texas |
| Thomas Hand and Rehabilitation Specialists, Limited Partnership | | |
| dba Thomas Physical & Hand Therapy | Limited Partnership | Texas |
| Port City Physical Therapy, Limited Partnership | Limited Partnership | Texas |

| <u>NAME OF SUBSIDIARY</u> | <u>TYPE OF ENTITY</u> | <u>STATE OF INCORPORATION OR FORMATION</u> |
|--|---------------------------|--|
| Proactive Physical Therapy, Limited Partnership | Limited Partnership | Texas |
| Momentum Therapy, Limited Partnership | Limited Partnership | Texas |
| Beaufort Physical Therapy, Limited Partnership | Limited Partnership | Texas |
| Brownwood Physical Therapy, Limited Partnership dba Pecan Valley Physical Therapy | Limited Partnership | Texas |
| Four Corners Physical Therapy, Limited Partnership | Limited Partnership | Texas |
| Wilmington Hand Therapy, Limited Partnership dba Hand Therapy of Wilmington | Limited Partnership | Texas |
| High Point Physical Therapy, Limited Partnership | Limited Partnership | Texas |
| Riverview Physical Therapy, Limited Partnership | Limited Partnership | Texas |
| Spine & Sport Physical Therapy, Limited Partnership | Limited Partnership | Texas |
| Norman Physical Therapy, Limited Partnership | Limited Partnership | Texas |
| Rice Rehabilitation Associates, Limited Partnership | Limited Partnership | Texas |
| Physical Therapy and Spine Institute, Limited Partnership | Limited Partnership | Texas |
| Forest City Physical Therapy, Limited Partnership | Limited Partnership | Texas |
| Leader Physical Therapy, Limited Partnership dba Memphis Physical Therapy | Limited Partnership | Texas |
| Coastal Physical Therapy, Limited Partnership | Limited Partnership | Texas |
| Eastgate Physical Therapy, Limited Partnership dba Summit Physical Therapy | Limited Partnership | Texas |
| Lucasville Therapy Services, Limited Partnership dba Physical Therapy of Wheelersburg | Limited Partnership | Texas |
| Ankeny Physical & Sports Therapy, Limited Partnership | Limited Partnership | Texas |
| Regional Physical Therapy Center, Limited Partnership | Limited Partnership | Texas |
| Precision Physical Therapy, Limited Partnership | Limited Partnership | Texas |
| Adams County Physical Therapy, Limited Partnership | Limited Partnership | Texas |
| Coppell Spine & Sports Rehab, Limited Partnership dba North Davis/Keller Physical Therapy dba Physical Therapy of Colleyville dba Physical Therapy of Corinth dba Physical Therapy of Flower Mound dba Physical Therapy of North Texas dba Southlake Physical Therapy dba Physical Therapy of Flower Mound South dba Physical Therapy of Trophy Club dba Heritage Trace Physical Therapy dba Trinity Sports & Physical Therapy dba Heritage Trace Physical Therapy dba Therapy Partners of Frisco/Little Elm | Limited Partnership | Texas |
| Julie Emond Physical Therapy, Limited Partnership dba Maple Valley Physical Therapy | Limited Partnership | Texas |
| City of Lakes Physical Therapy, Limited Partnership | Limited Partnership | Texas |
| Radtke Physical Therapy, Limited Partnership | Limited Partnership | Texas |
| Hoepfner Physical Therapy, Limited Partnership | Limited Partnership | Texas |
| Des Moines Physical Therapy, Limited Partnership | Limited Partnership | Texas |
| Shrewsbury Physical Therapy, Limited Partnership | Limited Partnership | Texas |
| Heritage Physical Therapy, Limited Partnership | Limited Partnership | Texas |
| Mansfield Physical Therapy, Limited Partnership | Limited Partnership | Texas |
| Texstar Physical Therapy, Limited Partnership | Limited Partnership | Texas |

| <u>NAME OF SUBSIDIARY</u> | <u>TYPE OF ENTITY</u> | <u>STATE OF INCORPORATION OR FORMATION</u> |
|--|---------------------------|--|
| Peninsula Physical Therapy, Limited Partnership dba Portland Physical Therapy | Limited Partnership | Texas |
| Flint Physical Therapy, Limited Partnership | Limited Partnership | Texas |
| Pelican State Physical Therapy, Limited Partnership dba Audubon Physical Therapy | Limited Partnership | Texas |
| Airpark Physical Therapy, Limited Partnership dba Philadelphia Physical Therapy | Limited Partnership | Texas |
| Paramount Physical Therapy & Hand Institute, Limited Partnership | Limited Partnership | Texas |
| Edge Physical Therapy, Limited Partnership dba River's Edge Physical Therapy | Limited Partnership | Texas |
| Laurel Physical Therapy, Limited Partnership dba South Mississippi Physical Therapy | Limited Partnership | Texas |
| Riverwest Physical Therapy, Limited Partnership | Limited Partnership | Texas |
| Northern Neck Physical Therapy, Limited Partnership | Limited Partnership | Texas |
| Intermountain Physical Therapy, Limited Partnership | Limited Partnership | Texas |
| Portsmouth Premier Physical Therapy, Limited Partnership | Limited Partnership | Texas |
| Covington Rehabilitation and Hand Therapy, Limited Partnership dba South Mississippi Physical Therapy | Limited Partnership | Texas |
| Crawford Physical Therapy, Limited Partnership | Limited Partnership | Texas |
| Mobile Spine and Rehabilitation, Limited Partnership | Limited Partnership | Texas |

| <u>NAME OF SUBSIDIARY</u> | <u>TYPE OF ENTITY</u> | <u>STATE OF INCORPORATION OR FORMATION</u> |
|--|---------------------------|--|
| University Physical Therapy, Limited Partnership | Limited Partnership | Texas |
| Oregon Spine & Physical Therapy, Limited Partnership | Limited Partnership | Texas |
| Audubon Physical Therapy, Limited Partnership | Limited Partnership | Texas |
| Bow Physical Therapy & Spine Center, Limited Partnership | Limited Partnership | Texas |
| Caldwell Management, Limited Partnership | Limited Partnership | Texas |
| North Shore Sports & Physical Therapy, Limited Partnership | Limited Partnership | Texas |
| Physical Therapy Connection of McLean, Limited Partnership | Limited Partnership | Texas |
| dba Physical Therapy Connection of Fairfax | | |
| dba Physical Therapy Connection of Reston | | |
| Royal Physical Therapy, Limited Partnership | Limited Partnership | Texas |
| Sport & Spine Clinic, L.P. | Limited Partnership | Texas |
| dba Sport & Spine Clinic of Edgar | | |
| dba Sport & Spine Clinic of Rib Mountain | | |
| Riverview Physical Therapy, Limited Partnership | Limited Partnership | Texas |
| Sport & Spine Clinic L.P. | Limited Partnership | Texas |
| Flannery Physical Therapy, Limited Partnership, | Limited Partnership | Texas |
| dba Physical Therapy Plus | | |
| Mountain View Physical Therapy, Limited Partnership | Limited Partnership | Texas |
| Ashland Physical Therapy, Limited Partnership | Limited Partnership | Texas |
| Lake Houston Physical Therapy, Limited Partnership | Limited Partnership | Texas |
| R. Clair Physical Therapy, Limited Partnership, dba Clair | | |
| Physical Therapy Limited Partnership | Limited Partnership | Texas |
| Green Oaks Physical Therapy, Limited | Limited Partnership | Texas |
| Partnership Therapy | | |
| dba Green Oaks Physical | | |
| dba Green Oaks PT – Cedar Hill | | |
| dba Green Oaks PT – Grand Prairie | | |
| Spectrum Physical Therapy, Limited Partnership | Limited Partnership | Texas |
| dba Southshore Physical Therapy | | |
| Precise Touch Physical Therapy, Limited Partnership | Limited Partnership | Texas |
| dba Mountain View Physical Therapy of Grants Pass | | |

| <u>NAME OF SUBSIDIARY</u> | <u>TYPE OF ENTITY</u> | <u>STATE OF INCORPORATION OR FORMATION</u> |
|--|---------------------------|--|
| Lucasville Physical Therapy, Limited Partnership dba Direct Care Physical Therapy dba Physical Therapy of Wheelersburg | Limited Partnership | Texas |
| Custom Physical Therapy, Limited Partnership | Limited Partnership | Texas |
| Workwise Therapy Services, Limited Partnership | Limited Partnership | Texas |
| High Plains Physical Therapy, Limited Partnership | Limited Partnership | Texas |
| Evergreen Physical Therapy, Limited Partnership | Limited Partnership | Texas |
| Wise Performance Physical Therapy, Limited Partnership | Limited Partnership | Texas |
| Moving Well Physical Therapy, Limited Partnership | Limited Partnership | Texas |

| <u>NAME OF SUBSIDIARY</u> | <u>TYPE OF ENTITY</u> | <u>STATE OF INCORPORATION OR FORMATION</u> |
|---|---------------------------|--|
| Cross Creek Physical Therapy, Limited Partnership | Limited Partnership | Texas |
| Georgia Orthopedic Physical Therapy, Limited Partnership | Limited Partnership | Texas |
| Port Orange Physical Therapy, Limited Partnership | Limited Partnership | Texas |
| Hamilton Physical Therapy Services, Limited Partnership | Limited Partnership | Texas |
| Ventana Therapy Center, Limited Partnership | Limited Partnership | Texas |
| Mariposa Hand & Rehab Specialists, Limited Partnership dba Sports Driven Rehabilitation & Training | Limited Partnership | Texas |
| Active PT and Sports Rehabilitation, Limited Partnership | Limited Partnership | Texas |
| New Horizons PT, Limited Partnership | Limited Partnership | Texas |
| Decatur Hand Therapy Specialists, Limited Partnership | Limited Partnership | Texas |
| Fredericksburg Physical Therapy, Limited Partnership | Limited Partnership | Texas |
| Pioneer Physical Therapy, Limited Partnership | Limited Partnership | Texas |
| Restore Physical Therapy, Limited Partnership | Limited Partnership | Texas |
| Harbor Physical Therapy, Limited Partnership | Limited Partnership | Texas |
| Rebud Occupational & Physical Therapy, Limited Partnership | Limited Partnership | Texas |
| Sycamore Hand Center, Limited Partnership | Limited Partnership | Texas |
| Hands-On Sports Medicine, Limited Partnership dba Metro Spine and Sports Rehabilitation | Limited Partnership | Texas |

NAME OF
SUBSIDIARY

Dekalb Comprehensive Physical Therapy, Limited Partnership
Triumph Physical Therapy, Limited Partnership

TYPE OF
ENTITY

Limited Partnership
Limited Partnership

STATE OF
INCORPORATION
OR FORMATION

Texas
Texas

| <u>NAME OF SUBSIDIARY</u> | <u>TYPE OF ENTITY</u> | <u>STATE OF INCORPORATION OR FORMATION</u> |
|--|---------------------------|--|
| Five Rivers Physical Therapy, Limited Partnership dba Peak Physical Therapy | Limited Partnership | Texas |
| Oak Openings Physical Therapy, Limited Partnership | Limited Partnership | Texas |
| Cutting Edge Physical Therapy, Limited Partnership | Limited Partnership | Texas |
| Excel Physical Therapy, Limited Partnership | Limited Partnership | Texas |
| Core PT, Limited Partnership | Limited Partnership | Texas |
| Quad City Physical Therapy, Limited Partnership | Limited Partnership | Texas |
| Cape Cod Hand Therapy, Limited Partnership | Limited Partnership | Texas |
| Excel PT Texas GP, LLC | Limited Liability Company | Texas |
| HPTS Management GP, LLC | Limited Liability Company | Texas |
| Thibodeau Physical Therapy, Limited Partnership | Limited Partnership | Texas |
| Northwoods Physical Therapy, Limited Partnership | Limited Partnership | Texas |

| <u>NAME OF SUBSIDIARY</u> | <u>TYPE OF ENTITY</u> | <u>STATE OF INCORPORATION OR FORMATION</u> |
|---|---------------------------|--|
| U.S. PT Managed Care, Inc. dba Virginia Sports Medicine & Physical Therapy | Corporation | Texas |
| PerformancePro Sports Medicine & Rehabilitation, Limited Partnership | Limited Partnership | Texas |
| Preferred Physical Therapy, Limited Partnership | Limited Partnership | Texas |
| Osteoarthritis Centers of America, Limited Partnership dba OsteoArthritis Centers of America | Limited Partnership | Texas |
| U.S. PT Solutions, Inc. dba Physical Therapy Solutions | Corporation | Texas |
| Dynamic Hand Therapy & Rehabilitation, Limited Partnership | Limited Partnership | Texas |
| STAR Physical Therapy, Limited Partnership | Limited Partnership | Texas |
| STAR PT Management GP, LLC | Limited Liability Company | Texas |
| Life Fitness Physical Therapy, LLC dba In Balance Physical Therapy | Limited Liability Company | Texas |
| Ultimate Performance Physical Therapy, Limited Partnership | Limited Partnership | Texas |
| Cedar Creek Physical Therapy, Limited Partnership | Limited Partnership | Texas |
| Charleston Specialty Rehab Institute, Limited Partnership | Limited Partnership | Texas |

| <u>NAME OF SUBSIDIARY</u> | <u>TYPE OF ENTITY</u> | <u>STATE OF INCORPORATION OR FORMATION</u> |
|--|---------------------------|--|
| New Heights Physical Therapy, Limited Partnership | Limited Partnership | Texas |
| Beacon Physical Therapy, Limited Partnership | Limited Partnership | Texas |
| Mission Rehabilitation and Sports Medicine Limited Partnership, Limited Partnership | Limited Partnership | Texas |
| RYKE Management GP, LLC | Limited Liability Company | Texas |
| Thunder Physical Therapy, Limited Partnership | Limited Partnership | Texas |
| LiveWell Physical Therapy, Limited Partnership | Limited Partnership | Texas |
| Max Motion Physical Therapy, Limited Partnership | Limited Partnership | Texas |
| DHT Hand Therapy, Limited Partnership dba Arizona Desert Hand Therapy | Limited Partnership | Texas |
| DHT Management GP, LLC | Limited Liability Company | Texas |
| Physical Therapy of Casper, Limited Partnership | Limited Partnership | Texas |
| Fit2WRK, Inc. | Corporation | Texas |
| Lone Star Procurement Group, Inc. dba Lone Star Healthcare Purchasing Network | Corporation | Texas |
| Gahanna Physical Therapy, Limited Partnership dba Cornerstone Physical Therapy | Limited Partnership | Texas |
| Northern Lights Physical Therapy, Limited Partnership | Limited Partnership | Texas |
| Georgia Pro Motion Physical Therapy, Limited Partnership | Limited Partnership | Texas |
| Physical Restoration & Sports Medicine, Limited Partnership | Limited Partnership | Texas |
| Phoenix Physical Therapy, Limited Partnership | Limited Partnership | Texas |
| Madison PT of New Jersey, PC | Professional Corporation | New Jersey |
| Madison Spine & Physical Therapy, PC | Professional Corporation | New Jersey |
| Montvale Physical Therapy, PC | Professional Corporation | New Jersey |
| Madison Spine & Physical Therapy, PC | Professional Corporation | New Jersey |
| Ohio Life Balance Physical Therapy, Limited Partnership dba Life Balance Physical Therapy | Limited Partnership | Texas |
| Highlands Physical Therapy & Sports Medicine, Limited Partnership | Limited Partnership | Texas |
| Maplewood Physical Therapy, Limited Partnership | Limited Partnership | Texas |
| North Jersey Game On Physical Therapy, Limited Partnership | Limited Partnership | Texas |

| <u>NAME OF SUBSIDIARY</u> | <u>TYPE OF ENTITY</u> | <u>STATE OF INCORPORATION OR FORMATION</u> |
|---|---------------------------|--|
| Prestige Physical Therapy, Limited Partnership | Limited Partnership | Texas |
| Bayside Physical Therapy & Sports Rehabilitation, Limited Partnership | Limited Partnership | Texas |
| Bayside Management GP, LLC | Limited Liability Company | Texas |
| Advance Rehabilitation & Consulting, Limited Partnership | Limited Partnership | Texas |
| Advance Rehabilitation Management GP, LLC | Limited Liability Company | Texas |
| ARCH Physical Therapy and Sports Medicine, Limited Partnership | Limited Partnership | Texas |
| Seacoast Physical Therapy, Limited Partnership | Limited Partnership | Texas |
| Integrated Rehab Group, Limited Partnership | Limited Partnership | Texas |
| Integrated Management GP, LLC | Limited Liability Company | Texas |
| South Sound Physical and Hand Therapy, LLC dba Parkside Physical Therapy | Limited Liability Company | Washington |
| Everett Physical Therapy and Sports Performance Center, LLC | Limited Liability Company | Washington |

| <u>NAME OF SUBSIDIARY</u> | <u>TYPE OF ENTITY</u> | <u>INCORPORATION OR FORMATION</u> |
|---|---------------------------|---------------------------------------|
| Redmond Ridge Physical Therapy, LLC | Limited Liability Company | Washington |
| Snohomish Physical Therapy, LLC | Limited Liability Company | Washington |
| Indy ProCare Physical Therapy, Limited Partnership | Limited Partnership | Texas |
| Madison Spine, Limited Partnership | Limited Partnership | Texas |
| Madison Physical Therapy, Limited Partnership | Limited Partnership | Texas |
| MSPT Management GP, LLC | Limited Liability Company | Texas |
| OrthoSport Physical Therapy (of Maryland), LLC | Limited Liability Company | Maryland |
| Agape Physical Therapy & Sports Rehabilitation, Limited Partnership | Limited Partnership | Texas |
| Agape Physical Therapy Management GP, LLC | Limited Liability Company | Texas |
| Green Country Physical Therapy, Limited Partnership | Limited Partnership | Texas |
| Arrowhead Physical Therapy, Limited Partnership dba Elite Sports Medicine & Physical Therapy | Limited Partnership | Texas |
| Pinnacle Therapy Services, LLC | Limited Liability Company | Texas |
| Kennebec Physical Therapy, LLC | Limited Liability Company | Texas |
| Therapyworks Physical Therapy, LLC dba Therapyworks | Limited Liability Company | Delaware |
| ProCare PT, Limited Partnership | Limited Partnership | Texas |
| ProCare PT Management GP, LLC | Limited Liability Company | Texas |
| North Lake Physical Therapy and Rehab, Limited Partnership | Limited Partnership | Texas |
| North Lake PT Management GP, LLC | Limited Liability Company | Texas |

| <u>NAME OF SUBSIDIARY</u> | <u>TYPE OF ENTITY</u> | <u>INCORPORATION OR FORMATION</u> |
|--|---------------------------|---------------------------------------|
| Mishock Physical Therapy, Limited Partnership dba Xcelerate Physical Therapy | Limited Partnership | Texas |
| Mishock PT Management GP, LLC | Limited Liability Company | Texas |
| High Performance Physical Therapy, LLC dba Atlanta Falcons Physical Therapy Centers | Limited Liability Company | Texas |
| ARC Physical Therapy Plus, Limited Partnership | Limited Partnership | Texas |
| ARC PT Management GP, LLC | Limited Liability Company | Texas |

CONSENT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

We have issued our reports dated March 11, 2014, with respect to the consolidated financial statements, schedule and internal control over financial reporting included in the Annual Report of U.S. Physical Therapy, Inc. on Form 10-K for the year ended December 31, 2013. We hereby consent to the incorporation by reference of said reports in the Registration Statements of U.S. Physical Therapy, Inc. on Form S-8s (File 333-30071, 333-64159, 333-67680, 333-67678, 333-82932, 333-103057, 333-113592, 333-116230, 333-153051 and 333-185381).

/s/ GRANT THORNTON LLP

Houston, Texas
March 11, 2014

CERTIFICATION

I, Christopher J. Reading, certify that:

1. I have reviewed this annual report on Form 10-K of U.S. Physical Therapy, Inc.;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer(s) and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
 - (a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
 - (b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
 - (c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
 - (d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer(s) and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
 - (a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
 - (b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: March 11, 2014

/s/ Christopher J. Reading
Christopher J. Reading
President and Chief Executive Officer
(principal executive officer)

CERTIFICATION

I, Lawrance W. McAfee, certify that:

1. I have reviewed this annual report on Form 10-K of U.S. Physical Therapy, Inc.;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer(s) and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
 - (a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
 - (b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
 - (c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
 - (d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer(s) and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
 - (a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
 - (b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: March 11, 2014

/s/ Lawrance W. McAfee

Lawrance W. McAfee

Executive Vice President and

Chief Financial Officer

(principal financial and accounting officer)

CERTIFICATION

I, Jon C. Bates, certify that:

1. I have reviewed this annual report on Form 10-K of U.S. Physical Therapy, Inc.;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer(s) and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
 - (a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
 - (b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
 - (c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
 - (d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer(s) and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
 - (a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
 - (b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: March 11, 2014

/s/ Jon C. Bates

Jon C. Bates

Vice President and Corporate Controller

**CERTIFICATION PURSUANT TO
18 U.S.C. SECTION 1350,
AS ADOPTED PURSUANT TO
SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002**

In connection with the Annual Report of U.S. Physical Therapy, Inc. (the “registrant”) on Form 10-K for the year ending December 31, 2013 as filed with the Securities and Exchange Commission on the date hereof (the “report”), we, Christopher J. Reading, Lawrence W. McAfee and Jon C. Bates, Chief Executive Officer, Chief Financial Officer and Controller, respectively, of the registrant, certify, pursuant to 18 U.S.C. § 1350, as adopted pursuant to § 906 of the Sarbanes-Oxley Act of 2002, that to our knowledge:

(1) The report fully complies with the requirements of section 13(a) or 15(d) of the Securities Exchange Act of 1934, as amended; and

(2) The information contained in the report fairly presents, in all material respects, the financial condition and results of operations of the registrant.

March 11, 2014

/s/ Christopher J. Reading

Christopher J. Reading
Chief Executive Officer

/s/ Lawrence W. McAfee

Lawrence W. McAfee
Chief Financial Officer

/s/ Jon C. Bates

Jon C. Bates
Vice President and Controller

A signed original of this written statement required by Section 906 has been provided to U. S. Physical Therapy, Inc. and will be retained by U. S. Physical Therapy, Inc. and furnished to the Securities and Exchange Commission or its staff upon request.