PharMerica CORP
Form 10-K
February 28, 2014

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, DC 20549

FORM 10-K
(Mark One)
þ ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the year ended December 31, 2013
or
o TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the transition period from to .
Commission File Number: 001-33380

PHARMERICA CORPORATION
(Exact name of registrant as specified in its charter)

Delaware	87-0792558
(State or Other Jurisdiction of Incorporation or Organization)	(I.R.S. Employer Identification No.)
1901 Campus Place Louisville, KY	40299
(Address of Principal Executive Offices)	(Zip Code)

(502) 627-7000
(Registrant's Telephone Number, Including Area Code)
Securities registered pursuant to Section 12(b) of the Act:

Title of each class	Name of exchange on which registered
Common stock $0.01 par value	New York Stock Exchange

Securities registered pursuant to Section 12(g) of the Act:
N/A
(Title of class)

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

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

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

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

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. þ

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 o	Accelerated filer þ
Non-accelerated filer o	Smaller reporting company o
(Do not check if a smaller reporting company)	

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

The aggregate market value of the voting and non-voting common equity of the registrant held by non-affiliates as of June 28, 2013 was $397,970,801.

Class of Common Stock	Outstanding at February 21, 2014
Common stock, $0.01 par value	29,717,601

DOCUMENTS INCORPORATED BY REFERENCE

Part III of this Form 10-K incorporates certain information by reference from registrant's definitive proxy statement for the 2014 annual meeting of stockholders, which proxy statement will be filed no later than 120 days after the close of the registrant's fiscal year ended December 31, 2013.

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Part I

Item 1. Business

Overview

Formed in 2006, PharMerica Corporation ("the Corporation," "we," "us," or "our"), a Delaware Corporation, is an institutional pharmacy services company that services healthcare facilities, provides pharmacy management services to hospitals, provides specialty infusion services to patients outside a hospital setting, and offers the only national oncology pharmacy in the United States. The Corporation is the second largest institutional pharmacy services company in the United States based on revenues and customer licensed beds under contract, operating 96 institutional pharmacies and 12 specialty infusion centers and 5 specialty oncology pharmacies in 45 states. The Corporation's customers are typically institutional healthcare providers, such as skilled nursing facilities, nursing centers, assisted living facilities, hospitals, individuals receiving in-home care and other long-term alternative care providers. The Corporation is generally the primary source of supply of pharmaceuticals to its customers. The Corporation also provides pharmacy management services to 83 hospitals in the United States.

Institutional Pharmacy Business

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

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

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

Hospital Pharmacy Management Services

We also provide hospital pharmacy management services. These services generally entail the overall management of the hospital pharmacy operations, including the ordering, receipt, storage, and dispensing of pharmaceuticals to the

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

Consultant Pharmacist Services

Federal and state regulations mandate that long-term care facilities, in addition to providing a source of pharmaceuticals, retain consultant pharmacist services to monitor and report on prescription drug therapy in order to maintain and improve the quality of resident care. On September 30, 2008, the United States Department of Health and Human Services Office of Inspector General ("OIG") published OIG Supplemental Compliance Program Guidance for Nursing Homes. With quality of care being the first risk area identified, the supplemental guidance is part of a series of recent government efforts focused on improving quality of care at

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skilled nursing and long-term care facilities. The guidance contains compliance recommendations and an expanded discussion of risk areas. The guidance stressed that facilities must provide pharmaceutical services to meet the needs of each resident and should be mindful of potential quality of care problems when implementing policies and procedures on proper medication management. It further stated that facilities can reduce risk by educating staff on medication management and improper pharmacy kickbacks for consultant pharmacists and that facilities should review the total compensation paid to consultant pharmacists to ensure it is not structured in a way that reflects the volume or value of particular drugs prescribed or administered to residents.

We provide consultant pharmacist services to approximately 70% of our patients serviced. The services offered by our consultant pharmacists include:

- Monthly reviews of each resident's drug regimen to assess the appropriateness and efficiency of drug therapies, including the review of medical records, monitoring drug interactions with other drugs or food, monitoring laboratory test results, and recommending alternative therapies;
- Participation on quality assurance and other committees of our customers, as required or requested by such customers;
- Monitoring and reporting on facility-wide drug utilization;
- Development and maintenance of pharmaceutical policy and procedure manuals; and
- Assistance with federal and state regulatory compliance pertaining to resident care.

Medical Records

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

- Real-time access to medication and treatment administration records, physician order sheets and psychotropic drug monitoring sheets;
- Online ordering to save time and resources;
- A customized database with the medication profiles of each resident's medication safety, efficiency and regulatory compliance;
- Web-based individual patient records detailing each prescribed medicine; and
- Electronic medical records to improve information to make it more legible and instantaneous.

Specialty Infusion Services

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

Specialty Oncology Pharmacy

We provide dispensing of oncology drugs, care management and other related services to patients, oncology practices, and hospitals. These services encompass drug procurement and delivery, inventory management, and prescription administration and coordination with the patient, oncology practice and payer. We procure oncology drugs from

manufacturers and wholesalers on behalf of oncologists and patients, handle administrative tasks related to prescription dispensing, distribute drugs directly to patients or to oncology practices, and are reimbursed by payers and patients. These services offer physicians an alternative to the traditional buy-and-bill distribution model, allowing them to outsource drug procurement, inventory management, and prescription administration.

Our Business Focus

Drive Scale Economies. We will focus on consistently providing quality pharmaceutical services to our customers at competitive prices and delivery of prescriptions in a timely and effective manner. Our business seeks to implement innovative and cost-effective solutions to improve the provision of medication to our customers and the residents and patients that they serve.

Focus on Organic Growth through New Sales and Client Retention. We aim to grow our business through expansion in our existing markets and by servicing new customers. We believe our industry has underlying market growth potential attributable to both an increase in drug utilization as well as the general aging population of the United States.

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Acquire Competitors. We also intend to expand our market share through selected geographic expansion in markets not currently served by us and through strategic acquisitions in existing and underserved markets. The Corporation currently operates in 45 states. We believe that there are growth opportunities in several other markets. There are numerous businesses in our markets, mostly small or regional companies that lack the scale that we believe will be necessary to ultimately compete in a market that is national in scope. We intend to actively seek opportunities to acquire companies. Since its formation in 2007, the Corporation has acquired twelve institutional pharmacy businesses, one specialty infusion services business and one specialty oncology pharmacy.

Sales and Marketing

We sell our products and services through a national sales force. Our sales force is organized along geographic lines to maximize coverage, manage costs, and align more effectively with our operating regions. Our sales representatives specialize in the products and services we offer and the markets in which we operate. Their knowledge permits us to meet the unique needs of our customers while maintaining profitable relationships.

Customers

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

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

During 2013, revenues from Kindred’s facilities represented approximately 9.2% of the Corporation’s total revenues. Kindred Healthcare did not renew the Corporation's contract for pharmacy services and the contract expired on December 31, 2013. As of January 1, 2014, we no longer provide pharmacy services to Kindred Healthcare.

Specialty Infusion Services. At December 31, 2013, the Corporation provided specialty infusion services to patients in 14 states with acute or chronic conditions in a setting outside of a hospital or nursing home.

Hospital Pharmacy Management Services. At December 31, 2013, the Corporation provided hospital pharmacy management services to Kindred and other customers at 83 locations. For the year ended December 31, 2013, revenues under the Kindred hospital pharmacy management service contracts represented approximately 3.3% of the Corporation’s total revenues.

Suppliers/Inventory

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

We seek to maintain an on-site inventory of pharmaceuticals and supplies to ensure prompt delivery to our customers. ABDC maintains local distribution facilities in most major geographic markets in which we operate. However, to take advantage of lower prices that can be realized by directly purchasing products from manufacturers, the Corporation implemented steps in 2013 to also establish our own distribution capabilities.

Brand versus Generic

The following table summarizes the Corporation's generic drug dispensing rate:

2011	2012	2013
79.6%	83.3%	83.4%

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The following table summarizes the material brand-to-generic conversions expected to occur in 2014 through 2017:

2014	2015	2016	2017
Avelox (1Q)	Lovaza (1Q)	Adviar Diskus (3Q)	Tamiflu (2Q)
Detrol LA (1Q)	Namenda (1Q)	Crestor (3Q)	
Evista (1Q)	Abilify (2Q)	Seroquel XR (4Q)	
Nuedexta (1Q)	Celebrex (2Q)	Zetia (4Q)	
Renegel (1Q)	Diovan (2Q)		
Renvela (1Q)	Zyvox (2Q)		
Xeloda (1Q)	Aggrenox (3Q)		
Actonel (2Q)	Gleevec (3Q)		
Copaxone (2Q)	Avodart (4Q)		
Nexium (2Q)	Patanol (4Q)		
Restasis (2Q)	Combivent (4Q)		
Travatan Z (4Q)			

Number in parentheses refers to
the quarter of conversion)

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

Supplier and Manufacturer Rebates

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

Information Technology

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

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

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Sources of Pharmacy Revenues

We receive payment for our services from third party payers, including Medicare Part D Plans, government reimbursement programs under Medicare and Medicaid, and non-government sources such as institutional healthcare providers, commercial insurance companies, health maintenance organizations, preferred provider organizations, private payers, and contracted providers. The sources and amounts of our revenues will be determined by a number of factors, including the mix of our customers' patients, brand to generic conversions and the rates and changes of reimbursement among payers. Changes in our customers' censuses, the case mix of the patients, brand and generic dispensing rates, and the payer mix among private pay, Medicare Part D, institutional healthcare providers, and Medicaid, will affect our profitability.

A summary of revenue by payer type for the years ended December 31, are as follows (dollars in millions):

	2011		2012		2013	
	Amount	% of Revenues	Amount	% of Revenues	Amount	% of Revenues
Medicare Part D	$998.1	48.0 %	$873.0	47.6 %	$813.7	46.3 %
Institutional healthcare providers	616.2	29.6	561.4	30.6	519.2	29.5
Medicaid	217.2	10.4	165.9	9.1	157.0	9.0
Private and other	92.7	4.5	84.7	4.6	77.2	4.4
Insured	90.0	4.3	79.5	4.3	113.0	6.4
Medicare	4.4	0.2	4.2	0.3	15.5	0.9
Hospital management fees	62.5	3.0	63.9	3.5	62.3	3.5
Total	$2,081.1	100.0 %	$1,832.6	100.0 %	$1,757.9	100.0 %

Competition

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

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

Patents, Trademarks and Licenses

We use a number of trademarks and service marks. All of the principal trademarks and service marks used in the course of our business have been registered in the United States or are the subject of pending applications for registration.

We have various proprietary products, processes, software and other intellectual property that are used either to facilitate the conduct of our business or that are made available as products or services to customers. We generally seek to protect such intellectual property through a combination of trade secret, patent and copyright laws and through confidentiality and other contractually imposed protections.

Although we believe that our products and processes do not infringe upon the intellectual property rights of any third parties, third parties may assert infringement claims against us from time to time.

Seasonality

Our largest customers in institutional pharmacy services are skilled nursing facilities. Both prescription and non-prescription drug sales at skilled nursing facilities are affected by the timing and severity of the cold/flu season and other seasonality of the long-term care facilities industry, however seasonality does not have a material effect on the Corporation's financial results.

Working Capital

For information about the Corporation's practices relating to working capital items, see Item 7 "Management's Discussion and Analysis of Financial Condition and Results of Operations—Liquidity and Capital Resources".

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Employees

As of December 31, 2013, we had approximately 5,800 employees which included approximately 1,100 part-time employees. The Corporation had approximately 400 employees that were covered by collective bargaining agreements as of December 31, 2013. These agreements expired on December 31, 2013, however the Corporation is awaiting determination from the National Labor Relations Board on certification of the union, once received we will proceed with negotiations. As of December 31, 2013, we employed approximately 1,700 licensed pharmacists. We believe that our relationships with our employees are good.

Government Regulation

General

Extensive federal, state and local regulations govern institutional pharmacies and the healthcare facilities that they serve. These regulations cover licenses, staffing qualifications, conduct of operations, reimbursement, recordkeeping and documentation requirements and the confidentiality and security of health-related information. Our institutional pharmacies are also subject to federal and state laws that regulate financial arrangements between healthcare providers, including the federal anti-kickback statutes and the federal physician self-referral laws.

Licensure, Certification and Regulation

States generally require that the state board of pharmacy license a pharmacy operating within the state. Many states also regulate out-of-state pharmacies that deliver prescription products to patients or residents in their states. We have the necessary pharmacy state licenses, or pending applications, for each pharmacy we operate. Our pharmacies are also registered with the appropriate federal and state authorities pursuant to statutes governing the regulation of controlled substances. In addition, pharmacists, nurses and other healthcare professionals who provide services on our behalf are in most cases required to obtain and maintain professional licenses and are subject to state regulation regarding professional standards of conduct.

The Drug Enforcement Agency (the “DEA”), the U.S. Food and Drug Administration (the “FDA”), and various state regulatory authorities regulate the distribution of pharmaceutical products and controlled substances. These laws impose a host of requirements on the pharmaceutical supply channel, including providers of institutional pharmacy services. Under the Comprehensive Drug Abuse Prevention and Control Act of 1970, as a dispenser of controlled substances, we must register with the DEA, file reports of inventories and transactions and provide adequate security measures. In addition, we are required to comply with all the relevant requirements of the Controlled Substances Act for the transfer and shipment of pharmaceuticals. The FDA, DEA, and state regulatory authorities have broad enforcement powers, including the ability to seize or recall products and impose significant criminal, civil and administrative sanctions for violations of these laws and regulations. We have received all necessary regulatory approvals and believe that our pharmacy operations are in substantial compliance with applicable federal and state good manufacturing practice requirements.

Client long-term care facilities are separately required to be licensed in the states in which they operate and, if serving Medicaid or Medicare patients, must be certified to be in compliance with applicable program participation requirements. Client facilities are also subject to the nursing home reforms of the Omnibus Budget Reconciliation Act of 1987, as amended, which imposed strict compliance standards relating to quality of care for facility operations, including vastly increased documentation and reporting requirements.

Laws Affecting Referrals and Business Practices

We are subject to federal and state laws that govern financial and other arrangements between healthcare providers. These laws prohibit certain direct and indirect payments or fee-splitting arrangements between healthcare providers that are designed to induce or encourage the referral of patients to, or the recommendation of, a particular provider for medical products and services. These laws include:

- the federal "anti-kickback" statute, which prohibits, among other things, knowingly or willfully soliciting, receiving, offering or paying remuneration "including any kickback, bribe or rebate" directly or indirectly in return for or to induce the referral of an individual to a person for the furnishing or arranging for the furnishing of any item or service for which payment may be made in whole or in part under Medicare, Medicaid or other federal healthcare programs; and
- the federal "Stark laws" which prohibit, with limited exceptions, the referral of patients by physicians for certain designated health services, to an entity with which the physician has a financial relationship.

These laws impact the relationships that we may have with potential referral sources. We have a variety of relationships with potential referral sources, including hospitals and skilled nursing facilities with which we have contracted to provide pharmacy services. With respect to the anti-kickback statute, the OIG has enacted safe harbor regulations that outline practices that are deemed protected from prosecution. While we endeavor to comply with the applicable safe harbors, certain of our current arrangements, none

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of which is material to us, may not qualify for safe harbor protection. Failure to meet a safe harbor does not mean that the arrangement necessarily violates the anti-kickback statute, but may subject the arrangement to greater scrutiny. In addition, as a means of providing guidance to healthcare providers, the OIG issues a variety of sub-regulatory guidance including Special Fraud Alerts, Special Advisory Bulletins, Advisory Opinions, and other compliance guidance documents. This guidance does not have the force of law, but identifies features of arrangements or transactions that may indicate that the arrangements or transactions violate the anti kickback statute or other federal health care laws. While we believe our practices comply with the anti-kickback statute, we cannot assure our practices that are outside of a safe harbor will not be found to violate the anti-kickback statute.

In addition to federal law, many states have enacted similar statutes that are not necessarily limited to items or services for which payment is made by federal healthcare programs. Violations of these laws may result in fines, imprisonment, denial of payment for services and exclusion from the Medicare and Medicaid programs and other state-funded programs.

Other provisions in the Social Security Act and in other federal and state laws authorize the imposition of penalties, including criminal and civil fines and exclusions from participation in Medicare, Medicaid and other federal healthcare programs for false claims, improper billing and other offenses. These laws include the federal False Claims Act, under which private parties have the right to bring “qui tam” whistleblower lawsuits against companies that submit false claims for payments to the government. Recent changes to the False Claims Act, expanding liability to certain additional parties and circumstances, may make these qui tam law lawsuits more prevalent. Some states have adopted similar state whistleblower and false claims laws.

In addition, a number of states have undertaken enforcement actions against pharmaceutical manufacturers involving pharmaceutical marketing programs, including looking at relationships with pharmacies and programs containing incentives for pharmacists to dispense one particular product rather than another. These enforcement actions arose under various state laws including fraud and abuse laws and consumer protection laws which generally prohibit false advertising, deceptive trade practices and the like.

In the ordinary course of business, we are regularly subject to inquiries, investigations and audits by federal and state agencies that oversee applicable healthcare program participation and payment regulations. We believe that the regulatory environment surrounding most segments of the healthcare industry remains intense. Federal and state governments continue to impose intensive enforcement policies resulting in a significant number of inspections, citations for regulatory deficiencies and other regulatory sanctions including demands for refund of overpayments, terminations from the Medicare and Medicaid programs, bars on Medicare and Medicaid payments and fines. Such sanctions could have a material adverse effect on our financial condition, results of operation and liquidity.

We believe our contract arrangements with other healthcare providers and our pharmaceutical suppliers and our pharmacy practices are in substantial compliance with applicable federal and state laws. These laws may, however, be interpreted in the future in a manner inconsistent with our interpretation and application.

State Laws Affecting Access to Services

Some states have enacted “freedom of choice” or “any willing provider” requirements as part of their state Medicaid programs or in separate legislation. These laws may preclude a nursing center from requiring their patients and residents to purchase pharmacy or other ancillary medical services or supplies from particular providers that have a supplier relationship with the nursing center. Limitations such as these may increase the competition which we face in providing services to nursing center residents.

HIPAA

The Federal Health Insurance Portability and Accountability Act of 1996, commonly known as "HIPAA," mandates the adoption of regulations aimed at standardizing transaction formats and billing codes for documenting medical services, dealing with claims submissions and protecting the privacy and security of individually identifiable health information. HIPAA regulations that standardize transactions and code sets require standard formatting for healthcare providers, like us, that submit claims electronically.

The HIPAA privacy regulations apply to "protected health information," or "PHI," which is defined generally as individually identifiable health information transmitted or maintained in any form or medium, excluding certain education records and student medical records. The privacy regulations seek to limit the use and disclosure of most paper and oral communications, as well as those in electronic form, regarding an individual's past, present or future physical or mental health or condition, or relating to the provision of healthcare to the individual or payment for that healthcare, if the individual can or may be identified by such information. HIPAA provides for the imposition of civil or criminal penalties if PHI is improperly disclosed.

HIPAA's security regulations require us to ensure the confidentiality, integrity and availability of all electronic protected health information that we create, receive, maintain or transmit. We must protect against reasonably anticipated threats or hazards to the security of such information and the unauthorized use or disclosure of such information.

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In addition to HIPAA, we are subject to state privacy laws and other state privacy or health information requirements not preempted by HIPAA, including those which may furnish greater privacy protection for individuals than HIPAA.

The scope of our operations involving health information is broad and the nature of those operations is complex. Although we believe that our contract arrangements with healthcare payers and providers and our business practices are in compliance with applicable federal and state electronic transmissions, privacy and security of health information laws, the requirements of these laws, including HIPAA, are complicated and are subject to interpretation. In addition, state regulation of matters also covered by HIPAA, especially the privacy standards, is increasing, and determining which state laws are preempted by HIPAA is a matter of interpretation. Failure to comply with HIPAA or similar state laws could subject us to loss of customers, denial of the right to conduct business, civil damages, fines, criminal penalties and other enforcement actions.

The Health Information Technology for Economic and Clinical Health Act ("HITECH"), part of the American Recovery and Reinvestment Act of 2009, changed several aspects of HIPAA including, without limitation, the following: (i) applies HIPAA security provisions and penalties directly to business associates of covered entities; (ii) requires certain notifications in the event of a security breach involving PHI; (iii) restricts certain unauthorized disclosures; (iv) changes the treatment of certain marketing activities; and (v) strengthens enforcement activities. In addition, the Secretary issued an interim final rule on August 24, 2009 that requires notifications for certain unpermitted disclosures of PHI. The final rule was issued on January 17, 2013.

2010 Health Care Reform Legislation

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

FUL and AMP Changes

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

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

In September 2011, CMS issued the first draft FUL reimbursement files for multiple source drugs, including the draft methodology used to calculate the FULs in accordance with the Health Care Legislation. CMS continues to release this monthly data and a three-month rolling average and is expected to do so going forward. CMS has not posted monthly AMPs for individual drugs, but only posted the weighted average of monthly AMPs in a FUL group and the calculation methodology.

On February 2, 2012, CMS issued proposed regulations further clarifying the AMP and FUL changes described above. CMS has since indicated that the final rule will be issued in July 2014.

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

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Part D Coverage Gap

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

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

Short Cycle Dispensing

Pursuant to the 2010 Health Care Reform Legislation, Prescription Drug Plans ("PDPs") are required, under Medicare Part D and Medicare Advantage prescription drug plans ("Medicare Advantage" or "MAPDs") to utilize specific, uniform dispensing techniques, such as weekly, daily, or automated dose dispensing, when dispensing covered Medicare Part D drugs to beneficiaries who reside in a long-term care facility to reduce waste associated with 30 to 90 day prescriptions for such beneficiaries. Pursuant to CMS issued regulation, beginning January 1, 2013, pharmacies dispensing to long-term care facilities must dispense no more than 14-day supplies of brand-name oral solid medications covered by Medicare Part D. The Corporation fully implemented short cycle dispensing on January 1, 2013. Additionally, in January 2014, CMS issued a proposed rule entitled "Medicare Program; Contract Year 2015 Policy and Technical Changes to the Medicare Advantage and the Medicare Prescription Drug Benefit Programs" (the "Proposed Rule"). The Proposed Rule prohibits a Plan Sponsor from penalizing a long-term care pharmacy for selecting efficient dispensing techniques. For example, under the Proposed Rule, the Plan Sponsor could not prorate dispensing fees based on days' supply or quantity dispensed. The impact of short cycle dispensing has not had a material adverse impact on the Corporation's results of operations.

Medicare Part D Proposed Changes

In the Proposed Rule, CMS clarifies the meaning of drug categories and classes of clinical concern for which all Part D drugs therein must be included on Part D sponsor formularies, subject to certain exceptions. CMS establishes criteria for determining which categories or classes of drugs are protected and states that anticonvulsants, antineoplastics, and antiretrovirals meet the criteria, while antidepressants, antipsychotics, and immunosuppressants do not. However, CMS defers any change in formulary requirements for the antipsychotic class and continues to require all drugs from within that class to be on Part D formularies in 2015.

In the Proposed Rule, CMS also proposes to require physicians and eligible professionals to enroll in the Medicare program in order to prescribe covered Part D drugs. CMS proposes that a prescriber or eligible professional of Part D drugs must have either an approved enrollment record in the Medicare fee-for-service program or a valid opt-out affidavit on file with a Part A or Part B Medicare Administrative Contractor for a prescription written by a prescriber to be eligible for coverage under the Part D program. Until CMS issues final guidance, the Corporation is unable to evaluate the full impact of these proposed changes to drug categories and classes and prescriber enrollment requirements on its business.

Overview of Reimbursement

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

Medicare and Medicaid.

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

Medicare

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

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Part A

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

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

Part B

The MMA also changed the Medicare payment methodology and conditions for coverage of certain items of durable medical equipment, prosthetics, orthotics, and supplies ("DMEPOS") under Medicare Part B. The Corporation provides some of these products to its customers. The changes include, among other things, a new competitive bidding program for selected supplies, under which only suppliers that were winning bidders are eligible to provide services, at prices established as a result of the competitive bids, to Medicare beneficiaries. The competitive bidding is occurring for selected areas of the country in successive phases, with all areas of the country to be subject to either competitive bidding or rate adjustment using competitively bid rates by 2016. Enteral nutrients, equipment and supplies, oxygen equipment, hospital beds, walkers, negative pressure wound therapy pumps and supplies are among the 10 categories of DMEPOS included in the competitive bidding process. The Corporation submitted, and was awarded, competitive bids in certain geographic areas. Amounts paid under the competitive bidding program are expected to be significantly lower than the prior Medicare fee schedule rates. Medicare Part B is not material to the Corporation, representing 0.9% of revenues.

Part D

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

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

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

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

In addition, we receive rebates from pharmaceutical manufacturers for undertaking certain activities that the manufacturers believe may increase the likelihood that we will dispense their products. CMS continues to question whether institutional pharmacies should be permitted to receive these access/performance rebates from manufacturers with respect to prescriptions covered under Medicare Part D, but has not prohibited the receipt of such rebates. CMS defines these as rebates a manufacturer provides to long-term care pharmacies that are designed to "prefer, protect, or maintain" that manufacturer's product selection by the long-term care pharmacy or to increase the volume of that manufacturer's products that are dispensed by the pharmacy under its formulary. CMS, in 2007, required PDPs to have policies and systems in place as part of their drug utilization management programs to protect

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beneficiaries and reduce costs when long-term care pharmacies receive incentives to move market share through access/performance rebates. The elimination or substantial reduction of manufacturer rebates, if not offset by other reimbursement, would have a material adverse effect on our business.

Medicaid

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

Environmental Matters

In operating our facilities, historically we have not encountered any material difficulties effecting compliance with applicable pollution control laws. No material capital expenditures for environmental control facilities are expected. While we cannot predict the effect which any future legislation, regulations or interpretations may have upon our operations, we do not anticipate any changes regarding pollution control laws that would have a material adverse impact on the Corporation.

Available Information

We make available free of charge on or through our web site, at www.pharmerica.com, our annual reports on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K and all amendments to those reports as soon as reasonably practicable after such material is electronically filed with the Securities and Exchange Commission ("SEC"). Additionally, the public may read and copy any materials we file with the SEC at the SEC's Public Reference Room at 100 F Street, NE, Room 1580, Washington, D.C., 20549. Information regarding operation of the Public Reference Room is available by calling the SEC at 1-800-SEC-0330. Information that we file with the SEC is also available at the SEC's web site at www.sec.gov.

Our SEC filings are available to the public through the New York Stock Exchange ("NYSE"), 20 Broad Street, New York, New York, 10005. Our Common Stock is listed on the NYSE and trades under the symbol "PMC".

The certifications of our Chief Executive Officer and Chief Financial Officer required under Section 302 of the Sarbanes-Oxley Act have been filed as Exhibits 31.1 and 31.2 to this Annual Report on Form 10-K.

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Item 1A. Risk Factors

You should consider carefully the risks described below, together with all of the other information, in evaluating our company and our common stock. If any of the risks described below actually occur, it could have a material adverse effect on our business, results of operations, financial condition and stock price.

Risk Factors Relating to Our Business

Financial soundness of our customers and suppliers may adversely affect our results of operations.

If our customers' operating and financial performance deteriorates, or if they are unable to make scheduled payments or obtain credit, our customers may not be able to pay, or may delay payment of accounts receivable owed to us. Any inability of customers to pay us for our products and services may adversely affect our earnings and cash flow. Additionally, both state and federal government sponsored payers, as a result of budget deficits or reductions, may seek to reduce their healthcare expenditures resulting in the long-term care customers renegotiating their contracts with us. Any reduction in payments by such government sponsored payers may adversely affect our earnings and cash flow. Also some of customers' real estate is owned by Real Estate Investment Trusts limiting their ability to renegotiate rental costs furthering their desire to reduce other controllable costs, such as pharmacy costs.

Intense competition may erode our profit margins.

The distribution of pharmaceuticals to healthcare facilities is highly competitive. In each geographic market, there are national, regional and local institutional pharmacies and numerous local retail pharmacies, which provide services comparable to those offered by our pharmacies and may be more established in the markets they serve than we are. We also compete against regional and local pharmacies that specialize in long-term care. Many of our competitors have equal or greater resources and access to capital than the Corporation. In addition, local pharmacies have strong personal relationships with their customers. Because relatively few barriers to entry exist in the local markets we serve, we may encounter substantial competition from local market entrants. In addition, owners of skilled nursing facilities, including prior and current customers, are also entering the institutional pharmacy market, particularly in areas of their geographic concentration. Consolidation within the institutional pharmacy industry may also lead to increased competition. Competitive pricing pressures may adversely affect our earnings and cash flow.

We compete based on innovation and service as well as price. To attract new clients and retain existing clients, we must continually meet service expectations of our clients and customers. We cannot be sure that we will continue to remain competitive with the service to our clients at our current levels of profitability.

If we lose relationships with one or more key pharmaceutical manufacturers or if the payments made or discounts provided by pharmaceutical manufacturers decline, our business and financial results could be adversely affected.

We maintain contractual relationships with numerous pharmaceutical manufacturers that may provide us with, among other things:

- discounts for drugs we purchase to be dispensed from our institutional pharmacies;
- rebates based upon distributions of drugs from our institutional pharmacies; and
- administrative fees for managing rebate programs.

If several of these contractual relationships are terminated or materially altered by the pharmaceutical manufacturers, our business and financial results could be materially adversely affected. In addition, formulary fee programs have been the subject of debate in federal and state legislatures and various other public and governmental forums. Changes in existing laws or regulations or in interpretations of existing laws or regulations or the adoption of new laws or

regulations relating to any of these programs may materially adversely affect our business.

CMS has questioned whether long-term care pharmacies should be permitted to receive discounts, rebates and other price concessions from pharmaceutical manufacturers with respect to prescriptions covered under the Medicare Part D benefit. Our business would be adversely affected if CMS should take any action that has the effect of eliminating or significantly reducing the rebates that we receive from pharmaceutical manufacturers.

Our operating revenue and profitability may suffer upon the occurrence of the loss of certain customers.

We have a number of customers that own or operate numerous facilities in our institutional pharmacy business. In addition, our hospital business revenues are primarily derived from one large multi-facility customer. If we are not able to continue these relationships or are only able to continue these relationships on less favorable terms than the ones currently in place, our operating revenues and results of operations would be materially impacted. There can be no assurance that these customers will not terminate all or a portion of their contracts with the Corporation.

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Home infusion joint ventures formed with hospitals could adversely affect our financial results.

The home infusion industry is currently seeing renewed activity in the formation of equity-based infusion joint ventures formed with hospitals. This activity stems, in part, from hospitals seeking to position themselves for new paradigms in the delivery of coordinated healthcare and new methods of payment, including an emerging interdisciplinary care model that is being labeled an “accountable care organization”. These organizations are encouraged by the 2010 Health Care Reform Legislation. These entities are being designed in order to save money and improve quality of care by better integrating care, with the healthcare provider possibly sharing in the financial benefits of the improved efficiency.

Participation in equity-based joint ventures offers hospitals and other providers an opportunity to more efficiently transfer patients to less expensive care settings, while keeping the patient within its network. Additionally, it provides many hospitals with a mechanism to invest accumulated profits in a growing sector with attractive margins.

If home infusion joint ventures continue to expand and we lose referrals as a result, our financial condition, results of operations and liquidity could be adversely affected.

Our operating revenue and profitability may suffer because of an increase in our generic dispensing rate.

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

If we fail to comply with complex and rapidly evolving laws and regulations, we could suffer penalties, be required to pay substantial damages or make significant changes to our operations.

We are subject to numerous federal and state regulations. If we fail to comply with existing or future applicable laws and regulations, we could suffer civil or criminal penalties, including the loss of our licenses to operate our institutional pharmacies and our ability to participate in federal and state healthcare programs. As a consequence of the severe penalties we could face, we must devote significant operational and managerial resources to complying with these laws and regulations. Although we believe that we are substantially compliant with all existing statutes and regulations applicable to our business, different interpretations and enforcement policies of these laws and regulations could subject our current practices to allegations of impropriety or illegality, or could require us to make significant changes to our operations. In addition, we cannot predict the impact of future legislation and regulatory changes on our business or assure that we will be able to obtain or maintain the regulatory approvals required to operate our business.

As a result of political, economic, and regulatory influences, the healthcare delivery industry in the United States is under intense scrutiny and subject to fundamental changes. We cannot predict which reform proposals will be adopted, when they may be adopted, or what impact they may have on us.

The costs associated with complying with federal and state regulations could be significant and the failure to comply with any such legal requirements could have a material adverse effect on our financial condition, results of operations, and liquidity.

Pharmaceutical products can develop unexpected safety or efficacy concerns.

Unexpected safety or efficacy concerns can arise with respect to marketed products, whether or not scientifically justified, leading to product recalls, withdrawals or declining sales. If we fail to or do not promptly withdraw pharmaceutical products upon a recall by a drug manufacturer, our business and results of operations could be negatively impacted.

Legal and regulatory changes reducing reimbursement rates for pharmaceuticals and/or medical treatments or services may reduce our profitability.

Both our own profit margins and the profit margins of our customers may be adversely affected by laws and regulations reducing reimbursement rates and charges. The sources and amounts of our revenues are determined by a number of factors, including licensed bed capacity and occupancy rates of our customers, the number of drugs administered to patients, the mix of pharmaceuticals

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dispensed, whether the drugs are brand or generic, and the rates of reimbursement among payers. Changes in the number of drugs administered to patients, as well as payer mix among private pay, Medicare and Medicaid, in our customers' facilities will significantly affect our earnings and cash flow.

Further modifications to the Medicare Part D program may reduce revenue and impose additional costs to the industry.

The Medicare Prescription Drug Improvement and Modernization Act of 2003 or MMA included a major expansion of the Medicare program with the addition of a prescription drug benefit under the new Medicare Part D program. The continued impact of these regulations depends upon a variety of factors, including our ongoing relationships with the Part D Plans and the patient mix of our customers. Future modifications to the Medicare Part D program may reduce revenue and impose additional costs to the industry. In addition, we cannot assure you that Medicare Part D and the regulations promulgated under Medicare Part D will not have a material adverse effect on our institutional pharmacy business.

Possible changes in, or our failure to satisfy our manufacturers' rebate programs could adversely affect our results of operations.

There can be no assurance that pharmaceutical manufacturers will continue to offer these rebates or that they will not change the terms upon which rebates are offered. A decrease in prescription volumes dispensed or a decrease in the number of brand or generic drugs which participate in rebate programs and are used by the geriatric population could affect our ability to satisfy our manufacturers' rebate programs. The termination of such programs or our failure to satisfy the criterion for earning rebates may have an adverse affect on our cost of goods sold, financial condition, results of operations and liquidity.

Changes in Medicaid reimbursement may reduce our revenue.

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

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

In September 2011, CMS issued the first draft FUL reimbursement files for multiple source drugs, including the draft methodology used to calculate the FULs in accordance with the Health Care Legislation.CMS continues to release monthly data and a three-month rolling average and is expected to do so going forward. CMS has not posted monthly AMPs for individual drugs, but only posted the weighted average of monthly AMPs in a FUL group and the calculation methodology.

On February 2, 2012, CMS issued a proposed regulation further clarifying the AMP and FUL changes described above. CMS has indicated that the final rule will be issued in July 2014.

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

Adverse results in material litigation matters or governmental inquiries could have a material adverse effect upon the Corporation’s business.

The Corporation may from time to time become subject in the ordinary course of business to material legal action related to, among other things, intellectual property disputes, professional liability and employee-related matters, as well as inquiries from governmental agencies and Medicare or Medicaid carriers requesting comment and information on allegations of billing irregularities and other matters that are brought to their attention through billing audits, third parties or other sources. The healthcare industry is subject to substantial federal and state government regulation and audit. Legal actions could result in substantial monetary damages as well as damage to the Corporation’s reputation with customers, which could have a material adverse effect upon our financial condition, results of operations, and liquidity.

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If we or our customers fail to comply with Medicare and Medicaid regulations, we may be subjected to penalties or loss of eligibility to participate in these programs.

The Medicare and Medicaid programs are highly regulated. These programs are also subject to frequent and substantial changes. If we or our customers' facilities fail to comply with applicable reimbursement laws and regulations, whether purposely or inadvertently, our reimbursement under these programs could be curtailed or reduced and our eligibility to continue to participate in these programs could be adversely affected. Federal or state governments may also impose other penalties on us for failure to comply with the applicable reimbursement regulations. Failure by our customers to comply with these or future laws and regulations could result in our inability to provide pharmacy services to these customers and their residents. We do not believe that we have taken any actions that could subject us to material penalties under these rules and regulations.

Among these laws is the federal anti-kickback statute. This statute prohibits anyone from knowingly and willfully soliciting, receiving, offering or paying any remuneration with the intent to refer, or to arrange for the referral or order of, services or items payable under a federal healthcare program. Courts have interpreted this statute broadly. Violations of the anti-kickback statute may be punished by a criminal fine of up to $25,000 for each violation or imprisonment, civil money penalties of up to $50,000 per violation and damages of up to three times the total amount of the remuneration and/or exclusion from participation in federal healthcare programs, including Medicare and Medicaid. This law impacts the relationships that we may have with potential referral sources. We have a variety of relationships with potential referral sources, including hospitals and skilled nursing facilities with which we have contracted to provide pharmacy services. The OIG, among other regulatory agencies, is responsible for identifying and eliminating fraud, abuse or waste. The OIG carries out this responsibility through a nationwide program of audits, investigations and inspections. The OIG has promulgated safe harbor regulations that outline practices that are deemed protected from prosecution under the anti-kickback statute. While we endeavor to comply with the applicable safe harbors, certain of our current arrangements may not qualify for safe harbor protection. Failure to meet a safe harbor does not mean that the arrangement necessarily violates the anti-kickback statute, but may subject the arrangement to greater scrutiny. It cannot be assured that practices outside of a safe harbor will not be found to violate the anti-kickback statute.

The anti-kickback statute and similar state laws and regulations are expansive. We do not always have the benefit of significant regulatory or judicial interpretation of these laws and regulations. In the future, different interpretations or enforcement of these laws and regulations could subject our current or past practices to allegations of impropriety or illegality, or could require us to make changes in our facilities, equipment, personnel, services, capital expenditure programs and operating expenses. A determination that we have violated these laws, or the public announcement that we are being investigated for possible violations of these laws, could have a material adverse effect on our business, financial condition, results of operations or prospects and our business reputation could suffer significantly. If we fail to comply with the anti-kickback statute or other applicable laws and regulations, we could be subjected to liabilities, including criminal penalties, civil penalties (including the loss of our licenses to operate one or more facilities), and exclusion of one or more facilities from participation in the Medicare, Medicaid and other federal and state healthcare programs. In addition, we are unable to predict whether other legislation or regulations at the federal or state level will be adopted, what form such legislation or regulations may take or their impact.

Continuing government and private efforts to contain healthcare costs may reduce our future revenue.

We could be adversely affected by the continuing efforts of government and private payers to contain healthcare costs. To reduce healthcare costs, payers seek to lower reimbursement rates, limit the scope of covered services and negotiate reduced or capped pricing arrangements. While many of the proposed policy changes would require congressional approval to implement, we cannot assure you that reimbursement payments under governmental and private third party payer programs will remain at levels comparable to present levels or will be sufficient to cover the costs allocable to patients eligible for reimbursement under these programs. Any changes that lower reimbursement

rates under Medicare, Medicaid or private pay programs could result in a substantial reduction in our net operating revenues. Our operating margins may continue to be under pressure because of deterioration in reimbursement, changes in payer mix and growth in operating expenses in excess of increases, if any, in payments by third party payers.

Healthcare reform could adversely affect the liquidity of our customers which would have an adverse effect on their ability to make timely payments to us for our products and services.

Healthcare reform and legislation may have an adverse effect on our business through decreasing funds available to our customers. Limitations or restrictions on Medicare and Medicaid payments to our customers could adversely impact the liquidity of our customers, resulting in their inability to pay us, or to timely pay us, for our products and services. This inability could have a material adverse effect on our financial condition, results of operations, and liquidity.

The changing U.S. healthcare industry and increasing enforcement environment may negatively impact our business.

Our products and services are part of the structure of the healthcare financing and reimbursement system currently existing in the United States. In recent years, the healthcare industry has undergone significant changes in an effort to reduce costs and

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government spending. These changes include an increased reliance on managed care, cuts in Medicare funding affecting our healthcare provider customer base and consolidation of competitors, suppliers and customers.

We expect the healthcare industry to continue to change significantly in the future. Some of these potential changes, such as a reduction in governmental support of healthcare services or adverse changes in legislation or regulations governing prescription drug pricing, healthcare services or mandated benefits, may cause healthcare providers to reduce the amount of our products and services they purchase or the price they are willing to pay for our products and services. If we are unable to adjust to changes in the healthcare environment, it could have a material adverse effect on our financial condition, results of operations and liquidity.

Further, both federal and state government agencies have increased their focus on and coordination of civil and criminal enforcement efforts in the healthcare area. The OIG and the U.S. Department of Justice have, from time to time, established national enforcement initiatives, targeting all providers of a particular type, that focus on specific billing practices or other suspected areas of abuse. In addition, under the federal False Claims Act, private parties have the right to bring “qui tam” whistleblower lawsuits against companies that submit false claims for payments to the government. A number of states have adopted similar state whistleblower and false claims provisions. We do not believe that we have taken any actions that could subject us to material penalties under these provisions.

Further consolidation of managed care organizations and other third-party payers may adversely affect our profits.

Managed care organizations and other third-party payers have continued to consolidate in order to enhance their ability to influence the delivery of healthcare services. Consequently, the healthcare needs of a large percentage of the U.S. population are increasingly served by a small number of managed care organizations. These organizations generally enter into service agreements with a limited number of providers for needed services. In addition, private payers, including managed care payers, increasingly are demanding discounted fee structures. To the extent that these organizations terminate us as a preferred provider, engage our competitors as a preferred or exclusive provider or demand discounted fee structures, our liquidity and results of operations could be materially and adversely affected.

If we or our customers fail to comply with licensure requirements, laws and regulations in respect of healthcare fraud or other applicable laws and regulations, we could suffer penalties or be required to make significant changes to our operations.

Our pharmacies must be licensed by the state board of pharmacy in the state in which they operate. Many states also regulate out-of-state pharmacies that are delivering prescription products to patients or residents in their states. The failure to obtain or renew any required regulatory approvals or licenses could adversely impact the operation of our business. In addition, the healthcare facilities we service are also subject to extensive federal, state and local regulations and are required to be licensed in the states in which they are located. The failure by these healthcare facilities to comply with these or future regulations or to obtain or renew any required licenses could result in our inability to provide pharmacy services to these facilities and their residents and could have a material adverse effect on our financial condition, results of operations and liquidity.

While we believe that we are in substantial compliance with all applicable laws, many of the regulations applicable to us, including those relating to marketing incentives offered by pharmaceutical suppliers, and rebates paid by pharmaceutical manufacturers are vague or indefinite and have not been interpreted by the courts. They may be interpreted or applied by a prosecutorial, regulatory or judicial authority in a manner that could require us to make changes in our operations. These changes may be material and may require the expenditure of material funds to implement. We believe that the regulatory environment surrounding most segments of the healthcare industry remains intense. Federal and state governments continue to impose intensive enforcement policies resulting in a significant number of inspections, citations of regulatory deficiencies and other regulatory sanctions including demands for refund of overpayments, terminations from the Medicare and Medicaid programs, bans on Medicare and Medicaid

payments and fines. If we or our customers fail to comply with the extensive applicable laws and 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 regardless of whether we have actually been involved in any violations or wrong-doing.

Federal and state medical privacy regulations may increase the costs of operations and expose us to civil and criminal sanctions.

We must comply with extensive federal and state requirements regarding the transmission and retention of health information. The Health Insurance Portability and Accountability Act of 1996 and its implementing regulations, referred to as HIPAA, was enacted to ensure that employees can retain and at times transfer their health insurance when they change jobs, to enhance the privacy and security of personal health information and to simplify healthcare administrative processes. HIPAA requires the adoption of standards for the exchange of electronic health information.

The Health Information Technology for Economic and Clinical Health Act (“HITECH”), part of the American Recovery and Reinvestment Act of 2009, changed several aspects of HIPAA including, without limitation, the following: (i) applies HIPAA security

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provisions and penalties directly to business associates of covered entities; (ii) requires certain notifications in the event of a security breach involving PHI; (iii) restricts certain unauthorized disclosures; (iv) changes the treatment of certain marketing activities; and (v) strengthens enforcement activities. In addition, the Secretary issued an interim final rule on August 24, 2009 that requires notifications for certain unpermitted disclosures of PHI. The final rule was issued on January 17, 2013.

Failure to comply with either HIPAA or HITECH could result in fines and penalties that could have a material adverse effect on our results of operations, financial condition, and liquidity.

Acquisitions, investments and strategic alliances that we have made or may make in the future may use significant resources, may be unsuccessful and could expose us to unforeseen liabilities.

We have made and anticipate that we may continue to make acquisitions of, investments in and strategic alliances with complementary businesses to enable us to capitalize on our position in the geographic markets in which we operate and to expand our businesses in new geographic markets. At any particular time, we may be in various stages of assessment, discussion and negotiation with regard to one or more potential acquisitions, investments or strategic alliances, not all of which, if any, will be consummated. Our acquisition program and strategy has and may lead us to contemplate acquisitions of companies in bankruptcy or financial distress, all of which entail additional risks and uncertainties. Such risks and uncertainties include, without limitation, that, before assets may be acquired, customers may leave in search of more stable providers and vendors may terminate key relationships. Also, assets are generally acquired on an “as is” basis, with no recourse to the seller if the assets are not as valuable as may be represented. Finally, while bankrupt companies may be acquired for comparatively little money, the cost of continuing the operations may significantly exceed expectations. Our growth plans rely, in part, on the successful completion of future acquisitions. If we are unsuccessful, our business would suffer.

We intend to make public disclosure of pending and completed acquisitions when appropriate or required by applicable securities laws and regulations. Acquisitions may involve significant cash expenditures, debt incurrence, additional operating losses, amortization of certain intangible assets of acquired companies, and expenses that could have a material adverse effect on our financial condition, results of operations and liquidity. Acquisitions involve numerous risks and uncertainties, including, without limitation:

- difficulties integrating acquired operations, personnel and information systems, or in realizing projected efficiencies and cost savings;
- diversion of management’s time from existing operations;
- potential loss of key employees or customers of acquired companies;
- inaccurate assessment of assets and liabilities and exposure to undisclosed or unforeseen liabilities of acquired companies, including liabilities for failure to comply with healthcare laws;
- increases in our indebtedness and a limitation on our ability to access additional capital when needed; and
- failure to operate acquired facilities profitably or to achieve improvements in their financial performance.

Risks generally associated with our sophisticated information systems may adversely affect our results of operations.

We rely on sophisticated information systems in our business to obtain, rapidly process, analyze, and manage data to facilitate the dispensing of prescription and non-prescription pharmaceuticals in accordance with physician orders and deliver those medications to patients and long-term care residents on a timely basis; to manage the accurate billing and collections for thousands of customers; and to process payments to suppliers. Our business and results of operations may be materially adversely affected if these systems are interrupted or damaged or if they fail for an extended period of time. Significant disruptions to our infrastructure or any of our facilities due to failure of technology or some other catastrophic event could adversely impact our business.

We purchase a significant portion of our pharmaceutical products from one supplier—AmerisourceBergen.

We are required to purchase a substantial amount of our pharmaceutical products from AmerisourceBergen, pursuant to the Amended Prime Vendor Agreement. If AmerisourceBergen fails to deliver products in accordance with the Amended Prime Vendor Agreement, there can be no assurance that our operations would not be disrupted or that we could obtain the products at similar cost or at all. In this event, failure to satisfy our customers' requirements would result in defaults under these customer contracts subjecting us to damages and the potential termination of those contracts. Such events could have a material adverse effect on our financial condition, results of operations and liquidity. In addition, under the terms of the Amended Prime Vendor Agreement by and between ABDC, a wholly owned subsidiary of AmerisoureBergen Corporation, the Corporation, Pharmacy Corporation of America and Chem Rx Pharmacy Services, LLC, entered into on January 4, 2011, (the "Amended Prime Vendor Agreement"), we are limited in our ability to negotiate potentially better pricing and other terms with other drug distributors, which could negatively impact our competitive position.

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Prescription volumes may decline, and our net revenues and profitability may be negatively impacted, if products are withdrawn from the market or if increased safety risk profiles of specific drugs result in utilization decreases.

We dispense significant volumes of drugs from our pharmacies. These volumes are the basis for our net revenues and profitability. When increased safety risk profiles of specific drugs or classes of drugs result in utilization decreases, physicians may cease writing or reduce the numbers of prescriptions written for these drugs. Additionally, negative press regarding drugs with higher safety risk profiles may result in reduced consumer demand for such drugs. On occasion, products are withdrawn by their manufacturers. In cases where there are no acceptable prescription drug equivalents or alternatives for these prescription drugs, our volumes, net revenues, profitability and cash flows may decline.

We could be required to record a material non-cash charge to income if our recorded goodwill or intangible assets are impaired, or if we shorten intangible asset useful lives.

We have $282.6 million of goodwill and $135.9 million of recorded intangible assets on our consolidated balance sheet as of December 31, 2013. Our intangible assets primarily represent the value of client relationships that were recorded from past acquisitions. Under current accounting rules, intangible assets are amortized over their useful lives. These assets may become impaired with the loss of significant clients. If the carrying amount of the assets exceeds the undiscounted pre-tax expected future cash flows from the lowest appropriate asset grouping, we would be required to record a non-cash impairment charge to our consolidated income statements in the amount the carrying value of these assets exceeds its fair value. In addition, while the intangible assets may not be impaired, the useful lives are subject to continual assessment, taking into account historical and expected losses of relationships that were in the base at time of acquisition. This assessment may result in a reduction of the remaining weighted average useful life of these assets, resulting in potentially significant increases to non-cash amortization expense that is charged to our consolidated income statements. A goodwill or intangible asset impairment charge, or a reduction of useful lives, could have a material effect on our results of operations.

We are highly dependent on our senior management team and our pharmacy professionals.

We are highly dependent upon the members of our senior management and our pharmacists and other pharmacy professionals. Our business is managed by a small number of senior management personnel. If we were unable to retain these persons, we might be materially adversely affected due to the limited pool of senior management personnel with significant experience in our industry. Accordingly, we believe we could experience significant difficulty in replacing key management personnel. We expect that any employment contracts we enter into with our key management personnel will be subject to termination without cause by either party. Moreover, although the majority of the members of our senior management team have significant experience in the industry, they will need time to fully assess and understand our business and operations. We can offer no assurance how long these members of senior management will choose to remain with us.

In addition, our continued success depends on our ability to attract and retain pharmacists and other pharmacy professionals. Competition for qualified pharmacists and other pharmacy professionals is intense. The loss of pharmacy personnel or the inability to attract or retain sufficient numbers of qualified pharmacy professionals could adversely affect our business. Although we generally have been able to meet our staffing requirements for pharmacists and other pharmacy professionals, our inability to do so in the future could have a material adverse effect on our financial condition, results of operations and liquidity.

Our revenues and volume trends may be adversely affected by certain factors relevant to the markets in which we have pharmacies, including weather conditions and other natural disasters.

Our revenues and volume trends will be predicated on many factors, including physicians' pharmaceutical decisions on patients, payer programs, seasonal and severe weather conditions including the effects of extreme low temperatures, hurricanes and tornadoes, earthquakes, current local economic and demographic changes. Any of these factors could have a material adverse effect on our revenues and volume trends, and many of these factors will not be within the control of our management. These factors may also have an effect on our customers and their ability to continue to operate. For further discussion, see Note 9.

There are inherent uncertainties involved in estimates, judgments, and assumptions used in the determination of our litigation-related accruals and the preparation of financial statements in accordance with generally accepted accounting principles in the United States (U.S. GAAP). Any changes in estimates, judgments, and assumptions could have a material adverse effect on the Company's financial position, results of operations, or cash flows.

Our financial statements filed with the SEC are prepared in accordance with U.S. GAAP, and the preparation of such financial statements includes making estimates, judgments, and assumptions that affect reported amounts of assets, liabilities, and related reserves, revenues, expenses, and income. We evaluate our exposure to legal proceedings and establish reserves for the estimated liabilities in accordance with GAAP. Assessing and predicting the outcome of these matters involves substantial uncertainties. Unexpected outcomes in these legal proceedings, or changes in management's evaluations or predictions and accompanying changes in established reserves, could have a material adverse impact on our financial results. Estimates are inherently subject to change in the

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future, and such changes could result in corresponding changes to the amounts of assets, liabilities, income, or expenses and likewise could have an adverse effect on our financial position, results of operations, or cash flows.

Risk Factors Relating to Ownership of Our Common Stock and Our Senior Secured Credit Facility

Certain provisions of our certificate of incorporation and bylaws and provisions of Delaware law could delay or prevent a change of control that stockholders favor.

Provisions of our certificate of incorporation and bylaws may discourage, delay or prevent a merger or other change of control that stockholders may consider favorable or may impede the ability of the holders of our common stock to change our management and Board of Directors. The provisions of our certificate of incorporation and bylaws, among other things:

- prohibit stockholder action except at an annual or special meeting. Specifically, this means our stockholders are unable to act by written consent;
- regulate how stockholders may present proposals or nominate directors for election at annual meetings of stockholders. Advance notice of such proposals or nominations is required;
- regulate how special meetings of stockholders may be called. Our stockholders do not have the right to call special meetings;
- authorize our board of directors to issue preferred stock in one or more series, without stockholder approval. Under this authority, our Board of Directors adopted the Rights Agreement which could ensure continuity of management by rendering it more difficult for a potential acquirer to obtain control of us; and
- require an affirmative vote of the holders of three-quarters or more of the combined voting power of our common stock entitled to vote in the election of our directors in order for the stockholders to amend our bylaws.

In addition, because we have not chosen to be exempt from Section 203 of the Delaware General Corporation Law ("DGCL"), this provision could also delay or prevent a change of control that some stockholders may view as favorable. Section 203 provides that unless board and/or stockholder approval is obtained pursuant to the requirements of the statute, persons that acquire, or are affiliated with a person that acquires, more than 15% of the outstanding voting stock of a Delaware corporation shall not engage in any business combination with that corporation, including by merger, consolidation or acquisitions of additional shares, for a three-year period following the date on which that person or its affiliate becomes the holder of more than 15% of the corporation's outstanding voting stock.

The market price and trading volume of our common stock may be volatile.

The market price of our common stock could fluctuate significantly for many reasons, including, without limitation the following:

- as a result of the risk factors listed in this document;
- actual or anticipated fluctuations in our results of operations;
- for reasons unrelated to our specific performance, such as reports by industry analysts, investor perceptions, or negative announcements by our customers or competitors regarding their own performance;
- regulatory changes that could impact our business or that of our customers; and
- general economic and industry conditions.

In addition, when the market price of a company's common stock drops significantly, stockholders often institute securities class action lawsuits against the company. A lawsuit against us could cause us to incur substantial costs and could divert the time and attention of our management and other resources.

Acquisitions, investments and strategic alliances we may make in the future may need to be financed by borrowings under the Credit Agreement for which funds may not be made available by certain participants.

We have made and anticipate that we may continue to make acquisitions of, investments in and strategic alliances with complementary businesses to enable us to capitalize on our position in the geographic markets in which we operate and to expand our business in new geographic markets. Our growth plans rely, in part, on the successful completion of future acquisitions. At any particular time, we may need to finance such acquisitions and strategic alliances with borrowings under the Credit Agreement. The financial markets are very volatile and certain participants in our Credit Agreement may not be able to participate in funding their commitments under the revolving line of credit. If we are unsuccessful in obtaining the financing, our business would be impacted.

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We are exposed to interest rate changes.

We are exposed to market risk related to changes in interest rates. As of December 31, 2013, we had outstanding debt of $231.3 million, all of which was subject to variable rates of interest. See Item 7A, “Quantitative and Qualitative Disclosures about Market Risk.”

We have indebtedness, which restricts our ability to pay cash dividends and has a negative impact on our financing options and liquidity.

We have $231.3 million in indebtedness outstanding as of December 31, 2013 under our Credit Agreement and revolver.

On May 2, 2011, the Corporation entered into a long-term credit agreement (the "Credit Agreement") among the Corporation, the Lenders named therein, and Citibank N.A. ("Citibank"), as Administrative Agent. The Credit Agreement contains customary restrictions, requirements and other limitations on our ability to incur indebtedness. The Credit Agreement also contains financial covenants that require us to satisfy certain financial tests and maintain certain financial ratios, including a maximum of debt to EBITDA ratio. The Credit Agreement limits our ability to declare and pay dividends or other distributions on our shares of common stock. If our lenders permit us to declare dividends, the dividend amounts, if any, will be determined by our Board of Directors, which will consider a number of factors, including our financial condition, capital requirements, funds generated from operations, future business prospects, applicable contractual restrictions and any other factors our Board of Directors may deem relevant. The amount of this outstanding indebtedness could limit our ability to pay cash dividends and to obtain additional financing in the future for working capital, capital expenditure and acquisition purposes. A significant portion of our cash flows will be dedicated to debt service and will be unavailable for investment, capital expenditures or other operating expenses.

As a result of these and other factors, we cannot assure you that our business will generate sufficient cash flows from operations or that future borrowings will be available to us in amounts sufficient to enable us to pay our indebtedness or to fund our other liquidity needs. If we do not generate or are unable to borrow sufficient amounts of cash on satisfactory terms to meet these needs, we may need to seek to refinance all or a portion of our indebtedness on or before maturity, sell assets, curtail discretionary capital expenditures or seek additional capital. There can be no assurance that additional capital will be available to us on acceptable terms, or at all, which could adversely impact our business, results of operations, liquidity, capital resources, and financial condition.

We anticipate that future earnings will be used principally to support operations and finance the growth of our business. Thus, we do not intend to pay dividends or other cash distributions on our common stock in the foreseeable future. See Part II, Item 5 “Market for Registrant’s Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities.”

See Item 7 “Management’s Discussion and Analysis of Financial Condition and Results of Operations—Liquidity and Capital Resources.”

The ability to successfully renegotiate the Credit Agreement could adversely affect the Corporation’s liquidity.

The scheduled payments under the Corporation’s Credit Agreement are set to increase substantially at September 30, 2015. The Corporation intends to refinance its debt arrangements however, there is no assurance that it will be able to enter into a new agreement or that a new agreement will have terms similar to the existing agreement. If the Corporation is unable to refinance its debt obligations, it could adversely impact our business, results of operations, liquidity, capital resources, and financial condition.

Item 1B. Unresolved Staff Comments

None.

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Item 2. Properties

We have facilities including offices and key operating facilities in various locations throughout the United States. The Corporation's corporate headquarters are located in Louisville, Kentucky. In addition to the pharmacies listed below, the Corporation also has muliple facilities throughout the nation with several overhead and administrative functions. As of December 31, 2013, all facilities were leased. We consider all of these facilities to be suitable, adequate, and are utilized at full capacity.

The following table presents certain information with respect to operating leases of our pharmacies identified by the Corporation as properties as of December 31, 2013:

State	# of Facilities	Square Footage	State	# of Facilities	Square Footage
Alabama	2	20,330	Mississippi	1	11,600
Arizona	2	21,436	Missouri	1	4,090
Arkansas	1	6,850	Montana	1	2,440
California	10	100,451	Nebraska	1	5,120
Colorado	4	28,971	Nevada	3	16,373
Connecticut	1	15,600	New Hamphire	1	7,500
Delaware	1	5,739	New Jersey	1	14,309
Florida	6	67,112	New Mexico	2	12,891
Georgia	2	33,202	New York	4	95,031
Hawaii	5	15,506	North Carolina	3	21,250
Idaho	1	4,031	Ohio	2	26,125
Illinois	1	15,495	Oklahoma	2	11,318
Indiana	1	20,386	Pennsylvania	7	50,634
Iowa	1	6,250	Rhode Island	1	9,415
Kansas	1	9,977	South Carolina	3	22,042
Kentucky	2	43,500	South Dakota	2	12,050
Louisiana	1	4,914	Tennessee	5	47,837
Maine	1	10,200	Texas	13	91,034
Maryland	1	10,744	Utah	3	18,002
Massachusetts	2	56,611	Virginia	2	15,807
Michigan	2	13,720	Washington	2	14,792
Minnesota	2	13,872	West Virginia	1	1,419
			Wisconsin	1	11,068

Item 3. Legal Proceedings

On April 15, 2013, the U.S. Department of Justice, through the U.S. Attorney's Office for the Eastern District of Virginia, filed a complaint in the United States District Court for the Eastern District of Virginia against the Corporation's two pharmacies in Virginia Beach, Virginia and Fredericksburg, Virginia alleging that these two pharmacies failed to comply with the Controlled Substances Act ("CSA") by dispensing Schedule II drugs without a proper prescription. The parties reached a settlement in December 2013 and filed a stipulation for dismissal of the case in January 2014. Under the settlement, the Corporation will pay $1.0 million and will enter into a Memorandum of Agreement ("MOA") with the DEA through which it will agree to certain CSA compliance obligations. The precise terms of the MOA are currently being negotiated between the parties. In connection with the settlement, the Corporation did not admit liability for the alleged CSA violations.

On June 10, 2013, the United States District Court for the Eastern District of Wisconsin unsealed two consolidated qui tam complaints filed in 2009 and 2011 by relators who are former employees of the Corporation and a company acquired by the Corporation. The United States, acting through the U.S. Attorney's Office in Wisconsin, intervened in part and declined to intervene in part and filed its complaint in intervention on August 9, 2013, when the matter was formally brought to the Corporation's attention. The first complaint seeks statutory fines for the Corporation's alleged dispensing of Schedule II controlled substances without a valid prescription in violation of the Controlled Substances Act. It also seeks monetary damages and equitable relief alleging that this conduct caused false claims to be submitted in violation of the federal False Claims Act (the "FCA"). The Corporation has moved to dismiss the government's complaint for failure to state a claim upon which relief may be granted and is awaiting the Court's decision. The second complaint alleges that the Corporation submitted false claims to Medicare Part D and to Medicaid for drugs in connection with which the Corporation allegedly received kickbacks from the manufacturer in the form of market share rebates and other remuneration, all in violation of the Federal Antikickback statute (the "AKS/FCA" claims). The second complaint also includes a claim by the relator under the retaliatory termination provisions of the FCA. The government declined to intervene in the AKS/FCA claims and the relator thereafter moved, with the government's permission, to dismiss the AKS/FCA claims, which motion the Court has granted. The relator is independently pursuing the retaliatory termination claims. The Corporation has moved to dismiss the relator's complaint for failure to state a claim upon which relief may be granted and is awaiting the Court's decision. The Corporation intends to vigorously defend itself in both matters.

On November 20, 2013 the complaint filed by a relator, Robert Gadbois, on behalf of the U.S. Government and various state governments, was unsealed by the United States District for the District of Rhode Island against the Corporation alleging that the Corporation dispensed controlled and non-controlled substances in violation of the CSA and thus the dispenses were not eligible for

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payment and therefore that the claims the Corporation submitted to the Government were false within the meaning of the FCA. The U.S. Government and the various state governments have declined to intervene in this case. The case therefore has been unsealed but relator has not yet served the Corporation. Gadbois has moved the court to file a Second Amended Complaint, which motion is still pending before the Court. Once relator serves the Complaint, the Corporation intends to defend the case vigorously.

On August 8, 2013, a complaint filed by the relator, Richard Templin, in the United States District Court for the Southern District of Texas was unsealed. The complaint sought monetary damages and alleged that the Corporation violated the federal False Claims Act and the Anti-Kickback Act by allegedly receiving rebates from pharmaceutical manufacturers, and by allegedly providing or receiving other remuneration from pharmaceutical manufacturers and its nursing facility customers in exchange for referrals. The relator then voluntarily dismissed all claims against the Corporation and the case is no longer pending.

On November 12, 2013, a relator, Fox Rx, Inc. ("Fox"), on behalf of the U.S. Government and various state governments and the District of Columbia, filed a complaint in the United States District Court for the Southern District of New York against the Corporation alleging that the Corporation violated the FCA by submitting false claims to Fox, other Medicare Part D sponsors and to Medicaid, by allegedly billing for expired drugs or for brand drugs when generic drugs should have been substituted. Following the U.S. Government's decision to decline to intervene in the case, the complaint was unsealed and served on the Corporation. The Corporation intends to vigorously defend itself against these allegations.

On March 4, 2011, a relator, Mark Silver, on behalf of the U.S. Government and various state governments, filed a complaint in the United States District for the District of New Jersey against the Corporation alleging that the Corporation violated the False Claims Act and Anti-Kickback Statute through its agreements to provide prescription drugs to nursing homes under certain Medicare and Medicaid programs. On February 19, 2013, the U.S. Government declined to intervene in the case. The complaint has been amended several times, most recently on November 12, 2013 and thereafter served upon the Corporation. On December 6, 2013, the Corporation moved to dismiss the amended complaint for failure to state a claim upon which relief may be granted and is awaiting the Court's decision. The Corporation intends to vigorously defend itself against these allegations.

On January 31, 2014, a relator, Frank Kurnik, on behalf of the U.S. Government and various state governments served its complaint filed in the United States District for the District of South Carolina alleging that the Corporation solicited and received remuneration in violation of the federal Anti-kickback Statute from drug manufacturer Amgen in exchange for preferring and promoting Amgen's drug Aranesp over a competing drug called Procrit. The U.S. Government and the various states declined to intervene in the case. The Corporation intends to vigorously defend itself against these allegations.

The U.S. Department of Justice, through the U.S. Attorney's Office for the Western District of Virginia, is investigating whether the Corporation's activities in connection with agreements it had with the manufacturer of the pharmaceutical Depakote violated the False Claims Act or the Anti-Kickback Statute. The Corporation is cooperating with these investigations and believes it has complied with applicable laws and regulations with respect to these matters.

In addition, the Corporation is involved in certain legal actions and regulatory investigations arising in the ordinary course of business. At this time, the Corporation is unable to determine the impact of these investigations on its consolidated financial condition, results of operations, or liquidity. At December 31, 2013, the Corporation had accrued approximately $20.0 million related to the legal actions and investigations.

In addition, the Corporation is involved in certain legal actions and regulatory investigations arising in the ordinary course of business. Also see Note 6 to the Corporation’s Consolidated Financial Statements set forth in Part II, Item 8

of this report.

Item 4. Mine Safety Disclosures

Not applicable.

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PART II

Item 5. Market for Registrant's Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities

Market Information

Our only class of common equity is our $0.01 par value common stock, which trades on the NYSE under the symbol "PMC."

The following table sets forth the high and low prices per share during the period and the closing price of our common stock as reported by the NYSE for the fiscal periods indicated.

	High	Low	Close
Fiscal 2012			
First Quarter	$15.54	$12.00	$12.43
Second Quarter	$12.90	$9.03	$10.92
Third Quarter	$13.40	$9.82	$12.66
Fourth Quarter	$14.85	$11.75	$14.24
Fiscal 2013			
First Quarter	$15.42	$13.39	$14.00
Second Quarter	$16.45	$12.22	$13.86
Third Quarter	$15.80	$11.84	$13.27
Fourth Quarter	$22.85	$13.24	$21.50

Stockholders

As of January 31, 2014, we had approximately 2,749 stockholders of record of the Corporation's common stock. Because many of our shares of common stock are held by brokers and other institutions on behalf of stockholders, we are unable to estimate the total number of stockholders represented by these record holders.

Cash Dividends

The Corporation has never paid a cash dividend on its common stock and does not expect to pay cash dividends on its common stock in the foreseeable future. Our Credit Agreement also limits our ability to declare and pay dividends or other distributions on our shares of common stock. Management believes the stockholders are better served if all of the Corporation's earnings are retained for expansion of the business.

Securities authorized for issuance under equity compensation plans

The Corporation has adopted the Amended and Restated PharMerica Corporation 2007 Omnibus Incentive Plan (as amended and restated, "Omnibus Plan") under which the Corporation is authorized to grant equity-based and other awards to its employees, officers, directors and consultants. In connection with the Corporation's 2010 Annual Meeting of Stockholders, the stockholders of the Corporation approved and adopted the amended and restated Omnibus Plan to, among other things, implement a "fungible share pool" effective as of January 1, 2010, and preserve preferential tax treatment as "qualified performance-based compensation" under Section 162(m) of the Internal Revenue Code.

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

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The following table sets forth equity compensation plan information as of December 31, 2013:

Plan Category	Number of securities to be issued upon exercise of outstanding options, warrants and rights	Weighted-average exercise price of outstanding options, warrants and rights	Number of securities remaining available for future issuance under equity compensation plans (excluding securities reflected in column (a))
	(a)	(b)	(c)
Equity compensation plans approved by stockholders	2,386,247 (1)	$ 14.63 (2)	3,170,983 (3)

(1) Includes the following:

- 1,289,573 shares of common stock to be issued upon exercise of outstanding stock options granted under the Omnibus Plan;
- 470,349 shares of common stock to be issued upon vesting of performance share units under the Omnibus Plan;
- 7,831 shares of common stock to be issued upon vesting of restricted stock awards under the Omnibus Plan; and
- 618,494 shares of common stock to be issued upon vesting of restricted stock units under the Omnibus Plan.

(2) The weighted average exercise price in column (b) does not take into account the 1,096,674 shares of common stock potentially to be issued under restricted stock awards, performance share units and restricted stock units.

(3) The 3,170,983 shares does not take into consideration the dilution of 1.65 shares of stock for any full-value award, including restricted stock awards, restricted stock units and performance share units at target. The number of shares remaining available for future issuance calculated under the fungible share pool would be 2,258,761.

See Note 10 to the Consolidated Financial Statements included in this Report for information regarding the material features of the Omnibus Plan.

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Stock Performance Graph

The following graph compares the cumulative total return on a $100 investment in each of the Common Stock of the Corporation, the Standard & Poor's 500 Stock Index and the Standard & Poor's Healthcare Index for the period from December 31, 2008 to December 31, 2013. This graph assumes an investment in the Corporation's common stock and the indices of $100 on December 31, 2008 and that all dividends were reinvested:

	PharMerica Corporation	S&P 500	S&P Healthcare
December 31, 2008	$ 100.00	$ 100.00	$ 100.00
March 31, 2009	106.19	146.44	116.60
June 30, 2009	144.16	141.71	114.58
September 30, 2009	143.52	129.13	114.58
December 31, 2009	101.34	123.45	117.07
March 31, 2010	106.19	88.33	91.48
June 30, 2010	93.55	101.78	99.04
September 30, 2010	60.82	117.03	107.87
December 31, 2010	73.07	123.45	117.07
March 31, 2011	116.27	129.47	120.45
June 30, 2011	81.43	114.11	105.64
September 30, 2011	91.07	126.34	114.33
December 31, 2011	96.87	139.23	117.89
March 31, 2012	79.32	155.93	140.83
June 30, 2012	69.69	150.81	142.45
September 30, 2012	80.79	159.50	150.38
December 31, 2012	90.87	157.89	149.62
March 31, 2013	89.34	173.73	172.40
June 30, 2013	88.45	177.83	178.14
September 30, 2013	84.68	186.17	189.40
December 31, 2013	137.20	204.63	207.59

Recent Sales of Unregistered Securities

None.

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Purchases of Equity Securities by the Issuer and Affiliated Purchasers

On August 24, 2010, the Corporation announced a stock repurchase program where the Corporation is authorized to repurchase up to $25.0 million of the Corporation's common stock, of which $10.5 million was used to purchase the Corporation's common stock. On July 2, 2012, the Board of Directors authorized an increase to the existing stock repurchase program that will allow the Corporation to again purchase back up to a maximum of $25.0 million of the Corporation's common stock. The stock repurchase program does not have an expiration date and may be limited, terminated or extended at any time without prior notice. The Corporation did not repurchase shares under this program for the three months ended December 31, 2013.

Additionally, the Corporation may redeem shares from employees upon vesting of the Corporation's stock awards for minimum statutory tax withholding purposes and exercise cost of stock options. The Corporation redeemed 480,339 shares of certain vested awards and the exercise of certain stock options for an aggregate price of $9.9 million during the three months ended December 31, 2013.

The following table summarizes our share repurchase activity by month for the three months ended December 31, 2013:

Period	Total Number of Shares Purchased		Weighted Average Price Paid per Share	Total Number of Shares Purchased as Part of a Publicly Announced Plans or Programs (2)	Approximate Dollar Value of Shares that may yet be Purchased under the Plans or Programs (in millions)
October 1, 2013 - October 31, 2013	327	(1)	$ 14.11	-	$ 19.7
November 1, 2013 - November 30, 2013	479,735	(1)	20.79	-	19.7
December 1, 2013 - December 31, 2013	277	(1)	21.35	-	19.7

(1) The Corporation repurchased 480,339 shares of common stock in connection with the vesting of certain stock awards to cover minimum statutory withholding taxes and exercise cost of stock options.

(2) The Corporation did not repurchase shares under the stock repurchase program for the three months ended December 31, 2013.

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Item 6. Selected Financial Data

The following table presents our selected historical consolidated financial and operating data. The selected historical financial and operating data should be read in conjunction with, and is qualified in its entirety by reference to, Item 7, "Management's Discussion and Analysis of Financial Condition and Results of Operations" and our consolidated financial statements and notes thereto included elsewhere in this Annual Report on Form 10-K (in millions, except where indicated):

	Years Ended December 31,				
	2009	2010	2011	2012	2013
Statement of operations data:					
Revenues	$1,841.2	$1,847.3	$2,081.1	$1,832.6	$1,757.9
Cost of goods sold	1,563.3	1,604.8	1,786.2	1,532.4	1,430.7
Gross profit	277.9	242.5	294.9	300.2	327.2
Selling, general and administrative	193.2	182.8	216.5	214.7	225.3
Amortization expense	9.0	9.3	11.0	12.3	15.4
Impairment of intangible assets	-	-	5.1	-	-
Merger, acquisition, integration costs and other	5.2	14.6	16.8	17.8	8.1
Settlement, litigation and other related charges	-	-	(1.5)	2.1	19.6
Restructuring and impairment charges	-	-	-	-	4.4
Hurricane Sandy disaster costs	-	-	-	4.5	(1.4)
Operating income (1)	$70.5	$35.8	$47.0	$48.8	$55.8
Net income	$42.2	$19.2	$23.4	$22.9	$18.9
Earnings per common share: (2)					
Basic	$1.39	$0.64	$0.80	$0.78	$0.64
Diluted	$1.39	$0.64	$0.79	$0.77	$0.63
Adjusted earnings per diluted common share (3)	$1.39	$1.03	$1.32	$1.41	$1.83
Shares used in computing earnings per common share:					
Basic	30.3	30.0	29.3	29.5	29.6
Diluted	30.4	30.1	29.5	29.9	30.1
Balance sheet data:					
Cash and cash equivalents	$51.2	$10.8	$17.4	$12.3	$24.2
Working capital (4)	$312.8	$280.9	$348.4	$322.1	$260.2
Goodwill (4)	$140.1	$179.4	$214.9	$269.4	$282.6
Intangible assets, net	$90.8	$102.2	$100.2	$121.9	$135.9
Total assets (4)	$724.3	$759.7	$834.0	$886.3	$901.4
Long-term debt, including current portion	$240.0	$245.6	$300.0	$315.5	$231.3
Total stockholder's equity	$370.9	$384.4	$413.8	$442.6	$462.5
Supplemental information:					
Adjusted EBITDA (3)	$107.7	$83.7	$104.5	$111.2	$132.8
Adjusted EBITDA Margin (3)	5.8%	4.5%	5.0%	6.1%	7.5%
Adjusted EBITDA per prescription dispensed (3)	$2.76	$2.21	$2.51	$2.84	$3.52
Net cash provided by operating activities	$84.8	$98.2	$26.8	$85.7	$155.7
Net cash used by investing activities	$(76.1)	$(133.2)	$(64.0)	$(105.3)	$(53.7)
Net cash (used in) provided by financing activities	$1.2	$(5.4)	$43.8	$14.5	$(90.1)
Statistical information (in whole numbers except where indicated) Volume information:					
Prescriptions dispensed (in thousands)	39,037	37,826	41,677	39,212	37,731

Revenue per prescription dispensed (6)	$47.17		$48.84		$49.93		$46.74		$46.67	
Gross profit per prescription dispensed (6)	$7.12		$6.41		$7.08		$7.66		$8.75	
Gross profit margin (6)	15.1	%	13.1	%	14.2	%	16.4	%	18.8	%
Generic drug dispensing rate (5)	74.6	%	76.5	%	79.6	%	83.3	%	83.4	%

(1) Includes depreciation expense of $18.0 million, $18.8 million, $20.1 million, $18.6 million and $19.3 million for the years ended December 31, 2009, 2010, 2011, 2012 and 2013, respectively.

(2) The Corporation has never declared a cash dividend. Earnings per share in whole dollars and cents.

(3) See “Use of Non GAAP Measures for Measuring Annual Results” for a definition and Reconciliation of Adjusted Earnings per Diluted Common Share to Earnings Per Diluted Common Share and for Reconciliation of Net Income to Adjusted EBITDA and Adjusted EBITDA Margin.

(4) As adjusted, see Note 2—Acquisitions in the Consolidated Financial Statements.

(5) Single source generic drugs, previously classified as brand drugs, are now being classified as generics for purposes of the generic dispensing rate calculation in all periods.

(6) Amounts in 2013 do not include the $2.9 million California Medicaid estimated recoupment.

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Use of Non-GAAP Measures for Measuring Annual Results

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

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

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Reconciliation of Net Income to Adjusted EBITDA

	Years Ended December 31,				
	2009	2010	2011	2012	2013
Net income	$42.2	$19.2	$ 23.4	$22.9	$18.9
Add:					
Interest expense, net	9.4	3.6	8.8	10.0	10.6
Merger, acquisition, integration costs and other charges	5.2	14.6	16.8	17.8	8.1
Settlement, litigation and other related charges	-	-	(1.5)	2.1	19.6
California Medicaid estimated recoupment	-	-	-	-	2.9
Restructuring and impairment charges	-	-	-	-	4.4
Hurricane Sandy disaster costs	-	-	-	4.5	(1.4)
Stock-based compensation and deferred compensation	5.0	5.2	6.0	7.1	8.7
Provision for income taxes	18.9	13.0	14.8	15.9	26.3
Impairment of intangible assets	-	-	5.1	-	-
Depreciation and amortization expense	27.0	28.1	31.1	30.9	34.7
Adjusted EBITDA	$107.7	$83.7	Denominator for basic earnings per share - weighted average shares	30,073,133	30,431,845	29,944,875
Effect of dilutive	522,169	464,449	558,053	462,286	

securities (stock options, restricted stock units and performance share units)					
Denominator for earnings per diluted share - adjusted weighted average shares	30,595,302	30,896,294		30,502,928	30,798,834
Basic earnings per share	$0.28	$0.10	$	0.12	$0.49
Earnings per diluted share	$0.28	$0.10	$	0.12	$0.48
Unexercised employee stock options and unvested restricted shares excluded from the effect of dilutive securities above (a)	465,377	197		481,844	504

(a) These unexercised employee stock options, unvested restricted shares and performance shares that have not yet met performance conditions are not included in the computation of diluted earnings per share because to do so would be anti-dilutive for the periods presented.

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

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

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

CAUTIONARY STATEMENT REGARDING FORWARD-LOOKING STATEMENTS

This Quarterly Report on Form 10-Q contains forward-looking statements, within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended, which reflect the Corporation's current estimates, expectations and projections about the Corporation's future results, performance, prospects and opportunities. Forward looking statements include, among other things, the information concerning the Corporation's possible future results of operations including revenues, costs of goods sold, and gross margin, business and growth strategies, financing plans, the Corporation's competitive position and the effects of competition, the projected growth of the industries in which we operate, and the Corporation's ability to consummate strategic acquisitions. Forward-looking statements include statements that are not historical facts and can be identified by forward-looking words such as "anticipate," "believe," "could," "estimate," "expect," "intend," "plan," "may," "should," "will," "would," "project," and similar expressions. These forward-looking statements are based upon information currently available to the Corporation and are subject to a number of risks, uncertainties and other factors that could cause the Corporation's actual results, performance, prospects or opportunities to differ materially from those expressed in, or implied by, these forward-looking statements. Important factors that could cause the Corporation's actual results to differ materially from the results referred to in the forward-looking statements the Corporation makes in this report include:

- the Corporation's access to capital, credit ratings, indebtedness, and ability to raise additional financings and operate under the terms of the Corporation's debt obligations;
- anti-takeover provisions of the Delaware General Corporation Law, which in concert with our certificate of incorporation and our by-laws could delay or deter a change in control;
- the effects of adverse economic trends or intense competition in the markets in which we operate;
- the Corporation's risk of loss of revenues due to a customer or owner of skilled nursing facility entering the institutional pharmacy business;
- the effects of the loss of a large customer and the Corporation's ability to adequately restructure its operations to offset the loss;
- the demand for the Corporation's products and services;
- the risk of retaining existing customers and service contracts and the Corporation's ability to attract new customers for growth of the Corporation's business;
- the effects of renegotiating contract pricing relating to significant customers and suppliers, including the hospital pharmacy business which is substantially dependent on service provided to one customer;
- the impacts of cyber security risks and/or incidents;
- the effects of a failure in the security or stability of our technology infrastructure, or the infrastructure of one or more of our key vendors, or a significant failure or disruption in service;
- the effects of an increase in credit risk, loss or bankruptcy of or default by any significant customer, supplier, or other entity relevant to the Corporation's operations;
- the Corporation's ability to successfully pursue the Corporation's development and acquisition activities and successfully integrate new operations and systems, including the realization of anticipated revenues, economies of scale, cost savings, and productivity gains associated with such operations;
- the Corporation's ability to control costs, particularly labor and employee benefit costs, rising pharmaceutical costs, and regulatory compliance costs;
- the effects of healthcare reform and government regulations, including interpretation of regulations and changes in the nature and enforcement of regulations governing the healthcare and institutional pharmacy services industries including the dispensing of antipsychotic prescriptions;
- changes in the reimbursement rates or methods of payment from Medicare and Medicaid and other third party payers to both us and our customers;
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- the potential impact of state government budget shortfalls and their ability to pay the Corporation and its customers for services provided;
- the Corporation's ability, and the ability of the Corporation's customers, to comply with Medicare or Medicaid reimbursement regulations or other applicable laws;
- the effects of changes in the interest rate on the Corporation's outstanding floating rate debt instrument and the increases in interest expense, including increases in interest rate terms on any new debt financing;
- further consolidation of managed care organizations and other third party payers;
- political and economic conditions nationally, regionally, and in the markets in which the Corporation operates;
- natural disasters, war, civil unrest, terrorism, fire, floods, tornadoes, earthquakes, hurricanes, epidemic, pandemic, catastrophic event or other matters beyond the Corporation's control;
- increases in energy costs, including state and federal taxes, and the impact on the costs of delivery expenses and utility expenses;
- elimination of, changes in, or the Corporation's failure to satisfy pharmaceutical manufacturers' rebate programs;
- the Corporation's ability to attract and retain key executives, pharmacists, and other healthcare personnel;
- the Corporation's risk of loss not covered by insurance;
- the outcome of litigation to which the Corporation is a party from time to time, including adverse results in material litigation or governmental inquiries including the possible insufficiency of any accruals established by the Corporation from time to time;
- changes in accounting rules and standards, audits, compliance with the Sarbanes-Oxley Act, and regulatory investigations;
- changes in market conditions that would result in the impairment of goodwill or other assets of the Corporation;
- changes in market conditions in which we operate that would influence the value of the Corporation's stock;
- the uncertainty as to the long-term value of the Corporation's common stock;
- the Corporation's ability to anticipate a shift in demand for generic drug equivalents and the impact on the financial results including the negative impact on brand drug rebates;
- the effect on prescription volumes and the Corporation's net revenues and profitability if the safety risk profiles of drugs increase or if drugs are withdrawn from the market, including as a result of manufacturing issues, or if prescription drugs transition to over-the-counter products;
- the effects on the Corporation's results of operations related to interpretations of accounting principles by the SEC staff that may differ from those of management;

- the potential impact of the litigation proceedings with ABDC regarding the Amended PVA;
- the Corporation's ability to comply with the terms of its Memorandum of Agreement with the DEA and the Corporate Integrity Agreement with the OIG;
- the Corporation's ability to collect outstanding receivables;
- changes in tax laws and regulations;
- the effects of changes to critical accounting estimates; and
- other factors, risks and uncertainties referenced in the Corporation's filings with the Commission, including the "Risk Factors" set forth in the Corporation's Annual Report on Form 10-K for the year ended December 31, 2014.

YOU ARE CAUTIONED NOT TO PLACE UNDUE RELIANCE ON ANY FORWARD-LOOKING STATEMENTS, ALL OF WHICH SPEAK ONLY AS OF THE DATE OF THIS QUARTERLY REPORT. EXCEPT AS REQUIRED BY LAW, WE UNDERTAKE NO OBLIGATION TO PUBLICLY UPDATE OR RELEASE ANY REVISIONS TO THESE FORWARD-LOOKING STATEMENTS TO REFLECT ANY EVENTS OR CIRCUMSTANCES AFTER THE DATE OF THIS QUARTERLY REPORT OR TO REFLECT THE OCCURRENCE OF UNANTICIPATED EVENTS. ALL SUBSEQUENT WRITTEN AND ORAL FORWARD-LOOKING STATEMENTS ATTRIBUTABLE TO US OR ANY PERSON ACTING ON THE CORPORATION'S BEHALF ARE EXPRESSLY QUALIFIED IN THEIR ENTIRETY BY THE CAUTIONARY STATEMENTS CONTAINED OR REFERRED TO IN THIS SECTION AND IN OUR RISK FACTORS SET FORTH IN PART I, ITEM 1A OF THE CORPORATION'S ANNUAL REPORT ON FORM 10-K FOR THE YEAR ENDED DECEMBER 31, 2014 AND IN OTHER REPORTS FILED WITH THE SEC BY THE CORPORATION.
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General

The condensed consolidated financial statements and Management's Discussion and Analysis of Financial Condition and Results of Operations included in this quarterly report on Form 10-Q as of and for the three and nine months ended September 30, 2015, reflect the financial position, results of operations, and cash flows of the Corporation.

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

Institutional Pharmacy Business

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

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

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

Hospital Pharmacy Management Services

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

Consultant Pharmacist Services

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

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

- Monthly reviews of each resident's drug regimen to assess the appropriateness and efficiency of drug therapies, including the review of medical records, monitoring drug interactions with other drugs or food, monitoring laboratory test results, and recommending alternative therapies;
- Participation on quality assurance and other committees of our customers, as required or requested by such customers;
- Monitoring and reporting on facility-wide drug utilization;
- Development and maintenance of pharmaceutical policy and procedure manuals; and
- Assistance with federal and state regulatory compliance pertaining to resident care.

Medical Records

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

- Real-time access to medication and treatment administration records, physician order sheets and psychotropic drug monitoring sheets;
- Online ordering to save time and resources;
- A customized database with the medication profiles of each resident's medication safety, efficiency and regulatory compliance;
- Web-based individual patient records detailing each prescribed medicine; and
- Electronic medical records to improve information to make it more legible and instantaneous.

Specialty Infusion Services

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

Specialty Oncology Pharmacy

We provide dispensing of oncology drugs, care management and other related services to patients, oncology practices, and hospitals. These services encompass clinical coordination and review, compliance to appropriate oncology protocols, patient assistance with outside funding, and timely delivery of medication. We coordinate the administration of medications to the physician's office or directly to the patient at the appropriate point of treatment. We work directly with the payers to bill insurance companies for the medication provided, ensuring all prior authorizations and approvals are obtained. These services offer physicians an alternative to the traditional buy-and-bill distribution model, allowing them to outsource drug procurement, inventory management, and prescription administration.

Suppliers/Inventory

We obtain pharmaceutical and other products from Cardinal Health ("Cardinal") and other contracts negotiated directly with pharmaceutical manufacturers for discounted prices. The Corporation entered into a Prime Vendor Agreement with Cardinal effective April 1, 2015. The loss of a supplier could adversely affect our business if alternate sources of supply are unavailable.

We seek to maintain an on-site inventory of pharmaceuticals and supplies to ensure prompt delivery to our customers. Cardinal maintains local distribution facilities in most major geographic markets in which we operate. In addition, beginning in the fourth quarter of 2013, we began supplying many of our pharmacies with select products from a distribution center operated by a third-party logistics company.

Brand to Generic Conversions

The following table summarizes the material brand-to-generic conversions expected to occur in 2015 through 2018:

2015	2016	2017	2018
Patanol (Q4)	Gleevec (Q1)	Azilect (Q1)	Nasonex (Q2)
Renagel (Q4)	Nuedexta (Q1)	Vytorin (Q2)	
Renvela(Q4)	Combivent (Q2)		
	Crestor (Q2)		
	Cubicin (Q2)		
	Tamiflu (Q3)		
	Kaletra (Q4)		
	Seroquel XR (Q4)		
	Zetia (Q4)		

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

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

Supplier and Manufacturer Rebates

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

2010 Health Care Reform Legislation

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

FUL and AMP Changes

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

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

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

In September 2011, CMS issued the first draft FUL reimbursement files for multiple source drugs, including the draft methodology used to calculate the FULs in accordance with the 2010 Health Care Reform Legislation. CMS continues to release this monthly data and a three-month rolling average and is expected to do so going forward. CMS has not posted monthly AMPs for individual drugs, but only posted the weighted average of monthly AMPs in a FUL group and the calculation methodology.

CMS has stated that AMP-based FULSs will be published at or about the same time that CMS publishes the Medicaid Covered Outpatient Drug final rule. On August 4, 2015, the Office of the Management and Budget (the "OMB") received the Medicaid Covered Outpatient Drug final rule for final review. The OMB website stated that it expected final action on this rule in August 2015; however, final action has not yet been taken.

CMS will continue to post draft monthly FULs. The Corporation will continue to analyze the draft monthly FULs, including the relationship of those FULs to the National Average Drug Acquisition pricing.

Part D Coverage Gap

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

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

Short Cycle Dispensing and Dispensing Fees

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

In a February 12, 2015 Final Rule entitled "Medicare Program: Contract Year 2016 Policy and Technical Changes to the Medicare Advantage and the Medicare Prescription Drug Benefit Programs", CMS finalized a regulation, effective January 1, 2016, prohibiting financial arrangements that penalize more efficient long-term care dispensing techniques (e.g., dispensing a three day supply over a 14-day supply) through pro-rated dispensing fees based on a day's supply or quantity dispensed. CMS also finalized a requirement that, effective January 1, 2016, any differences in payment methodologies among long-term care pharmacies incentivize more efficient dispensing techniques. The Corporation is unable to evaluate the full impact of these changes on its business at this time.

Medicare Part D Changes

In a May 23, 2014 Final Rule entitled "Medicare Program: Contract Year 2015 Policy and Technical Changes to the Medicare Advantage and the Medicare Prescription Drug Benefit Programs," CMS finalized a requirement that applicable January 1, 2016 and enforceable June 1, 2016, certain prescribers of Part D covered drugs must be enrolled as Medicare providers (or be granted a valid opt-out affidavit on file with a Part A or Part B Medicare Administrative Contractor) in order for a claim to be covered under Medicare Part D. CMS also finalized several specific requirements to reduce prescriber fraud, waste, and abuse. The Corporation is unable to evaluate the full impact of these changes on its business at this time.

CIA and DEA MOA

In May 2015, the Corporation entered into a five-year corporate integrity agreement ("CIA") with the OIG and a Memorandum of Agreement ("MOA") with the Drug Enforcement Agency ("DEA") concurrent with the execution of settlement agreements with the OIG and the DEA settling alleged Controlled Substance Act ("CSA") violations and associated False Claims Act allegations.

The CIA requires the Corporation, among other things to: (i) create procedures designed to ensure it complies with the CSA and related regulations; (ii) retain an independent review organization to review the Corporation's compliance with the terms of the CIA and report to the OIG regarding that compliance; and (iii) provide training for certain Corporation employees as to the Corporation's requirements under the CSA. If the Corporation fails to comply with the terms of the CIA, it may be required to pay certain monetary penalties. Furthermore, if the Corporation commits a material breach of the CIA, the OIG may exclude the Corporation from participating in federal healthcare programs. Any such exclusion would result in the revocation or termination of contracts and/or licenses and potentially have a material adverse effect on our financial condition, results of operations and business prospects.

The MOA provides for an independent obligation for the Corporation to comply with all requirements of the CSA, specifically relating to the dispensing of Scheduled prescription drugs. If the Corporation fails to comply with the terms of the MOA, the DEA may suspend a Corporation's pharmacy's DEA Certificate of Registration and begin an administrative hearing process pursuant to 21 U.S.C. § 824. Any such suspension would prohibit the Corporation's pharmacy from dispensing Scheduled prescription drugs and would lead to the revocation or termination of contracts and/or licenses and potentially have a materially adverse effect on our financial condition, results of operation and business prospects.

Critical Accounting Estimates

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

- It requires assumptions to be made that were uncertain at the time the estimate was made; and
- Changes in the estimate or different estimates could have a material impact on our condensed consolidated results of operations or financial condition.

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

Allowance for doubtful accounts and provision for doubtful accounts

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

Our quarterly provision for doubtful accounts included in our condensed consolidated statements of operations is as follows (dollars in millions):

	2014				2015			
	Amount	% of Revenues			Amount	% of Revenues		
First Quarter	$5.6	1.2	%	First Quarter	$5.0	1.0	%	
Second Quarter	5.7	1.3		Second Quarter	3.0	0.6		
Third Quarter	5.3	1.1		Third Quarter	1.5	0.3		
Fourth Quarter	6.6	1.3						

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

	2014	2015
First Quarter	37.7	34.0
Second Quarter	37.0	35.4
Third Quarter	36.7	35.5
Fourth Quarter	34.9	

The following table shows our summarized aging categories by quarter:

2014	2015

	First	Second	Third	Fourth	First	Second	Third
0 to 60 days	56.7%	53.9 %	57.3%	58.8 %	61.4%	60.0 %	58.9%
61 to 120 days	17.7	17.3	16.9	17.2	15.8	15.7	15.2
Over 120 days	25.6	28.8	25.8	24.0	22.8	24.3	25.9

The following table shows our allowance for doubtful accounts as a percent of gross accounts receivable (dollars in millions):

2014				2015			
	Allowance	Gross Accounts Receivable	% of Gross Accounts Receivable		Allowance	Gross Accounts Receivable	% of Gross Accounts Receivable
First Quarter	$57.7	$ 242.2	23.8 %	First Quarter	$59.7	$ 259.2	23.0 %
Second Quarter	60.3	246.5	24.5	Second Quarter	58.8	257.9	22.8
Third Quarter	57.4	272.4	21.1	Third Quarter	57.7	253.5	22.8
Fourth Quarter	58.1	253.5	22.9				

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

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

	Three Months Ended September 30,					
	2014			2015		
	Amount	% of Revenues		Amount	% of Revenues	
Medicare Part D	$214.6	45.6	%	$234.6	47.0	%
Institutional healthcare providers	110.4	23.5		114.5	23.0	
Medicaid	39.5	8.4		34.3	6.9	
Private and other	19.5	4.1		19.9	4.0	
Insured	64.8	13.8		74.2	14.9	
Medicare	5.9	1.3		5.7	1.1	
Hospital management fees	15.5	3.3		15.6	3.1	
Total	$470.2	100.0	%	$498.8	100.0	%

	Nine Months Ended September 30,					
	2014			2015		
	Amount	% of Revenues		Amount	% of Revenues	
Medicare Part D	$618.2	45.1	%	$703.2	46.6	%
Institutional healthcare providers	337.3	24.6		354.1	23.5	
Medicaid	122.9	9.0		110.8	7.4	
Private and other	59.0	4.3		61.6	4.0	
Insured	173.1	12.6		215.0	14.3	
Medicare	16.3	1.2		16.3	1.1	
Hospital management fees	44.2	3.2		46.8	3.1	
Total	$1,371.0	100.0	%	$1,507.8	100.0	%

Inventory and cost of drugs dispensed

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

As of December 31, 2014 and September 30, 2015, our inventories were $135.5 million and $117.5 million, respectively.

The inventory days on hand were as follows for the periods presented:

	2014	2015
First Quarter	26.0	26.1
Second Quarter	35.1	29.6

Third Quarter	31.7	25.7
Fourth Quarter	29.1	

Goodwill and other intangible assets

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

Our goodwill as of December 31, 2014 (as adjusted) and September 30, 2015 was $323.6 million and $341.8 million, respectively.

The Corporation's policy is to perform a quantitative assessment of its institutional pharmacy and specialty infusion reporting units to determine whether it is more likely than not (defined as having a likelihood of more than 50 percent) that the fair value of a reporting unit is less than its carrying amount. The Corporation performed a quantitative assessment as of December 31, 2014. The institutional pharmacy and specialty infusion reporting unit's fair value as calculated for the analysis were approximately 48.2% and 13.1%, respectively, greater than book value at December 31, 2014. As a result of the excess on the specialty infusion unit not being significant, the Corporation continues to closely monitor the results of the specialty infusion reporting unit. The specialty infusion reporting unit had goodwill with a carrying value of $57.7 million at December 31, 2014. The Corporation also performed a qualitative assessment of its specialty oncology reporting unit as of December 31, 2014 and did not find it necessary to perform the first step of the two-step impairment test based on that analysis.

There were no impairment triggering events during the nine months ended September 30, 2015.

Accounting for income taxes

We assess the likelihood that deferred tax assets will be realized from future taxable income. A valuation allowance is provided for deferred tax assets if it is more-likely-than-not that some portion or all of the net deferred tax assets will not be realized. Our net deferred tax asset balances as of December 31, 2014 and September 30, 2015 were $27.1 million and $23.0 million, respectively. Our valuation allowances for state deferred tax assets in our condensed consolidated balance sheets as of December 31, 2014 and September 30, 2015 were $4.1 million.

Definitions

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

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

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

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

Revenue per prescription dispensed: Represents the revenue divided by the total prescriptions dispensed.

Results of Operations

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

	Three Months Ended September 30,					Nine Months Ended September 30,				
	2014		Increase (Decrease)		2015	2014		Increase (Decrease)		2015
	Amount	% of Revenues			Amount	% of Revenues	Amount	% of Revenues		Amount	% of Revenue
Revenues	$470.2	100.0	$ 28.6	6.1 %	$498.8	100.0	$1,371.0	100.0	$136.8	10.0%	$1,507.8	100.0
Cost of goods sold	387.2	82.3	33.0	8.5	420.2	84.2	1,126.1	82.1	133.3	11.8	1,259.4	83.5
Gross profit	$83.0	17.7	$ (4.4)	(5.3)%	$78.6	15.8	$244.9	17.9	$3.5	1.4 %	$248.4	16.5
Pharmacy (in whole numbers except where indicated)												
Financial data												
Prescriptions dispensed (in thousands)	8,492		(284)	(3.3) %	8,208		25,511		202	0.8 %	25,713	
Revenue per prescription dispensed	$55.37		$ 5.40	9.8 %	$60.77		$53.74		$4.90	9.1 %	$58.64	
Gross profit per prescription dispensed	$9.77		$ (0.19)	(1.9)%	$9.58		$9.60		$0.06	6.3 %	$9.66	
Gross profit margin	17.7 %		(1.9)%	(10.7)%	15.8 %		17.9 %		(1.4)	(7.8)%	16.5 %	
Generic dispensing rate	85.1 %		1.4 %	1.6 %	86.5 %		84.9 %		1.0 %	1.2 %	85.9 %	

Revenues

Revenues increased $28.6 million for the three months ended September 30, 2015 compared to the three months ended September 30, 2014 which was driven by recent acquisitions, growth in the Corporation's specialty pharmacy businesses, and branded drug inflation. The increase of $28.6 million is comprised of a favorable rate variance of approximately $44.3 million or $5.40 increase per prescription dispensed, partially offset by an unfavorable volume variance of approximately $15.7 million or 284,000 fewer prescriptions dispensed. The revenue per prescription dispensed increase was due to the increased volume in the Corporation's specialty pharmacy businesses, which carries higher revenue per script and branded drug inflation.

Revenues increased $136.8 million for the nine months ended September 30, 2015 compared to the nine months ended September 30, 2014 which was driven by recent acquisitions, growth in the Corporation's specialty pharmacy businesses, and branded drug inflation. The increase of $136.8 million is comprised of a favorable rate variance of approximately $126.0 million or $4.90 increase per prescription dispensed, along with a favorable volume variance of

approximately $10.8 million or 202,000 more prescriptions dispensed. The revenue per prescription dispensed increase was due to the increased volume in the Corporation's specialty pharmacy businesses, which carries higher revenue per script and branded drug inflation.

Gross Profit

Gross profit for the three months ended September 30, 2015 was $78.6 million or $9.58 per prescription dispensed compared to $83.0 million or $9.77 per prescription dispensed for the three months ended September 30, 2014. The decrease in gross profit was primarily driven by lower volumes resulting from an improvement in the Corporation's client mix and higher drug costs under the Corporation's prime vendor agreement.

Gross profit margin for the three months ended September 30, 2015 was 15.8% compared to 17.7% for the three months ended September 30, 2014. The gross profit margin was adversely impacted by the increased volume in the Corporation's specialty pharmacy businesses, which carry lower profit margins as well as volume decreases in the long-term care pharmacy business and higher drug costs under the Corporation's prime vendor agreement.

Gross profit for the nine months ended September 30, 2015 was $248.4 million or $9.66 per prescription dispensed compared to $244.9 million or $9.60 per prescription dispensed for the nine months ended September 30, 2014. The increase in gross profit was driven by 2014 acquisitions, growth in the Corporation's specialty pharmacy businesses, and branded drug inflation. The increase in gross profit was partially offset by volume decreases in the long-term care pharmacy business and higher drug costs under the Corporation's prime vendor agreement.

Gross profit margin for the nine months ended September 30, 2015 was 16.5% compared to 17.9% for the nine months ended September 30, 2014. The gross profit margin was adversely impacted by the increased volume in the Corporation's specialty pharmacy businesses, which carry lower profit margins as well as volume decreases in the long-term care pharmacy business and higher drug costs under the Corporation's prime vendor agreement.

Selling, General and Administrative Expenses

Selling, general and administrative expenses were $52.7 million, or 10.6% of revenues, for the three months ended September 30, 2015 compared to $56.0 million, or 11.9% of revenues, for the three months ended September 30, 2014. The decrease of $3.3 million was due to cost improvements and a reduction in bad debt expense as the Corporation improved its client mix.

Selling, general and administrative expenses were $167.1 million, or 11.1% of revenues, for the nine months ended September 30, 2015 compared to $171.1 million, or 12.5% of revenues, for the nine months ended September 30, 2014. The decrease of $4.0 million was due to cost improvements and a reduction in bad debt expense as the Corporation improved its client mix.

Depreciation and Amortization

Depreciation expense was $5.7 million for the three months ended September 30, 2015 as compared to $4.9 million for the three months ended September 30, 2014 and $17.2 million for the nine months ended September 30, 2015 as compared to $14.5 million for the nine months ended September 30 2014. Depreciation expense increased $0.8 million for the three months and $2.7 million for the nine months, due to depreciation expense recognized on the assets acquired through the 2014 Acquisitions as well as additions to fixed assets.

Amortization expense was $7.0 million for the three months ended September 30, 2015 compared to $4.9 million for the three months ended September 30, 2014 and $20.6 million for the nine months ended September 30, 2015 as compared to $13.6 million for the nine months ended September 30, 2014. The increase of $2.1 million for the three months and $7.0 million for the nine months, was due primarily to the amortization expense recognized on intangibles acquired through the 2014 and 2015 acquisitions.

Settlement, Litigation and Other Related Charges

Settlement, litigation and other related charges were $2.1 million for the three months ended September 30, 2015 compared to $1.1 million for the three months ended September 30, 2014 and were $11.3 million for the nine months ended September 30, 2015 as compared to $28.9 million for the nine months ended September 30, 2014. These costs relate to the Corporation's defense and settlement of certain governmental investigations and other litigation.

Restructuring and Impairment Charges

Restructuring and impairment charges were $0.2 million for the three months ended September 30, 2015 compared to $0.1 million for the three months ended September 30, 2014 and were $0.3 million for the nine months ended September 30, 2015 compared to $3.2 million for the nine months ended September 30, 2014. These costs are part of the Corporation's initiative to realign the organization in connection with the loss of two significant customers, which were primarily recognized in 2014, along with the specialty infusion restructuring and centralization initiative in 2015.

Merger, Acquisition, Integration Costs and Other Charges

Merger, acquisition, integration costs and other charges were $8.0 million for the three months ended September 30, 2015 compared to $3.8 million for the three months ended September 30, 2014 and were $15.2 million for the nine months ended September 30, 2015 compared to $10.3 million for the nine months ended September 30, 2014. The increase was related to costs associated with the 2014 and 2015 acquisitions.

Interest Expense

Interest expense was $2.1 million for the three months ended September 30, 2015 and 2014 and was $5.4 for the nine months ended September 30, 2015 compared to $6.9 million for the nine months ended September 30, 2014. The decrease was primarily due to lower interest rates as a result of the new credit agreement signed in 2014, along with lower amortization of deferred financing costs.

Tax Provision

The effective tax rate for the nine months ended September 30, 2015 was 47.5%, comprised of the 35.0% federal statutory rate and 2.2% for the state rate, and 10.3% for discrete events. The discrete events included a non-deductible $4.4 million legal charge and $1.2 million of other items. Excluding the impact of the discrete events, the provision for income taxes as a percentage of pre-tax income would have been 37.2%. The effective tax rate excluding discrete events for the nine months ended September 30, 2014 was 37.0%. The increase in the effective tax rate excluding the

impact of the discrete events between the two periods was primarily the result of an increase in certain non-deductible employee compensation costs.

Liquidity and Capital Resources

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

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2014	2015	2014	2015
Net cash provided by (used in) operating activities	$19.7	$37.5	$(2.4)	$59.6
Net cash used in investing activities	(113.4)	(6.8)	(143.3)	(38.3)
Net cash provided by (used in) financing activities	89.7	(12.0)	128.6	(14.6)
Net change in cash and cash equivalents	(4.0)	18.7	(17.1)	6.7
Cash and cash equivalents at beginning of period	11.1	21.3	24.2	33.3
Cash and cash equivalents at end of period	$7.1	$40.0	$7.1	$40.0

Operating Activities – Cash provided by operating activities aggregated $37.5 million for the three months ended September 30, 2015 and $59.6 million for the nine months ended September 30, 2015 compared to $19.7 million for the three months ended September 30, 2014 and cash used in operating activities of $2.4 million for the nine months ended September 30, 2014. The increase in cash from operating activities is due primarily to the $48.8 million in ABDC drug purchase payments withheld, the Corporation's inventory purchasing strategy and new prime vendor agreement, and an increase in net income in the nine months ended September 30, 2015, which were partially offset by an increase in ABDC rebates receivable.

Investing Activities – Cash used in investing activities aggregated $6.8 million and $38.3 million for the three and nine months ended September 30, 2015, respectively, compared to $113.4 million and $143.3 million for the three and nine months ended September 30, 2014, respectively. The decrease is due to the acquisitions completed by the Corporation in the third quarter of 2014.

Financing Activities – Cash used in financing activities aggregated $12.0 million for the three months ended September 30, 2015 and $14.6 million for the nine months ended September 30, 2015 compared to cash provided by financing activities of $89.7 million and $128.6 million for the three and nine months ended September 30, 2014, respectively. The decrease in cash provided by financing activities is due primarily to borrowings on the revolving credit facility to fund 2014 Acquisitions, along with term and revolving credit facility payments in the third quarter of 2015.

Credit Agreement

On September 17, 2014, the Corporation entered into a Credit Agreement by and among the Corporation, the lenders named therein, Bank of America, N.A., as administrative agent, JP Morgan Chase Bank N.A., as syndication agent, and U.S. Bank, National Association, Citibank, N.A., MUFG Union Bank, N.A., BBVA Compass Bank and SunTrust Bank as co-documentation agents (the "Credit Agreement"). The Credit Agreement consists of a $225.0 million term loan facility and a $310.0 million revolving credit facility. The terms and conditions of the Credit Agreement are customary to facilities of this nature. Unless terminated earlier, the Credit Agreement will mature on September 17, 2019, and the principal amount outstanding thereunder, together with all accrued unpaid interest and other amounts owed thereunder, if any, will be payable in full on such date.

The Credit Agreement requires term loan principal payments by the Corporation in an amount of $2.8 million each quarter beginning September 2015 through September 2019. The final principal repayment installment of term loans shall be repaid on the term maturity date, September 17, 2019. In addition, the term loan is subject to certain

prepayment obligations relating to certain asset sales, certain casualty losses and the incurrence of certain indebtedness.

The Corporation had a total of $222.2 million outstanding of term debt under the Credit Agreement and $115.0 million outstanding under the revolving portion of the Credit Agreement as of September 30, 2015. The Credit Agreement provides for the issuance of letters of credit which, when issued, constitute usage and reduce availability on the revolving portion of the Credit Agreement. The amount of letters of credit outstanding as of September 30, 2015 was $3.0 million. After giving effect to the letters of credit and amounts outstanding under the revolving credit agreement, total availability under the revolving credit facility was $192.0 million as of September 30, 2015.

The Corporation was compliant with all debt covenant requirements at September 30, 2015.

Drug Wholesaler Agreement

We obtain pharmaceutical and other products from Cardinal pursuant to a Prime Vendor Agreement with Cardinal effective April 1, 2015. The Corporation also obtains pharmaceutical and other products for discounted prices directly from pharmaceutical manufacturers. While the loss of a supplier could adversely affect our business if alternate sources of supply are unavailable, numerous sources of supply are generally available to us and we have not experienced any difficulty in obtaining pharmaceuticals or other products and supplies to conduct our business.

The Corporation seeks to maintain an on-site inventory of pharmaceuticals and supplies to ensure prompt delivery to our customers. Cardinal maintains local distribution facilities in most geographic markets in which we operate.

Treasury Stock

In August 2010, the Board of Directors authorized a share repurchase of up to $25.0 million of the Corporation's common stock, of which $10.5 million was used. On July 2, 2012 the Board of Directors authorized an increase to the remaining portion of the existing stock repurchase program that allows the Corporation to again repurchase up to a maximum of $25.0 million of the Corporation's common stock. Approximately $19.7 million remained available under the program as of September 30, 2015. Share repurchases under this authorization may be made in the open market through unsolicited or solicited privately negotiated transactions, or in such other appropriate manner, and may be funded from available cash or the revolving credit facility. The amount and timing of the repurchases, if any, would be determined by the Corporation's management and would depend on a variety of factors including price, corporate and regulatory requirements, capital availability and other market conditions. Common stock acquired through the share repurchase program would be held as treasury shares and may be used for general corporate purposes, including reissuance in connection with acquisitions, employee stock option exercises or other employee stock plans. The share repurchase program does not have an expiration date and may be limited, terminated or extended at any time without prior notice. During the three months ended September 30, 2015, the Corporation repurchased no shares of common stock.

The Corporation may redeem shares from employees upon the vesting of the Corporation's stock awards for minimum statutory tax withholding purposes and to cover option exercise costs. The Corporation redeemed 156,963 shares from the vesting of certain awards and the exercise of certain stock options, for an aggregate price of approximately $4.3 million during the nine months ended September 30, 2015. These shares have also been designated by the Corporation as treasury stock.

Supplemental Quarterly Information

The following tables represent the results of the Corporation's quarterly operations for the year ended December 31, 2014 and for the first, second and third quarters of 2015 (in millions, except where indicated):

	2014 Quarters				2015 Quarters		
	First	Second	Third	Fourth	First	Second	Third
Revenues	$452.2	$448.6	$470.2	$523.5	$511.6	$497.5	$498.8
Cost of goods sold	372.2	366.7	387.2	429.1	423.0	416.3	420.2
Gross profit	80.0	81.9	83.0	94.4	88.6	81.2	78.6
Selling, general and administrative	57.2	57.9	56.0	65.2	59.0	55.4	52.7
Amortization expense	4.4	4.3	4.9	6.5	6.6	7.0	7.0
Merger, acquisition, integration costs, and other charges	5.0	1.5	3.8	3.3	3.8	3.4	8.0
Settlement, litigation and other related charges	1.2	26.6	1.1	8.4	2.3	6.9	2.1
Restructuring and impairment charges	1.9	1.2	0.1	0.1	0.1	-	0.2
Hurricane Sandy disaster costs	-	0.1	-	(1.8)	-	-	0.1
Operating income (loss)	10.3	(9.7)	17.1	12.7	16.8	8.5	8.5
Interest expense, net	2.5	2.3	2.1	3.0	1.4	1.9	2.1
Loss on debt extinguishment	-	-	4.3	-	-	-	-
Income (loss) before income taxes	7.8	(12.0)	10.7	9.7	15.4	6.6	6.4
Provision (benefit) for income taxes	3.0	(2.3)	2.2	6.5	5.8	4.3	3.4
Net income (loss)	$4.8	$(9.7)	$8.5	$3.2	$9.6	$2.3	$3.0
Earnings (loss) per share (1):							
Basic	$0.16	$(0.32)	$0.28	$0.11	$0.32	$0.08	$0.10
Diluted	$0.16	$(0.32)	$0.28	$0.10	$0.31	$0.07	$0.10
Adjusted diluted earnings per diluted share (1)(2):	$0.37	$0.40	$0.45	$0.45	$0.48	$0.37	$0.39
Shares used in computing earnings (loss) per share:							
Basic	29.8	30.0	30.1	30.1	30.2	30.4	30.4
Diluted	30.4	30.0	30.6	30.7	30.7	30.8	30.9
Balance sheet data:							
Cash and cash equivalents	$12.7	$11.1	$7.1	$33.3	$25.2	$21.3	$40.0
Working capital (3)	$273.4	$310.3	$335.1	$319.1	$292.8	$293.5	$285.1
Goodwill (3)	$282.7	$286.9	$319.5	$323.6	$341.9	$341.9	$341.8
Intangible assets, net	$131.9	$130.4	$184.1	$177.6	$179.2	$172.2	$165.2
Total assets (3)	$868.6	$922.5	$1,045.5	$1,074.0	$1,044.9	$1,062.3	$1,060.0
Long-term debt	$230.9	$268.9	$360.9	$350.7	$325.5	$349.3	$337.4
Total stockholders' equity	$470.0	$462.2	$472.7	$478.1	$487.1	$492.1	$496.9
Supplemental information:							
Adjusted EBITDA(2)	$29.7	$30.6	$33.0	$37.3	$37.4	$33.2	$33.3

Adjusted EBITDA Margin (2)	6.6	%	6.8	%	7.0	%	7.1	%	7.3	%	6.7	%	6.7	%
Adjusted EBITDA per prescription dispensed (2)	$3.45		$3.64		$3.89		$3.93		$4.13		$3.93		$4.06	
Net cash provided by (used in) operating activities	$4.4		$(26.5)		$19.7		$50.8		$44.3		$(22.2)		$37.5	
Net cash used in investing activities	$(16.3)		$(13.6)		$(113.4)		$(13.7)		$(25.0)		$(6.5)		$(6.8)	
Net cash (used in) provided by financing activities	$0.4		$38.5		$89.7		$(10.9)		$(27.4)		$24.8		$(12.0)	
Statistical information (in whole numbers except where indicated)														
Volume information														
Prescriptions dispensed (in thousands)	8,608		8,411		8,492		9,491		9,053		8,452		8,208	
Revenue per prescription dispensed	$52.53		$53.33		$55.37		$55.16		$56.51		$58.86		$60.77	
Gross profit per prescription dispensed	$9.29		$9.74		$9.77		$9.95		$9.79		$9.61		$9.58	
Gross profit margin	17.7	%	18.3	%	17.7	%	18.0	%	17.3	%	16.3	%	15.8	%
Generic drug dispensing rate	84.5	%	85.0	%	85.1	%	84.9	%	85.3	%	86.0	%	86.5	%
Inventory days on hand	26.0		35.1		31.7		29.1		26.1		29.6		25.7	
Revenue days outstanding	37.7		37.0		36.7		34.9		34.0		35.4		35.5	

(1) The Corporation has never declared a cash dividend. Earnings (loss) per common share in actual cents.

(2) See "Use of Non-GAAP Measures for Measuring Quarterly Results" for a definition and Reconciliation of Adjusted Earnings Per Diluted Common Share to Earnings (Loss) Per Diluted Common Share, and for Reconciliation of Net Income (Loss) to Adjusted EBITDA and Adjusted EBITDA Margin.

(3) As adjusted, see Note 2—Acquisitions in the Condensed Consolidated Financial Statements.

Use of Non-GAAP Measures for Measuring Quarterly Results

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

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

Unaudited Reconciliation of Net Income (Loss) to Adjusted EBITDA (dollars in millions)

	2014 Quarters				2015 Quarters		
	First	Second	Third	Fourth	First	Second	Third
Net income (loss)	$4.8	$ (9.7)	$8.5	$ 3.2	$9.6	$ 2.3	$3.0
Add:							
Interest expense, net	2.5	2.3	2.1	3.0	1.4	1.9	2.1
Merger, acquisition, integration costs and other charges	5.0	1.5	3.1	3.3	3.8	3.4	8.0
Settlement, litigation and other related charges	1.2	26.6	1.1	8.4	2.3	6.9	2.1
Restructuring and impairment charges	1.9	1.2	0.1	0.1	0.1	-	0.2
Loss on extinguishment of debt	-	-	4.3	-	-	-	-
Hurricane Sandy disaster costs	-	0.1	-	(1.8)	-	-	0.1
Stock-based compensation and deferred compensation	2.1	1.8	1.8	2.3	2.0	1.7	1.7
Provision (benefit) for income taxes	3.0	(2.3)	2.2	6.5	5.8	4.3	3.4
Depreciation and amortization expense	9.2	9.1	9.8	12.3	12.4	12.7	12.7
Adjusted EBITDA	$29.7	$ 30.6	$33.0	$ 37.3	$37.4	$ 33.2	$33.3
Adjusted EBITDA Margin	6.6 %	6.8 %	7.0 %	7.1 %	7.3 %	6.7 %	6.7 %

Unaudited Reconciliation of Adjusted EBITDA to Net Operating Cash Flows (dollars in millions)

	2014 Quarters				2015 Quarters		
	First	Second	Third	Fourth	First	Second	Third
Adjusted EBITDA	$29.7	$ 30.6	$33.0	$37.3	$37.4	$ 33.2	$33.3
Interest expense, net	(2.5)	(2.3)	(2.1)	(3.0)	(1.4)	(1.9)	(2.1)
Merger, acquisition, integration costs and other charges	(5.6)	(29.4)	(4.3)	(11.8)	(6.2)	(10.3)	(10.4)
Provision for bad debt	5.6	5.7	5.3	6.6	5.0	3.0	1.5
Amortization of deferred financing fees	0.7	0.6	0.5	0.1	0.1	0.2	0.1
(Gain) loss on disposition of equipment	(0.1)	-	-	-	0.1	-	-
(Gain) loss on acquisition	(0.3)	-	0.1	-	-	-	-
Provision (benefit) for income taxes	(3.0)	2.3	(2.2)	(6.5)	(5.8)	(4.3)	(3.4)
Deferred income taxes	4.0	(3.3)	(4.0)	1.0	2.3	0.2	2.1
Changes in federal and state income tax payable (receivable)	(1.3)	(2.8)	3.7	7.6	0.1	(9.1)	(1.0)
Excess tax benefit from stock-based compensation	(2.7)	(0.5)	(0.2)	-	(1.9)	(0.2)	(0.2)
Changes in assets and liabilities	(20.2)	(27.4)	(10.1)	19.1	14.6	(33.1)	17.6
Other	0.1	-	-	0.4	-	0.1	-
Net Cash Flows Provided by (Used in) Operating Activities	$4.4	$ (26.5)	$19.7	$50.8	$44.3	$ (22.2)	$37.5

Unaudited Reconciliation of Diluted Earnings (Loss) Per Share to Adjusted Diluted Earnings Per Share

	2014 Quarters				2015 Quarters		
	First	Second	Third	Fourth	First	Second	Third
Diluted earnings (loss) per share	$0.16	$ (0.32)	$0.28	$0.10	$0.31	$ 0.07	$0.10
Add:							
Diluted earnings per share impact of:							
Merger, acquisition, integration costs and other charges	0.10	0.03	0.06	0.08	0.08	0.07	0.17

Settlement, litigation and other related charges	0.03	0.61	0.02	0.11	0.05	0.13	0.04
Restructuring and impairment charges	0.04	0.03	-	-	-	-	0.01
Loss on extinguishment of debt	-	-	0.09	-	-	-	-
Hurricane Sandy disaster costs	-	-	-	(0.04)	-	-	-
Stock-based compensation and deferred compensation	0.04	0.04	0.04	0.05	0.04	0.04	0.04
Impact of discrete items on tax provision	-	0.01	(0.04)	0.15	-	0.06	0.03
Adjusted diluted earnings per share	$0.37	$0.40	$0.45	$0.45	$0.48	$ 0.37	$0.39

Item 3. Quantitative and Qualitative Disclosures about Market Risk

During the reporting period, there have been no material changes in the disclosures set forth in Part II, Item 7a in our Form 10-K for the year ended December 31, 2014.

Item 4. Controls and Procedures

Evaluation of Disclosure Controls and Procedures

The Corporation has carried out an evaluation under the supervision and with the participation of management, including the Corporation's Chief Executive Officer and Chief Financial Officer, of the effectiveness of the design and operation of the Corporation's "disclosure controls and procedures" as defined in Rule 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934, as amended (the "Exchange Act") as of the end of the period covered by this report. The Corporation's disclosure controls and procedures are designed so that information required to be disclosed in the Corporation's reports filed under the Exchange Act, such as this Quarterly Report on Form 10-Q, is recorded, processed, summarized and reported within the time periods specified in the Commission's rules and forms. The Corporation's disclosure controls and procedures are also intended to ensure that such information is accumulated and communicated to the Corporation's management, including the Chief Executive Officer and Chief Financial Officer, as appropriate to allow timely decisions regarding required disclosure. There are inherent limitations to the effectiveness of any system of disclosure controls and procedures, including the possibility of human error and the circumvention or overriding of the controls and procedures. Accordingly, even effective disclosure controls and procedures can only provide reasonable assurance of achieving their control objectives, and management necessarily is required to use its judgment in evaluating the cost-benefit relationship of possible disclosure controls and procedures. Based upon this evaluation, the Chief Executive Officer and Chief Financial Officer have concluded that, as of September 30, 2015, the Corporation's disclosure controls and procedures are effective to provide reasonable assurance that information required to be disclosed in the reports that the Corporation files and submits under the Exchange Act is recorded, processed, summarized and reported as and when required and such information is accumulated and communicated as appropriate to allow timely decisions regarding required disclosures.

Changes in Internal Control Over Financial Reporting

There have been no changes in the Corporation's internal control over financial reporting during the quarter ended September 30, 2015, that have materially affected, or are reasonably likely to materially affect, the Corporation's internal control over financial reporting.

PART II. OTHER INFORMATION

Item 1. Legal Proceedings

The information called for by this item is incorporated herein by reference to Note 5 included in Part I, Item 1, Financial Statements (Unaudited) - Notes to Condensed Consolidated Financial Statements.

Item 1A. Risk Factors

Except as set forth below, there have been no material changes in our risk factors from those disclosed in the Corporation's Annual Report on Form 10-K for the year ended December 31, 2014. We encourage you to read these risk factors, together with the risk factor below, in their entirety.

If we fail to comply with the terms of our Corporate Integrity Agreement with the OIG or Memorandum of Agreement with the DEA, it could subject us to substantial monetary penalties or suspension or termination from participation in federal healthcare programs.

In May 2015, the Corporation entered into a five-year corporate integrity agreement ("CIA") with the United States Department of Health and Human Services Office of Inspector General ("OIG") and a Memorandum of Agreement ("MOA") with the Drug Enforcement Agency ("DEA") concurrent with the execution of settlement agreements with the OIG and the DEA settling alleged Controlled Substance Act ("CSA") violations and associated False Claims Act allegations.

The CIA requires the Corporation, among other things to: (i) create procedures designed to ensure it complies with the CSA and related regulations; (ii) retain an independent review organization to review the Corporation's compliance with the terms of the CIA and report to the OIG regarding that compliance; and (iii) provide training for certain Corporation employees as to the Corporation's requirements under the CSA. If the Corporation fails to comply with the terms of the CIA, it may be required to pay certain monetary penalties. The imposition of monetary penalties would adversely affect our profitability. Furthermore, if the Corporation commits a material breach of the CIA, the OIG may exclude the Corporation from participating in federal healthcare programs. Any such exclusion would result in the revocation or termination of contracts and/or licenses and potentially have a material adverse effect on our financial condition, results of operations and business prospects.

The MOA provides for an independent obligation for the Corporation to comply with all requirements of the CSA, specifically relating to the dispensing of scheduled prescription drugs. If the Corporation fails to comply with the terms of the MOA, the DEA may suspend a Corporation's pharmacy's DEA Certificate of Registration and begin an administrative hearing process pursuant to 21 U.S.C. § 824. Any such suspension would prohibit the Corporation's pharmacy from dispensing Scheduled prescription drugs and would lead to the revocation or termination of contracts and/or licenses and potentially have a materially adverse effect on our financial condition, results of operation and business prospects.

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

In August 2010, the Board of Directors authorized a share repurchase program of up to $25.0 million of the Corporation's common stock, of which $10.5 million was used. On July 2, 2012, the Board of Directors authorized an increase to the remaining portion of the existing share repurchase program that allows the Corporation to again repurchase up to a maximum of $25.0 million of the Corporation's common stock. The Corporation did not repurchase any common stock shares under this program during the nine months ended September 30, 2015.

Additionally, the Corporation may redeem shares from employees upon vesting of the Corporation's stock awards for minimum statutory tax withholding purposes and to cover option exercise costs. The Corporation redeemed 156,963 shares from the vesting of certain awards and the exercise of certain stock options, for an aggregate price of approximately $4.3 million during the nine months ended September 30, 2015. These shares have been designated by the Corporation as treasury stock.

The following table summarizes our share repurchase activity by month for the three months ended September 30, 2015:

Period	Total Number of Shares Purchased		Weighted Average Price Paid per Share	Total Number of Shares Purchased as Part of a Publicly Announced Plans or Programs (2)	Approximate Dollar Value of Shares that may yet be Purchased under the Plans or Programs (in millions)
July 1, 2015 - July 31, 2015	277	(1)	$ 35.28	-	$ 19.7
August 1, 2015 - August 31, 2015	8,456	(1)	34.08	-	19.7
September 1, 2015 - September 30, 2015	3,746	(1)	31.34	-	19.7

(1) The Corporation repurchased 12,479 shares of common stock in connection with the vesting of certain stock awards to cover minimum statutory withholding taxes.

(2) On August 24, 2010, the Board of Directors announced a share repurchase program whereby the Corporation is authorized to purchase up to $25.0 million of the Corporation's common stock, of which $10.5 million was used. On July 2, 2012, the Board of Directors authorized an increase to the remaining portion of the existing share repurchase program that allows the Corporation to again repurchase up to a maximum of $25.0 million of the Corporation's common stock. The Corporation did not repurchase any common stock shares under this program during the nine months ended September 30, 2015.

Item 4. Mine Safety Disclosures

Not Applicable

Item 6. Exhibits

Exhibit No.	
10.28*	Corporate Integrity Agreement, dated May 14, 2015, by and between PharMerica Corporation and the Office of Inspector General of the United States Department of Health and Human Services.
10.29*	Memorandum of Agreement, dated May 14, 2015, by and between PharMerica Corporation and the United States Department of Justice, Drug Enforcement Administration.
31.1*	Certification of Chief Executive Officer required by Rule 13a-14(a) or Rule 15d-14(a) of the Securities Exchange Act of 1934, as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
31.2*	Certification of Chief Financial Officer required by Rule 13a-14(a) or Rule 15d-14(a) of the Securities Exchange Act of 1934, as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
32.1*	Certification of Chief Executive Officer, pursuant to 18 U.S.C. 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002
32.2*	Certification of Chief Financial Officer pursuant to 18 U.S.C. 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002
101.INS	XBRL Instance Document.
101.SCH	XBRL Taxonomy Extension Schema Document.
101.CAL	XBRL Taxonomy Extension Calculation Linkbase Document.
101.DEF	XBRL Taxonomy Extension Definition Linkbase Document.
101.LAB	XBRL Taxonomy Extension Label Linkbase Document.
101.PRE	XBRL Taxonomy Extension Presentation Linkbase Document.

*Furnished herewith.

SIGNATURES

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

PHARMERICA CORPORATION

Date: November 6, 2015 /s/ Gregory S. Weishar
Gregory S. Weishar
Chief Executive Officer and
Director

Date: November 6, 2015 /s/ David W. Froesel, Jr.
David W. Froesel, Jr.
Executive Vice President, Chief
Financial Officer and Treasurer

/s/ Berard E. Tomassetti
Date: November 6, 2015 Berard E. Tomassetti
Senior Vice President and
Chief Accounting Officer

Exhibit Index

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