RENAL CARE GROUP INC
Form 10-Q
August 09, 2004

Table of Contents

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

FORM 10-Q

(Mark One)

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

For the Quarterly Period Ended June 30, 2004

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 No. 0-27640

RENAL CARE GROUP, INC.

(Exact name of registrant as specified in its charter)

Delaware	**62-1622383**
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

2525 West End Avenue, Suite 600, Nashville, Tennessee 37203
(Address of principal executive offices) (Zip code)

Registrant s telephone number, including area code: **(615) 345-5500**

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

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

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

Class	Outstanding at August 5, 2004
Common Stock, $.01 par value	67,070,176

RENAL CARE GROUP, INC.

INDEX

		Page No.
PART I FINANCIAL INFORMATION		
Item 1.	Financial Statements	
	Condensed Consolidated Balance Sheets December 31, 2003 and June 30, 2004 (unaudited)	1
	Condensed Consolidated Income Statements (unaudited) For the three months and six months ended June 30, 2003 and 2004	2
	Condensed Consolidated Statements of Cash Flows (unaudited) For the six months ended June 30, 2003 and 2004	3
	Notes to Condensed Consolidated Financial Statements (unaudited)	4
Item 2.	Management s Discussion and Analysis of Financial Condition and Results of Operations	15
	Risk Factors	20
Item 3.	Quantitative and Qualitative Disclosures About Market Risk	28
Item 4.	Controls and Procedures	28
PART II	OTHER INFORMATION	
Item 2.	Changes in Securities, Use of Proceeds and Issuer Purchases of Equity Securities	29
Item 4.	Submission of Matters to a Vote of Security Holders	29
Item 6.	Exhibits and Reports on Form 8-K	30
Signature		31
Exhibit Index		32

EX-31.1 SECTION 302 CEO CERTIFICATION
EX-31.2 SECTION 302 CFO CERTIFICATION
EX-32.1 SECTION 906 CEO CERTIFICATION
EX-32.2 SECTION 906 CFO CERTIFICATION

Note: Items 1, 3, and 5 of Part II are omitted because they are not applicable

Table of Contents

PART I FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

RENAL CARE GROUP, INC.

Condensed Consolidated Balance Sheets
(in thousands, except per share data)

	December 31, 2003	June 30, 2004
		(unaudited)
ASSETS		
Current assets:		
Cash and cash equivalents	$ 50,295	$ 44,182
Accounts receivable, net	173,679	231,629
Inventories	26,345	24,161
Prepaid expenses and other current assets	28,050	24,259
Income tax receivable	1,910	10,643
Deferred income taxes	11,825	21,958
Total current assets	292,104	356,832
Property, plant and equipment, net	224,397	289,427
Intangible assets, net	14,046	30,700
Goodwill	286,578	626,656
Other assets	2,748	7,469
Total assets	$ 819,873	$ 1,311,084
LIABILITIES AND STOCKHOLDERS EQUITY		
Current liabilities:		
Accounts payable and accrued expenses	$ 123,206	$ 129,019
Due to third-party payors	46,049	68,700
Current portion of long-term debt	182	20,834
Total current liabilities	169,437	218,553
Long-term debt, net of current portion	2,652	490,635
Deferred income taxes	38,390	35,841
Other long-term liabilities	5,898	10,211
Minority interest	32,651	43,200
Total liabilities	249,028	798,440

Commitments and contingencies		
Stockholders equity:		
Preferred stock, $0.01 par value, 10,000 shares authorized, none issued		
Common stock, $0.01 par value, 90,000 and 150,000 shares authorized, 80,465 and 81,572 shares issued at December 31, 2003 and June 30, 2004, respectively	805	816
Treasury stock, 9,961 and 14,514 shares of common stock at December 31, 2003 and June 30, 2004, respectively	(234,404)	(372,249)
Additional paid-in capital	374,414	394,777
Retained earnings	430,030	489,300
Total stockholders equity	570,845	512,644
Total liabilities and stockholders equity	$ 819,873	$1,311,084

See accompanying notes to condensed consolidated financial statements.

1

Table of Contents

RENAL CARE GROUP, INC.

Condensed Consolidated Income Statements
(in thousands, except per share data)
(unaudited)

	Three Months Ended June 30,		Six Months Ended June 30,	
	2003	**2004**	**2003**	**2004**
Net revenue	$247,061	$340,854	$489,204	$618,882
Operating costs and expenses:				
Patient care costs	159,998	229,849	317,475	409,221
General and administrative expenses	21,187	27,341	47,475	50,017
Provision for doubtful accounts	6,468	8,049	12,880	15,159
Depreciation and amortization	11,579	14,900	21,877	27,063
Total operating costs and expenses	199,232	280,139	399,707	501,460
Income from operations	47,829	60,715	89,497	117,422
Interest expense, net	165	5,765	450	6,730
Income before minority interest and income taxes	47,664	54,950	89,047	110,692
Minority interest	6,029	7,690	12,337	14,904
Income before income taxes	41,635	47,260	76,710	95,788
Provision for income taxes	15,822	18,077	29,145	36,518
Net income	$ 25,813	$ 29,183	$ 47,565	$ 59,270
Net income per share:				
Basic	$ 0.35	$ 0.44	$ 0.66	$ 0.87
Diluted	$ 0.34	$ 0.42	$ 0.64	$ 0.84
Weighted average shares outstanding:				
Basic	72,806	66,832	72,539	67,871

Diluted	74,897	69,227	74,522	70,225

See accompanying notes to condensed consolidated financial statements.

Table of Contents

RENAL CARE GROUP, INC.

Condensed Consolidated Statements of Cash Flows
(in thousands)
(unaudited)

	Six Months Ended June 30,	
	2003	**2004**
OPERATING ACTIVITIES		
Net income	$ 47,565	$ 59,270
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	21,877	27,063
Loss on disposal of property and equipment	312	564
Income applicable to minority interest	12,337	14,904
Distributions to minority shareholders	(12,381)	(9,906)
Deferred income taxes		7,889
Changes in operating assets and liabilities, net of effects from acquisitions	5,404	(18,605)
Net cash provided by operating activities	75,114	81,179
INVESTING ACTIVITIES		
Cash paid for acquisitions, net of cash acquired	(5,492)	(230,746)
Purchases of property and equipment, net	(34,517)	(45,031)
Change in other assets	(780)	(5,299)
Net cash used in investing activities	(40,789)	(281,076)
FINANCING ACTIVITIES		
Proceeds from issuance of long-term debt		325,000
Payments on long-term debt		(4,063)
Net payments under line of credit and capital leases	(7,240)	(2,101)
Net proceeds from issuance of common stock	22,280	12,793
Repurchase of treasury shares	(4,380)	(137,845)
Net cash provided by financing activities	10,660	193,784
Increase (decrease) in cash and cash equivalents	44,985	(6,113)
Cash and cash equivalents at beginning of period	38,359	50,295
Cash and cash equivalents at end of period	$ 83,344	$ 44,182

See accompanying notes to condensed consolidated financial statements.

Table of Contents

RENAL CARE GROUP, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
JUNE 30, 2004
(dollars in thousands, except per share data)
(unaudited)

1. Basis of Presentation

Overview

Renal Care Group, Inc. (the Company) provides dialysis services to patients with chronic kidney failure, also known as end-stage renal disease (ESRD). As of June 30, 2004, the Company provided dialysis and ancillary services to over 28,700 patients through more than 395 owned outpatient dialysis centers in 31 states, in addition to providing acute dialysis services at more than 200 hospitals.

Renal Care Group s net revenue has been derived primarily from the following sources:

outpatient hemodialysis services;

ancillary services associated with dialysis, primarily the administration of EPOGEN® (erythropoietin alfa, which we refer to as EPO);

home dialysis services;

inpatient hemodialysis services provided to acute care hospitals and skilled nursing facilities;

laboratory services; and

management contracts with joint ventures, hospital-based dialysis programs and medical university dialysis programs.

Most patients with end-stage renal disease receive three dialysis treatments each week in an outpatient setting. Reimbursement for these services is provided primarily by the Medicare ESRD program based on rates established by the Centers for Medicare and Medicaid Services (CMS). For the six months ended June 30, 2003 and 2004, approximately 55% and 53%, respectively, of the Company s net revenue was derived from reimbursement under the Medicare and Medicaid programs. Medicare reimbursement is subject to rate and other legislative changes by Congress and periodic changes in regulations, including changes that may reduce payments under the ESRD program. Neither Congress nor CMS approved an increase in the composite rate for 2003 or 2004. Congress has approved an increase of 1.6% in the Medicare ESRD composite rate for 2005, as well as changes in the way we are paid for separately billable drugs. The Medicare Modernization Act of 2003 provides that dialysis providers will be reimbursed for separately billable drugs, including EPO, at the drugs average acquisition cost and that the composite rate will be increased by an amount equal to the providers lost profit on those separately billable drugs. Congress stated that it intended these changes to be budget neutral. On July 27, 2004 CMS issued proposed regulations to implement these changes, which propose that we will be reimbursed for separately billable drugs at a 3% discount from the average sale price and that the composite rate be increased by 11.3%. These proposed regulations also include a case-mix adjustment and a geographic adjustment to the composite rate as well as a related budget neutrality adjustment. If the proposed regulations become effective, management believes they will result in a net reduction of $0.03 per share in diluted net income for 2005.

The Medicare composite rate applies to a designated group of outpatient dialysis services, including the dialysis treatment, supplies used for the treatment, certain laboratory tests and medications, and most of the home dialysis services we provide. Renal Care Group receives separate reimbursement outside the composite rate for some other services, laboratory tests and drugs, including specific drugs such as EPO and some physician-ordered tests provided to dialysis patients. Congress and CMS have considered expanding the drugs and services that are included in the composite rate.

Table of Contents

If a patient is younger than 65 years old and has private health insurance, then that patient s treatment is typically reimbursed at rates significantly higher than Medicare during the first 30 months of care. After that period, Medicare becomes the primary payor. Reimbursement for dialysis services provided pursuant to a hospital contract is negotiated with the individual hospital and is usually higher than the Medicare composite rate. Because dialysis is a life-sustaining therapy to treat a chronic disease, utilization is predictable and is not subject to seasonal fluctuations.

Renal Care Group derives a significant portion of its net revenue and net income from the administration of EPO. EPO is manufactured by a single company, Amgen Inc. The Company administers EPO to most of its patients to treat anemia, a medical complication frequently experienced by dialysis patients. Net revenue from the administration of EPO was 24% and 27% of the net revenue of the Company for the six months ended June 30, 2003 and 2004, respectively.

Interim Financial Statements

Management believes the information contained in this quarterly report on Form 10-Q reflects all adjustments necessary to make the results of operations for the interim periods a fair representation of such operations. All of these adjustments are of a normal recurring nature. Operating results for interim periods are not necessarily indicative of results that may be expected for the year as a whole. We suggest that you read these financial statements in conjunction with our consolidated financial statements and the related notes thereto included in our current report on Form 8-K, as filed with the SEC on April 19, 2004.

2. Business Acquisitions

2004 Acquisitions

During the first six months of 2004, we completed three acquisitions. The combined net assets acquired and resulting net cash purchase price paid in these acquisitions were $230,746. Our largest acquisition was the purchase of National Nephrology Associates, Inc. (NNA) on April 2, 2004. The purchase price of NNA consisted of a net cash payment of approximately $163,000 and an assumption of all outstanding debt, including its $160,000, 9% senior subordinated notes. NNA provided dialysis services to approximately 5,600 patients and operated 87 outpatient dialysis facilities in 15 states, as well as providing acute dialysis services to approximately 55 hospitals. Each of the three transactions involved the acquisition of entities that provide care to ESRD patients through owned dialysis facilities. The acquired businesses either strengthened existing market share within a specific geographic area or provided an entrance into a new market. We began recording the results of operations for each of these acquired businesses at the effective date of the transaction.

The following table summarizes the preliminarily estimated fair values of the assets acquired and liabilities assumed at the date of acquisition for the three acquisitions completed during the first six months of 2004:

Accounts receivable, net	$ 45,410
Inventory and other current assets	23,382
Property, plant and equipment, net	48,818
Intangible assets	16,651
Goodwill	340,078
Other assets	10,397
Total assets acquired	484,736

Total liabilities assumed	253,990
Net assets acquired	$230,746

Some of the estimated fair values of assets and liabilities are preliminary and may be adjusted based on management s final analysis. These include items such as deferred tax assets and liabilities, a pending actuarial analysis of workers compensation and medical malpractice accruals, and obtaining independent appraisals for certain assets. Intangible assets primarily represent the value assigned to certain contracts such as non-competition agreements and acute dialysis service agreements entered into in the transactions. Related amounts will be amortized over the lives of the contracts, which generally range from five to fifteen years. The Company recorded estimated employee severance costs of $1,000 and estimated contract termination costs of $1,500 associated with the NNA acquisition. As of June 30, 2004 these amounts remain outstanding pending the employee terminations and resolution of the contractual matters.

Pro Forma Data

The following summary, prepared on a pro forma basis, combines our results of operations with those of the businesses we acquired in 2003 and 2004. These pro forma results reflect the acquisitions as if we consummated them as of the beginning of the periods presented, giving effect to adjustments such as amortization of intangibles, interest expense and related income taxes.

	Three Months Ended June 30,		Six Months Ended June 30,	
	2003	**2004**	**2003**	**2004**
Pro forma net revenue	$316,758	$341,425	$626,502	$685,068
Pro forma net income	$ 26,958	$ 29,261	$ 50,668	$ 60,876
Pro forma net income per share:				
Basic	$ 0.37	$ 0.44	$ 0.70	$ 0.90
Diluted	$ 0.36	$ 0.42	$ 0.68	$ 0.87

The unaudited pro forma results of operations are not necessarily indicative of what actually would have occurred if the acquisitions had been completed as of the beginning of the periods presented.

3. Long Term Debt

Long term debt consisted of the following as of December 31, 2003 and June 30, 2004:

	December 31, 2003	**June 30, 2004**
Term loan facility, bearing interest at 2.7% at June 30, 2004	$	$320,938
9% senior subordinated notes		159,700
Other	2,834	5,884
Total indebtedness, excluding fair value premium	2,834	486,522
Add: 9% senior subordinated notes fair value premium		24,947

Total long-term debt	2,834	511,469
Less: current portion	182	20,834
	$ 2,652	$490,635

Credit Agreements

As of December 31, 2003, we had two credit agreements with a group of banks totaling $150,000. On February 10, 2004, we entered into a new credit agreement (the 2004 Agreement) with a group of banks totaling up to $700,000. The 2004 Agreement replaced both of our prior facilities. The 2004 agreement has a $150,000 revolving credit facility, a $325,000 term loan facility and a $225,000 incremental term loan facility. Borrowings under the incremental term loan facility are subject to obtaining commitments from the banks and finalizing specific terms. The revolving credit facility and the $325,000 term loan facility have a final maturity of February 10, 2009. Each of our wholly-owned subsidiaries has guaranteed all of our obligations under the 2004 Agreement. Further, our obligations under the 2004 Agreement, and our subsidiaries obligations under their guarantees, are secured by a pledge of the equity interests we hold in each of our subsidiaries. The 2004 Agreement includes financial covenants that are customary based on the amount and duration of the agreement.

Borrowings under the revolving credit facility and $150,000 of the committed term loan facility under the 2004 Agreement may be used for acquisitions, repurchases of Company common stock, capital expenditures, working capital and general corporate purposes. Borrowings under the 2004 Agreement bear interest at variable rates determined by the Company s leverage ratio. Effective June 30, 2004, we entered into interest rate swap agreements to hedge interest rate risk on $150,000 of our term loan (See Interest Rate Swap below). The portion of our borrowings that is subject to variable rates carries a degree of interest rate risk. Specifically, the Company will face higher interest costs on this debt if interest rates rise.

Table of Contents

9% Senior Subordinated Notes

With our acquisition of NNA, we assumed all of NNA s outstanding debt including its 9% senior subordinated notes (the Notes), due 2011. We recorded the Notes at the face value of $160,000 plus an additional $25,600 representing the difference between the fair value of the Notes and the face amount on the date of acquisition. Accordingly, the Notes were recorded at the estimated fair value of $185,600. As of June 30, 2004, the outstanding balance of the Notes was $184,647.

The Notes bear interest at the rate of 9% per annum on the face amount. The $24,947 fair value premium that is unamortized is being recognized over the life of the Notes using the effective interest method and is recorded as a reduction to interest expense. Accordingly, the effective interest rate on the Notes as of June 30, 2004 was 6.4%. Each of our wholly-owned subsidiaries has guaranteed all of our obligations under these notes. The rights of the noteholders and our obligations under these notes are set forth in an indenture that NNA entered into in October 2003 and we assumed in connection with the NNA acquisition. The indenture includes customary financial covenants.

Interest Rate Swap

On June 3, 2004, we entered into interest rate swap agreements to hedge the interest rate risk on $150,000 of our term loan. These interest rate swap agreements became effective on June 30, 2004. Under these interest rate swap agreements we will exchange fixed and variable rate interest payments based on a $150,000 notional principal amount through March 30, 2007. The notional amount of $150,000 and interest payments of 3.5% are fixed in the agreements, with the interest payments being subject to adjustment based on our leverage ratio. The changes in cash flows under these agreements are expected to offset the changes in interest rate payments attributable to fluctuations in LIBOR. The hedge is structured to qualify for the shortcut method; therefore, changes in the fair value of the agreement will be directly recorded in comprehensive income. The interest payments under this agreement are settled on a net basis each calendar quarter.

The aggregate maturities of long-term debt, excluding the fair value premium, at June 30, 2004 are as follows:

2004	$ 14,009
2005	22,344
2006	30,469
2007	56,875
2008	156,406
Thereafter	206,419
	$486,522

Guarantor Information

Our wholly-owned subsidiaries have guaranteed the Notes as well as our obligations under the 2004 Agreement. We conduct substantially all of our business through subsidiaries. Presented below is condensed consolidating financial information as of June 30, 2004 and December 31, 2003 and for the three months and six months ended June 30, 2004 and 2003. The information segregates Renal Care Group, Inc. (the parent company), the combined wholly-owned subsidiary guarantors, the combined non-guarantor subsidiaries and consolidating adjustments. All of

the subsidiary guarantees are both full and unconditional, and joint and several.

Condensed Consolidating Balance Sheets

	Parent Company	Guarantor Subsidiaries	Non-Guarantor Subsidiaries	Consolidating Adjustments	Consolidated Total
As of December 31, 2003					
Cash and cash equivalents	$ 20,157	$ 2,646	$ 27,492	$	$ 50,295
Accounts receivable, net		117,209	56,470		173,679
Other current assets	35,329	21,467	11,334		68,130
Total current assets	55,486	141,322	95,296		292,104
Property, plant and equipment, net	27,841	123,894	69,924	2,738	224,397
Goodwill	1,483	187,848	96,947	300	286,578
Other assets	10,637	25,926	5,940	(25,709)	16,794
Total assets	$ 95,447	$478,990	$268,107	$(22,671)	$ 819,873
Current liabilities (including intercompany assets and liabilities)	$(261,412)	$315,138	$126,004	$(10,293)	$ 169,437
Long-term debt			2,652		2,652
Long-term liabilities	42,951	1,243	94		44,288
Minority interest		30,091	2,347	213	32,651
Stockholders equity	313,908	132,518	137,010	(12,591)	570,845
Total liabilities and stockholders equity	$ 95,447	$478,990	$268,107	$(22,671)	$ 819,873

	Parent Company	Guarantor Subsidiaries	Non-Guarantor Subsidiaries	Consolidating Adjustments	Consolidated Total
As of June 30, 2004					
Cash and cash equivalents	$	$ 9,473	$ 38,178	$ (3,469)	$ 44,182
Accounts receivable, net		174,193	56,933	503	231,629
Other current assets	50,018	23,223	8,810	(1,030)	81,021
Total current assets	50,018	206,889	103,921	(3,996)	356,832
Property, plant and equipment, net	33,486	169,666	84,805	1,470	289,427

Goodwill	1,483	497,123	127,750	300	626,656
Other assets	26,692	89,526	5,788	(83,837)	38,169
Total assets	$ 111,679	$963,204	$322,264	$(86,063)	$1,311,084
Current liabilities (including intercompany assets and liabilities)	$(653,702)	$736,258	$161,530	$(25,533)	$ 218,553
Long-term debt	487,301	327	3,007		490,635
Long-term liabilities	43,340	2,400	312		46,052
Minority interest		38,892	4,095	213	43,200
Stockholders equity	234,740	185,327	153,320	(60,743)	512,644
Total liabilities and stockholders equity	$ 111,679	$963,204	$322,264	$(86,063)	$1,311,084

Table of Contents

Condensed Consolidating Income Statements

	Parent Company	Guarantor Subsidiaries	Non-Guarantor Subsidiaries	Consolidating Adjustments	Consolidated Total
For the three months ended June 30, 2003					
Net revenue	$ 89	$170,386	$ 77,640	$(1,054)	$247,061
Total operating costs and expenses	9,995	129,085	61,206	(1,054)	199,232
Income (loss) from operations	(9,906)	41,301	16,434		47,829
Interest expense, net	165				165
Minority interest		5,325	704		6,029
Provision (benefit) for income taxes	(3,827)	13,672	5,977		15,822
Net income (loss)	$ (6,244)	$ 22,304	$ 9,753	$	$ 25,813

	Parent Company	Guarantor Subsidiaries	Non-Guarantor Subsidiaries	Consolidating Adjustments	Consolidated Total
For the three months ended June 30, 2004					
Net revenue	$ 747	$241,216	$100,123	$(1,232)	$340,854
Total operating costs and expenses	15,845	188,368	77,158	(1,232)	280,139
Income (loss) from operations	(15,098)	52,848	22,965		60,715
Interest expense, net	5,765				5,765
Minority interest		7,434	256		7,690
Provision (benefit) for income taxes	(7,980)	17,371	8,686		18,077
Net income (loss)	$(12,883)	$ 28,043	$ 14,023	$	$ 29,183

Table of Contents

Condensed Consolidating Income Statements

	Parent Company	Guarantor Subsidiaries	Non-Guarantor Subsidiaries	Consolidating Adjustments	Consolidated Total
For the six months ended June 30, 2003					
Net revenue	$ 89	$339,961	$151,208	$(2,054)	$489,204
Total operating costs and expenses	24,308	257,531	119,922	(2,054)	399,707
Income (loss) from operations	(24,219)	82,430	31,286		89,497
Interest expense, net	450				450
Minority interest		10,905	1,432		12,337
Provision (benefit) for income taxes	(9,372)	27,175	11,342		29,145
Net income (loss)	$(15,297)	$ 44,350	$ 18,512	$	$ 47,565

	Parent Company	Guarantor Subsidiaries	Non-Guarantor Subsidiaries	Consolidating Adjustments	Consolidated Total
For the six months ended June 30, 2004					
Net revenue	$ 934	$428,870	$191,509	$(2,431)	$618,882
Total operating costs and expenses	26,151	329,491	148,249	(2,431)	501,460
Income (loss) from operations	(25,217)	99,379	43,260		117,422
Interest expense, net	6,730				6,730
Minority interest		14,020	884		14,904
Provision (benefit) for income taxes	(12,192)	32,550	16,160		36,518
Net income (loss)	$(19,755)	$ 52,809	$ 26,216	$	$ 59,270

Table of Contents

Condensed Consolidating Statements of Cash Flows

	Parent Company	Guarantor Subsidiaries	Non-Guarantor Subsidiaries	Consolidating Adjustments	Consolidated Total
For the six months ended June 30, 2003					
Cash flows from operating activities:					
Net income (loss)	$ (15,297)	$ 44,350	$ 18,512	$	$ 47,565
Changes in operating and intercompany assets and liabilities and non-cash items included in net income	59,497	(24,757)	(6,103)	(1,088)	27,549
Net cash provided by (used in) operating activities	44,200	19,593	12,409	(1,088)	75,114
Net cash (used in) provided by investing activities	(5,039)	(22,077)	(15,077)	1,404	(40,789)
Net cash provided by financing activities	10,660				10,660
Increase (decrease) in cash and cash equivalents	49,821	(2,484)	(2,668)	316	44,985
Cash and cash equivalents, at beginning of period		2,484	36,191	(316)	38,359
Cash and cash equivalents, at end of period	$ 49,821	$	$ 33,523	$	$ 83,344

	Parent Company	Guarantor Subsidiaries	Non-Guarantor Subsidiaries	Consolidating Adjustments	Consolidated Total
For the six months ended June 30, 2004					
Cash flows from operating activities:					
Net income (loss)	$ (19,755)	$ 52,809	$ 26,216	$	$ 59,270
Changes in operating and intercompany assets and liabilities and non-cash items included in net income	(82,613)	43,692	17,415	43,415	21,909

Net cash provided by (used in) operating activities	(102,368)	96,501	43,631	43,415	81,179
Net cash (used in) provided by investing activities	(170,723)	(89,375)	(22,246)	1,268	(281,076)
Net cash provided by (used in) financing activities	252,934	(299)	(10,699)	(48,152)	193,784
(Decrease) increase in cash and cash equivalents	(20,157)	6,827	10,686	(3,469)	(6,113)
Cash and cash equivalents, at beginning of period	20,157	2,646	27,492		50,295
Cash and cash equivalents, at end of period	$	$ 9,473	$ 38,178	$ (3,469)	$ 44,182

Table of Contents

4. Net Income per Share

The following table sets forth the computation of basic and diluted net income per share (shares in thousands):

	Three Months Ended June 30,		Six Months Ended June 30,	
	2003	2004	2003	2004
Numerator:				
Numerator for basic and diluted net income per share net income	$25,813	$29,183	$47,565	$59,270
Denominator:				
Denominator for basic net income per share weighted-average shares	72,806	66,832	72,539	67,871
Effect of dilutive securities:				
Stock options	2,091	2,395	1,983	2,354
Denominator for diluted net income per share adjusted weighted-average shares and assumed conversions	74,897	69,227	74,522	70,225
Net income per share:				
Basic	$ 0.35	$ 0.44	$ 0.66	$ 0.87
Diluted	$ 0.34	$ 0.42	$ 0.64	$ 0.84

5. Stockholders Equity

Stock-based Compensation

We account for stock-based compensation to employees and directors using the intrinsic value method in accordance with the provisions of Accounting Principles Board Opinion No. 25, *Accounting for Stock Issued to Employees,* and related Interpretations. Accordingly, we recognize no compensation expense when we grant fixed options to employees and directors, because the exercise price of the stock options equals or exceeds the market price of the underlying stock on the dates of grant. Option grants to medical directors and non-vested stock grants are expensed over their vesting periods.

The following table presents the pro forma effect on net income and net income per share as if we had applied the fair value based method and recognition provisions of Statement of Financial Accounting Standards No.

Table of Contents

123, *Accounting for Stock-Based Compensation,* (SFAS No. 123) to stock-based compensation to employees and directors:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2003	2004	2003	2004
Net income, as reported	$25,813	$29,183	$47,565	$59,270
Add: stock-based compensation expense, net of related tax effects, included in the determination of net income as reported	283	26	344	57
Less: stock-based compensation expense, net of related tax effects, determined by the fair value-based method	(2,276)	(2,155)	(4,763)	(4,542)
Pro forma net income	$23,820	$27,054	$43,146	$54,785
Net income per share:				
Basic, as reported	$ 0.35	$ 0.44	$ 0.66	$ 0.87
Basic, pro forma	$ 0.33	$ 0.40	$ 0.59	$ 0.81
Diluted, as reported	$ 0.34	$ 0.42	$ 0.64	$ 0.84
Diluted, pro forma	$ 0.32	$ 0.39	$ 0.58	$ 0.78

The effects of applying SFAS No. 123 for providing pro forma disclosures are not likely to be representative of the effects on reported net income for future periods.

Stock Split

On April 27, 2004, we announced a three-for-two stock split in the form of a stock dividend distributed to shareholders of record as of May 7, 2004. On May 24, 2004 we issued one share for every two shares held by shareholders as of the record date. The par value of our common stock remained unchanged at $0.01.

Authorized Shares

On June 9, 2004, our shareholders approved an amendment to the certificate of incorporation increasing the number of authorized shares of common stock from 90,000 to 150,000.

6. Contingencies

On August 30, 2000, 19 patients were hospitalized and one patient died shortly after becoming ill while receiving treatment at one of our dialysis centers in Youngstown, Ohio. One of the 19 hospitalized patients also died some time later. In March 2001, one of the affected patients sued the Company in Mahoning County, Ohio for injuries related to the August 30, 2000 incident. Additional suits were filed. As of June 30, 2004, we had settled all but four of these suits. The suits allege negligence, medical malpractice and product liability. Additional defendants were named in each of the suits. Additional defendants in some of the suits include the water system vendors who installed and maintained the water system in the dialysis center. We have denied the allegations and have filed cross-claims against the water system vendors. We intend to pursue these cross-claims vigorously. Management believes that Renal Care Group s insurance should be adequate to cover these illnesses and does not anticipate a material adverse effect on our consolidated financial position or results of operations.

We are involved in other litigation and regulatory investigations arising in the ordinary course of business. In the opinion of management, after consultation with legal counsel, management believes these matters will be resolved without material adverse effect on Renal Care Group s consolidated financial position or results of operations.

Laws and regulations governing the Medicare and Medicaid programs are complex and subject to interpretation. We believe that we are in compliance with all applicable laws and regulations governing the Medicare and Medicaid programs. We are not aware of any pending or threatened investigations involving allegations of potential noncompliance with applicable laws or regulations. While no regulatory inquiries have been made, compliance with such laws and regulations can be subject to future government review and interpretation, and

non-compliance or alleged non-compliance could result in significant regulatory action including fines, penalties, and exclusion from the Medicare and Medicaid programs.

We generally engage practicing board-certified or board-eligible nephrologists to serve as medical directors for our centers. Medical directors are responsible for the administration and monitoring of patient care policies, including patient education, administration of dialysis treatment, development programs and assessment of all patients in our dialysis centers. We pay medical director fees that are consistent with the fair market value of the required supervisory services. Our medical director agreements typically have a term of seven years with a three-year renewal option.

7. Defined Benefit Plan

Effective January 29, 2003, we implemented a retirement benefit plan for our former Chairman, Chief Executive Officer and President. He died March 20, 2003. The plan provides that we will make 120 monthly payments of $54 each to our former Chairman s beneficiary, beginning in April 2003. As a result, in the first quarter of 2003, we recorded a $5,350 charge included in general and administrative expenses representing the pre-tax net present value of these payments. As of June 30, 2004, we have accrued liabilities totaling $4,792 related to this defined benefit plan.

ITEM 2. MANAGEMENT S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

Results of Operations

Three Months Ended June 30, 2003 Compared to Three Months Ended June 30, 2004

Net Revenue. Net revenue increased from $247.1 million for the three months ended June 30, 2003 to $340.9 million for the three months ended June 30, 2004, an increase of $93.8 million or 38.0%. This increase resulted primarily from a 35.3% increase in the number of treatments performed by Renal Care Group from 809,413 in the 2003 period to 1,095,250 in the 2004 period. This growth in treatments is the result of our acquisition of NNA and other dialysis facilities along with a 3.7% increase in same-market treatments for the 2004 period over the 2003 period. In addition, average net revenue per dialysis treatment increased 2.3% from $304 in 2003 to $311 in 2004. The increase in net revenue per treatment from 2003 is largely due to an increase in the utilization of certain ancillary drugs along with the impact of our annual price increase implemented in the fourth quarter of 2003. This increase was partially offset by lower revenue per treatment realized by the former NNA operations.

As we transition NNA s patients into our laboratory, we expect revenue per treatment to remain steady or improve in the remainder of 2004. Excluding any potential changes in ancillary drug utilization, we expect net revenue to remain between $310 and $315 per treatment for the remainder of 2004.

Patient Care Costs. Patient care costs consist of costs directly related to the care of patients, including direct labor, drugs and other medical supplies, and operational costs of facilities. Patient care costs increased from $160.0 million for the three months ended June 30, 2003 to $229.8 million for the three months ended June 30, 2004, an increase of 43.7%. This increase was due principally to the increase in the number of treatments performed during the period, which resulted in corresponding increases in the use of labor, drugs and supplies. Patient care costs as a percentage of net revenue increased from 64.8% in the 2003 period to 67.4% in the 2004 period. This increase is due to generally higher salary and benefit costs and routine supply costs experienced in the former NNA facilities. Patient care costs per treatment increased 6.1% from $198 in the 2003 period to $210 in the 2004 period. This increase was due to an increase in the utilization of certain ancillary drugs as well as the higher cost structure in the former NNA facilities.

General and Administrative Expenses. General and administrative expenses include corporate office costs and other costs not directly related to the care of patients, including facility administration, accounting, billing and information systems. General and administrative expenses increased from $21.2 million for the three months ended June 30, 2003 to $27.3 million for the three months ended June 30, 2004, an increase of 29.0%. The increase in general and administrative expenses over the second quarter of 2003 is due to increased costs associated with the acquisitions that we closed in the first half of 2004. General and administrative expenses as a percentage of net revenue decreased from 8.6% in 2003 to 8.0% in 2004 as we leveraged our corporate functions over a larger base of revenue as a result of our acquisitions in 2004.

Provision for Doubtful Accounts. We determine the provision for doubtful accounts as a function of payor mix, billing practices and other factors. We reserve for doubtful accounts in the period when we recognize the revenue. Management establishes these reserves based on its estimate of the net collectibility of accounts receivable while considering a variety of factors. These factors include, but are not limited to, analysis of revenues generated from payor sources, subsequent collection testing and regular reviews of detailed accounts receivable agings. We make adjustments to the allowance for doubtful accounts as necessary based on the results of management s ongoing reviews of the net collectibility of accounts receivable. The provision for doubtful accounts increased from $6.5 million for the three months ended June 30, 2003 to $8.0 million for the three months ended June 30, 2004, an increase of $1.6 million, or 24.4%. This increase was principally the result of increases in our net revenue. The provision for

doubtful accounts as a percentage of net revenue decreased from 2.6% in the 2003 period to 2.4% in the 2004 period. The decrease in the provision for doubtful accounts as a percentage of net revenue was due to improvements in the Company s historical collection results.

Depreciation and Amortization. Depreciation and amortization increased from $11.6 million for the three months ended June 30, 2003 to $14.9 million for the three months ended June 30, 2004, an increase of 28.7%. This

increase was due to increases in plant and equipment and separately identifiable intangible assets associated with our recent acquisitions, start-up of dialysis facilities, normal replacement costs of dialysis facilities and equipment, and purchases of information systems. Depreciation and amortization as a percentage of net revenue decreased from 4.7% in 2003 to 4.4% in 2004 principally as a result of NNA s practice of leasing dialysis equipment under operating leases, which resulted in lower depreciation and amortization and higher patient care costs.

Income from Operations. Income from operations increased from $47.8 million for the three months ended June 30, 2003 to $60.7 million for the three months ended June 30, 2004, an increase of 26.9%. Income from operations as a percentage of net revenue decreased from 19.4% in the 2003 period to 17.8% in the 2004 period principally as a result of the acquisition of NNA, which had generally lower margins than the Company as a result of its lower revenue per treatment and higher patient care costs and other factors discussed above.

Interest Expense, Net. Interest expense increased from $165,000 for the three months ended June 30, 2003 to $5.8 million for the three months ended June 30, 2004. This increase was due to higher average borrowings outstanding during the quarter, as a result of additional borrowings associated with the completion of our program to repurchase $250.0 million in common stock between November 2003 and March 2004, our recent acquisitions and the assumption of NNA s $160.0 million 9% senior subordinated notes.

Minority Interest. Minority interest represents the proportionate equity interest of other owners in consolidated entities that we do not wholly own. The financial results of those entities are included in the Company s consolidated results. Minority interest as a percentage of net revenue decreased from 2.4% in the 2003 period to 2.3% in the 2004 period. The decrease in minority interest expense as a percentage of revenue occurred as our recent acquisitions diluted the percentage of our facilities that operate as joint ventures. As of June 30, 2004, we were the majority and controlling owner in 64 joint ventures.

Provision for Income Taxes. Income tax expense increased from $15.8 million for the three months ended June 30, 2003 to $18.1 million for the three months ended June 30, 2004, an increase of $2.3 million or 14.3%. The increase is a result of higher pre-tax earnings described above. Our effective tax rate increased from 38.0% for the 2003 period to 38.3% for the 2004 period. The increase reflects a higher overall effective rate associated with the operations acquired from NNA.

Net Income. Net income increased from $25.8 million for the three months ended June 30, 2003 to $29.2 million for the three months ended June 30, 2004, an increase of $3.4 million or 13.1%. The increase is a result of the items discussed above.

Six Months Ended June 30, 2003 Compared to Six Months Ended June 30, 2004

Net Revenue. Net revenue increased from $489.2 million for the six months ended June 30, 2003 to $618.9 million for the six months ended June 30, 2004, an increase of $129.7 million or 26.5%. This increase resulted primarily from a 22.7% increase in the number of treatments performed by Renal Care Group from 1,593,254 in the 2003 period to 1,955,499 in the 2004 period. This growth in treatments is the result of our acquisition of NNA and other dialysis facilities along with a 3.6% increase in same-market treatments for the 2004 period over the 2003 period. In addition, average net revenue per dialysis treatment increased 3.3% from $306 in 2003 to $316 in 2004. The increase in net revenue per treatment is largely due to an increase in the utilization of certain ancillary drugs, the impact of our annual price increase implemented in the fourth quarter of 2003 and the favorable resolution of several contractual issues with payors during the first quarter 2004. This increase was partially offset by lower revenue per treatment realized by the former NNA operations.

Patient Care Costs. Patient care costs consist of costs directly related to the care of patients, including direct labor, drugs and other medical supplies, and operational costs of facilities. Patient care costs increased from $317.5 million for the six months ended June 30, 2003 to $409.2 million for the six months ended June 30, 2004, an increase of 28.9%. This increase was due principally to the increase in the number of treatments performed during the period, which was reflected in corresponding increases in the use of labor, drugs and supplies. Patient care costs as a percentage of net revenue increased from 64.9% in 2003 to 66.1% in 2004. This increase is due to generally higher salary and benefit costs and routine supply costs experienced in the former NNA facilities. Patient care costs

Table of Contents

per treatment increased 5.0% from $199 in 2003 to $209 in 2004. This increase was due to an increase in the utilization of certain ancillary drugs as well as the higher cost structure in the former NNA facilities.

General and Administrative Expenses. General and administrative expenses include corporate office costs and other costs not directly related to the care of patients, including facility administration, accounting, billing and information systems. General and administrative expenses increased from $47.5 million for the six months ended June 30, 2003 to $50.0 million for the six months ended June 30, 2004, an increase of 5.4%. The increase in general and administrative expenses over the 2003 period is due to costs associated with acquisitions that closed in the first half of 2004. This increase was partially offset by a $5.4 million charge related to a supplemental retirement benefit plan for the Company s former chairman, chief executive and president that we recorded in the first quarter of 2003. General and administrative expenses as a percentage of net revenue decreased from 9.7% in 2003 to 8.1% in 2004. This decrease was the result of leveraging our corporate functions over a larger base of revenue as well as the absence of the retirement charge in the 2004 period.

Provision for Doubtful Accounts. We determine the provision for doubtful accounts as a function of payor mix, billing practices and other factors. We reserve for doubtful accounts in the period in which the revenue is recognized. Management establishes these reserves based on its estimates of the net collectibility of accounts receivable while considering a variety of factors. These factors include, but are not limited to, analysis of revenues generated from payor sources, subsequent collection testing and regular reviews of detailed accounts receivable agings. We make adjustments to the allowance for doubtful accounts as necessary based on the results of management s ongoing reviews of the net collectibility of accounts receivable. The provision for doubtful accounts increased from $12.9 million for the six months ended June 30, 2003 to $15.2 million for the six months ended June 30, 2004, an increase of $2.3 million, or 17.7%. The provision for doubtful accounts as a percentage of net revenue decreased slightly from 2.6% in 2003 to 2.4% in 2004. The decrease in the provision for doubtful accounts as a percentage of net revenue was due to improvements in the Company s historical collection results.

Depreciation and Amortization. Depreciation and amortization increased from $21.9 million for the six months ended June 30, 2003 to $27.1 million for the six months ended June 30, 2004, an increase of $5.2 million, or 23.7%. This net increase was due to increases in plant and equipment and separately identifiable assets associated with our recent acquisitions, start-up of dialysis facilities, normal replacement costs of dialysis facilities and equipment, and purchases of information systems. Depreciation and amortization as a percentage of net revenue decreased from 4.5% in 2003 to 4.4% in 2004.

Income from Operations. Income from operations increased from $89.5 million for the six months ended June 30, 2003 to $117.4 million for the six months ended June 30, 2004, an increase of $27.9 million, or 31.2%. Income from operations as a percentage of net revenue increased from 18.3% in the 2003 period to 19.0% in the 2004 period as a result of the factors discussed above.

Interest Expense, Net. Interest expense increased from $450,000 for the six months ended June 30, 2003 to $6.7 million for the six months ended June 30, 2004. The increase was the result of higher average borrowings in 2004, as a result of additional borrowings associated with the completion of our program to repurchase $250.0 million in common stock between November 2003 and March 2004, our recent acquisitions and the assumption of NNA s $160.0 million 9% senior subordinated notes.

Minority Interest. Minority interest represents the proportionate equity interest of other owners in consolidated entities that we do not wholly own. The financial results of those entities are included in the Company s consolidated results. Minority interest as a percentage of net revenue decreased from 2.5% in the 2003 period to 2.4% in the 2004 period. The decrease in minority interest expense as a percentage of revenue occurred as our recent acquisitions diluted the percentage of our facilities that operate as joint ventures. As of June 30, 2004, we were the majority and

controlling owner in 64 joint ventures.

Provision for Income Taxes. Income tax expense increased from $29.1 million for the six months ended June 30, 2003 to $36.5 million for the six months ended June 30, 2004, an increase of $7.4 million or 25.3%. The increase is a result of higher pre-tax earnings described above. The Company s effective tax rate increased from 38.0% for the 2003 period to 38.1% for the 2004 period. The increase reflects a higher overall effective rate associated with the operations acquired from NNA.

Net Income. Net income increased from $47.6 million for the six months ended June 30, 2003 to $59.3 million for the six months ended June 30, 2004, an increase of $11.7 million or 24.6%. The increase is a result of the items discussed above.

Liquidity and Capital Resources

We require capital primarily to acquire and develop dialysis centers, to purchase property and equipment for existing centers, to repurchase shares of our common stock and to finance working capital needs. At June 30, 2004, our working capital was $138.3 million, cash and cash equivalents were $44.2 million, and our current ratio was approximately 1.6 to 1.0.

Net cash provided by operating activities was $81.2 million for the six months ended June 30, 2004. Cash provided by operating activities consists of net income before depreciation and amortization expense and income applicable to minority interest, adjusted for changes in components of working capital. Net cash used in investing activities was $281.1 million for the six months ended June 30, 2004. Net cash used in investing activities consisted primarily of $230.7 million of cash paid for acquisitions, net of cash acquired, as well as $45.0 million of purchases of property and equipment. Net cash provided by financing activities was $193.8 million for the six months ended June 30, 2004. Net cash provided by financing activities primarily reflects proceeds from the issuance of long-term debt of $325.0 million, net proceeds of $12.8 million from the issuance of common stock, offset by $137.8 million in repurchases of our common stock.

As of December 31, 2003, we had two credit agreements with a group of banks totaling $150.0 million. On February 10, 2004, we entered into a new credit agreement (the 2004 Agreement) with a group of banks totaling up to $700.0 million. The 2004 Agreement replaced both of our prior facilities. The 2004 agreement has a $150.0 million revolving credit facility, a $325.0 million term loan facility and a $225.0 million incremental term loan facility. Borrowings under the incremental term loan facility are subject to obtaining commitments from the banks and finalizing specific terms. The revolving credit facility and the $325.0 million term loan facility have a final maturity of February 10, 2009. Each of our wholly-owned subsidiaries has guaranteed all of our obligations under the 2004 Agreement. Further, our obligations under the 2004 Agreement, and our subsidiaries obligations under their guarantees, are secured by a pledge of the equity interests we hold in each of our subsidiaries. The 2004 Agreement includes financial covenants that are customary based on the amount and duration of the agreement.

Borrowings under the $150.0 million revolving credit facility may be used for acquisitions, repurchases of our stock, capital expenditures, working capital and general corporate purposes. As of June 30, 2004, we can borrow up to $150.0 million under the revolving credit facility but cannot borrow any additional amounts under the $325.0 million term loan facility which was fully funded at closing of the 2004 Agreement. At June 30, 2004, our outstanding indebtedness was $511.5 million, including a remaining balance of $320.9 million under the term loan facility, $184.6 million of senior subordinated notes assumed in the NNA transaction and $5.9 million of other indebtedness, primarily capital leases.

The senior subordinated notes we assumed in the NNA transaction bear interest at the rate of 9% per annum on the face amount that was $160.0 million at the date of acquisition. As of June 30, 2004 these notes have a remaining face value of $159.7 million and are recorded at their fair value of $184.6 million. These notes do not provide for scheduled principal amortization and are scheduled to mature on November 1, 2011. Each of our wholly-owned subsidiaries has guaranteed all of our obligations under these notes. The rights of the noteholders and our obligations under these notes are set forth in an indenture that NNA entered into in October 2003 and we assumed in connection with the NNA acquisition. The indenture includes customary financial covenants.

Borrowings under the 2004 Agreement bear interest at variable rates determined by our leverage ratio. These variable rate debt instruments carry a degree of interest rate risk and we will face higher interest costs on this debt if interest rates rise.

On June 3, 2004, we entered into interest rate swap agreements to hedge the interest rate risk on $150.0 million of our term loan. These interest rate swap agreements became effective on June 30, 2004. Under these

Table of Contents

interest rate swap agreements we will exchange fixed and variable rate interest payments based on a $150.0 million notional principal amount through March 30, 2007. The notional amount of $150.0 million and the interest rate of 3.5% plus an additional spread based on the Company s leverage ratio are fixed in the agreements. The changes in cash flows under these agreements are expected to offset the changes in interest rate payments attributable to fluctuations in LIBOR. The hedge is structured to qualify for the shortcut method; therefore, changes in the fair value of the agreement will be directly recorded in comprehensive income. The interest payments under this agreement are settled on a net basis each calendar quarter.

As a result of our indebtedness, we will incur substantial interest expense in and after 2004. Based on our outstanding indebtedness of $486.5 million, excluding the unamortized fair value premium of $24.9 million on the Notes, the aggregate maturities of our borrowings are as follows: 2004 - $14.0 million; 2005 - $22.3 million; 2006 - $30.5 million; 2007 - $56.9 million; 2008 - $156.4 million; and thereafter - $206.4 million.

A significant component of our growth strategy is the acquisition and development of dialysis facilities. There can be no assurance that we will be able to identify suitable acquisition candidates or to close acquisitions on acceptable terms. Management believes that existing cash and funds from operations, together with funds available under our credit facility, will be sufficient to meet our acquisition, expansion, capital expenditure and working capital needs for the foreseeable future. However, in order to finance certain large strategic acquisition opportunities, we may need to incur additional short and long-term bank indebtedness or to issue equity or debt securities. The availability and terms of any future financing will depend on market and other conditions. There can be no assurance that we will be able to secure additional financing, if required, on acceptable terms.

We plan to make capital expenditures of between $85.0 million and $95.0 million in 2004, primarily for equipment replacement, expansion of existing dialysis facilities and construction of de novo facilities. We expect that these capital expenditures will be funded with cash provided by operating activities and our existing credit facilities. Management believes that capital resources available to us will be sufficient to meet the needs of our business, both on a short- and long-term basis.

Management, from time to time, determines the appropriateness of repurchasing common stock in accordance with a repurchase plan initially authorized by the Board of Directors in October 2000. In 2001, we began repurchasing shares of our common stock by purchasing 150,000 shares of common stock for approximately $3.1 million. In 2002, we repurchased 4.3 million shares of our common stock for approximately $90.9 million. In October 2003, we announced that the Board of Directors had approved an increase in the repurchase plan to allow the purchase of up to a total of $450.0 million in common stock, and we announced that we intended to repurchase $250.0 million in common stock between November 1, 2003 and March 31, 2004. During 2003, we repurchased 5.5 million shares of common stock for $140.5 million. In the first half of 2004, we repurchased 4.6 million shares for $137.8 million. Through June 30, 2004, we had repurchased an aggregate of 14.5 million shares under the plan, for a total of approximately $372.2 million.

Critical Accounting Policies

The Securities and Exchange Commission (SEC) issued a financial reporting release, FR-60, *Cautionary Advice Regarding Disclosure About Critical Accounting Policies*. In accordance with that release, management has identified accounting policies that it considers critical to the business of Renal Care Group. Those policies include net revenue and contractual provisions, provision for doubtful accounts, self-insurance accruals, and impairment of long-lived assets and long-lived assets to be disposed of. These policies were identified as critical based on their importance to the consolidated financial statements as well as on the degrees of subjectivity and complexity involved in these policies. There have been no changes in Renal Care Group s critical accounting policies or in the application of those policies from those described in the annual report on Form 10-K, as filed with the SEC on March 4, 2004 and in the

current report on Form 8-K, as filed with the SEC on April 19, 2004.

Table of Contents

RISK FACTORS

*You should carefully consider the risks described below before investing in Renal Care Group. The risks and uncertainties described below **are not** the only ones facing Renal Care Group. Other risks and uncertainties that we have not predicted or assessed may also adversely affect us.*

If any of the following risks occurs, our earnings, financial condition or business could be materially harmed, and the trading price of our common stock could decline, resulting in the loss of all or part of your investment.

If Congress or CMS changes the Medicare or Medicaid programs for dialysis, then our revenue and earnings could decrease.

If the government changes the Medicare, Medicaid or similar government programs or the rates those programs pay for our services, then our revenue and earnings may decline. We estimate that approximately 50% of our net revenue for 2002, 49% of our net revenue for 2003, and 49% of our net revenue for the six months ended June 30, 2004 consisted of reimbursements from Medicare, including reimbursement for the administration of EPO. We also estimate that approximately 7% of our net revenue for 2002, 6% of our net revenue for 2003 and 4% of our net revenue for the six months ended June 30, 2004 consisted of reimbursements from Medicaid or comparable state programs. Any of the following actions in connection with government programs could cause our revenue and earnings to decline:

- a reduction of the amount paid to us under government programs;
- an increase in the costs associated with performing our services that are subject to inflation, such as labor and supply costs, without a corresponding increase in reimbursement rates;
- the inclusion of some or all ancillary services, for which we are now reimbursed separately, in the flat composite rate for a dialysis treatment; or
- changes in laws, or the interpretations of laws, which could cause us to modify our operations.

Specifically, Congress and CMS have proposed expanding the drugs and services that are included in the flat composite rate. CMS has indicated that it believes such a mechanism would be fairer and easier to administer. In addition, Congress mandated a change in the way we will be paid beginning in 2005 for some of the drugs, including EPO, that we bill for outside of the flat composite rate. This change will result in lower reimbursement for these drugs and a higher composite rate. Congress stated that these changes are not intended to reduce overall reimbursement to dialysis providers. CMS recently issued proposed regulations to implement these changes. These proposed regulations provide that we will be reimbursed for separately billable drugs at a 3% discount from the average sale price and that the composite rate will be increased by 11.3%. These proposed regulations also include a case-mix adjustment and a geographic adjustment to the composite rate as well as a buget-neutrality adjustment. If these regulations become effective as proposed, management believes they will result in a net reduction of $0.03 per share in diluted net income in 2005.

If states lower Medicaid reimbursement, then we would be less profitable.

The Medicaid programs in some of the states in which we operate have formerly reimbursed us, or currently reimburse us, at rates higher than those paid by Medicare. Some of these programs, like Washington s, Wisconsin s, and New Mexico s have approved reductions in reimbursement. Other programs have proposed reductions or have announced that they are considering reductions. In addition, a number of the states where we operate are experiencing budget shortfalls, and some of these states may consider reducing Medicaid reimbursement or changing their

Medicaid programs to cut costs. We are unable to predict whether and, if so, when any reductions in Medicaid reimbursement, other than those already approved, might occur and what their precise effect will be.

If reimbursement for EPO decreases, then we could be less profitable.

If government or private payors decrease reimbursement rates for EPO, for which we are currently reimbursed separately outside of the flat composite rate, then our revenue and earnings will decline. Revenues from the administration of EPO were approximately 23% of our net revenue for 2002, 24% of our net revenue for 2003 and 27% of our net revenue for the six months ended June 30, 2004. Most of our payments for EPO come from government programs. For the six months ended June 30, 2004, Medicare and Medicaid reimbursement represented approximately 53% of the total revenue we derived from EPO. A reduction in the reimbursement rate for EPO or the

Table of Contents

inclusion of EPO in the list of items covered by the flat composite rate could materially and adversely affect our revenue and earnings. As discussed above, Congress has mandated a change in the way we will be reimbursed for EPO, and CMS has proposed regulations to implement the change. This change and others in the proposed regulations could, as discussed above, adversely affect our net income in 2005.

If Amgen raises the price for EPO or if EPO becomes in short supply, then we could be less profitable.

EPO is produced by a single manufacturer, Amgen, Inc., and there are no substitute products currently marketed to dialysis providers in the United States. In April 2002, Amgen announced a 3.9% increase in the price of EPO. This price increase adversely affected our earnings in 2003 and changes in the rebate structure under our current contract with Amgen may adversely affect our earnings in 2004. If Amgen imposes additional EPO price increases or if Amgen or other factors interrupt the supply of EPO, then our revenue and earnings will decline.

If Amgen markets Aranesp® for ESRD patients, then we could be less profitable.

Amgen has developed and obtained FDA approval for a new drug to treat anemia that is marketed as Aranesp® (darbepoetin alfa). Aranesp® is a longer acting form of bio-engineered protein that, like EPO, can be used to treat anemia. EPO is usually administered in conjunction with each dialysis treatment. Aranesp® can remain effective for between two and three weeks. If Amgen markets Aranesp® for the treatment of dialysis patients, then our earnings could be materially and adversely affected by either of the following factors:

- our margins realized from the administration of Aranesp® could be lower than the margins realized on the administration of EPO; or

- physicians could decide to administer Aranesp® in their offices, and we would not recognize revenue or profit from the administration of EPO or Aranesp®.

If payments by private insurers, hospitals or managed care organizations decrease, then our revenue and earnings could decrease.

If private insurers, managed care organizations or hospitals reduce their rates or if we experience a significant shift in our revenue mix toward additional Medicare or Medicaid reimbursement, then our revenue and earnings will decline. We estimate that approximately 43% of our net revenue for 2002, 45% of our net revenue for 2003, and 47% of our net revenue for the six months ended June 30, 2004 was derived from sources other than Medicare and Medicaid. In general, payments we receive from private insurers and hospitals for our services are at rates significantly higher than the Medicare or Medicaid rates. Payments we receive from managed care organizations are also at rates higher than Medicare and Medicaid rates but lower than those paid by private insurers. In addition, we have been able to implement annual price increases for private insurers and managed care organizations that we have not been able to implement for federal programs. Management believes that health insurance pricing is cyclical and that we may be at or near the top of the cycle. As a result, management believes that our ability to maintain or raise rates to private insurers and managed care companies will likely be more limited over the next several years than it has been in the recent past. We have recently experienced reductions in reimbursement from two commercial insurers, and management believes that the reductions in reimbursement by these two commercial insurers along with pricing pressure from other commercial insurers and managed care organizations will likely adversely impact our revenue per treatment and earnings per share in 2004. Any of the following events could have a material adverse effect on our revenue and earnings:

- any number of economic or demographic factors could cause private insurers, hospitals or managed care companies to reduce the rates they pay us or to refuse to pay price increases or work to reduce the rate of our price increases;

a portion of our business that is currently reimbursed by private insurers or hospitals may become reimbursed by managed care organizations, which generally have lower rates for our services;

a portion of our business that is currently reimbursed by private insurers at rates based on our billed charges may become reimbursed under a contract at lower rates; or

the scope of coverage by Medicare or Medicaid under the flat composite rate could expand and, as a result, reduce the extent of our services being reimbursed at the higher private-insurance rates.

Table of Contents

If local physicians stop sending patients to our centers or were prohibited from doing so for regulatory reasons, then our revenue and earnings would decline.

Our dialysis centers depend on local nephrologists sending patients to the centers. Typically, one or a few physicians patients make up all or a significant portion of the patient base at each of our dialysis centers, and the loss of the patient base of one or more of these physicians could have a material adverse effect on the operations of that center. The loss of the patient base of a significant number of local physicians could cause our revenue and earnings to decline. In many instances, the primary referral sources for our centers are physicians who also serve as medical directors of our centers and may be shareholders. If the medical director relationship or stock ownership were found to violate applicable federal or state law, including fraud and abuse laws and laws prohibiting self-referrals, then the physicians acting as medical directors or owning our stock could be forced to stop referring patients to our centers.

A number of our medical director agreements will expire over the next three years, unless they are renewed or renegotiated. We did not renew or renegotiate a small number of our medical director agreements that expired in 2003, and we may not be able to renew or renegotiate expiring medical director agreements successfully, or we may not be able to enforce the non-competition provisions of some of our medical director or other agreements. Any of these factors could result in a loss of patients, since dialysis patients are typically treated at a center where their physician or a member of his or her practice group serves as medical director. We believe that our future success will depend in part on our ability to attract and retain qualified physicians to serve as medical directors of our dialysis centers.

If our business is alleged or found to violate heath care or other applicable laws, our revenue and earnings could decrease.

We are subject to extensive federal, state and local regulation. The laws that apply to our operations include, but are not limited to, the following:

- fraud and abuse prohibitions under state and federal health care laws;
- prohibitions and limitations on patient referrals;
- billing and reimbursement rules, including false claims prohibitions under health care reimbursement laws;
- rules regarding the collection, use, storage and disclosure of patient health information, including the federal Health Insurance Portability and Accountability Act of 1996, which we refer to as HIPAA, and state law equivalents of HIPAA;
- facility licensure;
- health and safety requirements;
- environmental compliance; and
- medical and toxic waste disposal.

Much of the regulation of our business, particularly in the areas of fraud and abuse and patient referral, is complex and open to differing interpretations. Due to the broad application of the statutory provisions and the absence in many instances of regulations or court decisions addressing the specific arrangements by which we conduct our business, including our arrangements with medical directors, physician stockholders and physician joint venture partners, governmental agencies could challenge some of our practices under these laws.

New regulations governing electronic transactions and the collection, use, storage, and disclosure of health information impose significant administrative and financial obligations on our business. If, after the required compliance date, we are found to have violated these regulations, we could be subject to:

criminal or civil penalties, including significant fines;

claims by people who believe their health information has been improperly used or disclosed; and

administrative penalties by payors.

Government investigations of health care providers, including dialysis providers, have continued to increase. We have been the subject of investigations in the past, and the government may investigate our business in the future. One of our competitors, DaVita, Inc., has announced that it is the subject of an investigation by the U.S. Attorney for the Eastern District of Pennsylvania. Another competitor, Gambro Healthcare, Inc., has announced that it is the subject of an investigation by the U.S. Attorney s Office in St. Louis, Missouri, and Gambro recently announced that it had reached an agreement in principle to settle matters related to that investigation and to pay approximately $355.0 million in connection with the settlement. If any of our operations are found to violate applicable laws, then we may be subject to severe sanctions, or we could be required to alter or discontinue the challenged conduct or both. If we are required to alter our practices, we may not be able to do so successfully. If any of these events occurs, our revenue and earnings could decline.

If our joint ventures are found to violate the law, our business could be damaged.

A number of the dialysis centers we operate are owned by joint ventures in which we own a controlling interest and one or more physicians or physician practice groups maintain a minority interest. The physician owners may also provide medical director services to those centers or other centers we own and operate. Because our relationships with physicians are governed by the Anti-Kickback Statute, we have sought to satisfy as many safe harbor requirements as possible in structuring these joint venture arrangements. However, our joint venture arrangements do not satisfy all elements of a safe harbor. Also, we believe we have structured the physician relationships in these joint ventures in a way that meets applicable exceptions under the Stark Law or that otherwise complies with the Stark Law. If the joint ventures were found to be in violation of the Anti-Kickback Statute or the Stark Law, we could be required to restructure them or refuse to accept referrals for designated health services from the physicians with whom the joint venture centers have a relationship. We also could be required to repay to Medicare amounts received by the joint ventures pursuant to prohibited referrals, and we could be subject to monetary penalties. If the joint venture centers are subject to any of these penalties, our business could be damaged.

Changes in the health care delivery, financing or reimbursement systems could adversely affect our business.

The health care industry in the United States may be entering a period of change and uncertainty. Health care organizations, public or private, may dramatically change the way they operate and pay for services. Our business is designed to function within the current health care financing and reimbursement system. During the past several years, the health care industry has been subject to increasing levels of government regulation of, among other things, reimbursement rates and relationships with referring physicians. In addition, proposals to reform the health care system have been considered by Congress. In light of the continued increases in the cost of health care and the current economic weakness, there may be new proposals to change the health care system and control costs. These proposals, if enacted, could further increase the government s oversight role and involvement in health care, lower reimbursement rates and otherwise change the operating environment for health care companies. We cannot predict the likelihood of those events or what impact they may have on our business.

The dialysis business is highly competitive. If we do not compete effectively in our markets, then we could lose market share and our rate of growth could slow.

The dialysis industry is largely consolidated, and the consolidation trend continues as large providers acquire smaller providers. There is a small number of large dialysis companies that compete for the acquisition of outpatient dialysis centers and the development of relationships with referring physicians. Two of our major competitors are part of larger companies that also manufacture dialysis equipment, which allows them to benefit from lower equipment

costs. Several of our competitors, including these equipment manufacturers, are larger than we are and have greater financial resources and more established operations. We may also face competition from new entrants into the market, including centers established by former medical directors or other referring physicians. We cannot assure you that we will be able to compete effectively with any of our competitors.

Table of Contents

If we are unable to make acquisitions in the future, then our rate of growth will slow.

Much of our historical growth has come from acquisitions. Although we intend to continue to pursue growth through the acquisition of dialysis centers, we may be unable to identify and complete suitable acquisitions at prices we are willing to pay, or we may be unable to obtain the necessary financing. Further, due to the increased size of our business, the amount that acquired businesses contribute to our revenue and profits will continue to be smaller on a percentage basis. Also, as a result of consolidation in the dialysis industry, we believe the four largest providers of outpatient dialysis services now own approximately 66% of the outpatient dialysis facilities in the United States. We compete with these other companies to identify and complete suitable acquisitions. We believe this competition has intensified in light of the smaller pool of available acquisition candidates and other market forces. As a result, we believe it will be more difficult for us to acquire suitable companies on favorable terms. Further, the businesses we acquire may not perform well enough to justify our investment. If we are unable to make additional acquisitions on suitable terms, then we may not meet our growth expectations.

If we complete future acquisitions, we may dilute existing stockholders by issuing more of our common stock or we may incur expenses related to debt and goodwill, which could reduce our earnings.

We may issue equity securities in future acquisitions that could be dilutive to our shareholders. We also may incur additional debt in future acquisitions. Interest expense on debt incurred to fund our acquisitions may significantly reduce our profitability. While goodwill and other intangible assets with indefinite lives are not amortized to expense under generally accepted accounting principles, we are required to review all of these assets at regular intervals for impairment and to charge an appropriate amount to expense when we identify impairment. If we identify impairment and are required to write off a significant portion of our intangible assets at one time, then there could be a material adverse impact on our stock price.

We may not have sufficient cash flow from our business to pay our substantial debt.

As of June 30, 2004, we had total consolidated debt of approximately $511.5 million, including a $24.9 million fair value premium on the 9% senior subordinated notes, and cash of approximately $44.2 million. Also, subject to limitations, including those included in our credit facility and those contained included in the indenture for the 9% senior subordinated notes we assumed in the NNA acquisition, we are not and will not be prohibited from incurring additional debt.

Due to the large amount of our consolidated debt, we may not generate enough cash from our operations to meet these obligations or to fund other liquidity needs. Our ability to generate cash in the future is, to some extent, subject to risks and uncertainties that are beyond our control. If we are unable to meet our debt obligations, we may need to refinance all or a portion of our indebtedness, sell assets or raise funds in the capital markets. However, we can not assure you that, if we are unable to pay our debt, we will be able to refinance it, obtain additional equity capital or sell assets, in each case on commercially reasonable terms, or at all, or otherwise to fund our liquidity needs.

If for any reason we are unable to meet our debt obligations, we would be in default under the terms of the agreements governing our outstanding debt. If such a default were to occur, the lenders under our credit facility could elect to declare all amounts outstanding under the credit facility immediately due and payable, and the lenders would not be obligated to continue to advance funds under our credit facility. In addition, if such a default were to occur, the 9% senior subordinated notes would become immediately due and payable. If the amounts outstanding under these debt agreements are accelerated, we cannot assure you that our assets will be sufficient to repay the money we owe to banks and other debt holders.

If a change of control occurs, we may have to spend a substantial amount of cash or incur additional indebtedness to satisfy our obligation to repurchase the notes we assumed in the NNA acquisition from holders who choose to tender their notes pursuant to certain procedures in the indenture.

Upon specified change of control events the holders of the 9% senior subordinated notes we assumed in the NNA acquisition have the right to require us to repurchase all or any part (equal to $1,000 or an integral multiple thereof) of the notes they hold at an offer price in cash equal to 101% of the aggregate principal amount of the notes plus accrued and unpaid interest thereon, if any, to the date of purchase. When a change of control occurs, we may

not be able to pay the purchase price for all of the notes tendered for repurchase. Our failure to purchase tendered notes would constitute an event of default under the indenture governing the 9% senior subordinated notes, which in turn would constitute a default under our credit facility. In addition, the terms of our credit facility restrict our ability to purchase the 9% senior subordinated notes. Future credit agreements or other agreements relating to debt may contain similar or more restrictive provisions. We may not be able to secure the consent of our lenders to repurchase the 9% senior subordinated notes or refinance the borrowings that prohibit us from repurchasing the notes. If we do not obtain a consent or repay the borrowings, we could not repurchase the notes.

Alternatively, even if we are able to pay the purchase price for the notes tendered for repurchase, we may have to use a substantial amount of cash to do so, which will deplete our funds to meet our other cash obligations or cause us to incur additional indebtedness to repurchase the notes.

These repurchase requirements may also delay or make it harder for others to obtain control of Renal Care Group.

The large amount and terms of our outstanding debt may prevent us from taking actions we would otherwise consider in our best interest.

The indenture governing our 9% senior subordinated notes and our credit facility contain numerous financial and operating covenants that limit our ability to engage in activities such as:

- incurring additional debt;
- acquiring and developing new dialysis centers;
- making investments;
- creating liens;
- creating restrictions on the ability of our subsidiaries to pay dividends or other amounts to us;
- disposing of assets;
- paying dividends on our capital stock;
- repurchasing our capital stock;
- engaging in transactions with our affiliates; or
- consolidating, merging or selling all or substantially all of our assets.

Our credit facility also requires us to comply with financial covenants including a net worth test, a leverage ratio test and a fixed charge coverage ratio test. Our ability to comply with these covenants may be affected by events beyond our control, including those described in this Risk Factors section. A breach of any of the covenants contained in our credit facility or our inability to comply with the required financial covenants could result in an event of default, which would allow the lenders under our credit facility to declare all borrowings outstanding to be due and payable, which would, in turn, trigger an event of default under the indenture governing our 9% senior subordinated notes. In addition, our lenders could require us to apply all of our available cash to repay our borrowings or they could prevent us from making debt service payments on our 9% senior subordinated notes. If the amounts outstanding under our credit facility or these notes are accelerated, we cannot assure you that our assets would be sufficient to repay in full the money we owe the banks and our other debt holders.

The large amount of our outstanding debt and the limitations our credit facility impose on us could have adverse consequences, including:

- we will have to use much of our cash flow for scheduled debt service rather than for operations, future business opportunities or other purposes, such as funding working capital and capital expenditures;

- we may not be able to increase our borrowings under our credit facility or obtain other debt financing

for future working capital, capital expenditures, acquisitions or other corporate purposes;

we could be less able to take advantage of significant business opportunities, including acquisitions or divestitures;

it may be difficult for us to satisfy our obligations under our 9% senior subordinated notes;

our vulnerability to general adverse economic and industry conditions could be increased; and

we could be at a competitive disadvantage to competitors with less debt.

If we fail to integrate acquired companies, then we will be less profitable.

We have grown significantly by acquisitions of other dialysis providers since our formation. We recently acquired NNA, Midwest Kidney Centers, and a dialysis program in Des Moines, Iowa, and we intend to pursue acquisitions of more dialysis businesses in the future. We are unable to predict the number and size of any future acquisitions. We face significant challenges in integrating an acquired company s management and other personnel, clinical operations, and financial and operating systems with ours, often without the benefit of continued services from key personnel of the acquired company. We face these challenges particularly in larger acquisitions like the acquisition of NNA. We may be unable to integrate the businesses we acquire successfully or to achieve anticipated benefits from an acquisition in a timely manner, which could lead to substantial costs and delays or other operational, technical or financial problems, including diverting management s attention from our existing business. Any of these results could damage our profitability and our prospects for future growth.

If acquired businesses have unknown liabilities, then we could be exposed to liabilities that could harm our business and profitability.

Businesses we acquire may have unknown or contingent liabilities, including liabilities for failure to comply with health care laws. Although we generally attempt to identify practices that may give rise to unknown or contingent liabilities and conform them to our standards after the acquisition, private plaintiffs or governmental agencies may still assert claims. Even though we generally seek to obtain indemnification from the sellers of businesses we buy, unknown and contingent liabilities may not be covered by indemnification or may exceed contractual limits or the financial capacity of the indemnifying party.

If our costs of insurance and claims increase, then our earnings could decrease.

We currently maintain programs of general and professional liability insurance and directors and officers insurance with significant deductible or self-insured retention amounts on each claim. In addition, we generally self-insure our employee health plan and workers compensation program, while maintaining excess insurance for some very large claims. We have accepted higher deductibles and self-insurance exposure in each of the last several years to offset part of the increases in premiums for the programs. These deductibles and premiums increased substantially in 2002 and 2003. The rate of increase in deductibles and premiums has moderated somewhat in 2004, but there have been increases, and there may be larger increases in the future. Our earnings could be materially and adversely affected by any of the following:

further increases in premiums, deductibles and self-insurance retentions;

increases in the number of liability claims against us or the cost of settling or trying cases related to those claims; and

an inability to obtain one or more types of insurance on acceptable terms.

If our board of directors does not approve an acquisition or change in control, then our shareholders may not realize the full value of their stock.

Our certificate of incorporation and bylaws contain a number of provisions that may delay, deter or inhibit a future acquisition or change in control that is not first approved by our board of directors. This could occur even if our shareholders receive an attractive offer for their shares or if a substantial number or even a majority of our shareholders believe the takeover is in their best interest. These provisions are intended to encourage any person

interested in acquiring us to negotiate with and obtain approval from our board of directors before pursuing a transaction. Provisions that could delay, deter or inhibit a future acquisition or change in control include the following:

- a staggered board of directors that would require two annual meetings to replace a majority of the board of directors;
- restrictions on calling special meetings at which an acquisition or change in control might be brought to a vote of the shareholders;
- blank check preferred stock that may be issued by our board of directors without shareholder approval and that may be substantially dilutive or contain preferences or rights objectionable to an acquiror; and
- a poison pill that would substantially dilute the interest sought by an acquiror.

These provisions could also discourage bids for our common stock at a premium and cause the market price of our common stock to decline.

Our stock price is volatile and as a result, the value of your investment may go down for reasons unrelated to the performance of our business.

Our common stock is traded on the New York Stock Exchange. The market price of our common stock has been volatile, ranging from a low closing price of $27.55 per share to a high closing price of $34.29 per share during the six months ended June 30, 2004. The market price for our common stock could fluctuate substantially based on a variety of factors, including the following:

- future announcements concerning us, our competitors or the health care market;
- the threat of litigation or government investigation;
- changes in government regulations; and
- changes in earnings estimates by analysts.

Furthermore, stock prices for many companies fluctuate widely for reasons that may be unrelated to their operating results. These fluctuations, coupled with changes in demand or reimbursement levels for our services and general economic, political and market conditions, could cause the market price of our common stock to decline.

Forward-Looking Statements

Some of the information in this quarterly report on Form 10-Q represents forward-looking statements that involve substantial risks and uncertainties. You can identify these statements by forward-looking words such as may, will, expect, anticipate, believe, intend, estimate and continue or similar words. You should read statements that co these words carefully for the following reasons:

- the statements discuss our future expectations;
- the statements contain projections of our future earnings or of our financial condition; and
- the statements state other forward-looking information.

We believe it is important to communicate our expectations to our investors. There may, however, be events in the future that we are not able to predict accurately or over which we have no control. The risk factors listed above, as

well as any cautionary language in or incorporated by reference into this quarterly report on Form 10-Q, provide examples of risks, uncertainties and events that may cause our actual results to differ materially from the expectations we describe in our forward-looking statements. The SEC allows us to incorporate by reference the information we file with them, which means we can disclose important information to you by referring you to those documents. Before

Table of Contents

you invest in our common stock, you should be aware that the occurrence of any of the events described in the above risk factors, elsewhere in or incorporated by reference into this quarterly report on Form 10-Q and other events that we have not predicted or assessed could have a material adverse effect on our earnings, financial condition and business. If the events described above or other unpredicted events occur, then the trading price of our common stock could decline and you may lose all or part of your investment.

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

The following discusses our exposure to market risk related to changes in interest rates.

Cash balances

We maintain all cash in United States dollars in highly liquid, interest-bearing, investment grade instruments with maturities of less than three months, which we consider cash equivalents; therefore, the Company has no market risk sensitive instruments.

Outstanding debt

As of June 30, 2004, we had outstanding debt of $511.5 million, including a $24.9 million fair value premium on the 9% senior subordinated notes. This debt consisted of $320.9 million outstanding under the term facility in our 2004 credit agreement, $184.6 million of indebtedness relating to the 9% senior subordinated notes due 2011 and approximately $5.9 million outstanding under various capital leases and notes payable. Borrowings of $170.9 million under the term loan bear interest at variable rates based on LIBOR rates or the prime rate that are determined by our leverage ratio. The remaining $150.0 million under the term loan are fixed at a rate of 3.5% plus an additional spread based on the Company s leverage ratio under interest rate swap agreements that became effective on June 30, 2004. Our weighted average borrowing rate under the term loan as of June 30, 2004, was 2.7%. We expect this rate to rise in the future as the swap agreements take effect in the third quarter of 2004 and if interest rates rise on the portion that bears interest at floating rates. Outstanding senior subordinated notes bear nominal interest at 9% on the outstanding $159.7 million face amount of the notes. The unamortized $24.9 million fair value premium is being recognized over the life of the notes using the effective interest method and is recorded as a reduction to interest expense. Accordingly, the effective interest rate on the notes as of June 30, 2004 was 6.4%. At June 30, 2004, the fair value of our indebtedness under the credit facility and senior subordinated notes approximated carrying value. At the June 30, 2004 borrowing levels and excluding the impact of our interest rate swap agreements, if there had been a 1% increase in the variable interest rates, then our pre-tax income would have decreased by approximately $787,000 for the three months ended June 30, 2004.

ITEM 4. CONTROLS AND PROCEDURES

Evaluation of Disclosure Controls and Procedures

(a) Our chief executive officer and chief financial officer evaluated our disclosure controls and procedures as of the end of the period covered by this report. Based on that evaluation, the chief executive officer and chief financial officer have concluded that as of the end of the period covered by this report Renal Care Group maintains disclosure controls and procedures that provide reasonable assurance that information required to be disclosed in our reports under the Exchange Act is recorded, processed, summarized and reported within the periods specified in the SEC s rules and forms.

(b) There have been no changes in our internal control over financial reporting during the period covered by this report that have materially affected, or are reasonably likely materially to affect, our internal control over financial reporting.

Table of Contents

PART II OTHER INFORMATION

ITEM 2. CHANGES IN SECURITIES, USE OF PROCEEDS AND ISSUER PURCHASES OF EQUITY SECURITIES

During the quarter ended June 30, 2004, we purchased shares of our common stock as part of a publicly announced program as follows:

Period	Total Number of Shares Purchased	Average Price Paid per Share	Number of Shares Purchased as Part of Publicly Announced Plans or Programs	Approximate Dollar Value of Shares that May Yet Be Purchased Under the Plans or Programs
April 1, 2004 to April 30, 2004	72,000	$30.65	72,000	$77,750,722
May 1, 2004 to May 31, 2004				$77,750,722
June 1, 2004 to June 30, 2004				$77,750,722
Total	72,000	$30.65	72,000	

The Registrant s share repurchase program was originally announced on October 2, 2000, and was amended by announcements on July 9, 2002, November 18, 2002, August 12, 2003 and October 28, 2003. The program permits repurchases of up to $450.0 million of common stock. The program expires December 31, 2004. No share repurchase plan or program expired during the period covered by this quarterly report.

The Company s certificate of incorporation was amended to increase the number of authorized shares of common stock from 90,000,000 to 150,000,000.

ITEM 4. SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS

On June 9, 2004, the Company held its annual meeting of shareholders in Nashville, Tennessee for the following purposes and with the following results:

1. To elect Joseph C. Hutts, Harry R. Jacobson, M.D. and Thomas A. Lowery, M.D. as Class II Directors, each to serve for a term of three years and until his successor is elected:

	FOR	ABSTAIN

Election of Joseph C. Hutts	30,920,029	2,007,007
Election of Harry R. Jacobson, M.D	30,660,310	2,266,726
Election of Thomas A. Lowery, M.D.	31,831,868	1,095,168

Directors whose terms continued following the meeting but who were not subject to election at the meeting are: Gary A. Brukardt, Peter J. Grua, William P. Johnston, William V. Lapham, Stephen D. McMurray, M.D. and C. Thomas Smith.

Table of Contents

2. To approve the Renal Care Group, Inc. 2004 Stock and Incentive Compensation Plan (the 2004 Incentive Plan):

FOR	AGAINST	ABSTAIN
16,805,820	12,183,672	63,391

3. To approve an amendment to the Renal Care Group, Inc. 1996 Stock Option Plan for Outside Directors (the Directors Plan) to allow the grant of options to directors who are medical directors and the Chairman or Vice Chairman of the board of directors, if such director is not also an employee of the company:

FOR	AGAINST	ABSTAIN
24,277,424	4,710,600	64,859

4. To approve an amendment to our Certificate of Incorporation to increase the number of authorized shares of $0.01 par value common stock from 90,000,000 shares to 150,000,000 shares:

FOR	AGAINST	ABSTAIN
29,601,143	3,273,371	52,522

ITEM 6. EXHIBITS AND REPORTS ON FORM 8-K

(a) Exhibits:

31.1 Certification pursuant to Rule 13a-14(a)/15d-14(a), as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002

31.2 Certification pursuant to Rule 13a-14(a)/15d-14(a), as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002

32.1* Certification pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002

32.2* Certification pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002

* In accordance with Release No. 34-47551, this exhibit is furnished to the SEC as an accompanying document. It is not deemed to be filed for purposes of Section 18 of the Securities Exchange Act of 1934 or otherwise subject to the liabilities of that Section, and it shall not be deemed incorporated by reference into any filing under the Securities Act of 1933.

(b) Reports on Form 8-K

Form 8-K filed April 16, 2004
Form 8-K filed April 19, 2004
Form 8-K/A filed April 19, 2004
Form 8-K filed April 28, 2004
Form 8-K filed April 30, 2004
Form 8-K/A filed May 7, 2004

Form 8-K filed June 9, 2004
Form 8-K/A filed June 9, 2004

Table of Contents

SIGNATURE

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.

	RENAL CARE GROUP, INC. (Registrant)
August 9, 2004	BY: /s/ David M. Dill David M. Dill Executive Vice President, Chief Financial Officer (Principal Financial Officer and Principal Accounting Officer)

31

Table of Contents

RENAL CARE GROUP, INC.

EXHIBIT INDEX

Number and Description of Exhibit	
31.1	Certification pursuant to Rule 13a-14(a)/15d-14(a), as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
31.2	Certification pursuant to Rule 13a-14(a)/15d-14(a), as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
32.1*	Certification pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002
32.2*	Certification pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002

* In accordance with Release No. 34-47551, this exhibit is furnished to the SEC as an accompanying document. It is not deemed to be filed for purposes of Section 18 of the Securities Exchange Act of 1934 or otherwise subject to the liabilities of that Section, and it shall not be deemed incorporated by reference into any filing under the Securities Act of 1933.