PARTICIPANTS

Corporate Participants

Mary Ann Arico – Chief Investor Relations Officer, HealthSouth Corp.
Jay Grinney – President, Chief Executive Officer & Director, HealthSouth Corp.
Douglas E. Coltharp – Chief Financial Officer & Executive Vice President, HealthSouth Corp.
Mark J. Tarr – Chief Operating Officer & Executive Vice President, HealthSouth Corp.

Other Participants

Frank G. Morgan – Analyst, RBC Capital Markets LLC
Whit Mayo – Analyst, Robert W. Baird & Co. Equity Capital Markets
Sheryl R. Skolnick – Analyst, CRT Capital Group LLC
Rob M. Mains – Analyst, Stifel, Nicolaus & Co., Inc.
Gary Lieberman – Analyst, Wells Fargo Securities LLC
Darren Lehrich – Analyst, Deutsche Bank Securities, Inc.
A.J. Rice – Analyst, UBS Securities LLC
Miles L. Highsmith – Analyst, RBC Capital Markets LLC
Joanna S. Gajuk – Analyst, Merrill Lynch, Pierce, Fenner & Smith, Inc.

MANAGEMENT DISCUSSION SECTION

Operator: Good morning, everyone, and welcome to HealthSouth's Third Quarter 2013 Earnings Conference Call. At this time, I would like to inform all participants that their lines will be in a listen-only mode. After the speakers' remarks, there will be a question-and-answer period. [Operator Instructions] You will be limited to one question and one follow-up. Today's conference call is being recorded. If you have any objections, you may disconnect at this time.

I will now turn the call over to Mary Ann Arico, Chief Investor Relations Officer. Please go ahead.

Mary Ann Arico, Chief Investor Relations Officer

Thank you operator and Good morning everyone. Thank you for joining us today for the HealthSouth Third Quarter 2013 Earnings Call. With me on the call in Birmingham today are Jay Grinney, President and Chief Executive Officer, Doug Coltharp, Executive Vice President and Chief Financial Officer Mark Tarr, Executive Vice President and Chief Operating Officer John Whittington, Executive Vice President, General Counsel and Corporate Secretary Andy Price, Chief Accounting Officer; Ed Fay, Treasurer, and Julie Duck, Senior Vice President Financial Operations Before we begin, if you do not already have a copy, the press release, financial statements, the related 8K filing with the SEC and the supplemental slides are available on our website, at www.healthsouth.com.

Moving to slide 2, the Safe Harbor, which is also set forth in greater detail on the last page of the Earnings Release. During the call, we will make forward-looking statements which are subject to risks and uncertainties, many of which are beyond our control. Certain risks, uncertainties and other factors that could cause actual results to differ materially from management's projections, forecasts, estimates, and expectations are discussed in the Company's SEC filings including the Form 10-K for 2012, the Form 10-Q for the quarter ending March 31, 2013, June 30, 2013 and the Form 10-Q for third quarter 2013 which we expect to file this week. We encourage you to read them.

You are cautioned not to place undue reliance on the estimates, projections, guidance and other forward-looking information presented. Statements made throughout this presentation are based on current estimates of future events and speak only as of today. The company does not undertake a duty to update or correct these forward-looking statements.

Our slide presentation and discussion on this call will include certain non-GAAP financial measures. For such measures, reconciliation to the most directly comparable GAAP measure is available at the end of the slide presentation or at the end of the related press release, both of which are available on our website and as part of the Form 8-K filed last night with the SEC.

Before I turn it over to Jay, I would like to remind you that we will adhere to the one question and one follow-up question rule to allow everyone to submit a question. If you have additional questions, please feel free to put yourself back in the queue. And with that, I will turn the call over to Jay.

Jay Grinney, President, Chief Executive Officer & Director

Great, thank you, Mary Ann, and good morning, everyone. Before we begin, I want to apologize. It's my understanding that there may be some technical difficulties. I hope you have been able to listen in on the early part of the call. No offense to Mary Ann, you haven't missed much, so we'll begin the call now. But it's my understanding we have had some technical difficulties.

So, with that, we'll begin, and as we have reported in the past, we are pleased again to report the results of another solid quarter for HealthSouth. Top line growth of 5% was driven by strong discharge growth of 5.7%, with 3.2% of this growth coming from same-store hospitals and 2.5% coming from our four new hospitals in Augusta, Georgia; Ocala, Florida; Littleton, Colorado; and Stuart, Florida. Continued disciplined expense management and favorable adjustments to our self-insurance reserve allowed us to generate $135.5 million of adjusted EBITDA, an increase of 8.2% quarter-over-quarter. Most importantly, our adjusted free cash flow for the quarter was $106.4 million, which brings our year-to-date adjusted free cash flow to $264.6 million, an increase of $77.8 million or 41.6% compared to the first nine months of 2012.

In addition to having a solid quarter operationally, we also were able to continue our investment in future growth. During the third quarter, we entered into the final stages of the construction on our 53-bed replacement hospital in Ludlow, Massachusetts, and expect to transfer patients to this new facility by mid to late December. We also completed the design work on two new 50-bed hospitals, one in Altamonte Springs, Florida, and the other in Newnan, Georgia, both of which are expected to be operational in the fourth quarter of next year. Finally, we have successfully resolved the contested CON [Certificate of Need] for our new 34-bed hospital in Middletown, Delaware, and also expect this hospital will open in Q4 of next year. Overall, our development pipeline remains strong, and we remain optimistic about our ability to continue to add to our portfolio by expanding into new markets and enhancing our position in existing markets.

Based on the company's strong year-to-date performance, we are raising our full-year guidance as follows: Full-year adjusted EBITDA is now expected to be between $533 million and $538 million, while full-year EPS is now expected to be between $3.06 and $3.09 per diluted share.

This updated guidance incorporates the following key assumptions, which, along with other guidance considerations, can be found on pages 17 and 18 of the supplemental slides that were issued with our press release. We're assuming Q4 discharge growth will be between 3% and 4%. As a reminder, discharges grew 5.4% in the fourth quarter of 2012, so we're projecting solid growth despite a tough comp. We expect inpatient pricing before sequestration to be between 2.3% and 2.6%, which reflects the IRF-PPS final rule increase that went into effect October 1 and also reflects price increases in our managed care book of business and the expectation that we will

continue to treat higher acuity patients. Sequestration will continue to be a headwind in the fourth quarter. We expect net operating revenues will be reduced by approximately $9 million, and adjusted EBITDA will be reduced by approximately $8 million in the quarter. And finally, our Q4 SW&B expense will reflect the October 1 resumption of our merit program for all non-management personnel and the average increase for this program was approximately 2.2%.

Before Doug reviews the quarter in greater detail, I want to comment on the progress we have made with the shareholder distribution element of our business model. As you recall, in January we announced we would be looking for ways to return capital to our shareholders, because we had successfully deleveraged the company and were generating free cash flow in excess of what was required to fund our organic growth.

In the first quarter, we launched and completed a tender offer for our common shares, resulting in the repurchase of approximately 9.5% of our then-outstanding shares at a price of $25.50. In the second quarter, we announced the initiation of a quarterly cash dividend of $0.18 per share, which we paid on October 15. And yesterday, we announced a share repurchase authorization for up to $200 million of our common stock. We believe these actions clearly demonstrate we are proactively executing this new element of our business plan and remain committed to returning excess free cash flow to our shareholders.

With that, I'll now turn the agenda over to Doug. Following Doug's comments, we'll open the lines for questions.

Douglas E. Coltharp, Chief Financial Officer & Executive Vice President

Thank you, Jay, and good morning, everyone. As Jay highlighted, Q3 represented another very solid quarter for HealthSouth. In spite of sequestration, revenue increased by 5% over Q3 2012, driven by inpatient revenue growth of 6%, offset by a $2.9 million decline in outpatient and other revenue.

Inpatient revenue was comprised of a 5.7% increase in discharges and a 0.3% increase in revenue per discharge. Discharge growth for the quarter included same-store growth of 3.2% and new store growth of 2.5%. The 30 basis point increase in revenue per discharge was attributable to pricing adjustments, higher patient acuity and a higher percentage of Medicare patients, offset by sequestration and a modest decline in our average length of stay, attributable to the timing of patient discharges around third quarter end. The $2.9 million decline in outpatient and other revenue was primarily attributable to a decline in visits. At the end of Q3 2013, we operated 21 outpatient satellite clinics as compared to 26 at the end of Q3 2012.

Bad debt expense for Q3 increased by 10 basis points to 1.4% of revenue as a result of an increase in the number of medical necessity claims denials and continued administrative delays in the adjudication of previously denied claims. The claims denials continue to originate primarily from one fiscal intermediary. The delays in the adjudication process appear to be driven from a shortage in administrative law judges.

SWB as a percent of revenue for Q3 decreased by 100 basis points to 47.8%, as compared to 48.8% in Q3 2012. SWB this year was favorably impacted by a $6.3 million reduction in group medical and workers' compensation reserves due to favorable trends in claims, offset by the impact of sequestration and the ramp-up of our new hospitals. Labor productivity, as measured by employees per occupied bed, or EPOB, exclusive of the impact of these new hospitals, was flat to Q3 2012.

Our hospital-related expenses for Q3 as a percent of revenue were flat with the same period last year. Q3 of this year was positively impacted by a $1.5 million reduction in general and professional

liability reserves, also attributable to favorable trends in claims, offset by the impact of sequestration, the continued implementation of our clinical information system and the ramp-up of the new hospitals.

G&A, which excludes stock-based compensation, for Q3 2013, was 4% of revenue, an improvement of 30 basis points from Q3 2012, as we continue to leverage the costs related to our corporate office.

Adjusted EBITDA for Q3 2013 was $135.5 million, an increase of $10.3 million, or 8.2% over Q3 2012. For the first three quarters of 2013, adjusted EBITDA was $409.3 million, an increase of $32 million, or 8.5% over the comparable period in 2012. These increases were accomplished in spite of sequestration, which negatively impacted Q3 by $8 million and the first three quarters by $17 million.

Consistent with our expectations, both D&A and interest expense increased in Q3 2013 over Q3 2012. The increase in D&A stems from our continued capital investments in capacity additions, hospital refurbishments and the clinical information system. The increase in interest expense was primarily attributable to the issuance of the 2024 senior notes, which we issued in September of 2012.

Diluted EPS for Q3 was $0.59 per share as compared to $0.44 a share in Q3 2012. EPS in Q3 2013 benefited from two items having a net after-tax impact of $0.16 per share: a $21.3 million gain in government class action and related settlements and the repurchase of 9.1 million shares via the tender offer we completed in Q1 of this year and that Jay commented on in his introductory remarks. As a reminder, EPS in Q3 2012 benefited from two items having a net after-tax impact of $0.05 per share: a $4.9 million gain related to the consolidation of St. Vincent Rehabilitation Hospital and a $3.5 million gain in government, class action, and related settlements.

As Jay highlighted in his comments, during Q3 we again demonstrated the strong cash flow generating ability of our company. Adjusted free cash flow for the quarter was $106.4 million as compared to $71.6 million in Q3 2012. And for the first three quarters of 2013, adjusted free cash flow was $264.6 million versus $186.8 million for the same period of 2012.

As can be seen on slide 16 of the supplemental slides, in addition to the previously discussed increase in adjusted EBITDA, adjusted free cash flow for the first nine months of 2013 benefited from a smaller increase in net working capital and lower maintenance CapEx.

Working capital in 2013 is benefiting from a slower rate of growth in accounts receivable as compared to the same period in 2012, primarily related to the resumption of medical necessity claims denials in 2012. Working capital in 2013 also benefits from an increased in payroll-related liabilities after experiencing a decline in these liabilities in 2012, primarily attributable to tax withholding payments related to the vesting of certain employee equity awards.

Maintenance CapEx for the first nine months of 2013 was $54.3 million. The year-over-year decline in maintenance CapEx for the first three quarters of 2013 is predominantly a pacing issue, and our estimate for the full-year remains at $80 million to $90 million. The key considerations regarding adjusted free cash flow for 2013 may be found on slide 20 of the supplemental slides.

During Q3, we continued to invest in capacity additions and facility upgrades. We also completed the purchase of four hospitals previously subject to lease agreements. For the first nine months of 2013, discretionary CapEx was $157 million. This included the acquisition earlier this year of the Walton Rehabilitation Hospital in Augusta, Georgia, as well as approximately $70 million for the aforementioned purchase of the leased hospitals. The potential to purchase a leased property typically arises as a result of either a lease maturing or an embedded purchase option becoming

exercisable. As we have discussed previously, we expect cash outlays for the purchase of leased properties to decrease in subsequent years based on the timing of these factors.

Our balance sheet and liquidity remained strong at the end of Q3. Our leverage ratio remained at 2.5 times, and the outstanding balance in our $600 million revolving credit facility declined to $35 million from $73 million at the end of Q2.

Today, we will provide the required notice to the trustee in order to exercise the call option to redeem 10% of the outstanding principal amount of our 2018 and 2020 senior notes at a price of 103% for an aggregate of approximately $60 million. This transaction will be completed in Q4 and is consistent with our strategy of proactively managing our debt maturities and reducing our financing costs.

And now at this time, I'll ask the operator to open the lines for questions.

QUESTION AND ANSWER SECTION

Operator: Thank you. [Operator Instructions] Your first question comes from Frank Morgan of RBC Capital Markets.

<A – Jay Grinney – HealthSouth Corp.>: Good morning.

<Q – Frank Morgan – RBC Capital Markets LLC>: Good morning. Just a couple of questions here on the – just curious about the incremental costs associated with the rollout of your clinical IT systems. And then also, just the cost of the drag of these three start-up hospitals and any commentary around when those may be turning into, becoming profitable? Thanks.

<A – Jay Grinney – HealthSouth Corp.>: Let me – I'm going to ask Doug to talk about CIS. The hospitals for the – in fact all of the hospitals are now EBITDA positive. So, they are all coming out of the gate very nicely. As you know, before each hospital is opened, there are certain start-up costs that cannot be capitalized that occur prior to opening, and then once they're opened, we have to treat 30 patients before we're able to get Medicare in and complete all the certification and so on to be able to start billing Medicare for those patients.

So, with respect to the CIS, I'm going to ask Doug to respond to that.

<A – Douglas Coltharp – HealthSouth Corp.>: And Frank, the year-over-year increase in CIS implementation costs is very consistent with the expectations that we had previously provided. For the second half of 2013, it's creating a headwind of about $1 million per quarter. The implementation remains on track, and I'll ask Mark to maybe provide a comment on just the number of hospitals in which it's installed and the overall rollout plans.

<A – Mark Tarr – HealthSouth Corp.>: Yeah. Frank, this is Mark. We have it in 31 of our hospitals now. Next week, we'll go live for an additional five hospitals, putting us at a total of 36 hospitals ending this year. So, the implementation process has gone well. The integration with our partnered hospitals or referral labs or diagnostic capabilities in order to transfer information back and forth has gone extremely well from the interface perspective. So, we're very pleased with the overall system.

<A – Jay Grinney – HealthSouth Corp.>: And the final comment I would make is, I know we have reported previously that we were evaluating whether or not we wanted to ramp up the pace of implementation. We looked at that, we looked at the incremental costs that would be involved, and we have concluded that that does not make sense to do that right now. There is no real near-term compelling reason to do – to accelerate. We think that the electronic medical record system is absolutely the right investment to make for the long term. And we certainly believe that it will position us very nicely in that new world order of accountable care organizations, bundled

payments, integrated care, coordinated care, whatever you want to call it. But we made the decision not to accelerate that pace, and we should have all of the hospitals up on this by the end of 2017.

<Q – Frank Morgan – RBC Capital Markets LLC>: Okay. Thanks.

Operator: Thank you. Your next question comes from Whit Mayo of Robert Baird.

<Q – Whit Mayo – Robert W. Baird & Co. Equity Capital Markets>: Hey, thanks. Jay, on the buyback announcement, is that something that you're committed to executing over a specific timeframe, or is there a less concrete plan on that at this point?

<A – Jay Grinney – HealthSouth Corp.>: I would say it's a less concrete plan. I mean, you can look at buybacks in a lot of different ways. As we think about the next several quarters anyway, certainly the next two quarters, we anticipate that there is the potential for some volatility in healthcare stocks, as Washington grapples with the budget and some kind of debt ceiling resolution. There is also the doc fix out there. And if the future is any guide – excuse me, the past is any guide to the future, we've seen this play out before, where proposals are tossed out there, some elements of the market go nuts, they overreact, and so we see this at least in the short-term as being a little more defensive. But as you saw in the release, this is an open-ended share repurchase authorization. So we'll be looking at this and evaluating the strategy on a real-time basis, but we see it as sort of a opportunistic opportunity to take advantage of any change, dramatic change in the stock price that may occur as a result of what's going on in Washington or what's not going on in Washington.

<Q – Whit Mayo – Robert W. Baird & Co. Equity Capital Markets>: Okay, that's helpful, it sounds very opportunistic, and I guess it ranks at the lower end of your capital deployment priorities at this point?

<A – Jay Grinney – HealthSouth Corp.>: But only in the short term. I mean, again, we put this in place to be proactive over the long term, and I'm trying to just give some visibility on Q4, Q1 of next year, what we're thinking, and the thinking is there could be announcements that are completely outside of our control, the reaction of which is completely outside of our control. If that happens, and the stock moves down, we think it's a great opportunity to buy, we'll do it.

<Q – Whit Mayo – Robert W. Baird & Co. Equity Capital Markets>: And this – my second question is a little random, but I think you've got a call option to acquire some equity in Surgical Care Affiliates, and does that enter your thinking at all with their IPO underway, and maybe just explain some of the mechanics behind the trigger of that?

<A – Jay Grinney – HealthSouth Corp.>: It doesn't really change much of our thinking, but I'm going to ask Doug to explain what we have – what the option is, and what the mechanics are, and what we're hearing right now, whether or not we'll even be able to exercise that option.

<A – Douglas Coltharp – HealthSouth Corp.>: Whit, broadly speaking, we acquired, or got as part of the purchase price consideration when we sold the surgical care centers back in 2007, an option to acquire 5% of the equity if there were certain performance metrics that were met by the company and if there were an IPO or another monetization event that resulted in the sale of at least 30% of the shares. So, there are kind of two triggers there. It's one the financial performance and then the monetization at that level.

We know from the S-1, preliminary S-1 that has been filed by SCA that they believe that the financial metrics have been met and that the option would be in the money. That then leads to the question of whether or not the IPO will result in the sale of more than 30% of the shares – and

actually I believe it's whether more than 30% of the shares will be traded or listed. If it does, it will probably make sense for us to go ahead and exercise that option.

What we do with that equity after we have exercised the option remains to be determined. But I don't think that there is any intent here for us to get back into the surgery center business.

<Q – Whit Mayo – Robert W. Baird & Co. Equity Capital Markets>: Okay. That's helpful. Thanks.

<A – Douglas Coltharp – HealthSouth Corp.>: And there's no way for us to tell right now based on the financial information that is available to us, which is the same information available to the public through the company's filings, what the potential value of that option is.

<Q – Whit Mayo – Robert W. Baird & Co. Equity Capital Markets>: Okay. Thanks a lot.

Operator: Thank you. Your next question comes from Sheryl Skolnick of CRT Capital Group.

<Q – Sheryl Skolnick – CRT Capital Group LLC>: Good morning. Thank you very much. Jay, you touched on the situation in Washington, and I would agree it's smart to keep your powder dry in the event that Washington does manage to agree to do something and that something is a target at HealthSouth and its peers' business potential. But – so that's smart thinking, and I think, let's hope you don't have to use it for that. But it does bring up the issue of – can you give us any sense of the things that you're looking at for 2014 and going out of 2013 into 2014, as the opportunities to add additional capacity, to create the passive growth to extend beyond the fourth quarter of 2014 and maybe one facility for 2015? So that would be on the growth side. And then, on the pricing and perhaps even strategic acquisition opportunities and what you see. So, I'm asking you to give me color on 2014 without asking you to give me guidance, if that makes sense.

<A – Jay Grinney – HealthSouth Corp.>: Yeah. I think that makes perfect sense. And I think that the way to look at 2014m and frankly 2015 and 2016, is a continuation of our current business plan. Our development pipeline is very attractively populated with opportunities that we think will allow us to continue to add hospitals, enter new markets. In some cases, we're going to be rounding out existing markets and expanding our presence in certain states, but the opportunity is definitely there. As we have reported previously, a lot of the transactions are acquisitions of existing units of not-for-profit, predominantly not-for-profit hospitals IRF [inpatient rehabilitation facilities] units, and then taking that unit and bringing it into a freestanding hospital in that market. And that would be very similar to what we see in about a third of our existing portfolio, where we have joint ventures with large acute care systems. So that certainly creates, I think, a very nice opportunity for us into 2014, into 2015, and into 2016.

With respect to moving beyond our core business, we still believe that that has to be driven by either the progression of the industry to some kind of ACO or bundled payment or something that is – that looks a lot different than what we have right now, where a true integrated continuum is valuable. What we're seeing in our markets is that there is a lot of talk about ACOs, there's a lot of talk about these different payment models, but there isn't a whole lot of movement in that direction. So we want to be – we want to keep our eyes on the future and try to anticipate where things are going. But as we think about where those – what services might be attractive, we've said in the past we think home care is attractive in that new world order to meet the integration needs. But right now, I mean I've got to tell you that home care I think is going to be in for some very, very tough sledding over the next couple years. And it just does not make any sense to us to jump into that space and to try to manage down a 3.5% per year pricing cut from the largest payer.

We've certainly seen what some of the companies out there are reporting, we were in touch with a lot of privately held companies, and it's just tough. It is very, very challenging. So we would need a lot more regulatory clarity before that then made sense. So we need visibility on the pace of the

delivery system evolution, and then we would need a lot more clarity on what kind of pricing and/or patient criteria environment might be out there.

<Q – Sheryl Skolnick – CRT Capital Group LLC>: That's great, Jay. Thank you. That's terrific on the top line. What about, as you look at the business in terms of the structure and leveraging your cost base, do you have a sense that there is any new opportunities or continuation of existing opportunities, to drive more efficiencies through the model?

<A – Jay Grinney – HealthSouth Corp.>: I think we're pretty efficient right now, and the opportunities will come with the ability of Mark and the regional presidents and the hospital CEOs to add that new volume in a very profitable manner incrementally. And they've really been able to do that, I think, very effectively. We feel very good about our business model in that regard. And as you know and I think everyone knows, the underlying demand curve for inpatient rehabilitative services is pretty strong. And it's just driven by the aging of the population and the inevitable need that we all will have for rehabilitative services the older we get.

We are looking at our hospitals' physical plants. We're looking at an opportunity to standardize many of the functions within our physical plants, trying to get ahead of some of the ongoing maintenance needs, looking at the overall capabilities of our plant managers, looking at opportunities to improve that element of our cost structure. But beyond that, I think it's a lot of singles and doubles. There aren't really any home runs, and that's again a function of the fact that we're already pretty lean and mean. But we're always looking for those opportunities to make us even more disciplined from a cost standpoint.

<Q – Sheryl Skolnick – CRT Capital Group LLC>: Great. Thank you so much and terrific job. It's hard work to do what you guys do every day.

<A – Jay Grinney – HealthSouth Corp.>: Thank you.

Operator: Thank you. Your next question comes from Rob Mains of Stifel.

<Q – Rob Mains – Stifel, Nicolaus & Co., Inc.>: Yeah. Thanks. Good morning.

<A – Jay Grinney – HealthSouth Corp.>: Good morning.

<Q – Rob Mains – Stifel, Nicolaus & Co., Inc.>: Kind of keeping on the Washington theme, last call you gave us a pretty nice update on sort of what your thinking is in terms of how the inpatient rehab facility can be at the table in terms of discussions of how to save cost, but to do so in a rational manner. My first question is, do you feel that those discussions are getting any traction?

<A – Jay Grinney – HealthSouth Corp.>: The answer is yes. And for those who are not participating on the last quarter call, what Rob is referring to is the fact that we have offered an alternative cost saving measure to the proposal to reset the 60% rule up to 75%. And our position is, when that occurs, the Medicare beneficiary who needs rehabilitative care, whose physician has determined they need inpatient rehabilitative care, but now because of a government fiat, a CMS regulation, they can't get that care, they're going to be forced to go into the second best alternative. And in some cases, it's not even the second best alternative, and that would be the local nursing home.

So resetting the rule, while it may generate some savings – some scored savings, it really puts the burden of that shift onto the backs of the Medicare beneficiaries. Our proposal, and it is getting traction, to answer your question, Rob, it's definitely getting traction in DC. How much and whether or not we'll be successful is, I think, still up in the air. But we're working the Hill pretty hard with a proposal to have the outlier payments be revised in a manner that would cap any individual IRF Medicare payments to a percentage of their total.

So as we look at it, and we've done a pretty deep dive on this, we've actually engaged a third party to look at it in even greater detail and really do some hard data analytics, but – and this is found on page nine, by the way, of our Investor Reference Book. But if you look at the $200-and-some million that's spend on outlier payments in IRF today, about half, a little over half, goes to the top decile of hospitals. And if you dig into those hospitals that are getting outlier payments, and you start looking at the history, how much have they been getting year after year, there is an astonishing number of IRF providers who are living off of these outlier payments.

Well, outlier payments were designed to pay for the train wrecks, the high-cost patients. It was estimated about 3% of Medicare IRF payments would go to these kinds of patients, and you're seeing many of these IRF providers, they're getting 30%, 40%, 50% of their total IRF payments are coming through the outlier pool. And so we – what we're proposing is that that be limited – they've done this with home care, I believe, and maybe in other instances – limit the amount of outlier payments any single IRF can provide – can receive to say 10%. And then by doing that, it puts the burden on providers to become more efficient.

Still get the same kind of savings, and we do know that one member, in fact the ranking member on the Senate Budget Committee, has asked the CBO to score this. So we're hoping that that will occur. My guess is that CBO is being inundated with all kinds of requests to score this, that, and the other. But we're hoping that that will occur, because we think this is a very viable option to resetting the 75% – or the 60% rule and harming beneficiaries' access to rehabilitative care.

<Q – Rob Mains – Stifel, Nicolaus & Co., Inc.>: Okay. Great. That's helpful. And then kind of a corollary to the policy questions, you alluded to a lot of the competition being units in not-for-profit hospitals, and some of them are looking to partner. Just curious whether you're seeing any movement on the part of any of them to kind of just throw in the towel, given the challenges or the changes going on in the hospital business, and therefore creating a share opportunity for you?

<A – Jay Grinney – HealthSouth Corp.>: No. I don't know that there are many willing to just abandon their IRF business. There may be some, but I'm just doing a mental checklist in the development pipeline. Most of them are struggling with their IRF business and see that as being important long-term, and frankly, I think the fact that we're coming in offering to help them with their services and to joint venture those services is giving them a bit of a lifeline.

<Q – Rob Mains – Stifel, Nicolaus & Co., Inc.>: Got it. Thank you very much.

Operator: Thank you. Your next question comes from Gary Lieberman of Wells Fargo.

<A – Jay Grinney – HealthSouth Corp.>: Good morning, Gary.

<Q – Gary Lieberman – Wells Fargo Securities LLC>: Good morning. Thanks. How are you?

<A – Jay Grinney – HealthSouth Corp.>: Good.

<Q – Gary Lieberman – Wells Fargo Securities LLC>: I guess going back to the $30 million benefit that you partially attributed to improvement in medical necessity claims, can you talk a little bit about that? Is that you guys are doing a better job, is that the RAC [recovery audit contractors] sort of seeing the light, or what – how would do you characterize that?

<A – Douglas Coltharp – HealthSouth Corp.>: Yeah. So, what Gary is referring to is the improvement in 2013 in net working capital, a portion of which I attributed in my comments to slower growth this year versus last year in our receivables balance. And Gary, you may recall, based on really what has now been several years of discussions regarding the ADRs [additional documentation requests] and the medical necessity claims reviews, that there's been an on-again,

off-again nature to those. And what we experienced in 2012 is after a period of relative inactivity, those resumed. And at the same time, we were first witnessing the slowdown in the administration of the adjudication process. So, both of those factors led to a more rapid buildup in accounts receivable in 2012.

As we move into 2013, although that administrative backlog hasn't gotten any better, and we are seeing new claims denials come in, all of that is having a less – lesser impact, because it's not going from a ground zero up to 60 miles an hour. It's just really incremental to what was built in 2012. Does that make any sense?

<Q – Gary Lieberman – Wells Fargo Securities LLC>: Yeah. That's very helpful.

<A – Douglas Coltharp – HealthSouth Corp.>: Now, there is a component of it that is also the fact that we think we're pretty good at working these claims and providing the information and moving them through the adjudication process, but the bigger part is really just kind of a timing issue as to when those resumed and then what the incremental growth rate is.

<Q – Gary Lieberman – Wells Fargo Securities LLC>: Okay. And then, maybe on my follow-up, you talked about length of stay I guess decreasing, acuity went up. Can you discuss the dichotomy there? And then maybe what the impact of the change in length of stay had on revenue per discharge.

<A – Mark Tarr – HealthSouth Corp.>: Yeah. Hi, Gary. This is Mark. I mean the length of stay sometimes can be as simple, and it was in this case, as to which day of the week the quarter ends, and we typically have a disproportionate number of our discharges end on a Friday or a Thursday. So therefore, you get a high number of discharges at end of the month, which has a tendency to have an artificial impact on the length of stay itself. So that has a way, from a longer-term perspective, of evening out, but I don't want to – I don't want you to have the take-away that we're seeing a huge decrease in our length of stay from a clinical standpoint.

<A – Douglas Coltharp – HealthSouth Corp.>: In terms of its impact on pricing, it was of a magnitude that's sufficient for us to call out, but it was really a fraction of the impact from sequestration.

<Q – Gary Lieberman – Wells Fargo Securities LLC>: Okay, great. Thanks a lot.

<A – Jay Grinney – HealthSouth Corp.>: You bet.

Operator: Thank you. Your next question comes from Darren Lehrich of Deutsche Bank.

<A – Jay Grinney – HealthSouth Corp.>: Hi, Darren.

<Q – Darren Lehrich – Deutsche Bank Securities, Inc.>: Hey, good morning, everybody. So I just wanted to gain a little more insight into the reserve adjustments that you highlighted, I guess $8 million in total. And in particular, just as far as the medical claims go, Doug, how should we be thinking about that in terms of how they relate to this period versus prior periods? And then is there anything in particular you could attribute to the improvements here? I know you made some bed adjustments, or bed investments rather, several years ago. Is there anything you'd call out as it relates to what you're seeing?

<A – Douglas Coltharp – HealthSouth Corp.>: Sure. I'll try to provide some color there. First, the adjustment in the group medical reserves was the largest piece of the overall self insurance adjustment that we made. I also think it's fair to say, although these don't break out all the time in terms of black and white buckets, that most of that is attributable to the current year. In other words, we were running at a higher accrual rate through the first two quarters, and we saw an adjustment

based on the claims trends for this year that caused us to reverse a portion of that during the third quarter. So it was all contained within 2013.

There are two things, and, Darren, I think you have identified both of them here, that are going through that. The first is that we have made some changes to our programs and how we manage those programs, trying to provide our employees with more incentives and more information to maintain healthy lifestyles and to avoid some of the more either routine, unnecessary expenditures or the more catastrophic ones that result if you're not participating in wellness programs. And we definitely believe that that is having a positive impact on the claims trends.

But frankly, there is an element of this that is also a little bit harder to predict, and what we have witnessed for the first three quarters of 2013 is we have just seen a much lower incidence of high dollar claims. And that's great news, but it can change very rapidly as well. So to suggest that that portion of it might be a trend that continues into 2014 or beyond, that one is substantially harder to predict.

<A – Mark Tarr – HealthSouth Corp.>: Darren, this is Mark. On the workers comp side of that impact, we have tried to make sure our hospitals have the most updated equipment possible to help assist our staff in working with our patients. As you know, there is a fair amount of lifting and transferring of rehabilitation patients. So things like having new beds that have the scales built into the beds themselves, so we can weigh the patients without having to get them up out of bed, put in a wheelchair, and then wheeled on to scales down the hallway. We've also made sure that we have ample lifts available in close proximity to our nursing staff, Hoyer Lifts, to help lift the patients. And then thirdly, a fair amount of our patients now are obese, and we've made sure that we have the proper equipment to once again assist our staff in handling the larger patients that we're seeing in our hospitals nowadays. All will help us eliminate back injuries, injuries that occur with lifting and transferring of our patients.

<Q – Darren Lehrich – Deutsche Bank Securities, Inc.>: That's real helpful, and then maybe just one follow-up. You do employ a lot of people, and curious just around your comments, Doug, with regard to group medical and what seems to be some changes in your benefit programs. Can you just comment a little bit on how high deductible plans play into this for you guys and how some of your employees are electing some of those types of things?

<A – Jay Grinney – HealthSouth Corp.>: Darren, this is Jay. We have not changed our benefit offering at all. In fact, we have continued to provide full coverage for employees, for spouses. I know a lot of other companies are dropping coverage for spouses. There is a lot of publicity around the big companies that are saying they're going to exchanges. We haven't taken any of those actions, and we're not reducing our benefit offerings, and we're, I think, offering a very, very competitive package. So we have not seen any need to go to an increasingly higher deductible or copayment plan. And in fact, this year, as we have announced to our employees, the cost – the employee cost per paycheck for the new year is going to be between $6 and $12, depending, $6 is at the low end I guess for single and $12 is at the family level.

So, we just have put in programs, as Doug said, that have helped to incentivize our employees to live healthier lives, and those who are on medication, to get their medication, to make sure they're taking their medication. A couple years ago, we put in a program that incentivized employees to fill out a pretty comprehensive questionnaire. We gave them a rebate on their premiums for doing that. And that then allowed the benefits folks here at corporate, along with our third-party administrator, to help monitor some of those employees who have a little more complicated medical history to manage their conditions more effectively.

The other thing, I think, is we ought to just mention is part of this reserve adjustment is a function of looking back and recognizing that we had some pretty big claims in 2009, 2010, and 2011. I mean really unusual transplant-type claims. And of course, the actuaries who are using that information

say “okay, going forward you need to reserve at a higher amount.” But as Doug said, most of that reserve adjustment in the third quarter is attributable to 2013 group health lower costs.

<Q – Darren Lehrich – Deutsche Bank Securities, Inc.>: Great. Okay. Thanks very much.

<A – Jay Grinney – HealthSouth Corp.>: Yep.

Operator: Thank you. Your next question comes from A.J. Rice of UBS.

<Q – A.J. Rice – UBS Securities LLC>: Hi everybody.

<A – Jay Grinney – HealthSouth Corp.>: A.J.

<Q – A.J. Rice – UBS Securities LLC>: First, let me ask you about some of the labor metrics, turnover, productivity, and use of temporary staffing. Is any of that moving around very much, relative to where it’s been the last few quarters?

<A – Mark Tarr – HealthSouth Corp.>: Hi A.J., this is Mark. I would not say we’ve seen a large movement from quarter to quarter. So much of that depends upon our ability to recruit and maintain staff, of which we’ve shown a really nice trend on that over the past several years, particularly on the licensed therapy side, with our ability to retain our staff and reduce turnover far surpasses the industry average. So I would say, we’re not seeing any real major trends or shifts in that.

<Q – A.J. Rice – UBS Securities LLC>: Okay. And then maybe a follow-up, just to ask about, obviously your bad debt accrual’s a small number, up slightly. But you’re calling out the claims denial by fiscal intermediaries and the lengthening of the adjudication process. Is that just what you’ve been seeing on an ongoing basis, or is there anything new there that you’re flagging?

<A – Jay Grinney – HealthSouth Corp.>: I think the, it’s new this year, and that is the back-up at the ALJ level. It’s been pretty widely publicized that there are a lot of vacancies for administrative law judges. You combine that with increased denial activity, not just for IRFs, but with RAC audits et cetera, there is a – there is an increasing backlog across the system, and it’s not, from what I understand, not just related to healthcare. So that’s new within the last say 9 months to 12 months.

<Q – A.J. Rice – UBS Securities LLC>: Okay, but you wouldn’t forecast any meaningful movement on that bad debt percentage looking out over the next – to the next year or anything?

<A – Douglas Coltharp – HealthSouth Corp.>: Well, as far as we’ve looked forward in terms of providing any guidance is the fourth quarter, and there we’ve said our expectation is that it remains at a level consistent with that exhibited in Q3.

<Q – A.J. Rice – UBS Securities LLC>: Okay. All right. Thanks a lot.

<A – Jay Grinney – HealthSouth Corp.>: You bet.

Operator: Thank you. Your next question comes from Miles Highsmith of RBC.

<A – Jay Grinney – HealthSouth Corp.>: Good morning, Miles.

<Q – Miles Highsmith – RBC Capital Markets LLC>: Hi. Good morning, guys.

<A – Douglas Coltharp – HealthSouth Corp.>: Good morning.

<Q – Miles Highsmith – RBC Capital Markets LLC>: Hi. A question for you, Doug, on the bonds. So the 10% call option on the 7.25% is, as I understand it, exists through October 1 of 2014, 10% annually, and on the 7.75% annually through September 15 of 2015.

<A – Douglas Coltharp – HealthSouth Corp.>: Right.

<Q – Miles Highsmith – RBC Capital Markets LLC>: I'm just trying to understand the specific nuances, are there discrete periods where you have that option, or is it an option that exists at any time as long, as it's during the period of a year? I guess how many more chances will we see to, not what you're going to do, how many opportunities will you have to use that 10% on those two tranches? Thanks.

<A – Douglas Coltharp – HealthSouth Corp.>: Miles, I think you've got a correct understanding. We have the ability to exercise those options once during every 12-month period. So you may recall we first exercised that option when it became available to us in September of 2012. There is a 30-day period essentially from the time we give notice to the trustee to when it's exercised.

When we crossed that notification period in early September, the option for this year became available to us again. At that point in time, we were looking out there at things like whether or not the Fed was going to taper, any announcement with regard to a change in the Fed Chairmanship, the budget showdown, all of those things with which you're familiar, because the option is not just at a point in time, but is actionable any time for the next 12 months after it becomes exercisable. We decided to wait a little bit longer. We now feel like we have sufficient clarity to recognize that it makes sense to move forward.

So that option will exist, if we do that again, and say let's assume that we are giving notice to the trustee today, the option for 2014 will become actionable again once we have hit October 29 of 2014, but not prior to that point.

<Q – Miles Highsmith – RBC Capital Markets LLC>: Okay. So if I think about it right, then you'll have an opportunity starting October 29, but then you will not have another opportunity on 7.75%, if I'm thinking about it correctly, because that option expires September 15 of 2015. Is that fair?

<A – Douglas Coltharp – HealthSouth Corp.>: Yeah. Then you're moving into the normal call option on those. Remember, this 103% was an additive call option. So those bonds will actually be fully callable according to the schedule that is resident in the indenture. But because of the difference in the maturity date, there will be another 10% option remaining on the 2022 notes.

<Q – Miles Highsmith – RBC Capital Markets LLC>: Okay. Great. So just to recap, October 29 of 2014 will be the trigger period for next year's call option. So you would have the opportunity to call 10% of both tranches at that time, and that would be the final opportunity you would have before it goes into the regular call period on both tranches?

<A – Douglas Coltharp – HealthSouth Corp.>: No, the 2018s are done this year, and then there'll be an option after October 29 next year on the 2022s, and then another one of those options again in – nope, and then they'll be fully callable thereafter. So we've got the option on both notes that we're exercising today, we'll have the option on the 2022s only actionable after October 29, 2014, and beyond that, both tranches will be fully callable.

<Q – Miles Highsmith – RBC Capital Markets LLC>: Right, that's right. I said it wrong. Okay, great. Thank you very much.

<A – Jay Grinney – HealthSouth Corp.>: You're welcome.

Operator: Thank you. Your next question comes from Kevin Fischbeck of Bank of America Merrill Lynch.

<A – Jay Grinney – HealthSouth Corp.>: Good morning, Kevin.

<Q – Joanna Gajuk – Merrill Lynch, Pierce, Fenner & Smith, Inc.>: Good morning. Actually, this is Joanna Gajuk in for Kevin today. The question that I have just on the – some color on the very strong discharge number this quarter, the 5.7% growth, so any sort of details in terms of maybe the business lines that are a bit better and maybe by geography?

<A – Jay Grinney – HealthSouth Corp.>: No, the discharge growth that we saw in the quarter actually has been pretty consistent with what we've been seeing over the last probably – since 2008. Just a continuation, we continue to take market share. We continue to take advantage of the fact that the population is aging, and with that comes an increased demand in inpatient rehabilitative services. So, there wasn't really anything different in the third quarter. And from a geography standpoint, it was pretty evenly distributed across all of our regions.

<Q – Joanna Gajuk – Merrill Lynch, Pierce, Fenner & Smith, Inc.>: And on that and also your comment about the outlook for fourth quarter at 3% to 4%, it's pretty much just about the comps last year, correct? You don't see any changes in fourth quarter for your discharge outlook?

<A – Jay Grinney – HealthSouth Corp.>: That's correct, that's correct. We don't see anything in the fourth quarter that is going to change the overall profile, but to your point, we are up against some pretty tough comps with a 5.4% increase last year.

<Q – Joanna Gajuk – Merrill Lynch, Pierce, Fenner & Smith, Inc.>: Great. Thank you. That's all for me.

<A – Jay Grinney – HealthSouth Corp.>: All right. Thank you.

Operator: Thank you. There are no further questions. I will now hand the floor back over to Mary Ann Arico.

Mary Ann Arico, Chief Investor Relations Officer

Thank you, Christie. As a reminder, we will be filing the updated Investor Reference Book next week. If you have additional questions, I will be available later today. Please call me at 205-969-6175. Thank you.

Jay Grinney, President, Chief Executive Officer & Director

Thank you.

Operator: Thank you. This does conclude today's conference call. You may now disconnect.