

FIVE STAR QUALITY CARE INC
Form 8-K/A
July 28, 2005

**UNITED STATES
SECURITIES AND EXCHANGE COMMISSION**

WASHINGTON, D.C. 20549

FORM 8-K/A

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

Date of Report (Date of earliest event reported): **July 28, 2005 (June 3, 2005)**

FIVE STAR QUALITY CARE, INC.

(Exact Name of Registrant as Specified in Its Charter)

Maryland
(State or other jurisdiction
of incorporation)

Commission File No. 1-16817

04-3516029
(IRS Employer
Identification No.)

400 Centre Street, Newton, Massachusetts
(Address of Principal Executive Offices)

02458
(Zip Code)

Registrant's telephone number, including area code: **(617) 796-8387**

Check the appropriate box below if the Form 8-K filing is intended to simultaneously satisfy the filing obligation of the registrant under any of the following provisions:

- o Written communications pursuant to Rule 425 under the Securities Act (17 CFR 230.425)

- o Soliciting material pursuant to Rule 14a-12 under the Exchange Act (17 CFR 240.14a-12)

 - o Pre-commencement communications pursuant to Rule 14d-2(b) under the Exchange Act (17 CFR 240.14d-2(b))

 - o Pre-commencement communications pursuant to Rule 13e-4(c) under the Exchange Act (17 CFR 240.13e-4(c))
-

Edgar Filing: FIVE STAR QUALITY CARE INC - Form 8-K/A

This Current Report on Form 8-K/A amends the Current Report on Form 8-K of Five Star Quality Care, Inc., or Five Star, dated June 3, 2005, and is being filed solely for the purpose of including the consolidated financial statements of Gordon Health Ventures, LLC, or Gordon. Five Star filed the June 3, 2005, Current Report on Form 8-K with the Securities and Exchange Commission to report, among other items, information concerning the acquisition by Five Star on June 3, 2005 of six assisted living communities from Franciscan Manor Associates, LLC, Muirfield Associates, LLC, Prestwicke Associates, LLC, Royal Aberdeen Associates, LLC, Troon Associates, LLC and Turnberry Associates, LLC, subsidiaries of Gordon, for a purchase price of approximately \$58.0 million.

Item 9.01. Financial Statements and Exhibits.

(a) *Financial Statements of Business Acquired.*

Gordon Audited Historical Financial Statements and Unaudited Interim Financial Statements

| | |
|--|------------|
| <u>Report of Independent Auditors</u> | <u>F-1</u> |
| <u>Consolidated Balance Sheets at December 31, 2004 and March 31, 2005 (unaudited)</u> | <u>F-2</u> |
| <u>Consolidated Statements of Income for the year ended December 31, 2004 and the three months ended March 31, 2005 and 2004 (unaudited)</u> | <u>F-3</u> |
| <u>Consolidated Statements of Members' Deficit for the year ended December 31, 2004 and the three months ended March 31, 2005 (unaudited)</u> | <u>F-4</u> |
| <u>Consolidated Statements of Cash Flows for the year ended December 31, 2004 and the three months ended March 31, 2005 and 2004 (unaudited)</u> | <u>F-5</u> |
| <u>Notes to Consolidated Financial Statements</u> | <u>F-6</u> |

(b) *Pro Forma Financial Information.*

Five Star Unaudited Pro Forma Consolidated Financial Statements

| | |
|---|-------------|
| <u>Introduction to Unaudited Pro Forma Consolidated Financial Statements</u> | <u>F-11</u> |
| <u>Unaudited Pro Forma Consolidated Balance Sheet at March 31, 2005</u> | <u>F-12</u> |
| <u>Unaudited Pro Forma Consolidated Statement of Operations for the three months ended March 31, 2005</u> | <u>F-13</u> |
| <u>Unaudited Pro Forma Consolidated Statement of Operations for the year ended December 31, 2004</u> | <u>F-14</u> |
| <u>Notes to Unaudited Pro Forma Consolidated Financial Statements</u> | <u>F-15</u> |

(c) *Exhibits.*

(a) *Financial Statements of Business Acquired.*

Report of Independent Auditors

Edgar Filing: FIVE STAR QUALITY CARE INC - Form 8-K/A

To the Management and Members of

Gordon Health Ventures, LLC

We have audited the accompanying consolidated balance sheet of Gordon Health Ventures, LLC (the Company) as of December 31, 2004, and the related consolidated statements of income, members' deficit and cash flows for the year then ended. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. We were not engaged to perform an audit of the Company's internal control over financial reporting. Our audit included consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the consolidated financial position of the Company at December 31, 2004, and the consolidated results of its operations and its cash flows for the year then ended, in conformity with accounting principles generally accepted in the United States.

The accompanying consolidated financial statements have been prepared assuming that the Company will continue as a going concern. As more fully described in Note 1, the Company has a working capital deficiency and members' deficit. In addition, the Company has not complied with certain terms and covenants of its loan agreement. These conditions raise substantial doubt about the Company's ability to continue as a going concern. Management's plans in regard to these matters are also described in Note 1. The financial statements do not include any adjustments to reflect the possible future effects on the recoverability and classification of assets or the amounts and classification of liabilities that may result from the outcome of this uncertainty.

/s/ Ernst & Young LLP

April 15, 2005

Except for Note 9, as to which

date is June 3, 2005

GORDON HEALTH VENTURES, LLC

CONSOLIDATED BALANCE SHEETS

Edgar Filing: FIVE STAR QUALITY CARE INC - Form 8-K/A

| | December 31, 2004 | March 31, 2005 (Unaudited) |
|--|----------------------|----------------------------------|
| ASSETS | | |
| Current assets: | | |
| Cash and cash equivalents | \$ 6,000 | \$ 8,827 |
| Restricted cash | 259,006 | 159,179 |
| Accounts receivable, net | 207,227 | 391,501 |
| Inventories | 58,220 | 69,475 |
| Prepaid expenses | 186,350 | 134,662 |
| Total current assets | 716,803 | 763,644 |
| Property and equipment, net | 38,782,561 | 38,465,006 |
| Due from affiliate | 152,651 | 152,651 |
| Deferred financing costs, net | 234,186 | 207,186 |
| | \$ 39,886,201 | \$ 39,588,487 |
| LIABILITIES AND MEMBERS DEFICIT | | |
| Current liabilities: | | |
| Bank overdrafts | \$ 316,639 | \$ 814,308 |
| Accounts payable | 1,327,842 | 686,809 |
| Accrued expenses | 1,360,838 | 1,206,641 |
| Resident security deposits | 876,748 | 813,631 |
| Unearned revenue | 874,331 | 874,331 |
| Delinquent taxes payable | 3,998,368 | 4,150,139 |
| Mortgage notes payable | 45,123,184 | 44,976,512 |
| Total current liabilities | 53,877,950 | 53,522,371 |
| Commitments and contingencies | | |
| Members deficit | (13,991,749) | (13,933,884) |
| | \$ 39,886,201 | \$ 39,588,487 |

See notes to consolidated financial statements.

GORDON HEALTH VENTURES, LLC

CONSOLIDATED STATEMENTS OF INCOME

| | Year Ended December 31, 2004 | 2004 | Three Months Ended March 31, (Unaudited) | 2005 |
|-------------------------------|------------------------------------|--------------|--|------|
| Revenues | | | | |
| Net revenues from residents | \$ 20,070,423 | \$ 4,848,330 | \$ 4,942,349 | |
| Total revenues | 20,070,423 | 4,848,330 | 4,942,349 | |
| Expenses | | | | |
| Payroll and related expenses | 10,084,757 | 2,523,466 | 2,512,916 | |
| Food and supplies | 1,239,553 | 309,873 | 301,028 | |
| Property taxes | 966,444 | 241,611 | 184,425 | |
| Utilities | 680,628 | 176,033 | 202,561 | |
| Insurance | 468,389 | 109,428 | 121,827 | |
| General and administrative | 1,555,695 | 233,847 | 173,943 | |
| Depreciation and amortization | 1,478,914 | 369,728 | 367,000 | |
| Total expenses | 16,474,380 | 3,963,986 | 3,863,700 | |
| Operating income | 3,596,043 | 884,344 | 1,078,649 | |
| Other expense | | | | |
| Interest expense | 2,945,575 | 692,417 | 825,417 | |
| | 2,945,575 | 692,417 | 825,417 | |
| Net income | \$ 650,468 | \$ 191,927 | \$ 253,232 | |

See notes to consolidated financial statements.

GORDON HEALTH VENTURES, LLC

CONSOLIDATED STATEMENTS OF MEMBERS DEFICIT

| | | |
|---------------------------------------|----|--------------|
| Balance at January 1, 2004 | \$ | (14,236,342) |
| Distributions | | (405,875) |
| Net income | | 650,468 |
| Balance at December 31, 2004 | | (13,991,749) |
| Distributions (unaudited) | | (195,367) |
| Net income (unaudited) | | 253,232 |
| Balance at March 31, 2005 (unaudited) | \$ | (13,933,884) |

See notes to consolidated financial statements.

GORDON HEALTH VENTURES, LLC

CONSOLIDATED STATEMENTS OF CASH FLOWS

| | Year Ended December 31, 2004 | 2004 | Three Months Ended March 31, (Unaudited) | 2005 |
|---|------------------------------------|------------|--|--------------|
| Operating activities | | | | |
| Net income | \$ 650,468 | \$ 191,927 | | \$ 253,232 |
| Adjustments to reconcile net income to cash provided by operating activities: | | | | |
| Provision for bad debts | 145,000 | | | |
| Depreciation | 1,370,827 | 342,728 | | 340,000 |
| Amortization | 108,087 | 27,000 | | 27,000 |
| Changes in assets and liabilities: | | | | |
| Restricted cash | 239,696 | 84,493 | | 99,827 |
| Accounts receivable | (95,721) | (22,724) | | (184,274) |
| Inventories | (2,283) | (571) | | (11,255) |
| Prepaid expenses | (22,464) | (5,616) | | 51,688 |
| Due from affiliate | (5,183) | | | |
| Bank overdrafts | 160,103 | | | 497,669 |
| Accounts payable | 13,611 | 139,835 | | (641,033) |
| Accrued expenses | (426,569) | (99,788) | | (154,197) |
| Resident security deposits | (23,784) | (5,946) | | (63,117) |
| Unearned revenue | 52,157 | 13,039 | | |
| Delinquent taxes payable | (778,639) | (211,454) | | 151,771 |
| Net cash provided by operating activities | 1,385,306 | 452,923 | | 367,311 |
| Investing activity | | | | |
| Purchases of property and equipment | (121,373) | | | (22,445) |
| Net cash used in investing activity | (121,373) | | | (22,445) |
| Financing activities | | | | |
| Repayment of mortgage notes payable | (861,785) | (352,386) | | (146,672) |
| Distributions to member(s) | (405,875) | (101,469) | | (195,367) |
| Net cash used in financing activities | (1,267,660) | (453,855) | | (342,039) |
| Change in cash and cash equivalents | (3,727) | (932) | | 2,827 |
| Cash and cash equivalents at beginning of period | 9,727 | 9,727 | | 6,000 |
| Cash and cash equivalents at end of period | \$ 6,000 | \$ 8,795 | | \$ 8,827 |
| Supplemental cash flow information | | | | |
| Cash paid for interest | \$ 2,845,203 | \$ 664,947 | | \$ 1,155,175 |

See notes to consolidated financial statements.

GORDON HEALTH VENTURES, LLC

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

1. Organization

Gordon Health Ventures, LLC (the Company or Gordon) was formed in 2000 as a Pennsylvania limited liability company. Pursuant to the formation agreement, profits, losses and distributions are generally allocated to the members in proportion to their respective share of ownership. The Company will continue until dissolved, pursuant to the provisions of its formation agreement. The Company owns and operates six assisted-living communities located in suburban Pittsburgh, Pennsylvania, and comprised of approximately 600 living units.

The Company has experienced cash flow shortfalls. The Company is in default of its credit agreement with its lender and operating under a forbearance agreement, and the Company owes amounts to taxing authorities for unpaid federal and state payroll withholding and corporate taxes. The Company has negotiated the deferral of payment of these amounts; however, the Company's ability to continue to sustain its operations depends on, among other things, its ability to renegotiate or repay all amounts owing to its lender, the various taxing authorities and others. On January 21, 2005, Franciscan Manor Associates, LLC, Muirfield Associates, LLC, Prestwicke Associates, LLC, Royal Aberdeen Associates, LLC, Troon Associates, LLC, and Turnberry Associates, LLC, subsidiaries of the Company, entered into a purchase and sale agreement with Five Star Quality Care, Inc. (Five Star) for the sale of six assisted-living communities. The assets to be sold to Five Star include land, buildings and improvements, furniture, fixtures and other personal property, inventory, licenses and permits, files, records and resident agreements, deposits and warranties. In order for the Company to sustain its operations over the next twelve months, and in the presently foreseeable longer term, the Company is dependent upon its ability to continue to defer or renegotiate payment of the amounts owing to its lender, the various taxing authorities and others, or its subsidiaries' ability to close on the asset sale to Five Star. If the Company or its subsidiaries are unable to take any of the foregoing actions, it is likely that the Company will be required to cease operations, and its ability to realize the carrying value of its assets will be in doubt.

2. Summary of Significant Accounting Policies

Basis of Presentation

The consolidated financial statements include the Company's investments in 100%-owned subsidiaries. All of the subsidiaries are single-member Pennsylvania limited liability companies whose single member is the Company. The wholly owned subsidiaries are Franciscan Manor Associates, LLC, Muirfield Associates, LLC, Prestwicke Associates, LLC, Royal Aberdeen Associates, LLC, Troon Associates, LLC and Turnberry Associates, LLC. All intercompany transactions have been eliminated.

The consolidated financial statements as of March 31, 2005 and for the three months ended March 31, 2005 and 2004 are unaudited. In the opinion of the Company's management, all adjustments, consisting only of normal, recurring adjustments, necessary for a fair presentation

of such consolidated financial statements, have been included. The results of operations for the three months ended March 31, 2005 are not necessarily indicative of the Company's future results of operations, including for the full year ended December 31, 2005.

Revenues from Residents

Revenues consist of resident fees and other ancillary service revenues, which are generated primarily from monthly charges for assisted-living apartments, and are recognized monthly based on the terms of the residents' agreements. Advance payments are received for services and are deferred until the services are provided. Ancillary revenue is generated on a fee for service basis for supplemental items requested by residents, and is recognized as the services are provided.

Cash and Cash Equivalents

Edgar Filing: FIVE STAR QUALITY CARE INC - Form 8-K/A

The Company considers all short-term highly liquid investments purchased with an original maturity of 90 days or less to be cash equivalents.

Restricted Cash

Restricted cash consists of escrow payments deposited with the Company's mortgage lender for the payment of real estate taxes.

Accounts Receivable

Accounts receivable are recorded at their estimated net realizable value. In the case of receivables generated from residents, reserves for uncollectible amounts are estimated based upon factors which include, but are not limited to, the age of the receivable and the terms of the agreements with residents or their third-party payors. In the case of other receivables, such as those due from other entities with which Gordon has transacted business, reserves are estimated based upon factors which include, but are not limited to, the agreements with such payors, their stated intent to pay, their financial capacity to pay and other factors, which may include litigation. Accounts receivable reserves are estimates, the Company periodically reviews and revises these estimates based on new information, and such adjustments may be material. As of December 31, 2004 and March 31, 2005, the Company's bad debt reserve totaled \$145,000.

Inventories

Inventories of food, beverage, medical and other administrative supplies are stated at the lower of cost or market as determined by the first-in, first-out method.

Deferred Financing Costs

Financing costs are capitalized and amortized over the term of the related debt on a straight-line basis, which approximates the effective interest method. Accumulated amortization of deferred

financing costs totaled \$1,788,737 at December 31, 2004, and \$1,815,737 and \$1,707,671 (unaudited) at March 31, 2005 and 2004, respectively.

Advertising Costs

The Company expenses all advertising costs as incurred. The Company expensed advertising costs totaling approximately \$147,061 for the year ended December 31, 2004, and \$29,216 and \$11,750 (unaudited) for the three months ended March 31, 2005 and 2004, respectively.

Income Taxes

No provision for federal income taxes has been made in the financial statements of the Company since these taxes are the responsibility of the members rather than of the Company.

Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States requires management to make estimates or assumptions that affect the reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

Property and Equipment

Depreciation of property and equipment is expensed on a straight-line basis over estimated useful lives of up to 39 years. The cost of renewals and betterments that extend the lives or productive capacities of properties is capitalized, and expenditures for normal repairs and maintenance are charged to expense as incurred. Management regularly evaluates whether events or changes in circumstances have occurred that could indicate an impairment in the value of long-lived assets. If there is an indication that the carrying value of an asset is not recoverable, management estimates the projected undiscounted cash flows to determine if an impairment loss should be recognized. The amount of impairment loss is determined by comparing the historical carrying value of the asset to its estimated fair value. Since inception, the Company has not recorded any impairment losses.

3. Property and Equipment

Property and equipment consist of the following:

Edgar Filing: FIVE STAR QUALITY CARE INC - Form 8-K/A

| | December 31, 2004 | March 31, 2005 (Unaudited) |
|---------------------------------|----------------------|----------------------------------|
| Land, building and improvements | \$ 43,746,526 | \$ 43,764,046 |
| Furniture and fixtures | 1,614,655 | 1,617,875 |
| Motor vehicles | 407,575 | 407,575 |
| Machinery and equipment | 195,038 | 196,743 |
| | 45,963,794 | 45,986,239 |
| Less: accumulated depreciation | (7,181,233) | (7,521,233) |
| Property and equipment, net | \$ 38,782,561 | \$ 38,465,006 |

F-8

4. Mortgage Notes Payable

The Company's wholly owned subsidiaries have entered into a credit agreement with a lender for financing related to the six assisted-living communities. The notes bear interest at three-month LIBOR plus 4.5% (6.9% at December 31, 2004), and are secured by mortgages on the six assisted-living communities and an assignment of leases (primarily resident occupancy agreements). Under the credit agreement, the subsidiaries are required to make monthly minimum payments of \$336,000 for principal and interest. The notes mature on February 28, 2007. The Company is required to meet certain financial covenants under the terms of the credit agreement. All amounts owing under the credit agreement are guaranteed by the Company and one of its members.

Upon any event of default, the indebtedness becomes immediately due and payable. The Company has not remedied events of default which have occurred as a result of its failure to make timely payments to the lender and to satisfy reporting and other covenant requirements in the credit agreement. Consequently, the mortgage notes payable have been classified as a current liability as of December 31, 2004 and March 31, 2005.

5. Delinquent Taxes Payable

Delinquent taxes payable include the following:

| | December 31, 2004 | March 31, 2005 (Unaudited) |
|---|----------------------|----------------------------------|
| Federal payroll taxes withheld and not remitted | \$ 2,088,609 | \$ 2,170,023 |
| Penalties and interest on federal payroll taxes | 1,362,161 | 1,364,253 |
| State payroll taxes withheld and not remitted | 186,364 | 213,056 |
| Penalties and interest on state payroll taxes | 87,792 | 129,365 |
| Unpaid state corporate income taxes | 273,442 | 273,442 |
| | \$ 3,998,368 | \$ 4,150,139 |

6. Benefit Plan

Gordon has a 401(k) benefit plan for its employees. The plan allows participants to make elective pre-tax contributions from their annual salary, up to the maximum allowed by law. The Company does not match any of the employees' contributions.

7. Transactions with Related Parties

The Company leases its corporate offices from an affiliate under a five-year operating lease that commenced on September 1, 2001. The lease requires monthly base rent of \$6,416. Total rent

incurred and paid was \$76,992 for the year ended December 31, 2004 and \$19,248 (unaudited) for each of the three months ended March 31, 2005 and 2004. Future minimum lease payments as of December 31, 2005 under the terms of the operating lease in 2005 and 2006 are \$76,992 and \$51,328, respectively.

The Company has made noninterest bearing advances that are due on demand to an affiliate. During 2004, the Company advanced \$5,183 to this affiliate. As of December 31, 2004, the affiliate owed the Company \$152,651.

8. Contingencies

The Company is subject to litigation incidental to its business, and generally covered by insurance. The Company believes that the results of such litigation will not have a materially adverse effect on the Company's financial condition.

9. Subsequent Event

On June 3, 2005, the Company completed the sale to Five Star of its six assisted-living communities which represented substantially all of the Company's operations upon that date.

(b) *Pro Forma Financial Information.*

INTRODUCTION TO UNAUDITED PRO FORMA FINANCIAL STATEMENTS

The unaudited pro forma balance sheet at March 31, 2005, presents the financial position of Five Star Quality Care, Inc. as if our acquisition of six assisted living communities from Gordon Health Ventures, LLC, or Gordon, and our sale leaseback transaction of four communities with Senior Housing Properties Trust, or Senior Housing, had been completed as of March 31, 2005, as described in the notes thereto. The unaudited pro forma statement of operations for the three months ended March 31, 2005, presents our results of operations as if the acquisition and sale leaseback transactions had been completed as of January 1, 2005, as described in the notes thereto. The unaudited pro forma statement of operations for the year ended December 31, 2004, presents our results of operations as if the acquisition and sale leaseback transactions had been completed as of January 1, 2004, as described in the notes thereto.

These unaudited pro forma financial statements do not represent our financial condition or results of operations for any future date or period. Actual future results may be materially different from pro forma results. Differences could arise from many factors, including, but not limited to, competition in our business, the impact of changes to rates under Medicare and Medicaid reimbursement programs, our ability to successfully attract residents to our facilities, our ability to control operating expenses and our capital structure and other changes. These unaudited pro forma financial statements should be read in connection with our audited financial statements and the related management's discussion and analysis of financial condition and results of operation for the year ended December 31, 2004 (audited) and the three months ended March 31, 2005 (unaudited), included in our Annual Report on Form 10-K for the year ended December 31, 2004 and our Quarterly Report on Form 10-Q for the quarter ended March 31, 2005, respectively. You also should read the consolidated financial statements of Gordon which are included in this Form 8-K/A in connection with these unaudited pro forma financial statements.

FIVE STAR QUALITY CARE, INC.

UNAUDITED PRO FORMA CONSOLIDATED BALANCE SHEET

At March 31, 2005

(amounts in thousands, except share and per share amounts)

| | Historical | Adjustments | | Pro Forma |
|--|------------|-----------------------|------------------------------|------------|
| | | Sale/Leaseback (A) | Gordon Acquisition (B) | |
| ASSETS | | | | |
| Current assets | | | | |
| Cash | \$ 20,104 | \$ 23,900 | \$ (25,000) | \$ 19,004 |
| Accounts receivable, net | 37,118 | | | 37,118 |
| Prepaid expenses | 6,443 | | | 6,443 |
| Other current assets | 5,862 | | | 5,862 |
| Total current assets | 69,527 | 23,900 | (25,000) | 68,427 |
| Property and equipment, net | 104,176 | (21,836) | 59,000 | 141,340 |
| Restricted cash insurance arrangements | 18,943 | | | 18,943 |
| Restricted cash other | 12,294 | | | 12,294 |
| Mortgage notes receivable | 6,076 | | | 6,076 |
| Goodwill | 11,551 | | | 11,551 |
| Other long term assets | 2,131 | | | 2,131 |
| Total assets | \$ 224,698 | \$ 2,064 | \$ 34,000 | \$ 260,762 |
| LIABILITIES AND SHAREHOLDERS EQUITY | | | | |
| Current liabilities | | | | |
| Accounts payable | \$ 10,835 | | | \$ 10,835 |
| Accrued expenses | 14,869 | | | 14,869 |
| Accrued compensation and benefits | 9,223 | | | 9,223 |
| Due to Senior Housing Properties Trust | 7,986 | | | 7,986 |
| Revolving line of credit | | | 10,000 | 10,000 |
| Due to Sunrise Senior Living, Inc. | 965 | | | 965 |
| Mortgage notes payable | 493 | | | 493 |
| Accrued real estate taxes | 4,539 | | | 4,539 |
| Security deposit liability | 3,676 | | | 3,676 |
| Other current liabilities | 5,666 | | | 5,666 |
| Total current liabilities | 58,252 | | 10,000 | 68,252 |
| Long term liabilities | | | | |
| Mortgage notes payable | 41,746 | | 24,000 | 65,746 |
| Continuing care contracts | 9,170 | | | 9,170 |
| Other long term liabilities | 18,014 | 2,064 | | 20,078 |
| Total long term liabilities | 68,930 | 2,064 | 24,000 | 94,994 |
| Shareholders equity | | | | |
| Common stock, par value \$0.01 per share | 121 | | | 121 |
| Additional paid in capital | 114,753 | | | 114,753 |
| Accumulated deficit | (17,358) | | | (17,358) |
| Total shareholders equity | 97,516 | | | 97,516 |
| Total liabilities and shareholders equity | \$ 224,698 | \$ 2,064 | \$ 34,000 | \$ 260,762 |

See notes to unaudited pro forma financial statements.

F-12

FIVE STAR QUALITY CARE, INC.

UNAUDITED PRO FORMA CONSOLIDATED STATEMENT OF OPERATIONS

For the three months ended March 31, 2005

(amounts in thousands, except share and per share amounts)

| | Historical | Sale/Leaseback Transaction with Senior Housing | Historical (F) | Gordon Acquisition Adjustments | Pro Forma |
|--|------------|--|-------------------|-----------------------------------|------------|
| REVENUES: | | | | | |
| Net revenues from residents | \$ 177,201 | \$ | \$ 4,942 | \$ | \$ 182,143 |
| Pharmacy revenue | 5,256 | | | | 5,256 |
| Total revenues | 182,457 | | 4,942 | | 187,399 |
| OPERATING EXPENSES: | | | | | |
| Property level operating expenses | 137,037 | | 2,814 | (300)(G) | 139,551 |
| Pharmacy expenses | 5,024 | | | | 5,024 |
| Management fee to Sunrise Senior Living Services, Inc. | 5,620 | | | | 5,620 |
| Rent expense | 24,459 | 540(C) | | | 24,999 |
| General and administrative | 7,008 | | 683 | (1)(G) | 7,690 |
| Depreciation and amortization | 1,601 | (151)(D) | 367 | 51(H) | 1,868 |
| Total operating expenses | 180,749 | 389 | 3,864 | (250) | 184,752 |
| Operating income | 1,708 | (389) | 1,078 | 250 | 2,647 |
| Interest and other income | 137 | 32(E) | | | 169 |
| Interest expense | (615) | | (825) | 135(I) | (1,305) |
| Income (loss) from continuing operations before income taxes | 1,230 | (357) | 253 | 385 | 1,511 |
| Provision for income taxes | (35) | | | | (35) |
| Income (loss) from continuing operations | 1,195 | (357) | 253 | 385 | 1,476 |
| Income (loss) from discontinued operations | 58 | | | | 58 |
| Net Income (loss) | \$ 1,253 | \$ (357) | \$ 253 | \$ 385 | \$ 1,534 |
| Weighted Average Shares Outstanding | 12,212 | | | | 12,212 |
| Basic and diluted loss per share from: | | | | | |
| Continuing operations | \$ 0.10 | | | | \$ 0.12 |
| Discontinued operations | \$ 0.00 | | | | \$ 0.00 |
| Net income (loss) per share | \$ 0.10 | | | | \$ 0.12 |

See notes to unaudited pro forma financial statements.

FIVE STAR QUALITY CARE, INC.

UNAUDITED PRO FORMA CONSOLIDATED STATEMENT OF OPERATIONS

For the Year ended December 31, 2004

(amounts in thousands, except share and per share amounts)

| | Historical | Sale/Leaseback Adjustments | Gordon Acquisition Historical (F) | Adjustments | Pro forma |
|--|------------|-------------------------------|---|-------------|------------|
| REVENUES: | | | | | |
| Net revenues from residents | \$ 614,796 | \$ | \$ 20,070 | \$ | \$ 634,866 |
| Pharmacy revenue | 13,209 | | | | 13,209 |
| Total revenues | 628,005 | | 20,070 | | 648,075 |
| OPERATING EXPENSES: | | | | | |
| Property level operating expenses | 486,206 | | 13,439 | (1,200)(G) | 498,445 |
| Pharmacy expenses | 12,093 | | | | 12,093 |
| Management fee to Sunrise Senior Living Services, Inc. | 19,293 | | | | 19,293 |
| Rent expense | 83,370 | 2,160(C) | | | 85,530 |
| General and administrative | 20,053 | | 1,556 | (6)(G) | 21,603 |
| Depreciation and amortization | 3,666 | (601)(D) | 1,479 | 196(H) | 4,740 |
| Total operating expenses | 624,681 | 1,559 | 16,474 | (1,010) | 641,704 |
| Operating income | 3,324 | (1,559) | 3,596 | 1,010 | 6,371 |
| Interest and other income | 1,666 | 129(E) | | | 1,795 |
| Interest expense | (880) | | (2,946) | 186(I) | (3,640) |
| Income (loss) from continuing operations before income taxes | 4,110 | (1,430) | 650 | 1,196 | 4,526 |
| Provision for income taxes | (120) | | | | (120) |
| Income (loss) from continuing operations | 3,990 | (1,430) | 650 | 1,196 | 4,406 |
| Loss from discontinued operations | (699) | | | | (699) |
| Net Income (loss) | \$ 3,291 | \$ (1,430) | \$ 650 | \$ 1,196 | \$ 3,707 |
| Weighted Average Shares | | | | | |
| Outstanding | 8,716 | | | | 8,716 |
| Basic and diluted loss per share from: | | | | | |
| Continuing operations | \$ 0.46 | | | | \$ 0.51 |
| Discontinued operations | \$ (0.08) | | | | \$ (0.08) |
| Net income (loss) per share | \$ 0.38 | | | | \$ 0.43 |

See notes to unaudited pro forma financial statements.

FIVE STAR QUALITY CARE, INC.**NOTES TO UNAUDITED PRO FORMA CONSOLIDATED FINANCIAL STATEMENTS**

(amounts in thousands, except share and per share amounts)

Adjustments for the pro forma consolidated balance sheet as of March 31, 2005

A. Represents our sale of four of our assisted living communities to Senior Housing for \$24,000 on June 3, 2005. Adjustments equal cash received less book value of assets on June 3, 2005. Simultaneously with the sale, we leased back these communities from Senior Housing and used the cash from the sale to purchase six assisted living communities from Gordon (see Note B). Adjustments are calculated as follows:

| | | |
|--|----|----------|
| Sale price | \$ | 24,000 |
| Less: estimated closing costs | | (100) |
| Cash received | | 23,900 |
| Book value of sold assets as of June 3, 2005 | | (21,836) |
| Deferred gain on sale of assets | \$ | 2,064 |

B. On June 3, 2005, we acquired six assisted living communities from Gordon for a purchase price, excluding estimated closing costs of \$1,000, of \$58,000. To finance this transaction we entered into a sale leaseback agreement with Senior Housing for four of our assisted living communities (see Note A). We also entered into a \$43,500 first mortgage line of credit with Senior Housing, of which \$24,000 was drawn at closing and the balance can be drawn for future acquisitions or other business purposes. The remaining balance of the purchase price was funded with drawings under our revolving line of credit. The net amount we paid was calculated as follows:

| | | |
|---------------------------------------|----|--------|
| Purchase price of communities | \$ | 58,000 |
| Estimated closing costs | | 1,000 |
| Total property and equipment acquired | \$ | 59,000 |
| Paid by: | | |
| Available cash | \$ | 25,000 |
| Mortgage line of credit | | 24,000 |
| Revolving line of credit | | 10,000 |
| Total amount paid | \$ | 59,000 |

Adjustments for the pro forma consolidated statement of operations for the three months ended March 31, 2005 and the year ended December 31, 2004

C. Our lease with Senior Housing for the four properties subject to the sale leaseback transaction will require us to make minimum rent payments of \$2,160 per year, or \$540 for the three month period. In addition to minimum rent under this lease, beginning in 2007

we may be required to make percentage rent payments under certain circumstances relating to revenues at the communities subject to the lease with Senior Housing.

D. Represents elimination of depreciation on the four properties we sold to Senior Housing in the sale leaseback transaction. The adjustment is calculated as follows:

| | Three Months Ended March 2005 | Year Ended December 2004 |
|--|----------------------------------|-----------------------------|
| Our depreciation of the sold buildings (approximately \$19,335) using a 40-year life. | \$ (121) | \$ (483) |
| Our depreciation of the sold furniture and other fixed assets (approximately \$827) using a seven-year life. | (30) | (118) |
| Total adjustment | \$ (151) | \$ (601) |

E. Represents the amortization of the deferred gain on the four communities we sold to Senior Housing (see Note A). Deferred gain is being recognized on a straight line basis over a 16-year period, which is the term of the lease with Senior Housing. The adjustment is calculated as follows:

| | |
|--------------------------|----------|
| Deferred gain | \$ 2,064 |
| Divided by term of lease | 16 |
| Annual adjustment | \$ 129 |
| Quarterly adjustment | \$ 32 |

F. Represents the historical statement of operations of Gordon.

G. Represents the elimination of historically incurred payroll and general and administrative costs of Gordon comprising compensation and related expenses for Gordon officers and other employees whom we do not employ, rent for a corporate office lease that we did not assume and other expenses, net of our additional estimated management costs and costs under our shared services agreement. The adjustment is calculated as follows:

| | Three Months Ended March 2005 | Year Ended December 2004 |
|--|----------------------------------|-----------------------------|
| Elimination of seller's payroll from property level operating expenses | \$ (300) | \$ (1,200) |
| Elimination of seller's general and administrative expenses | \$ (144) | \$ (576) |
| Estimated management costs required by us | 113 | 450 |
| Shared services fee (represents 0.6% of pro forma revenues) | 30 | 120 |
| | \$ (1) | \$ (6) |

Total adjustment to general and administrative
expenses

F-16

H. Represents the elimination of historical depreciation and amortization expense related to Gordon. This amount is offset by depreciation that we will incur as a result of the six communities that we acquired from Gordon. The adjustment is calculated as follows:

| | Three Months Ended March 2005 | Year Ended December 2004 |
|---|--|-------------------------------------|
| Elimination of historical amounts | \$ (367) | \$ (1,479) |
| Our depreciation of the cost of the acquired buildings (estimated to be \$50,150) using a 40-year life | 313 | 1,254 |
| Our depreciation of the cost of the acquired furniture and other fixed assets (estimated to be \$2,950) using a seven-year life | 105 | 421 |
| Total adjustment | \$ 51 | \$ 196 |

I. Represents elimination of interest on debt repaid by Gordon in connection with our acquisition, offset by interest on debt we obtained to finance the acquisition. The adjustment is calculated as follows:

| | Three Months Ended March 2005 | Year Ended December 2004 |
|--|--|-------------------------------------|
| Elimination of historical amounts | \$ 825 | \$ 2,946 |
| Our interest expense on \$24,000 related to our mortgage line of credit with Senior Housing (see Note B) at an annual rate of 9.0% | (540) | (2,160) |
| Our interest expense on \$10,000 related to our revolving line of credit (see Note B) at an annual rate of 6.0% | (150) | (600) |
| Total adjustment | \$ 135 | \$ 186 |

Edgar Filing: FIVE STAR QUALITY CARE INC - Form 8-K/A

(c) *Exhibits.*

2.1 Second Amendment to Purchase and Sale Agreement, dated as of May 13, 2005, by and among Five Star, as Purchaser, and Franciscan Manor Associates, LLC, Muirfield Associates, LLC, Prestwicke Associates, LLC, Royal Aberdeen Associates, LLC, Troon Associates, LLC and Turnberry Associates, LLC, as Sellers. *(Incorporated by reference to Five Star's Current Report on Form 8-K dated June 3, 2005.)*

2.2 Third Amendment to Purchase and Sale Agreement, dated as of May 16, 2005, by and among Five Star, as Purchaser, and Franciscan Manor Associates, LLC, Muirfield Associates, LLC, Prestwicke Associates, LLC, Royal Aberdeen Associates, LLC, Troon Associates, LLC and Turnberry Associates, LLC, as Sellers. *(Incorporated by reference to Five Star's Current Report on Form 8-K dated June 3, 2005.)*

2.3 Fourth Amendment to Purchase and Sale Agreement, dated as of May 25, 2005, by and among Five Star, as Purchaser, and Franciscan Manor Associates, LLC, Muirfield Associates, LLC, Prestwicke Associates, LLC, Royal Aberdeen Associates, LLC, Troon Associates, LLC and Turnberry Associates, LLC, as Sellers. *(Incorporated by reference to Five Star's Current Report on Form 8-K dated June 3, 2005.)*

2.4 Fifth Amendment to Purchase and Sale Agreement, dated as of May 27, 2005, by and among Five Star, as Purchaser, and Franciscan Manor Associates, LLC, Muirfield Associates, LLC, Prestwicke Associates, LLC, Royal Aberdeen Associates, LLC, Troon Associates, LLC and Turnberry Associates, LLC, as Sellers. *(Incorporated by reference to Five Star's Current Report on Form 8-K dated June 3, 2005.)*

2.5 Sixth Amendment to Purchase and Sale Agreement, dated as of June 3, 2005, by and among Five Star, as Purchaser, and Franciscan Manor Associates, LLC, Muirfield Associates, LLC, Prestwicke Associates, LLC, Royal Aberdeen Associates, LLC, Troon Associates, LLC and Turnberry Associates, LLC, as Sellers. *(Incorporated by reference to Five Star's Current Report on Form 8-K dated June 3, 2005.)*

10.1 Promissory Note, dated as of June 3, 2005, made by Five Star to the order of Senior Housing. *(Incorporated by reference to Five Star's Current Report on Form 8-K dated June 3, 2005.)*

10.2 Loan Agreement, dated as of June 3, 2005, by and among Senior Housing, Five Star, Five Star Quality Care-GHV, LLC and Five Star Quality Care-MVSP, LLC. *(Incorporated by reference to Five Star's Current Report on Form 8-K dated June 3, 2005.)*

Edgar Filing: FIVE STAR QUALITY CARE INC - Form 8-K/A

10.3 Guaranty Agreement, dated as of June 3, 2005, made by Five Star Quality Care-GHV, LLC and Five Star Quality Care-MVSP, LLC in favor of Senior Housing. *(Incorporated by reference to Five Star's Current Report on Form 8-K dated June 3, 2005.)*

10.4 Purchase and Sale Agreement, dated as of June 3, 2005, by and among FSQ Crown Villa Business Trust, Morningside of Belmont, LLC, Morningside of Greenwood, L.P. and Five Star Quality Care-GA, LLC, as Sellers, and SNH CHS Properties Trust, SNH/LTA Properties Trust and SNH/LTA Properties GA LLC, as Purchasers. *(Incorporated by reference to Five Star's Current Report on Form 8-K dated June 3, 2005.)*

10.5 First Amendment to Second Amended and Restated Lease Agreement, dated as of May 17, 2005, by and among Ellicott City Land I LLC, Ellicott City Land II LLC, HRES2 Properties Trust, SNH CHS Properties Trust, SPTIHS Properties Trust, SPT-Michigan Trust, SPTMNR Properties Trust, SNH/LTA Properties Trust and SNH/LTA Properties GA LLC, as Landlord, and Five Star Quality Care Trust, as Tenant. *(Incorporated by reference to Five Star's Current Report on Form 8-K dated June 3, 2005.)*

10.6 Second Amendment to Second Amended and Restated Lease Agreement, dated as of June 3, 2005, by and among Ellicott City Land I LLC, Ellicott City Land II LLC, HRES2 Properties Trust, SNH CHS Properties Trust, SPTIHS Properties Trust, SPT-Michigan Trust, SPTMNR Properties Trust, SNH/LTA Properties Trust and SNH/LTA Properties GA LLC, as Landlord, and Five Star Quality Care Trust, as Tenant. *(Incorporated by reference to Five Star's Current Report on Form 8-K dated June 3, 2005.)*

10.7 Second Amendment to Security Agreement, dated as of May 17, 2005, by and among certain affiliates of Senior Housing, as Landlord, and Five Star Quality Care Trust, as Tenant. *(Incorporated by reference to Five Star's Current Report on Form 8-K dated June 3, 2005.)*

10.8 Amended and Restated Pledge of Shares of Beneficial Interest Agreement, dated as of May 6, 2005, made by FSQ, Inc. for the benefit of the Landlord under the Second Amended and Restated Lease Agreement, dated as of November 19, 2004, by and among certain affiliates of Senior Housing, as Landlord, and Five Star Quality Care Trust, as Tenant. *(Incorporated by reference to Five Star's Current Report on Form 8-K dated June 3, 2005.)*

10.9 Confirmation of Guarantees and Confirmation and Amendment of Other Incidental Documents, dated as of June 3, 2005, by and among Five Star, certain affiliates of Five Star and certain affiliates of Senior Housing. *(Incorporated by reference to Five Star's Current Report on Form 8-K dated June 3, 2005.)*

99.1 Press release dated June 6, 2005. (*Incorporated by reference to Five Star's Current Report on Form 8-K dated June 3, 2005.*)

[Remainder of this Page Intentionally Left Blank.]

SIGNATURES

Edgar Filing: FIVE STAR QUALITY CARE INC - Form 8-K/A

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 hereunto duly authorized.

FIVE STAR QUALITY CARE, INC.

By: /s/ Bruce J. Mackey Jr.
Name: Bruce J. Mackey Jr.
Title: Treasurer and Chief Financial
Officer

Date: July 28, 2005

