

FIVE STAR QUALITY CARE INC

Form 10-K/A

April 16, 2014

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**UNITED STATES**  
**SECURITIES AND EXCHANGE COMMISSION**

WASHINGTON, D.C. 20549

**FORM 10-K/A**

**Amendment No. 1**

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

**For the fiscal year ended December 31, 2012**

**or**

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

**Commission File Number 001-16817**

**FIVE STAR QUALITY CARE, INC.**

(Exact Name of Registrant as Specified in Its Charter)

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**Maryland**  
(State of Incorporation)

**04-3516029**  
(IRS Employer Identification No.)

**400 Centre Street, Newton, Massachusetts 02458**

(Address of Principal Executive Offices) (Zip Code)

(Registrant's Telephone Number, Including Area Code): **617-796-8387**

Securities registered pursuant to Section 12(b) of the Act:

<b>Title Of Each Class</b>	<b>Name Of Each Exchange On Which Registered</b>
Common Stock	New York Stock Exchange

Securities registered pursuant to Section 12(g) of the Act: **None**

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

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

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

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

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K.

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of large accelerated filer, accelerated filer and smaller reporting company in Rule 12b-2 of the Exchange Act. (Check one):

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Large accelerated filer

Accelerated filer

Non-accelerated filer

Smaller reporting company

(Do not check if a smaller reporting company)

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

The aggregate market value of the voting shares of common stock, \$.01 par value, or common shares, of the registrant held by non-affiliates was \$130.5 million based on the \$3.07 closing price per common share on the New York Stock Exchange on June 29, 2012. For purposes of this calculation, an aggregate of 5,407,952.1 common shares, including 4,235,000 common shares held by Senior Housing Properties Trust, or SNH, are held by the directors and officers of the registrant and SNH and have been included in the number of common shares held by affiliates.

Number of the registrant's common shares outstanding as of February 15, 2013: 48,234,022.

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*References in this Annual Report on Form 10-K to we, us or our mean Five Star Quality Care, Inc. and its consolidated subsidiaries unless the context otherwise requires.*

**WARNING CONCERNING FORWARD LOOKING STATEMENTS**

THIS ANNUAL REPORT ON FORM 10-K CONTAINS STATEMENTS THAT CONSTITUTE FORWARD LOOKING STATEMENTS WITHIN THE MEANING OF THE PRIVATE SECURITIES LITIGATION REFORM ACT OF 1995 AND OTHER SECURITIES LAWS. ALSO, WHENEVER WE USE WORDS SUCH AS BELIEVE , EXPECT , ANTICIPATE , INTEND , PLAN , ESTIMATE OR SIMILAR EXPRESSIONS, WE ARE MAKING FORWARD LOOKING STATEMENTS. THESE FORWARD LOOKING STATEMENTS ARE BASED UPON OUR PRESENT INTENT, BELIEFS OR EXPECTATIONS, BUT FORWARD LOOKING STATEMENTS ARE NOT GUARANTEED TO OCCUR AND MAY NOT OCCUR. FORWARD LOOKING STATEMENTS IN THIS REPORT RELATE TO VARIOUS ASPECTS OF OUR BUSINESS, INCLUDING:

- OUR ABILITY TO OPERATE OUR SENIOR LIVING COMMUNITIES AND REHABILITATION HOSPITALS PROFITABLY,
  
- OUR ABILITY TO COMPLY AND TO REMAIN IN COMPLIANCE WITH APPLICABLE MEDICARE, MEDICAID AND OTHER FEDERAL AND STATE REGULATORY AND RATE SETTING REQUIREMENTS,
  
- OUR ABILITY TO MEET OUR RENT AND DEBT OBLIGATIONS,
  
- OUR ABILITY TO RAISE EQUITY OR DEBT CAPITAL,
  
- OUR ABILITY TO COMPETE FOR ACQUISITIONS EFFECTIVELY,
  
- THE FUTURE AVAILABILITY OF BORROWINGS UNDER OUR CREDIT FACILITIES,
  
- OUR EXPECTATION THAT WE WILL BENEFIT FINANCIALLY BY PARTICIPATING IN AFFILIATES INSURANCE COMPANY, OR AIC, WITH REIT MANAGEMENT & RESEARCH LLC, OR RMR, AND COMPANIES TO WHICH RMR PROVIDES MANAGEMENT SERVICES, AND

- OTHER MATTERS.

OUR ACTUAL RESULTS MAY DIFFER MATERIALLY FROM THOSE CONTAINED IN OR IMPLIED BY OUR FORWARD LOOKING STATEMENTS AS A RESULT OF VARIOUS FACTORS. FACTORS THAT COULD HAVE A MATERIAL ADVERSE EFFECT ON OUR FORWARD LOOKING STATEMENTS AND UPON OUR BUSINESS, RESULTS OF OPERATIONS, FINANCIAL CONDITION, CASH FLOWS, LIQUIDITY AND PROSPECTS INCLUDE, BUT ARE NOT LIMITED TO:

- CHANGES IN MEDICARE AND MEDICAID POLICIES WHICH COULD RESULT IN REDUCED RATES OF PAYMENT,
  - THE IMPACT OF CHANGES IN THE ECONOMY AND THE CAPITAL MARKETS ON US AND OUR RESIDENTS AND OTHER CUSTOMERS,
  - COMPETITION WITHIN THE SENIOR LIVING SERVICES AND REHABILITATION HOSPITAL BUSINESSES,
  - INCREASES IN INSURANCE AND TORT LIABILITY COSTS,
  - ACTUAL AND POTENTIAL CONFLICTS OF INTEREST WITH OUR MANAGING DIRECTORS, SENIOR HOUSING PROPERTIES TRUST OR ITS SUBSIDIARIES, OR SNH, RMR, AIC AND THEIR RELATED PERSONS AND ENTITIES,
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- COMPLIANCE WITH, AND CHANGES TO FEDERAL, STATE AND LOCAL LAWS AND REGULATIONS THAT COULD AFFECT OUR SERVICES OR IMPOSE REQUIREMENTS, COSTS AND ADMINISTRATIVE BURDENS THAT MAY REDUCE OUR ABILITY TO PROFITABLY OPERATE OUR BUSINESS, AND

- ACTS OF TERRORISM, OUTBREAKS OF SO CALLED PANDEMICS OR OTHER MANMADE OR NATURAL DISASTERS BEYOND OUR CONTROL.

FOR EXAMPLE:

- THE VARIOUS GOVERNMENTS WHICH PAY US FOR THE SERVICES WE PROVIDE TO OUR RESIDENTS AND PATIENTS ARE CURRENTLY EXPERIENCING, AND ARE EXPECTED TO CONTINUE TO EXPERIENCE, BUDGETARY PRESSURES AND CONSTRAINTS AND MAY LOWER THE MEDICARE, MEDICAID AND OTHER RATES THEY PAY US. BECAUSE WE OFTEN CANNOT ETHICALLY LOWER THE QUALITY OF THE SERVICES WE PROVIDE TO MATCH THE AVAILABLE MEDICARE, MEDICAID AND OTHER RATES WE ARE PAID, WE MAY EXPERIENCE LOSSES AND SUCH LOSSES MAY BE MATERIAL,

- THIS ANNUAL REPORT ON FORM 10-K STATES THAT WE EXPECT THAT WE MAY ENTER INTO ADDITIONAL MANAGEMENT ARRANGEMENTS WITH SNH SIMILAR TO THOSE CURRENTLY IN EFFECT FOR US TO MANAGE ADDITIONAL SENIOR LIVING COMMUNITIES SNH MAY ACQUIRE IN THE FUTURE. HOWEVER, THERE CAN BE NO ASSURANCE THAT SNH WILL ACQUIRE OTHER COMMUNITIES OR THAT WE AND SNH WILL ENTER INTO ANY ADDITIONAL MANAGEMENT ARRANGEMENTS,

- OUR ABILITY TO OPERATE AND MANAGE NEW SENIOR LIVING COMMUNITIES PROFITABLY DEPENDS UPON MANY FACTORS, INCLUDING OUR ABILITY TO INTEGRATE NEW COMMUNITIES INTO OUR EXISTING OPERATIONS AND SOME FACTORS WHICH ARE BEYOND OUR CONTROL SUCH AS THE DEMAND FOR OUR SERVICES ARISING FROM ECONOMIC CONDITIONS GENERALLY. WE MAY NOT BE ABLE TO SUCCESSFULLY INTEGRATE NEW COMMUNITIES OR OPERATE AND MANAGE NEW COMMUNITIES PROFITABLY,

- THIS ANNUAL REPORT ON FORM 10-K STATES THAT AT DECEMBER 31, 2012, WE HAD \$24.6 MILLION OF CASH AND CASH EQUIVALENTS, THAT THERE WERE NO AMOUNTS OUTSTANDING UNDER OUR CREDIT FACILITIES, THAT WE HAD AN AGGREGATE OF \$184.4 MILLION AVAILABLE TO BORROW UNDER OUR CREDIT FACILITIES, AND THAT WE HAVE IN THE PAST SOLD IMPROVEMENTS TO SNH AND INTEND TO REQUEST TO SELL ADDITIONAL IMPROVEMENTS TO SNH FOR INCREASED RENT PURSUANT TO OUR LEASES WITH SNH; ALL OF WHICH MAY IMPLY THAT WE HAVE ABUNDANT CASH LIQUIDITY. HOWEVER, OUR OPERATIONS AND BUSINESS REQUIRE SIGNIFICANT AMOUNTS OF WORKING CASH AND REQUIRE US TO MAKE SIGNIFICANT CAPITAL EXPENDITURES TO MAINTAIN OUR COMPETITIVENESS. FURTHER, OUR \$35.0 MILLION CREDIT FACILITY EXPIRES IN MARCH 2013, AND WE MAY NOT SEEK, OR BE SUCCESSFUL IF WE DO, A RENEWAL OR REPLACEMENT OF THAT CREDIT FACILITY. ACCORDINGLY, WE MAY NOT HAVE SUFFICIENT CASH LIQUIDITY,

- THIS ANNUAL REPORT ON FORM 10-K STATES THAT SPECIAL COMMITTEES OF EACH OF OUR BOARD OF DIRECTORS AND SNH'S BOARD OF TRUSTEES COMPOSED SOLELY OF OUR INDEPENDENT DIRECTORS AND SNH'S INDEPENDENT TRUSTEES WHO ARE NOT ALSO DIRECTORS OR TRUSTEES OF THE OTHER PARTY AND WHO WERE REPRESENTED BY SEPARATE COUNSEL REVIEWED AND APPROVED THE TERMS OF THE MANAGEMENT AGREEMENTS AND POOLING AGREEMENTS BETWEEN US AND SNH AND THAT A SPECIAL COMMITTEE OF OUR BOARD OF DIRECTORS COMPOSED SOLELY OF OUR INDEPENDENT DIRECTORS NEGOTIATED AND APPROVED THE TERMS OF OUR HEADQUARTERS LEASE WITH RMR. AN IMPLICATION OF THESE STATEMENTS MAY BE THAT THESE TERMS ARE AS FAVORABLE TO US AS TERMS WE COULD OBTAIN FOR SIMILAR ARRANGEMENTS FROM UNRELATED THIRD PARTIES.
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HOWEVER, DESPITE THESE PROCEDURAL SAFEGUARDS, WE COULD STILL BE SUBJECTED TO CLAIMS CHALLENGING THESE TRANSACTIONS OR OUR ENTRY INTO THESE TRANSACTIONS BECAUSE OF THE MULTIPLE RELATIONSHIPS AMONG US, SNH AND RMR AND THEIR RELATED PERSONS AND ENTITIES, AND DEFENDING EVEN MERITLESS CLAIMS COULD BE EXPENSIVE AND DISTRACTING TO MANAGEMENT,

- OUR RESIDENTS AND PATIENTS WHO PAY FOR OUR SERVICES WITH THEIR PRIVATE RESOURCES MAY BECOME UNABLE TO AFFORD OUR SERVICES WHICH COULD RESULT IN DECREASED OCCUPANCY AND DECREASED REVENUES AT OUR SENIOR LIVING COMMUNITIES AND REHABILITATION HOSPITALS AND INCREASED RELIANCE ON LOWER RATES FROM GOVERNMENT AND OTHER PAYERS,

- WE INTEND TO OPERATE OUR REHABILITATION HOSPITALS PROFITABLY. HOWEVER, WE HAVE HISTORICALLY EXPERIENCED LOSSES FROM OUR REHABILITATION HOSPITALS AND WE MAY BE UNABLE TO OPERATE OUR REHABILITATION HOSPITALS PROFITABLY,

- WE MAY BE UNABLE TO REPAY OUR DEBT OBLIGATIONS WHEN THEY BECOME DUE,

- CONTINUED AVAILABILITY OF BORROWINGS UNDER OUR CREDIT FACILITIES IS SUBJECT TO OUR SATISFYING CERTAIN FINANCIAL COVENANTS AND MEETING OTHER CUSTOMARY CONDITIONS,

- THE AMOUNT OF AVAILABLE BORROWINGS UNDER OUR CREDIT FACILITIES IS SUBJECT TO OUR HAVING QUALIFIED COLLATERAL, WHICH IS PRIMARILY BASED ON THE VALUE OF OUR ACCOUNTS RECEIVABLE AND INVENTORY SECURING OUR \$35.0 MILLION CREDIT FACILITY AND THE VALUE OF THE PROPERTIES SECURING OUR \$150.0 MILLION CREDIT FACILITY. ACCORDINGLY, THE AVAILABILITY OF BORROWINGS UNDER OUR CREDIT FACILITIES AT ANY TIME MAY BE LESS THAN \$35.0 MILLION AND \$150.0 MILLION, RESPECTIVELY; FURTHER, OUR \$35.0 MILLION CREDIT FACILITY IS SCHEDULED TO EXPIRE IN MARCH 2013, AND WE MAY NOT SEEK, OR BE SUCCESSFUL IF WE DO, A RENEWAL OR REPLACEMENT OF THAT CREDIT FACILITY,

- ACTUAL COSTS UNDER OUR CREDIT FACILITIES WILL BE HIGHER THAN LIBOR PLUS A SPREAD BECAUSE OF OTHER FEES AND EXPENSES ASSOCIATED WITH OUR CREDIT FACILITIES,

- THIS ANNUAL REPORT ON FORM 10-K STATES THAT WE MAY PURCHASE ADDITIONAL OUTSTANDING PRINCIPAL AMOUNTS OF OUR CONVERTIBLE SENIOR NOTES DUE IN 2026 FROM TIME TO TIME. HOWEVER, THERE CAN BE NO ASSURANCE WE WILL DO SO,



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- THIS ANNUAL REPORT ON FORM 10-K STATES THAT OUR CASH RECEIPTS RESULTING FROM THE SALE OF OUR PHARMACY BUSINESS ARE \$34.3 MILLION, BEFORE TAXES AND TRANSACTION COSTS. HOWEVER, THE PURCHASE AGREEMENT INCLUDED CUSTOMARY INDEMNIFICATION OBLIGATIONS AND REQUIRED US TO ESCROW A PORTION OF THE PURCHASE PRICE IN CONNECTION WITH THE INDEMNIFICATION OBLIGATIONS. IF WE ARE REQUIRED TO PAY AMOUNTS (INCLUDING WITH ESCROWED PROCEEDS) TO SATISFY INDEMNIFICATION OBLIGATIONS IN THE FUTURE, THE ACTUAL CASH RECEIPTS WE MAY REALIZE FROM THIS SALE, AND ANY CORRESPONDING CAPITAL GAIN, MAY BE REDUCED,

- THIS ANNUAL REPORT ON FORM 10-K STATES THAT WE HAVE ENTERED AN AGREEMENT TO SELL TWO SNFS LOCATED IN MICHIGAN THAT WE OWN. THIS SALE IS SUBJECT TO VARIOUS TERMS AND CONDITIONS TYPICAL OF SUCH TRANSACTIONS, INCLUDING REGULATORY APPROVALS. THESE TERMS AND CONDITIONS MAY NOT BE MET. AS A RESULT, THIS TRANSACTION MAY BE DELAYED OR MAY NOT OCCUR OR ITS TERMS MAY CHANGE,

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- THIS ANNUAL REPORT ON FORM 10-K STATES THAT WE AND SNH ARE OFFERING FOR SALE AN ASSISTED LIVING COMMUNITY LOCATED IN PENNSYLVANIA THAT WE LEASE FROM SNH. WE AND SNH MAY NOT BE ABLE TO SELL THIS PROPERTY ON ACCEPTABLE TERMS OR OTHERWISE, AND

- THIS ANNUAL REPORT ON FORM 10-K STATES THAT WE BELIEVE THAT OUR CONTINUING RELATIONSHIPS WITH SNH, RMR AND AIC AND THEIR AFFILIATED AND RELATED PERSONS AND ENTITIES MAY BENEFIT US AND PROVIDE US WITH COMPETITIVE ADVANTAGES IN OPERATING AND GROWING OUR BUSINESS. IN FACT, THE ADVANTAGES WE BELIEVE WE MAY REALIZE FROM THESE RELATIONSHIPS MAY NOT MATERIALIZE.

THESE RESULTS COULD OCCUR DUE TO MANY DIFFERENT CIRCUMSTANCES, SOME OF WHICH ARE BEYOND OUR CONTROL, SUCH AS NATURAL DISASTERS, CHANGED MEDICARE AND MEDICAID RATES, NEW LEGISLATION AFFECTING OUR BUSINESS, CHANGES IN OUR REVENUES OR COSTS, OR CHANGES IN CAPITAL MARKETS OR THE ECONOMY GENERALLY.

THE INFORMATION CONTAINED ELSEWHERE IN THIS ANNUAL REPORT ON FORM 10-K OR IN OUR FILINGS WITH THE SECURITIES AND EXCHANGE COMMISSION, OR SEC, INCLUDING UNDER THE CAPTION "RISK FACTORS", OR INCORPORATED HEREIN OR THEREIN, IDENTIFIES OTHER IMPORTANT FACTORS THAT COULD CAUSE DIFFERENCES FROM OUR FORWARD LOOKING STATEMENTS. OUR FILINGS WITH THE SEC ARE AVAILABLE ON THE SEC'S WEBSITE AT WWW.SEC.GOV.

YOU SHOULD NOT PLACE UNDUE RELIANCE UPON OUR FORWARD LOOKING STATEMENTS.

EXCEPT AS REQUIRED BY LAW, WE DO NOT INTEND TO UPDATE OR CHANGE ANY FORWARD LOOKING STATEMENTS AS A RESULT OF NEW INFORMATION, FUTURE EVENTS OR OTHERWISE.

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**FIVE STAR QUALITY CARE, INC.**

**2012 ANNUAL REPORT ON FORM 10-K/A**

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**EXPLANATORY NOTE**

**(dollars in thousands)**

We are filing this Amendment No. 1 to our Annual Report on Form 10-K for the year ended December 31, 2012, or this Amended 2012 Annual Report, to amend and restate financial statements and other financial information in our Annual Report on Form 10-K for the year ended December 31, 2012, or our 2012 Annual Report, which was filed with the Securities and Exchange Commission, or the SEC, on February 19, 2013.

As more fully described in Note 18 to the Notes to our Consolidated Financial Statements included in Item 15 of this Amended 2012 Annual Report, subsequent to the filing of our 2012 Annual Report our management and the Audit Committee of our Board of Directors, or our Audit Committee, concluded that our consolidated financial statements for the years ended December 31, 2012 and 2011 contained within our 2012 Annual Report should be restated, and that those financial statements previously filed with the SEC should no longer be relied upon. We are restating our consolidated financial statements for the years ended December 31, 2012 and 2011 contained within this Amended 2012 Annual Report to correct certain errors in the accounting for income taxes and other errors. Specifically, the accounting for income tax errors relate to, among other things, the measurement of deferred tax assets for net operating losses and tax credits and the measurement of deferred tax assets and liabilities for temporary differences related to fixed assets, intangible assets and investments. In addition, as part of the restatement we have corrected certain other errors related to insurance receivables, security deposits, accrual of fixed asset additions, classification of senior living operating expenses and certain other immaterial items. The net impact of correcting the errors resulted in an increase to our shareholders' equity of \$6,749 and \$8,127 at December 31, 2012 and 2011, respectively, and a decrease to net income of \$1,404 for the year ended December 31, 2012 and an increase to net income of \$6,586 for the year ended December 31, 2011. We corrected the presentation and disclosure of our consolidated statements of cash flows to separately identify the net cash flows from discontinued operations, by category and in total. The restated financial statements include the proceeds from the sale of our pharmacy business of \$34,298 for the year ended December 31, 2012 as cash provided by investing activities of discontinued operations and reflect the correction of other errors in the separate disclosures of cash flows for continuing operations and discontinued operations. We have also corrected the footnote presentation of the classification of \$11,550 and \$11,692 of our available for sale debt securities as of December 31, 2012 and December 31, 2011, respectively, from Level 1 assets to Level 2 assets as defined in the fair value hierarchy and corrected the disclosure of the fair value of our mortgage notes payable which increased \$9,947 and \$8,956 as of December 31, 2012 and December 31, 2011, respectively.

In the second quarter of 2013, we and Senior Housing Properties Trust, or SNH, offered for sale 10 senior living communities that we lease from SNH and classified those communities as discontinued operations. Also, during the second quarter of 2013, we offered for sale one senior living community we own and classified this community as discontinued operations. In the third quarter of 2013, in connection with entering into a purchase agreement with SNH and certain unrelated parties, we reclassified our rehabilitation hospital business as discontinued operations. These 11 senior living communities and our rehabilitation hospital business are retrospectively presented as discontinued operations throughout this Amended 2012 Annual Report. Please see Note 18 to the Notes to our Consolidated Financial Statements included in Item 15 of this Amended 2012 Annual Report for more information regarding the effect of the retrospective adjustments to reflect discontinued operations and the correction of errors for the years ended December 31, 2012 and 2011.

As a result of the errors described above, we determined that our disclosure controls and procedures were not effective as of December 31, 2012, and we reassessed the effectiveness of our internal control over financial reporting and determined that we had material weaknesses in our internal controls over accounting for income taxes, that we lacked sufficient personnel with requisite technical accounting competencies and that we had an insufficient level of oversight in the financial statement close process. As a result, we concluded that our internal control over financial reporting was ineffective as of December 31, 2012.

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### *Amendments to our 2012 Annual Report included in this Amended 2012 Annual Report*

The following sections of our 2012 Annual Report are amended and being filed in their entirety in this Amended 2012 Annual Report:

- Part I, Item 1. Business;
  
- Part I, Item 1A. Risk Factors;
  
- Part I, Item 2. Properties;
  
- Part II, Item 6. Selected Financial Data;
  
- Part II, Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations;
  
- Part II, Item 9A. Controls and Procedures; and
  
- Part IV, Item 15. Exhibits and Financial Statement Schedules.

This Amended 2012 Annual Report contains only the items and exhibits to our 2012 Annual Report that are being amended and restated, and unaffected items are not included herein.

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**PART I**

**Item 1. Business**

**GENERAL**

We operate senior living communities, including independent living communities, assisted living communities and skilled nursing facilities, or SNFs. As of December 31, 2012, we operated 250 senior living communities located in 31 states containing 29,701 living units, including 219 primarily independent and assisted living communities with 26,856 living units and 31 SNFs with 2,845 living units. As of December 31, 2012, we owned and operated 30 communities (2,920 living units), we leased and operated 181 communities (20,091 living units) and we managed 39 communities (6,690 living units). Our 250 senior living communities included 10,311 independent living apartments, 14,116 assisted living suites and 5,274 skilled nursing units. We have classified as discontinued operations two SNFs and one assisted living community owned and operated by us containing 303 living units as well as seven SNFs and four assisted living communities we lease from SNH and operate containing 824 living units and have excluded such SNFs and assisted living communities from all the preceding data in this paragraph.

As of December 31, 2013, we also leased from SNH and operated two rehabilitation hospitals with 321 beds that provide inpatient rehabilitation services to patients at the two hospitals and at three satellite locations. In addition, as of that date, we leased and operated 13 outpatient clinics affiliated with these rehabilitation hospitals. We have classified the rehabilitation hospital business as discontinued operations.

We were created by SNH in April 2000 to operate 54 SNFs and two assisted living communities repossessed from former SNH tenants. As of December 31, 2012, we leased from SNH 188 senior living communities and two rehabilitation hospitals pursuant to four long term leases (including 11 senior living communities and two rehabilitation hospitals that we have classified as discontinued operations). For more information about our leases with SNH see "Our SNH Leases and Management Agreements" in Item 2 of this Amended 2012 Annual Report. We were incorporated in Delaware in April 2000 and reincorporated in Maryland in September 2001. On December 31, 2001, SNH distributed substantially all of our then outstanding shares of common stock, \$.01 par value, or our common shares, to its shareholders and we became a separate, publicly owned company listed on the American Stock Exchange (now the NYSE MKT). In February 2011, we transferred the listing of our common shares to the New York Stock Exchange, or the NYSE.

The property information included in this Amended 2012 Annual Report retrospectively reports certain properties that we have classified as discontinued operations subsequent to the filing of our 2012 Annual Report. This retrospective reporting is in accordance with accounting interpretations of the SEC that requires restated financial statements to reflect the effects of subsequent accounting matters requiring retrospective treatment that have been reflected in filings with the SEC subsequent to the original filing of the financial statements, and which subsequent filings are incorporated by reference into a registration statement. Accordingly, 11 senior living communities and our rehabilitation hospital business which we classified as discontinued operations in the second and third quarters of 2013, respectively, are retrospectively accounted for as discontinued operations throughout this Amended 2012 Annual Report.

Our principal executive offices are located at 400 Centre Street, Newton, Massachusetts 02458, and our telephone number is (617) 796-8387.

**TYPES OF PROPERTIES**

Our present business plan contemplates the ownership, leasing and management of independent living communities, assisted living communities, SNFs and rehabilitation hospitals. Some of our properties combine more than one type of service in a single building or campus.

*Independent Living Communities.* Independent living communities provide high levels of privacy to residents and require residents to be capable of relatively high degrees of independence. An independent living apartment usually bundles several services as part of a regular monthly charge. For example, the base charge may include one or two meals per day in a central dining room, weekly maid service or services of a social director. Additional services are generally available from staff employees on a fee for service basis. In some independent living communities, separate parts of the community are dedicated to assisted living or nursing services. As of December 31, 2012, our continuing operations included 10,311 independent living apartments in 86 communities that we operate.

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*Assisted Living Communities.* Assisted living communities are typically comprised of one bedroom units which include private bathrooms and efficiency kitchens. Services bundled within one charge usually include three meals per day in a central dining room, daily housekeeping, laundry, medical reminders and 24 hour availability of assistance with the activities of daily living such as dressing and bathing. Professional nursing and healthcare services are usually available at the community as requested or at regularly scheduled times. As of December 31, 2012, our continuing operations included 14,116 assisted living suites in 197 communities that we operate.

*Skilled Nursing Facilities.* SNFs generally provide extensive nursing and healthcare services similar to those available in hospitals, without the high costs associated with operating theaters, emergency rooms or intensive care units. A typical purpose built SNF generally includes one or two beds per room with a separate bathroom in each room and shared dining facilities. SNFs are staffed by licensed nursing professionals 24 hours per day. As of December 31, 2012, our continuing operations included 5,274 skilled nursing units in 72 communities that we operate.

*Rehabilitation Hospitals.* Rehabilitation hospitals, also known as inpatient rehabilitation facilities, or IRFs, provide intensive physical therapy, occupational therapy and speech language pathology services beyond the capabilities customarily available in SNFs. Patients in IRFs generally receive a minimum of three hours of daily rehabilitation services. IRFs also provide onsite pharmacy, radiology, laboratory, telemetry, hemodialysis and orthotics/prosthetics services. Outpatient satellite clinics are often included as part of the services offered by IRFs. As of December 31, 2012, our two rehabilitation hospitals had 321 beds available for inpatient services and provided rehabilitation services at the two hospitals and at three satellite locations. In addition, we operate 13 outpatient clinics affiliated with our rehabilitation hospitals where patients discharged from hospitals can continue their therapy programs and receive amputee, brain injury, neurorehabilitation, cardio-pulmonary, orthopedic, spinal cord injury, stroke and other rehabilitation services. We have classified our rehabilitation hospital business as discontinued operations.

**OUR RECENT HISTORY**

Senior Living

We have grown our business through acquisitions, through initiation of long term leases of independent and assisted living communities where residents private resources account for a large majority of revenues and through entering into long term contracts to manage independent and assisted living communities. In 2012 we began managing 17 additional communities containing 3,364 living units pursuant to long term contracts with SNH. These communities are located in 11 states throughout the United States.

Sale of Institutional Pharmacy Business

We operated five institutional pharmacies providing large quantities of drugs at locations where patients with recurring pharmacy requirements are concentrated. In September 2012, we completed the sale of our pharmacy business to Omnicare, Inc., or Omnicare. We received \$34.3 million in sale proceeds from Omnicare, which included \$3.8 million in working capital. We recorded a pre-tax capital gain on the sale of the pharmacy business of \$23.3 million. In connection with the sale, Omnicare did not acquire the real estate we owned associated with one pharmacy located in South Carolina. We intend to sell this real estate and we recorded a \$350,000 asset impairment charge in the third quarter of 2012 to reduce the carrying value of this property to its estimated fair value less costs to sell.



Debt Financings

In April 2012, we entered into a new \$150.0 million secured revolving credit facility, or our Credit Facility, that is available for general business purposes, including acquisitions, and which is in addition to our \$35.0 million revolving secured line of credit, or our Credit Agreement. The maturity date of our Credit Facility is April 13, 2015, and, subject to our payment of extension fees and meeting certain other conditions, includes options for us to extend the stated maturity date of our Credit Facility for two one-year periods. Borrowings under our Credit Facility typically bear interest at LIBOR plus a spread of 250 basis points, or 2.71% as of December 31, 2012. We may draw, repay and redraw funds until maturity, and no principal repayment is due until maturity. We are the borrower under our Credit Facility, and certain of our subsidiaries guarantee our obligations under our Credit Facility, which is secured by real estate mortgages on 15 senior living communities with 1,549 living units owned by our guarantor subsidiaries and our guarantor subsidiaries' accounts receivable and related collateral. Our Credit Facility provides for acceleration of payment of all amounts payable upon the occurrence and continuation of certain events of default, including a change of control of us. Our Credit Facility contains a number of financial and other covenants, including covenants that restrict

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our ability to incur indebtedness or to pay dividends or make other distributions under certain circumstances and require us to maintain financial ratios and a minimum net worth.

In 2006, we issued \$126.5 million principal amount of Convertible Senior Notes due 2026, or the Notes. The Notes bear interest at 3.75% per annum, payable semi-annually, and will mature on October 15, 2026. We may prepay the Notes at any time and holders of the Notes may require that we purchase all or a portion of the Notes on each of October 15, 2013, 2016 and 2021. In 2012, we purchased and retired \$12.4 million par value of the outstanding Notes and recorded a gain of \$45,000, net of related unamortized costs, on early extinguishment of debt. We funded these purchases principally with available cash. As a result of these purchases and other purchases we made in prior years, \$24.9 million in principal amount of the Notes remain outstanding.

Discontinued Operations

Under our leases with SNH, we may request SNH to sell certain noneconomic properties that we lease pursuant to those leases, which if sold, would reduce our rent payable to SNH, as determined pursuant to the lease. For more information about our leases with SNH see Our SNH Leases and Management Agreements in Item 2 of this Amended 2012 Annual Report.

During 2011, we agreed with SNH that SNH should sell one assisted living community located in Pennsylvania with 103 living units, which we lease from SNH. We and SNH are in the process of offering this assisted living community for sale and, if sold, our annual minimum rent payable to SNH will decrease by 9.0% of the net proceeds of the sale to SNH, in accordance with the terms of our lease with SNH.

In October 2012, we entered an agreement to sell two SNFs that we own that are located in Michigan with a total of 271 living units for \$8.0 million, including the assumption by the buyer of \$7.5 million of United States Department of Housing and Urban Development, or HUD, mortgage debt. In connection with this agreement, we recorded a \$294,000 asset impairment charge to reduce the carrying value of these properties to their estimated fair value less costs to sell. Completion of this sale is subject to customary closing conditions, including regulatory approvals, and we can provide no assurance that a sale of these SNFs will be completed.

In addition, 11 senior living communities, which we classified as discontinued operations in our Quarterly Report on Form 10-Q for the quarter ended June 30, 2013, and our rehabilitation hospital business, which we classified as discontinued operations during the third quarter of 2013, are retrospectively accounted for as discontinued operations throughout this Amended 2012 Annual Report.

**OUR GROWTH STRATEGY**

We believe that the aging of the U.S. population will increase demand for senior living communities. Our principal growth strategy is to profit from this anticipated demand by operating communities that provide high quality services to residents who pay with private resources.

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We seek to improve the profitability of our existing operations by increasing our revenues and improving our operating margins. We attempt to increase revenues by increasing rates and occupancies. We attempt to improve margins by limiting increases in expenses and otherwise improving operating efficiencies. For example, during the last few years, the senior living industry has generally experienced declining occupancies as a result of a slowdown in the U.S. economy. During this same period, we have improved operating margins and profitability by increasing rates and limiting increases in our expenses. To the extent that the U.S. economy and the housing market improve, we expect that our occupancies may increase and our profitability may grow; however, the condition of the U.S. economy and the housing market are beyond our control and may not improve.

In addition to managing our existing operations, we currently intend to continue to grow our business by adding to our operations primarily independent and assisted living communities we operate and manage where residents' private resources account for a large majority of revenues. We expect some of these increases may be achieved by our entering leases or management agreements and some may be achieved by our purchasing communities. Since we became a public company in late 2001, we have acquired or have begun to lease 180 primarily independent and assisted living communities; in the year ended December 31, 2012, these 180 communities realized approximately 86% of their revenues from residents' private resources, rather than from Medicare and Medicaid. Historically, we have principally expanded our operations by entering operating leases. Recently, we have started to expand our operations by acquiring

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senior living communities for our own account and entering agreements to manage senior living communities which are owned by others. In the future, we expect to continue to grow our business by adding communities that we either own, lease or manage.

**OPERATING STRUCTURE**

We have four operating divisions. Three of our divisions are each responsible for multiple regions with respect to our senior living communities that consist of independent, assisted living and skilled nursing units. One of our divisions is responsible for our rehabilitation and wellness inpatient and outpatient clinics which are associated with our senior living communities. Each division is headed by a divisional vice president with extensive experience in the senior living industry. We have several regional offices within our divisions. Each regional office is responsible for multiple communities and is headed by a regional director of operations with extensive experience in the senior living industry. Each regional office is typically supported by a clinical or wellness director, a rehabilitation services director, a regional accounts manager, a human resources specialist and a sales and marketing specialist. Regional staffs are responsible for all of our senior living community operations within a region, including:

- resident services;
  
- Medicare and Medicaid billing;
  
- marketing and sales;
  
- hiring of community personnel;
  
- compliance with applicable legal and regulatory requirements; and
  
- supporting our development and acquisition plans within their region.

Our corporate office staff, located in Massachusetts, provides services such as:

- the establishment of company wide policies and procedures relating to resident care;

- human resources policies and procedures;
- information technology;
- private pay billing for our independent living apartments and assisted living communities;
- maintenance of licensing and certification;
- legal services;
- central purchasing;
- budgeting and supervision of maintenance and capital expenditures;
- implementation of our growth strategy; and
- accounting and finance functions, including operations, budgeting, certain accounts receivable and collections functions, accounts payable, payroll and financial reporting.

As described in this Amended 2012 Annual Report, we have a business management and shared services agreement, or the business management agreement, with RMR pursuant to which RMR provides to us certain business management, administrative and information system services, including internal audit, capital markets, legal, investor relations and tax services, among other matters.

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**STAFFING**

*Independent and Assisted Living Community Staffing.* Each of the independent and assisted living communities we operate has an executive director responsible for the day to day operations of the community, including quality of care, resident services, sales and marketing, financial performance and staff supervision. The executive director is supported by department heads who oversee the care and service of the residents, a wellness director who is responsible for coordinating the services necessary to meet the healthcare needs of our residents and a marketing director who is responsible for selling our services. Other important staff includes the dining services coordinator, the activities coordinator and the property maintenance coordinator.

*Skilled Nursing Facility Staffing.* Each of our SNFs is managed by a state licensed administrator who is supported by other professional personnel, including a director of nursing, an activities director, a marketing director, a social services director, a business office manager, and physical, occupational and speech therapists. Our directors of nursing are state licensed nurses who supervise our registered nurses, licensed practical nurses and nursing assistants. Staff size and composition vary depending on the size and occupancy of each SNF and on the type of care provided by the SNF. Our SNFs also contract with physicians who provide certain medical services.

*Rehabilitation Hospital Staffing.* Each of our rehabilitation hospitals is operated under the leadership of a hospital based chief executive officer with the support of senior staff, including a medical director, chief financial officer, director of patient care services, director of rehabilitation and director of case management. The hospitals are also staffed with board certified physicians who primarily specialize in internal medicine, neurology or psychiatry, as well as other licensed professionals, including rehabilitation nurses, physical therapists, occupational therapists, speech and language pathologists, nutrition counselors, neuropsychologists and pharmacists. Each outpatient clinic associated with our rehabilitation hospitals is managed by an outpatient director who is a registered occupational or physical therapist.

**EMPLOYEES**

As of February 15, 2013, we had approximately 27,144 employees, including 17,032 full time equivalents. Approximately 84 of these employees, including approximately 55 full time equivalents, are represented under one collective bargaining agreement which expired in October 2012, but was extended until the end of February 2013 to facilitate negotiations. We believe our relations with our union and non-union employees are good.

**GOVERNMENT REGULATION AND REIMBURSEMENT**

The healthcare industry is subject to extensive and frequently changing federal, state and local laws and regulations. These laws and regulations vary by jurisdiction but may address, among other things, licensure, personnel training, staffing ratios, quality of medical care, facility requirements, government healthcare program participation, fraud and abuse, reimbursement for patient services and patient records.

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We are subject to, and our operations must comply with, these laws and regulations. From time to time, our facilities receive notices from federal, state and local agencies regarding noncompliance with such requirements. Upon receipt of these notices, we review them for correctness and, based on our review, we either take corrective action or contest the allegation of noncompliance. When corrective action is required, we work with the relevant agency to address and remediate any violations. Challenging and appealing any notices or allegations of noncompliance require the expenditure of significant legal fees and management attention. Any adverse determination concerning any of our licenses or eligibility for Medicare or Medicaid reimbursement, any penalties, repayments or sanctions, and the increasing costs of required compliance with applicable laws may adversely affect our ability to meet our financial obligations and negatively affect our financial condition and results of operations.

The healthcare industry depends significantly upon federal and state programs for revenues and, as a result, is affected by the budgetary policies of both the federal and state governments. Reimbursements under the Medicare and Medicaid programs for skilled nursing, physical therapy and rehabilitation services provide operating revenues at our rehabilitation hospitals and affiliated clinics and at some of our senior living communities (principally our SNFs). We derived approximately 24%, 26% and 26% of our consolidated revenues from continuing operations from Medicare and Medicaid programs for each of the years ended December 31, 2012, 2011 and 2010, respectively. We derived approximately 70%, 68% and 64% of our rehabilitation hospital revenues, which we have classified as discontinued operations, from Medicare and Medicaid programs for each of the years ended December 31, 2012, 2011 and 2010, respectively.

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In addition to existing government regulation, we are aware of numerous healthcare regulatory initiatives on the federal, state and local levels, which may affect our business operations if implemented.