ADCARE HEALTH SYSTEMS, INC
Form 10-K
March 30, 2016

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549
FORM 10-K

(Mark One)

ý ANNUAL REPORT UNDER SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the fiscal year ended December 31, 2015

o TRANSITION REPORT UNDER SECTION 13 OR 15(d) OF THE EXCHANGE ACT

For the transition period from to

Commission file number 001-33135

AdCare Health Systems, Inc.
(Exact name of registrant as specified in its charter)

Georgia	31-1332119
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)
1145 Hembree Road, Roswell, GA	30076-1122
(Address of principal executive offices)	(Zip Code)

Registrant's telephone number including area code (678) 869-5116

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

Title of each class	Name of each exchange on which registered
Common Stock, no par value	NYSE MKT
Preferred Stock, no par value	NYSE MKT

Securities registered under Section 12(g) of the Exchange 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 o No ý

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

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 ý 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 (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes ý No o

Indicate by check mark if disclosure of delinquent filers in response 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. o

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 definition of "large accelerated filer", "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act. (Check one):

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

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

The aggregate market value of AdCare Health Systems, Inc. common stock held by non-affiliates as of June 30, 2015, the last business day of AdCare Health Systems Inc's most recently completed second fiscal quarter, was $59,631,263. The number of shares of AdCare Health Systems, Inc., common stock, no par value, outstanding as of March 28, 2016, was 19,948,534.

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Special Note Regarding Forward Looking Statements

Certain statements in this Annual Report on Form 10-K (this "Annual Report") contain "forward-looking" information as that term is defined by the Private Securities Litigation Reform Act of 1995. Any statements that do not relate to historical or current facts or matters are forward-looking statements. Examples of forward-looking statements include all statements regarding our expected future financial position, results of operations, cash flows, liquidity, financing and refinancing plans, strategic and business plans, projected expenses and capital expenditures, competitive position, growth and acquisition opportunities, and compliance with, and changes in, governmental regulations. You can identify some of the forward-looking statements by the use of forward-looking words such as "anticipate," "believe," "plan," "estimate," "expect," "intend," "should," "may" and other similar expressions, although not all forward-looking statements contain these identifying words.

Our actual results may differ materially from those projected or contemplated by our forward-looking statements as a result of various factors, including, among others, the following:

- Our ability to achieve the benefits that we expected to achieve from our transition to a healthcare property holding and leasing company, including increased cash flow, reduced general and administrative expenses, and a lower cost of capital;
- The impact of liabilities associated with our legacy business of owning and operating healthcare properties, including pending and potential professional and general liability claims;
- Our reliance on a single tenant with respect to nine of our 35 leased healthcare properties;
- Our dependence on the operating success of our tenants and their ability to meet their obligations to us;
- The effect of increasing healthcare regulation and enforcement on our tenants, and the dependence of our tenants on reimbursement from governmental and other third-party payors;
- The impact of litigation and rising insurance costs on the business of our tenants;
- The effect of our tenants declaring bankruptcy or becoming insolvent;
- The ability and willingness of our tenants to renew their leases with us upon expiration, and our ability to reposition our properties on the same or better terms in the event of nonrenewal or if we otherwise need to replace an existing tenant;
- The significant amount of our indebtedness, our ability to service our indebtedness, covenants in our debt agreements that may restrict our ability to pay dividends or incur additional indebtedness, and our ability to refinance our indebtedness on favorable terms;
- Our ability to raise capital through equity and debt financings, and the cost of such capital;
- Increases in market interest rates;
- The availability of, and our ability to identify, suitable acquisition opportunities, and our ability to complete such acquisitions and lease the respective properties on favorable terms; and
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Other risks inherent in the real estate business, including uninsured or underinsured losses affecting our properties, the possibility of environmental compliance costs and liabilities, and the illiquidity of real estate investments.

We urge you to carefully consider these risks and review the additional disclosures we make concerning risks and other factors that may materially affect the outcome of our forward-looking statements and our future business and operating results, including those made in Part I, Item IA, “Risk Factors” in this Annual Report, as such risk factors may be amended, supplemented or superseded from time to time by other reports we file with the Securities and Exchange Commission (“SEC”), including subsequent Annual Reports on Form 10-K and Quarterly Reports on Form 10-Q. We caution you that any forward-looking statements made in this Annual Report are not guarantees of future performance, events or results, and you should not place undue reliance on these forward-looking statements, which speak only as of the date of this Annual Report. We do not intend, and we undertake no obligation, to update any forward-looking information to reflect events or circumstances after the date of this Annual Report or to reflect the occurrence of unanticipated events, unless required by law to do so.

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PART I.

Item 1. Business

Overview

AdCare Health Systems, Inc. (“AdCare”), through its subsidiaries (together, the “Company” or “we”), is a self-managed real estate investment company that invests primarily in real estate purposed for long-term care and senior living. Our business primarily consists of leasing and subleasing such facilities to third-party tenants, which operate the facilities. As of December 31, 2015, the Company owned, leased, or managed for third parties 38 facilities primarily in the Southeast. The Company's facilities provide a range of healthcare and related services to patients and residents, including skilled nursing and assisted living services, social services, various therapy services, and other rehabilitative and healthcare services for both long-term and short-stay patients and residents.

We were incorporated in Ohio on August 14, 1991, under the name Passport Retirement, Inc. In 1995, we acquired substantially all of the assets and liabilities of AdCare Health Systems, Inc. and changed our name to AdCare Health Systems, Inc. AdCare completed its initial public offering in November 2006. Initially based in Ohio, we expanded our portfolio through a series of strategic acquisitions to include properties in a number of other states, primarily in the Southeast. In 2012, we relocated our executive offices and accounting operations to Georgia, and AdCare changed its state of incorporation from Ohio to Georgia on December 12, 2013.

Historically, our business focused on owning, leasing and operating skilled nursing and assisted living facilities. The Company also managed certain facilities on behalf of unaffiliated owners and operators with whom we entered into management contracts. In July 2014, our Board of Directors (the "Board") approved a strategic plan to transition (the “Transition”) the Company to a healthcare property holding and leasing company through a series of leasing and subleasing transactions. As of December 31, 2015, we completed the Transition through: (i) leasing to third-party operators all of the healthcare properties which we own and previously operated; (ii) subleasing to third-party operators all of the healthcare properties which we lease (but does not own) and previously operated; and (iii) continuing one remaining management agreement to manage two skilled nursing facilities and one assisted living facility.

We lease our currently-owned healthcare properties, and sublease our currently-leased healthcare properties, on a triple net basis, meaning that the lessee (i.e., the new third-party operator of the property) is obligated under the lease or sublease, as applicable, for all costs of the property in respect to insurance, taxes and facility maintenance, as well as the lease or sublease payments, as applicable. These leases are generally long-term in nature with renewal options and annual rent escalation clauses.

As a result of the Transition, the Company now has many of the characteristics of a real estate investment trust ("REIT") and is focused on the ownership, acquisition and leasing of healthcare related properties. The Board is analyzing and considering: (i) whether and, if so, when, we could satisfy the requirements to qualify as a REIT under the Internal Revenue Code of 1986, as amended (the “Code”); (ii) the structural and operational complexities which would need to be addressed before we could qualify as a REIT, including the disposition of certain assets or the termination of certain operations which may not be REIT compliant; and (iii) if we were to qualify as a REIT, whether electing REIT status would be in the best interests of the Company and its shareholders in light of various factors, including our significant consolidated Federal net operating loss carryforwards of approximately $58.3 million as of December 31, 2015. There is no assurance that the Company will qualify as a REIT in future taxable years or, if it were to so qualify, that the Board would determine that electing REIT status would be in the best interests of the Company and its shareholders.

On March 29, 2016, the Company announced that given that the transition to a healthcare property holding and leasing company is complete, the Board of Directors has begun to explore strategic alternatives for the Company.

Our principal executive offices are located at 1145 Hembree Road, Roswell, GA 30076, and our telephone number is (678) 869-5116. We maintain a website at www.adcarehealth.com. The contents of this website are not incorporated into this Annual Report.

Portfolio of Healthcare Investments

As of December 31, 2015, our owned, leased, and managed portfolio consisted of 35 skilled nursing facilities, two assisted living facilities, and one independent living facility. Skilled nursing facilities provide daily nursing care, therapeutic rehabilitation, social services, housekeeping, nutrition and administrative services for individuals requiring certain assistance with activities in daily living. A typical skilled nursing facility includes mostly two bed units, each equipped with a private or shared bathroom and community dining facilities. Assisted living facilities provide personal care services, support and housing for those who need help

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with activities of daily living, such as bathing, eating and dressing, yet require limited medical care. Assisted living facilities typically are comprised of one and two bedroom suites equipped with private bathrooms and efficiency kitchens.

Our leases generally have initial terms of five to fifteen years with renewal options. The leases are "triple net leases" under which the tenant is responsible for the payment of all taxes, utilities, insurance premium costs, repairs and other charges relating to the operation of the properties. The tenant is obligated at its expense to keep all improvements, fixtures and other components of the properties covered by "all risk" insurance and to maintain specified minimal personal injury and property damage insurance, protecting us as well as the tenant. All of our leases contain annual escalators in rent payments. Leases are typically guaranteed by the parent corporation of the lessee or affiliates of the lessee. Leases are also typically backed by other collateral such as security deposits, machinery, equipment, furnishings and other personal property.

The following table provides summary information regarding the number of facilities and related beds/units by state and property type as of December 31, 2015:

	Owned		Leased		Managed for Third-Parties		Total	
	Facilities	Beds/Units	Facilities	Beds/Units	Facilities	Beds/Units	Facilities	Beds/Units
State								
Alabama	2	304	—	—	—	—	2	304
Arkansas	9	958	—	—	—	—	9	958
Georgia	4	463	10	1,168	—	—	14	1,631
North Carolina	1	106	—	—	—	—	1	106
Ohio	4	279	1	94	3	332	8	705
Oklahoma	2	197	—	—	—	—	2	197
South Carolina	2	180	—	—	—	—	2	180
Total	24	2,487	11	1,262	3	332	38	4,081
Facility Type								
Skilled Nursing	22	2,375	11	1,262	2	249	35	3,886
Assisted Living	2	112	—	—	—	—	2	112
Independent Living	—	—	—	—	1	83	1	83
Total	24	2,487	11	1,262	3	332	38	4,081

The following table provides summary information regarding the number of facilities and related beds/units by operator affiliation as of December 31, 2015:

Operator Affiliation	Number of Facilities	Beds / Units
Aria Health Group, LLC (1)	9	958
Beacon Health Management	7	585
C.R. Management	7	830
Wellington Health Services	4	641
New Beginnings Care (2)	3	252
Symmetry Healthcare	3	286
Southwest LTC	2	197
Subtotal	35	3,749
AdCare Managed	3	332
Total	38	4,081

(1) AdCare subleased through its subsidiaries nine facilities located in Arkansas to affiliates of Aria Health Group, LLC pursuant to separate sublease agreements. Eight of the Aria subleases commenced on May 1, 2015 and one

sublease commenced on November 1, 2015. Effective February 3, 2016, each sublease was terminated due to the failure to pay rent pursuant to the terms of such sublease. Subsequently, on February 5, 2016, the Company entered into a Master Lease Agreement, as amended,

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with Skyline Healthcare LLC to lease the facilities commencing April 1, 2016. (See Part II, Item 8, Financial Statements and Supplemental Data, Note 19, Subsequent Events)

(2) On January 22, 2016, New Beginnings Care LLC and its affiliates ("New Beginnings") filed a petition to reorganize its finances under the Bankruptcy Code. To date, New Beginnings has neither affirmed nor rejected the Master Lease entered into on November 3, 2015 with respect to the Jeffersonville, Oceanside, and Savannah Beach facilities. The Company is in discussions with New Beginnings and other potential operators about leasing such facilities.

Acquisitions, Dispositions, and Leasing Transactions

Acquisitions. The Company did not complete any acquisitions during the three years ended December 31, 2015.

Dispositions. On July 1, 2015, the Company sold its Bentonville Manor Nursing Home, an 83-bed skilled nursing facility located in Bentonville, Arkansas, for approximately $3.4 million. Net proceeds were used to repay certain mortgage indebtedness with respect to the facility.

On October 30, 2015, the Company sold its Companions Specialized Care Center, a 102-bed skilled nursing facility located in Tulsa, Oklahoma, for approximately $3.5 million. Net proceeds were used to repay certain mortgage indebtedness with respect to the facility.

On November 20, 2015, Riverchase Village ADK, LLC (“Riverchase”) completed the sale to an unrelated third party of the Riverchase Village facility, a 105-unit assisted living facility located in Hoover, Alabama, for a purchase price of $6.9 million. Until the sale of the Riverchase Village facility, Riverchase was a consolidating variable interest entity (a “VIE”) of the Company. Riverchase was owned by Christopher F. Brogdon, a former director of the Company and a greater than 5% beneficial holder of the Company’s common stock. Riverchase financed its acquisition of the Riverchase Village facility using the proceeds of revenue bonds issued by the Medical Clinic Board of the City of Hoover (the “Riverchase Bonds”), as to which the Company was a guarantor. In connection with the sale of the Riverchase Village facility, the Riverchase Bonds were repaid in full and AdCare was released from its guaranty.

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Leasing Transactions. During the three years ended December 31, 2015, the Company leased or subleased, as applicable, to tenants:

Facility Name	State	Owned / Leased	Disposition Type	Operations Disposition Date
2014				
Thomasville	GA	Leased	Sublease	7/1/2014
Red Rose	MO	Leased	Termination of Lease	9/30/2014
Southland	GA	Owned	Lease	11/1/2014
Lumber City	GA	Leased	Sublease	11/1/2014
Coosa Valley	AL	Owned	Lease	12/1/2014
Attalla	AL	Owned	Lease	12/1/2014
2015				
College Park	GA	Owned	Lease	4/1/2015
LaGrange	GA	Leased	Sublease	4/1/2015
Sumter Valley	SC	Owned	Lease	4/1/2015
Georgetown	SC	Owned	Lease	4/1/2015
Powder Springs	GA	Leased	Sublease	4/1/2015
Tara	GA	Leased	Sublease	4/1/2015
Heritage Park	AR	Owned	Lease	5/1/2015
Homestead Manor	AR	Owned	Lease	5/1/2015
Stone County SNF	AR	Owned	Lease	5/1/2015
Stone County ALF	AR	Owned	Lease	5/1/2015
Northridge	AR	Owned	Lease	5/1/2015
West Markham	AR	Owned	Lease	5/1/2015
Woodland Hills	AR	Owned	Lease	5/1/2015
Cumberland	AR	Owned	Lease	5/1/2015
Mountain Trace	NC	Owned	Lease	6/1/2015
Glenvue	GA	Owned	Lease	7/1/2015
Hearth & Care of Greenfield	OH	Owned	Lease	8/1/2015
The Pavilion Care Center	OH	Owned	Lease	8/1/2015
Eaglewood ALF	OH	Owned	Lease	8/1/2015
Eaglewood Care Center	OH	Owned	Lease	8/1/2015
Covington Care Center	OH	Leased	Sublease	8/1/2015
Bonterra	GA	Leased	Sublease	9/1/2015
Parkview	GA	Leased	Sublease	9/1/2015
Autumn Breeze	GA	Owned	Lease	9/30/2015
River Valley	AR	Owned	Lease	11/1/2015
Quail Creek	OK	Owned	Lease	12/31/2015
Northwest	OK	Owned	Lease	12/31/2015

Industry Trends

The skilled nursing segment of the long-term care industry has evolved to meet the growing demand for post-acute and custodial healthcare services generated by an aging population, increasing life expectancies and the trend toward shifting of patient care to lower cost settings. The growth of the senior population in the United States continues to increase healthcare costs, often faster than the available funding from government-sponsored healthcare programs. In response, federal and state governments have adopted cost-containment measures that encourage the treatment of patients in more cost-effective settings, such as skilled nursing facilities, for which the staffing requirements and associated costs are often significantly lower than acute care hospitals, inpatient rehabilitation facilities and other post-acute care settings. As a result, skilled nursing facilities are generally serving a larger population of higher acuity patients than in the past. The skilled nursing industry is large, highly fragmented, and characterized

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predominantly by numerous local and regional providers. Based on a decrease in the number of skilled nursing facilities over the past few years, we expect that the supply and demand balance in the skilled nursing industry will continue to improve. We also anticipate that, as life expectancy continues to increase in the United States, the overall demand for skilled nursing services will increase. At present, the primary market demographic for skilled nursing services is primarily individuals age 75 and older. According to the 2010 U.S. Census, there were over 40 million people in the United States in 2010 that are over 65 years old. The 2010 U.S. Census estimates this group is one of the fastest growing segments of the United States population and is expected to more than double between 2000 and 2030. We believe the skilled nursing industry has been and will continue to be impacted by several other trends. The use of long-term care insurance is increasing among seniors as a means of planning for the costs of skilled nursing services. In addition, as a result of increased mobility in society, reduction of average family size, and the increased number of two-wage earner couples, more seniors are looking for alternatives outside their own family for their care.

Competitive Strengths

We believe we possess the following competitive strengths:

Long-Term, Triple-Net Lease Structure. All of our real estate properties are leased under triple-net operating leases with initial terms ranging from five to fifteen years pursuant to which the tenants are responsible for all facility maintenance, insurance and taxes, and utilities. As of December 31, 2015, the leases had an average remaining initial term of approximately 10 years. In addition, the average rent escalator is approximately 2.5%. We also typically receive additional security under these leases in the form of security deposits from the lessee and guarantees from the parent of the lessee or other related entities.

Operator Diversification. As of December 31, 2015, our portfolio of 38 properties (including three facilities that are managed by us) was operated by seven operators or their affiliates. Each of our tenants operate between two and nine of our facilities, with our most significant tenant, Aria Health Group LLC, operating nine facilities, or 24% of the total number of our facilities. Tenants are typically local or regionally-focused operators. We believe that our tenant diversification should limit the effect of any operator’s financial or operating performance decline on our overall performance.

Geographically Diverse Property Portfolio. Our portfolio of 38 properties, comprising 4,081 beds/units, is diversified across seven states. Our properties in any one state did not account for more than 40% of our total beds/units as of December 31, 2015. We believe this geographic diversification will limit the effect of a decline in any one regional market on our overall performance.

Experienced Management Team. Our management team has extensive healthcare services, real estate, acquisitions, and capital raising experience. William McBride, III, our Chairman and Chief Executive Officer has more than 30 years of healthcare, financing, real estate and corporate leadership experience in both the long-term care and REIT sectors. Allan J. Rimland, our President and Chief Financial Officer has more than 25 years of experience in investment banking and expertise within the healthcare services and related real estate sectors, including positions with leading bulge bracket and mid-sized investment banks. Through years of public company experience, our management team also has extensive experience accessing both debt and equity capital markets to fund growth.

Business Strategy

Our business strategy primarily is focused on investing capital in our current portfolio and growing our portfolio through the acquisition of skilled nursing and other healthcare facilities. More specifically, we seek to:

Focus on Senior Housing Segment. We intend to continue to focus our investment program on senior housing, primarily the skilled nursing facility segment of the long-term care continuum. We have historically been focused on

senior housing, and senior management has operating and financial experience and a significant number of relationships in the long-term care industry. In addition, we believe investing in the sector bests meets our investing criteria.

Invest Capital in Our Current Portfolio. We intend to continue to support our operators by providing capital to them for a variety of purposes, including facility modernization and potentially replacing or renovating facilities in our portfolio that may have become less competitive. We expect to structure these investments as either lease amendments that produce additional rent or as loans that are repaid by operators during the applicable lease term.

Provide Capital to Underserved Operators. We believe that there is a significant opportunity to be a capital source to long-term care operators through the acquisition and leasing of healthcare properties that are consistent with our investment and financing strategy, but that, due to size and other considerations, are not a focus for large healthcare REITs. We seek primarily small to mid-size acquisition transactions with a focus on individual facilities with existing operators, as well as small groups of facilities and

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larger portfolios. In addition to pursuing acquisitions using triple-net lease structures, we may pursue other forms of investment, including mortgage loans and joint ventures.

Identify Talented Operators. As a result of our management team's operating experience, network of relationships and industry insight, we have been able and expect to continue to be able to identify qualified tenants. We seek tenants who possess local market knowledge, demonstrate hands-on management, have proven track records and focus on patient care.

Monitor Investments. We monitor our real estate investments through, among other things: (i) reviewing and evaluating tenant financial statements to assess operational and financial trends and performance; (ii) reviewing the state surveys, occupancy rates and patient payor mix of our facilities; (iii) verifying the payments of property and other taxes and insurance with respect to our facilities; and (iv) conducting periodic physical inspections of our facilities. For tenants or facilities that do not meet performance expectations, we may seek to work with our tenants to ensure our mutual success or seek to re-lease facilities to stronger operators.

Competition

We generally compete for real property investments with publicly traded, private and non-listed healthcare REITs, real estate partnerships, healthcare providers, healthcare lenders and other investors, including developers, banks, insurance companies, pension funds, government-sponsored entities and private equity firms, some of whom may have greater financial resources and lower costs of capital than we do. Increased competition challenges our ability to identify and successfully capitalize on opportunities that meet our investment criteria, which is affected by, among other factors, the availability of suitable acquisition or investment targets, our ability to negotiate acceptable transaction terms and our access to and cost of capital.

Our ability to generate rental revenues from our properties also depends on the competition faced by our tenants. Our tenants compete on a local and regional basis with other healthcare operating companies that provide comparable services. Our tenants compete to attract and retain patients and residents based on scope and quality of care, reputation and financial condition, price, location and physical appearance of the properties, services offered, qualified personnel, physician referrals and family preferences. The ability of our tenants to compete successfully could be affected by private, federal and state reimbursement programs and other laws and regulations.

Revenue Sources and Recognition

Triple-Net Leased Properties. Our triple-net leases provide for periodic and determinable increases in rent. We recognize rental revenues under these leases on a straight-line basis over the applicable lease term when collectibility is reasonably assured. Recognizing rental income on a straight-line basis generally results in recognized revenues during the first half of a lease term exceeding the cash amounts contractually due from our tenants, creating a straight-line rent receivable that is included in other assets on our consolidated balance sheets.

Other. We recognize management fee revenues received currently under one contractual agreement with a third party. Further, we recognize interest income from lease inducements receivables and capital loans as made to tenants.

Allowances. We assess the collectibility of our rent receivables, including straight-line rent receivables. We base our assessment of the collectibility of rent receivables (other than straight-line rent receivables) on several factors, including, payment history, the financial strength of the tenant and any guarantors, the value of the underlying collateral, and current economic conditions. If our evaluation of these factors indicates it is probable that we will be unable to recover the full value of the receivable, then we provide a reserve against the portion of the receivable that we estimate may not be recovered. If our evaluation of these factors indicates it is probable that we will be unable to receive the rent payments, then we provide a reserve against the recognized straight-line rent receivable asset for the portion that we estimate may not be recovered. If we change our assumptions or estimates regarding the collectibility of future rent payments required by a lease, then we may adjust our reserve to increase or reduce the rental revenue recognized in the period we make such change in our assumptions or estimates.

At December 31, 2015, we allowed for approximately $12.5 million on approximately $20.9 million of gross patient care related receivables. Allowance for patient care receivables are estimated based on an aged bucket method incorporating different payor types. All patient care receivables exceeding 365 days are fully allowed at December 31, 2015. The increase in the reserves for patient care is primarily included in discontinued operations.

Government Regulation

Healthcare Regulation. Our tenants are typically subject to extensive and complex federal, state and local laws and regulations relating to quality of care, licensure and certificate of need ("CON"), government reimbursement, fraud and abuse practices, qualifications of personnel, adequacy of plant and equipment, data privacy and security, and other laws and regulations governing

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the operation of healthcare facilities. We expect that the healthcare industry will, in general, continue to face increased regulation and pressure in these areas. The applicable rules are wide-ranging and can subject our tenants to civil, criminal, and administrative sanctions, including: the possible loss of accreditation or license; denial of reimbursement; imposition of fines; suspension, decertification, or exclusion from federal and state healthcare programs; or facility closure. Changes in laws or regulations, reimbursement policies, enforcement activity and regulatory non-compliance by tenants, operators and managers can all have a significant effect on their operations and financial condition, which in turn may adversely impact us, as detailed below and set forth under “Risk Factors” in Part I, Item 1A of this Annual Report.

Although the properties within our portfolio may be subject to varying levels of governmental scrutiny, we expect that the healthcare industry, in general, will continue to face increased regulation and pressure in the areas of fraud, waste and abuse, including, but not limited to, the Federal Anti-Kickback Statute, the Federal Stark Law, the Federal False Claims Act, and comparable state counterparts, as well as cost control, healthcare management and provision of services, among others. We also expect that efforts by third-party payors, such as the federal Medicare program, state Medicaid programs and private insurance carriers (including health maintenance organizations and other health plans), to impose greater discounts and more stringent cost controls upon tenants (through changes in reimbursement rates and methodologies, discounted fee structures, the assumption by healthcare providers of all or a portion of the financial risk or otherwise) will intensify and continue. A significant expansion of applicable federal, state or local laws and regulations, existing or future healthcare reform measures, new interpretations of existing laws and regulations, changes in enforcement priorities, or significant limits on the scope of services reimbursed or reductions in reimbursement rates could have a material adverse effect on certain of our tenants’ liquidity, financial condition and results of operations and, in turn, their ability to satisfy their contractual obligations, including making rental payments under and otherwise complying with the terms of our leases.

Licensure, Certification and CONs. In general, the operators of our skilled nursing facilities must be licensed and periodically certified through various regulatory agencies that determine compliance with federal, state and local laws to participate in the Medicare and Medicaid programs. Legal requirements pertaining to such licensure and certification relate to the quality of medical care provided by the operator, qualifications of the tenant’s administrative personnel and clinical staff, adequacy of the physical plant and equipment and continuing compliance with applicable laws and regulations. A loss of licensure or certification could adversely affect a skilled nursing facility’s ability to receive payments from the Medicare and Medicaid programs, which, in turn, could adversely affect its ability to satisfy its obligations to us.

In addition, many of our skilled nursing facilities are subject to state CON laws that require governmental approval prior to the development or expansion of healthcare facilities and services. The approval process in these states generally requires a facility to demonstrate the need for additional or expanded healthcare facilities or services. CONs, where applicable, are also sometimes necessary for changes in ownership or control of licensed facilities, addition of beds, investment in major capital equipment, introduction of new services or termination of services previously approved through the CON process. CON laws and regulations may restrict a tenant's ability to expand our properties and grow its business in certain circumstances, which could have an adverse effect on the tenant’s revenues and, in turn, its ability to make rental payments under and otherwise comply with the terms of our leases. In addition, CON laws may constrain the ability of an operator to transfer responsibility for operating a particular facility to a new operator. If we have to replace a property operator who is excluded from participating in a federal or state healthcare program (as discussed below), our ability to replace the operator may be affected by a particular state’s CON laws, regulations, and applicable guidance governing changes in provider control.

Compared to skilled nursing facilities, seniors housing communities (other than those that receive Medicaid payments) do not receive significant funding from governmental healthcare programs and are subject to relatively few, if any, federal regulations. Instead, to the extent they are regulated, such regulation consists primarily of state and local laws

governing licensure, provision of services, staffing requirements and other operational matters, which vary greatly from one jurisdiction to another. Although recent growth in the U.S. seniors housing industry has attracted the attention of various federal agencies that believe more federal regulation of these properties is necessary, Congress thus far has deferred to state regulation of seniors housing communities. However, as a result of this growth and increased federal scrutiny, some states have revised and strengthened their regulation of seniors housing communities, and more states are expected to do the same in the future.

Fraud and Abuse Enforcement, Other Related Laws, Initiatives, and Considerations. Long-term/post-acute care facilities (and seniors housing facilities that receive Medicaid payments) are subject to federal, state, and local laws, regulations, and applicable guidance that govern the operations and financial and other arrangements that may be entered into by healthcare providers. Certain of these laws prohibit direct or indirect payments of any kind for the purpose of inducing or encouraging the referral of patients for medical products or services reimbursable by government healthcare programs. Other laws require providers to furnish only medically necessary services and submit to the government valid and accurate statements for each service. Still other laws require providers to comply with a variety of safety, health and other requirements relating to the condition of the licensed property and the quality of care provided. Sanctions for violations of these laws, regulations, and other applicable guidance may include, but

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are not limited to, criminal and/or civil penalties and fines, loss of licensure, immediate termination of government payments, and exclusion from any government healthcare program. In certain circumstances, violation of these rules (such as those prohibiting abusive and fraudulent behavior) with respect to one property may subject other facilities under common control or ownership to sanctions, including exclusion from participation in the Medicare and Medicaid programs, as well as other government healthcare programs. In the ordinary course of its business, a property operator is regularly subjected to inquiries, investigations, and audits by the federal and state agencies that oversee these laws and regulations.

Long-term/post-acute care facilities (and seniors housing facilities that receive Medicaid payments) are also subject to the Federal Anti-Kickback Statute, which generally prohibits persons from offering, providing, soliciting, or receiving remuneration to induce either the referral of an individual or the furnishing of a good or service for which payment may be made under a federal healthcare program, such as Medicare or Medicaid. Long-term/post-acute care facilities are also subject to the Federal Ethics in Patient Referral Act of 1989, commonly referred to as the Stark Law. The Stark Law generally prohibits the submission of claims to Medicare for payment if the claim results from a physician referral for certain designated services and the physician has a financial relationship with the health service provider that does not qualify under one of the exceptions for a financial relationship under the Stark Law. Similar prohibitions on physician self-referrals and submission of claims apply to state Medicaid programs. Further, long-term/post-acute care facilities (and seniors housing facilities that receive Medicaid payments), are subject to substantial financial penalties under the Civil Monetary Penalties Act and the Federal False Claims Act and, in particular, actions under the Federal False Claims Act's "whistleblower" provisions. Private enforcement of healthcare fraud has increased due in large part to amendments to the Federal False Claims Act that encourage private individuals to sue on behalf of the government. These whistleblower suits brought by private individuals, known as qui tam actions, may be filed by almost anyone, including present and former patients, nurses and other employees, and competitors. Significantly, if a claim is successfully adjudicated, the Federal False Claims Act provides for treble damages and a civil penalty of up to $11,000 per claim.

Prosecutions, investigations, or whistleblower actions could have a material adverse effect on a property operator's liquidity, financial condition, and operations, which could adversely affect the ability of the operator to meet its financial obligations to us. Finally, various state false claim act and anti-kickback laws may also apply to each property operator. Violation of any of the foregoing statutes can result in criminal and/or civil penalties that could have a material adverse effect on the ability of an operator to meet its financial obligations to us.

Other legislative developments, including the Health Insurance Portability and Accountability Act of 1996 ("HIPAA"), have greatly expanded the definition of healthcare fraud and related offenses and broadened its scope to include private healthcare plans in addition to government payors. Congress also has greatly increased funding for the Department of Justice, Federal Bureau of Investigation and the Office of the Inspector General ("OIG") of the Department of Health and Human Services ("HHS") to audit, investigate and prosecute suspected healthcare fraud. Moreover, a significant portion of the billions in healthcare fraud recoveries over the past several years has also been returned to government agencies to further fund their fraud investigation and prosecution efforts.

Additionally, other HIPAA provisions and regulations provide for communication of health information through standard electronic transaction formats and for the privacy and security of health information. In order to comply with the regulations, healthcare providers often must undertake significant operational and technical implementation efforts. Operators also may face significant financial exposure if they fail to maintain the privacy and security of medical records and other personal health information about individuals. The Health Information Technology for Economic and Clinical Health ("HITECH") Act, passed in February 2009, strengthened the HHS Secretary's authority to impose civil money penalties for HIPAA violations occurring after February 18, 2009. HITECH directs the HHS Secretary to provide for periodic audits to ensure covered entities and their business associates (as that term is defined under HIPAA) comply with the applicable HITECH requirements, increasing the likelihood that a HIPAA violation

will result in an enforcement action. The Centers for Medicare and Medicaid Services ("CMS") issued an interim Final Rule which conformed HIPAA enforcement regulations to HITECH, increasing the maximum penalty for multiple violations of a single requirement or prohibition to $1.5 million. Higher penalties may accrue for violations of multiple requirements or prohibitions. Additionally, on January 17, 2013, CMS released an omnibus final rule, which expands the applicability of HIPAA and HITECH and strengthens the government’s ability to enforce these laws. The final rule broadens the definition of “business associate” and provides for civil money penalty liability against covered entities and business associates for the acts of their agents regardless of whether a business associate agreement is in place. This rule also modified the standard for when a breach of unsecured personally identifiable health information must be reported. Some covered entities have entered into settlement agreements with HHS for allegedly failing to adopt policies and procedures sufficient to implement the breach notification provisions in the HITECH Act. Additionally, the final rule adopts certain changes to the HIPAA enforcement regulations to incorporate the increased and tiered civil monetary penalty structure provided by HITECH, and makes business associates of covered entities directly liable under HIPAA for compliance with certain of the HIPAA privacy standards and HIPAA security standards. HIPAA violations are also potentially subject to criminal penalties.

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There has been increased federal and state HIPAA privacy and security enforcement efforts and we expect this trend to continue. Under HITECH, state attorneys general have the right to prosecute HIPAA violations committed against residents of their states. Several such actions have already been brought against both covered entities and a business associate, and continued enforcement actions are likely to occur in the future. In addition, HITECH mandates that the Secretary of HHS conduct periodic compliance audits of HIPAA covered entities and business associates. It also tasks HHS with establishing a methodology whereby individuals who are harmed by HIPAA violations may receive a percentage of the civil monetary penalty fine or monetary settlement paid by the violator.

In addition to HIPAA, numerous other state and federal laws govern the collection, dissemination, use, access to and confidentiality of individually identifiable health information. In addition, some states are considering new laws and regulations that further protect the confidentiality, privacy or security of medical records or other types of medical or personal information. These laws may be similar to or even more stringent than the federal provisions and are not preempted by HIPAA. Not only may some of these state laws impose fines and penalties upon violators, but some afford private rights of action to individuals who believe their personal information has been misused.

Most recently with respect to HIPAA, in September, 2015, OIG issued two reports calling for better privacy oversight of covered entities by the CMS Office for Civil Rights ("OCR"). The first report, titled “OCR Should Strengthen its Oversight of Covered Entities’ Compliance with the HIPAA Privacy Standards,” found that OCR’s oversight is primarily reactive, as OCR has not fully implemented the required audit program to proactively assess possible noncompliance from covered entities. OIG recommended, among other things, that OCR fully implement a permanent audit program and develop a policy requiring OCR staff to check whether covered entities had previously been investigated for noncompliance. The second report, titled “OCR Should Strengthen its Follow-up of Breaches of Patient Information Reported by Covered Entities,” found that (1) OCR did not record corrective action information for 23% of closed “large-breach” cases in which it made determinations of noncompliance, and (2) OCR did not record “small-breach” information in its case-tracking system, which limits its ability to track and identify covered entities with multiple small breaches. OIG recommended, among other things, that OCR enter small-breach information into its case-tracking system and maintain complete documentation of corrective actions taken. OCR agreed with OIG’s recommendations in both reports. If followed, these reports and recommendations may impact our tenants.

Congress has significantly increased funding to the governmental agencies charged with enforcing the healthcare fraud and abuse laws to facilitate increased audits, investigations and prosecutions of providers suspected of healthcare fraud. As a result, government investigations and enforcement actions brought against healthcare providers have increased significantly in recent years and are expected to continue. A violation of federal or state anti-fraud and abuse laws or regulations, or other related laws or regulations discussed above, by a tenant of our properties could have a material adverse effect on the tenant’s liquidity, financial condition or results of operations, which could adversely affect its ability to satisfy its contractual obligations, including making rental payments under and otherwise complying with the terms of our leases.

Government Reimbursement

The majority of skilled nursing facilities' reimbursement is through Medicare and Medicaid. These programs are often their largest source of funding. Senior housing communities generally do not receive funding from Medicare or Medicaid, but their ability to retain their residents is impacted by policy decisions and initiatives established by the administrators of Medicare and Medicaid. In March 2010, President Obama signed into law the Patient Protection and Affordable Care Act and the Health Care and Education Reconciliation Act of 2010 , which represents significant changes to the current U.S. healthcare system (collectively the “Healthcare Reform Law”). The passage of the Healthcare Reform Law allowed formerly uninsured Americans to acquire coverage and utilize additional healthcare services. In addition, the Healthcare Reform Law gave the CMS new authorities to implement Medicaid waiver and pilot programs that impact healthcare and long term custodial care reimbursement by Medicare and Medicaid. These

activities promote “aging in place”, allowing senior citizens to stay longer in seniors housing communities, and diverting or delaying their admission into skilled nursing facilities. The potential risks that accompany these regulatory and market changes are discussed below.

- Enabled by the Medicare Modernization Act (2003) and subsequent laws, Medicare and Medicaid have implemented pilot programs (officially termed demonstrations or models) to “divert” elderly from skilled nursing facilitates and promote “aging in place” in “the least restrictive environment.” Several states have implemented Home and Community-based Medicaid waiver programs that increase the support services available to senior citizens in senior housing, lengthening the time that many seniors can live outside of a skilled nursing facility. These Medicaid waiver programs are subject to re-approval and pilots are time-limited. Roll-back or expiration of these programs could have an adverse effect on the senior housing market.

- Changes in certification and participation requirements of the Medicare and Medicaid programs have restricted, and are likely to continue to restrict further, eligibility for reimbursement under those programs. On July 16, 2015, CMS issued a proposed

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rule that, for the first time in nearly 25 years, would comprehensively update the skilled nursing facility ("SNF") requirements for participation under Medicare and Medicaid. Among other things, the proposed rule addresses requirements relating to quality of care and quality of life, facility responsibilities and staffing considerations, resident assessments, and compliance and ethics programs. We cannot accurately predict the effect the final rule will have on our tenants' business once it is promulgated. Failure to obtain and maintain Medicare and Medicaid certification by our tenants would result in denial of Medicare and Medicaid payments which would likely result in a significant loss of revenue. In addition, private payors, including managed care payors, increasingly are demanding that providers accept discounted payments resulting in lost revenue for specific patients. Efforts to impose reduced payments, greater discounts and more stringent cost controls by government and other payors are expected to continue. Any reforms that significantly limit rates of reimbursement under the Medicare and Medicaid programs could have a material adverse effect on our tenants' profitability and cash flows which, in turn, could adversely affect their ability to satisfy their obligations to us. We are unable to predict what reform proposals or reimbursement limitations will be adopted in the future or the effect such changes will have on our tenants' operations. No assurance can be given that such reforms will not have a material adverse effect on our tenants or on their ability to fulfil their obligations to us.

- As a result of the Healthcare Reform Law, and specifically Medicaid expansion and establishment of Health Insurance Exchanges providing subsidized health insurance, an estimated seventeen million more Americans have health insurance. These newly-insured Americans utilize services delivered by providers at medical buildings and other healthcare facilities. The Healthcare Reform Law remains controversial and continued attempts to repeal or reverse aspects of the law could result in insured individuals losing coverage, and consequently foregoing services offered by provider tenants in medical buildings and other healthcare facilities. On June 28, 2012, the United States Supreme Court upheld the individual mandate of the Health Reform Laws but partially invalidated the expansion of Medicaid. The ruling on Medicaid expansion will allow states not to participate in the expansion - and to forego funding for the Medicaid expansion - without losing their existing Medicaid funding. Given that the federal government substantially funds the Medicaid expansion, it is unclear how many states will ultimately pursue this option. The participation by states in the Medicaid expansion could have the dual effect of increasing our tenants' revenues, through new patients, but could also further strain state budgets. While the federal government will pay for approximately 100% of those additional costs from 2014 to 2016, states will be expected to pay for part of those additional costs beginning in 2017. We cannot predict whether other current or future efforts to repeal or amend the Healthcare Reform Laws will be successful, nor can we predict the impact that such a repeal or amendment would have on our operators or tenants and their ability to meet their obligations to us. We cannot predict whether the existing Healthcare Reform Laws, or future healthcare reform legislation or regulatory changes, will have a material impact on our operators' or tenants' property or business. If the operations, cash flows or financial condition of our operators and tenants are materially adversely impacted by the Healthcare Reform Laws or future legislation, our revenue and operations may be adversely affected as well.

- The CMS is currently in the midst of transitioning Medicare from a traditional fee for service reimbursement model to capitated, value-based, and bundled payment approaches in which the government pays a set amount for each beneficiary for a defined period of time, based on that person's underlying medical needs, rather than the actual services provided. The result is increasing use of management tools to oversee individual providers and coordinate their services. This puts downward pressure on the number and expense of services provided. Roughly eight million Medicare beneficiaries now receive care via Accountable Care Organizations, and Medicare Advantage health plans now provide care for roughly seventeen million Medicare beneficiaries. The continued trend toward capitated, value based, and bundled payment approaches has the potential to diminish the market for certain healthcare providers. In addition, on April 1, 2014, the Protecting Access to Medicare Act of 2014 ("Access to Medicare Act") was enacted. The Access to Medicare Act implements value-based purchasing for SNFs. Beginning in fiscal year 2019, 2% of SNF payments will be withheld and approximately 50% to 70% of the amount withheld will be paid to SNFs through value-based payments. SNFs began reporting the claims-based 30-Day All-Cause Readmission Measure on October

1, 2015 and will begin reporting a resource use measure by October 1, 2016. Both measures will be publicly available by October 1, 2017.

- In October 2015, the U.S. Government Accountability Office ("GAO") released a report recommending that CMS continue to improve data and oversight of nursing home quality measures. The GAO found that although CMS collects several types of data that give some insight into the quality of nursing homes, the data could provide a clearer picture of nursing home quality if some underlying problems with the data (i.e., the use of self-reported data and non-standardized survey methodologies) are corrected. The GAO recommends, among other things, that CMS implement a clear plan for ongoing auditing of self-reported data and establish a process for monitoring oversight modifications to better assess their effects. According to the GAO, timely completion of these actions is particularly important because Medicare payments to nursing homes will be dependent on quality data, through the implementation of the value based purchasing program, starting in fiscal year 2019. HHS agreed with the GAO's recommendations, and to the extent such recommendations are implemented, they could impact our operators and tenants.

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- The majority of Medicare payments continue to be made through traditional Medicare Part A and Part B fee-for-service schedules. The Medicare and CHIP ("Children's Health Insurance Program") Reauthorization Act of 2015 (“MACRA”) addresses the risk of a Sustainable Growth Rate cut in Medicare payments for physician services. However, other annual Medicare payment regulations, particularly with respect to certain hospitals, skilled nursing care, and home health services have resulted in lower net pay increases than providers of those services have often expected. In addition, MACRA establishes a multi-year transition into pay-for-quality approaches for Medicare physicians and other providers. This will include payment reductions for providers who do not meet government quality standards. The implementation of pay-for-quality models is expected to produce funding disparities that could adversely impact some provider tenants in medical buildings and other healthcare properties.

- Medicare reimburses nursing centers under a fixed payment methodology named the Skilled Nursing Facility Prospective Payment System (“SNF PPS”). SNF PPS is an acuity based classification system that uses nursing and therapy indexes adjusted by geographical wage indexes to calculate per diem rates for each Medicare patient. Payment rates are updated annually and are generally increased or decreased each October when the federal fiscal year begins. On July 30, 2015, CMS released its final rule outlining the fiscal year 2016 Medicare payments for skilled nursing facilities, which began October 1, 2015. The 2016 final rule provides for an approximate 1.2% rate update. This estimated increase consists of a 2.3% market basket increase, reduced by a 0.6% forecast error adjustment and further reduced 0.5% for a multifactor productivity adjustment required by the Healthcare Reform Law. CMS estimates the update will increase overall payments to skilled nursing facilities in fiscal year 2016 by $430 million compared to fiscal year 2015 levels. The effect of the 2016 PPS rate update on our tenants’ revenues will be dependent upon their census and the mix of patients at the various PPS pay rates. In addition, we cannot predict how future changes may impact reimbursement rates under the SNF PPS system.

- In January 2016, the Medicare Payment Advisory Commission finalized its recommendations, among other things advising Congress to eliminate market basket updates for SNFs for fiscal years 2017 and 2018 and directing the Secretary of HHS to revise the SNF prospective payment system. To the extent that these recommendations are implemented, they could impact our tenants.

- The OIG has increased focus in recent years on billing practices by SNFs. In September 2015, OIG issued a report calling for reevaluation of the Medicare payment system for skilled nursing facilities. In particular, OIG found that Medicare payments for therapy greatly exceeded SNFs’ costs for therapy, and that, under the current payment system, SNFs increasingly billed for the highest level of therapy even though key beneficiary characteristics remained largely the same. OIG determined that its findings demonstrated the need for CMS to reevaluate the Medicare SNF payment system, concluding that payment reform could save Medicare billions of dollars and encourage SNFs to provide services that are better aligned with beneficiaries’ care needs. Most recently, OIG issued (1) its findings regarding the fiscal year 2015 Top Management and Performance Challenges Facing HHS and (2) the FY 2016 OIG Work Plan. Both cited SNF billing as an area that creates incentives for providers to bill more expensive care instead of the appropriate levels of care, requiring ongoing government monitoring and auditing for compliance. The OIG formulates a formal work plan each year for nursing centers. The OIG’s most recent work plan indicates that quality of care, assessment and monitoring, poorly performing nursing facilities, hospitalizations, criminal background checks, Medicare Part B services, accuracy of nursing facilities Minimum Data, transparency of ownership, and civil monetary penalty funds will be the investigative focus in 2016. If followed, these reports and recommendations may impact our tenants. We cannot predict the likelihood, scope or outcome of any such investigations on our tenants.

We are neither an ongoing participant in, nor a direct recipient of, any reimbursement under these programs with respect to our facilities.

Environmental Regulation

As an owner of real property, we are subject to various federal, state and local laws and regulations regarding environmental, health and safety matters.

These laws and regulations address, among other things, asbestos, polychlorinated biphenyls, fuel oil management, wastewater discharges, air emissions, radioactive materials, medical wastes, and hazardous wastes, and, in certain cases, the costs of complying with these laws and regulations and the penalties for non-compliance can be substantial. Although we do not currently operate or manage our properties, we may be held primarily or jointly and severally liable for costs relating to the investigation and clean-up of our current and former properties from which there is or has been an actual or threatened release of a regulated material and any other affected properties, regardless of whether we knew of or caused the release. Such costs typically are not limited by law or regulation and could exceed the property's value. In addition, we may be liable for certain other costs, such as governmental fines and injuries to persons, property or natural resources, as a result of any such actual or threatened release. For a discussion

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of risks related to environmental liabilities, see “Risk Factors-Risks Related to Us as a Property Healthcare Holding and Leasing Company” included in Part I, Item 1A, Risk Factors, of this Annual Report.

Under the terms of our leases, we generally have a right to indemnification by the tenants of our properties for any contamination caused by them. However, we cannot be assured that our tenants will have the financial capability or willingness to satisfy their respective indemnification obligations to us, and any failure, inability or unwillingness to do so may require us to satisfy the underlying environmental claims. In general, we have also agreed to indemnify our tenants against any environmental claims (including penalties and clean-up costs) resulting from any condition arising in, on or under, or relating to, our properties at any time before the applicable lease commencement date.

We did not make any material capital expenditures in connection with environmental, health, and safety laws, ordinances and regulations in 2015 and do not expect that we will be required to make any such capital expenditures during 2016.

Employees

As of December 31, 2015, we had 31 employees of which 24 were full-time employees (excluding employees related to the Company's management services agreement for three facilities in Ohio).

Item 1A. Risk Factors

The following are certain risk factors that could affect our business, operations and financial condition. These risk factors should be considered in connection with evaluating the forward-looking statements contained in this Annual Report because these factors could cause the actual results and conditions to differ materially from those projected in forward-looking statements. This section does not describe all risks applicable to our business, and we intend it only as a summary of certain material factors. If any of the following risks actually occur, our business, financial condition or results of operations could be negatively affected. In that case, the trading price of our common stock and our Series A Preferred Stock could decline.

Risks Related to Our Business

We have a history of operating losses and may incur losses in the future.

For the year ended December 31, 2015, the Company had a net loss of $23.5 million compared to a net loss of $13.6 million for the year ended December 31, 2014. We make no assurances that we will be able to operate profitably. As of December 31, 2015, we have a working capital deficit of approximately $38.6 million.

Our leases with tenants comprise our rental revenue and any failure, inability or unwillingness by these tenants to satisfy their obligations under our agreements could have a material adverse effect on us.

Our business depends upon our tenants meeting their obligations to us, including their obligations to pay rent, maintain certain insurance coverage, pay real estate and other taxes and maintain and repair the leased properties. We cannot assure you that these tenants will have sufficient assets, income and access to financing to enable them to satisfy their respective obligations to us, and any failure, inability or unwillingness by these tenants to do so could have a material adverse effect on us. In addition, any failure by these tenants to effectively conduct their operations or to maintain and improve our properties could adversely affect their business reputation and their ability to attract and retain patients and residents in our properties, which could have a material adverse effect on us. Our tenants have agreed to indemnify, defend and hold us harmless from and against various claims, litigation and liabilities arising in connection with their respective businesses, and we cannot assure you that our tenants will have sufficient assets, income, access to financing and insurance coverage to enable them to satisfy their respective indemnification obligations.

We will depend on Skyline Healthcare LLC (or an affiliated entity) for a significant portion of our revenues and any inability or unwillingness by it to satisfy its obligations under its agreement with us could have a material adverse effect on us.

On February 5, 2016, we entered into a Master Lease Agreement pursuant to which we will lease to Skyline Healthcare LLC ("Skyline"), or an affiliated entity, our facilities located in Arkansas. The lease is expected to commence on April 1, 2016, subject to, among other things: (i) Skyline's (or its affiliated entity's) receipt of all licenses from the Arkansas Department of Health to operate the leased facilities; and (ii) the approval of the mortgage lenders for the leased facilities. The nine facilities subject to the Master Lease Agreement constitute 24% of the total number of our facilities, and we estimate that the rental revenue under the Master Lease Agreement for such nine facilities will constitute $6.5 million per year on an annualized basis, or 22% of our annual rental revenue.

Upon commencement of the lease, we will depend on Skyline (or its affiliated entity) for a significant portion of our revenues. Because our lease with Skyline (or its affiliated entity) is a triple-net lease, we also depend on Skyline (or its affiliated entity) to pay all insurance, taxes, utilities and maintenance and repair expenses in connection with the leased properties. We cannot assure you that Skyline (or its affiliated entity) will have sufficient assets, income and access to financing to enable it to make rental payments to us or to otherwise satisfy its obligations under the Master Lease Agreement, and any inability or unwillingness by Skyline (or its affiliated entity) to do so could have a material adverse effect on us.

A prolonged economic slowdown could adversely impact the results of operations of our tenants, which could impair their ability to meet their obligations to us.

We believe the risks associated with our investments will be more acute during periods of economic slowdown or recession (such as the recent recession) due to the adverse impact caused by various factors, including inflation, deflation, increased unemployment, volatile energy costs, geopolitical issues, the availability and cost of credit, the U.S. mortgage market, a distressed real estate market, market volatility and weakened business and consumer confidence. This difficult operating environment caused by an economic slowdown or recession could have an adverse impact on the ability of our tenants to maintain occupancy rates, which could harm their financial condition. Any sustained period of increased payment delinquencies, foreclosures or losses by our tenants could adversely affect our income from investments in our portfolio.

Certain third parties may not be able to satisfy their obligations to us or our tenants due to uncertainty in the capital markets.

Interest rate fluctuations, financial market volatility or credit market disruptions could limit the ability of our tenants to obtain credit to finance their businesses on acceptable terms, which could adversely affect their ability to satisfy their obligations to us. Similarly, if any of our other counterparties, such as banking institutions, title companies and escrow agents, experiences difficulty in accessing capital or other sources of funds or fails to remain viable, it could have an adverse effect on our business.

Increased competition, as well as increased operating costs, could result in lower revenues for some of our tenants and may affect their ability to meet their obligations to us.

The long-term care industry is highly competitive, and we expect that it will become more competitive in the future. Our tenants are competing with numerous other companies providing similar healthcare services or alternatives such as home health agencies, life care at home, community-based service programs, retirement communities and convalescent centers. Our tenants compete on a number of different levels, including the quality of care provided, reputation, the physical appearance of a facility, price, the range of services offered, family preference, alternatives for healthcare delivery, the supply of competing properties, physicians, staff, referral sources, location and the size and demographics of the population in the surrounding areas. We cannot be certain that the tenants of all of our facilities will be able to achieve occupancy and rate levels that will enable them to meet all of their obligations to us. Our tenants may encounter increased competition in the future that could limit their ability to attract patient's or residents or expand their businesses and, therefore, affect their ability to make their lease payments.

In addition, the market for qualified nurses, healthcare professionals and other key personnel is highly competitive, and our tenants may experience difficulties in attracting and retaining qualified personnel. Increases in labor costs due to higher wages and greater benefits required to attract and retain qualified healthcare personnel incurred by our tenants could affect their ability to meet their obligations to us. This situation could be particularly acute in certain states that have enacted legislation establishing minimum staffing requirements.

A severe cold and flu season, epidemics, or any other widespread illnesses could adversely affect the occupancy of our tenants' facilities.

Our and our tenants' revenues are dependent upon occupancy. It is impossible to predict the severity of the cold and flu season or the occurrence of epidemics or any other widespread illnesses. The occupancy of our skilled nursing and assisted living facilities could significantly decrease in the event of a severe cold and flu season, an epidemic, or any other widespread illness. Such a decrease could affect the operating income of our tenants and the ability of our tenants to make payments to us.

The bankruptcy, insolvency or financial deterioration of our tenants could limit or delay our ability to collect unpaid rents or require us to find new tenants.

We are exposed to the risk that a distressed tenant may not be able to meet its obligations to us or other third parties. This risk is heightened during a period of economic or political instability. We are also exposed to increased risk in situations where we lease multiple properties to a single tenant (or affiliated tenants) under a master lease, as a tenant failure or default could reduce or eliminate rental revenue from multiple properties. If tenants are unable to comply with the terms of their leases, then we may be

forced to modify the leases in ways that are unfavorable to us. Alternatively, the failure of a tenant to perform under a lease could require us to declare a default, repossess the property, find a suitable replacement tenant, hire third-party managers to operate the property or sell the property. There is no assurance that we would be able to lease a property on substantially equivalent or better terms than the prior lease, or at all, find another qualified tenant, successfully reposition the property for other uses or sell the property on terms that are favorable to us. It may be more difficult to find a replacement tenant for a healthcare property than it would be to find a replacement tenant for a general commercial property due to the specialized nature of the business. Even if we are able to find a suitable replacement tenant for a property, transfers of operations of skilled nursing facilities, and assisted living facilities are subject to regulatory approvals not required for transfers of other types of commercial operations, which may affect our ability to successfully transition a property.

If any lease expires or is terminated, then we could be responsible for all of the operating expenses for that property until it is leased again or sold. If a significant number of our properties are unleased, then our operating expenses could increase significantly. Any significant increase in our operating costs may have a material adverse effect on our business, financial condition and results of operations, and our ability to pay dividends to our shareholders.

Although each of our lease agreements typically provides us with or will provide us with, the right to terminate, evict a tenant, foreclose on our collateral, demand immediate payment and exercise other remedies upon the bankruptcy or insolvency of an tenant, the Bankruptcy Code would limit or, at a minimum, delay our ability to collect unpaid pre-bankruptcy rents and to pursue other remedies against a bankrupt tenant. A bankruptcy filing by one of our tenants would typically prevent us from collecting unpaid pre-bankruptcy rents or evicting the tenant absent approval of the bankruptcy court. The Bankruptcy Code provides a tenant with the option to assume or reject an unexpired lease within certain specified periods of time. Generally, a lessee is required to pay all rent that becomes payable between the date of its bankruptcy filing and the date of the assumption or rejection of the lease (although such payments will likely be delayed as a result of the bankruptcy filing). Any tenant that chooses to assume its lease with us must cure all monetary defaults existing under the lease (including payment of unpaid pre-bankruptcy rents) and provide adequate assurance of its ability to perform its future obligations under the lease. Any tenant that opts to reject its lease with us would face a claim by us for unpaid and future rents payable under the lease, but such claim would be subject to a statutory “cap” and would generally result in a recovery substantially less than the face value of such claim. Although the tenant’s rejection of the lease would permit us to recover possession of the leased facility, we would likely face losses, costs and delays associated with re-leasing the facility to a new tenant.

Several other factors could impact our rights under leases with bankrupt tenants. First, the tenant could seek to assign its lease with us to a third party. The Bankruptcy Code generally disregards anti-assignment provisions in leases to permit the assignment of unexpired leases to third parties (provided all monetary defaults under the lease are cured and the third party can demonstrate its ability to perform its obligations under the lease). Second, in instances in which we have entered into a master lease agreement with a tenant that operates more than one facility, the bankruptcy court could determine that the master lease was comprised of separate, divisible leases (each of which could be separately assumed or rejected), rather than a single, integrated lease (which would have to be assumed or rejected in its entirety). Finally, the bankruptcy court could recharacterize our lease agreement as a disguised financing arrangement, which could require us to receive bankruptcy court approval to foreclose or pursue other remedies with respect to the facility.

If we must replace any of our tenants, we might be unable to rent the properties on as favorable terms, or at all, and we could be subject to delays, limitations and expenses, which could have a material adverse effect on us.

We cannot predict whether our tenants will renew existing leases beyond their current term. If any of our triple-net leases are not renewed, we would attempt to rent those properties to another tenant. In addition, following expiration of a lease term or if we exercise our right to replace a tenant in default, rental payments on the related properties could decline or cease altogether while we reposition the properties with a suitable replacement tenant. We also might not be

successful in identifying suitable replacements or entering into leases or other arrangements with new tenants on a timely basis or on terms as favorable to us as our current leases, if at all, and we may be required to fund certain expenses and obligations (e.g., real estate and bed taxes, debt costs and maintenance expenses) to preserve the value of, and avoid the imposition of liens on, our properties while they are being repositioned. In addition, we may incur certain obligations and liabilities, including obligations to indemnify the replacement tenant, which could have a material adverse effect on us.

In the event of non-renewal or a tenant default, our ability to reposition our properties with a suitable replacement tenant could be significantly delayed or limited by state licensing, receivership, CON or other laws, as well as by the Medicare and Medicaid change-of-ownership rules, as further discussed below, and we could incur substantial additional expenses in connection with any licensing, receivership or change-of-ownership proceedings. Our ability to locate and attract suitable replacement tenants also could be impaired by the specialized healthcare uses or contractual restrictions on use of the properties, and we may be forced to spend substantial amounts to adapt the properties to other uses. Any such delays, limitations and expenses could adversely impact

our ability to collect rent, obtain possession of leased properties or otherwise exercise remedies for tenant default and could have a material adverse effect on us.

Moreover, in connection with certain of our properties, we have entered into intercreditor agreements with the tenants' lenders or tri-party agreements with our lenders. Our ability to exercise remedies under the applicable leases or to reposition the applicable properties may be significantly delayed or limited by the terms of the intercreditor agreement or tri-party agreement. Any such delay or limit on our rights and remedies could adversely affect our ability to mitigate our losses and could have a material adverse effect on us.

Required regulatory approvals can delay or prohibit transfers of our healthcare facilities.

Transfers of healthcare facilities to successor tenants may be subject to regulatory approvals or ratifications, including, but not limited to, change of ownership approvals under CON laws and Medicare and Medicaid provider arrangements that are not required for transfers of other types of commercial operations and other types of real estate. The replacement of any tenant or operator could be delayed by the regulatory approval process of any federal, state or local government agency necessary for the transfer of the facility or the replacement of the operator licensed to manage the facility. If we are unable to find a suitable replacement tenant upon favorable terms, or at all, we may take possession of a facility, which might expose us to successor liability, require us to indemnify subsequent to whom we might transfer the operating rights and licenses, or spend substantial time and funds to adapt the facility to other uses, all of which could have a material adverse effect on us.

Our tenants may be subject to significant legal actions that could result in their increased operating costs and substantial uninsured liabilities, which may affect their ability to meet their obligations to us.

As is typical in the long-term healthcare industry, our tenants may be subject to claims for damages relating to the services that they provide. We give no assurance that the insurance coverage maintained by our tenants will cover all claims made against them or continue to be available at a reasonable cost, if at all. In some states, insurance coverage for the risk of punitive damages may not, in certain cases, be available to operators due to state law prohibitions or limitations of availability. As a result, our tenants doing business in these states may be liable for punitive damage awards that are either not covered by their insurance or are in excess of their insurance policy limits.

We also believe that there has been, and will continue to be, an increase in governmental investigations of long-term care providers, particularly in the area of Medicare/Medicaid false claims, as well as an increase in enforcement actions resulting from these investigations. The OIG, the enforcement arm of the Medicare and Medicaid programs, formulates a formal work plan each year for nursing centers. The OIG's most recent work plan indicates that quality of care, assessment and monitoring, poorly performing nursing facilities, hospitalizations, criminal background checks, Medicare part B services, accuracy of nursing facilities Minimum Data, transparency of ownership, and civil monetary penalty funds will be an investigative focus in 2016. We cannot predict the likelihood, scope or outcome of any such investigations of our facilities or our tenants. Insurance is not available to our tenants to cover such losses. Any adverse determination in a legal proceeding or governmental investigation, whether currently asserted or arising in the future, could have a material adverse effect on a tenant's financial condition. If a tenant is unable to obtain or maintain insurance coverage, if judgments are obtained in excess of the insurance coverage, if a tenant is required to pay uninsured punitive damages, or if a tenant is subject to an uninsurable government enforcement action, then such tenant could be exposed to substantial additional liabilities. Such liabilities could adversely affect a tenant's ability to meet its obligations to us.

In addition, we may, in some circumstances, be named as a defendant in litigation involving the services provided by our tenants. Although we generally have no involvement in the services provided by our tenants, and our standard lease agreements generally require (or will require) our tenants to indemnify us and carry insurance to cover us in certain cases, a significant judgment against us in such litigation could exceed our and our tenants' insurance coverage,

which would require us to make payments to cover any such judgment.

Our tenants may be sued under a federal whistleblower statute.

Our tenants who engage in business with the federal government may be sued under a federal whistleblower statute designed to combat fraud and abuse in the healthcare industry. See “Governmental Regulation-Healthcare Regulation” included in Item 1 of this Annual Report. These lawsuits can involve significant monetary damages and award bounties to private plaintiffs who successfully bring these suits. If any of these lawsuits were brought against our tenants, such suits combined with increased operating costs and substantial uninsured liabilities could have a material adverse effect on our tenants’ liquidity, financial condition and results of operations and on their ability to satisfy their obligations under our leases, which, in turn, could have a material adverse effect on us.

The amount and scope of insurance coverage provided by our policies and policies maintained by our tenants may not adequately insure against losses.

We maintain or require in our leases that our tenants maintain all applicable lines of insurance on our properties and their operations. Although we regularly review the amount and scope of insurance provided by our policies and required to be maintained by our tenants and believe the coverage provided to be customary for similarly situated companies in our industry, we cannot assure you that we or our tenants will continue to be able to maintain adequate levels of insurance. We also cannot assure you that we or our tenants will maintain the required coverages, that we will continue to require the same levels of insurance under our leases, that such insurance will be available at a reasonable cost in the future or that the policies maintained will fully cover all losses on our properties upon the occurrence of a catastrophic event, nor can we make any guaranty as to the future financial viability of the insurers that underwrite our policies and the policies maintained by our tenants.

For various reasons, including to reduce and manage costs, many healthcare companies utilize different organizational and corporate structures coupled with captive programs that may provide less insurance coverage than a traditional insurance policy. Companies that insure any part of their general and professional liability risks through their own captive limited purpose entities generally estimate the future cost of general and professional liability through actuarial studies that rely primarily on historical data. However, due to the rise in the number and severity of professional claims against healthcare providers, these actuarial studies may underestimate the future cost of claims, and reserves for future claims may not be adequate to cover the actual cost of those claims. As a result, the tenants of our properties who self-insure could incur large funded and unfunded general and professional liability expenses, which could materially adversely affect their liquidity, financial condition and results of operations and, in turn, their ability to satisfy their obligations to us. If tenants of our properties decide to implement a captive or self-insurance program, any large funded and unfunded general and professional liability expenses incurred could have a material adverse effect on us.

Should an uninsured loss or a loss in excess of insured limits occur, we could incur substantial liability or lose all or a portion of the capital we have invested in a property, as well as the anticipated future revenues from the property. Following the occurrence of such an event, we might nevertheless remain obligated for any mortgage debt or other financial obligations related to the property. We cannot assure you that material uninsured losses, or losses in excess of insurance proceeds, will not occur in the future.

Failure by our tenants to comply with various local, state and federal government regulations may adversely impact their ability to make lease payments to us.

Healthcare operators are subject to numerous federal, state and local laws and regulations, including those described below, that are subject to frequent and substantial changes (sometimes applied retroactively) resulting from new legislation, adoption of rules and regulations, and administrative and judicial interpretations of existing law. Although we cannot accurately predict the ultimate timing or effect of these changes, such changes could have a material effect on our tenants' costs of doing business and on the amount of reimbursement by both government and other third-party payors. The failure of any of our tenants to comply with these laws, requirements and regulations could adversely affect its ability to meet its obligations to us.

- Healthcare Reform. The Patient Protection and Affordable Care Act and the Health Care and Education Reconciliation Act of 2010 (collectively, the "Healthcare Reform Law"), which were signed into law in March 2010, represent the most comprehensive change to healthcare benefits since the inception of the Medicare program in 1965 and affect reimbursement for governmental programs, private insurance and employee welfare benefit plans in various ways. Among other things, the Healthcare Reform Law expands Medicaid eligibility, requires most individuals to have health insurance, establishes new regulations for health plans, creates health insurance exchanges, and modifies certain payment systems to encourage more cost-effective care and a reduction of inefficiencies and

waste, including through new tools to address fraud and abuse. We cannot accurately predict the impact of the Healthcare Reform Law on our tenants or their ability to meet their obligations to us.

- Reimbursement; Medicare and Medicaid. A significant portion of the revenue of the healthcare operators to which we lease, or will lease, properties is, or will be, derived from governmentally-funded reimbursement programs, primarily Medicare and Medicaid. Failure to maintain certification in these programs would result in a loss of funding from such programs and could negatively impact an operator's ability to meet its obligations to us.

- Quality of Care Initiatives. The Center for Medicare and Medicaid Services ("CMS") has implemented a number of initiatives focused on the quality of care provided by nursing homes that could affect our tenants. Any unsatisfactory rating of our tenants under any rating system promulgated by the CMS could result in the loss of patients or residents or lower reimbursement rates, which could adversely impact their revenues and our business.

- Licensing and Certification. Healthcare operators are subject to various federal, state and local licensing and certification laws and regulations, including laws and regulations under Medicare and Medicaid requiring operators to comply with extensive standards governing operations. Many of our properties may require a license, registration, and/or CON to operate. State and local laws also may regulate the expansion, including the addition of new beds or services or acquisition of medical equipment, and the construction or renovation of health care facilities, by requiring a CON or other similar approval from a state agency. Governmental agencies administering these laws and regulations regularly inspect facilities and investigate complaints. Failure to obtain any required licensure, certification, or CON, the loss or suspension of any required licensure, certification, or CON, or any violations or deficiencies with respect to relevant operating standards may require a facility to cease operations or result in ineligibility for reimbursement until the necessary licenses, certifications, or CON are obtained or reinstated or until any such violations or deficiencies are cured. In such event, our revenues from these facilities could be reduced or eliminated for an extended period of time or permanently.

- Fraud and Abuse Laws and Regulations. There are various federal and state civil and criminal laws and regulations governing a wide array of healthcare provider referrals, relationships and arrangements, including laws and regulations prohibiting fraud by healthcare providers. In addition, the Stark Law broadly defines the scope of prohibited physician referrals under federal health care programs to providers with which they have ownership or other financial arrangements. Many states have adopted, or are considering, legislative proposals similar to these laws, some of which extend beyond federal health care programs, to prohibit the payment or receipt of remuneration for the referral of patients and physician referrals regardless of the source of the payment for the care. Many of these complex laws raise issues that have not been clearly interpreted by the relevant governmental authorities and courts. We cannot assure you that governmental officials charged with responsibility for enforcing the provisions of these laws and regulations will not assert that one or more of our arrangements are in violation of the provisions of such laws and regulations. In addition, federal and state governments are devoting increasing attention and resources to anti-fraud initiatives against healthcare providers. The violation of any of these laws or regulations by any of our tenants may result in the imposition of fines or other penalties, including exclusion from Medicare, Medicaid and all other federal and state healthcare programs. Such fines or penalties could jeopardize a tenant's ability to make lease payments to us or to continue operating its facility.

- Privacy Laws. Healthcare operators are subject to federal, state and local laws and regulations designed to protect the privacy and security of patient health information. These laws and regulations require operators to expend the requisite resources to protect and secure patient health information, including the funding of costs associated with technology upgrades. Operators found in violation of these laws may face large penalties. In addition, compliance with an operator's notification requirements in the event of a breach of unsecured protected health information could cause reputational harm to an operator's business. Such penalties and damaged reputation could adversely affect a tenant's ability to meet its obligations to us.

- Other Laws. Other federal, state and local laws and regulations affect how our tenants conduct their business. We cannot accurately predict the effect that the costs of complying with these laws may have on the revenues of our tenants and, thus, their ability to meet their obligations to us.

- Legislative and Regulatory Developments. Each year, legislative and regulatory proposals are introduced at the federal, state and local levels that, if adopted, would result in major changes to the healthcare system in addition to those described herein. We cannot accurately predict whether any proposals will be adopted and, if adopted, what effect (if any) these proposals would have on our tenants or our business.

Our tenants may be adversely affected by healthcare regulation and enforcement.

Regulation of the long-term healthcare industry generally has intensified over time both in the number and type of regulations and in the efforts to enforce those regulations. This is particularly true for large for-profit, multi-facility

providers. Federal, state and local laws and regulations affecting the healthcare industry include those relating to, among other things, licensure, conduct of operations, ownership of facilities, addition of facilities and equipment, allowable costs, services, prices for services, qualified beneficiaries, quality of care, patient rights, fraudulent or abusive behavior, data privacy and security, and financial and other arrangements that may be entered into by healthcare providers. In addition, changes in enforcement policies by federal and state governments have resulted in an increase in the number of inspections, citations of regulatory deficiencies and other regulatory sanctions, including terminations from the Medicare and Medicaid programs, bars on Medicare and Medicaid payments for new admissions, civil monetary penalties and even criminal penalties. We are unable to predict the scope of future federal, state and local regulations and legislation, including the Medicare and Medicaid statutes and regulations, or the intensity of enforcement efforts with respect to such regulations and legislation, and any changes in the regulatory framework could have a material adverse effect on our tenants, operators and managers, which, in turn, could have a material adverse effect on us.

If our tenants fail to comply with the extensive laws, regulations and other requirements applicable to their businesses and the operation of our properties, they could become ineligible to receive reimbursement from governmental and private third-party payor programs, face bans on admissions of new patients or residents, suffer civil or criminal penalties or be required to make significant changes to their operations. Our tenants also could face increased costs related to healthcare regulation, such as the Affordable Care Act, or be forced to expend considerable resources in responding to an investigation or other enforcement action under applicable laws or regulations. In such event, the results of operations and financial condition of our tenants and the results of operations of our properties operated or managed by those entities could be adversely affected, which, in turn, could have a material adverse effect on us.

The impact of healthcare reform legislation on our tenants cannot be accurately predicted.

The health care industry in the United States is subject to fundamental changes due to ongoing health care reform efforts and related political, economic and regulatory influences. Notably, the Healthcare Reform Law resulted in expanded health care coverage to millions of previously uninsured people beginning in 2014 and has resulted in significant changes to the U.S. health care system. To help fund this expansion, the Affordable Care Act outlines certain reductions in Medicare reimbursements for various health care providers, including skilled nursing facilities, as well as certain other changes to Medicare payment methodologies.

Several provisions of the Healthcare Reform Law affect Medicare payments to skilled nursing facilities, including provisions changing Medicare payment methodology and implementing value-based purchasing and payment bundling. Although we cannot accurately predict how all of these provisions may be implemented, or the effect any such implementation would have on our tenants or our business, the Healthcare Reform Law could result in decreases in payments to our tenants, increase our tenants' costs or otherwise adversely affect the financial condition of our tenants, thereby negatively impacting their ability to meet their obligations to us.

The Healthcare Reform Law also requires skilled nursing facilities to have a compliance and ethics program that is effective in preventing and detecting criminal, civil and administrative violations and in promoting quality of care. If our tenants fall short in their compliance and ethics programs and quality assurance and performance improvement programs, then their reputations and ability to attract residents could be adversely affected.

This comprehensive health care legislation has resulted and will continue to result in extensive rulemaking by regulatory authorities, and also may be altered or amended. It is difficult to predict the full impact of the Healthcare Reform Law due to the complexity of the law and implementing regulations, as well our inability to foresee how CMS and other participants in the health care industry will respond to the choices available to them under the law. We also cannot accurately predict whether any new or pending legislative proposals will be adopted or, if adopted, what effect, if any, these proposals would have on our tenants' business. Similarly, while we can anticipate that some of the rulemaking that will be promulgated by regulatory authorities will affect our tenants and the manner in which they are reimbursed by the federal health care programs, we cannot accurately predict today the impact of those regulations on their business and therefore on our business. The provisions of the legislation and other regulations implementing the provisions of the Affordable Care Act may increase our tenants' costs or otherwise adversely affect the financial condition of our tenants, thereby negatively impacting their ability to meet their obligations to us.

Other legislative changes have been proposed and adopted since the Healthcare Reform Law was enacted that also may impact our business. For instance, on April 1, 2014, the President signed the Protecting Access to Medicare Act of 2014, which, among other things, requires CMS to measure, track, and publish readmission rates of skilled nursing facilities by 2017 and implement a value-based purchasing program for skilled nursing facilities (the "SNF VBP Program") by October 1, 2018. The SNF VBP Program will increase Medicare reimbursement rates for skilled nursing facilities that achieve certain levels of quality performance measures to be developed by CMS, relative to other facilities. The value-based payments authorized by the SNF VBP Program will be funded by reducing Medicare payment for all skilled nursing facilities by 2% and redistributing up to 70% of those funds to high-performing skilled

nursing facilities. If Medicare reimbursement provided to our tenants is reduced under the SNF VBP Program, that reduction may have an adverse impact on the ability of our tenants to meet their obligations to us.

Our tenants depend on reimbursement from governmental and other third-party payors, and reimbursement rates from such payors may be reduced.

Changes in the reimbursement rate or methods of payment from third-party payors, including the Medicare and Medicaid programs, or the implementation of other measures to reduce reimbursements for services provided by our tenants could result in a substantial reduction in the revenues and operating margins of our tenants. Significant limits on the scopes of services reimbursed and on reimbursement rates could have a material adverse effect on the results of operations and financial condition of our tenants, which could cause their revenues to decline and could negatively impact their ability to meet their obligations to us.

Additionally, net revenue realizable under third-party payor agreements can change after examination and retroactive adjustment by payors during the claims settlement processes or as a result of post-payment audits. Payors may disallow requests for reimbursement based on determinations that certain costs are not reimbursable or reasonable, additional documentation is necessary or certain services were not covered or were not medically necessary. New legislative and regulatory proposals could impose further limitations on government and private payments to healthcare providers. In some cases, states have enacted or are considering enacting measures designed to reduce Medicaid expenditures and to make changes to private healthcare insurance. No assurance is given that adequate third-party payor reimbursement levels will continue to be available for the services provided by our tenants.

The Healthcare Reform Law provides those states that expand their Medicaid coverage to otherwise eligible state residents with incomes at or below 138% of the federal poverty level with an increased federal medical assistance percentage, effective January 1, 2014, when certain conditions are met. On June 28, 2012, the United States Supreme Court upheld the individual mandate of the Health Reform Laws but partially invalidated the expansion of Medicaid. The ruling on Medicaid expansion allows states to elect not to participate in the expansion-and to forego funding for the Medicaid expansion-without losing their existing Medicaid funding. Given that the federal government substantially funds the Medicaid expansion, it is unclear how many states will ultimately pursue this option, although, as of early February 2016, roughly half of the states have expanded Medicaid coverage. The participation by states in the Medicaid expansion could have the dual effect of increasing our tenants' revenues, through new patients, but further straining state budgets and their ability to pay our tenants. While the federal government will pay for approximately 100% of those additional costs from 2014 through 2016, states will be expected to pay for part of those additional costs beginning in 2017. In light of this, at least one state that has passed legislation to allow the state to expand its Medicaid coverage has included sunset provisions in the legislation that require that the expanded benefits be reduced or eliminated if the federal government's funding for the program is decreased or eliminated, permitting the state to re-visit the issue once it begins to share financial responsibility for the expansion. With increasingly strained budgets, it is unclear how states that do not include such sunset provisions will pay their share of these additional Medicaid costs and what other health care expenditures could be reduced as a result. A significant reduction in other health care related spending by states to pay for increased Medicaid costs could affect our tenants' revenue streams.

Furthermore, the Supreme Court's decision upholding the constitutionality of the individual healthcare mandate while striking down the provisions linking federal funding of state Medicaid programs with a federally mandated expansion of those programs has contributed to the uncertainty regarding the impact that the law will have on healthcare delivery systems over the next decade. We can expect that federal authorities will continue to implement the law, but because of the Supreme Court's mixed ruling, the implementation will take longer than originally expected, with a commensurate increase in the period of uncertainty regarding the long-term financial impact on the delivery of and payment for healthcare.

Government budget deficits could lead to a reduction in Medicare and Medicaid reimbursement.

Many states are focusing on the reduction of expenditures under their Medicaid programs, which may result in a reduction in reimbursement rates for our tenants. These potential reductions could be compounded by the potential for federal cost-cutting efforts that could lead to reductions in reimbursement to our tenants under both the Medicare and Medicaid programs. Reductions in Medicare and Medicaid reimbursement to our tenants could reduce the cash flow of our tenants and their ability to make rent payments to us. The need to control Medicaid expenditures may be exacerbated by the potential for increased enrollment in Medicaid due to unemployment and declines in family incomes. Because the Healthcare Reform Law allows states to increase the number of people who are eligible for Medicaid and simplifies enrollment in this program, Medicaid enrollment may significantly increase in the future. Since our tenants' profit margins with respect to Medicaid patients are generally relatively low, more than modest reductions in Medicaid reimbursement and an increase in the number of Medicaid patients could place some tenants in financial distress, which, in turn, could adversely affect us. If funding for Medicare or Medicaid is reduced, then it

could have a material adverse effect on our tenants' results of operations and financial condition, which could adversely affect their ability to meet their obligations to us.

Changes in the reimbursement rates or methods of payment from third-party payors, including insurance companies and the Medicare and Medicaid programs, could have a material adverse effect on our tenants.

Our tenants rely on reimbursement from third-party payors, including the Medicare (both traditional Medicare and "managed" Medicare/Medicare Advantage) and Medicaid programs, for substantially all of their revenues. Federal and state legislators and regulators have adopted or proposed various cost-containment measures that would limit payments to healthcare providers, and budget crises and financial shortfalls have caused states to implement or consider Medicaid rate freezes or cuts. See "Governmental Regulation-Healthcare Regulation" included in Item 1 of this Annual Report. Private third-party payors also have continued their efforts to control healthcare costs. We cannot assure you that our tenants who currently depend on governmental or private payor

reimbursement will be adequately reimbursed for the services they provide. Significant limits by governmental and private third-party payors on the scope of services reimbursed or on reimbursement rates and fees, whether from statutory and regulatory changes, retroactive rate adjustments, recovery of program overpayments or set-offs, court decisions, administrative rulings, policy interpretations, payment or other delays by fiscal intermediaries or carriers, government funding restrictions (at a program level or with respect to specific facilities) and interruption or delays in payments due to any ongoing government investigations and audits at such property, or private payor efforts, could have a material adverse effect on the liquidity, financial condition and results of operations of certain of our tenants, which could affect adversely their ability to comply with the terms of our leases and have a material adverse effect on us.

If we lose our key management personnel, we may not be able to successfully manage our business or achieve our objectives, which could have a material adverse effect on our business, financial condition, results of operations and prospects.

We are dependent on our management team, and our future success depends largely upon the management experience, skill, and contacts of our management and the loss of any of our key management team could harm our business. If we lose the services of any or all of our management team, we may not be able to replace them with similarly qualified personnel, which could have a material adverse effect on our business, financial condition, results of operations and prospects.

Disasters and other adverse events may seriously harm our business.

Our facilities and our business may suffer harm as a result of natural or man-made disasters such as storms, earthquakes, hurricanes, tornadoes, floods, fires, terrorist attacks and other conditions. The impact, or impending threat, of such events may require that our tenants evacuate one or more facilities, which could be costly and would involve risks, including potentially fatal risks, for their patients. The impact of disasters and similar events is inherently uncertain. Such events could harm our tenants' patients and employees, severely damage or destroy one or more of our facilities, harm our tenants' business, reputation and financial performance, or otherwise cause our tenants' businesses to suffer in ways that we currently cannot predict.

Unforeseen costs associated with the acquisition of new healthcare properties could reduce our profitability.

Our business strategy contemplates future acquisitions that may not prove to be successful. For example, we might encounter unanticipated difficulties and expenditures relating to our acquired healthcare properties, including contingent liabilities, or our newly acquired healthcare properties might require significant management attention that would otherwise be devoted to our ongoing business. Such costs may negatively affect our results of operations.

Our real estate investments are relatively illiquid.

Real estate investments are relatively illiquid and generally cannot be sold quickly. In addition, nearly all of our healthcare properties serve as collateral for our secured debt obligations and cannot be readily sold. Additional factors that are specific to our industry also tend to limit our ability to vary our portfolio promptly in response to changes in economic or other conditions. For example, all of our healthcare properties are "special purpose" properties that cannot be readily converted into general residential, retail or office use. In addition, transfers of operations of skilled nursing facilities, assisted living facilities and other healthcare facilities are subject to regulatory approvals not required for transfers of other types of commercial operations and other types of real estate. Thus, if the operation of any of our healthcare properties becomes unprofitable due to competition, age of improvements or other factors such that a tenant becomes unable to meet its obligations to us, then the liquidation value of the property may be substantially less, particularly relative to the amount owing on any related mortgage loan, than would be the case if the property were readily adaptable to other uses. Furthermore, the receipt of liquidation proceeds or the replacement of a tenant that has

defaulted on its lease could be delayed by the approval process of any federal, state or local agency necessary for the transfer of the property or the replacement of the tenant with a new tenant licensed to manage the facility. In addition, certain significant expenditures associated with real estate investment, such as real estate taxes and maintenance costs, are generally not reduced when circumstances cause a reduction in income from the investment. Should such events occur, our revenues would be adversely affected.

As an owner with respect to real property, we may be exposed to possible environmental liabilities.

Under various federal, state and local environmental laws, ordinances and regulations, a current or previous owner of real property, such as us, may be liable in certain circumstances for the costs of investigation, removal or remediation of, or related releases of, certain hazardous or toxic substances at, under or disposed of in connection with such property, as well as certain other potential costs relating to hazardous or toxic substances, including government fines and damages for injuries to persons and adjacent property. Such laws often impose liability based on the owner’s knowledge of, or responsibility for, the presence or disposal of such substances. As a result, liability may be imposed on the owner in connection with the activities of an operator of the property.

The cost of any required investigation, remediation, removal, fines or personal or property damages and the owner's liability therefor could exceed the value of the property and the assets of the owner. In addition, the presence of such substances, or the failure to properly dispose of or remediate such substances, may adversely affect an operator's ability to attract additional patients or residents and our ability to sell or rent such property or to borrow using such property as collateral which, in turn, could negatively impact our revenues.

The industry in which we operate is highly competitive. Increasing investor interest in our sector and consolidation at the operator level could increase competition and reduce our profitability.

Our business is highly competitive, and we expect that it may become more competitive in the future. We compete for healthcare facility investments with other healthcare investors, many of which have greater resources and lower costs of capital than we do. Increased competition makes it more challenging for us to identify and successfully capitalize on opportunities that meet our investment criteria. If we cannot identify and purchase a sufficient number of healthcare facilities at favorable prices, or if we are unable to finance such acquisitions on commercially favorable terms, our business, results of operations and financial condition may be materially adversely affected. In addition, if our cost of capital should increase relative to the cost of capital of our competitors, the spread that we realize on our investments may decline if competitive pressures limit or prevent us from charging higher lease rates.

The geographic concentration of our facilities could leave us vulnerable to an economic downturn, regulatory changes in those areas.

Our properties are located in different states, with concentrations in Arkansas, Georgia, and Ohio. As a result of this concentration, the conditions of local economies and real estate markets, changes in governmental rules, regulations and reimbursement rates or criteria, changes in demographics, state funding, acts of nature and other factors that may result in a decrease in demand and reimbursement for skilled nursing services in these states could have a disproportionately adverse effect on our tenants' revenue, costs and results of operations, which may affect their ability to meet their obligations to us.

Our directors and officers substantially control all major decisions.

Our directors and officers beneficially own approximately 13.7% of our outstanding common stock. Therefore, our directors and officers will be able to influence major corporate actions required to be voted on by shareholders, such as the election of directors, the amendment of our charter documents and the approval of significant corporate transactions such as mergers, reorganizations, sales of substantially all of our assets and liquidation. Furthermore, our directors will be able to make decisions affecting our capital structure, including decisions to issue additional capital stock, implement stock repurchase programs and incur indebtedness. This control may have the effect of deterring hostile takeovers, delaying or preventing changes in control or changes in management, or limiting the ability of our other shareholders to approve transactions that they may deem to be in their best interest.

Provisions in our charter documents provide for indemnification of officers and directors, which could require us to direct funds away from our business and future operations.

Our charter documents provide for the indemnification of our officers and directors. We may be required to advance costs incurred by an officer or director and to pay judgments, fines and expenses incurred by an officer or director, including reasonable attorneys' fees, as a result of actions or proceedings in which our officers and directors are involved by reason of being or having been an officer or director of our Company. Funds paid in satisfaction of judgments, fines and expenses may be funds we need for the operation and growth of our business.

Risks Related to Our Capital Structure

We have substantial indebtedness, which may have a material adverse effect on our business and financial condition.

As of December 31, 2015, we had approximately $125.5 million in indebtedness, including current maturities of debt and debt related to discontinued operations. We may also obtain additional short-term and long-term debt to meet future capital needs, subject to certain restrictions under our existing indebtedness, which would increase our total debt. Our substantial amount of debt could have negative consequences to our business. For example, it could:

- increase our vulnerability to general adverse economic and industry conditions or a downturn in our business;
- require us to dedicate a substantial portion of cash flows from operations to interest and principal payments on outstanding debt, thereby limiting the availability of cash flow, dividends, and other general corporate purposes;
- require us to maintain certain debt coverage and other financial ratios at specified levels, thereby reducing our financial

flexibility;
- made it more difficult for us to satisfy our financial obligations;
- expose us to increases in interest rates for our variable rate debt;
- limit our ability to borrow additional funds on favorable terms, or at all, for working capital, debt service requirements, expansion of our business or other general corporate purposes;
- limit our ability to refinance all or a portion of our indebtedness on or before maturity on the same or more favorable terms, or at all;
- limit our flexibility in planning for, or reacting to, changes in our business and our industry;
- limit our ability to make acquisitions or take advantage of business opportunities as they arise;
- place us at a competitive disadvantage compared with our competitors that have less debt; and
- limit our ability to borrow additional funds, even when necessary to maintain adequate liquidity.

In addition, our ability to borrow funds in the future will depend in part on the satisfaction of the covenants in our credit facilities and other debt agreements. If we are unable to satisfy the financial covenants contained in those agreements, or are unable to generate cash sufficient to make required debt payments, the lenders and other parties to those arrangements could accelerate the maturity of some or all of our outstanding indebtedness.

We may not have sufficient liquidity to meet our capital needs.

For the year ended and as of December 31, 2015, we had a net loss of $23.5 million and negative working capital of $38.6 million. At December 31, 2015, we had $2.7 million in cash and cash equivalents, as well as restricted cash of $12.7 million, and $125.5 million in indebtedness, including current maturities of $51.9 million.

We continue to undertake measures to streamline our operations and cost infrastructure in connection with our new business model, including: (i) eliminating patient care services and related costs; (ii) increasing future minimum lease revenue; (iii) refinancing or repaying current maturities to reduce interest costs and reducing mandatory principal repayments through refinancing transactions with HUD or other lending sources; and (iv) reducing general and administrative expenses.

Over the next twelve months, we anticipate both access to and receipt of several sources of liquidity, including proceeds from at-the-market preferred stock offerings and cash from operations. We routinely have ongoing discussions with existing and new potential lenders to refinance current debt on a longer-term basis and, in recent periods, have refinanced short-term acquisition-related debt with traditional long-term mortgage notes, some of which have been executed under government guaranteed lending programs. We have been successful in recent years in raising new equity capital and believe, based on recent discussions that these markets will continue to be available to us for raising capital in 2016 and beyond.

In order to satisfy our capital needs, we seek to: (i) continue improving operating results through leasing and subleasing transactions executed with favorable terms and consistent and predictable cash flow; (ii) re-lease our Arkansas facilities with a new leasing arrangement made with a new operator; (iii) expand borrowing arrangements with certain lenders; (iv) refinance current debt where possible to obtain more favorable terms; and (v) raise capital through the issuance of debt or equity securities. The Company anticipates that these actions, if successful, will provide the opportunity to maintain liquidity on a short and long term basis, thereby permitting the Company to meet its operating and financing obligations for the next twelve months. However, there is no guarantee that such actions will be successful or that the anticipated operating results of the Transition will be realized. If such actions are not successful, or if the anticipated operating results of the Transition are not realized, then the Company may be required to restructure its outstanding indebtedness, implement further cost reduction initiatives or sell assets.

We are subject to risks associated with debt financing, which would negatively impact our business and limit our ability to pay dividends to our shareholders and to repay maturing indebtedness.

The financing required to make future investments and satisfy maturing debt commitments may be provided by private or public offerings of debt or equity, the assumption of secured indebtedness, or mortgage financing on a portion of our owned portfolio. To the extent we must obtain debt financing from external sources to fund our capital requirements, no assurance is given that such financing will be available on favorable terms, if at all. In addition, if we are unable to refinance or extend principal payments due at maturity or pay them with proceeds from other capital transactions, our cash flow may not be sufficient to repay our maturing indebtedness. Furthermore, if we have to pay higher interest rates in connection with a refinancing, the interest expense relating to that refinanced indebtedness would increase, which could reduce our profitability. Moreover, additional debt financing increases the amount of our leverage. The degree of leverage could have important consequences to our shareholders, including affecting our ability to obtain additional financing in the future, and making us more vulnerable to a downturn in our results of operations or the economy generally.

We rely on external sources of capital to fund future capital needs, and if we encounter difficulty in obtaining such capital, we may not be able to make future investments necessary to grow our business or meet maturing commitments.

We rely on external sources of capital, including debt and equity financing. If we are unable to obtain needed capital at all or only on unfavorable terms from these sources, we might not be able to make the investments needed to grow our business or to meet our obligations and commitments as they mature. Our access to capital depends upon a number of factors over which we have little or no control, including the performance of the national and global economies generally; competition in the healthcare industry; issues facing the healthcare industry, including regulations and government reimbursement policies; our tenants' operating costs; the market's perception of our growth potential; the market value of our properties; our current and potential future earnings and cash dividends; and the market price of the shares of our capital stock. We may not be in a position to take advantage of future investment opportunities if we are unable to access capital markets on a timely basis or are only able to obtain financing on unfavorable terms.

Our ability to raise capital through equity sales is dependent, in part, on the market price of our stock, and our failure to meet market expectations with respect to our business could negatively impact the market price of our stock and availability of equity capital.

As with other publicly-traded companies, the availability of equity capital will depend, in part, on the market price of our stock, which, in turn, will depend upon various market conditions and other factors that may change from time to time, including:

- the extent of investor interest;
- our financial performance and that of our tenants;
- general stock and bond market conditions; and
- other factors such as governmental regulatory action.

Covenants in the agreements evidencing our indebtedness limit our operational flexibility, and a covenant breach could materially adversely affect our operations.

The terms of our credit agreements and other agreements evidencing our indebtedness require us to comply with a number of financial and other covenants which may limit management's discretion by restricting our ability to, among other things, incur additional debt, and create liens. Any additional financing we may obtain could contain similar or more restrictive covenants. Our continued ability to incur indebtedness and conduct our operations is subject to compliance with these financial and other covenants. Breaches of these covenants could result in defaults under the instruments governing the applicable indebtedness in addition to any other indebtedness cross-defaulted against such instruments. Any such breach could materially adversely affect our business, results of operations and financial condition.

Our assets may be subject to impairment charges.

We periodically, but not less than annually, evaluate our real estate investments and other assets for impairment indicators. The judgment regarding the existence of impairment indicators is based on factors such as market conditions, operator performance and legal structure. If we determine that a significant impairment has occurred, then we are required to make an adjustment to the net carrying value of the asset, which could have a material adverse effect on our results of operations in the period in which the write-off occurs.

We may change our investment strategies and policies and capital structure.

The Board, without the approval of our shareholders, may alter our investment strategies and policies if it determines that a change is in our shareholders' best interests. The methods of implementing our investment strategies and policies may vary as new investments and financing techniques are developed.

Economic conditions and turbulence in the credit markets may create challenges in securing third-party borrowings or refinancing our existing indebtedness.

Depressed economic conditions, the availability and cost of credit, turmoil in the mortgage market and depressed real estate markets have in the past contributed, and will in the future contribute, to increased volatility and diminished expectations for real estate markets and the economy as a whole. Significant market disruption and volatility could impact our ability to secure third-party borrowings or refinance our existing indebtedness, which may prevent us from successfully implementing the Transition.

We are subject to possible conflicts of interest; we have engaged in, and may in the future engage in, transactions with parties that may be considered related parties.

From time to time, we have engaged in various transactions with related parties including Christopher Brogdon, a former director and owner of greater than 5% of our outstanding common stock. These transactions, along with other related party transactions, are described in Note 19 to our Consolidated Financial Statements included in Part II, Item 8., “Financial Statements and Supplementary Data,” and Part III., Item 13., “Certain Relationships and Related Transactions, and Director Independence.”

Although we do not believe the potential conflicts have adversely affected, or will adversely affect, our business, others may disagree with this position and litigation could ensue in the future. Our relationships with Mr. Brogdon and other related parties may give rise to litigation, or other issues which could result in substantial costs to us, and a diversion of our resources and management's attention, whether or not any allegations made are substantiated.

Risks Related to Our Stock

The price of our stock has fluctuated, and a number of factors may cause the price of our stock to decline.

The market price of our stock has fluctuated and may fluctuate significantly in the future, depending upon many factors, many of which are beyond our control. These factors include:

- actual or anticipated fluctuations in our operating results;
- changes in our financial condition, performance and prospects;
- changes in general economic and market conditions and other external factors;
- the market price of securities issued by other companies in our industry;
- announcements by us or our competitors of significant acquisitions, dispositions, strategic partnerships or other transactions;
- press releases or negative publicity relating to us or our competitors or relating to trends in healthcare;
- government action or regulation, including changes in federal, state and local healthcare regulations to which we or our tenants are subject;
- the level and quality of securities analysts' coverage for our stock;
- changes in financial estimates, our ability to meet those estimates, or recommendations by securities analysts with respect to us or our competitors; and
- future sales of our common stock, our Series A Preferred Stock or another series of our preferred stock, or debt securities.

In addition, the market price of our Series A Preferred Stock also depends upon:

- prevailing interest rates, increases in which may have an adverse effect on the market price of our Series A Preferred Stock;
- trading prices of preferred equity securities issued by other companies in our industry; and
- the annual yield from distributions on our Series A Preferred Stock as compared to yields on other financial instruments.

Furthermore, the stock market in recent years has experienced sweeping price and volume fluctuations that often have been unrelated to the operating performance of affected companies. These market fluctuations may also cause the price of our stock to decline.

In the event of fluctuations in the price of our stock, shareholders may be unable to resell shares of our stock at or above the price at which they purchased such shares. Additionally, due to fluctuations in the price of our stock,

comparing our operating results on a period-to-period basis may not be meaningful, and you should not rely on past results as an indication of future performance.

There are no assurances of our ability to pay dividends in the future.

We are a holding company, and we have no significant operations. We rely primarily on dividends and other distributions from our subsidiaries to us so we may, among other things, pay dividends on our capital stock, if and to the extent declared by the Board. The ability of our subsidiaries to pay dividends and make other distributions to us depends on their earnings and is restricted by the terms of certain agreements governing their indebtedness. If our subsidiaries are in default under such agreements, then they may not pay dividends or make other distributions to us.

In addition, we may only pay dividends on our capital stock if we have funds legally available to pay dividends and such payment is not restricted or prohibited by law, the terms of any shares with higher priority with respect to dividends or any documents governing our indebtedness. We are restricted by Georgia law from paying dividends on our capital stock if we are not able to pay our debts as they become due in the normal course of business or if our total assets would be less than the sum of our total

liabilities plus the amount that would be needed to satisfy preferential rights upon dissolution. In addition, no cash dividends may be declared or paid on the common stock unless full cumulative dividends on our Series A Preferred Stock have been, or contemporaneously are, declared and paid, or declared and a sum sufficient for the payment thereof is set apart for payments, for all past dividend periods. In addition, future debt, contractual covenants or arrangements we or our subsidiaries enter into may restrict or prevent future dividend payments.

As such, we could become unable, on a temporary or permanent basis, to pay dividends on our stock, including our common stock and our Series A Preferred Stock. The payment of any future dividends on our stock will be at the discretion of the Board and will depend, among other things, on the earnings and results of operations of our subsidiaries, their ability to pay dividends and make other distributions to us under agreements governing their indebtedness, our financial condition and capital requirements, any debt service requirements and any other factors the Board deems relevant.

The costs of being publicly owned may strain our resources and impact our business, financial condition, results of operations and prospects.

As a public company, we are subject to the reporting requirements of the Securities Exchange Act of 1934 (the "Exchange Act") and the Sarbanes-Oxley Act of 2002 ("Sarbanes-Oxley Act"). The Exchange Act requires that we file annual, quarterly and current reports with respect to our business and financial condition. The Sarbanes-Oxley Act requires that we maintain effective disclosure controls and procedures and internal controls for financial reporting. We are required to document and test our internal control procedures in order to satisfy the requirements of Section 404 of the Sarbanes-Oxley Act, which requires annual management assessments of the effectiveness of our internal controls over financial reporting.

These requirements may place a strain on our systems and resources and have required us, and may in the future require us, to hire additional accounting and financial resources with appropriate public company experience and technical accounting knowledge. In addition, failure to maintain such internal controls could result in us being unable to provide timely and reliable financial information which could potentially subject us to sanctions or investigations by the SEC or other regulatory authorities or cause us to be late in the filing of required reports or financial results. Any of the foregoing events could have a materially adverse effect on our business, financial condition, results of operations and prospects.

Provisions in Georgia law and our charter documents may delay or prevent a change in control or management that shareholders may consider desirable.

Various provisions of the Georgia Business Corporation Code (the "GBCC") and of our charter documents may inhibit changes in control not approved by the Board and may have the effect of depriving our investors of an opportunity to receive a premium over the prevailing market price of our common stock and other securities in the event of an attempted hostile takeover. These provisions could also discourage proxy contests and make it more difficult for shareholders to elect directors and take other corporate actions. As a result, the existence of these provisions may adversely affect the market price of our common stock and other securities. These provisions include:

- a requirement that special meetings of shareholders be called by the Board, the Chairman, the President, or the holders of shares with voting power of at least 25%;
- advance notice requirements for shareholder proposals and nominations;
- a requirement that directors may only be removed for cause and then only by an affirmative vote of at least a majority of all votes entitled to be cast in the election of such directors;
- a prohibition of shareholder action without a meeting by less than unanimous written consent;
- availability of "blank check" preferred stock; and
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a charter "constituency" clause authorizing (but not requiring) our directors to consider, in discharging their duties as directors, the effects of the Company's actions on other interests and persons in addition to our shareholders.

In addition, the Company has elected in its bylaws to be subject to the "fair price" and "business combination" provisions of the GBCC. The business combination provisions generally restrict us from engaging in certain business combination transactions with any "interested shareholder" (as defined in the GBCC) for a period of five years after the date of the transaction in which the person became an interested shareholder unless certain designated conditions are met. The fair price provisions generally restricts us from entering into certain business combinations with an interested shareholder unless the transaction is unanimously approved by the continuing directors who must constitute at least three members of the Board at the time of such approval; or the transaction is recommended by at least two-thirds of the continuing directors and approved by a majority of the shareholders excluding the interested shareholder.

The Board can use these and other provisions to prevent, delay or discourage a change in control of the Company or a change in our management. Any such delay or prevention of a change in control or management could deter potential acquirers or prevent the completion of a takeover transaction pursuant to which our shareholders could receive a substantial premium over the current market price of our common stock and other securities, which in turn may limit the price investors might be willing to pay for such securities.

Item 1B. Unresolved Staff Comments

Disclosure pursuant to Item 1B of Form 10-K is not required to be provided by smaller reporting companies.

Item 2. Properties

Operating Facilities

The following table provides summary information regarding our facilities leased and subleased to third parties as of December 31, 2015:

Facility Name	Beds/Units	Structure	Operator Affiliation
Alabama			
Attalla Health Care	182	Owned	C.R. Management
Coosa Valley Health Care	122	Owned	C.R. Management
Subtotal (2)	304		
Arkansas			
Cumberland H&R	77	Owned	Aria Health Group LLC
Heritage Park	93	Owned	Aria Health Group LLC
Homestead Manor	97	Owned	Aria Health Group LLC
Little Rock H&R	154	Owned	Aria Health Group LLC
Northridge Health	140	Owned	Aria Health Group LLC
River Valley Health	129	Owned	Aria Health Group LLC
Stone County Nursing	96	Owned	Aria Health Group LLC
Stone County ALF	32	Owned	Aria Health Group LLC
Woodland Hills	140	Owned	Aria Health Group LLC
Subtotal (9)	958		
Georgia			
Autumn Breeze	108	Owned	C.R. Management
Bonterra	115	Leased	Wellington Health Services
College Park	95	Owned	C.R. Management
Glenvue H&R	134	Owned	C.R. Management
Jeffersonville	117	Leased	New Beginnings Care
LaGrange	137	Leased	C.R. Management
Lumber City	86	Leased	Beacon Health Management
Oceanside	85	Leased	New Beginnings Care
Parkview Manor/Legacy	184	Leased	Wellington Health Services
Powder Springs	208	Leased	Wellington Health Services
Savannah Beach	50	Leased	New Beginnings Care
Southland Healthcare	126	Owned	Beacon Health Management
Tara	134	Leased	Wellington Health Services
Thomasville N&R	52	Leased	C.R. Management
Subtotal (14)	1,631		
North Carolina			
Mountain Trace Rehab	106	Owned	Symmetry Healthcare
Subtotal (1)	106		
Ohio			

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Covington Care	94	Leased	Beacon Health Management
Eaglewood ALF	80	Owned	Beacon Health Management
Eaglewood Care Center	99	Owned	Beacon Health Management
H&C of Greenfield	50	Owned	Beacon Health Management
Koester Pavilion	150	Managed	N/A
Spring Meade Health Center	99	Managed	N/A
Spring Meade Residence	83	Managed	N/A
The Pavilion Care Center	50	Owned	Beacon Health Management
Subtotal (8)	705		
Oklahoma			
NW Nursing Center	88	Owned	Southwest LTC
Quail Creek	109	Owned	Southwest LTC
Subtotal (2)	197		
South Carolina			
Georgetown Health	84	Owned	Symmetry Healthcare
Sumter Valley Nursing	96	Owned	Symmetry Healthcare
Subtotal (2)	180		
Total - All Facilities (38)	4,081		

All facilities are skilled nursing facilities except for Stone County ALF and Eaglewood ALF which are assisted living facilities and Spring Meade Residence which is an independent living facility.

The Company subleased through its subsidiaries nine facilities located in Arkansas to affiliates of Aria Health Group, LLC pursuant to separate sublease agreements. Eight of the Aria subleases commenced on May 1, 2015 and one sublease commenced on November 1, 2015. Effective February 3, 2016, each sublease was terminated due to the failure to pay rent pursuant to the terms of such sublease. Subsequently, on February 5, 2016, the Company entered into a Master Lease Agreement, as amended, with Skyline Healthcare LLC to lease the facilities commencing April 1, 2016. (See Part II, Item 8, Financial Statements and Supplemental Data, Note 19, Subsequent Events).

On January 22, 2016, New Beginnings Care LLC and its affiliates ("New Beginnings") filed a petition to reorganize its finances under the Bankruptcy Code. To date, New Beginnings has neither affirmed nor rejected the Master Lease entered into on November 3, 2015 with respect to the Jeffersonville, Oceanside, and Savannah Beach facilities. The Company is in discussions with New Beginnings and other potential operators about leasing such facilities.

In March 2016, CMS decertified the Jeffersonville facility meaning the facility can no longer accept Medicare or Medicaid patients. The operator is considering appealing the decision by CMS.

For a detailed description of the Company's operating leases, please see Note 7 - Leases to our Consolidated Financial Statements included in Part II, Item 8., "Financial Statements and Supplementary Data".

For a detailed description of the Company's related mortgages payable for owned facilities, please see Note 9 - Notes Payable and Other Debt to our Consolidated Financial Statements included in Part II, Item 8., "Financial Statements and Supplementary Data".

Corporate Office

Our corporate office is located in Roswell, Georgia. We own two office buildings in Roswell which contain approximately 13,700 square feet of office space. In addition, we lease approximately 3,100 square feet of office space in the Atlanta, Georgia area with a term through September 2020.

Item 3. Legal Proceedings

We are party to various legal actions and administrative proceedings and are subject to various claims arising in the ordinary course of business, including claims that the services we provided during the time we operated skilled nursing facilities resulted in injury or death to the residents of our facilities and claims related to employment, staffing requirements and commercial matters. Although we intend to vigorously defend ourselves in these matters, there is no assurance that the outcomes of these matters will not have a material adverse effect on our business, results of

operations and financial condition.

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We previously operated, and our tenants now operate, in an industry that is extremely regulated. As such, in the ordinary course of business, our tenants are continuously subject to state and federal regulatory scrutiny, supervision and control. Such regulatory scrutiny often includes inquiries, investigations, examinations, audits, site visits and surveys, some of which are non-routine. In addition, we believe that there has been, and will continue to be, an increase in governmental investigations of long-term care providers, particularly in the area of Medicare/Medicaid false claims, as well as an increase in enforcement actions resulting from these investigations. Adverse determinations in legal proceedings or governmental investigations against or involving us, for our prior operations, or our tenants, whether currently asserted or arising in the future, could have a material adverse effect on our business, results of operations and financial condition.

The Company is a defendant in a purported class action lawsuit captioned Amy Cleveland et al. v. APHR&R Nursing, LLC et al, filed on March 4, 2015 with the Circuit Court of Pulaski County, Arkansas, 16th Division, 6th Circuit (the "Complaint"). The Complaint asserted claims on behalf of a purported class consisting of the residents at: (i) Stone County Nursing and Rehabilitation Center; (ii) Bentonville Manor Nursing Home; (iii) Heritage Park Nursing Center; (iv) Homestead Manor Nursing Home; (v) River Valley Health and Rehabilitation Center; (vi) Northridge Healthcare and Rehabilitation; (vii) Woodland Hills Healthcare and Rehabilitation; (viii) West Markham Sub Acute and Rehabilitation Center; and (ix) Cumberland Health and Rehabilitation Center, all of which were managed by subsidiaries or affiliates of the Company. The lawsuit alleged that the nine facilities were understaffed during the class period which resulted in breaches or violation of the nursing home admission agreements, the Arkansas Deceptive Trade Practices Act, and the Long Term Care Facilities Residents' Act. The Complaint also included individual negligence claims on behalf of former deceased resident Amy Cleveland. The Complaint sought certification of a class of residents consisting of all residents of the facilities during the class period, judgment against all defendants for actual, compensatory and punitive damages and attorney fees. With respect to the allegations concerning Amy Cleveland, the Complaint sought damages for injuries, general and special damages, prejudgment and post-judgment interest, attorney fees and punitive damages.

On December 16, 2015, the Company's insurance carrier reached a settlement with each of the individual plaintiffs on behalf of the Company and all other defendants pursuant to which separate payments are to be made by the Company's carrier to the plaintiffs. The individual settlements are contingent on approval by the probate courts having jurisdiction over the deceased plaintiffs' respective estates, if applicable. As of March 28, 2016, all but three of the individual settlement agreements had been approved and the settlement consideration paid to the plaintiffs.

Item 4. Mine Safety Disclosures

Not applicable.

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PART II

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

Market for Registrant's Common Equity

Our common stock is listed for trading on the NYSE MKT under the symbol "ADK." The high and low sales prices of our common stock and cash dividends declared during the quarters listed below were as follows:

		Sales Price		Cash Dividends
		High	Low	Declared
2015	First Quarter	$4.50	$3.79	$0.050
	Second Quarter	$4.45	$3.32	$0.055
	Third Quarter	$4.00	$3.10	$0.060
	Fourth Quarter	$3.42	$1.90	$—
2014	First Quarter	$4.67	$4.00	$—
	Second Quarter	$4.70	$3.65	$—
	Third Quarter	$5.05	$4.22	$—
	Fourth Quarter	$4.77	$3.58	$—

Based on information supplied from our transfer agent, there were approximately 19,948,534 shareholders of record of our common stock as of March 28, 2016.

We are a holding company, and we have no significant operations. We rely primarily on dividends and other distributions from our subsidiaries to us so we may, among other things, pay dividends on our common stock, if and to the extent declared by the Board. The ability of our subsidiaries to pay dividends and make other distributions to us depends on their earnings and is restricted by the terms of certain agreements governing their indebtedness. If our subsidiaries are in default under such agreements, then they may not pay dividends or make other distributions to us.

In addition, we may only pay dividends on our common stock if we have funds legally available to pay dividends and such payment is not restricted or prohibited by law, the terms of any shares with higher priority with respect to dividends or any documents governing our indebtedness. We are restricted by Georgia law from paying dividends on our common stock if we are not able to pay our debts as they become due in the normal course of business or if our total assets would be less than the sum of our total liabilities plus the amount that would be needed to satisfy preferential rights upon dissolution of the holders of our Series A Preferred Stock and any other shareholders whose preferential rights are superior. In addition, no cash dividends may be declared or paid on the common stock unless full cumulative dividends on our Series A Preferred Stock have been, or contemporaneously are, declared and paid, or declared and a sum sufficient for the payment thereof is set apart for payments, for all past dividend periods. In addition, future debt, contractual covenants or arrangements we or our subsidiaries enter into may restrict or prevent future dividend payments. See “Risk Factors – Risk Related to Our Stock - There are no assurances of our ability to pay dividends in the future” included in Part I, Item 1A, Risk Factors, of this Annual Report.

The Board determined not to declare a cash dividend on the common stock for the fourth quarter of 2015. The Board intends to continue to evaluate the Company's dividend policy throughout 2016. The Board believes that it is prudent and appropriate to retain capital to focus on specific areas of long-term value creation and near-term investments to maximize shareholder value. The Company does not anticipate paying cash dividends on the common stock in the foreseeable future.

Equity Compensation Plan Information

The following table sets forth additional information as of December 31, 2015, concerning shares of our common stock that may be issued upon the exercise of options and other rights under our existing equity compensation plans and arrangements, divided between plans approved by our shareholders and plans or arrangements not submitted to

the shareholders for approval. The information includes the number of shares covered by and the weighted average exercise price of, outstanding options, warrants, and the number of shares remaining available for future grants excluding the shares to be issued upon exercise of outstanding options, warrants, and other rights.

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Plan Category	(a) Number of Securities to be Issued Upon Exercise of Outstanding Options, Warrants	(b) Weighted-Average Exercise Price of Outstanding Options, Warrants	(c) Number of Securities Remaining Available for Future Issuance Under Equity Compensation Plans (Excluding Securities Reflected in Column (a))
Equity compensation plans approved by security holders[1]	266,514	$3.96	937,558
Equity compensation plans not approved by security holders[2]	2,051,475	$3.46	—
Total	2,317,989	$3.52	937,558

(1) Represents options issued pursuant to the: (i) AdCare Health Systems, Inc. 2011 Stock Incentive Plan and (ii) 2005 Stock Option Plan of AdCare Health Systems, Inc. which were all approved by our shareholders.

(2) Represents warrants issued outside of our shareholder approved plans as described below. The warrants listed below contain certain anti-dilution adjustments and therefore were adjusted for stock dividends in October 2010, October 2011, and October 2012, as applicable. The share numbers below reflect all such applicable adjustments.

- On November 16, 2007, we issued to our Board and members of our management team ten-year warrants, as adjusted for stock dividends, exercises and forfeitures, to purchase an aggregate 766,847 shares of our common stock at exercise prices ranging from $1.04 to $3.43.
- On September 24, 2009, we issued to Christopher Brogdon, as inducement to become our Chief Acquisition Officer, an eight-year warrant, as adjusted, to purchase 347,288 shares of our common stock at exercise prices ranging from $2.59 to $4.32.
- On May 2, 2011, we issued to Noble Financial, as partial consideration for providing certain financing to the Company, a five-year warrant, as adjusted, to purchase 55,125 shares of our common stock at an exercise price of $4.08.
- On December 19, 2011, we issued to David Rubenstein, as inducement to become our Chief Operating Officer, ten-year warrants, as adjusted for stock dividends and forfeitures, to purchase an aggregate 174,993 shares of our common stock at exercises prices ranging from $3.93 to $4.73.
- On December 28, 2012, we issued to Strome Alpha Offshore, Ltd., as partial consideration for providing certain financing to the Company, a ten-year warrant to purchase 50,000 shares of our common stock at an exercise price of $3.80.
- On May 15, 2013, we issued to Ronald W. Fleming, as an inducement to become our Chief Financial Officer, a ten-year warrant, as adjusted for forfeitures, to purchase 23,333 shares of our common stock at an exercise price of $5.90, which vests as to one-third of the underlying shares of each of the successive three anniversaries of the issue date.
- On November 26, 2013, we issued to an investor relations firm, as partial consideration for providing certain investor relations services to the Company, a ten-year warrant to purchase 10,000 shares of our common stock at an exercise price of $3.96.
- On March 28, 2014, we issued to the placement agents in the Company’s offering of the Subordinated Convertible Promissory Notes Issued in 2014 ("2014 Notes"), as partial compensation for serving as placement agents in such offering, five-year warrants to purchase an aggregate of 48,889 shares of common stock at an exercise price of $4.50 per share.
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On October 10, 2014, we issued to William McBride III, as an inducement to become our Chief Executive Officer, a ten-year warrant to purchase 300,000 shares of our common stock at an exercise price per share of $4.49, which vests as to one-third of the underlying shares on each of the successive three anniversaries of the issue date.

- On February 20, 2015, David Tenwick, director, sold 109,472 fully vested and unexercised warrants for a total sale price of $281,343 to Park City Capital Offshore Master, Ltd., an affiliate of director Michael J. Fox.
- On April 1, 2015, we issued to Allan J. Rimland, as an incentive to become our President and Chief Financial Officer, a ten-year warrant to purchase 275,000 shares of common stock at an exercise price per share equal to $4.25 which shall vest as to one-third of the underlying shares on each of the three subsequent anniversaries of the issue date.

Item 6. Selected Financial Data

Disclosure pursuant to Item 6 of Form 10-K is not required to be provided by smaller reporting companies.

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Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations

Overview

The Company is a self-managed real estate investment company that invests primarily in real estate purposed for long-term care and senior living. Our business primarily consists of leasing and subleasing such facilities to third-party tenants. As of December 31, 2015, the Company owned, leased, or managed for third parties 38 facilities primarily in the Southeast. The operators of the Company's facilities provide a range of health care and related services to patients and residents, including skilled nursing and assisted living services, social services, various therapy services, and other rehabilitative and healthcare services for both long-term and short-stay patients and residents.

We were incorporated in Ohio on August 14, 1991, under the name Passport Retirement, Inc. In 1995, we acquired substantially all of the assets and liabilities of AdCare Health Systems, Inc. and changed our name to AdCare Health Systems, Inc. AdCare completed its initial public offering in November 2006. Initially based in Ohio, we expanded our portfolio through a series of strategic acquisitions to include properties in a number of other states, primarily in the Southeast. In 2012, we relocated our executive offices and accounting operations to Georgia, and AdCare changed its state of incorporation from Ohio to Georgia on December 12, 2013.

Historically, our business focused on owning, leasing and operating skilled nursing and assisted living facilities. The Company also managed certain facilities on behalf of unaffiliated long-term care operators and owners and operators with whom we entered into management contracts. In July 2014, the Board approved a strategic plan to transition the Company to a healthcare property holding and leasing company through a series of leasing and subleasing transactions. As of December 31, 2015, we completed the Transition through: (i) leasing to third-party operators all of the healthcare properties which we own and previously operated; (ii) subleasing to third-party operators all of the healthcare properties which we lease (but do not own) and previously operated; and (iii) continuing in effect the one remaining management agreement to manage two skilled nursing facilities and one assisted living facility.

We lease our currently-owned healthcare properties, and sublease our currently-leased healthcare properties, on a triple-net basis, meaning that the lessee (i.e., the new third-party operator of the property) is obligated under the lease or sublease, as applicable, for all liabilities of the property in respect to insurance, taxes and facility maintenance, as well as the lease or sublease payments, as applicable. These leases are generally long-term in nature with renewal options and annual escalation clauses. The Company has many of the characteristics of a REIT. The Board is analyzing and considering: (i) whether and, if so, when, we could satisfy the requirements to qualify as a REIT under the Code; (ii) the structural and operational complexities which would need to be addressed before the we could qualify as a REIT, including the disposition of certain assets or the termination of certain operations which may not be REIT compliant; and (iii) if we were to qualify as a REIT, whether electing REIT status would be in the best interests of the Company and its shareholders in light of various factors, including our significant consolidated federal net operating losses of approximately $58.3 million as of December 31, 2015. There is no assurance that the Company will qualify as a REIT in future taxable years or, if it were to so qualify, that the Board would determine that electing REIT status would be in the best interests of the Company and its shareholders.

As a result of the Transition, the Company is now focused on the ownership, acquisition and leasing of healthcare related properties.

On March 29, 2016, the Company announced that given that the transition to a healthcare property holding and leasing company is complete, the Board of Directors has begun to explore strategic alternatives for the Company.

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The following table provides summary information regarding the number of facilities and related beds/units as of December 31, 2015:

	Owned		Leased		Managed for Third Parties		Total	
	Facilities	Beds/Units	Facilities	Beds/Units	Facilities	Beds/Units	Facilities	Beds/Units
State								
Arkansas	9	958	—	—	—	—	9	958
Alabama	2	304	—	—	—	—	2	304
Georgia	4	463	10	1,168	—	—	14	1,631
North Carolina	1	106	—	—	—	—	1	106
Ohio	4	279	1	94	3	332	8	705
Oklahoma	2	197	—	—	—	—	2	197
South Carolina	2	180	—	—	—	—	2	180
Total	24	2,487	11	1,262	3	332	38	4,081
Facility Type								
Skilled Nursing	22	2,375	11	1,262	2	249	35	3,886
Assisted Living	2	112	—	—	—	—	2	112
Independent Living	—	—	—	—	1	83	1	83
Total	24	2,487	11	1,262	3	332	38	4,081

Liquidity

At December 31, 2015, we had $2.7 million in cash and cash equivalents as well as restricted cash of $12.7 million. Over the next twelve months, we anticipate both access to and receipt of several sources of liquidity, including cash flows from operations, and sales of preferred stock pursuant to an At-The-Market shelf registration. We routinely have ongoing discussions with existing and potential new lenders to refinance current debt on a longer term basis and, in recent periods, have refinanced shorter term acquisition debt, including seller notes, with traditional longer term mortgage notes, some of which have been executed under government guaranteed lending programs. During 2016, we anticipate net proceeds of approximately $9.1 million on the refinancing of existing debt with such government guaranteed lending programs. At December 31, 2015, we had $125.5 million in indebtedness of which the current portion is $51.0 million. We anticipate our operating cash requirements in 2016 as being less than in 2015 due to the completion of the Transition. We expect sufficient funds for our operations, scheduled debt service, at least through the next twelve months. We have been successful in recent years in raising new equity capital and believe, based on recent discussions, that these markets will continue to be available to us for raising capital in 2016 and beyond. We believe our long-term liquidity needs will be satisfied by these same sources, as well as borrowings as required to refinance indebtedness.

On March 24, 2016, the Company received a commitment to refinance the Bentonville, Heritage Park and River Valley Credit Facility, the Little Rock Credit Facility, and the Northridge, Woodland Hills and Abington Credit Facility for a combined total of $25.4 million of debt, subject to definitive documentation and certain closing conditions. On March 24, 2016, the Company also obtained a lender commitment to extend the maturity date of the Georgetown and Sumter Credit Facility from September 2016 to June 2017 subject to definitive documentation and certain closing conditions. On March 29, 2016, the Company obtained a lender commitment to extend the maturity date of the Quail Creek Credit facility from September 2016 to September 2018 subject to definitive documentation and certain closing conditions.

For a more detailed discussion, see Note 3 - Liquidity and Profitability and Note 14 Preferred Stock and Dividends, located in Part II, Item 8., Notes to Consolidated Financial Statements.

Acquisitions

The Company had no acquisitions during the years ended December 31, 2015 or 2014.

Divestitures

For information regarding the Company's divestitures, please refer to Note 11 - Discontinued Operations, located in Part II, Item 8., Notes to Consolidated Financial Statements of this Annual Report on Form 10-K.

The following table summarizes the activity of discontinued operations for the years ended December 31, 2015 and 2014:

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	For the year ended December 31,	
(Amounts in 000's)	2015	2014
Total revenues	$87,920	$222,104
Cost of services	$89,783	$188,952
Net (loss) income	$(4,892)	$23,783
Interest expense, net	$(1,510)	$(1,152)
Income tax benefit (expense)	$(251)	$253
Gain on disposal of assets	$1,251	$—

Critical Accounting Policies

We prepare our financial statements in accordance with accounting principles generally accepted in the United States ("GAAP"). The preparation of these financial statements requires us to make estimates and judgments that affect the reported amount of assets, liabilities, revenues and expenses. On an ongoing basis we review our judgments and estimates, including, but not limited to, those related to doubtful accounts, income taxes, stock compensation, intangible assets and loss contingencies. We base our estimates on historical experience, business knowledge and on various other assumptions that we believe to be reasonable under the circumstances at the time. Actual results may vary from our estimates. These estimates are evaluated by management and revised as circumstances change. We believe that the following represents our critical accounting policies.

Consolidation of Entities in Which We Have Determined to Have a Controlling Financial Interest

Arrangements with other business enterprises are evaluated, and those in which AdCare is determined to have controlling financial interest are consolidated. Guidance is provided by Financial Accounting Standards Board Accounting Standards Codification ("ASC") Topic 810-10, Consolidation—Overall, which addresses the consolidation of business enterprises to which the usual condition of consolidation (ownership of a majority voting interest) does not apply. This interpretation focuses on controlling financial interests that may be achieved through arrangements that do not involve voting interests. It concludes that, in absences of clear control through voting interests, a company's exposure (variable interest) to the economic risks and potential rewards from the variable interest entity's assets and activities are the best evidence of control. If an enterprise holds the power to direct and right to receive benefits of an entity, it would be considered the primary beneficiary. The primary beneficiary is required to consolidate the assets, liabilities and results of operations of the variable interest entity in its financial statements.

On November 20, 2015, Riverchase Village ADK, LLC (“Riverchase”) completed the previously announced sale to an unrelated third party of the Riverchase Village facility, an assisted living facility located in Hoover, Alabama, for a purchase price (as subsequently amended) of $6.9 million. Riverchase was a consolidating variable interest entity of the Company which is owned by Christopher F. Brogdon, a former director of the Company and a greater than 5% beneficial holder of the Company’s common stock. Riverchase financed the acquisition of the Riverchase Village facility using the proceeds of the Riverchase Bonds, as to which the Company was a guarantor.

In connection with the sale of the Riverchase Village facility, the Riverchase Bonds were repaid in full and the Company was released from its guaranty. In addition, the Company no longer holds a purchase option for the Riverchase facility. Management determined that the Company was no longer the primary beneficiary and that the Riverchase variable interest entity should be deconsilidated from the Company's consolidated financial statements at December 31, 2015. At deconsolidation, an eliminated intercompany balance of approximately $1.6 million consisting of operating losses sustained from 2010-2013, which were funded by AdCare and recognized in the Company's consolidated statements of operations from 2010-2013 attributable to the non-controlling interest in 2010-2013, were re-attributed to AdCare’s shareholders

We have evaluated and concluded that as of December 31, 2015, we have no relationship with a variable interest entity in which we are the primary beneficiary required to consolidate the entity.

Revenue Recognition

Triple-Net Leased Properties. Our triple-net leases provide for periodic and determinable increases in rent. We recognize rental revenues under these leases on a straight-line basis over the applicable lease term when collectibility is reasonably assured. Recognizing rental income on a straight-line basis generally results in recognized revenues

during the first half of a lease term exceeding the cash amounts contractually due from our tenants, creating a straight-line rent receivable that is included in other assets on our consolidated balance sheets.

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Other. We recognize management fee revenues received under various contractual agreements with third-party companies. Further, we recognize interest income from lease inducements receivables and capital loans as made to tenants.

Allowances. We assess the collectibility of our rent receivables, including straight-line rent receivables. We base our assessment of the collectibility of rent receivables (other than straight-line rent receivables) on several factors, including, payment history, the financial strength of the tenant and any guarantors, the value of the underlying collateral, and current economic conditions. If our evaluation of these factors indicates it is probable that we will be unable to recover the full value of the receivable, we provide a reserve against the portion of the receivable that we estimate may not be recovered. If our evaluation of these factors indicates it is probable that we will be unable to receive the rent payments due in the future, we provide a reserve against the recognized straight-line rent receivable asset for the portion that we estimate may not be recovered. If we change our assumptions or estimates regarding the collectibility of future rent payments required by a lease, we may adjust our reserve to increase or reduce the rental revenue recognized in the period we make such change in our assumptions or estimates.

At December 31, 2015, we allowed for approximately $12.5 million on approximately $20.9 million of gross patient care related receivables. Allowance for patient care receivables are estimated based on an aged bucket method incorporating different payor types. All patient care receivables exceeding 365 days are fully allowed at December 31, 2015.

Asset Impairment

The Company reviews the carrying value of long-lived assets that are held and used in our operations for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. Recoverability of these assets is determined based upon expected undiscounted future net cash flows from the operations to which the assets relate, utilizing management’s best estimate, assumptions, and projections at the time. If the carrying value is determined to be unrecoverable from future operating cash flows, the asset is deemed impaired and an impairment loss would be recognized to the extent the carrying value exceeded the estimated fair value of the asset. We estimate the fair value of assets based on the estimated future discounted cash flows of the asset. Management has evaluated its long-lived assets and has identified asset impairment during the years ended December 31, 2015 and 2014.

The Company tests indefinite-lived intangible assets for impairment on an annual basis or more frequently if events or changes in circumstances indicate that the carrying amount of the intangible asset may not be recoverable. Goodwill represents the excess of the purchase price over the fair value of identifiable net assets acquired in business combinations. Goodwill is subject to annual testing for impairment. In addition, goodwill is tested for impairment if events occur or circumstances change that would reduce the fair value of a facility below its carrying amount. The Company performs its annual test for impairment during the fourth quarter of each year (see Note 6 - Intangible Assets and Goodwill to our Consolidated Financial Statements included in Part II, Item 8., "Financial Statements and Supplementary Data.").

The Company's asset impairment analysis is consistent with the fair value measurements described in ASC Topic 820, Fair Value Measurements and Disclosures. During the year ended December 31, 2014, the Company recorded an impairment of $1.8 million related to an adjustment to the fair value less the cost to sell the 102-bed nursing facility located in Tulsa, Oklahoma. During the year ended December 31, 2015, the Company recognized impairment charges of approximately $0.5 million and $0.1 million to write down the carrying value of its two office buildings located in Roswell, Georgia and one office building located in Rogers, Arkansas, respectively (see Note 11 - Discontinued Operations to our Consolidated Financial Statements included in Part II, Item 8., "Financial Statements and Supplementary Data"). The impairment charges represent the difference between fair values from the carrying value.

Stock-Based Compensation

The Company follows the provisions of ASC Topic 718, Compensation - Stock Compensation ("ASC 718"), which requires the measurement and recognition of compensation expense for all share-based payment awards either modified or granted to employees, non-employees, and directors based upon estimated fair values. The

Black-Scholes-Merton option-pricing model, consistent with the provisions of ASC 718, was used to determine the fair value of each option and warrant granted. Option valuation models require the input of highly subjective assumptions, including the expected stock price volatility. The Company uses projected volatility rates, which are based upon historical volatility rates, trended into future years. Because the Company's stock options have characteristics significantly different from those of traded options, and because changes in the subjective input assumptions can materially affect the fair value estimate, in management’s opinion, the existing models do not necessarily provide a reliable single measure of the fair value of our options.

Income Taxes

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As required by ASC Topic 740, Income Taxes ("ASC 740"), the Company establishes deferred tax assets and liabilities for temporary differences between the financial reporting basis and the tax basis of our assets and liabilities at tax rates in effect when such temporary differences are expected to reverse. When necessary, we record a valuation allowance to reduce our net deferred tax assets to the amount that is more likely than not to be realized. At December 31, 2015, the Company has a valuation allowance of approximately $24.6 million. In future periods, we will continue to assess the need for and adequacy of the remaining valuation allowance. ASC 740 provides information and procedures for financial statement recognition and measurement of tax positions taken, or expected to be taken, in tax returns.

In determining the need for a valuation allowance, the annual income tax rate, or the need for and magnitude of liabilities for uncertain tax positions, we make certain estimates and assumptions. These estimates and assumptions are based on, among other things, knowledge of operations, markets, historical trends and likely future changes and, when appropriate, the opinions of advisors with knowledge and expertise in certain fields. Due to certain risks associated with our estimates and assumptions, actual results could differ.

In October 2014, the Georgia Department of Revenue ("GDOR") initiated an examination of the Company's Georgia income tax returns and net worth returns for the 2010, 2011, 2012, and 2013 tax years. To date, the GDOR has not proposed any adjustments.

The Company is not currently under examination by any other major income tax jurisdiction.

Recently Issued Accounting Pronouncements

The information required by this Item is provided in Note 1 - Summary of Significant Accounting Policies to our Consolidated Financial Statements included in Part II, Item 8., "Financial Statements and Supplementary Data."

Results of Operations

Year Ended December 31, 2015 and 2014

The following table sets forth, for the periods indicated, statement of operations items and the amount and percentage of change of these items. The results of operations for any particular period are not necessarily indicative of results for any future period. The following data should be read in conjunction with our consolidated financial statements and the notes thereto, which are included herein.

Given the Company's transition to a healthcare property holding and leasing company during 2014 and 2015, the amounts presented below are not reflective of our ongoing annualized performance due to leasing activity throughout the periods.

Certain reclassifications have been made to the 2014 financial information to conform to the 2015 presentation with no effect on the Company's consolidated financial position or results of operations. These reclassifications did not affect total assets, total liabilities, or stockholders' equity. Reclassifications were made to the Consolidated Statements of Operations for the year ended December 31, 2014 to reflect the same facilities in discontinued operations for both periods presented.

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(Amounts in 000's)	Year Ended December 31, 2015	2014	Increase (Decrease) Amount	Percent
Revenues:				
Rental revenues	$17,254	$1,832	$15,422	841.8 %
Management fee revenues	910	1,493	(583)	(39.1)%
Other revenues	236	—	236	100.0 %
Total revenues	18,400	3,325	15,075	453.4 %
Expenses:				
General and administrative expenses	10,544	15,696	(5,152)	(32.8)%
Facility rent expense	5,758	1,512	4,246	280.8 %
Depreciation and amortization	7,345	7,393	(48)	(0.7)%
Other operating expenses	2,394	2,922	(528)	(18.1)%
Total expenses	26,041	27,523	(1,482)	(5.4)%
Income (loss) from operations	(7,641)	(24,198)	16,557	(68.4)%
Other Income (Expense):				
Interest expense, net	(8,462)	(10,677)	2,215	(20.8)%
Loss on extinguishment of debt	(680)	(1,803)	1,123	(62.3)%
Loss on legal settlement	—	(600)	600	(100.0)%
Other expense	(918)	(779)	(139)	17.8 %
Total other expense, net	(10,060)	(13,859)	3,799	(27.4)%
Loss from continuing operations before income taxes	(17,701)	(38,057)	20,356	(53.5)%
Income tax expense	(110)	(131)	21	(16.0)%
Loss from continuing operations	$(17,811)	$(38,188)	$20,377	(53.4)%
(Loss) income from discontinued operations, net of tax	$(4,892)	$23,783	$(28,675)	(120.6)%
Net loss	$(22,703)	$(14,405)	$(8,298)	57.6 %

Year Ended December 31, 2015 Compared to Year Ended December 31, 2014:

Rental Revenues—Total rental revenue increased by $15.4 million, or 841.8%, to $17.3 million for the year ended December 31, 2015, compared with $1.8 million for the year ended December 31, 2014. The increase reflects the Company's continuing transition to a healthcare property holding and leasing company in 2015 and accordingly an increase in leasing of facilities to third-party operators. As of December 31, 2015, we have leased or subleased all of our facilities. As of December 31, 2014, we had leased three owned and five subleased skilled nursing and rehabilitation facilities.

Management Fee Revenues—Management revenues decreased by $0.6 million, or 39.1%, to $0.9 million for the year ended December 31, 2015, compared with $1.5 million for the year ended December 31, 2014. The decrease is primarily due to the discontinuance of management agreements effective as of March 1, 2014 and December 31, 2014 (see Note 18 - Related Party Transactions to our Consolidated Financial Statements included in Part II, Item 8., "Financial Statements and Supplementary Data").

Other revenues—Total other revenues increased by $0.2 million, or 100%, to $0.2 million for the year ended December 31, 2015. The $0.2 million increase is primarily due to interest income on lease inducement receivables.

General and Administrative—General and administrative costs decreased by $5.2 million or 32.8%, to $10.5 million for the year ended December 31, 2015, compared with $15.7 million for the year ended December 31, 2014. The net decrease is primarily due to the following: (i) a decrease in salaries, wages and employee benefits expense of approximately $4.2 million, partially offset by an increase in contract services expense of approximately $0.6 million; (ii) a decrease of $0.4 million in legal expenses; (iii) a decrease of approximately $0.2 million in stock-based compensation; (iv) a decrease of approximately $0.4 million in travel and other reimbursable expenses; (v) a decrease of approximately $0.2 million in IT-related expenses; and (vi) a decrease of approximately $0.3 million in director fees and related expenses.

Facility Rent Expense—Facility rent expense increased by $4.2 million or 280.8%, to $5.8 million for the year ended December 31, 2015, compared with $1.5 million for the year ended December 31, 2014. The increase is primarily due to lease extensions and

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amendments entered into during the year ended December 31, 2015 (see Note 7 - Leases, located in Part I, Item 1., Notes to Consolidated Financial Statements). On account of the Transition, the facility rent expense presented for 2015 and 2014 are not reflective of our ongoing annualized performance due to leasing activity throughout the periods.

Depreciation and Amortization—Depreciation and amortization decreased by $0.05 million or 0.7%, to $7.3 million for the year ended December 31, 2015, compared with $7.4 million for the year ended December 31, 2014. The decrease is primarily due to certain assets becoming fully depreciated for the year ended December 31, 2015. The decrease is partially offset by impairment charges incurred by the Company during the years ended December 31, 2015.

Other operating expenses—Other operating expense decreased by $0.5 million or 18.1%, to $2.4 million for the year ended December 31, 2015, compared with $2.9 million for the year ended December 31, 2014. The decrease is primarily due to a decrease in salary continuation costs of $2.8 million related to the Transition, partially offset by allowance increases for a potentially uncollectible note and lease inducement of an aggregate $2.1 million and other costs of approximately $0.2 million.

Interest Expense, net—Interest expense, net decreased by $2.2 million or 62.3%, to $8.5 million for the year ended December 31, 2015, compared with $10.7 million for the year ended December 31, 2014. The decrease is primarily due to the extinguishment of certain debt and refinancing of certain loan agreements to more favorable terms (for further information, see Item 8, Notes to Consolidated Financial Statements - Note 9 - Notes Payable and Other Debt, of this Annual Report).

Loss on Debt Extinguishment—Loss on extinguishment of debt decreased by $1.1 million or 62.3%, to $0.7 million for the year ended December 31, 2015, compared with $1.8 million for the year ended December 31, 2014. The decrease is primarily due to the February 2015 issuance of promissory notes related to the refinancing of certain loan agreements with one of our lenders (for further information, see Note 9 - Notes Payable and Other Debt, located in Part II, Item 8., Notes to Consolidated Financial Statements).

Other Expense— Other expense increased by $0.1 million or 17.8%, to $0.9 million for the year ended December 31, 2015, compared with $0.8 million for the year ended December 31, 2014. The increase is primarily due to additional costs the Company incurred during the year ended December 31, 2015 associated with the Transition.

Liquidity and Capital Resources

At December 31, 2015, we had $2.7 million in cash and cash equivalents as well as restricted cash of $12.7 million. Over the next twelve months, we anticipate both access to and receipt of several sources of liquidity, including cash flows from operations, and sales of preferred stock pursuant to an At-The-Market shelf registration. We routinely have ongoing discussions with existing and new potential lenders to refinance current debt on a long-term basis and, in recent periods, have refinanced short-term acquisition-related debt with traditional long-term mortgage notes, some of which have been executed under government guaranteed lending programs.

At December 31, 2015, we had $125.5 million in indebtedness of which the current portion is $51.0 million. Over the next twelve months, we anticipate net principal disbursements of approximately $46.4 million (inclusive of a debt pay-down of approximately $5.5 million using current restricted cash, $1.4 million of amortization on shorter term vendor notes, $3.1 million of routine debt service amortization, and a $0.7 million payment of other debt) which reflect the offset of anticipated proceeds on refinancing of approximately $38.5 million.

We anticipate our operating cash requirements in 2016 as being less than in 2015 due to the Company's completed Transition. Based on the described sources of liquidity, we expect sufficient funds for our operations and scheduled debt service, at least through the next twelve months. We have been successful in recent years in raising new equity capital and believe, based on recent discussions, that these markets will continue to be available to us for raising capital in 2016 and beyond. We believe our long-term liquidity needs will be satisfied by these same sources, as well as borrowings as required to refinance indebtedness (for a more detailed discussion, see Note 3 - Liquidity and Profitability, located in Part II, Item 8., Notes to Consolidated Financial Statements).

The following table presents selected data from our consolidated statement of cash flows for the periods presented:

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	Year Ended December 31,	
Amounts in (000's)	2015	2014
Net cash used in operating activities—continuing operations	$(11,727)	$(23,915)
Net cash (used in) provided by operating activities—discontinued operations	(6,079)	17,780
Net cash (used in) provided by investing activities—continuing operations	(5,749)	1,605
Net cash provided by (used in) investing activities—discontinued operations	15,594	(1,489)
Net cash provided by (used in) financing activities—continuing operations	12,703	(2,359)
Net cash used in financing activities—discontinued operations	(12,757)	(261)
Net Change in Cash	(8,015)	(8,639)
Cash, Beginning	10,735	19,374
Cash, Ending	$2,720	$10,735

Year Ended December 31, 2015

Net cash used in operating activities—continuing operations for the year ended December 31, 2015, was approximately $11.7 million consisting primarily of our loss from operations less changes in working capital, and noncash charges (primarily depreciation and amortization, share-based compensation, rent revenue in excess of cash received, and amortization of debt discounts and related deferred financing costs) all primarily the result of routine operating activity. Net cash used in operating activities—discontinued operations was approximately $6.1 million due primarily to a $18.5 million decrease in accounts payable and accrued liabilities offset by noncash charges.

Net cash used in investing activities—continuing operations for the year ended December 31, 2015, was approximately $5.7 million. This is primarily the result of a increase in restricted cash deposits offset by lower capital expenditures. Net cash provided by investing activities—discontinued operations was approximately $15.6 million primarily due to proceeds of $13.9 million related to the sale of Companions, Bentonville, and Riverchase.

Net cash provided by financing activities—continuing operations was approximately $12.7 million for the year ended December 31, 2015. This is primarily the result of cash proceeds received from additional debt borrowings and preferred stock issuances partially offset by repayments of existing debt obligations and payments of preferred stock dividends. Net cash used in financing activities - discontinued operations was approximately $12.8 million due to the payoff of loans related to the entities sold, Companions, Bentonville, and Riverchase.

Year Ended December 31, 2014

Net cash used in operating activities—continuing operations for the year ended December 31, 2014, was $23.9 million consisting primarily of our loss from continuing operations less changes in working capital, and noncash charges (primarily depreciation and amortization, share-based compensation, and amortization of debt discounts and related deferred financing costs) all primarily the result of routine operating activity. Net cash provided by operating activities—discontinued operations was approximately $17.8 million consisting primarily of our income from discontinued operations of $23.8 million less changes in working capital, and noncash charges (primarily depreciation and amortization and bad debt expense) all primarily the result of routine operating activity.

Net cash provided by investing activities—continuing operations for the year ended December 31, 2014, was approximately $1.6 million. This is primarily the result of a decrease in restricted cash deposits offset to a lesser extent by capital expenditures. Net cash used in investing activities—discontinued operations was approximately $1.5 million for the year ended December 31, 2014 consisting primarily of capital expenditures.

Net cash used in financing activities—continuing operations was approximately $2.4 million for the year ended December 31, 2014. This is primarily the result of proceeds received from additional debt borrowings offset to a greater extent by repayments of existing debt obligations and payments of preferred stock dividends. Net cash used in financing activities—discontinued operations was approximately $0.3 million consisting of payment of debt issuance costs and repayments of existing debt obligations.

Notes Payable and Other Debt

Notes payable and other debt consists of the following:

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	December 31,	
Amounts in (000's)	2015	2014
Revolving credit facilities and lines of credit	$—	$6,832
Senior debt—guaranteed by HUD [a]	25,469	26,022
Senior debt—guaranteed by USDA [a]	26,463	27,128
Senior debt—guaranteed by SBA [a]	3,548	3,703
Senior debt—bonds, net of discount [b]	7,025	12,967
Senior debt—other mortgage indebtedness [c] [d]	51,128	60,277
Other debt	2,638	430
Convertible debt	9,200	14,000
Total	125,471	151,359
Less current portion	50,960	22,012
Less: portion included in liabilities of variable interest entity held for sale [b]	—	5,956
Less: portion included in liabilities of disposal group held for sale [c]	958	5,197
Less: portion included in liabilities of disposal group held for use [d]	—	4,035
Notes payable and other debt, net of current portion	$73,553	$114,159

[a] United States Department of Housing and Urban Development ("HUD"), United States Department of Agriculture ("USDA"), Small Business Administration ("SBA")

[b] The senior debt - bonds, net of discount included $6.0 million at December 31, 2014 related to revenue bonds issued by the Medical Clinical Board of the City of Hoover in the State of Alabama to the Company's consolidated VIE, Riverchase. On November 20, 2015, the Company completed the sale of the Riverchase facility financed with such bonds to an unrelated third-party.

[c] At December 31, 2014, the senior debt - other mortgage indebtedness included $5.0 million related to the outstanding loan entered into in conjunction with the acquisition of Companions, a skilled nursing facility located in Tulsa, Oklahoma, as well as a related $0.2 million outstanding line of credit balance. On October 30, 2015, the Company completed the sale of Companions. At December 31, 2015, the senior debt - other mortgage indebtedness includes $1.0 million related to the outstanding loan on one of the two office buildings located in Roswell, Georgia.

[d] At December 31, 2014, the senior debt - other mortgage indebtedness included $4.0 million related to the outstanding loans entered into in conjunction with the acquisition of a skilled nursing facility located in Bentonville, Arkansas and one of the two office buildings located in Roswell, Georgia. During the twelve months ended December 31, 2015, the Bentonville, Arkansas facility was sold and the outstanding loan on the office building in Roswell, Georgia was reclassified to liabilities held for sale.

For a detailed description of each of the Company's debt financings, please see Note 9 - Notes Payable and Other Debt to our Consolidated Financial Statements included in Part II, Item 8., "Financial Statements and Supplementary Data".

Scheduled Maturities

The schedule below summarizes the scheduled maturities as of December 31, 2015 for each of the next five years and thereafter.

	Amounts in (000's)
2016	$51,918
2017	12,580
2018	1,800
2019	1,848
2020	1,945
Thereafter	55,585
Subtotal	125,676
Less: unamortized discounts	(205)
Total notes payable and other debt	$125,471

Debt Covenant Compliance

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As of December 31, 2015, the Company has approximately 38 credit related instruments outstanding that include various financial and administrative covenant requirements. Covenant requirements include, but are not limited to, fixed charge coverage ratios, debt service coverage ratios, minimum EBITDA or EBITDAR, current ratios and tangible net worth requirements. Certain financial covenant requirements are based on consolidated financial measurements whereas others are based on other levels (i.e. facility, multiple facilities or a combination of subsidiaries comprising less than the Company's consolidated financial measurements). Covenants are based on annual or quarterly financial metric measurements. The Company routinely tracks and monitors its compliance with its covenant requirements. In recent periods, including as of December 31, 2015, the Company has not been in compliance with certain financial and administrative covenants. For each instance of such non-compliance, the Company has obtained waivers or amendments to such requirements including as necessary modifications to future covenant requirements or the elimination of certain requirements in future periods.
The table below indicates which of the Company's credit-related instruments were not in compliance as of December 31, 2015:

Credit Facility	Balance at December 31, 2015 (000's)	Entity	Financial Covenant	Measurement Period	Min/Max Financial Covenant Required	Financial Covenant Metric Achieved		Future Financial Covenant Metric Required
Community Bank - Mountain Trace Nursing ADK, LLC - USDA	$ 4,507	Subsidiary	Minimum Debt Service Coverage Ratio	Quarterly	1.0	0.5	*	1.0
PrivateBank - Mortgage Note - Valley River Nursing, LLC; Park Heritage Nursing, LLC; Benton Nursing, LLC	$ 7,359	Operator	Minimum EBITDAR (000s)	Quarterly	$265	$36	*	$265
		Guarantor	Minimum Debt Service Coverage Ratio	Annual	1.0	0.4	*	1.0
Private Bank - Mortgage Note - Little Rock HC&R Nursing, LLC	$ 11,399	Operator	Minimum EBITDAR (000s)	Quarterly	$450	$23	*	$450
		Guarantor	Minimum Debt Service Coverage Ratio	Annual	1.0	0.4	*	1.0
		Guarantor	Maximum Annual Leverage Ratio	Annual	11	222	*	11
PrivateBank - Mortgage Note - APH&R Property Holdings, LLC; Northridge HC&R Property Holdings, LLC; Woodland Hills HC Property Holdings, LLC	$ 11,816	Operator	Minimum EBITDAR (000s)	Quarterly	$495	$(601)	*	$495
		Guarantor	Minimum Debt Service Coverage Ratio	Annual	1.0	0.4	*	1.0
		Guarantor		Annual	11.0	222	*	11.0

			Maximum Annual Leverage Ratio					
PrivateBank - Mortgage Note - Georgetown HC&R Property Holdings, LLC; Sumter Valley HC&R Property Holdings, LLC	$ 9,149	Operator	Minimum Debt Service Coverage Ratio	Quarterly	1.8	1.1	*	1.8
		Guarantor	Minimum Debt Service Coverage Ratio	Annual	1.0	0.4	*	1.0
		Guarantor	Maximum Annual Leverage Ratio	Annual	11	222	*	11
Congressional Bank - Mortgage Note - QC Property Holdings, LLC	$ 5,000	Subsidiary	Minimum Fixed Charge Coverage Ratio	Quarterly	1.1	(0.5)	*	1.1
		Subsidiary	Minimum Debt Service Coverage Ratio	Annual	1.5	(1.1)	*	1.5

* Waiver or amendment for violation of covenant obtained.

Receivables

Our operations could be adversely affected if we experience significant delays in receipt of rental income from our operators. Our future liquidity will continue to be dependent upon the relative amounts of current assets (principally cash and accounts receivable)

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and current liabilities (principally accounts payable and accrued expenses). In that regard, accounts receivable can have a significant impact on our liquidity.

Accounts receivable totaled $8.8 million at December 31, 2015 compared to $24.3 million at December 31, 2014, of which $8.0 million and $24.2 million, respectively, related to patient care receivables from our legacy operations. The allowance for bad debt was $12.5 million and $6.7 million at December 31, 2015 and 2014, respectively. We continually evaluate the adequacy of our bad debt reserves based on aging of older balances, payment terms and historical collection trends after facility operations transfer to third-party operators. We continue to evaluate and implement additional processes to strengthen our collection efforts and reduce the incidence of uncollectible accounts.

Off-Balance Sheet Arrangements

Letters of Credit

There were $0.4 million and $3.8 million of outstanding letters of credit at December 31, 2015 and 2014, respectively, that are pledged as collateral of borrowing capacity on the PrivateBank revolver.

Operating Leases

The Company leases a total of eleven skilled nursing facilities under non-cancelable leases, most of which have rent escalation clauses and provisions for payments of real estate taxes, insurance and maintenance costs; each of the skilled nursing facilities that are leased by the Company are subleased to and operated by third-party operators. The Company also leases certain office space located in Atlanta, Georgia.

Future minimum lease payments for each of the next five years ending December 31, are as follows:

	(Amounts in 000's)
2016	$8,083
2017	8,181
2018	8,346
2019	8,526
2020	8,697
Thereafter	55,320
Total	$97,153

The Company has also entered into lease agreements for various equipment used in its day-to-day operations. These leases are included in future minimum lease payments above. For a detailed description of the Company's operating leases, please see Note 7 - Leases to our Consolidated Financial Statements included in Part II, Item 8., "Financial Statements and Supplementary Data".

Leased and Subleased Facilities to Third-Party Operators

In connection with the Company's transition to a self-managed real estate investment company, thirty-five facilities (twenty-four owned by us and eleven leased to us) are leased or subleased on a triple net basis, meaning that the lessee (i.e., the new third-party operator of the property) is obligated under the lease or sublease, as applicable, for all liabilities of the property in respect to insurance, taxes and facility maintenance, as well as the lease or sublease payments, as applicable.

Future minimum lease receivables for each of the next five years ending December 31, are as follows:

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	(Amounts in 000's)
2016	$26,052
2017	26,845
2018	27,474
2019	28,082
2020	27,634
Thereafter	204,913
Total	$341,000

The following is a summary of the Company's leases and subleases to third-parties and which comprise the future minimum lease receivable of the Company. Each lease or sublease is structured as a "triple-net" lease. For those facilities where the Company subleases, the renewal option in the sublease agreement is dependent on the Company renewal of its lease agreement. Generally, the sublease agreements are cross-defaulted where applicable for subleases of multiple facilities by the same lessor.

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Facility Name	Operator Affiliation	Initial Lease Term Commencement Date	Initial Lease Term Expiration Date	Initial Annual Rent (Thousands)
Owned				
Cumberland H&R	Aria Health Group LLC	5/1/2015	4/30/2030	$540
Heritage Park	Aria Health Group LLC	5/1/2015	4/30/2030	240
Homestead Manor	Aria Health Group LLC	5/1/2015	4/30/2030	120
Little Rock H&R	Aria Health Group LLC	5/1/2015	4/30/2030	1,602
Northridge Health	Aria Health Group LLC	5/1/2015	4/30/2030	420
River Valley Health	Aria Health Group LLC	11/1/2015	4/30/2030	480
Stone County ALF	Aria Health Group LLC	5/1/2015	4/30/2030	60
Stone County Nursing	Aria Health Group LLC	5/1/2015	4/30/2030	838
Woodland Hills	Aria Health Group LLC	5/1/2015	4/30/2030	480
Eaglewood ALF	Beacon Health Management	8/1/2015	7/31/2025	720
Eaglewood Care Center	Beacon Health Management	8/1/2015	7/31/2025	720
H&C of Greenfield	Beacon Health Management	8/1/2015	7/31/2025	360
Southland Healthcare	Beacon Health Management	11/1/2014	10/31/2024	900
The Pavilion Care Center	Beacon Health Management	8/1/2015	7/31/2025	360
Attalla Health Care	C.R. Management	12/1/2014	8/31/2030	1,080
Autumn Breeze	C.R. Management	9/30/2015	9/30/2025	840
College Park	C.R. Management	4/1/2015	3/31/2020	600
Coosa Valley Health Care	C.R. Management	12/1/2014	8/31/2030	900
Glenvue H&R	C.R. Management	7/1/2015	6/30/2025	1,140
NW Nursing Center	Southwest LTC	12/31/2015	11/30/2025	300
Quail Creek	Southwest LTC	12/31/2015	11/30/2025	660
Georgetown Health	Symmetry Healthcare	4/1/2015	3/31/2030	288
Mountain Trace Rehab	Symmetry Healthcare	6/1/2015	5/31/2030	648
Sumter Valley Nursing	Symmetry Healthcare	4/1/2015	3/31/2030	770
Subtotal Owned Facilities (24)				$15,066
Leased				
Covington Care	Beacon Health Management	8/1/2015	4/30/2025	$780
Lumber City	Beacon Health Management	11/1/2014	8/31/2027	840
LaGrange	C.R. Management	4/1/2015	8/31/2027	960
Thomasville N&R	C.R. Management	7/1/2014	8/31/2027	324
Jeffersonville	New Beginnings Care	11/1/2015	7/31/2020	648
Oceanside	New Beginnings Care	11/1/2015	7/31/2020	421
Savannah Beach	New Beginnings Care	11/1/2015	7/31/2020	247
Bonterra	Wellington Health Services	9/1/2015	8/31/2025	1,020
Parkview Manor/Legacy	Wellington Health Services	9/1/2015	8/31/2025	1,020
Powder Springs	Wellington Health Services	4/1/2015	8/31/2027	2,100
Tara	Wellington Health Services	4/1/2015	8/31/2027	1,800
Subtotal Leased Facilities (11)				$10,160
Total (35)				$25,226

All facilities are skilled nursing facilities except for Stone County and Eaglewood which are assisted living facilities and Spring Meade Residence which is an independent living facility. All facilities have renewal provisions of one term of five years except facilities (Mountain Trace, Quail Creek, NW Nursing, Sumter Valley, and Georgetown) which have two renewal terms with each being five years. The leases also contain standard rent escalations that range from 2% to 3.5% annually.

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AdCare subleased through its subsidiaries nine facilities located in Arkansas to affiliates of Aria Health Group, LLC pursuant to separate sublease agreements. Eight of the Aria subleases commenced on May 1, 2015 and one sublease commenced on November 1, 2015. Effective February 3, 2016, each sublease was terminated due to the failure to pay rent pursuant to the terms of such sublease. Subsequently, on February 5, 2016, the Company entered into a Master Lease Agreement, as amended, with Skyline Healthcare LLC to lease the facilities commencing April 1, 2016. (See Part II, Item 8, Financial Statements and Supplemental Data, Note 19, Subsequent Events).

On January 22, 2016, New Beginnings filed a petition to reorganize its finances under the Bankruptcy Code. To date, New Beginnings has neither affirmed nor rejected the Master Lease entered into on November 3, 2015 with respect to the Jeffersonville, Oceanside, and Savannah Beach facilities. The Company is in discussions with New Beginnings and other potential operators about renting such facilities.

In March 2016, the CMS decertified the Jeffersonville facility meaning the facility can no longer accept Medicare or Medicaid patients. The operator is considering appealing the decision by CMS.

ITEM 7A. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

Disclosure pursuant to Item 7A. of Form 10-K is not required to be reported by smaller reporting companies.

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Item 8. Financial Statements and Supplementary Data

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Report of Independent Registered Public Accounting Firm
The Board of Directors and Stockholders
AdCare Health Systems, Inc.:
We have audited the accompanying consolidated balance sheets of AdCare Health Systems, Inc. and subsidiaries as of December 31, 2015 and 2014, and the related consolidated statements of operations, stockholders' equity, and cash flows for each of the years then ended. These consolidated financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (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. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of AdCare Health Systems, Inc. and subsidiaries as of December 31, 2015 and 2014, and the results of their operations and their cash flows for each of the years then ended, in conformity with U.S. generally accepted accounting principles.
/s/ KPMG LLP
Atlanta, Georgia
March 30, 2016

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ADCARE HEALTH SYSTEMS, INC. AND SUBSIDIARIES
CONSOLIDATED BALANCE SHEETS
(Amounts in 000's except share data)

	December 31, 2015	2014
ASSETS		
Current Assets:		
Cash and cash equivalents	$2,720	$10,735
Restricted cash and investments	9,169	3,321
Accounts receivable, net of allowance of $12,487 and $6,708	8,805	24,294
Prepaid expenses and other	3,214	1,746
Deferred tax asset	—	569
Assets of disposal group held for sale	1,249	5,813
Assets of disposal group held for use	—	4,592
Assets of variable interest entity held for sale	—	5,924
Total current assets	25,157	56,994
Restricted cash and investments	3,558	5,456
Property and equipment, net	126,676	130,993
Intangible assets—bed licenses	2,471	2,471
Intangible assets—lease rights, net	3,420	4,087
Goodwill	4,183	4,224
Lease deposits	1,812	1,683
Deferred financing costs, net	2,913	3,464
Other assets	1,795	590
Total assets	$171,985	$209,962
LIABILITIES AND EQUITY		
Current Liabilities:		
Current portion of notes payable and other debt	$50,960	$2,436
Current portion of convertible debt	—	14,000
Revolving credit facilities and lines of credit	—	5,576
Accounts payable	8,741	16,434
Accrued expenses	3,125	15,653
Liabilities of disposal group held for sale	958	5,197
Liabilities of disposal group held for use	—	4,035
Liabilities of variable interest entity held for sale	—	5,956
Total current liabilities	63,784	69,287
Notes payable and other debt, net of current portion:		
Senior debt	56,871	106,089
Bonds, net	6,940	7,011
Convertible debt	9,200	—
Revolving credit facilities and lines of credit	—	1,059
Other debt	542	—
Other liabilities	3,380	2,130
Deferred tax liability	389	605
Total liabilities	141,106	186,181
Commitments and contingencies (Note 15)		

Preferred stock, no par value; 5,000 and 5,000 shares authorized; 2,427 and 950 shares issued and outstanding, redemption amount $60,273 and $23,750 at December 31, 2015 and 2014, respectively	54,714	20,392
Stockholders' equity:		
Common stock and additional paid-in capital, no par value; 55,000 shares authorized; 19,861 and 19,151 shares issued and outstanding at December 31, 2015 and 2014, respectively	60,958	61,896
Accumulated deficit	(84,793)	(56,067)
Total stockholders' equity (deficit)	(23,835)	5,829
Noncontrolling interest in subsidiary	—	(2,440)
Total equity (deficit)	(23,835)	3,389
Total liabilities and equity (deficit)	$171,985	$209,962

See accompanying notes to consolidated financial statements

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ADCARE HEALTH SYSTEMS, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF OPERATIONS
(Amounts in 000's, except share and per share data)

	Year Ended December 31,	
	2015	2014
Revenues:		
Rental revenues	$17,254	$1,832
Management fee revenues	910	1,493
Other revenues	236	—
Total revenues	18,400	3,325
Expenses:		
General and administrative expenses	10,544	15,696
Facility rent expense	5,758	1,512
Depreciation and amortization	7,345	7,393
Other operating expenses	2,394	2,922
Total expenses	26,041	27,523
Loss from operations	(7,641)	(24,198)
Other Income (Expense):		
Interest expense, net	(8,462)	(10,677)
Loss on extinguishment of debt	(680)	(1,803)
Loss on legal settlement	—	(600)
Other expense	(918)	(779)
Total other expense, net	(10,060)	(13,859)
Loss from continuing operations before Income taxes	(17,701)	(38,057)
Income tax expense	(110)	(131)
Loss from continuing operations	(17,811)	(38,188)
Income (loss) from discontinued operations, net of tax	(4,892)	23,783
Net loss	(22,703)	(14,405)
Net (income) loss attributable to noncontrolling interests	(815)	806
Net loss attributable to AdCare Health Systems, Inc.	(23,518)	(13,599)
Preferred stock dividends	(5,208)	(2,584)
Net loss attributable to AdCare Health Systems, Inc. common stockholders	$(28,726)	$(16,183)
Net loss per share of common stock attributable to AdCare Health Systems, Inc		
Basic and diluted:		
Continuing Operations	$(1.17)	$(2.27)
Discontinued Operations	(0.29)	1.37
	$(1.46)	$(0.90)
Weighted average shares of common stock outstanding:		
Basic and diluted	19,680	17,930

See accompanying notes to consolidated financial statements

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ADCARE HEALTH SYSTEMS, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY
(Amounts in 000's)

	Shares	Common Stock and Additional Paid-in Capital	Accumulated Deficit	Noncontrolling Interest in Subsidiary	Total
Balance, December 31, 2013	16,016	$48,370	$(39,884)	$ (1,634)	$6,852
Stock-based compensation expense	—	1,155	—	—	1,155
Exercises of options and warrants	1,073	3,257	—	—	3,257
Stock issued for converted debt and interest	1,861	8,706	—	—	8,706
Nonemployee warrants issued for services	—	321	—	—	321
Nonemployee warrants issued in conjunction with debt offering	—	87	—	—	87
Issuance of restricted stock, net of forfeitures	201	—	—	—	—
Preferred stock dividends	—	—	(2,584)	—	(2,584)
Net (loss)	—	—	(13,599)	(806)	(14,405)
Balance, December 31, 2014	19,151	61,896	(56,067)	(2,440)	3,389
Stock-based compensation expense	—	942	—	—	942
Exercises of options and warrants	527	1,791	—	—	1,791
Nonemployee warrant cancellation	—	(320)	—	—	(320)
Issuance of restricted stock, net of forfeitures	183	—	—	—	—
Reclass of share-based award to liability	—	(75)	—	—	(75)
Common stock dividends	—	(3,276)	—	—	(3,276)
Preferred stock dividends	—	—	(5,208)	—	(5,208)
Net income (loss)	—	—	(23,518)	815	(22,703)
Deconsolidation of noncontrolling interest	—	—	—	1,625	1,625
Balance, December 31, 2015	19,861	$60,958	$(84,793)	$ —	$(23,835)

See accompanying notes to consolidated financial statements

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ADCARE HEALTH SYSTEMS, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CASH FLOWS
(Amounts in 000's)

	Year Ended December 31,	
	2015	2014
Cash flows from operating activities:		
Net Loss	$(22,703)	$(14,405)
Loss from discontinued operations	4,892	(23,783)
Loss from continuing operations	(17,811)	(38,188)
Adjustments to reconcile net loss from continuing operations to net cash used in operating activities:		
Depreciation and amortization	7,345	7,393
Warrants (cancelled) issued for services	(320)	408
Stock-based compensation expense	942	1,155
Reclass of restricted stock	(75)	—
Rent expense in excess of cash paid	162	209
Rent revenue in excess of cash received	(1,211)	(21)
Amortization of deferred financing costs	1,149	2,122
Amortization of debt discounts and premiums	14	(9)
Loss on debt extinguishment	680	1,803
Deferred tax expense	102	98
Loss on disposal of assets	—	7
Provision for bad debts	2,132	—
Changes in certain assets and liabilities, net of acquisitions:		
Accounts receivable	(2,220)	369
Prepaid expenses and other	(2,029)	(653)
Other assets	(127)	(554)
Accounts payable and other liabilities	(460)	1,946
Net cash used in operating activities—continuing operations	(11,727)	(23,915)
Net cash (used in) provided by operating activities—discontinued operations	(6,079)	17,780
Net cash used in operating activities	(17,806)	(6,135)
Cash flow from investing activities:		
Change in restricted cash and investments	(3,950)	5,744
Purchase of property and equipment	(1,799)	(4,139)
Net cash (used in) provided by investing activities—continuing operations	(5,749)	1,605
Net cash provided by (used in) investing activities—discontinued operations	15,594	(1,489)
Net cash provided by investing activities	9,845	116
Cash flows from financing activities:		
Proceeds from debt	22,757	25,716
Proceeds from convertible debt	2,049	6,055
Repayment on notes payable	(25,652)	(24,905)
Repayment on bonds payable	—	(2,994)
Repayment on convertible debt	(6,849)	(4,094)
Proceeds from lines of credit	28,310	69,874
Repayment on lines of credit	(34,944)	(71,590)
Debt issuance costs	(598)	(1,044)
Exercise of options and warrants	1,791	3,257
Proceeds from preferred stock issuances	34,323	—
Other	—	(50)

Dividends on common stock	(3,276)	—
Dividends paid on preferred stock	(5,208)	(2,584)
Net cash provided by (used in) financing activities—continuing operations	12,703	(2,359)
Net cash used in financing activities—discontinued operations	(12,757)	(261)
Net cash provided by (used in) financing activities	(54)	(2,620)
Net change in cash	(8,015)	(8,639)
Cash, beginning	10,735	19,374
Cash, ending	$2,720	$10,735
Supplemental Disclosure of Cash Flow Information:		
Cash paid during the year for:		
Interest	$8,367	$9,859
Income taxes	$8	$33
Supplemental Disclosure of Non-Cash Activities:		
Payments for 2015 Notes received from 2014 Note holders	$5,651	$—
2011 Notes surrendered and cancelled in payment for 2014 Notes	$—	$445
Land received in settlement of note receivable	$—	$640
Conversion of debt to equity	$—	$6,930
Warrants issued in conjunction with convertible debt offering	$—	$87
Notes issued in conjunction with financing of exit fees	$680	$—
Non-cash discounts to financed insurance	$721	$14

See accompanying notes to consolidated financial statements

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ADCARE HEALTH SYSTEMS, INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
NOTE 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES
Description of Business
AdCare Health Systems, Inc. (“AdCare”), through its subsidiaries (together, the “Company” or “we”), is a self-managed real estate investment company that invests primarily in real estate purposed for long-term healthcare and senior living. Our business primarily consists of leasing and subleasing such facilities to third-party tenants, which operate the facilities. As of December 31, 2015, the Company owned, leased, or managed for third parties 38 facilities primarily in the Southeast. The operators of the Company's facilities provide a range of health care services to patients and residents, including skilled nursing and assisted living services, social services, various therapy services, and other rehabilitative and healthcare services for both long-term and short-stay patients and residents.

The Company was incorporated in Ohio on August 14, 1991, under the name Passport Retirement, Inc. In 1995, the Company acquired substantially all of the assets and liabilities of AdCare Health Systems, Inc. and changed its name to AdCare Health Systems, Inc. AdCare completed its initial public offering in November 2006. Initially based in Ohio, the Company expanded its portfolio through a series of strategic acquisitions to include properties in a number of other states, primarily in the Southeast. In 2012, the Company relocated its executive offices and accounting operations to Georgia, and AdCare changed its state of incorporation from the Ohio to Georgia on December 12, 2013.
Historically, the Company's business focused on owning and operating skilled nursing and assisted living facilities. The Company also managed facilities on behalf of unaffiliated owners with whom the Company entered into management contracts. In July 2014, the Company's Board of Directors (the “Board”) approved a strategic plan to transition (the “Transition”) the Company to a healthcare property holding and leasing company through a series of leasing and subleasing transactions. As of December 31, 2015, the Company completed the Transition through: (i) leasing to third-party operators all of the healthcare properties which it owns and previously operated; (ii) subleasing to third-party operators all of the healthcare properties which it leases (but does not own) and previously operated; and (iii) continuing the one remaining management agreement to manage two skilled nursing facilities and one independent living facility for third parties.

The Company leases its currently-owned healthcare properties, and subleases its currently-leased healthcare properties, on a triple-net basis, meaning that the lessee (i.e., the new third-party operator of the property) is obligated under the lease or sublease, as applicable, for all costs of operating the properties including insurance, taxes and facility maintenance, as well as the lease or sublease payments, as applicable. These leases are generally long-term in nature with renewal options and annual escalation clauses. As a result of the Transition, the Company now has many of the characteristics of a real estate investment trust ("REIT") and is now focused on the ownership, acquisition and leasing of healthcare related properties. The Board is analyzing and considering: (i) whether and, if so, when, we could satisfy the requirements to qualify as a REIT under the Internal Revenue Code of 1986, as amended (the “Code”); (ii) the structural and operational complexities which would need to be addressed before we could qualify as a REIT, including the disposition of certain assets or the termination of certain operations which may not be REIT compliant; and (iii) if we were to qualify as a REIT, whether electing REIT status would be in the best interests of the Company and its shareholders in light of various factors, including our significant consolidated Federal net operating loss carryforwards of approximately $58.3 million as of December 31, 2015. There is no assurance that the Company will qualify as a REIT in future taxable years or, if it were to so qualify, that the Board would determine that electing REIT status would be in the best interests of the Company and its shareholders.

As of December 31, 2015, the Company owns, leases, or manages 38 facilities primarily in the Southeast. Of the 38 facilities, the Company: (i) leased 22 owned and subleased 11 leased skilled nursing facilities to third-party operators; (ii) leased two owned assisted living facilities to third-party operators; and (iii) managed on behalf of third-party owners two skilled nursing facilities and one assisted living facility (see Note 7 - Leases for a full description of the

Company's leases).

Basis of Presentation

The accompanying consolidated financial statements are prepared in conformity with U.S. generally accepted accounting principles ("GAAP") in accordance with the Financial Accounting Standards Board ("FASB") Accounting Standards Codification ("ASC").

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Use of Estimates

The preparation of consolidated financial statements in conformity with GAAP requires management to make certain estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the consolidated financial statements and the reported results of operations during the reporting period. Examples of significant estimates include allowance for doubtful accounts, contractual allowances for Medicaid, Medicare, and managed care reimbursements, deferred tax valuation allowance, fair value of derivative instruments, fair value of employee and nonemployee stock based awards, fair value estimation methods used to determine the assigned fair value of assets and liabilities acquired in acquisitions, valuation of goodwill and other long-lived assets, and cash flow projections. Actual results could differ materially from those estimates.

Principles of Consolidation

The consolidated financial statements include the Company's majority owned and controlled subsidiaries. All intercompany transactions and balances have been eliminated through consolidation. For subsidiaries that are not wholly owned by the Company, the portions not controlled by the Company are presented as non-controlling interests in the consolidated financial statements.

Arrangements with other business enterprises are evaluated, and those in which AdCare is determined to have controlling financial interest are consolidated. Guidance is provided by FASB ASC Topic 810-10, Consolidation—Overall, which includes consolidation of business enterprises to which the usual condition of consolidation (ownership of a majority voting interest) does not apply. This guidance includes controlling financial interests that may be achieved through arrangements that do not involve voting interests. In absences of clear control through voting interests, a company's exposure (variable interest) to the economic risks and potential rewards from the variable interest entity's assets and activities are the best evidence of control. If an enterprise holds the power to direct and right to receive benefits of an entity, it would be considered the primary beneficiary. The primary beneficiary is required to consolidate the assets, liabilities and results of operations of the variable interest entity in its financial statements.

The Company has evaluated and concluded that as of December 31, 2015, they have no relationship with a variable interest entity ("VIE") in which they are the primary beneficiary required to consolidate the entity.

Reclassifications

Certain reclassifications have been made to the 2014 financial information to conform to the 2015 presentation with no effect on the Company's consolidated financial position or results of operations. These reclassifications did not affect total assets, total liabilities, or stockholders' equity. Reclassifications were made to the Balance Sheet as of December 31, 2014 and the consolidated statements of operations and consolidated statements of cash flows for the year ended December 31, 2014 to reflect the same facilities in discontinued operations for both periods presented.

Cash, Cash Equivalents, and Restricted Cash and Investments

The Company considers all unrestricted short-term investments with original maturities less than three months, which are readily convertible into cash, to be cash equivalents. Certain cash, cash equivalents and investment amounts are restricted for specific purposes such as mortgage escrow requirements, reserves for capital expenditures on United States Housing and Urban Development ("HUD") insured facilities and collateral for other debt obligations.

Revenue Recognition

Triple-Net Leased Properties. The Company's triple-net leases provide for periodic and determinable increases in rent. The Company recognizes rental revenues under these leases on a straight-line basis over the applicable lease term when collectibility is reasonably assured. Recognizing rental income on a straight-line basis generally results in recognized revenues during the first half of a lease term exceeding the cash amounts contractually due from our tenants, creating a straight-line rent receivable that is included in other assets on our consolidated balance sheets.

Management Fee Revenue and Other. The Company recognizes management fee revenues as services are provided. Further, the Company recognizes interest income from lease inducements receivables and loans made to tenants.

Allowances. The Company assesses the collectibility of our rent receivables, including straight-line rent receivables. The Company bases its assessment of the collectibility of rent receivables on several factors, including, payment

history, the financial strength of the tenant and any guarantors, the value of the underlying collateral, and current economic conditions. If the Company's evaluation of these factors indicates it is probable that the Company will be unable to receive the rent payments, the Company provides a reserve against the recognized straight-line rent receivable asset for the portion that we estimate may not be recovered. If the Company changes its assumptions or estimates regarding the collectibility of future rent payments required by a lease, the Company

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may adjust its reserve to increase or reduce the rental revenue recognized in the period the Company makes such change in its assumptions or estimates.

At December 31, 2015, the Company allowed for approximately $12.5 million on approximately $20.9 million of gross patient care related receivables primarily from our operations before completion of our Transition. Allowance for patient care receivables are estimated based on an aged bucket method incorporating different payor types. All patient care receivables exceeding 365 days are fully allowed at December 31, 2015. The increase in the reserves for patient care is primarily included in discontinued operations.

Concentrations of Credit Risk

Financial instruments which potentially expose the Company to concentrations of credit risk consist primarily of cash and cash equivalents, restricted cash, restricted investments, accounts receivable and straight-line rent receivable. Cash and cash equivalents, restricted cash and restricted investments are held with various financial institutions. From time to time, these balances exceed the federally insured limits. These balances are maintained with high quality financial institutions which management believes limits the risk.

Accounts receivable are recorded at net realizable value. The Company performs ongoing evaluations of its tenants and significant third-party payors with which they contract, and generally does not require collateral. The Company maintains an allowance for doubtful accounts which management believes is sufficient to cover potential losses. Delinquent accounts receivable are charged against the allowance for doubtful accounts once likelihood of collection has been determined. Accounts receivable are considered to be past due and placed on delinquent status based upon contractual terms, how frequently payments are received, and on an individual account basis.

Property and Equipment

Property and equipment are stated at cost. Expenditures for major improvements are capitalized. Depreciation commences when the assets are placed in service. Maintenance and repairs which do not improve or extend the life of the respective assets are charged to expense as incurred. Upon disposal of assets, the cost and related accumulated depreciation are removed from the accounts and any gain or loss is recorded. Depreciation is recorded on a straight-line basis over the estimated useful lives of the respective assets. Property and equipment also includes bed license intangibles for states other than Ohio (where the building and bed license are deemed complimentary assets) and are amortized over the life of the building. The Company reviews property and equipment for potential impairment whenever events or changes in circumstances indicate that the carrying amounts of assets may not be recoverable.

Leases and Leasehold Improvements

The Company leases certain facilities and equipment for use in its day-to-day operations. At the inception of each lease, the Company performs an evaluation to determine whether the lease should be classified as an operating lease or capital lease. As of December 31, 2015, all of the Company's leased facilities are accounted for as operating leases. For operating leases that contain scheduled rent increases, the Company records rent expense on a straight-line basis over the term of the lease. The lease term is also used to provide the basis for establishing depreciable lives for leasehold improvements.

Intangible Assets and Goodwill

Intangible assets consist of finite lived and indefinite lived intangibles. The Company's finite lived intangibles include lease rights and certain certificate of need ("CON") and bed licenses that are not separable from the associated buildings. Finite lived intangibles are amortized over their estimated useful lives. For the Company's lease related intangibles, the estimated useful life is based on the terms of the underlying facility leases averaging approximately ten years. For the Company's CON/bed licenses that are not separable from the buildings, the estimated useful life is based on the building life when acquired with an average estimated useful life of approximately 32 years. The Company evaluates the recoverability of the finite lived intangibles whenever an impairment indicator is present.

The Company's indefinite lived intangibles consist primarily of values assigned to CON/bed licenses that are separable from the buildings. The Company does not amortize goodwill or indefinite lived intangibles. On an annual basis, the Company evaluates the recoverability of the indefinite lived intangibles and goodwill by performing an impairment test. The Company performs its annual test for impairment during the fourth quarter of each year. For the

year ended December 31, 2015, the test results indicated no impairment necessary.

Deferred Financing Costs

The Company records deferred financing costs associated with debt obligations as an asset. Costs are amortized over the term of the related debt using the straight-line method and are reflected as interest expense. The straight-line method yields results substantially similar to those that would be produced under the effective interest rate method.

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Income Taxes and Uncertain Tax Positions

Deferred tax assets or liabilities are recognized for the estimated future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective income tax basis. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. The effect on deferred tax assets and liabilities of a change in tax rates is recognized in the period that included the enactment date. Deferred tax assets are also recognized for the future tax benefits from net operating loss and other carry forwards. Valuation allowances are recorded for deferred tax assets when the recoverability of such assets is not deemed more likely than not.

Judgment is required in evaluating uncertain tax positions. The Company determines whether it is more likely than not that a tax position will be sustained upon examination. If a tax position meets the more-likely-than-not recognition threshold it is measured to determine the amount of benefit to recognize in the financial statements. The Company classifies unrecognized tax benefits that are not expected to result in payment or receipt of cash within one year as non-current liabilities in the consolidated balance sheets. The Company is subject to income taxes in the U.S. and numerous state and local jurisdictions. In general, the Company's tax returns filed for the 1998 through 2015 tax years are still subject to potential examination by taxing authorities.

In early 2014, the Internal Revenue Service ("IRS") initiated an examination of the Company's income tax return for the 2011 income tax year. On May 7, 2014, the IRS completed and closed the examination and no changes were required to the Company's 2011 income tax return.

In October 2014, the Georgia Department of Revenue ("GDOR") initiated an examination of the Company's Georgia income tax returns and net worth returns for the 2010, 2011, 2012, and 2013 tax years. To date, the GDOR has not proposed any adjustments.

The Company is not currently under examination by any other major income tax jurisdiction.

Stock Based Compensation

The Company follows the provisions of ASC topic 718 “Compensation - Stock Compensation”, which requires the use of the fair-value based method to determine compensation for all arrangements under which employees, non-employees, and others receive shares of stock or equity instruments (options, warrants or restricted shares). All awards are amortized on a straight-line basis over their vesting terms.

Fair Value Measurements and Financial Instruments

Accounting guidance establishes a three-level valuation hierarchy for disclosure of fair value measurements. The valuation hierarchy is based upon the transparency of inputs to the valuation of an asset or liability as of the measurement date. The categorization of a measurement within the valuation hierarchy is based upon the lowest level of input that is significant to the fair value measurement. The three levels are defined as follows:

Level 1— Quoted market prices in active markets for identical assets or liabilities

Level 2— Other observable market-based inputs or unobservable inputs that are corroborated by market data

Level 3— Significant unobservable inputs

The respective carrying value of certain financial instruments of the Company approximates their fair value. These instruments include cash and cash equivalents, restricted cash and investments, accounts receivable, notes receivable, and accounts payable. Fair values were assumed to approximate carrying values for these financial instruments since they are short-term in nature and their carrying amounts approximate fair values, they are receivable or payable on demand, or the interest rates earned and/or paid approximate current market rates.

Self-Insurance

The Company was self-insured for employee medical claims (in all states except for Oklahoma, where the Company participates in the Oklahoma state subsidy program) and had a large deductible workers' compensation plan (in all states except for Ohio, where workers' compensation is covered under a premium-only policy provided by the Ohio Bureau of Workers' Compensation). Additionally, the Company maintains insurance programs, including general and professional liability, property, casualty, directors' and officers' liability, crime, automobile, employment practices liability and earthquake and flood.

In 2015, the insurance program changed with the needs of the company and the transition of operations. The Workers Compensation transitioned from a high deductible to a guaranteed cost program in February 2015. Professional liability insurance was provided

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to facilities operations up until the date of transfer when new operators insurance substituted for new claims. Claims which were associated with prior operations of the company but not reported as of the transition date were self-insured.

The Company's prior facility operations subject it to certain liability risks which may result in malpractice claims being asserted against the Company if its services are alleged to have resulted in patient injury or other adverse effects. The Company is self-insured with respect to such claims (see Note 8 - Accrued Expenses).

The company maintains a running self-insurance reserve accrual based on outstanding claims obtained from quarterly loss runs provided by the carrier.

As of December 31, 2015, claims incurred but not reported or unsettled claims for the legacy self-insured employee medical plan and the large deductible workers' compensation plan are recognized as a liability in the consolidated financial statements.

Recently Issued Accounting Pronouncements

Except for rules and interpretive releases of the Securities and Exchange Commission ("SEC") under authority of federal securities laws, FASB ASC is the sole source of authoritative GAAP literature applicable to the Company. The Company has reviewed the FASB accounting pronouncements and Accounting Standards Update ("ASU") interpretations that have effectiveness dates during the periods reported and in future periods.

In April 2014, the FASB issued ASU 2014-08, which amends the definition of a discontinued operation to include only those disposals of components of an entity that represent a strategic shift that has (or will have) a major effect on an entity’s operations and financial results. This ASU should be applied prospectively and is effective for the Company for the 2015 annual and interim reporting periods. Early adoption is permitted for disposals that have not been reported in financial statements previously issued. The Company adopted this ASU January 1, 2015.

In May 2014, the FASB issued ASU 2014-09 guidance which requires revenue to be recognized in an amount that reflects the consideration expected to be received in exchange for those goods and services. The new standard requires the disclosure of sufficient quantitative and qualitative information for financial statement users to understand the nature, amount, timing and uncertainty of revenue and associated cash flows arising from contracts with customers. The new guidance does not affect the recognition of revenue from leases. In August 2015, the FASB delayed the effective date of the new revenue standard by one year. As a result, this new revenue standard is effective for annual reporting periods beginning after December 15, 2017, including interim periods within those reporting periods. Early application is permitted under the original effective date of fiscal years, and interim periods within those fiscal years, beginning after December 15, 2016. The Company is currently evaluating the impact on the Company's financial position and results of operations and related disclosures.

In August 2014, the FASB issued ASU 2014-15, which provides guidance regarding an entity’s ability to continue as a going concern, which requires management to assess a company’s ability to continue as a going concern and to provide related footnote disclosures in certain circumstances. Before this new standard, there was minimal guidance in GAAP specific to going concern. Under the new standard, disclosures are required when conditions give rise to substantial doubt about a company’s ability to continue as a going concern within one year from the financial statement issuance date. The guidance is effective for annual reporting periods beginning after December 15, 2016, including interim periods within that reporting period, with early adoption permitted. The Company has not yet determined the impact, if any, that the adoption of this new standard will have on its consolidated financial statements.

In April 2015, the FASB issued ASU 2015-03, which requires debt issuance costs to be presented as a direct reduction from the carrying amount of the debt liability, consistent with the presentation of debt discounts. The amortization of debt issuance costs will be reported as interest expense. The new standard is to be applied on a retrospective basis and reported as a change in an accounting principle. In August 2015, the FASB released clarifying guidance for debt issuance costs related to line-of-credit arrangements, which permits debt issuance costs to be presented as an asset, regardless of whether there are any outstanding borrowings on the line-of-credit arrangement. Debt issuance costs associated with a line of credit can be amortized ratably over the term of the line-of-credit arrangement. This standard is effective for annual reporting periods beginning after December 15, 2015, including interim periods within that reporting period. Early adoption is permitted for financial statements that have not been previously issued. The

Company has concluded that changes in its accounting required by this new guidance will not materially impact the Company's financial position or results of operations and related disclosures..

In September 2015, the FASB issued ASU 2015-16, which requires that an acquirer in a business combination recognize adjustments to provisional amounts that are identified during the measurement period in the reporting period in which the adjustment amounts are determined. Under this guidance the acquirer recognizes, in the same period's financial statements, the effect on earnings of changes in depreciation, amortization, or other income effects, if any, as a result of the change to the provisional amounts, calculated

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as if the accounting had been completed at the acquisition date. New disclosures are required to present separately on the face of the income statement or disclose in the notes the portion of the amount recognized in current-period earnings by line item that would have been recognized in previous reporting periods if the adjustment to the provisional amounts had been recognized as of the acquisition date. This guidance is effective for annual reporting periods beginning after December 15, 2015, including interim periods within that reporting period. At adoption, the new guidance is to be applied prospectively to adjustments to provisional amounts that occur after the effective date with earlier application permitted for financial statements that have not been issued. The Company is currently evaluating changes in its accounting required by this new standard and the impact to the Company's financial position and related disclosures.

In November 2015, the FASB issued ASU 2015 - 17 under the simplification and productivity initiative for presentation of deferred income tax liabilities and assets. This guidance simplifies the presentation of deferred income taxes such that deferred tax liabilities and assets are to be classified as noncurrent in a classified balance sheet. The update does not amend the current requirement that deferred tax liabilities and assets of a tax-paying component of an entity be offset and presented as a single amount. This guidance is effective for annual reporting periods beginning after December 15, 2016, including interim periods within that reporting period. Early adoption is permitted as of the beginning of an interim or annual reporting period and may be applied either prospectively to all deferred tax liabilities and assets or retrospectively to all periods presented. The Company has elected to early adopt, prospectively, the new guidance as of the balance sheet date. At December 31, 2015, the adoption resulted in a reclassification from current to noncurrent deferred tax assets of $6.2 million before consideration of the related valuation allowance. with the net amount presented as noncurrent deferred tax liability. The Company did not have any reclasses of the deferred tax liability amounts.Prior periods are not retrospectively adjusted under the prospective adoption.

In January 2016, the FASB issued ASU 2016-01 which provides revised accounting guidance related to the accounting for and reporting of financial instruments. This guidance significantly revises an entity’s accounting related to (i) the classification and measurement of investments in equity securities and (ii) the presentation of certain fair value changes for financial liabilities measured at fair value. It also amends certain disclosure requirements associated with the fair value of financial instruments. The ASU is effective for annual periods and interim periods within those annual periods beginning after December 15, 2017; earlier adoption is permitted. The adoption of this guidance is not expected to have a material impact on the Company's consolidated financial condition, results of operations or cash flows.

In February 2016, the FASB issued ASU 2016-02 as a comprehensive new leases standard that amends various aspects of existing guidance for leases and requires additional disclosures about leasing arrangements. It will require companies to recognize lease assets and lease liabilities by lessees for those leases classified as operating leases under previous guidance, ASC 840, Leases. ASU 2016-02 creates a new Topic, ASC 842, Leases. This new Topic retains a distinction between finance leases and operating leases. The classification criteria for distinguishing between finance leases and operating leases are substantially similar to the classification criteria for distinguishing between capital leases and operating leases in the previous leases guidance. The ASU is effective for annual periods beginning after December 15, 2018, including interim periods within those fiscal years; earlier adoption is permitted. In the financial statements in which the ASU is first applied, leases shall be measured and recognized at the beginning of the earliest comparative period presented with an adjustment to equity. The Company is currently evaluating the impact of the adoption of this guidance on its consolidated financial condition, results of operations and cash flows.

NOTE 2. EARNINGS PER SHARE

Basic earnings per share is computed by dividing net income or loss attributable to common stockholders by the weighted-average number of shares of common stock outstanding during the period. Diluted earnings per share is similar to basic earnings per share except net income or loss is adjusted by the impact of the assumed issuance of

convertible shares and the weighted-average number of shares of common stock outstanding (which includes potentially dilutive securities, such as options, warrants, non-vested shares, and additional shares issuable under convertible notes outstanding during the period when such potentially dilutive securities are not anti-dilutive). Potentially dilutive securities from options, warrants and unvested restricted shares are calculated in accordance with the treasury stock method, which assumes that proceeds from the exercise of all options and warrants with exercise prices exceeding the average market value are used to repurchase common stock at market value. The incremental shares remaining after the proceeds are exhausted represent the potentially dilutive effect of the securities. Potentially dilutive securities from convertible promissory notes are calculated based on the assumed issuance at the beginning of the period, as well as any adjustment to income that would result from their assumed issuance. For 2015 and 2014, potentially dilutive securities of 4.5 million and 7.0 million, respectively, were excluded from the diluted loss per share calculation because including them would have been anti-dilutive in both periods.

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The following table provides a reconciliation of net loss for continuing and discontinued operations and the number of shares used in the computation of both basic and diluted earnings per share:

	Year Ended December 31,					
	2015			2014		
(Amounts in 000's, except per share data)	Loss	Shares	Per Share	(Loss) Income	Shares	Per Share
Continuing Operations:						
Loss from continuing operations	$(17,811)			$(38,188)		
Preferred stock dividends	(5,208)			(2,584)		
Basic loss from continuing operations	$(23,019)	19,680	$(1.17)	$(40,772)	17,930	$(2.27)
Diluted loss from continuing operations	$(23,019)	19,680	$(1.17)	$(40,772)	17,930	$(2.27)
Discontinued Operations:						
Income (loss) from discontinued operations	$(4,892)			$23,783		
Net (income) loss attributable to noncontrolling interests	(815)			806		
Basic (loss) income from discontinued operations attributable to the Company	$(5,707)	19,680	$(0.29)	$24,589	17,930	$1.37
Diluted (loss) income from discontinued operations attributable to the Company	$(5,707)	19,680	$(0.29)	$24,589	17,930	$1.37
Net Loss Attributable to AdCare:						
Basic loss	$(28,726)	19,680	$(1.46)	$(16,183)	17,930	$(0.90)
Diluted loss	$(28,726)	19,680	$(1.46)	$(16,183)	17,930	$(0.90)

(1) Securities outstanding that were excluded from the computation, prior to the use of the treasury stock method, because they would have been anti-dilutive are as follows:

	December 31,	
(Amounts in 000’s)	2015	2014
Stock options	267	934
Common stock warrants - employee	1,887	1,689
Common stock warrants - nonemployee	164	1,028
Shares issuable upon conversion of convertible debt	2,165	3,334
Total shares	4,483	6,985

NOTE 3. LIQUIDITY AND PROFITABILITY

Sources of Liquidity

The Company continues to undertake measures to streamline its operations and cost infrastructure in connection with its new business model, including: (i) eliminating patient care services and related costs; (ii) increasing future minimum lease revenue; (iii) refinancing or repaying current maturities to reduce interest costs and reducing mandatory principal repayments through refinancing transactions with HUD or other lending sources; and (iv) reducing general and administrative expenses.

At December 31, 2015, the Company had $2.7 million in cash and cash equivalents as well as restricted cash of $12.7 million. Over the next twelve months, the Company anticipates both access to and receipt of several sources of liquidity.

At December 31, 2015, the Company had three office buildings held for sale. The Company completed the sale of one of its office spaces on February 12, 2015 for $0.3 million and expects to sell its other two office spaces by the third quarter of 2016. The office space sold on February 12, 2015 was unencumbered and the Company anticipates that the sale of the other two spaces will approximate the related obligations.

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The Company routinely has discussions with existing and new potential lenders to refinance current debt on a long-term basis and, in recent periods, has refinanced short-term acquisition-related debt with traditional long-term mortgage notes, some of which have been executed under government guaranteed lending programs.

On July 21, 2015, the Company entered into separate At Market Issuance Sales Agreements (together, the “Sales Agreements”) with each of MLV & Co. LLC and JMP Securities LLC (each, an “Agent” and together, the “Agents”), pursuant to which the Company may offer and sell, from time to time, up to 800,000 shares of the Company’s 10.875% Series A Cumulative Redeemable Preferred Stock, no par value per share and liquidation preference of $25.00 per share (the "Series A Preferred Stock"), through an “at-the-market” offering program ("ATM"). As of December 31, 2015, the Company sold 313,695 shares of Series A Preferred Stock under the ATM, generating net proceeds to the Company of approximately $6.7 million. (see Note 12 - Dividends and Preferred Stock).

On July 30, 2015, the Company amended the terms of that certain 8% subordinated convertible note, issued by the Company to Cantone Asset Management, LLC ("CAM") and due July 31, 2015, with a principal payment amount as of such date of $4.8 million to: (i) extend the maturity date with respect to $1.5 million of the principal amount of the such note to October 31, 2017; (ii) increase the interest rate from 8.0% to 10.0% per annum; and (iii) increase the conversion price from $3.97 to $4.25 per share (see Note 9 - Notes Payable and Other Debt).

Cash Requirements

At December 31, 2015, the Company had $125.5 million in indebtedness of which the current portion is $51.9 million. This current portion is comprised of the following components: (i) debt of held for sale entities of approximately $1.0 million, which includes senior debt - mortgage indebtedness; and (ii) remaining debt of approximately $51.1 million which includes senior debt - mortgage indebtedness (for a complete listing of our debt , see Note 9 - Notes Payable and Other Debt). As indicated previously, the Company routinely has discussions with existing and potential new lenders to refinance current debt on a longer term basis and, in recent periods, has refinanced shorter term acquisition debt with traditional longer term mortgage notes, some of which have been executed under government guaranteed lending programs.

The Company anticipates net principal disbursements of approximately $46.4 million (including a debt pay-down of approximately $5.5 million using current restricted cash, $1.4 million of payments on shorter term vendor notes, $3.1 million of routine debt service amortization, and a $0.7 million payment of other debt) which reflect the offset of anticipated proceeds on refinancing of approximately $38.5 million. On March 24, 2016, the Company received a lender commitment to refinance approximately$25.4 million and to extend $9.1 million of current maturities, subject to definitive documentation and certain closing conditions. On March 29, 2016, the Company received a lender commitment to extend approximately $5.0 million of current maturities, subject to definitive documentation and certain closing conditions. The Company anticipates operating cash requirements in 2016 as being substantially less than in 2015 due to the Transition. Based on the described sources of liquidity, the Company expects sufficient funds for its operations and scheduled debt service, at least through the next twelve months. On a longer term basis, at December 31, 2015, the Company has approximately $64.5 million of debt maturities due over the next two year period ending December 31, 2017. These debt maturities include $9.2 million of convertible promissory notes, which are convertible into shares of the common stock. The Company has been successful in recent years in raising new equity capital and believes based on recent discussions that these markets will continue to be available for raising capital in the future. The Company believes its long-term liquidity needs will be satisfied by these same sources, as well as borrowings as required to refinance indebtedness.

The Company has absorbed negative cash flows from operations in the past but anticipates a reversal to a positive cash flow from operations during 2016. In order to satisfy the Company's capital needs, the Company seeks to: (i) continue improving operating results through its leasing and subleasing transactions executed with favorable terms

and consistent and predictable cash flow; (ii) re-lease Arkansas facilities with a new leasing arrangement made with a new operator (iii) expand borrowing arrangements with certain lenders; (iv) refinance current debt where possible to obtain more favorable terms; and (v) raise capital through the issuance of debt or equity securities. The Company anticipates that these actions, if successful, will provide the opportunity to maintain liquidity on a short and long-term basis, thereby permitting the Company to meet our operating and financing obligations for the next twelve months. However, there is no guarantee that such actions will be successful or that anticipated operating results of the Transition. If the Company is unable to expand existing borrowing agreements, refinance current debt, or raise capital through the issuance of securities, then the Company may be required to restructure its outstanding indebtedness, implement further cost reduction initiatives or sell assets.

NOTE 4. RESTRICTED CASH AND INVESTMENTS

The following presents the Company's various restricted cash, escrow deposits and investments:

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	December 31,	
Amounts in (000's)	2015	2014
Collateral cash and certificates of deposit	$7,687	$2,302
Current replacement reserves	950	646
Escrow deposits	532	338
Other restricted cash	—	35
Total current portion	9,169	3,321
Restricted investments for other debt obligations	2,264	3,446
HUD replacement reserves	1,174	1,074
Reserves for capital improvements	120	936
Total noncurrent portion	3,558	5,456
Total restricted cash and investments	$12,727	$8,777

Collateral cash and certificates of deposit—In securing mortgage financing from certain lending institutions, the Company and certain wholly-owned subsidiaries of the Company are required to deposit cash and/or certificates of deposit to be held as collateral in accordance with the terms of the loan agreements.

Current replacement reserves—Cash reserves set aside for non-critical building repairs to be completed within the next 12 months.

Escrow deposits—In connection with financing secured through our lenders, several wholly-owned subsidiaries of the Company are required to make monthly escrow deposits for taxes and insurance.

Restricted investments for other debt obligations—In compliance with certain financing and insurance agreements, the Company and certain wholly-owned subsidiaries of the Company are required to deposit cash held as collateral by the lender or in escrow with certain designated financial institutions.

HUD replacement reserves—The regulatory agreements entered into in connection with the financing secured through HUD require monthly escrow deposits for replacement and improvement of the HUD project assets.

NOTE 5. PROPERTY AND EQUIPMENT

Property and Equipment consist of the following:

		December 31,	
(Amounts in 000's)	Estimated Useful Lives (Years)	2015	2014
Buildings and improvements	5 - 40	$128,912	$128,136
Equipment	2 - 10	13,470	13,294
Land	—	7,128	7,127
Computer related	2 - 10	2,999	2,908
Construction in process	—	390	52
		152,899	151,517
Less: accumulated depreciation and amortization		26,223	20,524
Property and equipment, net		$126,676	$130,993

For the twelve months ended December 31, 2015 and 2014, total depreciation and amortization expense was $7.3 million and $7.4 million, respectively. Total depreciation and amortization expense excludes $0.1 million and $2.1 million in 2015 and 2014, respectively, that is recognized in Loss from Discontinued Operations, net of tax. During the twelve months ended December 31, 2014, the Company recorded an impairment of $1.8 million related to an adjustment to the fair value less the cost to sell Companions 102-bed nursing facility located in Tulsa, Oklahoma. The assets and liabilities of Companions were included in Assets and Liabilities Held for Sale as of December 31, 2014. On October 30, 2015, the Company completed the sale of Companions (see Note 11 - Discontinued Operations).

During the twelve months ended December 31, 2015, the Company recognized impairment charges of approximately $0.5 million and $0.1 million to write down the carrying value of its two office buildings located in Roswell, Georgia

and one office building

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located in Rogers, Arkansas, respectively. The assets and liabilities of the office buildings are included in Assets and Liabilities Held for Sale as of December 31, 2015 (see Note 11 - Discontinued Operations).

NOTE 6. INTANGIBLE ASSETS AND GOODWILL

Intangible assets consist of the following:

(Amounts in 000's)	Bed Licenses (included in property and equipment)	Bed Licenses—Separable	Lease Rights	Total
Balances, December 31, 2013				
Gross	$37,220	$2,471	$8,824	$48,515
Accumulated amortization	(2,482)	—	(3,935)	(6,417)
Net carrying amount	$34,738	$2,471	$4,889	$42,098
Dispositions				
Gross	—	—	(1,418)	(1,418)
Accumulated amortization	—	—	1,418	1,418
Amortization expense	(1,173)	—	(802)	(1,975)
Reclass to held for sale				
Gross	(1,530)	—	—	(1,530)
Accumulated amortization	68	—	—	68
Balances, December 31, 2014				
Gross	35,690	2,471	7,406	45,567
Accumulated amortization	(3,587)	—	(3,319)	(6,906)
Net carrying amount	32,103	2,471	4,087	38,661
Dispositions				
Gross	—	—	(525)	(525)
Accumulated amortization	—	—	525	525
Amortization expense	(1,173)	—	(667)	(1,840)
Balances, December 31, 2015				
Gross	$35,690	$2,471	$6,881	$45,042
Accumulated amortization	(4,760)	—	(3,461)	(8,221)
Net carrying amount	$30,930	$2,471	$3,420	$36,821

Amortization expense for bed licenses is included in property and equipment depreciation and amortization expense (see Note 5 - Property and Equipment).

Estimated amortization expense for all finite-lived intangibles for each of the future years ending December 31 is as follows:

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Amounts in (000's)	Bed Licenses	Lease Rights
2016	$1,173	$667
2017	1,173	667
2018	1,173	667
2019	1,173	667
2020	1,173	482
Thereafter	25,065	270
Total	$30,930	$3,420

The following table summarizes the changes in the carrying amount of goodwill for the years ended December 31, 2015 and 2014.

	(Amounts in 000's)
Balances, December 31, 2013	
Goodwill	$5,023
Accumulated impairment losses	(799)
Total	$4,224
Balances, December 31, 2014	
Goodwill	$5,023
Accumulated impairment losses	(799)
Total	$4,224
Impairment loss	(41)
Net change during year	(41)
Balances, December 31, 2015	
Goodwill	$5,023
Accumulated impairment losses	(840)
Total	$4,183

On July 1, 2015, the Company completed the sale of its Bentonville Manor Nursing Home, 83-bed skilled nursing facility located in Bentonville, Arkansas ("Bentonville") for approximately $3.4 million net of closing costs. The Company wrote off the remaining goodwill of $0.04 million at the time of sale. For the year ended December 31, 2015, the Company determined that no other impairment adjustments were necessary for goodwill. The Company does not amortize goodwill or indefinite lived intangibles, which consist of separable bed licenses.

NOTE 7. LEASES

Operating Leases

The Company leases a total of eleven skilled nursing facilities from unaffiliated owners under non-cancelable leases, most of which have rent escalation clauses and provisions for payments of real estate taxes, insurance and maintenance costs; each of the skilled nursing facilities that are leased by the Company are subleased to and operated by third-party operators. The Company also leases certain office space located in Atlanta, Georgia.

Foster Prime Lease. Eight of the Company's skilled nursing facilities (collectively, the "Georgia Facilities") are leased under a single master indivisible arrangement, by and between ADK Georgia, LLC, a Georgia limited liability company and subsidiary of the Company (“ADK”), and William M. Foster ("Lessor"), as landlord (the "Prime Lease"). Under the Prime Lease, a breach at a single facility could subject one or more of the other facilities covered by the same master lease to the same default risk. In addition, other potential defaults related to an individual facility may cause a default of the entire Prime Lease. With an indivisible lease, it is difficult to restructure the composition of the portfolio or economic terms of the lease without the consent of the landlord.

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On August 14, 2015, ADK and Lessor entered into an amendment to the Prime Lease (the “Second Amendment”) whereby the parties amended the Prime Lease to extend its initial term by seven years, resulting in a new lease termination date of August 31, 2027. In consideration for the extension, among other things, the Company agreed to: (i) pay to Lessor a fee of $575,000; (ii) release to Lessor upon the earlier of January 1, 2016 or the termination of the Prime Lease one month of pre-paid rent in the amount of $398,000; (iii) release to Lessor upon the earlier of January 1, 2017 or the termination of the Prime Lease the security deposit paid under the Prime Lease in the amount of $500,000; and (iv) pay to Lessor within ten days of the end of each quarter a payment of $26,000. The annual base rent due in the first year immediately following the execution of the Second Amendment is approximately $5.3 million.

Under the Second Amendment, the Company (and not Lessor) is responsible for the cost of maintaining the Georgia Facilities, including the cost to repair or replace all structural or capital items due to ordinary wear and tear.

Pursuant to the Second Amendment: (i) Lessor consented to ADK’s sublease of the Georgia Facilities to third-party operators and ADK agreed to obtain Lessor’s consent prior to any future sublease of any of the Georgia Facilities; and (ii) the Company executed a Lease Guaranty for the benefit of Lessor whereby the Company guaranteed the performance of all of ADK’s obligations under the Prime Lease. In connection with such guaranty, the Company also consented to being primarily responsible for all of ADK’s obligations under the Prime Lease, thereby allowing Lessor to proceed directly against the Company, without having taken any prior action against ADK, should ADK be in default under the Prime Lease.

On September 9, 2015 ADK and Lessor entered into a third amendment to the Prime Lease whereby commencing on July 1, 2016 and continuing during lease years two through five, rent increases at 2% annually then increase at 2.5% annually for the remainder of the lease term. As of December 31, 2015, the Company was in compliance with all financial and administrative covenants of this lease agreement.

Bonterra/Parkview Master Lease. Two of the Company's facilities are leased under a single indivisible agreement (the "Bonterra/Parkview Master Lease"); therefore, a breach at a single facility could subject the second facility to the same default risk. On September 1, 2015, the Bonterra/Parkview Master Lease was amended (the "Bonterra/Parkview Master Lease Amendment"), whereby the parties agreed to: (i) extend its initial term by three years, resulting in a new lease termination date of August 31, 2025; (ii) provide consent to the sublease of the two facilities to a third-party operator; and (iii) extend the optional renewal terms to two separate twelve-year renewal periods. In consideration for the amended terms, among other things, the Company agreed to a monthly increase in base rent equal to 37.5% of the difference between the base rent owed by the Company under the Bonterra/Parkview Master Lease and the base rent owed to the Company by the new sublease operator. The annual base rent due in the first year immediately following the execution of the Bonterra/Parkview Master Lease Amendment is approximately $1.9 million. As of December 31, 2015, the Company was in compliance with all financial and administrative covenants of this lease agreement.

Covington Prime Lease. One of the Company's facilities is leased under an agreement dated August 26, 2002, as subsequently amended (the "Covington Prime Lease"), by and between the Company and Covington Realty, LLC. On August 1, 2015, the Covington Prime Lease was amended (the "Covington Prime Lease Amendment"), whereby the parties agreed to: (i) provide consent to the sublease of the facility to a third-party operator; (ii) extend the term of the lease to expire on April 30, 2025; and (iii) set the annual base rent, effective May 1, 2015 and continuing throughout the lease term, equal to 102% of the immediately preceding lease year's base rent. The annual base rent due in the first year immediately following the execution of the Covington Prime Lease Amendment is approximately $0.6 million. As of December 31, 2015, the Company was in compliance with all financial and administrative covenants of this lease agreement.

Future Minimum Lease Payments

Future minimum lease payments for each of the next five years ending December 31 are as follows:

	(Amounts in 000's)
2016	$8,083
2017	8,181
2018	8,346

2019	8,526
2020	8,697
Thereafter	55,320
Total	$97,153

The Company has also entered into lease agreements for various equipment used in its day-to-day operations. These leases are included in future minimum lease payments above.

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Leased and Subleased Facilities to Third-Party Operators

In connection with the Company's transition to a self-managed real estate investment company, thirty-five facilities (twenty-four owned by us and eleven leased to us) are leased or subleased on a triple net basis, meaning that the lessee (i.e., the new third-party operator of the property) is obligated under the lease or sublease, as applicable, for all costs of operating the property, including insurance, taxes and facility maintenance, as well as the lease or sublease payments, as applicable.

Future Minimum Lease Receivables

Future minimum lease receivables for each of the next five years ending December 31 are as follows:

	(Amounts in 000's)
2016	$26,052
2017	26,845
2018	27,474
2019	