Brookdale Senior Living Inc.
Form 10-Q
November 04, 2009

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

Form 10-Q

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

For the quarterly period ended September 30, 2009

or

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

For the transition period from _____________ to _____________

Commission File Number: 001-32641

BROOKDALE SENIOR LIVING INC.
(Exact name of registrant as specified in its charter)

Delaware (State or other jurisdiction of incorporation or organization)	20-3068069 (I.R.S. Employer Identification No.)
111 Westwood Place, Suite 200, Brentwood, Tennessee (Address of principal executive offices)	37027 (Zip Code)

(615) 221-2250
(Registrant's telephone number, including area code)

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 T 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 £ No £

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

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

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

As of October 30, 2009, 118,620,006 shares of the registrant's common stock, $0.01 par value, were outstanding (excluding unvested restricted shares).

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FORM 10-Q

FOR THE QUARTER ENDED SEPTEMBER 30, 2009

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PART I. FINANCIAL INFORMATION

Item 1. Financial Statements

BROOKDALE SENIOR LIVING INC.
CONDENSED CONSOLIDATED BALANCE SHEETS
(In thousands, except stock amounts)

	September 30, 2009	December 31, 2008
Assets	(Unaudited)	
Current assets		
Cash and cash equivalents	$ 159,313	$ 53,973
Cash and escrow deposits — restricted	104,434	86,723
Accounts receivable, net	81,583	91,646
Deferred tax asset	14,677	14,677
Prepaid expenses and other current assets, net	46,195	33,766
Total current assets	406,202	280,785
Property, plant and equipment and leasehold intangibles, net	3,620,469	3,697,834
Cash and escrow deposits — restricted	66,971	29,988
Investment in unconsolidated ventures	22,180	28,420
Goodwill	109,967	109,967
Other intangible assets, net	206,438	231,589
Other assets, net	69,455	70,675
Total assets	$ 4,501,682	$ 4,449,258
Liabilities and Stockholders' Equity		
Current liabilities		
Current portion of long-term debt	$ 155,397	$ 158,476
Current portion of line of credit		4,453
Trade accounts payable	42,541	29,105
Accrued expenses	184,873	170,366
Refundable entrance fees and deferred revenue	256,061	253,647
Tenant security deposits	14,920	29,965
Total current liabilities	653,792	646,012
Long-term debt, less current portion	2,304,168	2,235,000
Line of credit, less current portion		155,000
Deferred entrance fee revenue	81,221	76,410
Deferred liabilities	145,998	135,947
Deferred tax liability	159,389	178,647
Other liabilities	55,460	61,641
Total liabilities	3,400,028	3,488,657
Commitments and contingencies		
Stockholders' Equity		
Preferred stock, $0.01 par value, 50,000,000 shares authorized at September 30, 2009 and December 31, 2008; no shares issued and outstanding	—	—

Common stock, $0.01 par value, 200,000,000 shares authorized at September 30, 2009 and December 31, 2008; 124,386,194 and 106,467,764 shares issued and 123,174,893 and 105,256,463 shares outstanding (including 4,556,436 and 3,542,801 unvested restricted shares), respectively	1,232	1,053
Additional paid-in-capital	1,876,783	1,690,851
Treasury stock, at cost; 1,211,301 shares at September 30, 2009 and December 31, 2008	(29,187)	(29,187)
Accumulated deficit	(746,176)	(700,720)
Accumulated other comprehensive loss	(998)	(1,396)
Total stockholders' equity	1,101,654	960,601
Total liabilities and stockholders' equity	$4,501,682	$4,449,258

See accompanying notes to condensed consolidated financial statements.

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BROOKDALE SENIOR LIVING INC.
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS
(Unaudited, in thousands, except per share data)

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2009	2008	2009	2008
Revenue				
Resident fees	$503,856	$480,750	$1,499,544	$1,435,522
Management fees	1,987	1,527	5,002	5,604
Total revenue	505,843	482,277	1,504,546	1,441,126
Expense				
Facility operating expense (excluding depreciation and amortization of $45,851, $45,670, $137,102 and $143,765, respectively)	328,939	322,601	963,637	934,186
General and administrative expense (including non-cash stock-based compensation expense of $7,869, $6,737, $21,549 and $23,368, respectively)	34,720	32,948	100,148	109,633
Hurricane and named tropical storms expense		3,613		3,613
Facility lease expense	68,036	67,017	204,211	202,028
Depreciation and amortization	66,983	67,066	202,378	207,882
Total operating expense	498,678	493,245	1,470,374	1,457,342
Income (loss) from operations	7,165	(10,968)	34,172	(16,216)
Interest income	623	1,383	1,771	6,169
Interest expense				
Debt	(30,574)	(37,599)	(96,845)	(110,894)
Amortization of deferred financing costs	(2,167)	(3,004)	(7,099)	(6,940)
Change in fair value of derivatives and amortization	(2,478)	(8,454)	1,137	(17,344)
Loss on extinguishment of debt	(1,178)		(2,918)	(3,052)
Equity in earnings (loss) of unconsolidated ventures	42	358	1,218	(750)
Other non-operating (expense) income	(52)	69	4,172	(424)
Loss before income taxes	(28,619)	(58,215)	(64,392)	(149,451)
Benefit for income taxes	7,329	22,338	18,936	54,996
Net loss	$(21,290)	$(35,877)	$(45,456)	$(94,455)
Basic and diluted loss per share	$(0.18)	$(0.36)	$(0.42)	$(0.93)
Weighted average shares used in computing basic and diluted loss per share	118,455	101,398	108,807	101,748
Dividends declared per share	$	$0.25	$	$0.75

See accompanying notes to condensed consolidated financial statements.

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BROOKDALE SENIOR LIVING INC.
CONDENSED CONSOLIDATED STATEMENT OF EQUITY
(Unaudited, in thousands)

	Common Stock						
	Shares	Amount	Additional Paid-In-Capital	Treasury Stock	Accumulated Deficit	Accumulated Other Comprehensive Loss	Total
Balances at January 1, 2009	105,256	$ 1,053	$ 1,690,851	$ (29,187)	$ (700,720)	$ (1,396)	$ 960,601
Compensation expense related to restricted stock and restricted stock unit grants			21,549				21,549
Net loss					(45,456)		(45,456)
Issuance of common stock under Associate Stock Purchase Plan	92	1	742				743
Restricted stock, net	1,780	18	(18)				
Reclassification of net loss on derivatives into earnings						369	369
Amortization of payments from settlement of forward interest rate swaps						282	282
Issuance of common stock from equity offering, net	16,047	160	163,667				163,827
Other			(8)			(253)	(261)
Balances at September 30, 2009	123,175	$ 1,232	$ 1,876,783	$ (29,187)	$ (746,176)	$ (998)	$ 1,101,654

See accompanying notes to condensed consolidated financial statements.

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BROOKDALE SENIOR LIVING INC.
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(Unaudited, in thousands)

	Nine Months Ended September 30, 2009	Nine Months Ended September 30, 2008
Cash Flows from Operating Activities		
Net loss	$(45,456)	$(94,455)
Adjustments to reconcile net loss to net cash provided by operating activities:		
Loss on extinguishment of debt	2,918	3,052
Depreciation and amortization	209,477	214,822
Equity in (earnings) loss of unconsolidated ventures	(1,218)	750
Distributions from unconsolidated ventures from cumulative share of net earnings	455	1,918
Amortization of deferred gain	(3,259)	(3,257)
Amortization of entrance fees	(16,084)	(16,527)
Proceeds from deferred entrance fee revenue	23,225	15,210
Deferred income tax benefit	(19,440)	(57,243)
Change in deferred lease liability	12,073	15,675
Change in fair value of derivatives and amortization	(1,137)	17,344
Gain on sale of assets	(4,352)	
Non-cash stock-based compensation	21,549	23,368
Changes in operating assets and liabilities:		
Accounts receivable, net	11,234	(18,165)
Prepaid expenses and other assets, net	(10,734)	1,263
Accounts payable and accrued expenses	29,557	3,051
Tenant refundable fees and security deposits	(14,297)	(439)
Deferred revenue	1,811	(3,392)
Other	(10,350)	4,379
Net cash provided by operating activities	185,972	107,354
Cash Flows from Investing Activities		
Decrease in lease security deposits and lease acquisition deposits, net	2,071	2,416
Increase in cash and escrow deposits — restricted	(54,694)	(7,795)
Net proceeds from the sale of property, plant and equipment	210	
Additions to property, plant and equipment and leasehold intangibles, net of related payables	(87,507)	(134,179)
Acquisition of assets, net of related payables and cash received	(1,227)	(5,105)
(Issuance of) payment on notes receivable, net	(590)	39,661
Investment in unconsolidated ventures	(1,246)	(1,163)
Distributions received from unconsolidated ventures	969	300
Proceeds from sale leaseback transaction	9,166	
Proceeds from sale of unconsolidated venture	8,831	4,165
Net cash used in investing activities	(124,017)	(101,700)
Cash Flows from Financing Activities		
Proceeds from debt	67,986	467,769
Repayment of debt and capital lease obligation	(21,194)	(229,210)

Proceeds from line of credit	60,446	264,757
Repayment of line of credit	(219,899)	(378,000)
Payment of dividends		(103,696)
Purchase of treasury stock		(29,187)
Payment of financing costs, net of related payables	(7,258)	(13,720)
Proceeds from public equity offering, net	163,827	
Other	(713)	(1,373)
Refundable entrance fees:		
Proceeds from refundable entrance fees	17,032	15,185
Refunds of entrance fees	(16,842)	(14,331)
Recouponing and payment of swap termination		(27,627)
Cash portion of loss on extinguishment of debt		(1,240)
Net cash provided by (used in) financing activities	43,385	(50,673)
Net increase (decrease) in cash and cash equivalents	105,340	(45,019)
Cash and cash equivalents at beginning of period	53,973	100,904
Cash and cash equivalents at end of period	$159,313	$55,885

See accompanying notes to condensed consolidated financial statements.

BROOKDALE SENIOR LIVING INC.
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)

1. Description of Business

Brookdale Senior Living Inc. ("Brookdale", "BSL" or the "Company") is a leading owner and operator of senior living communities throughout the United States. The Company provides an exceptional living experience through properties that are designed, purpose-built and operated to provide the highest quality service, care and living accommodations for residents. The Company owns, leases and operates retirement centers, assisted living and dementia-care communities and continuing care retirement centers ("CCRCs").

2. Summary of Significant Accounting Policies

Basis of Presentation

The accompanying unaudited interim condensed consolidated financial statements have been prepared pursuant to the rules and regulations of the Securities and Exchange Commission for quarterly reports on Form 10-Q. In the opinion of management, these financial statements include all adjustments necessary to present fairly the financial position, results of operations and cash flows of the Company as of September 30, 2009, and for all periods presented. The condensed consolidated financial statements are prepared on the accrual basis of accounting. All adjustments made have been of a normal and recurring nature. Certain information and footnote disclosures normally included in annual financial statements prepared in accordance with generally accepted accounting principles have been condensed or omitted. The Company believes that the disclosures included are adequate and provide a fair presentation of interim period results. Interim financial statements are not necessarily indicative of the financial position or operating results for an entire year. It is suggested that these interim financial statements be read in conjunction with the audited financial statements and the notes thereto, together with management's discussion and analysis of financial condition and results of operations, included in the Company's Annual Report on Form 10-K for the fiscal year ended December 31, 2008, as filed with the Securities and Exchange Commission.

Revenue Recognition

Resident Fees

Resident fee revenue is recorded when services are rendered and consist of fees for basic housing, support services and fees associated with additional services such as personalized health and assisted living care. Residency agreements are generally for a term of 30 days to one year, with resident fees billed monthly in advance. Revenue for certain skilled nursing services and ancillary charges is recognized as services are provided and is billed monthly in arrears.

Entrance Fees

Certain of the Company's communities have residency agreements which require the resident to pay an upfront fee prior to occupying the community. In addition, in connection with the Company's MyChoice program, new and existing residents are allowed to pay additional entrance fee amounts in return for a reduced monthly service fee. The non-refundable portion of the entrance fee is recorded as deferred revenue and amortized over the estimated stay of the resident based on an actuarial valuation. The refundable portion of a resident's entrance fee is generally refundable within a certain number of months or days following contract termination or in certain agreements, upon the resale of the resident’s unit or a comparable unit or 12 months after the resident vacates the unit. In such instances the refundable portion of the fee is not amortized and included in refundable entrance fees and deferred revenue.

Certain contracts require the refundable portion of the entrance fee plus a percentage of the appreciation of the unit, if any, to be refunded only upon resale of a comparable unit (“contingently refundable”). Upon resale the Company may receive reoccupancy proceeds in the form of additional contingently refundable fees, refundable fees, or non-refundable fees. The Company estimates the amount of reoccupancy proceeds to be received from additional

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contingently refundable fees or non-refundable fees and records such amount as deferred revenue. The deferred revenue is amortized over the life of the community and was approximately $62.2 million and $63.4 million at September 30, 2009 and December 31, 2008, respectively. All remaining contingently refundable fees not recorded as deferred revenue and amortized are included in refundable entrance fees and deferred revenue.

All refundable amounts due to residents at any time in the future, including those recorded as deferred revenue, are classified as current liabilities.

The non-refundable portion of entrance fees expected to be earned and recognized in revenue in one year is recorded as a current liability. The balance of the non-refundable portion is recorded as a long-term liability.

Community Fees

Substantially all community fees received are non-refundable and are recorded initially as deferred revenue. The deferred amounts, including both the deferred revenue and the related direct resident lease origination costs, are amortized over the estimated stay of the resident which is consistent with the implied contractual terms of the resident lease.

Management Fees

Management fee revenue is recorded as services are provided to the owners of the communities. Revenues are determined by an agreed upon percentage of gross revenues (as defined).

Fair Value Measurements

Cash and cash equivalents, cash and escrow deposits-restricted and derivative financial instruments are reflected in the accompanying condensed consolidated balance sheets at amounts considered by management to reasonably approximate fair value. Management estimates the fair value of its long-term debt using a discounted cash flow analysis based upon the Company’s current borrowing rate for debt with similar maturities and collateral securing the indebtedness. The Company had outstanding debt with a carrying value of $2.5 billion and $2.6 billion as of September 30, 2009 and December 31, 2008, respectively. The fair value of debt both as of September 30, 2009 and December 31, 2008 was $2.4 billion.

The Financial Accounting Standards Board (FASB) guidance on Fair Value Measurement 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. A financial instrument’s categorization 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 – Inputs to the valuation methodology are quoted prices (unadjusted) for identical assets or liabilities in active markets.
Level 2 – Inputs to the valuation methodology include quoted prices for similar assets and liabilities in active markets, and inputs that are observable for the asset or liability, either directly or indirectly, for substantially the full term of the financial instrument.
Level 3 – Inputs to the valuation methodology are unobservable and significant to the fair value measurement.

The Company’s derivative positions are valued using models developed internally by the respective counterparty that use as their basis readily observable market parameters (such as forward yield curves) and are classified within Level

2 of the valuation hierarchy.

The Company considers its own credit risk as well as the credit risk of its counterparties when evaluating the fair value of its derivatives. Any adjustments resulting from credit risk are recorded as a change in fair value of derivatives and amortization in the current period statement of operations (Note 16).

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Self-Insurance Liability Accruals

The Company is subject to various legal proceedings and claims that arise in the ordinary course of its business. Although the Company maintains general liability and professional liability insurance policies for its owned, leased and managed communities under a master insurance program, the Company's current policies provide for deductibles for each claim ($3.0 million on or prior to December 31, 2008 and $250,000 effective January 1, 2009). As a result, the Company is, in effect, self-insured for most claims. In addition, the Company maintains a self-insured workers compensation program and a self-insured employee medical program for amounts below excess loss coverage amounts, as defined. The Company reviews the adequacy of its accruals related to these liabilities on an ongoing basis, using historical claims, actuarial valuations, third party administrator estimates, consultants, advice from legal counsel and industry data, and adjusts accruals periodically. Estimated costs related to these self-insurance programs are accrued based on known claims and projected claims incurred but not yet reported. Subsequent changes in actual experience are monitored and estimates are updated as information is available.

Treasury Stock

The Company accounts for treasury stock under the cost method and includes treasury stock as a component of stockholders' equity.

New Accounting Pronouncements

The Company follows accounting standards set by the FASB. The FASB sets generally accepted accounting principles ("GAAP") that the Company follows to ensure consistent reporting of its financial condition, results of operations and cash flows. References to GAAP issued by the FASB in these footnotes are to the FASB Accounting Standards Codification, sometimes referred to as the Codification or ASC. The FASB finalized the Codification effective for periods ending on or after September 15, 2009. The Codification does not change how the Company accounts for its transactions or the nature of related disclosures made.

The FASB guidance on Business Combinations was effective for business combinations with an acquisition date on or after January 1, 2009 and is to be applied prospectively. The guidance was issued to improve the relevance, representational faithfulness, and comparability of the information that a reporting entity provides in its financial reports about a business combination and its effects. Itestablishes principles and requirements for how the acquirer recognizes and measures in its financial statements the identifiable assets acquired, the liabilities assumed, and any noncontrolling interest in the acquiree, recognizes and measures the goodwill acquired in the business combination or a gain from a bargain purchase and determines what information to disclose to enable users of the financial statements to evaluate the nature and financial effects of the business combination. As of September 30, 2009, this guidance has not had a material impact on the condensed consolidated financial statements.

The Company adopted the provisions of the FASB guidance on Consolidations relating to the accounting for noncontrolling interests on January 1, 2009. This guidance amends previous authoritative guidance by requiring companies to report a noncontrolling interest in a subsidiary as equity in its consolidated financial statements. Disclosure of the amounts of consolidated net income attributable to the parent and the noncontrolling interest are required. This guidance also clarifies that transactions that result in a change in a parent's ownership interest in a subsidiary that do not result in deconsolidation will be treated as equity transactions, while a gain or loss will be recognized by the parent when a subsidiary is deconsolidated. Other than the required disclosures, the adoption had no impact on the condensed consolidated financial statements.

In February 2008, the FASB issued guidance which delays the effective date of the FASB guidance on Fair Value Measurements for all nonfinancial assets and liabilities, except those that are recognized or disclosed at fair value in the financial statements on a recurring basis (at least annually). The guidance partially defers the effective date of the FASB guidance to fiscal years beginning after November 15, 2008 and as a result was effective for the Company beginning January 1, 2009. The adoption of the guidance had no impact on the condensed consolidated financial statements.

The Company adopted the provision of the FASB guidance on disclosures relating to Derivatives and Hedging on January 1, 2009. This guidance requires entities to provide enhanced disclosures about how and why an entity uses derivative instruments, how derivative instruments and related hedge items are accounted for and how derivative

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instruments and related hedged items affect an entity's financial position, results of operations and cash flows. Other than the required disclosures, the adoption had no impact on the condensed consolidated financial statements.

The Company adopted the provisions of the guidance relating to the Determination of the Useful Life of Intangible Assets on January 1, 2009. This guidance amends the factors that should be considered in developing renewal or extension assumptions used to determine the useful life of a recognized intangible asset and provides for enhanced disclosures regarding intangible assets. The intent of this guidance is to improve the consistency between the useful life of a recognized intangible asset and the period of expected cash flows used to measure the fair value of the asset. The disclosure provisions are effective as of the adoption date and the guidance for determining the useful life applies prospectively to all intangible assets acquired after the effective date. The adoption had no impact on the condensed consolidated financial statements.

The Company adopted the provisions of Emerging Issues Task Force ("EITF") guidance on Determining Whether Instruments Granted in Share-Based Payment Transactions Are Participating Securities on January 1, 2009. The EITF provides that unvested share-based payment awards that contain nonforfeitable rights to dividends or dividend equivalents (whether paid or unpaid) are participating securities and shall be included in the computation of earnings per share. The adoption did not have a material impact on the condensed consolidated financial statements.

The Company adopted the guidance relating to Interim Disclosures about Fair Value of Financial Instruments on June 1, 2009. This guidance requires disclosures about fair value of financial instruments for interim periods of publicly traded companies as well as in annual financial statements. Other than the required disclosures, the adoption had no impact on the condensed consolidated financial statements.

The Company adopted the guidance related to the Accounting for Assets Acquired and Liabilities Assumed in a Business Combination that Arise from Contingencies effective January 1, 2009. The guidance amends and clarifies guidance previously issued on Business Combinations and addresses application issues on initial recognition and measurement, subsequent measurement and accounting, and disclosure of assets and liabilities arising from contingencies in a business combination. The Company had no acquisitions during the nine months ended September 30, 2009; therefore, the adoption of the guidance had no impact on the condensed consolidated financial statements.

In May 2009, the FASB issued guidance on Subsequent Events. This guidance establishes general standards of accounting for and disclosure of events that occur after the balance sheet date but before the financial statements are issued or are available to be issued. Although the guidance is based on the same principles as those that currently exist in the auditing standards, it includes a new required disclosure of the date through which an entity has evaluated subsequent events. The Company adopted this guidance in June 2009 and other than the required disclosures, the adoption had no impact on the condensed consolidated financial statements.

In June 2009, the FASB issued guidance which amends previously issued guidance on the Consolidation of Variable Interest Entities. This guidance changes how a company determines when an entity that is insufficiently capitalized or is not controlled through voting (or similar rights) should be consolidated. The determination of whether a company is required to consolidate an entity is based on, among other things, an entity's purpose and design and a company's ability to direct the activities of the entity that most significantly impacts the entity's economic performance. The guidance is effective for the Company beginning January 1, 2010. The Company is currently evaluating the impact its provisions will have on its condensed consolidated financial statements.

Dividends

On December 30, 2008, the Company’s board of directors voted to suspend the Company’s quarterly cash dividend indefinitely.

Reclassifications

Certain prior period amounts have been reclassified to conform to the current financial statement presentation, with no effect on the Company’s condensed consolidated financial position or results of operations.

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3. Earnings Per Share

Basic earnings per share ("EPS") is calculated by dividing net income by the weighted average number of shares of common stock outstanding. Diluted EPS includes the components of basic EPS and also gives effect to dilutive common stock equivalents. For purposes of calculating basic and diluted earnings per share, vested restricted stock awards are considered outstanding. Under the treasury stock method, diluted EPS reflects the potential dilution that could occur if securities or other instruments that are convertible into common stock were exercised or could result in the issuance of common stock. Potentially dilutive common stock equivalents include unvested restricted stock and restricted stock units.

During the three and nine months ended September 30, 2009 and September 30, 2008, the Company reported a consolidated net loss. As a result of the net loss, unvested restricted stock and restricted stock unit awards were antidilutive for each period and were not included in the computation of diluted weighted average shares. The weighted average restricted stock and restricted stock unit grants excluded from the calculations of diluted net loss per share was 2.0 million and 1.4 million for the three months ended September 30, 2009 and 2008, respectively, and 1.2 million and 1.4 million for the nine months ended September 30, 2009 and 2008, respectively.

4. Stock-Based Compensation

The Company recorded $7.9 million and $6.7 million of compensation expense in connection with grants of restricted stock and restricted stock units for the three months ended September 30, 2009 and 2008, respectively, and $21.5 million and $23.4 million of such expense for the nine months ended September 30, 2009 and 2008, respectively. For the three and nine months ended September 30, 2009 and 2008, compensation expense was calculated net of forfeitures estimated from 0% - 6% of the shares granted.

For all awards with graded vesting other than awards with performance-based vesting conditions, the Company records compensation expense for the entire award on a straight-line basis over the requisite service period. For graded-vesting awards with performance-based vesting conditions, total compensation expense is recognized over the requisite service period for each separately vesting tranche of the award as if the award is, in substance, multiple awards once the performance target is deemed probable of achievement. Performance goals are evaluated quarterly. If such goals are not ultimately met or it is not probable the goals will be achieved, no compensation expense is recognized and any previously recognized compensation expense is reversed.

During the current year, the Company issued restricted stock units to its Chief Executive Officer. Under the terms of the award agreement, upon vesting, each restricted stock unit represents the right to receive one share of the Company's common stock.

Current year grants of restricted shares and restricted stock units under the Company's Omnibus Stock Incentive Plan were as follows (amounts in thousands except for value per share):

	Shares / Restricted Stock Units Granted	Value Per Share	Total Value
Three months ended March 31, 2009	84	$ 3.48 – $6.15	$ 301
Three months ended June 30, 2009	2,562	$ 5.14 – $9.39	$ 24,030
Three months ended September 30, 2009	65	$ 9.83 – $10.71	$ 694

The Company has an employee stock purchase plan for all eligible employees. The plan became effective on October 1, 2008. Under the plan, eligible employees of the Company can purchase shares of the Company's common stock on a quarterly basis at a discounted price through accumulated payroll deductions. Each eligible employee may elect to deduct up to 15% of his or her base pay each quarter. Subject to certain limitations specified in the plan, on the last trading date of each calendar quarter, the amount deducted from each participant's pay over the course of the quarter will be used to purchase whole shares of the Company's common stock at a purchase price equal to 90% of the closing market price on the New York Stock Exchange on such date. Initially, the Company has reserved 1,000,000 shares of common stock for issuance under the plan. The employee stock purchase plan also contains an "evergreen" provision that automatically increases the number of shares reserved for issuance under the plan by 200,000 shares on the first day of each calendar year beginning January 1, 2010. The impact on the Company's current year condensed consolidated financial statements is not material.

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5. Goodwill and Other Intangible Assets, Net

There were no changes in the carrying amount of goodwill for the nine months ended September 30, 2009. Goodwill by operating segment as of September 30, 2009 and December 31, 2008 was as follows (dollars in thousands):

	Retirement Centers	Assisted Living	Total
Goodwill	$ 7,155	$ 102,812	$ 109,967

Goodwill is tested for impairment annually with a test date of October 1 or sooner if indicators of impairment are present. No indicators of impairment were present during the nine months ended September 30, 2009.

Intangible assets with definite useful lives are amortized over their estimated lives and are tested for impairment whenever indicators of impairment arise. The following is a summary of other intangible assets at September 30, 2009 and December 31, 2008 (dollars in thousands):

	September 30, 2009			December 31, 2008		
	Gross Carrying Amount	Accumulated Amortization	Net	Gross Carrying Amount	Accumulated Amortization	Net
Community purchase options	$ 147,682	$ (9,245)	$ 138,437	$ 147,682	$ (6,457)	$ 141,225
Management contracts and other	158,041	(101,538)	56,503	158,041	(77,807)	80,234
Home health licenses	11,498	—	11,498	10,130	—	10,130
Total	$ 317,221	$ (110,783)	$ 206,438	$ 315,853	$ (84,264)	$ 231,589

Amortization expense related to definite-lived intangible assets for the three months ended September 30, 2009 and 2008 was $8.7 million and $8.9 million, respectively, and $26.5 million and $26.7 million of amortization expense was recorded for the nine months ended September 30, 2009 and 2008, respectively. Home health licenses were determined to be indefinite-lived intangible assets and are not subject to amortization.

6. Property, Plant and Equipment and Leasehold Intangibles, Net

Property, plant and equipment and leasehold intangibles, net, which include assets under capital leases, consist of the following (dollars in thousands):

	September 30, 2009	December 31, 2008
Land	$ 252,297	$ 253,453
Buildings and improvements	2,736,184	2,626,079
Furniture and equipment	301,577	277,680
Resident and operating lease intangibles	625,228	607,256
Construction in progress	16,741	98,418
Assets under capital and financing leases	575,351	555,872
	4,507,378	4,418,758
Accumulated depreciation and amortization	(886,909)	(720,924)

Property, plant and equipment and leasehold intangibles, net	$	3,620,469	$	3,697,834

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7. Sale-Leaseback Transaction

On March 2, 2009, the Company entered into a sale-leaseback transaction with a third party lessor for the sale and leaseback of one of its skilled nursing facilities. The Company sold the facility for a total of $10.0 million and immediately leased the facility back. Under the terms of the lease agreement, the Company will continue to operate the facility until December 31, 2019. The lease is accounted for as an operating lease.

8. Debt

Long-term Debt, Capital Leases and Financing Obligations

Long-term debt, capital leases and financing obligations consist of the following (dollars in thousands):

	September 30, 2009	December 31, 2008
Mortgage notes payable due 2009 through 2039; weighted average interest rate of 4.64% for the nine months ended September 30, 2009 (weighted average interest rate of 5.33% in 2008)	$ 1,325,029	$ 1,246,204
$150,000 Series A notes payable, secured by five communities and by a $3.0 million letter of credit, bearing interest at LIBOR plus 0.88%, payable in monthly installments of interest only until August 2011 and payable in monthly installments of principal and interest through maturity in August 2013	150,000	150,000
Mortgages payable due 2012; weighted average interest rate of 5.64% for the nine months ended September 30, 2009 (weighted average interest rate of 5.64% in 2008), payable interest only through July 2010 and payable in monthly installments of principal and interest through maturity in July 2012, secured by the underlying assets of the portfolio	212,407	212,407
Variable rate tax-exempt bonds credit-enhanced by Fannie Mae; weighted average interest rate of 1.91% for the nine months ended September 30, 2009 (weighted average interest rate of 4.40% in 2008), due 2032, payable interest only until maturity, secured by the underlying assets of the portfolio	100,841	100,841
Capital and financing lease obligations payable through 2020; weighted average interest rate of 8.82% for the nine months ended September 30, 2009 (weighted average interest rate of 8.81% in 2008)	323,474	318,440
Mortgage note, bearing interest at a variable rate of LIBOR plus 0.70%, payable interest only through maturity in August 2012. The note is secured by 15 of the Company’s communities and an $11.5 million guaranty by the Company	315,180	315,180
	32,634	50,404

Construction financing due 2011 through 2023; weighted average interest rate of 7.63% for the nine months ended September 30, 2009 (weighted average interest rate of 6.02% in 2008)				
Total debt		2,459,565		2,393,476
Less current portion		155,397		158,476
Total long-term debt	$	2,304,168	$	2,235,000

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Although certain debt obligations are scheduled to mature on or prior to September 30, 2010, the Company has the option, subject to the satisfaction of customary conditions (such as the absence of a material adverse change), to extend the maturity of approximately $131.0 million of certain non-recourse mortgages payable until 2011, as the instruments associated with these mortgages payable provide that the Company can extend the respective maturity dates for one 12 month term each from the existing maturity dates.

Credit Facilities

On February 27, 2009, the Company entered into a Second Amended and Restated Credit Agreement with Bank of America, N.A., as administrative agent, Banc of America Securities LLC, as sole lead arranger and book manager, and the several lenders from time to time parties thereto. The amended credit agreement amended and restated the Company's $245.0 million secured line of credit and terminated the associated $80.0 million letter of credit facility.

The amended credit agreement initially consisted of a $230.0 million revolving loan facility with a $25.0 million letter of credit sublimit and is scheduled to mature on August 31, 2010.

Pursuant to the terms of the amended credit agreement, certain of the Company's subsidiaries, as guarantors, will guarantee obligations under the amended credit agreement and the other loan documents. Further, in connection with the amended credit agreement, (i) the Company and certain guarantors executed and delivered a Pledge Agreement in favor of the administrative agent for the banks and other financial institutions from time to time parties to the amended credit agreement, pursuant to which such guarantors pledged certain assets for the benefit of the secured parties as collateral security for the payment and performance of the Company's obligations under the amended credit agreement and the other loan documents and (ii) certain guarantors granted mortgages and executed and delivered a Security Agreement, in each case, in favor of the administrative agent for the banks and other financial institutions from time to time parties to the amended credit agreement encumbering certain real and personal property of such guarantors. The collateral includes, among other things, certain real property and related personal property owned by the guarantors, equity interests in certain of the Company's subsidiaries, all related books and records and, to the extent not otherwise included, all proceeds and products of any and all of the foregoing.

At the option of the Company, amounts drawn under the revolving loan facility initially bore interest at either (i) LIBOR plus a margin of 7.0% or (ii) the greater of (a) the Bank of America prime rate or (b) the Federal Funds rate plus 0.5%, plus a margin of 7.0%. For purposes of determining the interest rate, in no event shall the base rate or LIBOR be less than 3.0%. In connection with the loan commitments, the Company will pay a quarterly commitment fee of 1.0% per annum on the average daily amount of undrawn funds. The Company was initially required to pay a fee equal to 7.0% of the amount of any issued and outstanding letters of credit; provided, with respect to drawable amounts that have been cash collateralized, the letter of credit fee shall be payable at a rate per annum equal to 2.0%.

The amended credit agreement contains typical representations and covenants for loans of this type, including restrictions on the Company's ability to pay dividends, make distributions, make acquisitions, incur capital expenditures, incur new liens or repurchase shares of the Company's common stock. The amended credit agreement also contains financial covenants, including covenants with respect to maximum consolidated adjusted leverage, minimum consolidated fixed charge coverage, minimum tangible net worth, and maximum total capital expenditures. A violation of any of these covenants (including any failure to remain in compliance with any financial covenants contained therein) could result in a default under the amended credit agreement, which would result in termination of all commitments and loans under the amended credit agreement and all other amounts owing under the amended credit agreement and certain other loan agreements becoming immediately due and payable.

On June 1, 2009, in connection with the equity offering described in Note 15, the Company entered into the First Amendment to the Second Amended and Restated Credit Agreement (the "First Amendment") pursuant to which the maximum revolving loans that can be outstanding at any time under the amended credit agreement was reduced to $75.0 million. In addition, the interest rate margin on loans, as well as fees on letters of credit, as a result of the maximum amount of the facility having been reduced to $75.0 million, was reduced to 6.0%.

Pursuant to the First Amendment, the Company has been given greater flexibility to make acquisitions by increasing aggregate permitted cash consideration from $10.0 million to $100.0 million, to make capital expenditures up to $30.0 million per quarter and to incur an additional $20.0 million in liens and letters of credit.

As of September 30, 2009, the Company has an available secured line of credit of $75.0 million (including a $25.0 million letter of credit sublimit) and separate unsecured letter of credit facilities of up to $48.5 million in the aggregate. As of September 30, 2009, there were no borrowings under the revolving loan facility, $23.7 million of letters of credit had been issued under the amended credit facility, and $48.5 million of letters of credit had been issued under the separate unsecured letter of credit facilities.

In late 2008, the Company began replacing some of its outstanding letters of credit with restricted cash in order to reduce the Company's letter of credit needs.

Financings

On January 30, 2009, the Company amended and restated a $52.6 million first mortgage loan, secured by the underlying properties, which was payable interest only through maturity in March 2009. Pursuant to the amendment, the maturity date has been extended to March 31, 2011. The amended and restated loan bears interest at LIBOR plus 4.0% and requires principal amortization. In connection with the amendment, the Company made a $3.0 million payment to reduce the outstanding principal amount of the loan.

On February 25, 2009, the Company amended a $41.0 million first mortgage loan, secured by the underlying properties, which was payable interest only through maturity in June 2009. Pursuant to the amendment, the maturity date has been extended to June 2011. The amended loan is evidenced by two promissory notes, the first of which is in the principal amount of $26.0 million and bears interest at LIBOR plus 3.0%. The second promissory note is in the amount of $15.0 million and bears interest at LIBOR plus 5.6%. Both notes require principal amortization. In connection with the amendment, the Company made a $2.0 million payment to reduce the outstanding principal amount of the $26.0 million loan.

Effective May 11, 2009, the Company exercised its option to extend the maturity date of $131.0 million of mortgage notes from May 11, 2009 to May 11, 2010. No other terms of the notes were changed in connection with the extension.

As of September 30, 2009, the Company is in compliance with the financial covenants of its outstanding debt and lease agreements.

Interest Rate Swaps and Caps

In the normal course of business, a variety of financial instruments are used to manage or hedge interest rate risk. Interest rate protection and swap agreements were entered into to effectively cap or convert floating rate debt to a fixed rate basis, as well as to hedge anticipated future financing transactions. Pursuant to the hedge agreements, the Company is required to secure its obligation to the counterparty if the fair value liability exceeds a specified threshold. Cash collateral pledged to the Company's counterparties was $18.1 million and $13.9 million as of September 30, 2009 and December 31, 2008, respectively.

All derivative instruments are recognized as either assets or liabilities in the condensed consolidated balance sheets at fair value. The change in mark-to-market of the value of the derivative is recorded as an adjustment to income or other comprehensive loss depending on whether it has been designated and qualifies as an accounting hedge.

Derivative contracts are not entered into for trading or speculative purposes. Furthermore, the Company has a policy of only entering into contracts with major financial institutions based upon their credit rating and other factors. Under certain circumstances, the Company may be required to replace a counterparty in the event that the counterparty does not maintain a specified credit rating.

The following table summarizes the Company’s swap instruments at September 30, 2009 (dollars in thousands):

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Current notional balance	$	351,840	
Highest possible notional	$	351,840	
Lowest interest rate		3.24	%
Highest interest rate		4.47	%
Average fixed rate		3.74	%
Earliest maturity date		2011	
Latest maturity date		2014	
Weighted average original maturity		4.7 years	
Estimated liability fair value (included in other liabilities at September 30, 2009)	$	(19,564	)
Estimated asset fair value (included in other assets, net at September 30, 2009)	$	—	

The following table summarizes the Company's cap instruments at September 30, 2009 (dollars in thousands):

Current notional balance	$	734,621	
Highest possible notional	$	734,621	
Lowest interest rate		4.96	%
Highest interest rate		6.50	%
Average fixed rate		5.97	%
Earliest maturity date		2011	
Latest maturity date		2012	
Weighted average original maturity		3.8 years	
Estimated liability fair value (included in other liabilities at September 30, 2009)	$	—	
Estimated asset fair value (included in other assets, net at September 30, 2009)	$	942	

During the three and nine months ended September 30, 2009, the fair value of the Company's interest rate swaps and caps decreased $2.5 million and increased $1.1 million, respectively. During the three and nine months ended September 30, 2008, the fair value of the Company's interest rate swaps and caps decreased $8.5 million and $17.3 million, respectively. This is included as a component of interest expense in the condensed consolidated statements of operations.

9. Litigation

The Company has been and is currently involved in litigation and claims incidental to the conduct of its business which are comparable to other companies in the senior living industry. Certain claims and lawsuits allege large damage amounts and may require significant costs to defend and resolve. Similarly, the senior living industry is continuously subject to scrutiny by governmental regulators, which could result in litigation related to regulatory compliance matters. As a result, the Company maintains insurance policies in amounts and with coverage and deductibles the Company believes are adequate, based on the nature and risks of its business, historical experience and industry standards. Effective January 1, 2009, the Company's current policies provide for deductibles of $250,000 for each claim. Accordingly, the Company is, in effect, self-insured for most claims.

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10. Supplemental Disclosure of Cash Flow Information

(dollars in thousands):

	Nine Months Ended September 30,	
	2009	2008
Supplemental Disclosure of Cash Flow Information:		
Interest paid	$99,460	$110,998
Income taxes paid	$1,846	$1,401
Supplemental Schedule of Non-cash Operating, Investing and Financing Activities:		
Capital leases:		
Property, plant and equipment and leasehold intangibles, net	$18,236	$35,942
Long-term debt	(18,236)	(35,942)
Net	$—	$—
Lease Incentive:		
Property, plant and equipment and leasehold intangibles, net	$1,237	$
Deferred liabilities	(1,237)	
Net	$—	$—
De-consolidation of an entity pursuant to FIN 46(R):		
Accounts receivable	$	$92
Prepaid expenses and other current assets		1,861
Property, plant and equipment and leasehold intangibles, net		35,268
Other assets, net		7
Investment in unconsolidated ventures		186
Long-term debt		(29,159)
Accrued expenses		(1,252)
Trade accounts payable		(20)
Tenant security deposits		(173)
Refundable entrance fees and deferred revenue		(89)
Additional paid-in-capital		(9,217)
Accumulated deficit		2,496
Net	$—	$—
Acquisition of assets, net of related payables and cash received:		
Other intangible assets, net	$1,227	$5,105
Reclassification of other intangibles, net	$141	$—

11. Facility Operating Leases

A summary of facility lease expense and the impact of straight-line adjustment and amortization of deferred gains are as follows (dollars in thousands):

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2009	2008	2009	2008
Cash basis payment	$ 65,331	$ 63,394	$ 195,397	$ 189,610
Straight-line expense	3,793	4,709	12,073	15,675
Amortization of deferred gain	(1,088)	(1,086)	(3,259)	(3,257)

Facility lease expense	$ 68,036	$ 67,017	$ 204,211	$ 202,028

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