

SEARS HOLDINGS CORP
Form DEF 14A
March 16, 2006

QuickLinks -- Click here to rapidly navigate through this document

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

SCHEDULE 14A

Proxy Statement Pursuant to Section 14(a) of
the Securities Exchange Act of 1934 (Amendment No.)

Filed by the Registrant

Filed by a Party other than the Registrant

Check the appropriate box:

- Preliminary Proxy Statement
- Confidential, for Use of the Commission Only (as permitted by Rule 14a-6(e)(2))**
- Definitive Proxy Statement
- Definitive Additional Materials
- Soliciting Material Pursuant to §240.14a-12

SEARS HOLDINGS CORPORATION

(Name of Registrant as Specified In Its Charter)

(Name of Person(s) Filing Proxy Statement, if other than the Registrant)

Payment of Filing Fee (Check the appropriate box):

- No fee required.
- Fee computed on table below per Exchange Act Rules 14a-6(i)(4) and 0-11.

(1) Title of each class of securities to which transaction applies:

(2) Aggregate number of securities to which transaction applies:

(3) Per unit price or other underlying value of transaction computed pursuant to Exchange Act Rule 0-11 (set forth the amount on which the filing fee is calculated and state how it was determined):

(4) Proposed maximum aggregate value of transaction:

(5) Total fee paid:

o Fee paid previously with preliminary materials.

o Check box if any part of the fee is offset as provided by Exchange Act Rule 0-11(a)(2) and identify the filing for which the offsetting fee was paid previously. Identify the previous filing by registration statement number, or the Form or Schedule and the date of its filing.

(1) Amount Previously Paid:

(2) Form, Schedule or Registration Statement No.:

(3) Filing Party:

(4) Date Filed:

Persons who are to respond to the collection of information contained in this form are not required to respond unless the form displays a currently valid OMB control number.

SEARS HOLDINGS CORPORATION
3333 Beverly Road
Hoffman Estates, Illinois 60179

March 15, 2006

AYLWIN B. LEWIS
Chief Executive Officer and President

Dear Stockholder:

I am pleased to invite you to attend the first Annual Meeting of Stockholders of Sears Holdings Corporation (the "Company" or "Sears Holdings") on Wednesday, April 12, 2006. The meeting will begin at 8:00 a.m. (Central time) in the Sears Holdings General Session Room, 3333 Beverly Road, Hoffman Estates, Illinois.

The Notice of Annual Meeting and Proxy Statement that follow this letter describe the matters to be voted on during the meeting. Your proxy card and the Company's 2005 Annual Report on Form 10-K are also enclosed.

Whether or not you plan to attend the meeting in person, please read the proxy statement and vote your shares. Instructions for Internet and telephone voting are attached to your proxy card. If you prefer, you can vote by mail by completing your proxy card and returning it in the enclosed postage-paid envelope.

If you plan to attend the meeting:

If you are a stockholder of record and you plan to attend the meeting, please keep the admission ticket that is attached to the enclosed proxy card, as you must present this ticket to be admitted to the meeting. Each stockholder may be asked to present valid picture identification, such as a driver's license or passport. Stockholders holding shares in brokerage accounts ("street-name stockholders") will need to bring a copy of a brokerage statement, proxy or letter from the broker confirming ownership of Sears Holdings shares as of the record date of February 24, 2006. Registration will begin at 7:30 a.m. and seating will begin at 7:45 a.m. Cameras, recording devices and other electronic devices will not be permitted at the meeting.

Sincerely,

Aylwin B. Lewis

Sears Holdings Corporation
3333 Beverly Road
Hoffman Estates, Illinois 60179

Notice of 2006 Annual Meeting of Stockholders

Date: April 12, 2006
Time: 8:00 a.m. Central time
Place: Sears Holdings General Session Room
3333 Beverly Road
Hoffman Estates, IL 60179

We invite you to attend the annual meeting of stockholders of Sears Holdings Corporation ("Sears Holdings," "Company," "we," "our" or "us") to:

1. Elect nine directors;
2. Approve the Sears Holdings Corporation 2006 Associate Stock Purchase Plan;
3. Approve the Sears Holdings Corporation 2006 Stock Plan;
4. Approve the Sears Holdings Corporation Umbrella Incentive Program;
5. Ratify the appointment by the Audit Committee of Deloitte & Touche LLP as the Company's independent public accountants for fiscal year 2006; and
6. Consider any other business that may properly come before the meeting or any adjournments or postponements of the meeting.

The Record Date for determining stockholders entitled to notice of, and to vote at, this annual meeting is February 24, 2006. Only stockholders of record at the close of business on that date can vote at the meeting.

For more information, please read the accompanying Proxy Statement.

This Notice of 2006 Annual Meeting of Stockholders, as well as the accompanying Proxy Statement and proxy card, are being mailed to our stockholders commencing on or about March 17, 2006.

It is important that your shares be represented at the meeting. Stockholders may vote their shares (1) in person at the Annual Meeting, (2) by telephone, (3) through the Internet or (4) by completing and mailing the enclosed proxy card in the return envelope provided. Specific instructions for voting by telephone or through the Internet are attached to the proxy card. If you attend the meeting and vote at it, your vote at the meeting will replace any earlier vote.

By Order of the Board of Directors

William R. Harker
Vice President, Acting General Counsel and Secretary

March 15, 2006

Proxy Statement

This Proxy Statement and the accompanying proxy card are being mailed to stockholders of Sears Holdings Corporation in connection with the solicitation of proxies by the Board of Directors for the 2006 Annual Meeting of Stockholders being held on April 12, 2006.

TABLE OF CONTENTS

| | |
|---|-----------|
| QUESTIONS AND ANSWERS | 3 |
| CORPORATE GOVERNANCE | 5 |
| Corporate Governance Practices | 5 |
| Director Independence | 6 |
| ITEM 1. ELECTION OF DIRECTORS | 6 |
| Committees of the Board of Directors | 8 |
| Annual Board Compensation | 9 |
| Communications with the Board of Directors | 9 |
| Nomination of Director Candidates | 9 |
| Amount and Nature of Beneficial Ownership | 11 |
| Certain Relationships and Transactions | 13 |
| Executive Compensation | 14 |
| Report of the Compensation Committee | 14 |
| Compensation Committee Interlocks and Insider Participation | 17 |
| Summary Compensation Table | 18 |
| Option Grants in Last Fiscal Year | 20 |
| Aggregated Option Exercises in Last Fiscal Year And Fiscal Year-End Option Values | 21 |
| Long Term Incentive Plan Awards in the Last Fiscal Year | 21 |
| Pension Plans | 22 |
| Executive Officer Employment Agreements | 22 |
| Stock Performance Graph | 24 |
| Equity Compensation Plan Information | 25 |
| ITEM 2. APPROVAL OF 2006 ASSOCIATE STOCK PURCHASE PLAN | 25 |
| ITEM 3. APPROVAL OF 2006 STOCK PLAN | 28 |
| ITEM 4. APPROVAL OF UMBRELLA INCENTIVE PROGRAM | 32 |
| ITEM 5. RATIFICATION OF APPOINTMENT OF INDEPENDENT PUBLIC ACCOUNTANTS | 41 |
| Prior Auditors of Kmart | 41 |
| Independent Auditor Fees | 41 |
| Report of the Audit Committee | 42 |
| Audit Committee Pre-Approval Policies and Procedures | 42 |
| OTHER INFORMATION | 43 |
| Other Business That May Come Before the Meeting | 43 |
| 2007 Annual Meeting of Stockholders | 43 |
| Procedures for Submitting Stockholder Proposals | 43 |
| Section 16(a) Beneficial Ownership Reporting Compliance | 43 |
| Solicitation of Proxies | 43 |
| IMPORTANT | 43 |

Edgar Filing: SEARS HOLDINGS CORP - Form DEF 14A

| | | |
|----------------------|---|--------|
| APPENDIX A | Audit Committee Charter | A-1 |
| APPENDIX B | Sears Holdings Corporation 2006 Associate Stock Purchase Plan | B-1 |
| APPENDIX C | Sears Holdings Corporation 2006 Stock Plan, as amended | C-1 |
| APPENDIX D | Sears Holdings Corporation Umbrella Incentive Program | D-1 |
| APPENDIX D-1 | Sears Holdings Corporation 2005 Senior Executive Long-Term Incentive Program | D-1-1 |
| APPENDIX D-1A | First Amendment to Sears Holdings Corporation 2005 Senior Executive Long-Term Incentive Program | D-1-A1 |
| APPENDIX D-2 | Sears Holdings Corporation 2005 Vice President Long-Term Incentive Program | D-2-1 |
| APPENDIX D-3 | Sears Holdings Corporation Senior Executive SHC 2005 Annual Incentive Plan | D-3-1 |
| APPENDIX D-4 | Sears Holdings Corporation 2005 Annual Incentive Plan | D-4-1 |
| APPENDIX D-5 | Sears Holdings Corporation 2006 Long-Term Incentive Program | D-5-1 |
| APPENDIX D-6 | Sears Holdings Corporation 2006 Annual Incentive Plan | D-6-1 |

QUESTIONS AND ANSWERS

Q:
What is a Proxy?

A:
A Proxy is a document, also referred to as a "proxy card," on which you authorize someone else to vote for you in the way that you want to vote. You may also choose to abstain from voting. **The Proxy is being solicited by our Board of Directors.**

Q:
What is a Proxy Statement?

A:
A Proxy Statement is a document, such as this one, required by the Securities and Exchange Commission (the "SEC") that, among other things, explains the items on which you are asked to vote on the proxy card.

Q:
What am I voting on at the Annual Meeting?

A:
At the Sears Holdings 2006 Annual Meeting, our stockholders are asked to:

elect nine directors (see page 6);

approve the Sears Holdings Corporation 2006 Associate Stock Purchase Plan (see page 25);

approve the Sears Holdings Corporation 2006 Stock Plan (see page 28);

approve the Sears Holdings Corporation Umbrella Incentive Program (see page 32);

ratify the appointment of Deloitte & Touche LLP as our independent public accountants for fiscal 2006 (see page 41); and

consider any other business that may properly come before the meeting or any adjournments or postponements of the meeting.

Q:
Who is entitled to vote?

A:
Only holders of our common stock at the close of business on February 24, 2006 (the "Record Date") are entitled to vote at the Annual Meeting. Each outstanding share of common stock has one vote. There were 158,997,881 shares of common stock outstanding on the Record Date.

Q:
How do I cast my vote?

A:
If you hold your shares directly in your own name, you are a "**registered stockholder**" and can vote in person at the Annual Meeting or you can complete and submit a Proxy through the Internet, by telephone or by mail. If your shares are registered in the name of a broker or other nominee, you are a "**street-name stockholder**" and will receive instructions from your broker or other nominee describing how to vote your shares.

Q:

How do I vote by telephone or through the Internet?

A:

If you are a registered stockholder, you may vote by telephone or through the Internet by following the instructions attached to your proxy card. If you are a street-name stockholder, your broker or other nominee has enclosed or provided a voting instruction card for you to use in directing your broker or nominee how to vote your shares.

Q:

Who will count the vote?

A:

A representative of ADP Investor Communication Services (ADP), an independent tabulator, will count the vote and act as the inspector of election.

Q:

Can I change my vote after I have voted?

A:

A subsequent vote by any means will change your prior vote. For example, if you voted by telephone, a subsequent Internet vote will change your vote. If you wish to change your vote by mail, you may do so by requesting, in writing, a new proxy card from the Corporate Secretary at Sears Holdings Corporation, 3333 Beverly Road, Hoffman Estates, IL 60179, Attn: Corporate Secretary. The last vote received prior to the meeting will be the one counted. If you are a registered stockholder, you may also change your vote by voting in person at the Annual Meeting.

Q:
Can I revoke a Proxy?

A:
Yes, registered stockholders may revoke a properly executed Proxy at any time before the polls close for the Annual Meeting by submitting a letter addressed to and received by the Corporate Secretary at the address listed in the answer to the previous question. Street-name stockholders cannot revoke their proxies in person at the Annual Meeting because the actual registered stockholders, the brokers or other nominees, will not be present. Street-name stockholders wishing to change their votes after returning voting instructions to their broker or other nominee should contact the broker or nominee directly.

Q:
What does it mean if I get more than one proxy card?

A:
It indicates that your shares are registered differently and are in more than one account. Sign and return all proxy cards, or vote each account by telephone or the Internet, to ensure that all your shares are voted. We encourage you to register all your accounts in the same name and address. Registered stockholders may contact our transfer agent, Computershare Trust Company, N.A., at P.O. Box 43069, Providence, RI 02940 (1-800-732-7780). Street-name stockholders holding shares through a broker or other nominee should contact their broker or nominee and request consolidation of their accounts.

Q:
What shares are included on my proxy card?

A:
Your proxy card represents all shares registered to your account in the same social security number and address, including any full and fractional shares you own under one or more of the following plans:

the Sears 401(k) Savings Plan

the Lands' End, Inc. Retirement Plan

the Sears Puerto Rico Savings Plan

We refer to these plans collectively as the "401(k) Plans." If you hold shares of Sears Holdings common stock through a 401(k) Plan, your proxy card will instruct the trustee of your plan how to vote the shares allocated to your plan account.

Q:
What happens if I submit a proxy card without giving specific voting instructions?

A:
If you hold your shares as a registered stockholder and you submit your proxy card with an unclear voting designation or with no voting designation at all, the proxies will vote your shares as recommended by the Board of Directors. If you do not vote shares that you hold through the 401(k) Plans by 11:59 p.m. Eastern time on the night before the Annual Meeting (or you submit your proxy card with an unclear voting designation or with no voting designation at all), then the plan trustee will vote the shares in your account in proportion to the way other participants in your 401(k) Plan vote their shares.

Q:
What makes a quorum?

A:
Each outstanding share of our common stock as of the Record Date is entitled to one vote at the Annual Meeting. A majority of the outstanding shares entitled to vote, being present or represented by Proxy at the meeting, constitutes a quorum. A quorum is necessary to conduct the Annual Meeting.

Q:
How does the voting work?

A:
For each item, voting works as follows:

Edgar Filing: SEARS HOLDINGS CORP - Form DEF 14A

Item 1: To elect any director, the vote of the holders of a plurality of the shares present or represented by Proxy and entitled to vote on the election of directors is required.

Items 2 - 5: Under the NASDAQ Marketplace Rules, ratification of the appointment of auditors and each of the 2006 Associate Stock Purchase Plan, the 2006 Stock Plan and the Umbrella Incentive Program will be deemed approved if a majority of the total votes cast on these items are voted "for" approval.

Abstentions from voting on a particular matter, and shares held in "street name" by brokers or other nominees that are not voted, including because the broker or nominee does not have discretionary authority to vote those shares as to a particular matter, will not be counted as votes either for or against that matter, and will also not be counted as votes cast or shares voting on that matter. Accordingly, abstentions and "broker non-votes" will have no effect on the voting on a matter that requires the affirmative vote of a certain percentage of the total votes cast, although those shares will count for quorum

purposes. Abstentions from voting for one or more director nominees will result in the respective nominees receiving fewer votes.

Q:
Who may attend the Annual Meeting?

A:
Any stockholder as of the Record Date may attend. Seating and parking are limited and admission is on a first-come basis. If you are a registered stockholder and you plan to attend the meeting, please keep the admission ticket attached to the enclosed proxy card, as you must present this ticket to be admitted to the meeting. Each stockholder may be asked to present valid picture identification (for example, a driver's license or passport). Street-name stockholders will need to bring a copy of a brokerage statement, proxy or letter from the broker or other nominee confirming ownership of Sears Holdings shares as of the Record Date.

Q:
Can I access future annual meeting materials through the Internet rather than receiving them by mail?

A:
Yes. *Registered stockholders* can sign up for electronic delivery at www.proxyvote.com or in the Investor Information section of our website at www.searsholdings.com. You must vote through the Internet in order to sign up for electronic delivery of future proxy materials. Just follow the instructions that appear after you finish voting. You will receive an e-mail next year containing our 2006 Annual Report on Form 10-K and the proxy statement for our 2007 annual meeting. *Street-name stockholders* may also have the opportunity to receive copies of these documents electronically. Please check the information provided in the proxy materials mailed to you by your broker or other nominee regarding the availability of this service.

CORPORATE GOVERNANCE

Corporate Governance Practices

Our Board of Directors (the "Board") is committed to effective corporate governance. The Board has approved and adopted Corporate Governance Guidelines that provide the framework for governance of our company. The Nominating and Corporate Governance Committee reviews and assesses the Corporate Governance Guidelines annually and recommends changes to the Board as appropriate. The Corporate Governance Guidelines, along with the charters of all Board committees, our Code of Conduct and our Board of Directors Code of Conduct are available on our website at www.searsholdings.com under the heading "Corporate Governance." In addition, the Audit Committee Charter is attached as **Appendix A** to this Proxy Statement.

Among other things, the Corporate Governance Guidelines provide that

A majority of the members of the Board must be independent Directors to the extent required by the securities laws and the rules of The NASDAQ Stock Market, Inc. ("NASDAQ").

Independent directors are to meet regularly, at least twice a year, in executive session without management present.

The Board and its committees have the power to engage at the Company's expense independent legal, financial or other advisors as deemed necessary, without consulting or obtaining the approval of the Company's officers in advance.

The Board conducts an annual evaluation to assess whether it and its committees are functioning effectively.

Director Independence

Based on the recommendation of the Nominating and Corporate Governance Committee of the Board of Directors, the Board has determined that each of the following Directors, who together constitute a majority of the members of our Board, is an "independent director" as defined in the Marketplace Rules of NASDAQ:

Donald J. Carty, Jr.
Michael A. Miles
Steven T. Mnuchin
Richard C. Perry
Ann N. Reese
Thomas J. Tisch

The Board has also determined that all members of the Audit Committee meet additional, heightened independence criteria applicable to audit committee members under the NASDAQ Marketplace Rules. The Board of Directors has further determined that Ann N. Reese, the chair of the Audit Committee, Donald J. Carty, Jr. and Steven T. Mnuchin are "audit committee financial experts," as defined in Item 401(h) of Regulation S-K promulgated by the SEC.

ITEM 1. ELECTION OF DIRECTORS

Item 1 is the election of nine nominees to our Board of Directors. All of the nominees are currently serving on our Board of Directors and have agreed to stand for reelection at the Annual Meeting. If elected, all nine nominees will hold office until the next Annual Meeting or until their successors are elected and qualified. The persons named in the enclosed proxy card (the "proxies") will vote FOR the election of all of the nominees listed below, unless otherwise instructed.

The number of Directors constituting the entire Board of Directors is currently fixed at eleven. Two of our current directors, Julian C. Day and Michael A. Miles, have decided not to stand for re-election to the Board at the Annual Meeting. Messrs. Day and Miles have indicated their intention to continue to serve as Directors until the Annual Meeting. The Board has voted to reduce the number of Directors constituting the entire Board of Directors to nine effective with the expiration of the terms of Messrs. Day and Miles at the Annual Meeting. The proxies may not vote for the election of more than nine nominees for Director at the Annual Meeting.

The Board of Directors expects all nominees to be available for election. If any nominee is not available, the proxies may vote your shares for a substituted nominee if you have submitted your proxy.

All of the current members of our Board of Directors except Richard C. Perry have served as directors since at least the consummation of the merger transaction involving Kmart Holding Corporation ("Kmart") and Sears, Roebuck and Co. ("Sears") on March 24, 2005 (the "Merger"). Mr. Perry was elected to our Board of Directors on September 26, 2005.

THE BOARD RECOMMENDS THAT YOU VOTE "FOR" ELECTION OF THE NINE NOMINEES FOR DIRECTOR.

Information regarding the Director nominees is set forth below.

Donald J. Carty, Jr., 59, served as Chairman of the Board and Chief Executive Officer of AMR Corporation and American Airlines, Inc. (air transportation) from 1998 until his retirement in 2003. He is a director of Dell, Inc., Hawaiian Holdings, Inc., CHC Helicopter Corp., Solutions Inc. and Placer Dome Inc. (which was recently acquired by Barrick Gold Corporation, for which Mr. Carty will also serve as a director).

William C. Crowley, 48, our Executive Vice President and Chief Financial Officer and Chief Administrative Officer, was previously Senior Vice President, Finance of Kmart, and had served as an officer of Kmart since 2003. Mr. Crowley is also the President and Chief Operating Officer of ESL Investments, Inc., a private investment firm, and has served in that capacity since 1999. He is a director of AutoNation, Inc.

Alan J. Lacy, 52, has served as Vice Chairman of our company and as Chairman of the Board of Sears Canada Inc. since March 2005. He was also our Chief Executive Officer from March 2005 to September 2005. Mr. Lacy served as Chairman, President and Chief Executive Officer of Sears from December 2000 to March 2005.

Edward S. Lampert, 43, Chairman of our Board of Directors, is the Chairman and Chief Executive Officer of ESL Investments, Inc., which he founded in April 1988. Mr. Lampert is a director of AutoNation, Inc. and AutoZone, Inc.

Aylwin B. Lewis, 51, has been our Chief Executive Officer and President since September 2005. From March 2005 until September 2005, Mr. Lewis served as our President and as the Chief Executive Officer of Kmart and Sears Retail. Prior to joining Kmart as Chief Executive Officer and President in October 2004, Mr. Lewis was President, Chief Multi-Branding and Operating Officer of YUM! Brands, Inc. (franchisor and licensor of quick-service restaurants) from 2000 until October 2004. Mr. Lewis is a director of The Walt Disney Company.

Steven T. Mnuchin, 43, is Chairman and Co-Chief Executive Officer of Dune Capital Management LP, a private investment firm, and has served in that capacity since September 2004. Previously, Mr. Mnuchin served as CEO of SFM Capital Management LP (an investment adviser) from 2003 to 2004 and as Vice Chairman of ESL Investments, Inc. during 2003. Prior to joining ESL, Mr. Mnuchin spent 17 years at Goldman, Sachs & Co. and served as Executive Vice President and Chief Information Officer. Mr. Mnuchin is a trustee of the Whitney Museum, the Hirshhorn Museum and Sculpture Garden Board, Riverdale Country School, New York Presbyterian Hospital and the OCD Foundation.

Richard C. Perry, 51, co-founded private investment management firm Perry Capital LLC in 1988. Prior to 1988, Mr. Perry worked in a number of capacities at Goldman, Sachs & Co. He also was an adjunct associate professor at the Stern School of Business at New York University. Mr. Perry also serves on the boards of Radio & Records, Inc. and Endurance Specialty Insurance, Ltd. He is a member of the boards of trustees of the Allen Stevenson School, Milton Academy, Facing History and Ourselves, Harlem Children's Zone and the University of Pennsylvania. Mr. Perry also serves on the Undergraduate Executive Board of the University of Pennsylvania's Wharton School.

Ann N. Reese, 52, co-founded the Center for Adoption Policy Studies in New York in 2001 and serves as its Executive Director. Prior to co-founding the Center, Ms. Reese served as a Principal with Clayton, Dubilier & Rice, a private equity investment firm, in 1999 and 2000. From 1995 to 1998, she was Executive Vice President and Chief Financial Officer of ITT Corp. Ms. Reese is a director of Xerox Corporation, Jones Apparel Group, Inc., Merrill Lynch & Co., Inc. and CBS Corporation.

Thomas J. Tisch, 51, has served as the Managing Partner of Four Partners, a private investment firm, since 1992. He is a trustee of the Manhattan Institute, New York University Medical Center and Brown University.

Information regarding current directors who are not standing for re-election is set forth below.

Julian C. Day, 53, is a private investor. Mr. Day joined Kmart in March 2002 and served as President and Chief Executive Officer of Kmart until October 2004. Mr. Day joined Sears as Executive Vice President and Chief Financial Officer in March 1999, and was Chief Operating Officer and a member of the Office of the Chief Executive from 2000 to 2002. Mr. Day is a director of PETCO Animal Supplies, Inc.

Michael A. Miles, 65, has been a Special Limited Partner of Forstmann Little & Co. and a member of its Advisory Board since February 1995. He served as Chairman of the Board and Chief Executive Officer of Philip Morris Companies Inc. (consumer products) from 1991 until his retirement in 1994. Mr. Miles is a director of AMR Corp., Citadel Broadcasting Corporation, Dell, Inc. and Time Warner Inc.

The Nominating and Corporate Governance Committee of our Board of Directors is responsible for reviewing the qualifications and independence of members of the Board and its various committees on a periodic basis, as well as the composition of the Board as a whole. This assessment includes members' qualification as independent and their economic interest in the Company through meaningful share ownership, as well as consideration of diversity, age, skills and experience in relation to the needs of the Board. Director nominees will be recommended to the Board by the Committee in accordance with the policies and principles in its charter. The ultimate responsibility for selection of director nominees resides with the Board of Directors.

The Board met eight times during fiscal 2005 (the 12-month period ended January 28, 2006). A majority of the Directors attended 100% of the Board Meetings and the meetings of the committees on which they serve, and all Directors attended at least 75% of such Board Meetings and committee meetings. Our Corporate Governance Guidelines provide that Directors are expected to attend the Annual Meeting of Stockholders.

Committees of the Board of Directors

The Board has standing Audit, Compensation, Finance, and Nominating and Corporate Governance Committees. All members of the Audit, Compensation, and Nominating and Corporate Governance Committees are independent, as defined in the NASDAQ Marketplace Rules.

The table below reflects the current membership of each committee and the number of meetings held by each committee in fiscal 2005.

| | <u>Audit</u> | <u>Compensation</u> | <u>Finance</u> | <u>Nominating and Corporate Governance</u> |
|---------------|--------------|---------------------|----------------|--|
| E. Lampert | | | X* | |
| D. Carty | X | | | |
| W. Crowley | | | X | |
| J. Day | | | | |
| A. Lacy | | | X | |
| A. Lewis | | | X | |
| M. Miles | | | | X |
| S. Mnuchin | X | | | X* |
| R. Perry | | | | |
| A. Reese | X* | X | | |
| T. Tisch | | | X* | X |
| 2005 Meetings | 9 | 5 | 5 | 5 |

*
Committee chair

Each committee operates under a written charter. The charters are available on our corporate website, www.searsholdings.com, under the heading "Corporate Governance." In addition, the Audit Committee Charter is attached as **Appendix A** to this Proxy Statement. The functions of each Committee are summarized below.

Audit Committee

Reviews the scope of the annual audit and the annual audit report of the independent auditors

Hires, subject to stockholder ratification, the firm of independent auditors to perform the annual audit

Reviews the Company's annual and quarterly financial statements, including disclosures made in management's discussion and analysis of results of operations and financial condition

Reviews the reports prepared by the independent auditors and management's responses thereto

Pre-approves audit and permitted non-audit services performed by the independent auditors

Reviews financial reports, internal controls and risk exposures

Reviews management's plan for establishing and maintaining internal controls

Reviews the scope of work performed by the internal audit staff

Compensation Committee

Reviews recommendations for and approves, subject to Board approval, the compensation of executive officers

Reviews and approves corporate goals and objectives relevant to CEO compensation, evaluates the CEO's performance and recommends to the Board the CEO's overall compensation level

Reviews and approves employment agreements, severance arrangements and change in control arrangements affecting the CEO and other senior executives

Finance Committee

Establishes and oversees matters related to capital allocation and expenditure policies and budgets

Edgar Filing: SEARS HOLDINGS CORP - Form DEF 14A

Establishes policies and procedures related to our company's share repurchase programs

Reviews our annual business plan

Reviews policies and investments related to retirement plans, including our pension and savings plans

Reviews operating performance metrics and investment rates of return

Nominating and Corporate Governance Committee

Reports annually to the full Board with an assessment of the Board's performance

Recommends to the full Board the nominees for directors

Reviews recommended compensation arrangements for the Board

Reviews and reassesses the adequacy of our Corporate Governance Guidelines

Annual Board Compensation

All non-employee Directors except Mr. Lampert are compensated for serving as Directors of our company. Each such non-employee Director receives a cash retainer of \$40,000 per year. The Audit Committee chair receives an additional retainer of \$10,000 per year. Mr. Lampert does not receive any compensation for serving as a Director. All Directors are reimbursed for out-of-pocket expenses incurred to attend meetings of the Board of Directors and committees of the Board of Directors.

Communications with the Board of Directors

You may contact any non-employee Director, or the entire Board, at any time. Your communication should be sent to the Sears Holdings Corporation Board of Directors Non-employee Directors, c/o Corporate Secretary, Sears Holdings Corporation, Law Department, 3333 Beverly Road, Hoffman Estates, IL 60179. Additional information regarding our policies on communicating with the Board of Directors can be found in our Corporate Governance Guidelines, located in the Corporate Governance section of our website, www.searsholdings.com.

Communications are distributed to the Board, or any Board member as appropriate, depending on the facts and circumstances outlined in the communication. Certain items that are unrelated to the duties and responsibilities of the Board will be excluded, such as

spam and other junk mail,

product and service complaints or inquiries,

new product suggestions,

resumes and other job inquiries,

surveys and

business solicitations or advertisements.

Material that is unduly hostile, threatening, illegal or similarly unsuitable will also be excluded. We will make available to any non-employee Director any communication that is filtered in accordance with the process described above, at that Director's request.

Nomination of Director Candidates

Directors may be nominated by the Board of Directors or by stockholders in accordance with our By-Laws. The Nominating and Corporate Governance Committee will, when appropriate, actively seek individuals qualified to become Board members, and solicit input on director candidates from a variety of sources, including current directors and our Chief Executive Officer and President. As a matter of course, the Committee will evaluate a candidate's qualifications and review all proposed nominees for the Board of Directors, including those proposed by stockholders, in accordance with its charter and our Corporate Governance Guidelines. This will include a review of the person's qualifications and independence, economic interest in the Company through meaningful share ownership, as well as consideration of diversity, age, skills

and experience in the context of the needs of the Board. While the Committee has the ability to retain a third party to assist in the nomination process, the Company has not paid a fee to any third party to identify or assist in identifying or evaluating potential nominees.

Director nominees recommended by the Nominating and Corporate Governance Committee are expected to be committed to representing the long-term interests of our stockholders. The Committee believes it is important to align the interests of directors with those of our stockholders, and therefore encourages each director and director nominee to own shares of our common stock in an amount that is meaningful to that individual. Board members should possess a high degree of integrity and have broad knowledge, experience and mature judgment. In addition to a meaningful economic commitment to our company as expressed in share ownership, directors and nominees should have predominately business backgrounds, have experience at policy-making levels in business and/or technology, and bring a diverse set of business experience and perspectives to the Board.

You can nominate a candidate for election to the Board by complying with the nomination procedures in our By-Laws. For an election to be held at an annual meeting of stockholders, nomination by a stockholder must be made by notice in writing delivered to the Corporate Secretary not later than 90 days in advance of such meeting. However, if the annual meeting is not held on or within eight days of the fourth Tuesday in May of a year, and if the Company provides stockholders with less than 100 days notice or public disclosure of the meeting date, the stockholder notice must be given not later than the 10th day following the notice or public disclosure of the meeting date. For an election to be held at a special meeting of stockholders, notice by a stockholder must be given not later than the 10th day following the date on which the Company first provides stockholders with notice or public disclosure of the meeting date.

A stockholder's notice to the Corporate Secretary must be in writing and be delivered to Sears Holdings Corporation, 3333 Beverly Road, Hoffman Estates, IL 60179, Attn: Corporate Secretary, and must include:

the name and address of the stockholder;

the name, age and business address of each nominee proposed in the notice;

such other information concerning each nominee as must be disclosed with respect to director nominees in proxy solicitations under the proxy rules of the SEC; and

the written consent of each nominee to serve as a director if so elected.

The chairman of the meeting may refuse to acknowledge the nomination of any person not made in compliance with the foregoing procedures. A stockholder's compliance with these procedures will not require the Company to include information regarding a proposed nominee in the Company's proxy solicitation materials.

Amount and Nature of Beneficial Ownership***Security Ownership of Directors and Management***

The following table sets forth information with respect to the beneficial ownership of our common stock as of January 31, 2006 by:

each of our Directors;

each Named Executive Officer (as defined under "Summary Compensation Table"); and

all of our Directors and Executive Officers as a group.

| Name of Beneficial Owner(1) | Common Stock(2) | Percent of Class(3) |
|--|-----------------|---------------------|
| D. Carty | 17,968 | * |
| W. Crowley | 0 | * |
| J. Day | 125,004 | * |
| A. Lacy | 210,335(4) | * |
| E. Lampert | 65,371,708(5) | 40.7% |
| A. Lewis | 91,465(6) | * |
| M. Miles | 5,390 | * |
| S. Mnuchin | 266,000(7)(8) | * |
| R. Perry | 2,692,000(9) | 1.7% |
| A. Reese | 10,000 | * |
| T. Tisch | 4,219,101(10) | 2.6% |
| M. Good | 6,777(11) | * |
| B. Johnson | 13,431 | * |
| D. Laughlin | 5,022(12) | * |
| P. Whitsett | 0 | * |
| Directors & Executive Officers as a group (22 persons) | 73,044,605 | 45.5% |

*

Less than 1%

(1) The address of each beneficial owner is c/o Sears Holdings Corporation, 3333 Beverly Road, Hoffman Estates, Illinois 60179.

(2) Ownership is as of January 31, 2006 and includes:

shares in which the director or executive officer may be deemed to have a beneficial interest (including shares that may be acquired upon exercise of options that are currently exercisable or will become exercisable by April 1, 2006); and

for executive officers, shares held as nontransferable restricted shares, which are subject to forfeiture under certain circumstances.

Unless otherwise indicated, the directors and executive officers listed in the table have sole voting and investment power with respect to the common stock listed next to their respective names. Information is provided for reporting purposes only and should not be construed as an admission of actual beneficial ownership.

(3)

Edgar Filing: SEARS HOLDINGS CORP - Form DEF 14A

There were 160,436,816 shares of our common stock outstanding as of January 31, 2006.

- (4) Includes 50,000 shares subject to exercisable options and 1,324 shares credited to Mr. Lacy's 401(k) Plan account.
- (5) See footnotes (c) and (d) to the Security Ownership of 5% Beneficial Owners table on pages 12 and 13.
- (6) Includes 37,500 shares subject to exercisable options.
- (7) Includes 250,000 shares owned by Dune Capital, a private investment fund controlled by Mr. Mnuchin, and 8,000 shares owned by the Steven T. Mnuchin 2002 Family Trust, the beneficial interests of which are owned by members of Mr. Mnuchin's immediate family. Mr. Mnuchin disclaims beneficial ownership of the shares owned by Dune Capital, except to the extent of his pecuniary interest therein.

Edgar Filing: SEARS HOLDINGS CORP - Form DEF 14A

- (8) Does not include 16,000 shares owned by the Mortara Trust U Article 6th, for which Mr. Mnuchin acts as trustee. Mr. Mnuchin disclaims beneficial ownership of these shares.
- (9) In an Initial Statement of Beneficial Ownership of Securities on Form 3 filed by Mr. Perry with the SEC on September 28, 2005, Mr. Perry disclosed ownership of these shares as follows: (a) 1,651,703 shares by Perry Partners International, Inc., the investment manager of which is Perry Corp., of which Mr. Perry is the President and sole shareholder; (b) 30,048 shares by Auda Classic PLC, which Perry Corp. holds the power to vote and dispose of pursuant to an investment contract; (c) 164,125 shares by Perry Commitment Fund International, L.P., the general partner of which is Perry Commitment International Associates L.L.C., of which Perry Corp. is Managing Member; (d) 85,875 shares by Perry Commitment Fund, L.P., the general partner of which is Perry Commitment Associates L.L.C., of which Perry Corp. is Managing Member; and (e) 760,249 shares by Perry Partners, L.P., the general partner of which is Perry Corp. Mr. Perry may be deemed to have voting and dispositive power with respect to all such shares. Mr. Perry disclaims beneficial ownership of all such shares, except to the extent of his pecuniary interest therein, if any.
- (10) Includes 3,139,799 shares owned by Andrew H. Tisch, Daniel R. Tisch and James S. Tisch, brothers of Thomas J. Tisch, or by trusts of which they are the managing trustees and beneficiaries, in respect of which Thomas J. Tisch has sole voting power. Thomas J. Tisch disclaims beneficial ownership of these shares.
- (11) Includes 616 shares credited to Mr. Good's 401(k) Plan account.
- (12) Includes 1,941 shares credited to Mr. Laughlin's 401(k) Plan account.

Security Ownership of 5% Beneficial Owners

The following table sets forth information with respect to beneficial ownership of our common stock by persons known by us to beneficially own 5% or more of our outstanding common stock.

| Name of Beneficial Owner | Amount and Nature of Beneficial Ownership (a) | Percent of Class |
|--|---|------------------|
| ESL Investments, Inc. and related entities, as a group(b) 200 Greenwich Ave. Greenwich, CT 06830 | 65,371,708(c)(d) | 40.7%(e) |
| Legg Mason Capital Management, Inc. and related entities, as a group(f) 100 Light Street Baltimore, MD 21202 | 11,358,193(g) | 7.06%(e) |
| Atticus Management LLC and Timothy R. Barakett 152 West 57 th Street, 45 th Floor New York, NY 10019 | 10,760,157(h) | 6.7%(e) |

a) Except as otherwise indicated, beneficial ownership is based on the latest Schedule 13G or Schedule 13D filed by the stockholder reporting its ownership as of December 31, 2005. Information is provided for reporting purposes only and should not be construed as an admission of actual beneficial ownership.

b) The group consists of ESL Investments, Inc., a Delaware corporation; Edward S. Lampert; RBS Investment Management, L.L.C., a Delaware limited liability company; ESL Institutional Partners, L.P., a Delaware limited partnership; CRK Partners, LLC, a Delaware limited liability company; RBS Partners, L.P., a Delaware limited partnership; ESL Partners, L.P., a Delaware limited partnership; ESL Investment Management, L.L.C., a Delaware limited liability company; and ESL Investors L.L.C., a Delaware limited liability company.

c)

ESL Investments, Inc. disclosed sole voting power and sole dispositive power as to 65,349,760 shares; Edward S. Lampert disclosed sole voting power and sole dispositive power as to 65,365,759 shares; CRK Partners, LLC disclosed sole voting power and sole dispositive power as to 747 shares; RBS Partners, L.P. disclosed sole voting power and sole dispositive power as to 65,010,774 shares; ESL Partners, L.P. disclosed sole voting power and sole dispositive power as to 48,068,142 shares; RBS Investment Management, L.L.C. disclosed sole voting power and sole dispositive power as to 338,239 shares; ESL Institutional Partners, L.P. disclosed sole voting power and sole dispositive power as to 338,239 shares; ESL Investors, L.L.C. disclosed

Edgar Filing: SEARS HOLDINGS CORP - Form DEF 14A

sole voting power and sole dispositive power as to 16,948,581 shares; and ESL Investment Management, L.L.C. disclosed sole voting power and sole dispositive power as to 15,999 shares.

- d) The amount of beneficial ownership of ESL Partners, L.P. and ESL Investors, L.L.C. was adjusted to reflect ownership of a total of 5,949 additional shares, reported in a Statement of Change in Beneficial Ownership on Form 4 filed with the SEC on February 14, 2006.
- e) There were 160,436,816 shares of our common stock outstanding as of January 31, 2006. The "Percent of Class" for the ESL Investments, Inc. group is based on that number of outstanding shares. The "Percent of Class" for each of the Legg Mason Capital Management and Atticus Management LLC groups was taken from the respective Schedule 13G filed by that group because Schedule 13G reports beneficial ownership as of December 31, 2005.
- f) The group consists of Legg Mason Capital Management, Inc., a Maryland corporation; Legg Mason Funds Management, Inc., a Maryland corporation; and Legg Mason Focus Capital, Inc., a Maryland corporation.
- g) Legg Mason Capital Management, Inc. disclosed shared voting power and shared dispositive power as to 9,536,410 shares; Legg Mason Funds Management, Inc. disclosed shared voting power and shared dispositive power as to 1,821,450 shares; Legg Mason Focus Capital, Inc. disclosed shared voting power and shared dispositive power as to 333 shares.
- h) Atticus Management LLC disclosed sole voting power and sole dispositive power as to 10,760,157 shares and Timothy R. Barakett disclosed shared voting power and shared dispositive power as to 10,760,157 shares.

Certain Relationships and Transactions

Our Board of Directors has delegated authority to direct investment of our surplus cash to Edward S. Lampert, subject to various limitations that have been or may be from time to time adopted by the Board of Directors and/or the Finance Committee of the Board of Directors. Mr. Lampert is Chairman of our Board of Directors and our Finance Committee and is the Chairman and Chief Executive Officer of ESL Investments, Inc. (together with its affiliated funds, "ESL"). Neither Mr. Lampert nor ESL will receive compensation for any such investment activities undertaken on our behalf. ESL beneficially owned approximately 41% of our outstanding common stock as of January 31, 2006.

Further, to clarify the expectations that the Board of Directors has with respect to the investment of our surplus cash, the Board has renounced, in accordance with Delaware law, any interest or expectancy of the Company associated with any investment opportunities in securities that may come to the attention of Mr. Lampert or any employee, officer, director or advisor to ESL and its affiliated investment entities who also serves as an officer or director of the Company (each, a "Covered Party") other than (a) investment opportunities that come to such Covered Party's attention directly and exclusively in such Covered Party's capacity as a director, officer or employee of the Company, (b) control investments in companies in the mass merchandising, retailing, commercial appliance distribution, product protection agreements, residential and commercial product installation and repair services and automotive repair and maintenance industries and (c) investment opportunities in companies or assets with a significant role in our company's retailing business, including investment in real estate currently leased by us or in suppliers for which we are a substantial customer representing over 10% of such companies' revenues, but excluding investments of ESL that were existing as of May 23, 2005.

Our company employs certain employees of ESL. William C. Crowley is a director and our Executive Vice President and Chief Financial and Chief Administrative Officer, while continuing his role as President and Chief Operating Officer of ESL. Our Vice President of Business Development and Senior Vice President of Real Estate are also employed by ESL.

Perry Capital LLC is an investment management firm controlled by Perry Corp., which is in turn controlled by Richard C. Perry, one of our Directors. On May 3, 2005, investment affiliates of Perry Capital LLC, through Capital Factors LLC, acquired the business and assets of Capital Factors, Inc. Capital Factors LLC and its predecessor (collectively, "Capital Factors") provide factoring services to companies in various industries, including those that sell into the retail industry. From time to time, Capital Factors has factored receivables (payables of the Company) for certain of our vendors, who sell the receivables to Capital Factors on a nonrecourse basis for collection by Capital Factors. As a result of Capital Factors having provided factoring services to vendors of Sears and Kmart Corporation, amounts were paid to Capital Factors by Sears and Kmart Corporation in respect of payables of those companies aggregating approximately \$60 million in 2004 and \$15 million in 2005. We expect that Capital Factors will continue to factor receivables for certain of the Company's vendors. We believe that Capital Factors handles more than \$3 billion in factoring volume.

Edgar Filing: SEARS HOLDINGS CORP - Form DEF 14A

From time to time, our pension funds may invest in investment funds for which Perry Corp. or its affiliates act as investment adviser. Perry Corp. is controlled by Richard C. Perry.

Executive Compensation

Report of the Compensation Committee

The Compensation Committee (the "Committee") was formed following the completion of the Sears, Roebuck and Co. ("Sears") and Kmart Holding Corporation ("Kmart") merger on March 24, 2005 (the "Merger"). The members of the Committee, therefore, in certain instances are reporting about past determinations made by the compensation committees of Sears and Kmart. In making compensation determinations after the Merger, the Committee developed a compensation philosophy to support a single organization with common pay practices designed to pay for performance.

The Committee is responsible to Sears Holdings Corporation's Board of Directors and to stockholders for approving compensation awarded to all of the Company's senior executives, including the Named Executive Officers. The Committee, or a sub-committee of the Committee, authorizes all awards under Sears Holdings Corporation's (the "Company") equity-based compensation plans.

Compensation Philosophy

Sears Holdings Corporation's executive compensation programs are designed to attract, motivate and retain executives critical to the Company's long-term success and the creation of stockholder value. Its fundamental philosophy is to closely link executive compensation with the achievement of annual and long-term performance goals. The Committee believes that these complex compensation decisions are best made after a deliberate review of Company performance and industry compensation levels. Sears Holdings Corporation awards compensation based upon Company, business unit and individual performance. Programs are designed to motivate our executive leadership members to achieve strategic business objectives and to continue to perform at the highest levels in the future.

The key elements of the Sears Holdings Corporation pay-for-performance compensation philosophy include base salary and incentive opportunities. Incentive opportunities include an annual incentive plan and long-term incentive programs designed to drive the correct short-term decisions that also support the long-term goals of the Company. In addition, equity grants are made on a limited basis to provide additional motivation and reward for high-performing executives.

The Committee is responsible for developing and administering the total compensation plan for executive officers of the Company. Pursuant to the Company's pay-for-performance philosophy, the compensation policies established by the Committee provide that a significant portion of each executive officer's annual compensation is contingent upon the financial performance of the Company, and also take into account the individual performance of the executive officer. Sears Holdings Corporation provides executive talent with compensation that it believes is competitive to the market and rewards its highest performers.

Sears Holdings Corporation's compensation philosophy recognizes that compensation programs must be designed to work in tandem with succession plans so that the overall level of talent improves continuously over time. As such, programs are in place to assess talent and create a robust succession plan. These programs are designed to evaluate, identify and financially reward individuals with the greatest potential to succeed in the future.

Individual Performance Evaluations

The primary factors used to evaluate Mr. Lewis' and Mr. Lacy's performance in fiscal 2005 were company profitability and the successful management of the Merger. The Committee discussed its review of Mr. Lewis' and Mr. Lacy's performance in private executive session. Each of the Company's executive officers received performance appraisals based on performance objectives relating to that executive's key accountabilities and any special projects undertaken during the year.

Compensation Program

The compensation program seeks to drive business financial performance through rewards systems focused on high levels of individual and team performance. The executive compensation program consists of three components:

Base Salary

Base salaries reward executives for contributions to Company success. The timing and amount of base salary increases depends upon the executive's past performance and experience, current level of contribution, future potential and the relevant labor market. Base salaries of those executive officers who joined the Company during fiscal year 2005 were set to attract desirable candidates to the Company during the course of the year, and the Committee believes that the market test of individual negotiations provided the best measure of relevant competitive practices. Other executive officer salaries were reviewed at the time the current Committee was created and, in some cases, revised during the year as determined advisable by the Committee as a result of the Committee's evaluation of the value of the role performed and the quality of the individual's performance in that role to the Company.

Annual Incentive Compensation

The Annual Incentive Plan for executive officers for fiscal year 2005 was based primarily on the achievement of Company and business unit EBITDA (earnings before interest, taxes, depreciation and amortization) or adjusted EBITDA goals. In addition, merchant executives have a portion of their annual incentive based on gross margin and gross profit. Some of the Company's executive officers were hired during the course of the 2005 fiscal year and were entitled to the minimum or guaranteed incentive payments specified in their respective employment agreements or offer letters.

Incentive award targets are determined by job and based on internal benchmarking and the competitive marketplace. Incentive targets for each job are defined as a percentage of base salary and include minimum, target and maximum values. In addition, similar to the process used for base salaries, incentive targets of those executive officers who joined the Company during fiscal year 2005 were set to attract desirable candidates to the Company during the course of the year, and the Committee believes that the market test of individual negotiations provided the best measure of relevant competitive practices. Other executive officer incentive targets were reviewed at the time the current Committee was created and, in some cases, revised during the year as determined advisable by the Committee as a result of the Committee's evaluation of the value of the role performed and the quality of the individual's performance in that role to the Company.

Long-Term Incentive Compensation

The Long-Term Incentive Plan focuses on motivating executives to assume accountability to achieve significant long-term lasting growth and returns by basing awards on three-year performance cycles. In April 2005, the Company initiated the Sears Holdings Corporation 2005 Senior Executive Long-Term Incentive Program (the "LTIP") for selected senior executives. The LTIP seeks to align participating executives' financial incentives with the Company's strategic direction and initiatives, which the Committee believes will thereby result in increased stockholder return. The plan is designed to reward achievement of adjusted EBITDA goals set forth therein. If the specified target adjusted EBITDA goals are achieved, each participant will receive a payment equal to his or her target award, payable in fiscal year 2008 for the performance period of fiscal year 2005 through fiscal year 2007. The LTIP also provides for minimum and maximum payment amounts that are dependent on the achievement of threshold and maximum adjusted EBITDA goals. Prior to grant the Committee reviews and approves target awards based on an evaluation of the value to the Company of the role performed. EBITDA goals for participating senior executives hired during the performance period are adjusted and target awards are prorated. The Committee believes that this plan is an important instrument in aligning the goals of the participants with the Company's financial success and that it is a valuable tool in attracting and retaining key officers.

From time to time and as business conditions warrant, the Company uses equity grants in the form of restricted shares and/or stock options to attract and retain key individuals. No equity grants were made to any of the Named Executive Officers other than Mr. Lewis and Mr. Lacy during fiscal year 2005.

CEO Compensation

At the completion of the Merger, Mr. Lacy became the CEO and Vice Chairman and Mr. Lewis became the President of the Company. On September 30, 2005, Mr. Lewis assumed the role of CEO.

Mr. Lewis' compensation follows the policies described above. Amounts paid and granted under these plans are disclosed in the compensation tables beginning on page 18. Kmart's compensation committee approved Mr. Lewis' employment agreement, which provided a 2005 annual base salary of \$1,000,000. His 2005 target incentive was based on achieving the Company's adjusted EBITDA goals. The Company's EBITDA results were below the target level of performance. Accordingly, Mr. Lewis' 2005 annual incentive of \$510,000 was also below the target level. In October 2004, Kmart granted Mr. Lewis options to purchase 150,000 shares of Kmart's common stock at an exercise price of \$88.62 per share, subject to the approval of Kmart's shareholders. Kmart's shareholders approved this grant on March 24, 2005. At the completion of the Merger, these options were converted into options to purchase 150,000 shares of the Company's common stock. The exercise price of these options did not change. The options vest in four equal annual installments on the last day of each fiscal year starting in fiscal 2005 and expire on October 18, 2014. On October 18, 2004, Mr. Lewis was also granted 50,781 Kmart Holding Corporation restricted shares with a grant price of \$88.62, subject to the approval of Kmart's shareholders. Kmart's shareholders approved this grant on March 24, 2005. These restricted shares vest in four annual installments with each of the first three installments consisting of a portion of the restricted stock that had a fair market value on October 18, 2004 of \$1 million, rounded to the nearest whole number of shares and the final installment representing the remainder of the restricted stock. With the approval of Kmart's shareholders, immediately prior to the completion of the Merger, Mr. Lewis was granted 8,011 Kmart Holding Corporation restricted shares with a grant price of \$124.82. These restricted shares vest in three equal annual installments. All restricted shares converted to Sears Holdings Corporation restricted shares at the completion of the Merger. Vesting of the restricted stock awards was subject to Kmart's achieving, for any of the fiscal years 2005 through the last fiscal year in which the shares would otherwise vest, either EBITDA, as reported in its audited financial statements, of at least \$100 million or gross proceeds from sales of real estate of at least \$50 million. The performance criteria were satisfied for fiscal 2005 and, accordingly, the first installments of restricted shares vested as of January 28, 2006.

Mr. Lacy's compensation follows the policies described above. Amounts paid and granted under these plans are disclosed in the compensation tables beginning on page 18. At the completion of the Merger, Mr. Lacy's annual base salary was \$1,500,000 pursuant to his employment agreement dated November 16, 2004 and assumed by the Company. Effective September 30, 2005, Mr. Lacy's annual base salary was reduced to \$1,000,000 to reflect his relinquishment of the CEO role. Mr. Lacy's 2005 target incentive was based on achieving the Company's adjusted EBITDA goals. The Company's EBITDA results were below the target level of performance. Accordingly, Mr. Lacy's 2005 annual incentive of \$772,296 was also below the target level. Mr. Lacy's incentive was also pro-rated for the time period in which he was CEO, with no incentive awarded for the period subsequent to his relinquishment of that role. At the completion of the Merger, pursuant to his employment agreement, Sears Holdings Corporation granted Mr. Lacy options to purchase 200,000 shares of Sears Holdings Corporation common stock at an exercise price of \$131.11 per share. The options vest in four equal annual installments on each of the four anniversary dates following the grant date and will expire on March 25, 2015. Vesting of these options will accelerate if Mr. Lacy's employment is terminated without cause, if he elects to terminate his employment in the 30 days following June 30, 2006 or in certain other circumstances that constitute "good reason" for him to terminate his employment. At the completion of the Merger, pursuant to his employment agreement, Mr. Lacy received 75,000 Sears Holdings Corporation restricted shares with a grant price of \$133.45 that become unrestricted on June 30, 2006.

Certain Tax Consequences

Internal Revenue Code Section 162(m) ("IRC Section 162(m)") provides that compensation in excess of \$1 million paid to certain executive officers is not deductible unless it is performance-based and paid under a program that meets certain other legal requirements. Neither base salary nor restricted stock that vests based solely on continued service qualify as performance-based compensation under IRC Section 162(m). A significant portion of the Company's executive compensation will satisfy the requirements for deductibility under IRC Section 162(m). However, the Committee retains the ability to evaluate the performance of our

executives and to pay appropriate compensation, even if it may result in the non-deductibility of certain compensation under federal tax law.

Compensation Committee

Thomas J. Tisch, Chair

Ann N. Reese

Compensation Committee Interlocks and Insider Participation

None of the members of the Board's Compensation Committee was, during fiscal 2005, an officer or employee of the Company. Information about transactions between the Company and its directors is set forth under "Certain Relationships and Transactions" above.

During our 2005 fiscal year, Ms. Reese and Mr. Tisch served on our Compensation Committee. In addition, Mr. Lampert served as Chairman of the Compensation Committee until September 30, 2005.

Summary Compensation Table

The following table sets forth information concerning the annual and long-term compensation paid to each person who served as our Chief Executive Officer during fiscal 2005 and to our four other most highly compensated executive officers for that fiscal year who were executive officers at the end of the fiscal year (collectively, the "Named Executive Officers"). At the completion of the Merger, Mr. Lacy became our Chief Executive Officer and Vice Chairman and Mr. Lewis became our President. On September 30, 2005, Mr. Lewis succeeded Mr. Lacy as our Chief Executive Officer. Mr. Lacy, Mr. Good and Mr. Laughlin served with Sears prior to the Merger, and Mr. Lewis, Mr. Johnson and Mr. Whitsett served with Kmart prior to the Merger. The compensation shown for the former Sears executives for

- private pay billing for our independent and assisted living communities;
- licensing and certification maintenance;
- legal services and regulatory compliance;
- central purchasing;
- budgeting and supervision of maintenance and capital expenditures;
- implementation of our growth strategy; and
- accounting, auditing and finance functions, including operations, budgeting, certain accounts receivable and collections functions, accounts payable, payroll, tax and financial reporting.

As described elsewhere in this Annual Report on Form 10 K, we have a business management agreement with The RMR Group LLC, or RMR LLC, pursuant to which RMR LLC provides to us certain business management services, including services related to compliance with various laws and rules applicable to our status as a publicly owned company, including our internal audit function, capital markets and financing activities and investor relations.

STAFFING

Independent and Assisted Living Community Staffing. Each of our independent and assisted living communities has an executive director that is responsible for the day to day operations of the applicable community, including quality of care, resident services, sales and marketing, financial performance and staff supervision. The executive director is supported by department heads who oversee the care and service of our residents, a wellness director who is responsible for coordinating the services necessary to meet the healthcare needs of our residents and a sales director who is responsible for sales and promoting our services and brand. These communities also typically have a dining services coordinator, an activities coordinator and a property maintenance coordinator.

Table of Contents

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

EMPLOYEES

As of February 17, 2017, we had approximately 24,500 employees, including approximately 16,000 full time equivalents. We believe our relations with our employees are good.

GOVERNMENT REGULATION AND REIMBURSEMENT

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

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

The healthcare industry depends significantly upon federal and state programs for revenues and, as a result, is affected by the budgetary policies of both the federal and state governments. Reimbursements under the Medicare and Medicaid programs for skilled nursing, physical therapy and rehabilitation and wellness services provided operating revenues at our outpatient clinics and some of our senior living communities (principally our SNFs). We derived approximately 22%, 22% and 23% of our consolidated revenues from continuing operations from Medicare and Medicaid programs for each of the years ended December 31, 2016, 2015 and 2014, respectively.

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

Independent Living Communities. Government benefits are not generally available for services at independent living communities, and residents in those communities use private resources to pay for their living units and the services they receive. The rates in these communities are determined by local market conditions and operating costs. However, a number of federal Supplemental Security Income program benefits pay housing costs for elderly or disabled recipients to live in these types of residential communities. The Social Security Act requires states to certify that they will establish and enforce standards for any category of group living arrangement in which a significant number of Supplemental Security Income recipients reside or are likely to reside. Categories of living arrangements that may be subject to these state standards include independent living communities and assisted living communities. Because independent living communities usually offer common dining facilities, in many jurisdictions they are required to

obtain licenses applicable to food service establishments in addition to complying with land use and life safety requirements. In addition, in some states, state or county health departments, social service agencies and/or offices on aging have jurisdiction over group residential communities for seniors and license independent living communities. To the extent that independent living communities include units to which assisted living or nursing services are provided, these units are subject to applicable state licensing regulations. If the communities receive Medicaid or Medicare funds, they are subject to certification standards and Conditions of Participation. In some states, insurance or consumer protection agencies regulate independent living communities in which residents pay entrance fees or prepay for services.

Assisted Living Communities. A majority of states provide or are approved to provide Medicaid payments for personal care and medical services to some residents in licensed assisted living communities under waivers granted by or under Medicaid state plans approved by the Centers for Medicare and Medicaid Services, or CMS, of the United States Department of

Table of Contents

Health and Human Services, or HHS. State Medicaid programs control costs for assisted living and other home and community based services by various means such as restrictive financial and functional eligibility standards, enrollment limits and waiting lists. Because rates paid to assisted living community operators are generally lower than rates paid to SNF operators, some states use Medicaid funding of assisted living as a means of lowering the cost of services for residents who may not need the higher level of health services provided in SNFs. States that administer Medicaid programs for services in assisted living communities are responsible for monitoring the services at, and physical conditions of, the participating communities.

As a result of the large number of states using Medicaid funds to purchase services at assisted living communities and the growth of assisted living in recent years, states have adopted licensing standards applicable to assisted living communities. According to the National Center for Assisted Living and the HHS Office of the Assistant Secretary for Planning and Evaluation, all states regulate assisted living and residential care communities, although states do not use a uniform approach. Most state licensing standards apply to assisted living communities regardless of whether they accept Medicaid funding. Also, according to the National Conference of State Legislatures, a few states require certificates of need, or CONs, from state health planning authorities before new assisted living communities may be developed. Based on our analysis of recent economic and regulatory trends, we believe that assisted living communities that become dependent upon Medicaid or other government payments for a majority of their revenues may decline in value because Medicaid and other public rates may fail to keep up with increasing costs. We also believe that assisted living communities located in states that adopt CON requirements or other limitations on the development of new assisted living communities may increase in value because those limitations may help ensure higher nongovernment rates and reduced competition.

HHS, the Senate Special Committee on Aging, and the Government Accountability Office, or the GAO, have studied and reported on the development of assisted living and its role in the continuum of long term care and as an alternative to SNFs. Since 2003, CMS has commenced a series of actions to increase its oversight of state quality assurance programs for assisted living communities and has provided guidance and technical assistance to states to improve their ability to monitor and improve the quality of services paid for through Medicaid waiver programs. CMS is encouraging state Medicaid programs to expand their use of home and community based services as alternatives to institutional services, pursuant to provisions of the Deficit Reduction Act of 2005, or the DRA, the Patient Protection and Affordable Care Act, as amended by the Health Care and Education Reconciliation Act, or collectively, the ACA, and other authorities, through the use of several programs. One such program, the Community First Choice Option, or the CFC Option, grants states that choose to participate in the program a 6% increase in federal matching payments for related medical assistance expenditures. As of March 2016, eight states had obtained a State Plan Amendment to participate in the CFC Option. We are unable to predict the effect of the implementation of the CFC Option and other similar programs, but their impact may be adverse and material to our operations and our future financial results of operations.

Skilled Nursing Facilities—Reimbursement. A majority of all SNF revenues in the United States comes from publicly funded programs. According to CMS, Medicaid is the largest source of public funding for SNFs, followed by Medicare. In 2015, approximately 32% of nursing care facility and continuing care retirement community revenues came from Medicaid and 24% from Medicare.

SNFs are highly regulated businesses. The federal and state governments regularly monitor the quality of care provided at SNFs. State health departments conduct surveys of resident care and inspect the physical condition of SNF properties. These periodic inspections and occasional changes in life safety and physical plant requirements sometimes require SNF operators to make significant capital improvements. These mandated capital improvements have usually resulted in Medicare and Medicaid rate adjustments, albeit on the basis of amortization of expenditures over the expected useful lives of the improvements.

Under the Medicare SNF prospective payment system, or SNF PPS, capital costs are part of the prospective rate and are not community specific. The SNF PPS and other recent legislative and regulatory actions with respect to state Medicaid rates limit the reimbursement levels for some SNF services. At the same time, federal and state enforcement agencies have increased oversight of SNFs, making licensing and certification of these communities more rigorous.

CMS implemented the SNF PPS pursuant to the Balanced Budget Act of 1997. Under the SNF PPS, SNFs receive a fixed payment for each day of care provided to residents who are Medicare beneficiaries. The SNF PPS requires SNFs to assign each resident to a care group depending on that resident's medical characteristics and service needs. These care groups are known as Resource Utilization Groups, or RUGs, and CMS establishes a per diem payment rate for each RUG. Effective October 2010, CMS adopted rules that implemented a new SNF PPS case mix classification system known as RUG-IV. CMS also requires the use of a resident assessment instrument called the Minimum Data Set 3.0, which SNFs must use to collect

Table of Contents

clinical data to assign residents to RUG IV reimbursement categories. Medicare SNF PPS payments cover substantially all services provided to Medicare residents in SNFs, including ancillary services such as rehabilitation therapies.

CMS updates SNF PPS payment rates each year by a market basket update to account for inflation and periodically implements changes to the RUG categories and payment rates. Since federal fiscal year 2012, the ACA has also reduced SNF PPS payment rates each year by a productivity adjustment based on national economic productivity statistics. Following the implementation of RUG-IV, Medicare billing increased nationally, partially because of the unexpectedly large proportion of patients grouped in the highest paying RUG therapy categories. CMS did not intend for the implementation of RUG-IV to increase Medicare billing. In 2011, CMS adopted a final rule designed to recalibrate the Medicare SNF PPS, which resulted in a reduction in aggregate Medicare payment rates for SNFs of approximately 11.1%, or \$3.87 billion, in federal fiscal year 2012. In subsequent years, CMS slightly increased the Medicare SNF PPS rates and estimated that those rates would increase payments to SNFs by an aggregate of approximately 1.8% for federal fiscal year 2013, 1.3% for federal fiscal year 2014, 2.0% for federal fiscal year 2015 and 1.2% for federal fiscal year 2016. In July 2016, CMS issued a final rule updating Medicare payments to SNFs for federal fiscal year 2017, which CMS estimated would increase payments to SNFs by an aggregate of 2.4%, or approximately \$920.0 million, compared to payments in federal fiscal year 2016. Due to the previous reduction of Medicare payment rates of approximately 11.1% for federal fiscal year 2012 discussed above, however, Medicare payment rates will be lower for federal fiscal year 2017 than they were in federal fiscal year 2011. The Medicare Access and CHIP Reauthorization Act of 2015, or MACRA, discussed below, limits the market basket increase for SNFs to 1.0% in federal fiscal year 2018. It is unclear whether these adjustments in Medicare rates will compensate for the increased costs we may incur for services to our residents whose services are paid for by Medicare.

The Middle Class Tax Relief and Job Creation Act of 2012, which was enacted in February 2012, incrementally reduced the SNF reimbursement rate for Medicare bad debt from 100% to 65% by federal fiscal year 2015 for beneficiaries dually eligible for Medicare and Medicaid. Because nearly 90% of SNF bad debt has historically been related to dual eligible beneficiaries, this rule has a substantial negative effect on SNFs, including some that we operate. The same law also reduced the SNF Medicare bad debt reimbursement rate for Medicare beneficiaries not eligible for Medicaid from 70% to 65% in federal fiscal year 2013 and going forward.

In addition, the Budget Control Act of 2011 and the Bipartisan Budget Act of 2013 allow for automatic reductions in federal spending by means of a process called sequestration, which reduces Medicare payment rates by 2.0% through 2023. In 2014 and 2015, Congress approved two additional one year extensions of Medicare sequestration, through 2025. Medicaid is exempt from the automatic reductions, as are certain Medicare benefits. The automatic 2.0% payment cuts took effect in April 2013 and had an adverse effect on our operations and financial results. Subsequent legislation appears to have modified some aspects of the sequestration process, but at this time it is unclear what impact this legislation may have on Medicare payments we receive. Any future reductions in Medicare payment rates could be adverse and material to our operations and to our future financial results of operations.

The federal government is seeking to slow the growth of Medicare and Medicaid payments for SNF services by several methods. In 2006, the government implemented limits on Medicare payments for outpatient therapies and then, pursuant to the DRA, created an exception process under which beneficiaries could request an exception from the cap and be granted the amount of services deemed medically necessary by Medicare. In April 2014, the Protecting Access to Medicare Act of 2014, or PAMA, extended the Medicare outpatient therapy cap exception process through March 2015, further postponing the implementation of firm limits on Medicare payments for outpatient therapies. PAMA also extended the 0.5% increase to the Medicare Physician Fee Schedule, or MPFS, rates through December 2014 and provided no increase in the MPFS rates, to which our Medicare outpatient therapy rates are tied, in the period between January 2015 and March 2015. In April 2015, Congress passed MACRA, which extended the outpatient therapy cap exceptions process from March 2015 through December 2017, further postponing the implementation of strict limits on Medicare payments for outpatient therapies. MACRA also repealed the Sustainable Growth Rate, or SGR, formula for calculating updates to MPFS rates, which would have led to a 21.2% rate reduction

effective April 2015, and replaced the SGR formula with a different reimbursement methodology, which is discussed in more detail below. Under MACRA, there were and will be MPFS conversion factor updates of 0.0% from January 2015 through June 2015, 0.5% from July 2015 through December 2015, 0.5% each year from 2016 through 2019 and 0.0% from 2020 through 2025.

The DRA established the five year Money Follows the Person demonstration project in 2007 to award competitive grants to 30 states to provide home and community based long term care services to qualified individuals relocated from SNFs, and to increase federal medical assistance for each qualifying beneficiary for a limited time period. The ACA expanded eligibility for this program and extended this program for an additional five years through 2016. According to the Henry J.

Table of Contents

Kaiser Family Foundation, as of May 2016, 43 states and the District of Columbia had operational Money Follows the Person programs.

The DRA also established the Post-Acute Care Payment Reform demonstration project under which CMS compared and assessed patient care needs, costs and outcomes of services at different post-acute care sites over three years. In January 2012, CMS issued a report to Congress regarding the project stating that CMS had successfully used a new uniform patient assessment tool to measure patient acuity in acute care hospitals and post-acute settings, providing the basis for the potential development of new standardized information reporting requirements and more uniform post-acute case mix payment systems. States are also permitted to include home and community based services as optional services under their Medicaid state plans or through Medicaid waiver programs, and states opting to do so may establish more stringent needs based criteria for SNF services than for home and community based services. The ACA expands the services that states may provide and limits their ability to set caps on enrollment, waiting lists or geographic limitations on home and community based services.

In addition, the DRA increased the “look-back” period for prohibited asset transfers that disqualify individuals from Medicaid SNF benefits from three to five years. The period of Medicaid ineligibility begins on the date of the prohibited transfer or the date an individual has entered the SNF and would otherwise be eligible for Medicaid coverage, whichever occurs later, rather than on the date of the prohibited transfer, effectively extending the Medicaid penalty period and requiring SNFs to collect charges directly from residents and their transferees.

Although Medicaid is exempt from the sequestration process described above, some of the states in which we operate either have not raised Medicaid rates by amounts sufficient to offset increasing costs or have frozen or reduced, or are expected to freeze or reduce, Medicaid rates. Some states are expanding their use of managed care, partly to control Medicaid program costs. According to the CMS Office of the Actuary, Medicaid enrollment is estimated to have increased 9.2% in 2014, 7.6% in 2015 and 3.1% in 2016, due primarily to the expansion in Medicaid eligibility under the ACA, which began in 2014. In addition, Medicaid enrollment is projected to increase at an average annual rate of 1.5% from 2016 through 2025.

We are unable to predict the impact on us of these or other recent legislative and regulatory actions or proposed actions with respect to federal Medicare rates, state Medicaid rates and the federal payments to states for Medicaid programs.

Skilled Nursing Facilities—Quality Improvement, Pay-for-Performance and Value-Based Purchasing Initiatives. In addition to the reimbursement and rate changes discussed above, payments to SNFs will be increasingly determined by the quality of care provided. The federal government has enhanced its focus on developing and imposing quality-related regulations, standards and programs to improve the quality of care provided at SNFs and to better align payment to quality outcomes. As mandated by MACRA, PAMA and the Improving Medicare Post-Acute Care Transformation Act of 2014, or the IMPACT Act, HHS and CMS have established different programs to achieve these goals, including the Quality Payment Program, the SNF Value-Based Purchasing Program and the SNF Quality Reporting Program described below. In addition, CMS maintains and enforces Conditions of Participation that healthcare organizations must meet in order to participate in the Medicare and Medicaid programs. These standards are designed to improve quality of care and protect the health and safety of beneficiaries. Through the Conditions of Participation, CMS is able to require certain quality standards protocols, including most recently, requiring SNFs to implement a quality assurance and performance improvement program. We are unable to predict the impact of these quality improvement initiatives on our Medicare reimbursement rates or the cost of our SNFs’ operations.

In October 2016, CMS issued a final rule to implement the Merit-Based Incentive Payment System, or MIPS, and Advanced Alternative Payment Models, or APMs, which together CMS calls the Quality Payment Program. These reforms were mandated under MACRA and replace the SGR methodology for updates to the MPFS to which our Medicare outpatient therapy rates are tied. Starting in 2019, providers may be subject to either MIPS payment adjustments or APM incentive payments. MIPS is a new Medicare program that combines certain parts of existing quality and incentive programs into a single program that addresses quality, resource use, clinical practice activities and meaningful use of electronic health records. APMs are innovative models approved by CMS for paying healthcare providers for services provided to Medicare beneficiaries which draw on existing programs, such as the bundled payment and shared savings models. Our Medicare Part B outpatient therapy revenue rates are tied to the

MPFS and may be affected by these regulatory changes.

PAMA established a SNF Value-Based Purchasing Program, which is intended to increase quality of care and reduce preventable hospitalizations. Under this program, HHS will assess SNFs based on hospital readmissions and make these assessments available to the public by October 2017. As part of PAMA implementation, in the SNF PPS final rule for fiscal year 2016, CMS adopted a 30 day all-cause, all-condition hospital readmission measure for SNFs, which was replaced with an all-condition, risk-adjusted potentially preventable hospital readmission rate measure in the SNF PPS final rule for fiscal year 2017. Under PAMA, beginning in federal fiscal year 2019, Medicare payment rates will be partially based on SNFs'

Table of Contents

performance scores on this measure. To fund the program, CMS will reduce Medicare payments to all SNFs by 2.0% through a withhold mechanism starting in October 2018 and then redistribute between 50% and 70% of the withheld payments as incentive payments to those SNFs with the highest rankings on this measure.

In October 2014, President Obama signed into law the IMPACT Act, which requires certain post-acute care providers, including SNFs, to begin collecting and reporting various types of data. Specifically, under the SNF Quality Reporting Program, HHS required SNFs to begin reporting certain quality measures and resource use measures in a standardized and interoperable format as of October 2016 and to begin reporting certain patient assessment data in such a format by October 2018. Beginning in federal fiscal year 2018, SNFs that fail to timely comply with the reporting requirements will be subject to a 2.0% reduction in their Medicare payment rates for that fiscal year. Beginning October 2018, HHS will make this data publicly available pursuant to certain procedures to be established. The IMPACT Act also requires the Secretary of HHS and the Medicare Payment Advisory Commission to submit reports to Congress recommending a future Medicare PPS for post-acute care providers and analyzing both its effects on the reported metrics and financial effect on post-acute care providers.

In September 2016, CMS issued a final rule to comprehensively update the Conditions of Participation for long term care facilities that participate in Medicare and Medicaid, such as our SNFs. The final rule, which went into effect beginning in November 2016, institutes a broad range of new requirements, some of which stem from statutory modifications under the ACA and the IMPACT Act. The requirements under the final rule largely match those set forth in the proposed rule, which was released by CMS in July 2015. In particular, the final rule requires our SNFs, in a multi-phased approach over the next few years, to: train staff on care for residents with dementia and on abuse prevention; consider residents' health needs when making decisions about the kinds and levels of staffing; ensure that staff have the appropriate skills and competencies to provide individualized, resident centered care; augment care planning activities, including considering residents' goals and preferences and, on discharge, giving residents necessary follow up information and improving communication with receiving facilities or services; permit dietitians and therapy providers to write orders under certain circumstances; meet heightened food and nutrition services requirements; implement an updated infection prevention and control program, including requiring each of our SNFs to designate an infection prevention and control officer; and strengthen residents' rights. In addition, the final rule requires our SNFs to: alter their staffing levels and competencies based on the results of mandated facility assessments; develop, implement and maintain a compliance and ethics program and a quality assurance and performance improvement program; and implement new practices surrounding the preparation and implementation of care plans and discharge summaries, among other new requirements. These requirements will increase the cost of operations for long term care facilities that participate in Medicare and Medicaid, including our SNFs. Specifically, CMS estimated in the final rule that the cost of complying with all of the new requirements per facility would be approximately \$62,900 in the first year, and approximately \$55,000 each year thereafter. However, we believe new requirements often cost considerably more than CMS estimates.

In August 2015, CMS announced that it will conduct the second phase of another SNF quality improvement program, the Initiative to Reduce Avoidable Hospitalizations Among Nursing Facility Residents, a pilot program first announced in 2012, which will be continued in partnership with selected organizations from October 2016 to October 2020. In this phase of the initiative, participants will test whether a new payment model for SNFs and practitioners, together with clinical and educational interventions that participants are currently implementing, will further reduce avoidable hospitalizations, lower combined Medicare and Medicaid spending and improve the quality of care received by long stay SNF residents.

As these quality improvement initiatives increase in size and scope, the federal government will likely monitor the impact of these programs more closely. For example, in October 2015, the GAO released a report calling for CMS to improve its data collection and oversight of SNFs to facilitate enhanced monitoring of the success of CMS's quality improvement activities, and HHS concurred with the GAO's recommendations. We are unable to predict the impact on us of these or other recent legislative and regulatory quality improvement actions or proposed actions.

Skilled Nursing Facilities—Survey and Enforcement. Pursuant to the Omnibus Reconciliation Act of 1987, Congress enacted major reforms to federal and state regulatory systems for SNFs that participate in the Medicare and Medicaid programs. Since then, the GAO has reported that, although much progress has been made, substantial problems

remain in the effectiveness of federal and state regulatory activities. The HHS Office of Inspector General, or the OIG, has issued several reports concerning quality of care and billing practices in SNFs, and the GAO has issued several reports recommending that CMS and states strengthen their compliance and enforcement practices, including federal oversight of state actions and to ensure that SNFs provide adequate care and states act more consistently. Moreover, in its fiscal year 2017 work plan, the OIG specifically stated that it will review compliance with various aspects of the SNF PPS, including the documentation requirement in support of claims paid by Medicare, and assess the incidence of serious quality of care issues, such as neglect. In recent years, the OIG and the GAO have also repeatedly called for increased oversight and payment system reform for SNFs.

Table of Contents

In June 2015, the OIG issued a report calling for CMS to accelerate efforts to implement a new method for paying SNFs for therapy, based on findings that many SNFs incorrectly or inconsistently used CMS's new patient assessments. The OIG also recommended that CMS reduce the financial incentive for SNFs to use assessments differently when decreasing and increasing therapy services and that it strengthen the oversight of SNF billing for changes in therapy. CMS concurred with these recommendations. In September 2015, the OIG issued another report questioning the appropriateness of payments to SNFs under the SNF PPS, and stating that Medicare payments for therapy greatly exceeded SNFs' costs for therapy. The OIG recommended that CMS evaluate the extent to which Medicare payment rates for therapy should be reduced, change the method for paying for therapy, adjust Medicare payments to eliminate any increases that are unrelated to beneficiary characteristics and strengthen oversight of SNF billing. CMS concurred with these recommendations and noted that it is working to identify potential alternative methodologies for paying for SNF PPS services, including therapy.

In addition to scrutiny from the GAO and the OIG, the Senate Special Committee on Aging and other congressional committees have also held hearings on related SNF issues. As a result, CMS has undertaken several initiatives to increase the effectiveness of Medicare and Medicaid SNF survey and enforcement activities. CMS has been taking steps to identify and focus enforcement efforts on SNFs and chains of SNF operators with findings of substandard care or repeat violations of Medicare and Medicaid standards. CMS has also increased its oversight of state survey agencies and has improved the process by which data is captured from these surveys. As an added measure of improving patient care, the ACA provides for the funding of a state background check system for job applicants to long term care providers who will have direct access to patients. CMS has begun the administration of this program, and, as of December 2016, had awarded funding to approximately half of the states.

In addition, CMS adopted regulations expanding federal and state authority to impose civil monetary penalties in instances of noncompliance. When CMS or state agencies identify deficiencies under state licensing and Medicare and Medicaid standards, they may impose sanctions and remedies such as denials of payment for new Medicare and Medicaid admissions, civil monetary penalties, state oversight, temporary management or receivership and loss of Medicare and Medicaid participation or licensure on SNF operators. Our communities may incur sanctions and penalties from time to time. If we are unable to cure deficiencies that have been identified or that are identified in the future, or if appeals of proposed sanctions or penalties are not successful, decertification or additional sanctions or penalties may be imposed. These consequences may adversely affect our ability to meet our financial obligations and negatively affect our financial condition and results of operations.

Certificates of Need. As a mechanism to prevent overbuilding and subsequent healthcare price inflation, many states limit the number of SNFs by requiring developers to obtain CONs before new facilities may be built or additional beds may be added to existing facilities. As noted above, a few states also limit the number of assisted living facilities by requiring CONs. In addition, some states (such as California and Texas) that have eliminated CON laws have retained other means of limiting new development, including moratoria, licensing laws or limitations upon participation in the state Medicaid program. These government requirements limit expansion, which we believe may make existing SNFs more valuable by limiting competition.

Healthcare Reform. The ACA, signed into law in March 2010, has resulted in changes to insurance, payment systems and healthcare delivery systems. The ACA is intended to expand access to health insurance coverage and reduce the growth of healthcare expenditures while simultaneously maintaining or improving the quality of healthcare. Some of the provisions of the ACA took effect immediately, whereas others will take effect at later dates. Due to the complexity of the ACA, its ramifications may only become apparent through later regulatory and judicial interpretations. In addition, to the extent the ACA is repealed and replaced under the new Trump Administration and the 115th Congress, additional risks and regulatory uncertainty may arise. Depending upon what aspects of the ACA are repealed and whether and how they are replaced, our future financial results could be adversely and materially affected.

The ACA establishes an Independent Payment Advisory Board to submit legislative proposals to Congress and take other actions with a goal of reducing Medicare spending growth. When and if such spending reductions take effect they may be adverse and material to our financial results. The ACA also provides for the National Pilot Program on

Payment Bundling to develop and evaluate making bundled payments for services provided during an episode of care, to include hospital and physician services and post acute care such as SNF services. The pilot program can be expanded at any point after January 2016 if it meets its goals. The ACA also includes the development of Medicare value based purchasing plans to include quality measures as a basis for bonuses and several initiatives to encourage states to develop and expand home and community based services under Medicaid.

The ACA includes various other provisions affecting Medicare and Medicaid providers, including expanded public disclosure requirements for SNFs and other providers, enforcement reforms and increased funding for Medicare and Medicaid program integrity control initiatives. The ACA has resulted in several changes to existing healthcare fraud and abuse laws,

Table of Contents

established additional enforcement tools and funding to the government, and provided for increased cooperation between agencies by establishing mechanisms for sharing information relating to noncompliance. Furthermore, the ACA has resulted in enhanced criminal and administrative penalties for noncompliance. For example, the ACA amended the Anti Kickback Statute to provide that a claim that includes items or services resulting from a violation of the Anti Kickback Statute now constitutes a false or fraudulent claim for purposes of the False Claims Act. In June 2012, the U.S. Supreme Court upheld two major provisions of the ACA—the individual mandate, which requires most Americans to maintain health insurance or to pay a penalty, and the Medicaid expansion, which requires states to expand their Medicaid programs by 2014 to cover all individuals under the age of 65 with incomes not exceeding 133% of the federal poverty level. In upholding the Medicaid expansion, the U.S. Supreme Court held that it violated the U.S. Constitution as drafted but remedied the violation by modifying the expansion to preclude the Secretary of HHS from withholding existing federal Medicaid funds from states that fail to comply with Medicaid expansion, instead allowing the Secretary only to deny new expansion funding. Under the ACA, the federal government will pay for 100% of a state’s Medicaid expansion costs for the first three years (2014–2016) and gradually reduce its subsidy to 90% for 2020 and future years. Based on the ruling, states may choose not to participate in the Medicaid expansion program without risking the loss of existing federal Medicaid funding. As of January 1, 2017, 31 states plus the District of Columbia had elected to expand Medicaid eligibility as provided under the ACA and 19 states had elected not to broaden Medicaid eligibility as of that date; those states that ultimately choose not to participate in Medicaid expansion will forgo the federal funds that would otherwise be available for that purpose. It is unclear what effect the U.S. Supreme Court ruling may have on future federal funding for states’ Medicaid programs. We expect that the reduction of the federal subsidy to 90% for 2020 and future years, and other budgetary constraints on state governments, may cause some states to reduce Medicaid payments to healthcare services providers like us. In addition, in June 2015, the U.S. Supreme Court decided that income tax credits under the ACA are available to individuals who purchase health insurance on an exchange created by the federal government, in the same way such credits are available to individuals who purchase health insurance on an exchange created by a state. Such subsidies provide certain eligible taxpayers with the ability to purchase or maintain health insurance. We cannot estimate the type and magnitude of the potential Medicare and Medicaid policy changes, rate reductions or other changes and the impact on us of the possible failure of these programs to increase rates to match our increasing expenses, but they may be material to and adversely affect our future results of operations. Similarly, we are unable to predict the impact on us of the insurance reforms, payment reforms, and healthcare delivery systems reforms contained in and to be developed pursuant to the ACA. Expanded insurance availability may provide more paying customers for the services we provide. If the changes implemented under the ACA result in reduced payments for our services or the failure of Medicare, Medicaid or insurance payment rates to cover our costs, however, our future financial results could be adversely and materially affected. In addition, other aspects of the ACA that affect employers generally, including the employer shared responsibility provisions that the Internal Revenue Service began enforcing in January 2015, may have an impact on the design and cost of the health coverage that we offer to our employees. Due to the scope and complexity of the provisions of the ACA that apply to employers and employer group health plans, it is difficult to predict the overall impact of the ACA on our employee benefit plans and our cost of doing business over the coming years. We will continue to analyze how to provide our employees with cost effective coverage, taking into account the various requirements of the ACA and the impact of any changes on our ability to attract and retain employees. For information on some recent changes that we have made to the health insurance coverage we offer employees in response to the rising cost of health insurance generally, see “Business—Insurance” in Part I, Item 1 of this Annual Report on Form 10-K.

Other Matters. Federal and state efforts to target false claims, fraud and abuse and violations of anti kickback laws, physician referral laws (including the Ethics in Patient Referrals Act of 1989), privacy laws and consumer protection laws by Medicare and Medicaid providers and providers under other public and private programs have increased in recent years, as have civil monetary penalties, treble damages, repayment requirements and criminal sanctions for noncompliance. The federal False Claims Act, as amended and expanded by the Fraud Enforcement and Recovery Act of 2009, and the ACA, provides significant civil money penalties and treble damages for false claims and authorizes individuals to bring claims on behalf of the federal government for false claims. The federal Civil Monetary Penalties

Law authorizes the Secretary of HHS to impose substantial civil penalties, treble damages and program exclusions administratively for false claims or violations of the federal Anti Kickback Statute. In addition, the ACA increased penalties under federal sentencing guidelines by between 20% and 50% for healthcare fraud offenses involving more than \$1.0 million. State Attorneys General typically enforce consumer protection laws relating to senior living services, clinics and other healthcare facilities.

Government authorities are devoting increasing attention and resources to the prevention, detection and prosecution of healthcare fraud and abuse. The OIG has guidelines for SNFs intended to assist them in developing voluntary compliance

Table of Contents

programs to prevent fraud and abuse; these guidelines recommend that CMS identify SNFs that are billing for higher paying RUGs and more closely monitor their compliance with patient therapy assessments as methods of fraud prevention. CMS contractors are expanding the retroactive audits of Medicare claims submitted by SNFs and other providers, and recouping alleged overpayments for services determined by auditors not to have been medically necessary or not to meet Medicare coverage criteria as billed. State Medicaid programs and other third party payers are conducting similar medical necessity and compliance audits.

The ACA facilitates the Department of Justice's, or the DOJ's, ability to investigate allegations of wrongdoing or fraud at SNFs, in part because of increased cooperation and data sharing among CMS, the OIG, the DOJ and the states. In January 2016, the OIG and the DOJ announced a settlement and corporate integrity agreement with the largest provider of contract therapy services in the nation, as well as settlements with four SNFs, all alleged to have submitted false claims for therapy services provided to SNF patients. The significant nature of the settlements indicates that the federal government is increasingly focused on the appropriateness of billing practices of, and medical necessity of services provided at, SNFs. In addition, the ACA requires all states to terminate the Medicaid participation of any provider that has been terminated under Medicare or any other state Medicaid plan. Moreover, state Medicaid fraud control agencies may investigate and prosecute assisted living communities and SNFs, clinics and other healthcare facilities under fraud and patient abuse and neglect laws. In March 2016, the DOJ also announced the launch of 10 regional intergovernmental task forces across the country to identify and take enforcement action against SNFs that provide substandard care to residents. We expect that increased enforcement and monitoring by government agencies will cause us to expend considerable amounts on regulatory compliance and likely reduce the profits available from providing healthcare services.

Current state laws and regulations allow enforcement officials to make determinations as to whether the care provided at our communities exceeds the level of care for which a particular community is licensed. A finding that a community is delivering care beyond the scope of its license could result in closure of the community and the immediate discharge and transfer of residents. Some states and the federal government allow certain citations of one community to impact other communities operated by the same entity or a related entity, including communities in other states. Revocation of a license or certification at one of our communities could therefore impact our ability to obtain new licenses or certifications or to maintain or renew existing licenses and certifications at other communities, and trigger defaults under our leases, our management agreements with SNH and our new credit facility or adversely affect our ability to operate or obtain financing in the future. In addition, an adverse finding by state officials could serve as the basis for lawsuits by private plaintiffs and lead to investigations under federal and state laws, which could result in civil and/or criminal penalties against the community as well as a related entity.

Our communities must comply with laws designed to protect the confidentiality and security of individually identifiable patient information. Under the federal Health Insurance Portability and Accountability Act of 1996, or HIPAA, and the Health Information Technology for Economic and Clinical Health Act, or the HITECH Act, our communities that are covered entities within the meaning of HIPAA must comply with rules adopted by HHS governing the privacy, security, use and disclosure of individually identifiable information, including financial information and protected health information, or PHI, and security rules for electronic PHI. There may be both civil monetary penalties and criminal sanctions for noncompliance with these laws. Under the HITECH Act, penalties for violation of certain provisions may be as high as \$50,000 per violation for a maximum civil penalty of \$1.5 million per calendar year. In January 2013, HHS released the HIPAA Omnibus Rule, or the Omnibus Rule, which went into effect in March 2013 and required compliance with most provisions by September 2013. Pursuant to the Omnibus Rule, covered entities were required to make certain modifications to any business associate agreements that they have in place with their business associates within the meaning of HIPAA. Further, the Omnibus Rule modified the standard for providing breach notices, which was previously based on an analysis of the harm resulting from any disclosure, to a more objective analysis on whether any PHI was actually acquired or viewed as a result of the breach. In addition to HIPAA, many states have enacted their own security and privacy laws relating to individually identifiable information, including financial information and PHI. In some states, these laws are more burdensome than HIPAA. In instances in which the state provisions are more stringent than or differ from HIPAA, our communities must comply with both the applicable federal and state standards. If we fail to comply with applicable

federal or state standards, we could be subject to civil sanctions and criminal penalties, which could materially and adversely affect our business, financial condition and results of operations. HIPAA enforcement efforts have increased considerably over the past few years, with HHS, through its Office for Civil Rights, entering into several multi-million dollar HIPAA settlements in 2016 alone.

Our communities must also comply with the Americans with Disabilities Act, or the ADA, and similar state and local laws to the extent that such communities are “public accommodations” as defined in those laws. The obligation to comply with the ADA and other similar laws is an ongoing obligation, and we continue to assess our communities and make appropriate modifications.

Table of Contents

Other legislative proposals introduced in Congress, proposed by federal or state agencies or under consideration by some state governments include the option of block grants for states rather than federal matching money for certain state Medicaid services, laws authorizing or directing Medicare to negotiate rate reductions for prescription drugs, additional Medicare and Medicaid enforcement procedures and federal and state cost containment measures, such as freezing Medicare or Medicaid SNF payment rates at their current levels and reducing or eliminating annual Medicare or Medicaid inflation allowances or gradually reducing rates for SNFs.

Some of the states in which we operate either have not raised Medicaid rates by amounts sufficient to offset increasing costs or have frozen or reduced, or are expected to freeze or reduce, Medicaid rates. Medicaid spending grew an estimated 11.6% in 2014 and 9.7% in 2015, and is projected to grow 3.7% in 2016 and 2017, primarily due to increased enrollment as some states chose to expand Medicaid coverage under the ACA. From 2018 through 2025, Medicaid spending is expected to grow by an average annual rate of 5.9%, mainly driven by increased spending per beneficiary due to aging of the population and more gradual growth in enrollment. Effective June 30, 2011, Congress ended certain temporary increases in federal payments to states for Medicaid programs that had been in effect since 2008. We expect the ending of these temporary federal payments, combined with other state budgetary pressures, to result in continued challenging state fiscal conditions, particularly in those states that are not participating in Medicaid expansion. As a result, some state budget deficits may increase, and certain states may continue to reduce Medicaid payments to healthcare providers like us as part of an effort to balance their budgets. These state level cuts have the potential to negatively impact our revenue from Medicaid sources.

INSURANCE

Litigation against senior living and healthcare companies continues to increase, and liability insurance costs continue to increase as a result. In addition, our employee benefit costs, including health insurance and workers' compensation insurance costs, continue to increase. To partially offset these insurance cost increases, we have taken a number of actions, including:

- becoming fully self insured for all health related claims of covered employees;
- increasing the deductible or retention amounts for which we are liable under our liability insurance;
- establishing an offshore captive insurance company which participates in our workers' compensation and professional and general liability insurance programs, which may allow us to reduce our net insurance costs by retaining the earnings on our reserves, provided our claims experience does not exceed that projected by various statutory and actuarial formulas;
- increasing the amounts that some of our employees are required to pay for health insurance coverage and copayments for health services and pharmaceutical prescriptions and decreasing the amount of certain healthcare benefits as well as adding a high deductible health insurance plan as an option for our employees;
- hiring insurance and other professional advisors to help us establish programs to reduce our workers' compensation and professional and general liabilities, including a program to monitor and proactively settle liability claims and to reduce workplace injuries;
- hiring insurance and other professional advisors to help us establish appropriate reserves for our retained liabilities and captive insurance programs; and
- participating with RMR LLC and other companies to which RMR LLC provides management services in a combined property insurance program through Affiliates Insurance Company, or AIC, and with respect to which AIC is an insurer or reinsurer of certain coverage amounts. We also participate with RMR LLC and other companies to which RMR LLC provides management services in a partial joint program for directors and officers' liability insurance as well as purchase such insurance for our own account. For more information, see Note 16 to our Consolidated Financial Statements included in Part IV, Item 15 of this Annual Report on Form 10 K.

We partially self insure up to certain limits for workers' compensation, professional and general liability, automobile and property coverage. Claims in excess of these limits are insured up to contractual limits, over which we are self insured. Our current insurance arrangements are generally renewable annually. We cannot be sure that our insurance charges and self insurance reserve requirements will not increase, and we cannot predict the amount of any such increase, or to what extent, if at all, we may be able to offset any such increase through higher deductibles, retention amounts, self insurance or other means in the future.

Table of Contents

COMPETITION

The senior living services business is highly competitive. We compete with numerous other senior living community operators, as well as companies that provide senior living services, such as home healthcare companies and other real estate based service providers. Some of our existing competitors are larger and have greater financial resources than us and some of our competitors are not for profit entities which have endowment income and may not face the same financial pressures that we do. Also, in recent years a significant number of new senior living communities have been developed, and we expect this increased development activity to continue in the future. This development activity has increased competitive pressures on us, particularly in the geographic markets where this development activity has been most focused, including Arizona, Georgia and Texas. We may enter into additional lease and management arrangements with SNH, and our relationships with SNH and RMR LLC may provide us with competitive advantages; however, SNH is not obligated to provide us with opportunities to lease or manage additional properties. We cannot be sure that we will be able to compete successfully or operate profitably. For more information on the competitive pressures we face and associated risks, see "Risk Factors" in Part I, Item 1A of this Annual Report on Form 10-K.

ENVIRONMENTAL AND CLIMATE CHANGE MATTERS

Under various laws, owners as well as tenants and operators of real estate may be required to investigate and clean up or remove hazardous substances present at or migrating from properties they own, lease or operate and may be held liable for property damage or personal injuries that result from hazardous substances. These laws also expose us to the possibility that we may become liable to reimburse governments or third parties for damages and costs they incur in connection with hazardous substances. Under our leases with SNH, we have also agreed to indemnify SNH for any such liabilities related to our leased senior living communities and the properties on which they are located. We have reviewed environmental conditions surveys of certain of our owned and leased properties. Based upon those surveys, we do not believe that there are environmental conditions at any of our owned or leased senior living communities that have had or will have a material adverse effect on us. However, we cannot be sure that environmental conditions are not present at our owned or leased senior living communities, or that potential costs we may incur in the future related to any such conditions will not have a material adverse effect on our business or financial condition and results of operations.

INTERNET WEBSITE

Our internet website address is www.fivestarseniorliving.com. Copies of our governance guidelines, our code of business conduct and ethics, or Code of Conduct, and the charters of our audit, quality of care, compensation and nominating and governance committees are posted on our website and may be obtained free of charge by writing to our Secretary, Five Star Senior Living Inc., 400 Centre Street, Newton, Massachusetts, 02458 or at our website. We also have a policy outlining procedures for handling concerns or complaints about accounting, internal accounting controls or auditing matters and a governance hotline accessible on our website that stockholders can use to report concerns or complaints about accounting, internal accounting controls or auditing matters or violations or possible violations of our Code of Conduct. We make available, free of charge, on our website, our Annual Reports on Form 10 K, our Quarterly Reports on Form 10 Q, our Current Reports on Form 8 K and amendments to these reports filed or furnished pursuant to Section 13(a) or 15(d) of the Securities Exchange Act of 1934, as amended, or the Exchange Act, as soon as reasonably practicable after these forms are filed with, or furnished to, the Securities and Exchange Commission, or SEC. Our Board of Directors provides a process for security holders to send communications to our Board of Directors or individual Directors. Information about the process for sending communications to our Board of Directors or individual Directors can be found on our website. Our website address and website addresses of one or more unrelated third parties are included several times in this Annual Report on Form 10-K as textual references only and the information in any such website is not incorporated by reference into this Annual Report on Form 10 K.

Item 1A. Risk Factors

Our business is subject to a number of risks and uncertainties. The risks described below may not be the only risks we face but are risks we believe material at this time. Additional risks that we do not yet know of, or that we currently think are immaterial, may also impair our business operations or financial results. If any of the events or circumstances described below occurs, our business, financial condition or results of operations and the market price of our securities could decline. Investors and prospective investors should consider the following risks and the information contained under the heading “Warning Concerning Forward Looking Statements” before deciding whether to invest in our securities.

Table of Contents

RISKS RELATED TO OUR BUSINESS

A small percentage decline in our revenues or increase in our expenses could have a material adverse impact on our operating results.

We have high operating leverage. As a result, a small percentage decline in our revenues or increase in our expenses could have a material adverse impact on our operating results because some of our fixed costs, such as our base rent, would not decrease during times of lower revenues and could not be reduced to offset other expenses which may be increasing.

Circumstances that adversely affect the ability of seniors or their families to pay for our services could cause our occupancy rates, revenues and results of operations to decline.

As further discussed below, government benefits, such as Medicare and Medicaid, are not generally available for services at independent and assisted living communities. Many seniors are not otherwise able to pay our monthly resident fees with private resources. Our residents paid approximately 78% of our senior living revenues from continuing operations during the year ended December 31, 2016 from their private resources, and we expect to continue to rely on the ability of our residents to pay for our services from their own financial resources. Economic downturns, softness in the U.S. housing market, higher levels of unemployment among resident family members, lower levels of consumer confidence, stock market volatility and/or changes in demographics could adversely affect the ability of seniors to afford our resident fees or entrance fees. If we are unable to retain and/or attract seniors with sufficient income, assets or other resources required to pay the fees associated with independent and assisted living services and other service offerings, our occupancy rates, revenues and results of operations could decline.

U.S. housing market conditions and the current trend for seniors to delay moving to senior living communities until they require greater care could have a material adverse effect on our business, financial condition and results of operations.

Downturns or stagnation in the U.S. housing market could adversely affect the ability, or perceived ability, of seniors to afford our entrance fees and resident fees as prospective residents frequently use the proceeds from the sale of their homes to cover the cost of such fees. If seniors have a difficult time selling their homes, their ability to relocate to our senior living communities or finance their stays at our senior living communities with private resources could be adversely affected. Also, seniors have been increasingly delaying their moves to senior living communities, including to our senior living communities, until they require greater care. Further, rehabilitation therapy and other services are increasingly being provided to seniors on an outpatient basis or in seniors' personal residences in response to market demand and government regulation, which may increase the trend for seniors to delay moving to senior living communities. Such delays may cause decreases in our occupancy rates and increases in our resident turnover rates.

Moreover, older aged persons may have greater care needs and require higher acuity services, which may increase our cost of business, expose us to additional liability or result in lost business and shorter stays at our senior living communities if we are not able to provide the requisite care services or fail to adequately provide those services. If such volatile U.S. housing market conditions and senior living moving trends continue for a protracted period, our occupancy rates, revenues, cash flows and results of operations could be negatively impacted.

The failure of Medicare and Medicaid rates to match our costs will reduce our income or create losses.

Some of our current operations, especially our SNFs, receive significant revenues from Medicare and Medicaid. We derived approximately 22% of our senior living revenues from continuing operations from these programs, for each of the years ended December 31, 2016 and 2015. Payments under Medicare and Medicaid are set by government policy, laws and regulations. The rates and amounts of these payments are subject to periodic adjustment. Current and projected federal budget deficits, federal spending priorities and challenging state fiscal conditions have resulted in numerous recent legislative and regulatory actions or proposed actions with respect to Medicare and Medicaid payments, insurance and healthcare delivery. Examples of these, and other information regarding such matters and developments, are provided under the caption "Business—Government Regulation and Reimbursement" in Part I, Item 1 of this Annual Report on Form 10-K. We cannot estimate the type and magnitude of these matters. However, these matters could result in the failure of Medicare or Medicaid payment rates to cover our costs of providing required services to residents, or in reductions in payments to us or other circumstances that could have a material adverse effect on our business, results of operations and financial condition.

Private third party payers continue to try to reduce healthcare costs.

Private third party payers such as insurance companies continue their efforts to control healthcare costs through direct contracts with healthcare providers, increased utilization review practices and greater enrollment in managed care programs and

15

Table of Contents

preferred provider organizations. These third party payers increasingly demand discounted fee structures and the assumption by healthcare providers of all or a portion of the financial risk. These efforts of third party payers to limit the amount of payments we receive for healthcare services could adversely affect us. Reimbursement payments under third party payer programs may not remain at levels comparable to present levels or be sufficient to cover the costs allocable to patients participating in such programs. Future changes in, or renegotiations of, the reimbursement rates or methods of third party payers, or the implementation of other measures to reduce payments for our services could result in a substantial reduction in our net operating revenues. At the same time, as a result of competitive pressures, our ability to maintain operating margins through price increases to private pay residents may be limited.

Provisions of the ACA and proposals to repeal and replace the ACA could reduce our income and increase our costs. The ACA contains insurance changes, payment changes and healthcare delivery systems changes that have affected, and will continue to affect, us unless such changes are repealed and replaced. The ACA provides for multiple reductions to the annual market basket updates for inflation that may result in reductions in SNF Medicare payment rates. In addition, certain provisions of the ACA that affect employers generally, including the employer shared responsibility provisions that went into effect on January 1, 2015, may have an impact on the design and cost of the health coverage that we offer to our employees. We are unable to predict the impact of the ACA on our future financial results of operations, but it may be adverse and material. In addition, maintaining compliance with the ACA will require us to expend management time and financial resources.

The ACA also established an Independent Payment Advisory Board to submit legislative proposals to Congress and take other actions with a goal of reducing Medicare spending growth. When and if such spending reductions take effect, they may be adverse and material to our financial results. The ACA includes other changes that may affect us, such as enforcement reforms and Medicare and Medicaid program integrity control initiatives, new compliance, ethics and public disclosure requirements, initiatives to encourage the development of home and community based long term care services rather than institutional services under Medicaid, value based purchasing plans and a Medicare post acute care pilot program to develop and evaluate making a bundled payment for services, including physician and SNF services, provided during an episode of care. We are unable to predict the impact on us of the insurance, payment, and healthcare delivery systems reforms contained in and to be developed pursuant to the ACA. If the changes implemented under the ACA result in reduced payments for our services or the failure of Medicare, Medicaid or insurance payment rates to cover our increasing costs, our future financial results could be adversely and materially affected.

In addition, to the extent the ACA is repealed or changed under the new Trump Administration and the 115th Congress, additional risks and regulatory uncertainty may arise. Depending upon what aspects of the ACA are repealed and whether and how they are replaced, our future financial results could be adversely and materially affected.

Increases in our labor costs may have a material adverse effect on us.

Wages and employee benefits associated with our continuing operations were approximately 42% of our 2016 total operating expenses. We compete with other senior living community operators, among others, to attract and retain qualified personnel responsible for the day to day operations of our senior living communities. The market for qualified nurses, therapists and other healthcare professionals is highly competitive, and periodic or geographic area shortages of such healthcare professionals may require us to increase the wages and benefits we offer to our employees in order to attract and retain such personnel or to utilize temporary personnel at an increased cost. In addition, employee benefit costs, including health insurance and workers' compensation insurance costs, have materially increased in recent years and, as noted above, we cannot predict the future impact of the ACA, or the repeal or replacement of the ACA, on the cost of employee health insurance. Although we determine our employee health insurance and workers' compensation self insurance reserves with guidance from third party professionals, our reserves may nonetheless be inadequate. Increasing employee health insurance and workers' compensation insurance costs and increasing self insurance reserves for labor related insurance may materially and adversely affect our earnings.

We cannot be sure that our labor costs will not increase or that any increases will be recovered by corresponding increases in the rates we charge to our residents or otherwise. Any significant failure by us to control labor costs or to pass any increases on to residents through rate increases could have a material adverse effect on our business,

financial condition and results of operations. Further, increased costs charged to our residents may reduce our occupancy and growth.

Table of Contents

Federal, state and local employment related laws and regulations could increase our cost of doing business, and our failure to comply with such laws and regulations could have a material adverse effect on our business, financial condition and results of operations.

Our operations are subject to a variety of federal, state and local employment related laws and regulations, including, but not limited to, the U.S. Fair Labor Standards Act, which governs such matters as minimum wages, the Family and Medical Leave Act, overtime pay, compensable time, recordkeeping and other working conditions, and a variety of similar laws that govern these and other employment related matters. Because labor represents a significant portion of our operating expenses, compliance with these evolving laws and regulations could substantially increase our cost of doing business, while failure to do so could subject us to significant back pay awards, fines and lawsuits. We are currently subject to employee-related claims in connection with our operations. These claims, lawsuits and proceedings are in various stages of adjudication or investigation and involve a wide variety of claims and potential outcomes. Our failure to comply with federal, state and local employment related laws and regulations could have a material adverse effect on our business, financial condition and results of operations.

Our business is subject to extensive regulation which increases our costs and may result in losses.

Licensing and Medicare and Medicaid laws require operators of senior living communities and rehabilitation and wellness clinics to comply with extensive standards governing operations and physical environments. Federal and state laws also prohibit fraud and abuse by senior living providers and rehabilitation and wellness clinic operators, including civil and criminal laws that prohibit false claims and regulate patient referrals in Medicare, Medicaid and other payer programs. In recent years, federal and state governments have devoted increased resources to monitoring the quality of care at senior living communities and to anti fraud investigations in healthcare generally. CMS contractors are expanding the retroactive audits of Medicare claims submitted by SNFs and other providers, and recouping alleged overpayments for services determined by auditors not to have been medically necessary or not to meet Medicare coverage criteria as billed. State Medicaid programs and other third party payers are conducting similar medical necessity and compliance audits. When federal or state agencies identify violations of anti fraud, false claims, anti kickback and physician referral laws, they may impose or seek civil or criminal penalties, treble damages and other government sanctions, and may revoke the community's license or make conditional or exclude the community from Medicare or Medicaid participation. The ACA amended the federal Anti Kickback Statute and the False Claims Act, making it easier for government agencies and private plaintiffs to prevail in lawsuits brought against healthcare providers, and for severe fines and penalties to be imposed on healthcare providers that violate applicable laws and regulations. In addition, when these agencies determine that there has been quality of care deficiencies or improper billing, they may impose or seek various remedies or sanctions, including denial of new admissions, exclusion from Medicare or Medicaid program participation, monetary penalties, restitution of overpayments, government oversight, temporary management, loss of licensure and criminal penalties. Current state laws and regulations allow enforcement officials to make determinations as to whether the care provided at our communities exceeds the level of care for which a particular community is licensed. A finding that a community is delivering care beyond the scope of its license could result in closure of the facility and the immediate discharge and transfer of residents. Certain states and the federal government may determine that citations relating to one community affect other communities operated by the same entity or related entities, which may negatively impact an operator's ability to maintain or renew other licenses or Medicare or Medicaid certifications or to secure new licenses or certifications. In addition, revocation of a license or certification at one community could impact our ability to obtain new licenses or certifications or to maintain or renew existing licenses and certifications at other communities, and trigger defaults under our leases, our management agreements with SNH and our new credit facility, or adversely affect our ability to operate or obtain financing in the future.

Our communities incur sanctions and penalties from time to time. As a result of the healthcare industry's extensive regulatory system and increasing enforcement initiatives, we have experienced increased costs for monitoring quality of care compliance, billing procedures and compliance with referral laws and other laws that apply to us, and we expect these costs may continue to increase. For example, as previously disclosed and disclosed elsewhere in this Annual Report on Form 10-K, as a result of our compliance program to review medical records related to our

Medicare billing practices, during 2014 we discovered potentially inadequate documentation and other issues at one of our leased SNFs. This compliance review was not initiated in response to any specific complaint or allegation, but was a review of the type that we periodically undertake to test our own compliance with applicable Medicare billing rules. As a result of these discoveries, in February 2015, we made a voluntary disclosure of deficiencies to the OIG pursuant to the OIG's Provider Self-Disclosure Protocol. We completed our investigation and assessment of these matters and submitted a final supplemental disclosure to the OIG in May 2015. In June 2016, we settled this matter with the OIG and agreed to pay approximately \$8.6 million in exchange for a customary release but did not admit any liability. The revenues we receive from Medicare and Medicaid may be subject to statutory and regulatory changes, retroactive rate adjustments, recovery of program overpayments or set offs, administrative rulings and policy interpretations, and payment

Table of Contents

delays. If we become subject to additional regulatory sanctions or repayment obligations at any of our existing communities (or at any of our newly acquired communities with prior deficiencies that we are unable to correct or resolve), our business may be adversely affected, and we might experience financial losses. Any adverse determination concerning any of our licenses or eligibility for Medicare or Medicaid reimbursement or any penalties, repayments, or sanctions, and the increasing costs of required compliance with applicable federal and state laws, may adversely affect our ability to meet our financial obligations and negatively affect our financial condition and results of operations.

The nature of our business exposes us to litigation and regulatory and government proceedings.

We have been, are currently, and expect in the future to be involved in claims, lawsuits and regulatory and government audits, investigations and proceedings arising in the ordinary course of our business, some of which may involve material amounts. For example, we were defendants in a lawsuit filed by the estate of a former resident of a senior living community operated by us in which a verdict was rendered against us awarding damages of approximately \$19.2 million, which consisted of \$2.5 million for pain and suffering and the remainder in punitive damages. In March 2016, pursuant to a settlement agreement we entered into with the plaintiff, approximately \$7.3 million was paid to the plaintiff, of which approximately \$3.0 million was paid by our liability insurer and the balance by us. We believe our liability insurer may be financially responsible for more than \$3.0 million and we are seeking additional payments from our liability insurer; however, we cannot predict the outcome of our ongoing negotiations or potential future litigation with our liability insurer. The defense and resolution of such claims, lawsuits and other proceedings may require us to incur significant expenses.

In several well publicized instances, private litigation by residents of senior living communities for alleged abuses has resulted in large damage awards against other senior living companies. Some lawyers and law firms specialize in bringing litigation against senior living community operators. As a result of this litigation and potential litigation, the cost of our liability insurance continues to increase. Medical liability insurance reform has at times been a topic of political debate, and some states have enacted legislation to limit future liability awards. However, such reforms have not generally been adopted, and we expect our insurance costs may continue to increase. Further, although we determine our self insurance reserves with guidance from third party professionals, our reserves may nonetheless be inadequate. Increasing liability insurance costs and increasing self insurance reserves could have a material adverse effect on our business, financial condition and results of operations.

If we do not achieve and maintain high quality of care, payments through pay-for-performance and value-based purchasing programs may be reduced, and the overall attractiveness of our senior living communities to potential residents could decrease as more quality data becomes publicly available.

As noted above, CMS is moving towards pay-for-performance programs, such as value-based payment. In October 2016, CMS issued a final rule to implement the Quality Payment Program. These reforms were mandated under MACRA and replace the SGR methodology for updates to the MPFS to which our Medicare outpatient therapy rates are tied. Starting in 2019, providers may be subject to either MIPS payment adjustments or APM incentive payments. Under PAMA, beginning in federal fiscal year 2019, Medicare payment rates will be partially based on SNFs' performance scores on a hospital readmissions measure as part of CMS's new SNF Value-Based Purchasing Program. Moreover, under the IMPACT Act, HHS will require SNFs to begin reporting certain quality measures and resource use measures in a standardized and interoperable format by October 1, 2016 and begin reporting certain patient assessment data in such a format by October 1, 2018. Under the SNF Quality Reporting Program, beginning in federal fiscal year 2018, SNFs that fail to comply with the reporting requirements by the established times will be subject to a 2.0% reduction in their Medicare payment rates for that fiscal year. Beginning October 1, 2018, HHS will make this data publicly available. We cannot predict the impact of these quality-driven payment reforms, but they may be material to and adversely affect our future results of operations. In addition, we cannot predict the impact of more quality data becoming publicly available, but if we do not achieve and maintain high quality of care, the overall attractiveness of our communities to potential residents could decrease.

Our growth strategy may not succeed.

We intend to continue to grow our business through acquisitions and by entering into additional long term lease and management arrangements for senior living communities where residents' private resources account for all or a large majority of revenues. Our business plan includes seeking to take advantage of expected long term increases in demand for senior living communities. Our growth strategy is subject to risks, including, but not limited to, the following:

- we may be unable to identify and make profitable acquisitions of additional senior living communities or to identify and lease or manage additional senior living communities on acceptable terms;

Table of Contents

we may be unable to access the capital required to fund acquisitions or to operate additional senior living communities;

we may be unable to identify and operate or manage additional senior living communities where residents' private resources account for all or a large majority of revenues;

we may not achieve the operating results we expect from newly acquired, leased or managed senior living communities;

the operations of newly acquired, leased or managed senior living communities may subject us to unanticipated contingent liabilities or regulatory matters;

we may be required to make significant capital expenditures to improve newly acquired, leased or managed senior living communities, including capital expenditures that were unanticipated at the time of acquisition or entry into the lease or management arrangements;

we may have difficulty retaining key employees and other personnel at newly acquired, leased or managed senior living communities;

to the extent we incur debt in connection with acquisitions or incur additional lease obligations associated with new leased senior living communities, our operating leverage and resulting risks of debt defaults may increase;

the occupancy at newly acquired, leased or managed senior living communities may decline and it may take a period of time to stabilize the operations of newly acquired, leased or managed senior living communities;

integrating the operations of newly acquired, leased or managed senior living communities may disrupt our existing operations, or may cost more than anticipated;

- we may acquire or agree to lease or manage senior living communities subject to unknown liabilities and without any recourse, or with limited recourse, such as liability for the cleanup of undisclosed environmental contamination or for claims by residents, vendors or other persons related to actions taken by former owners or operators of the communities;

any failure to comply with licensing requirements at our senior living communities may prevent our obtaining licenses for, or renewing licenses at, senior living communities we want to acquire, lease or manage; and

newly acquired, leased or managed senior living communities might require significant management attention that would otherwise be devoted to our ongoing business.

For these reasons, among others, we might not realize the anticipated benefits of our acquisitions or additional long term lease and management arrangements, and our growth strategy may not succeed and may cause us to experience losses.

We have not been consistently profitable, and we have limited resources and substantial lease obligations.

We have not been consistently profitable since we became a public company in 2001, and we currently have limited resources and substantial lease obligations. Given our history of losses, we cannot be sure that we will be able to achieve and/or maintain profitability in the future. If we are unable to effectively manage our operations and cash flow, or achieve profitability in other ways, the market price of our common shares may be adversely affected.

Current government policies regarding interest rates and trade policies may cause a recession.

The U.S. Federal Reserve policy regarding the timing and amount of future increases in interest rates, changing U.S. and other countries' trade policies and declining foreign economic conditions and markets may hinder the growth of the U.S. economy. It is unclear whether the U.S. economy will be able to withstand these market challenges and global uncertainty and achieve meaningful and sustained growth. Economic weakness in the U.S. economy generally or a new U.S. recession would likely adversely affect our financial condition, including by limiting our ability to pay rent and causing the value of our owned and operated senior living communities to decline. Further, general economic conditions, such as inflation, commodity costs, fuel and other energy costs, costs of labor, insurance and healthcare, interest rates, and tax rates, affect our operating and general and administrative expenses, and we have no control or limited ability to control such factors. Such economic

Table of Contents

uncertainties and conditions may adversely affect us and others, including our landlords and our residents and prospective residents, such as by reducing access to funding or credit, increasing the cost of credit, limiting the ability to manage interest rate risk and increasing the risk that obligations will not be fulfilled, as well as other impacts which we are unable to fully anticipate.

We may be unable to use our federal net operating loss or tax credit carry forwards before they expire, or our ability to use our federal net operating loss or tax credit carry forwards may be limited.

As of December 31, 2016, after reduction for the amounts utilized to offset federal taxable income in the twelve months ended December 31, 2016, our federal net operating loss carry forwards, which are scheduled to begin expiring in 2026 if unused, were approximately \$71.2 million, and our tax credit carry forwards, which begin expiring in 2022 if unused, were approximately \$21.6 million. If in the future we use our federal net operating loss or tax credit carry forwards to reduce our tax liabilities, the existence and amounts of these federal net operating loss or tax credit carry forwards may be subject to audit by the relevant tax authorities and the amounts of these federal net operating loss or tax credit carry forwards may be reduced.

Under Sections 382 and 383 of the Internal Revenue Code, or the IRC, our ability to use our federal net operating loss and tax credit carry forwards is limited if we undergo a change in ownership of more than 50% of our capital stock over a three year period. These change in ownership rules generally focus on ownership changes involving “5-percent shareholders” (as defined in the applicable treasury regulations promulgated under the IRC), including those arising from new stock issuances and other equity transactions. Our bylaws contain certain provisions to facilitate the preservation of the tax treatment of our net operating losses and tax credit carry forwards, including provisions generally prohibiting a person or group from becoming a “5-percent shareholder” without the consent of our Board of Directors. In November 2016, with the consent of our Board of Directors, ABP Acquisition LLC and certain related parties acquired 17,999,999 of our common shares, or approximately 36% of our common shares. Although this acquisition did not limit our ability to use our federal net operating loss or tax credit carry forwards, it limits the extent to which potential future acquisitions of our common shares by “5-percent shareholders” may be made without limiting our ability to use our federal net operating loss and tax credit carry forwards.

The credit agreement governing our new credit facility contains terms limiting our ability to incur additional debt. These terms, or our failure or inability to meet them, could adversely affect our business.

The agreement governing our new credit facility, or our credit agreement, includes various conditions to our borrowing, financial and other covenants, including covenants requiring us to maintain certain minimum debt service coverage and leverage ratios, and events of default. We may not be able to satisfy all of these conditions or may default on some of these covenants for various reasons, including for reasons beyond our control. Complying with these covenants may limit our ability to take actions that may be beneficial to us and our stockholders. Further, if we are unable to borrow under our new credit facility, we may be unable to meet our obligations or grow our business by acquiring senior living communities.

If we default under our credit agreement, our lenders may demand immediate payment of any amount outstanding and may elect not to fund future borrowings. Any such default would likely have serious and adverse consequences to us and would likely cause the market price of our common shares to decline.

We may obtain additional debt financing in the future. The covenants and conditions which apply to any such future indebtedness may be more restrictive than the covenants and conditions contained in our credit agreement.

Successful union organization of our employees may adversely affect our business, financial condition and results of operations.

From time to time labor unions attempt to organize our employees. If federal legislation modifies the labor laws to make it easier for employee groups to unionize, additional groups of employees may seek union representation. If our employees were to unionize, it could result in business interruptions, work stoppages, the degradation of service levels due to work rules, or increased operating expenses that may adversely affect our results of operations.

Our business could be adversely impacted if there are deficiencies in our disclosure controls and procedures or our internal control over financial reporting.

The design and effectiveness of our disclosure controls and procedures and our internal control over financial reporting may not prevent all errors, misstatements or misrepresentations. While our management will continue to

review the effectiveness of our disclosure controls and procedures and our internal control over financial reporting, there can be no guarantee that our disclosure controls and procedures and internal control over financial reporting will be effective in

20

Table of Contents

accomplishing all control objectives all of the time. Deficiencies, including any material weaknesses, in our disclosure controls and procedures or internal control over financial reporting could result in misstatements of our results of operations or our financial statements or could otherwise materially and adversely affect our business, reputation, results of operations, financial condition or liquidity.

Failure to comply with laws governing the privacy and security of personal information, including relating to health, could materially and adversely affect our business, financial condition and results of operations.

We are required to comply with federal and state laws governing the privacy, security, use and disclosure of personally identifiable information, including information relating to health. Under HIPAA and the HITECH Act, as updated by the HIPAA Omnibus Rule, we are required to comply with the HIPAA privacy rule, security standards and standards for electronic healthcare transactions. State laws also govern the privacy of individual health information, and rules regarding state privacy rights may be more stringent than HIPAA. Other federal and state laws govern the privacy of other personal information. If we fail to comply with applicable federal or state standards, we could be subject to civil sanctions and criminal penalties, which could materially and adversely affect our business, financial condition and results of operations. HIPAA enforcement efforts have increased considerably over the past few years, with HHS, through its Office for Civil Rights, entering into several multi-million dollar HIPAA settlements in 2016 alone.

We rely on information technology networks and related systems, and any material failure, inadequacy, interruption or security failure of those networks and systems could materially and adversely affect us.

Our information technology networks and related systems are essential to our ability to perform our day to day operations. As a result, we face risks associated with security breaches, whether through cyber attacks or cyber intrusions over the Internet, malware, computer viruses, attachments to emails, persons who access our systems from inside or outside our organization and other significant disruptions of our information technology networks and related systems. A security breach or other significant disruption involving our information technology networks and related systems could disrupt our operations; result in the unauthorized access to, and the destruction, loss, theft, misappropriation or release of, proprietary, personally identifiable, protected health, confidential, sensitive or otherwise valuable information, which others could use to compete against us or which could expose us to damage claims by third parties for disruptive, destructive or otherwise harmful purposes and outcomes; require significant management attention and resources to remedy any damages that result; subject us to claims for breach of contract, damages, credits, penalties or termination of leases or other agreements; or damage our business relationships or reputation generally. Any or all of the foregoing could materially and adversely affect us.

Although we take various actions to maintain the security and integrity of our information technology networks and related systems, and have implemented various measures to manage the risk of a security breach or disruption, we cannot be sure that our security efforts and measures will be effective or that any attempted security breaches or disruptions would not be successful or damaging. Even the most well protected information, networks, systems and facilities remain potentially vulnerable because the techniques used in such attempted security breaches evolve and generally are not recognized until launched against a target, and in some cases are designed to not be detected and, in fact, may not be detected. Accordingly, we may be unable to anticipate these techniques or to implement adequate security barriers or other preventative measures. It is therefore not possible for this risk to be entirely mitigated. Our business requires us to make significant capital expenditures to maintain and improve our senior living communities.

Our senior living communities sometimes require significant expenditures to address required ongoing maintenance or to make them more attractive to residents. Physical characteristics of senior living communities are mandated by various government authorities; changes in these regulations may require us to make significant expenditures. In addition, we are often required to make significant capital expenditures when we acquire, lease or manage new senior living communities. Our available financial resources may be insufficient to fund these expenditures. SNH has historically provided most of the capital required to improve the senior living communities we lease from them or manage for their account. However, when SNH funds capital expenditures at our leased senior living communities our rent increases, and when SNH funds capital expenditures at our managed senior living communities the invested capital upon which SNH's returns are based increases. We may be unable to pay increased rent at our leased senior

living communities without experiencing losses and increases in SNH's invested capital at our managed communities may reduce or prevent our receipt of incentive fees or subject the applicable management agreements to termination by SNH if it is unable to realize its return on invested capital under such agreements.

Table of Contents

We face significant competition.

We compete with numerous other senior living community operators, as well as companies that provide senior living services, such as home healthcare companies and other real estate based service providers. Some of our existing competitors are larger and have greater financial resources than us and some of our competitors are not for profit entities which have endowment income and may not face the same financial pressures that we do. We cannot be sure that we will be able to attract a sufficient number of residents to our senior living communities at rates that will generate acceptable returns or that we will be able to attract employees and keep wages and other employee benefits, insurance costs and other operating expenses at levels which will allow us to compete successfully and operate profitably.

In recent years, a significant number of new senior living communities have been developed, and we expect this increased development activity to continue in the future. This development activity has increased competitive pressures on us, particularly in the geographic markets where this development activity has been most focused, including Arizona, Georgia and Texas. These competitive pressures may prevent us from maintaining or improving occupancy and rates at our senior living communities, which may adversely affect their profitability and therefore negatively impact our revenues, cash flows and results from operations.

Increased leverage may harm our financial condition and results of operations.

Our total consolidated long term debt as of December 31, 2016 was approximately \$58.5 million and represented approximately 26% of our total book capitalization as of that date. We also had approximately \$1.9 million of short term mortgage debt. In addition to our indebtedness, we have substantial lease and other obligations.

Our level of indebtedness and substantial lease and other obligations could impact our business in the following ways, among others:

• our ability to satisfy our debt obligations could be affected;

- the funds required to make interest and principal payments will not be available for operations, working capital, capital expenditures, expansion, acquisitions or general corporate or other purposes;

• our ability to obtain additional financing may be impaired

• our flexibility in planning for, or reacting to, changes in our business and industry may be limited; and

- we may be more vulnerable to downturns in our business and industry or the economy generally.

Increasing interest rates may adversely affect us.

Since the most recent U.S. economic recession, the U.S. Federal Reserve has taken actions that have resulted in low interest rates for a long period of time. In December 2016, the U.S. Federal Reserve raised its benchmark interest rate by a quarter of a percentage point, and market interest rates rose after the recent presidential election in anticipation of possible increased government spending and inflation. Market interest rates may continue to increase, and increases may materially and negatively affect us in several ways, including:

Increases in interest rates could adversely impact the housing market and reduce demand for our services and occupancy at our senior living communities, could increase our rent expense at our leased senior living communities due to the landlord setting rent based on a required return on its investment, and could reduce the likelihood that we will earn incentive fees at our managed senior living communities due to the owner requiring a minimum return on its investment prior to our being eligible to receive an incentive fee.

- Amounts outstanding under our new credit facility require interest to be paid at variable interest rates. When interest rates increase, our interest costs will increase, which could adversely affect our cash flow, our ability to pay principal and interest on our debt and our cost of refinancing our debt when it becomes due and our ability to fund our operations and working capital. Additionally, if we choose to hedge our interest rate risk, we

cannot be sure that the hedge will be effective or that any hedging counterparty will meet its obligations to us.

An increase in interest rates could decrease the amount buyers may be willing to pay for our senior living communities, thereby reducing the market value of our senior living communities and limiting our ability to sell

Table of Contents

senior living communities. Further, increased interest rates would increase our costs for, and may limit our ability to obtain, mortgage financing secured by our senior living communities. Further, increased interest rates may effectively increase the cost of senior living communities we acquire to the extent we utilize leverage for those acquisitions and may result in a reduction in our acquisitions to the extent we reduce the amount we offer to pay for senior living communities, due to the effect of increased interest rates, to a price that sellers may not accept.

Increased interest rates may increase our operating costs to the extent we utilize financing, such as borrowings under our new credit facility, to fund our operations.

Termination of assisted living resident agreements and resident attrition could adversely affect our revenues and earnings.

State regulations governing assisted living communities typically require a written resident agreement with each resident. Most of these regulations also require that each resident have the right to terminate these assisted living resident agreements for any reason on reasonable notice. Consistent with these regulations, most of our resident agreements allow residents to terminate their agreements on 30 days' notice. Thus, we may be unable to contract with assisted living residents to stay for longer periods of time, unlike typical apartment leasing arrangements that involve lease agreements with terms of up to a year or longer. If a large number of residents elected to terminate their resident agreements at or around the same time, our revenues and earnings could be materially and adversely affected. In addition, the advanced ages of our senior living residents make resident turnover rates difficult to predict.

Our operations are subject to environmental and climate change risks.

Our operations are subject to risks associated with environmental hazards. We may be liable for environmental hazards at, or migrating from, the properties on which our owned, leased and managed senior living communities are located, including those created by prior owners or occupants, abutters or other persons. Various federal and state laws impose liabilities upon property owners and operators, including us, for environmental damages arising at, or migrating from, owned or operated properties, and we cannot be sure that we will not be held liable for the costs of environmental investigation and clean up at, or near, our owned or operated properties. As an owner or operator or previous owner or operator of properties, we also may be liable to pay damages to government agencies or third parties for costs and damages they incur arising from environmental hazards at, or migrating from, our owned or operated properties. In addition, under our leases with SNH, we have agreed to indemnify SNH for any such liabilities related to the properties on which our senior living communities that we lease from SNH are located. The costs and damages that may arise from environmental hazards are often difficult to project and may be substantial.

We believe some of our senior living communities may contain asbestos. We believe any asbestos at our senior living communities is contained in accordance with applicable laws and regulations, and we have no current plans to remove it. If we removed the asbestos or demolished the affected senior living communities, certain environmental regulations govern the manner in which the asbestos must be handled and removed, and we could incur substantial costs complying with such regulations.

Some observers believe severe weather activities in different parts of the country over the last few years are evidence of global climate change. Such severe weather may have an adverse effect on the senior living communities we operate. Further, the political debate about climate change has resulted in various treaties, laws and regulations that are intended to limit carbon emissions. These or future laws may cause costs at our senior living communities to increase. In the long term, we believe any such increased costs will be passed through and paid by our residents and other customers in higher charges for our services. Laws enacted to mitigate climate change may make some of our buildings obsolete or require us to make material investments in our senior living communities which could materially and adversely affect our financial condition and results of operations. For more information regarding climate change matters and their possible adverse impact on us, see "Management's Discussion and Analysis of Financial Condition and Results of Operations—Impact of Climate Change" in Part II, Item 7 of this Annual Report on Form 10-K.

Our former rehabilitation hospitals may be subject to retroactive Medicare reclassifications or repayments.

During the period we operated our rehabilitation hospitals, which were sold in the fourth quarter of 2013, Medicare payments accounted for a significant amount of the rehabilitation hospitals' revenues. CMS has established a standard

known as the “60% Rule”, which provides that at least 60% of an inpatient rehabilitation facility’s, or IRF’s, total inpatient population must require intensive rehabilitation services associated with treatment of at least one of thirteen designated medical conditions in order for the facility to be classified as an IRF by the Medicare program. Although we believe that our IRFs were operated in

23

Table of Contents

compliance with the 60% Rule during the period in which we operated them, CMS could determine that we were non-compliant in a prior year. Such an event would result in these rehabilitation hospitals being subject to Medicare reclassification to a different type of provider and our receiving lower Medicare payment rates retroactively. Also, retroactive audits of Medicare claims submitted by IRFs and other providers are expanding, and CMS is recouping amounts paid for services determined by auditors not to have been medically necessary or not to meet Medicare criteria for coverage as billed. If our IRFs were required to make substantial retroactive repayments to Medicare, our financial condition and results of operations could be adversely affected.

Changes in lease accounting standards may materially and adversely affect us.

The Financial Accounting Standards Board, or FASB, adopted new accounting rules to be effective for reporting periods beginning after December 15, 2018 which generally will require companies to capitalize long term leases on their balance sheets by recognizing lessees' rights and obligations. When the rules are effective, we will be required to account for the leases for our senior living communities, including those with SNH, in the assets and liabilities on our balance sheet, where previously we accounted for such leases on an "off balance sheet" basis. As a result, a significant amount of lease related assets and liabilities will be recorded on our balance sheet and we may be required to make other changes to the recording and classification of our lease related expenses. Though these changes will not have any direct impact on our overall financial condition, these changes could cause investors or others to believe that we are highly leveraged and could change the calculations of financial metrics and covenants, as well as third party financial models regarding our financial condition.

RISKS ARISING FROM CERTAIN OF OUR RELATIONSHIPS AND OUR ORGANIZATION AND STRUCTURE

Our agreements and relationships with SNH, one of our Managing Directors, RMR LLC and others related to them may create conflicts of interest or the appearance of such conflicts.

We have significant commercial and other relationships with SNH, one of our Managing Directors, Barry Portnoy, RMR LLC and others related to them, including:

• SNH owns 8.5% of our outstanding common shares as of December 31, 2016;

• The substantial majority of the senior living communities that we operate are owned by SNH;

• One of our Managing Directors, Barry Portnoy, and his son, Adam Portnoy, are managing trustees of SNH and they own, directly or indirectly, in aggregate 1.3% of SNH's outstanding common shares as of December 31, 2016;

RMR LLC provides management services to us and SNH and we pay RMR fees for those services based on a percentage of revenues, as defined under our business management agreement with RMR LLC. In the event of a conflict between us and SNH or us and RMR LLC, any of its affiliates or any public entity RMR LLC provides management services to, RMR LLC may act on its own and SNH's or such other entity's behalf rather than on our behalf;

Adam Portnoy and Barry Portnoy are the controlling shareholders, managing directors, officers and employees of The RMR Group Inc., or RMR Inc., and they are officers of, and own equity interests in, RMR LLC. RMR Inc. is the managing member of RMR LLC and RMR LLC is a subsidiary of RMR Inc.;

• Adam Portnoy and Barry Portnoy are our largest stockholders, and they own, directly or indirectly, in aggregate 36.7% of our outstanding common shares as of December 31, 2016;

Our President and Chief Executive Officer, Bruce J. Mackey Jr., our Chief Financial Officer and Treasurer, Richard A. Doyle, and our Senior Vice President and General Counsel, Katherine E. Potter, are also officers and employees of RMR LLC, as are SNH's president and chief operating officer and chief financial officer and treasurer;

•

Prior to December 31, 2001, we were a wholly owned subsidiary of SNH. On that date, SNH distributed substantially all of our then outstanding common shares it owned to its shareholders. In connection with that distribution, we entered into agreements with SNH and RMR LLC which, among other things, limit (subject to certain exceptions) ownership of more than 9.8% of our voting shares, restrict our ability to take any action that

Table of Contents

could jeopardize the tax status of SNH as a real estate investment trust and limit our ability to acquire real estate of types which are owned by SNH or other businesses managed by RMR LLC;

We lease our office headquarters building from a subsidiary of ABP Trust. ABP Trust is owned by Adam Portnoy and Barry Portnoy and they serve as its trustees and Adam Portnoy serves as its president;

- In order to accommodate healthcare licensing requirements, we manage a portion of a senior living community that SNH owns and which SNH leases to D&R Yonkers LLC. D&R Yonkers LLC is owned by SNH's president and chief operating officer and our Chief Financial Officer and Treasurer;

We, SNH, ABP Trust and four other companies to which RMR LLC provides management services currently own AIC, are parties to an amended and restated shareholders agreement regarding AIC and participate in AIC's property insurance program.

These relationships could create, or appear to create, conflicts of interest with respect to matters involving us, SNH, one of our Managing Directors, RMR LLC and others related to them. As a result of these relationships, our leases and management and pooling agreements with SNH, business management agreement with RMR LLC and other transactions with SNH, our Managing Director, RMR LLC and others related to them were not negotiated on an arm's length basis between unrelated third parties, and therefore the terms thereof may not be as favorable to us as they would have been if they were negotiated on an arm's length basis between unrelated third parties. In the past, in particular following periods of volatility in the overall market or declines in the market price of a company's securities, stockholder litigation, dissident stockholder director nominations and dissident stockholder proposals have often been instituted against companies alleging conflicts of interest in business dealings with affiliated and related persons and entities. These activities, if instituted against us, and the existence of conflicts of interest or the appearance of conflicts of interest, could result in substantial costs and diversion of our management's attention and could have a material adverse impact on our reputation, business and the market price of our common shares.

Adam Portnoy and Barry Portnoy own in aggregate 36.7% of our outstanding common shares. As a result, investors in our securities may have less influence over our business than shareholders of other publicly owned companies.

As of the date of this Annual Report on Form 10-K, Adam Portnoy and Barry Portnoy owned, directly or indirectly, in aggregate 36.7% of our outstanding common shares.

For so long as Adam Portnoy and Barry Portnoy and entities owned by them continue to retain a significant ownership stake in us, they may have significant influence in the election of the members of our Board of Directors, including our Independent Directors, and the outcome of stockholder actions. As a result, they may have the ability to significantly impact all matters affecting us, including:

the composition of our Board of Directors and, through our Board of Directors, determinations with respect to our management, business, investment, disposition and financing plans and policies, including the appointment and removal of our officers;

determinations with respect to mergers and other business combinations;

our acquisition or disposition of assets;

our financing activities;

our capital structure; and

the number of common shares available for issuance under our equity compensation plan.

In addition, the significant ownership of Adam Portnoy, Barry Portnoy, entities owned by them and SNH in us may discourage transactions involving a change of control of us, including transactions in which our stockholders might otherwise receive a premium for their common shares over the then current market price.

Table of Contents

As a result of the large ownership positions of Adam Portnoy, Barry Portnoy and SNH, trading in our common shares may be more difficult.

As of the date of this Annual Report on Form 10-K, Adam Portnoy and Barry Portnoy owned, directly or indirectly, in aggregate 36.7% of our outstanding common shares and SNH owned 8.5% of our outstanding common shares. These large shareholdings, some of which are subject to lock-up restrictions, reduce the number of our common shares that might otherwise be available to trade publicly, which could adversely affect the liquidity and market price of our common shares.

Our leases of certain of our senior living communities are subordinated to mortgage debt of SNH, and a default by SNH could result in the termination of those leases.

As of December 31, 2016, our leases with SNH for 17 of our senior living communities, which had aggregate 2016 revenues of \$159.4 million were subordinated to mortgage financing secured by such communities. As a result, in the event SNH was to default on such mortgage financing, by reason of our default under our leases or for reasons unrelated to us or beyond our control, and its lender were to foreclose on those properties, our leases would terminate. While we may be able to enter into new leases with the lenders or the purchaser or purchasers of such properties, or they may elect to continue our occupancy under the terms of the lease as if there had been no foreclosure, they would not be obligated to pursue either of those options and, if we are able to retain possession, the terms of our continued occupancy may not be as favorable to us as those contained in our leases with SNH. If we do not enter into new leases of such communities following a foreclosure, we would lose the right to continue to operate these communities and we may incur material obligations to residents, employees and other parties as a result of such loss.

Ownership limitations and certain provisions in our charter, bylaws and certain material agreements, as well as certain provisions of Maryland law, may deter, delay or prevent a change in our control or unsolicited acquisition proposals.

Our charter and bylaws contain separate provisions which prohibit any stockholder from owning more than 9.8% and 5% of the number or value of any class or series of our outstanding shares of stock. The 9.8% ownership limitation in our charter is consistent with our contractual obligation with SNH to not take actions that may conflict with SNH's status as a real estate investment trust under the IRC. The 5% ownership limitation in our bylaws, or our NOL bylaw, is intended to help us preserve the tax treatment of our NOLs and other tax benefits. We also believe these provisions promote good orderly governance. These provisions inhibit acquisitions of a significant stake in us and may deter, delay or prevent a change in control of us or unsolicited acquisition proposals that a stockholder may consider favorable.

On October 2, 2016, our Board of Directors granted a conditional exception from certain ownership limitations under our organizational documents, SNH granted certain consents and waivers under its leases, management or other agreements with us and our lenders granted certain consents and waivers under the agreement governing our prior credit facility that would allow Adam Portnoy, Barry Portnoy and certain of their related persons to acquire, subject to the satisfaction of specified conditions, in aggregate up to 38% of our issued and outstanding common shares, subject to certain limitations. On November 10, 2016, ABP Acquisition LLC, a company owned indirectly by Adam Portnoy and Barry Portnoy, completed the acquisition of 17,999,999 of our common shares at a purchase price of \$3.00 per share pursuant to a tender offer. The acquisition of 18,000,000 common shares was the maximum acquisition that our Board of Directors was prepared to approve for purposes of our NOL bylaw. Based on our Board of Directors' desire to continue to preserve the tax treatment of our NOLs and other tax benefits, ABP Acquisition LLC's acquisition of 17,999,999 common shares will reduce the size of any future acquisition that our Board of Directors may be prepared to approve for purposes of our NOL bylaw.

Other provisions contained in our charter and bylaws or under Maryland law may also inhibit acquisitions of a significant stake in us and deter, delay or prevent a change in control of us or unsolicited acquisition proposals that a stockholder may consider favorable, including, for example, provisions relating to:

- the division of our Directors into three classes, with the term of one class expiring each year, which could delay a change of control;

- stockholder voting rights and standards for the election of Directors and other provisions which require larger majorities for approval of actions which are not approved by our Directors than for actions which are approved by our

Directors;

the authority of our Board of Directors, and not our stockholders, to adopt, amend or repeal our bylaws and to fill vacancies on our Board of Directors;

26

Table of Contents

required qualifications for an individual to serve as a Director and a requirement that certain of our Directors be “Independent Directors” and other Directors be “Managing Directors”, as defined in our bylaws;

limitations on the ability of our stockholders to propose nominees for election as Directors and propose other business to be considered at a meeting of stockholders;

limitations on the ability of our stockholders to remove our Directors; and

the authority of our Board of Directors to create and issue new classes or series of stock (including stock with voting rights and other rights and privileges that may deter a change in control) and issue additional common shares.

In addition, our shareholders agreement with respect to AIC provides that AIC and the other shareholders of AIC may have rights to acquire our interests in AIC in the event that anyone acquires more than 9.8% of our shares or we experience some other change in control. The terms of our leases and management agreements with SNH provide that our rights under these agreements may be cancelled by SNH upon the acquisition by any person or group of more than 9.8% of our voting stock, and upon other change in control events, as defined in those documents including, in certain of the leases and management agreements, the adoption of any proposal (other than a precatory proposal) or the election to our Board of Directors of any individual if such proposal or individual was not approved, nominated or appointed, as the case may be, by vote of a majority of our Directors in office immediately prior to the making of such proposal or the nomination or appointment of such individual. In addition, a change in control event of us, including upon the acquisition by any person or group of more than 35% of our voting stock, is a default under our credit agreement, unless approved by our lenders.

Our ownership interest in AIC may prevent stockholders from accumulating a large stake in us, from nominating or serving as Directors, or from taking actions to otherwise control our business.

As an owner of AIC, we are licensed and approved as an insurance holding company; and any stockholder who owns or controls 10% or more of our securities or anyone who wishes to solicit proxies for election of, or to serve as, one of our Directors or for another proposal of business not approved by our Board of Directors may be required to receive pre-clearance from the concerned insurance regulators. These pre-approval procedures may discourage or prevent investors from purchasing our securities, from nominating persons to serve as our Directors or from taking other actions.

Our rights and the rights of our stockholders to take action against our Directors and officers are limited.

Our charter limits the liability of our Directors and officers to us and our stockholders for money damages to the maximum extent permitted under Maryland law. Under current Maryland law, our Directors and officers will not have any liability to us and our stockholders for money damages other than liability resulting from:

actual receipt of an improper benefit or profit in money, property or services; or

active and deliberate dishonesty by such Director or officer that was established by a final judgment as being material to the cause of action adjudicated.

Our charter and contractual obligations authorize and may require us to indemnify our present and former Directors and officers for actions taken by them in those and other capacities to the maximum extent permitted by Maryland law. In addition, we may be obligated to pay or reimburse the expenses incurred by our present and former Directors and officers without requiring a preliminary determination of their ultimate entitlement to indemnification. As a result, we and our stockholders may have more limited rights against our present and former Directors and officers than might otherwise exist absent the provisions in our charter and contracts or that might exist with other companies, which could limit our stockholders recourse in the event of actions not in their best interest.

Disputes with SNH and RMR LLC and stockholder litigation against us or our Directors and officers may be referred to binding arbitration proceedings.

Our contracts with SNH and RMR LLC provide that any dispute arising under those contracts may be referred to binding arbitration proceedings. Similarly, our bylaws provide that certain actions by our stockholders against us or against our Directors and officers, other than disputes, or any portion thereof, regarding the meaning, interpretation or validity of any provision of our charter or bylaws, may be referred to binding arbitration proceedings. As a result, we and our stockholders would not be able to pursue litigation in courts against SNH, RMR LLC or our Directors and officers for disputes referred to

Table of Contents

arbitration in accordance with our bylaws. In addition, the ability to collect attorneys' fees or other damages may be limited in the arbitration proceedings, which may discourage attorneys from agreeing to represent parties wishing to commence such a proceeding.

Our bylaws designate the Circuit Court for Baltimore City, Maryland as the sole and exclusive forum for certain actions and proceedings that may be initiated by our stockholders, which could limit our stockholders' ability to obtain a favorable judicial forum for disputes with us or our Directors, officers, manager, agents or employees.

Our bylaws currently provide that, unless the dispute has been referred to binding arbitration, the Circuit Court for Baltimore City, Maryland will be the sole and exclusive forum for: (1) any derivative action or proceeding brought on our behalf; (2) any action asserting a claim for breach of a duty owed by any Director, officer, manager, agent or employee of ours to us or our stockholders; (3) any action asserting a claim against us or any Director, officer, manager, agent or employee of ours arising pursuant to Maryland law, our charter or bylaws brought by or on behalf of a stockholder; or (4) any action asserting a claim against us or any Director, officer, manager, agent or employee of ours that is governed by the internal affairs doctrine. Our bylaws currently also provide that the Circuit Court for Baltimore City, Maryland will be the sole and exclusive forum for any dispute, or portion thereof, regarding the meaning, interpretation or validity of any provision of our charter or bylaws. Any person or entity purchasing or otherwise acquiring or holding any interest in our common shares shall be deemed to have notice of and to have consented to these provisions of our bylaws, as they may be amended from time to time. These choice of forum provisions may limit a stockholder's ability to bring a claim in a judicial forum that the stockholder believes is favorable for disputes with us or our Directors, officers, manager, agents or employees, which may discourage lawsuits against us and our Directors, officers, manager or agents.

We may experience losses from our business dealings with AIC.

We, SNH, ABP Trust and four other companies to which RMR LLC provides management services each own 14.3% of AIC, and we have invested \$6.0 million in AIC. We and those other AIC shareholders participate in a combined property insurance program arranged and reinsured in part by AIC and we periodically consider the possibilities for expanding our relationship with AIC to other types of insurance. Our principal reason for investing in AIC and for purchasing insurance in these programs is to seek to improve our financial results by obtaining improved insurance coverage at lower costs than may be otherwise available to us or by participating in any profits which we may realize as an owner of AIC. While we believe we have in the past benefitted from these arrangements, these beneficial financial results may not occur in the future, and we may need to invest additional capital in order to continue to pursue these results. AIC's business involves the risks typical of an insurance business, including the risk that it may not operate profitably. Accordingly, financial benefits from our business dealings with AIC may not be achieved in the future, and we may experience losses from these dealings.

RISKS RELATED TO OUR SECURITIES

We do not intend to pay cash dividends on our common shares in the foreseeable future.

We have never declared or paid any cash dividends on our common shares, and we currently do not anticipate paying any cash dividends in the foreseeable future.

Changes in market conditions could adversely affect the market price of our common shares.

As with other publicly traded equity securities, the market price of our common shares depends on various market conditions and other factors that may change from time to time, including:

- the liquidity of the market for our common shares;

- changes in our operating results;

- changes in analysts' expectations;

- the extent of investor interest in our common shares;

- market interest rates;

national economic conditions; and

28

Table of Contents

general market conditions.

In addition, the stock market in recent years has experienced broad price and volume fluctuations that often have been unrelated to the operating performance of particular companies. These market fluctuations may also cause the market price of our common shares to decline. Stockholders may be unable to resell our common shares at or above the price at which they purchased our common shares.

Item 1B. Unresolved Staff Comments

None.

Item 2. Properties

OUR SENIOR LIVING COMMUNITIES

We classify a senior living community based on the predominant type of services offered at that community. As of December 31, 2016, we owned or leased and operated 215 senior living communities which we have categorized into two groups as follows:

| Type of community | No. of communities | Type of units | | | | Total living units | Average occupancy for the year ended Dec. 31, 2016 | Revenues for the year ended Dec. 31, 2016 | Percent of revenues from private resources |
|---|--------------------|---------------------|-----------------------|----------------------|--------------------|--------------------|--|---|--|
| | | Indep. living apts. | Assist. living suites | Skilled nursing beds | Total living units | | | | |
| Independent and assisted living communities | 185 | 7,057 | 11,468 | 1,916 | 20,441 | 84.7 % | \$ 918,828 | 88.2 % | |
| SNFs | 30 | 69 | — | 2,532 | 2,601 | 80.7 % | 174,876 | 25.5 % | |
| Totals: | 215 | 7,126 | 11,468 | 4,448 | 23,042 | 84.3 % | \$ 1,093,704 | 78.2 % | |

(in thousands)

Excluded from the preceding and following data are 68 independent and assisted living communities with 3,646 independent living apartments, 4,711 assisted living suites and 431 skilled nursing beds that we manage for the account of SNH.

Independent and Assisted Living Communities

As of December 31, 2016, we owned or leased and operated 185 independent and assisted living communities. We leased 155 of these communities from SNH and four of these communities from HCP, Inc., or HCP. We own the remaining 26 communities. These 185 communities have 20,441 living units and are located in 26 states. The following table provides additional information about these communities and their operations as of December 31, 2016:

Table of Contents

| Location | No. of communities | Type of units | | | | Total living units | Average occupancy for the year ended Dec. 31, 2016 | Revenues for the year ended Dec. 31, 2016 | Percent of revenues from private resources | |
|--------------------|--------------------|---------------------|-----------------------|----------------------|--------------------|--------------------|--|---|--|---|
| | | Indep. living apts. | Assist. living suites | Skilled nursing beds | Total living units | | | | (in thousands) | % |
| 1. Alabama | 8 | 67 | 373 | — | 440 | 86.1 | % | \$ 16,886 | 100.0 | % |
| 2. Arizona | 4 | 501 | 306 | 199 | 1,006 | 76.1 | % | 42,480 | 81.2 | % |
| 3. California | 9 | 494 | 424 | 59 | 977 | 88.6 | % | 49,102 | 91.7 | % |
| 4. Delaware | 6 | 337 | 307 | 356 | 1,000 | 76.6 | % | 62,418 | 70.6 | % |
| 5. Florida | 9 | 1,184 | 709 | 155 | 2,048 | 92.3 | % | 85,842 | 80.8 | % |
| 6. Georgia | 11 | 111 | 527 | 40 | 678 | 85.0 | % | 27,287 | 92.4 | % |
| 7. Illinois | 4 | 112 | 199 | — | 311 | 98.2 | % | 6,194 | 100.0 | % |
| 8. Indiana | 16 | 955 | 577 | 140 | 1,672 | 81.2 | % | 60,538 | 91.2 | % |
| 9. Kansas | 3 | 332 | 67 | 198 | 597 | 86.2 | % | 29,590 | 75.8 | % |
| 10. Kentucky | 9 | 487 | 281 | 166 | 934 | 87.9 | % | 45,181 | 85.2 | % |
| 11. Maryland | 10 | 238 | 708 | — | 946 | 84.6 | % | 54,731 | 100.0 | % |
| 12. Massachusetts | 1 | — | 123 | — | 123 | 78.2 | % | 7,894 | 100.0 | % |
| 13. Minnesota | 1 | — | 230 | — | 230 | 85.7 | % | 13,192 | 92.0 | % |
| 14. Mississippi | 2 | — | 116 | — | 116 | 81.7 | % | 3,530 | 100.0 | % |
| 15. Missouri | 1 | 110 | — | — | 110 | 80.0 | % | 2,594 | 100.0 | % |
| 16. Nebraska | 2 | 27 | 111 | 62 | 200 | 82.8 | % | 8,432 | 66.6 | % |
| 17. New Jersey | 5 | 215 | 544 | 60 | 819 | 85.6 | % | 40,923 | 84.0 | % |
| 18. New Mexico | 1 | 112 | 35 | 57 | 204 | 77.3 | % | 11,711 | 87.4 | % |
| 19. North Carolina | 15 | 143 | 1,296 | — | 1,439 | 82.7 | % | 67,728 | 99.7 | % |
| 20. Ohio | 1 | 143 | 115 | 24 | 282 | 76.8 | % | 15,996 | 86.7 | % |
| 21. Pennsylvania | 10 | — | 982 | — | 982 | 87.6 | % | 41,018 | 100.0 | % |
| 22. South Carolina | 18 | 101 | 886 | 58 | 1,045 | 85.8 | % | 45,367 | 92.0 | % |
| 23. Tennessee | 13 | 158 | 707 | — | 865 | 92.6 | % | 31,353 | 100.0 | % |
| 24. Texas | 9 | 846 | 613 | 273 | 1,732 | 77.8 | % | 80,588 | 82.5 | % |
| 25. Virginia | 11 | 285 | 714 | — | 999 | 88.5 | % | 39,573 | 99.9 | % |
| 26. Wisconsin | 6 | 99 | 518 | 69 | 686 | 86.7 | % | 28,680 | 72.5 | % |
| Totals: | 185 | 7,057 | 11,468 | 1,916 | 20,441 | 84.7 | % | \$ 918,828 | 88.2 | % |

Skilled Nursing Facilities

As of December 31, 2016, we operated 30 SNFs that we lease from SNH with a combined 2,601 living units located in seven states. The following table provides additional information about these SNFs and their operations as of December 31, 2016:

| Location | No. of communities | Type of units | | | | Total living units | Average occupancy for the year ended Dec. 31, 2016 | Revenues for the year ended Dec. 31, 2016 | Percent of revenues from private resources | |
|---------------|--------------------|---------------------|-----------------------|----------------------|--------------------|--------------------|--|---|--|---|
| | | Indep. living apts. | Assist. living suites | Skilled nursing beds | Total living units | | | | (in thousands) | % |
| 1. California | 4 | — | — | 375 | 375 | 79.0 | % | 30,519 | 10.4 | % |
| 2. Colorado | 7 | 46 | — | 718 | 764 | 82.2 | % | 56,163 | 29.7 | % |
| 3. Iowa | 4 | 19 | — | 283 | 302 | 82.9 | % | 17,320 | 30.4 | % |
| 4. Kansas | 1 | 4 | — | 56 | 60 | 79.2 | % | 3,275 | 24.1 | % |
| 5. Nebraska | 10 | — | — | 602 | 602 | 80.4 | % | 33,338 | 28.4 | % |

Edgar Filing: SEARS HOLDINGS CORP - Form DEF 14A

| | | | | | | | | | | |
|--------------|----|----|---|-------|-------|------|---|------------|------|---|
| 6. Wisconsin | 2 | — | — | 309 | 309 | 80.0 | % | 21,322 | 29.2 | % |
| 7. Wyoming | 2 | — | — | 189 | 189 | 77.0 | % | 12,939 | 23.4 | % |
| Totals: | 30 | 69 | — | 2,532 | 2,601 | 80.7 | % | \$ 174,876 | 25.5 | % |

30

Table of Contents

OUR SNH LEASES AND MANAGEMENT AGREEMENTS

Leases with SNH

The following table provides a summary of our leases as of December 31, 2016 and is followed by a summary of the material terms of our leases as of December 31, 2016 with SNH. Because it is a summary, it does not contain all of the information that may be important to you. If you would like more information, you should read the leases which are among the exhibits listed in Part IV, Item 15 of this Annual Report on Form 10 K and incorporated herein by reference.

| | Number of Properties | Annual Rent as of December 31, 2016 | Current Expiration Date | Remaining Renewal Options |
|---|----------------------------|---|----------------------------|------------------------------|
| 1. Lease No. 1 for SNFs and independent and assisted living communities | 83 | 59.2 million | December 31, 2024 | Two 15-year renewal options. |
| 2. Lease No. 2 for SNFs, independent and assisted living communities | 47 | 64.7 million | June 30, 2026 | Two 10-year renewal options. |
| 3. Lease No. 3 for independent and assisted living communities ⁽¹⁾ | 17 | 34.9 million | December 31, 2028 | Two 15-year renewal options. |
| 4. Lease No. 4 for SNFs and independent and assisted living communities | 29 | 35.1 million | April 30, 2032 | Two 15-year renewal options. |
| 5. Lease No. 5 for independent and assisted living communities ⁽⁴⁾ | 9 | 9.8 million | December 31, 2028 | Two 15-year renewal options. |
| Totals | 185 | 203.8 million | | |

(1) Lease No. 3 exists to accommodate certain mortgage financing by SNH.

(2) Lease No. 5 was entered into in connection with the June 2016 sale and leaseback transaction with SNH.

Percentage Rent. Our leases with SNH require us to pay percentage rent at 178 of the 185 senior living communities we lease from SNH equal to 4% of the amount by which gross revenues, as defined in our leases, of each property exceeds gross revenues for a specific base year. These amounts are in addition to the annual rent amounts payable by us to SNH. We incurred total percentage rent of \$5.6 million in 2016. Different base years apply to those communities that pay percentage rent. The base year is usually the first full calendar year after each community is initially leased.

Operating Costs. Each lease is a so called “triple net” lease which requires us to pay all costs incurred in the operation of the properties, including the costs of maintenance, personnel, services to residents, insurance and real estate and personal property taxes.

Rent During Renewal Term. For all but seven of the properties we lease from SNH, rent during each applicable renewal term is determined in the same manner as the annual rent and percentage rent payable during the initial term. For the remaining seven properties, rent during the second renewal term is based on the fair market rental value of such properties.

Licenses. Our leases require us to obtain, maintain and comply with all applicable permits and licenses necessary to operate the leased properties.

Maintenance and Alterations. We are required to operate continuously and maintain, at our expense, the leased properties in good order and repair, including structural and nonstructural components. We may request that SNH fund amounts needed for qualifying improvements to the leased communities in return for rent increases according to formulas in the leases; however, SNH is not obligated to fund such requests, and we are not required to sell them to SNH. At the end of each lease term, we are required to surrender the leased properties in substantially the same condition as existed on the commencement date of the lease, subject to any permitted alterations and ordinary wear and tear.

Assignment and Subletting. SNH’s consent is generally required for any direct or indirect assignment or sublease of any of the properties. Also, in the event of any assignment or subletting, we remain liable under the terms of the applicable lease.

Indemnification and Insurance. With limited exceptions, we are required to indemnify SNH from all liabilities which may arise from the ownership or operation of the leased properties. We generally are required to maintain insurance against such risks and in such amounts as SNH shall reasonably require and may be commercially reasonable. Each lease requires that SNH be named as an additional insured under these insurance policies.

Table of Contents

Damage, Destruction, Condemnation and Environmental Matters. In the event of any damage, or immaterial condemnation, of a leased property, we are generally required to rebuild with insurance or condemnation proceeds or, if such proceeds are insufficient, other amounts made available by SNH, if any, but if other amounts are made available by SNH, our rent will be increased accordingly. In the event of any material or total condemnation of a leased property, the lease shall terminate with respect to such leased property, in which event SNH shall be entitled to the condemnation proceeds and our rent will be reduced accordingly. In the event of any material or total destruction of a leased property, we may terminate the lease with respect to such leased property, in which event we are required to pay to SNH any shortfall in the amount of proceeds SNH receives from insurance compared to the replacement cost of such leased property and our rent will be reduced accordingly. We are also required to remove and dispose of any hazardous substance at the leased properties in compliance with all applicable environmental laws and regulations.

Events of Default. Events of default under each lease generally include the following:

- our failure to pay rent or any money due under the lease when it is due, which failure continues for five business days;
- our failure to maintain the insurance required under such lease;
- any person or group acquiring ownership of 9.8% or more of our outstanding voting stock or any change in our control, the adoption of any stockholder proposal (other than a precatory proposal) or the election to our Board of Directors of any individual if such proposal or individual was not approved, nominated or appointed, as the case may be, by vote of a majority of our Directors in office immediately prior to the making of such proposal or the nomination or appointment of such individual;
- the occurrence of certain events with respect to our insolvency or dissolution;
- our default under indebtedness which gives the holder the right to accelerate our repayment of the indebtedness;
- our being declared ineligible to receive reimbursement under Medicare or Medicaid programs for any of the leased properties which participate in such programs or the revocation of any material license required for our operations; and
- our failure to perform any terms, covenants or agreements of such lease and the continuance thereof for a specified period of time after written notice.

Remedies. Upon the occurrence of any event of default, each lease provides that, among other things, SNH may, to the extent legally permitted:

- accelerate the rent;
- terminate the lease in whole or in part;
- enter the property and take possession of any and all our personal property and retain or sell the same at a public or private sale;
- make any payment or perform any act required to be performed by us under the lease; and
- rent the property and recover from us any deficiency between the amount of rent which would have been due under the lease and the rent received from the re letting.

We are obligated to reimburse SNH for all costs and expenses incurred in connection with any exercise of the foregoing remedies.

Management. We may not enter into any new management agreement affecting any leased property without the prior written consent of SNH.

Lease Subordination. Our leases may be subordinated to any mortgages on properties leased from SNH. As of December 31, 2016, SNH had mortgages on 17 of our communities to which our leases were subordinated. These 17 communities had 3,230 living units and 2016 revenues totaling \$159.4 million. SNH's outstanding borrowing secured by mortgages on these 17 communities totaled \$279.5 million as of December 31, 2016.

Table of Contents

Financing Limitations; Security. Our leases subject to mortgage financings of SNH require SNH's consent before we incur debt secured by our investments in our tenant subsidiaries that lease or operate the properties subject to these leases. Further, our leases subject to mortgage financings prohibit our tenant subsidiaries from incurring liabilities, other than operating liabilities incurred in the ordinary course of business, secured by our accounts receivable or purchase money debt. We may pledge interests in our leases only if the pledge is approved by SNH. In addition, in connection with our leases subject to mortgage financings with SNH, certain of our subsidiaries pledged to the lenders under such mortgage financings certain tangible and intangible personal property, such as accounts receivable and contract rights, located at, or arising from the operations of, the properties subject to such leases to secure their obligations under such leases and certain of their obligations relating to such mortgage financings.

Non Economic Circumstances. If we determine that continued operations of one or more properties is not economical, we may negotiate with SNH to close or sell that community, including SNH's ownership in the property. In the event of such a sale, SNH receives the net proceeds and our rent for the remaining properties in the applicable lease is reduced according to formulas contained in the applicable lease.

Management Agreements with SNH

As of December 31, 2016, 2015 and 2014 we managed 68, 60 and 46 senior living communities for the account of SNH, respectively, pursuant to long term management agreements and pooling agreements that combine various calculations of revenues and expenses from the operations of the communities covered by the applicable pooling agreement. On June 29, 2016, we and SNH terminated three of our four then existing pooling agreements and entered into 10 new pooling agreements, or the new pooling agreements, that combine our management agreements with SNH for senior living communities that include assisted living units, or AL Management Agreements. Our management agreements with SNH for the part of the senior living community owned by SNH and located in Yonkers, New York that is not subject to the requirements of New York healthcare licensing laws, as described elsewhere herein, and for the assisted living community owned by SNH and located in Villa Valencia, California, are not currently included in any of our pooling agreements with SNH. Pursuant to our AL Management Agreements and the new pooling agreements, we receive from SNH:

• a management fee equal to either 3% or 5% of the gross revenues realized at the applicable communities,

• reimbursement for our direct costs and expenses related to such communities,

• an annual incentive fee equal to either 35% or 20% of the annual net operating income of such communities

• remaining after SNH realizes an annual minimum return equal to either 8% or 7% of its invested capital, or, in the case of 10 communities, a specified amount plus 7% of its invested capital since December 31, 2015, and

• a fee for our management of capital expenditure projects equal to 3% of amounts funded by SNH.

Under the new pooling agreements, the calculations of our fees and of SNH's annual minimum return related to our AL Management Agreement that became effective before May 2015 and had been pooled under one of the previously existing pooling agreements are generally the same as they were under the previously existing pooling agreements. However, for certain communities, the new pooling agreements reduced SNH's annual minimum return to 7%, and also, with respect to 10 communities, reset SNH's annual minimum return as of January 1, 2016 to specified amounts. For our AL Management Agreements that became effective from and after May 2015, the new pooling agreements increased our management fee from 3% to 5% of the gross revenues realized at the applicable community, and changed our annual incentive fee from 35% to 20% of the annual net operating income of the applicable community remaining after SNH realizes its requisite annual minimum return.

We also have a pooling agreement with SNH that combines our management agreements with SNH for senior living communities consisting only of independent living units.

Our management agreements with SNH generally expire between 2030 and 2040, and are subject to automatic renewal for two consecutive 15 year terms, unless earlier terminated or timely notice of nonrenewal is delivered.

These management agreements also provide that SNH has, and in some cases we have, the option to terminate the

agreements upon the acquisition by a person or group of more than 9.8% of the other's voting stock and upon certain change in control events affecting the other party, as defined in the applicable agreements, including the adoption of any stockholder proposal (other than a precatory proposal) with respect to the other party, or the election to the board of directors or trustees, as applicable, of the other party of any individual, if such proposal or individual was not approved, nominated or appointed, as the case may be,

33

Table of Contents

by a majority of the other party's board of directors or board of trustees, as applicable, in office immediately prior to the making of such proposal or the nomination or appointment of such individual.

For more information regarding our leases and management arrangements with SNH, see Note 9 to our Consolidated Financial Statements included in Part IV, Item 15 of this Annual Report on Form 10-K. For more information regarding our relationship with SNH, see Note 16 to our Consolidated Financial Statements included in Part IV, Item 15 of this Annual Report on Form 10-K.

Item 3. Legal Proceedings

From time to time we are engaged in litigation in the ordinary course of our business. We do not believe any of the litigation which is currently pending is likely to have a materially adverse impact on our ability to continue in business.

Item 4. Mine Safety Disclosures

Not applicable.

Table of Contents

PART II

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

Our common shares were traded on the New York Stock Exchange, or the NYSE (symbol: FVE), through June 30, 2016. Beginning on July 1, 2016, our common shares are traded on The NASDAQ Stock Market LLC, or Nasdaq (symbol: FVE). The following table sets forth for the periods indicated the high and low sale prices for our common shares as reported by the NYSE or Nasdaq, as applicable:

| | High | Low |
|----------------|--------|--------|
| 2015 | | |
| First Quarter | \$4.45 | \$3.37 |
| Second Quarter | 5.07 | 3.91 |
| Third Quarter | 4.96 | 2.74 |
| Fourth Quarter | 3.98 | 3.02 |
| 2016 | | |
| First Quarter | \$3.14 | \$2.00 |
| Second Quarter | 2.74 | 1.65 |
| Third Quarter | 2.63 | 1.83 |
| Fourth Quarter | 3.04 | 2.29 |

The closing price of our common shares on the Nasdaq on February 17, 2017 was \$2.50 per share.

As of February 17, 2017, there were approximately 2,200 stockholders of record of our common shares.

We have never paid or declared any cash dividends on our common shares. At present, we intend to retain our future earnings, if any, to fund our operations and the growth of our business. Furthermore, our credit agreement restricts our payment of cash dividends on our common shares, unless certain requirements are met. Our future decisions concerning the payment of dividends on our common shares will depend upon our results of operations, financial condition and capital expenditure and investment plans, as well as other factors as our Board of Directors, in its discretion, may consider relevant, and the extent to which the declaration or payment of dividends may be limited by agreements we have entered or cause us to lose the benefits of certain of our agreements.

The following table provides information about our purchases of our equity securities during the year ended December 31, 2016:

| Calendar Month | Number of Shares Purchased ⁽¹⁾ | Average Price Paid per Share | Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs | Maximum Approximate Dollar Value of Shares that May Yet Be Purchased Under the Plans or Programs |
|----------------|---|------------------------------|--|--|
| September 2016 | 751 | \$ 1.91 | — | \$ — |
| December 2016 | 34,248 | \$ 2.45 | — | \$ — |
| Total | 34,999 | — | — | \$ — |

In 2016, all common share purchases were made to satisfy tax withholding and payment obligations of current and former employees and officers of us and of RMR LLC in connection with the vesting of awards of our common shares. We repurchased these shares at their fair market value based upon the trading price of our common shares on the repurchase date.

Item 6. Selected Financial Data

The following table sets forth selected financial data for the periods and dates indicated. Our comparative results are impacted by community acquisitions and dispositions during the periods shown. This data should be read in conjunction with, and is qualified in its entirety by reference to “Management’s Discussion and Analysis of Financial Condition and Results of Operations” of this Annual Report on Form 10 K and our Consolidated Financial Statements and accompanying notes included in Part IV, Item 15 of this Annual Report on Form 10 K.

35

Table of Contents

| | Year ended December 31, | | | | |
|--|---------------------------------------|-------------|-------------|-------------|-------------|
| | 2016 | 2015 | 2014 | 2013 | 2012 |
| | (in thousands, except per share data) | | | | |
| Operating data: | | | | | |
| Total revenues | \$1,378,108 | \$1,365,410 | \$1,328,075 | \$1,296,787 | \$1,207,806 |
| Net (loss) income from continuing operations | (22,007) | (40,759) | (79,350) | 3,449 | 10,590 |
| Net income (loss) from discontinued operations | 194 | (2,324) | (6,056) | (5,789) | 11,717 |
| Net (loss) income | (21,813) | (43,083) | (85,406) | (2,340) | 22,307 |
| Basic net (loss) income per share: | | | | | |
| (Loss) income from continuing operations | (0.45) | (0.84) | (1.65) | 0.07 | 0.23 |
| Income (loss) from discontinued operations | — | (0.05) | (0.13) | (0.12) | 0.24 |
| Net (loss) income | (0.45) | (0.89) | (1.78) | (0.05) | 0.47 |
| Diluted net (loss) income per share: | | | | | |
| (Loss) income from continuing operations | (0.45) | (0.84) | (1.65) | 0.07 | 0.23 |
| Income (loss) from discontinued operations | — | (0.05) | (0.13) | (0.12) | 0.23 |
| Net (loss) income | (0.45) | (0.89) | (1.78) | (0.05) | 0.46 |
| Balance sheet data (as of December 31): | | | | | |
| Total assets | 509,734 | 531,770 | 534,973 | 590,183 | 594,991 |
| Total long term debt | 58,494 | 60,396 | 49,373 | 36,461 | 37,621 |
| Total other long term liabilities | 113,981 | 43,002 | 43,426 | 44,816 | 43,067 |

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

GENERAL INDUSTRY TRENDS

The primary market for senior living services is individuals age 75 and older, and, according to U.S. Census data, that group is projected to be the fastest growing age cohort in the United States over the next 20 years. Further, as a result of scientific and medical breakthroughs, seniors are living longer. Due to demographic trends, and continuing advances in science, nutrition and healthcare, the senior population is expected to continue to grow, and we expect the demand for senior living services to increase in future years.

Despite the general trend of growth described in the preceding paragraph, economic downturns, softness in the U.S. housing market, higher levels of unemployment among resident family members, lower levels of consumer confidence, stock market volatility and/or changes in demographics could adversely affect the ability of seniors to afford our resident fees or entrance fees. Prospective residents who plan to use the proceeds from the sale of their homes to cover the cost of such fees seem to be especially affected by cyclical factors affecting the U.S. housing market. During the past several years, weak economic conditions in many areas throughout the United States have negatively affected businesses in these areas. These conditions have resulted in, among other things, a decrease in occupancy at senior living communities, including ours, and it is unclear when these conditions may materially improve. Although many of the services that we provide to residents are needs driven, some prospective residents may be deferring decisions to relocate to senior living communities in light of economic circumstances, among other reasons.

In recent years, a significant number of new senior living communities have been developed, and we expect this increased development activity to continue in the future. This development activity has increased competitive pressures on us, particularly in the geographic markets where this development activity has been most focused, including Arizona, Georgia and Texas. These competitive pressures may prevent us from maintaining or improving occupancy and rates at our senior living communities, which may adversely affect their profitability and therefore negatively impact our revenues, cash flows and results from operations.

OPERATIONS

We primarily earn our senior living revenues by providing housing and services to our senior living communities' residents. During 2016, approximately 22% of our senior living revenues from continuing operations came from the Medicare and Medicaid programs and approximately 78% of our senior living revenues from continuing operations came from residents' private resources. We bill all private pay residents in advance for the housing and services to be provided in the following month.

Our material expenses are:

36

Table of Contents

• Wages and benefits—includes wages and wage related expenses, such as health insurance, workers' compensation insurance and other benefits for our employees working at our senior living communities.

• Other senior living operating expenses—includes utilities, housekeeping, dietary, maintenance, insurance and community level administrative costs at our senior living communities.

• Rent expense—as of December 31, 2016, we lease 185 senior living communities from SNH and four senior living communities from HCP.

• General and administrative expenses—principally wages and wage related expenses for headquarters and regional staff supporting our communities.

• Costs incurred on behalf of managed communities—includes wages and benefits for staff and other operating expenses related to the communities that we manage for the account of SNH, which are reimbursed to us by SNH, including from revenues we receive from the applicable managed communities, pursuant to our management agreements with SNH.

• Depreciation and amortization expense—we incur depreciation expense on buildings and furniture and equipment that we own and we incur amortization expense on certain identifiable intangible assets.

• Interest and other expenses—primarily includes interest on outstanding debt and amortization of deferred financing costs.

We have two operating segments: (i) senior living communities and (ii) rehabilitation and wellness. In the senior living communities segment, we operate for our own account or manage for the account of others independent living communities, assisted living communities and SNFs that are subject to centralized oversight and provide housing and services to elderly residents. In the rehabilitation and wellness operating segment, we provide services in the inpatient setting and in outpatient clinics. We have determined that our two operating segments meet the aggregation criteria as prescribed under the FASB Accounting Standards Codification™ Topic 280, Segment Reporting, and we have therefore determined that our business is comprised of one reportable segment, senior living. All of our operations and assets are located within the United States, except for the operations of our Cayman Islands organized captive insurance company subsidiary, which participates in our workers' compensation and professional and general liability insurance programs.

EXPANSION ACTIVITIES

In May 2014, we acquired a senior living community located in Alabama with 116 living units for \$19.9 million, including our assumption of \$13.9 million of mortgage debt and \$0.1 million of net working capital liabilities, but excluding closing costs.

In December 2014, we began managing for the account of SNH two senior living communities located in Wisconsin with a combined 228 living units.

In February 2015, SNH acquired a land parcel adjacent to a senior living community we lease from SNH located in Florida for \$0.5 million. We and SNH added this property to the lease for that senior living community, and our annual rent payable to SNH increased by \$39,200 as a result.

In May 2015, we began managing for the account of SNH 14 senior living communities located in four states with a combined 838 living units.

Also in May 2015, we began managing for the account of SNH a senior living community located in Georgia with 40 living units. This senior living community is adjacent to another community that we manage for the account of SNH and the operations of these two communities are now conducted as a single integrated community.

In November 2015, we acquired two independent living communities located in Tennessee with a combined 152 living units for an aggregate purchase price of \$26.2 million, including our assumption of \$17.3 million of mortgage debt, but excluding closing costs.

In April, May and July 2016, we began managing for the account of SNH three senior living communities located in North Carolina, Georgia and Alabama with a combined 301 living units.

37

Table of Contents

In September 2016, SNH acquired an additional living unit at a senior living community we lease from SNH located in Florida which was added to the lease for that senior living community, and our annual rent payable to SNH increased by \$10,000 as a result.

In December 2016, we began leasing from SNH two senior living communities located in Illinois with a combined 126 living units which were added to one of our leases with SNH, and our annual rent payable to SNH increased by \$1.4 million as a result.

Also in December 2016, we began managing for the account of SNH five senior living communities located in Georgia with a combined 395 living units.

Also in December 2016, SNH acquired a land parcel adjacent to a senior living community located in Georgia that we manage for the account of SNH which was added to the management agreement for the senior living community.

For more information regarding our leases and management arrangements with SNH, see Note 9 to our Consolidated Financial Statements included in Part IV, Item 15 of this Annual Report on Form 10-K.

INVESTMENT ACTIVITIES

During 2016, 2015 and 2014, we made capital expenditures for property, plant and equipment related to our continuing operations, on a net basis after considering the proceeds from sales to SNH of improvements we made to senior living communities we lease from SNH, of \$34.0 million, \$36.2 million and \$24.1 million, respectively.

During 2016, 2015 and 2014, we received gross proceeds of \$17.9 million, \$10.9 million and \$10.9 million, respectively, in connection with the sale of available for sale securities, and recorded net realized gains of \$0.1 million, \$0.2 million and \$0.4 million, respectively.

DISPOSITION ACTIVITIES

We and SNH have sold certain senior living communities we leased from SNH that we and SNH had previously agreed to sell and we had classified as discontinued operations, and our rent payable to SNH was reduced as these sales occurred. These sales included:

• In January 2014, we and SNH sold an assisted living community located in Texas with 48 living units, and our annual rent payable to SNH decreased by \$0.2 million as a result.

• In June 2014, we and SNH sold two SNFs located in Wisconsin with a combined 139 living units, and our annual rent payable to SNH decreased by \$0.5 million as a result.

• In October 2014, we and SNH sold an assisted living community located in Virginia with 55 living units, and our annual rent payable to SNH decreased by \$0.3 million as a result.

• Also in October 2014, we and SNH sold an assisted living community and a SNF located in Arizona with a combined 160 living units, and our annual rent payable to SNH decreased by \$0.6 million as a result.

• In February 2015, we and SNH sold a vacant assisted living community located in Pennsylvania, and our annual rent payable to SNH decreased by approximately \$22,500 as a result.

• In July 2015, we and SNH sold a SNF located in Iowa with 12 living units, and our annual rent payable to SNH decreased by \$15,500 as a result.

•

In August 2015, we and SNH sold a SNF located in Wisconsin with 39 living units, and our annual rent payable to SNH decreased by \$85,000 as a result.

In December 2015, we and SNH sold a SNF located in Iowa with 117 living units, and our annual rent payable to SNH decreased by \$2,100 as a result.

In June 2016, we entered into a transaction agreement and related agreements with SNH pursuant to which, among other things, we sold seven senior living communities to SNH for \$112.4 million and SNH simultaneously leased these

Table of Contents

communities back to us under a new long term lease agreement. Under the new lease, we are required to pay SNH initial annual rent of \$8.4 million, plus percentage rent beginning in 2018.

In September 2016, we and SNH sold a vacant SNF located in Wisconsin, and our annual rent payable to SNH decreased by \$24,800 as a result.

Also in September 2016, we sold an assisted living community we owned with 32 living units located in Alabama for \$0.2 million, excluding closing costs. The results of operations for this community were previously included in discontinued operations.

In December 2016, SNH sold a memory care building located in Florida that we historically managed, and the separate management agreement for this building was terminated as a result.

For more information regarding our leases and management agreements with SNH, see Note 9 to our Consolidated Financial Statements included in Part IV, Item 15 of this Annual Report on Form 10-K.

Table of Contents

RESULTS OF OPERATIONS (dollars in thousands)

Key Statistical Data For the Years Ended December 31, 2016 and 2015

The following tables present a summary of our operations for the years ended December 31, 2016 and 2015:

Year Ended December 31,

| (dollars in thousands, except average monthly rate) | 2016 | 2015 | Change | %/ bps Change | |
|--|-------------|-------------|----------|------------------|-----|
| Senior living revenue | \$1,115,551 | \$1,113,971 | \$1,580 | 0.1 | % |
| Management fee revenue | 12,350 | 10,728 | 1,622 | 15.1 | % |
| Reimbursed costs incurred on behalf of managed communities | 250,207 | 240,711 | 9,496 | 3.9 | % |
| Total revenues | 1,378,108 | 1,365,410 | 12,698 | 0.9 | % |
| Senior living wages and benefits | (545,603) | (539,086) | (6,517) | (1.2) | % |
| Other senior living operating expenses | (284,533) | (293,501) | 8,968 | 3.1 | % |
| Costs incurred on behalf of managed communities | (250,207) | (240,711) | (9,496) | (3.9) | % |
| Rent expense | (201,667) | (199,075) | (2,592) | (1.3) | % |
| General and administrative expenses | (73,516) | (70,757) | (2,759) | (3.9) | % |
| Depreciation and amortization expense | (38,052) | (33,815) | (4,237) | (12.5) | % |
| Goodwill impairment | — | (25,344) | 25,344 | 100.0 | % |
| Long lived asset impairment | (502) | (145) | (357) | (246.2) | % |
| Interest, dividend and other income | 984 | 982 | 2 | 0.2 | % |
| Interest and other expense | (4,912) | (4,927) | 15 | 0.3 | % |
| Gain on early extinguishment of debt | — | 692 | (692) | (100.0) | % |
| Gain on sale of available for sale securities reclassified from accumulated other comprehensive income | 107 | 160 | (53) | (33.1) | % |
| Provision for income taxes | (2,351) | (662) | (1,689) | (255.1) | % |
| Equity in earnings of an investee | 137 | 20 | 117 | 585.0 | % |
| Loss from continuing operations | \$(22,007) | \$(40,759) | \$18,752 | 48.6 | % |
| Total number of communities (end of period): | | | | | |
| Owned and leased communities ⁽¹⁾ | 215 | 214 | 1 | 0.5 | % |
| Managed communities | 68 | 60 | 8 | 13.3 | % |
| Number of total communities ⁽¹⁾ | 283 | 274 | 9 | 3.3 | % |
| Total number of living units (end of period): | | | | | |
| Owned and leased living units ⁽¹⁾⁽²⁾ | 23,042 | 23,227 | (185) | (0.8) | % |
| Managed living units ⁽²⁾ | 8,788 | 8,190 | 598 | 7.3 | % |
| Number of total living units ⁽¹⁾⁽²⁾ | 31,830 | 31,417 | 413 | 1.3 | % |
| Owned and leased communities ⁽¹⁾ : | | | | | |
| Occupancy % ⁽²⁾ | 84.3 | % 85.2 | % n/a | (90) | bps |
| Average monthly rate ⁽³⁾ | \$4,640 | \$4,590 | \$50 | 1.1 | % |
| Percent of senior living revenue from Medicaid | 11.5 | % 11.2 | % n/a | 30 | bps |
| Percent of senior living revenue from Medicare | 10.3 | % 11.1 | % n/a | (80) | bps |
| Percent of senior living revenue from private and other sources | 78.2 | % 77.7 | % n/a | 50 | bps |

(1) Excludes senior living communities classified as discontinued operations.

(2) For the year ended December 31, 2016, the calculation of occupancy includes only living units categorized as in service; occupancy calculations for periods prior to 2016 included certain living units categorized as out of service.

(3) Average monthly rate is calculated by taking the average daily rate, which is defined as total operating revenues divided by occupied units during the period, and multiplying it by 30 days.

Table of Contents

Comparable communities (senior living communities that we owned, leased or managed and operated continuously since January 1, 2015):

| (dollars in thousands, except average monthly rate) | Year Ended December 31, | | | | |
|---|-------------------------|-------------|----------|--------|--------|
| | 2016 | 2015 | Change | %/bps | Change |
| Senior living revenue | \$1,109,631 | \$1,106,556 | \$3,075 | 0.3 | % |
| Management fee revenue | 10,127 | 10,048 | 79 | 0.8 | % |
| Senior living wages and benefits | (544,187) | (534,052) | (10,135) | (1.9) | % |
| Other senior living operating expenses | (282,234) | (290,616) | 8,382 | 2.9 | % |
| Total number of communities (end of period): | | | | | |
| Owned and leased communities ⁽¹⁾ | 211 | 211 | — | — | |
| Managed communities | 46 | 46 | — | — | |
| Number of total communities ⁽¹⁾ | 257 | 257 | — | — | |
| Total number of living units (end of period): | | | | | |
| Owned and leased living units ⁽¹⁾⁽²⁾ | 22,765 | 22,917 | (152) | (0.7) | % |
| Managed living units | 7,208 | 7,306 | (98) | (1.3) | % |
| Number of total living units ⁽¹⁾⁽²⁾ | 29,973 | 30,223 | (250) | (0.8) | % |
| Owned and leased communities ⁽¹⁾ : | | | | | |
| Occupancy % ⁽²⁾ | 84.2 | % 85.3 | % n/a | (110) | bps |
| Average monthly rate ⁽³⁾ | \$4,651 | \$4,586 | \$65 | 1.4 | % |
| Percent of senior living revenue from Medicaid | 11.5 | % 10.9 | % n/a | 60 | bps |
| Percent of senior living revenue from Medicare | 10.3 | % 11.1 | % n/a | (80) | bps |
| Percent of senior living revenue from private and other sources | 78.2 | % 78.0 | % n/a | 20 | bps |

(1) Excludes senior living communities classified as discontinued operations.

(2) For the year ended December 31, 2016, the calculation of occupancy includes only living units categorized as in service; occupancy calculations for periods prior to 2016 included certain living units categorized as out of service.

(3) Average monthly rate is calculated by taking the average daily rate, which is defined as total operating revenues divided by occupied units during the period, and multiplying it by 30 days.

Year Ended December 31, 2016, Compared to Year Ended December 31, 2015

Senior living revenue. Senior living revenue increased by 0.1% for the year ended December 31, 2016 compared to the year ended December 31, 2015 primarily due to an increase in average monthly rates to residents who pay privately for services, a \$1.0 million reversal in revenue reserves recorded in 2016 as a result of the final settlement amount of the Medicare compliance assessment at one of our SNFs, or the Compliance Assessment, being less than the previously estimated amount, a \$2.4 million revenue reserve recorded in 2015 related to the Compliance Assessment and our acquisition of two senior living communities during the fourth quarter of 2015, partially offset by a decrease in occupancy at our comparable senior living communities.

Management fee revenue. Management fee revenue increased by 15.1% for the year ended December 31, 2016 compared to the year ended December 31, 2015 primarily due to an increase in the base management fee to 5% from 3% under our management agreements with SNH for certain senior living communities and fees for the management of capital expenditure projects by us at the senior living communities we manage for the account of SNH, each of which became effective as of July 1, 2016, and an increase in the number of managed communities from 60 to 68. Reimbursed costs incurred on behalf of managed communities. Reimbursed costs incurred on behalf of managed communities increased by 3.9% for the year ended December 31, 2016 compared to the year ended December 31, 2015 primarily due to an increase in the number of managed communities from 60 to 68.

Senior living wages and benefits. Senior living wages and benefits increased by 1.2% for the year ended December 31, 2016 compared to the year ended December 31, 2015 primarily due to annual wage increases, increases in employee health insurance costs and our acquisition of two senior living communities during the fourth quarter of 2015, partially offset by decreases in workers' compensation insurance costs.

Table of Contents

Other senior living operating expenses. Other senior living operating expenses, which include utilities, housekeeping, dietary, maintenance, insurance and community level administrative costs, decreased by 3.1% for the year ended December 31, 2016 compared to the year ended December 31, 2015 primarily due to a \$0.5 million reversal in accrued liability recorded in 2016 for estimated penalties related to the Compliance Assessment, \$4.2 million in penalties, compliance costs and professional fees recorded in 2015 related to the Compliance Assessment and a \$4.2 million charge recorded in 2015 in connection with the settlement of our Arizona litigation matter, partially offset by transaction costs we incurred primarily related to the June 2016 sale and leaseback transaction and increased professional and general liability insurance expense.

Rent expense. Rent expense increased by 1.3% for the year ended December 31, 2016 compared to the year ended December 31, 2015 primarily due to additional rent related to senior living community capital improvements we sold to SNH since January 1, 2015 pursuant to our leases with SNH and an increase in the number of leased communities as a result of the June 2016 sale and leaseback transaction as well as two communities we began to lease from SNH during the fourth quarter of 2016, partially offset by rent reductions as a result of the sale of certain communities that we leased from SNH during 2015 and 2016 and amortization of the deferred gain we realized from the June 2016 sale and leaseback transaction.

General and administrative expenses. General and administrative expenses increased by 3.9% for the year ended December 31, 2016 compared to the year ended December 31, 2015 primarily due to increases in certain corporate wages and benefits, transaction costs relating to our acquisition and disposition activities, purchased services and professional fees, partially offset by separation payments for our former chief financial officer and treasurer and a reduction in the business management and other professional fees we incurred in 2015.

Depreciation and amortization expense. Depreciation and amortization expense increased by 12.5% for the year ended December 31, 2016 compared to the year ended December 31, 2015 primarily due to our acquisition of two senior living communities during the fourth quarter of 2015 and capital expenditures at our owned and leased senior living communities (net of our sales of capital improvements to SNH at our leased communities).

Goodwill impairment. For the year ended December 31, 2015, we recorded a non-cash charge for goodwill impairment of \$25.3 million to write down the goodwill in our senior living reporting unit to its implied fair value. For more information related to this non-cash charge for goodwill impairment, see Note 4 to our Consolidated Financial Statements included in Part IV, Item 15 of this Annual Report on Form 10-K.

Long lived asset impairment. For the years ended December 31, 2016 and 2015, we recorded non-cash charges for long lived assets impairment of \$0.5 million and \$0.1 million, respectively, to reduce the carrying value of certain of our long lived assets to their estimated fair values.

Interest, dividend and other income. Interest, dividend and other income increased by 0.2% for the year ended December 31, 2016 compared to the year ended December 31, 2015 primarily due to higher investable cash and cash equivalents balances.

Interest and other expense. Interest and other expense decreased by 0.3% for the year ended December 31, 2016 compared to the year ended December 31, 2015 primarily due to the repayment of all of the outstanding borrowings under our prior credit facility with proceeds from the June 2016 sale and leaseback transaction, partially offset by our assumption of a mortgage note in connection with our acquisition of two senior living communities during the fourth quarter of 2015.

Gain on early extinguishment of debt. For the year ended December 31, 2015, we recorded a gain on early extinguishment of debt of \$0.7 million in connection with our prepayment of a mortgage note.

Gain on sale of available for sale securities reclassified from accumulated other comprehensive income. Gain on sale of available for sale securities reclassified from accumulated other comprehensive income represents our realized gain

on investments.

Provision for income taxes. For the years ended December 31, 2016 and December 31, 2015, we recognized a provision for income taxes from continuing operations of \$2.4 million and \$0.7 million, respectively. The 2016 increase in our provision for income taxes compared to the year ended December 31, 2015 is primarily due to the taxes on the gain we realized for tax purposes in connection with the June 2016 sale and leaseback transaction. We did not recognize any federal tax expense for 2016 because our federal taxable income and expense were offset by our federal net operating loss carry forwards and tax credit carry forwards. For additional information regarding our taxes, see Note 5 to our Consolidated Financial Statements included in Part IV, Item 15 of this Annual Report on Form 10-K.

42

Table of Contents

Equity in earnings of an investee. Equity in earnings of an investee represents our proportionate share of earnings from AIC.

Discontinued operations:

We recorded income from discontinued operations for the year ended December 31, 2016 of \$0.2 million compared to a loss of \$2.3 million for the year ended December 31, 2015. The loss from discontinued operations for the year ended December 31, 2015 was primarily due to losses incurred at assisted living communities and SNFs that have been sold.

Key Statistical Data For the Years Ended December 31, 2015 and 2014

The following tables present a summary of our operations for the years ended December 31, 2015 and 2014:

| (dollars in thousands, except average monthly rate) | Year Ended December 31, | | | | |
|--|-------------------------|-------------|-----------|----------|--------|
| | 2015 | 2014 | Change | %/bps | Change |
| Senior living revenue | \$1,113,971 | \$1,099,228 | \$14,743 | 1.3 | % |
| Management fee revenue | 10,728 | 9,765 | 963 | 9.9 | % |
| Reimbursed costs incurred on behalf of managed communities | 240,711 | 219,082 | 21,629 | 9.9 | % |
| Total revenues | 1,365,410 | 1,328,075 | 37,335 | 2.4 | % |
| Senior living wages and benefits | (539,086) | (533,549) | (5,537) | (1.0) | % |
| Other senior living operating expenses | (293,501) | (292,457) | (1,044) | (0.4) | % |
| Costs incurred on behalf of managed communities | (240,711) | (219,082) | (21,629) | (9.9) | % |
| Rent expense | (199,075) | (197,359) | (1,716) | (0.9) | % |
| General and administrative expenses | (70,757) | (72,385) | 1,628 | 2.2 | % |
| Depreciation and amortization expense | (33,815) | (31,834) | (1,981) | (6.2) | % |
| Goodwill impairment | (25,344) | — | (25,344) | (100.0) | % |
| Long lived asset impairment | (145) | (589) | 444 | 75.4 | % |
| Interest, dividend and other income | 982 | 867 | 115 | 13.3 | % |
| Interest and other expense | (4,927) | (5,131) | 204 | 4.0 | % |
| Loss on early extinguishment of debt | 692 | — | 692 | 100.0 | % |
| Gain on sale of available for sale securities reclassified from accumulated other comprehensive income | 160 | 392 | (232) | (59.2) | % |
| Provision for income taxes | (662) | (56,385) | 55,723 | 98.8 | % |
| Equity in earnings of an investee | 20 | 87 | (67) | (77.0) | % |
| Loss from continuing operations | \$(40,759) | \$(79,350) | \$38,591 | (48.6) | % |
| Total number of communities (end of period): | | | | | |
| Owned and leased communities ⁽¹⁾ | 214 | 212 | 2 | 0.9 | % |
| Managed communities | 60 | 46 | 14 | 30.4 | % |
| Number of total communities ⁽¹⁾ | 274 | 258 | 16 | 6.2 | % |
| Total number of living units (end of period): | | | | | |
| Owned and leased living units ⁽¹⁾ | 23,227 | 23,101 | 126 | 0.5 | % |
| Managed living units | 8,190 | 7,278 | 912 | 12.5 | % |
| Number of total living units ⁽¹⁾ | 31,417 | 30,379 | 1,038 | 3.4 | % |
| Owned and leased communities ⁽¹⁾ : | | | | | |
| Occupancy % | 85.2 | % 86.0 | % n/a | (80) | bps |
| Average monthly rate ⁽²⁾ | \$4,590 | \$4,516 | \$74 | 1.6 | % |
| Percent of senior living revenue from Medicaid | 11.2 | % 10.9 | % n/a | 30 | bps |
| Percent of senior living revenue from Medicare | 11.1 | % 11.9 | % n/a | (80) | bps |
| Percent of senior living revenue from private and other sources | 77.7 | % 77.2 | % n/a | 50 | bps |

(1) Excludes senior living communities classified as discontinued operations.

(2) Average monthly rate is calculated by taking the average daily rate, which is defined as total operating revenues divided by occupied units during the period, and multiplying it by 30 days.

Table of Contents

Comparable communities (senior living communities that we owned, leased or managed and operated continuously since January 1, 2014):

| (dollars in thousands, except average monthly rate) | Year Ended December 31, | | | | |
|---|-------------------------|-------------|----------|-------|--------|
| | 2015 | 2014 | Change | %/bps | Change |
| Senior living revenue | \$1,108,218 | \$1,095,917 | \$12,301 | 1.1 | % |
| Management fee revenue | 9,757 | 9,249 | 508 | 5.5 | % |
| Senior living wages and benefits | (536,943) | (532,256) | (4,687) | (0.9 |)% |
| Other senior living operating expenses | (291,809) | (291,656) | (153) | (0.1 |)% |
| Total number of communities (end of period): | | | | | |
| Owned and leased communities ⁽¹⁾ | 211 | 211 | n/a | — | |
| Managed communities | 44 | 44 | n/a | — | |
| Number of total communities ⁽¹⁾ | 255 | 255 | n/a | — | |
| Total number of living units (end of period): | | | | | |
| Owned and leased living units ⁽¹⁾⁽²⁾ | 22,961 | 22,948 | 13 | 0.1 | % |
| Managed living units | 7,079 | 7,051 | 28 | 0.4 | % |
| Number of total living units ⁽¹⁾⁽²⁾ | 30,040 | 29,999 | 41 | 0.1 | % |
| Owned and leased communities ⁽¹⁾ : | | | | | |
| Occupancy % ⁽²⁾ | 85.1 | % 86.0 | % n/a | (90 |) bps |
| Average monthly rate ⁽³⁾ | \$4,596 | \$4,519 | \$77 | 1.7 | % |
| Percent of senior living revenue from Medicaid | 11.2 | % 10.9 | % n/a | 30 | bps |
| Percent of senior living revenue from Medicare | 11.2 | % 11.9 | % n/a | (70 |) bps |
| Percent of senior living revenue from private and other sources | 77.6 | % 77.2 | % n/a | 40 | bps |

(1) Excludes senior living communities classified as discontinued operations.

(2) Excludes 38 living units in one senior living community that was temporarily closed for a major renovation during part of 2014, and includes certain other living units added or removed at the comparable communities.

(3) Average monthly rate is calculated by taking the average daily rate, which is defined as total operating revenues divided by occupied units during the period, and multiplying it by 30 days.

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

Senior living revenue. Senior living revenue increased by 1.3% for the year ended December 31, 2015 compared to the year ended December 31, 2014 primarily due to an increase in average monthly rates to private pay residents and a \$4.3 million revenue reserve recorded in 2014 in connection with the Compliance Assessment, partially offset by a decrease in occupancy at our comparable senior living communities and a \$2.4 million increase in the revenue reserve recorded in 2015 in connection with the Compliance Assessment.

Management fee revenue. Management fee revenue and reimbursed costs at our managed communities each increased 9.9% during the year ended December 31, 2015 compared to the year ended December 31, 2014 primarily due to an increase in the number of managed communities from 46 to 60 and an increase in average monthly rates to private pay residents, partially offset by a decrease in occupancy at our comparable managed communities.

Senior living wages and benefits. Senior living wages and benefits increased by 1.0% for the year ended December 31, 2015 compared to the year ended December 31, 2014 primarily due to wage rate increases.

Other senior living operating expenses. Other senior living operating expenses, which include utilities, housekeeping, dietary, maintenance, insurance and community level administrative costs, increased by 0.4% during the year ended December 31, 2015 compared to the year ended December 31, 2014 primarily due to a \$4.2 million charge recorded in 2015 in connection with the settlement of the Arizona litigation and \$4.2 million in penalties, compliance costs and professional fees recorded in 2015 related to the Compliance Assessment, partially offset by decreased costs related to

our professional and general liability insurance programs, a decrease in pharmacy related expenses and favorable adjustments to bad debt expense as a result of improved receivables collections.

44

Table of Contents

Rent expense. Rent expense increased by 0.9% for the year ended December 31, 2015 compared to the year ended December 31, 2014 primarily due to additional rent related to senior living community capital improvements purchased by SNH since January 1, 2014 pursuant to our leases with SNH, partially offset by rent reductions as a result of the sale of certain communities that we leased from SNH during 2014 and 2015.

General and administrative expenses. General and administrative expenses decreased by 2.2% for the year ended December 31, 2015 compared to the year ended December 31, 2014 primarily due to decreased audit and public company related costs in 2015, partially offset by an increase in wages for certain specialized personnel, including information technology, accounting and tax, recruiting costs, separation payments for our former chief financial officer and treasurer and business management and other professional fees.

Depreciation and amortization expense. Depreciation and amortization expense increased by 6.2% for the year ended December 31, 2015 compared to the year ended December 31, 2014 primarily due to capital expenditures at our owned and leased senior living communities (net of our sales of capital improvements to SNH at our leased communities), our acquisition of one senior living community in May 2014 and two senior living communities in November 2015.

Goodwill impairment. For the year ended December 31, 2015, we recorded a non-cash charge for goodwill impairment of \$25.3 million to write down the goodwill in our senior living reporting unit to its implied fair value. For more information related to this non-cash charge for goodwill impairment, see Note 4 to our Consolidated Financial Statements included in Part IV, Item 15 of this Annual Report on Form 10-K.

Long lived asset impairment. For the years ended December 31, 2015 and 2014, we recorded non-cash impairment charges to certain of our long lived assets of \$0.1 million and \$0.6 million, respectively, to reduce the carrying values to their estimated fair values.

Interest, dividend and other income. Interest, dividend and other income increased by 13.3% for the year ended December 31, 2015 compared to the year ended December 31, 2014 primarily due to higher investable cash and cash equivalents balances.

Interest and other expense. Interest and other expense decreased by 4.0% for the year ended December 31, 2015 compared to the year ended December 31, 2014 primarily due to our prepayment of a mortgage during the second quarter of 2015 and decreased deferred financing fees relating to our prior credit facility that we amortized as interest expense, partially offset by our assumption of a mortgage note in connection with our acquisition of a senior living community in the second quarter of 2014.

Gain on sale of available for sale securities reclassified from accumulated other comprehensive income. Gain on sale of available for sale securities reclassified from accumulated other comprehensive income represents our realized gain on investments sold.

Provision for income taxes. For the year ended December 31, 2015, we recognized income tax expense from continuing operations of \$0.7 million, of which \$1.0 million represents current state tax expense that is payable without regard to our tax loss carry forwards. The decrease in our provision for income taxes compared to the year ended December 31, 2014 is a result of establishing a full valuation allowance against our net deferred tax assets in 2014. We did not recognize any income tax expense or benefit from our discontinued operations in 2015. For additional information regarding our taxes, see Note 5 to our Consolidated Financial Statements included in Part IV, Item 15 of this Annual Report on Form 10-K.

Equity in earnings of an investee. Equity in earnings of an investee represents our proportionate share of earnings from AIC.

Discontinued operations:

We recorded a loss from discontinued operations of \$2.3 million for the year ended December 31, 2015 compared to a loss from discontinued operations of \$6.1 million for the year ended December 31, 2014. The losses in both periods

were primarily due to losses incurred at SNFs and assisted living communities that we have sold. The loss for the year ended December 31, 2014 also includes income tax expense of \$0.1 million that we recognized in that period related to our discontinued operations.

Table of Contents

LIQUIDITY AND CAPITAL RESOURCES

As of December 31, 2016, we had \$16.6 million of unrestricted cash and cash equivalents and \$85.3 million available to borrow under our prior credit facility. As of February 28, 2017, we had \$20.0 million in cash and cash equivalents and \$100.0 million available to borrow under our new credit facility.

Our principal sources of funds to meet operating and capital expenses and debt service obligations are cash flows from operating activities, unrestricted cash balances, borrowings under our new credit facility and proceeds from our sales to SNH of qualified capital improvements we may make to communities that we lease from SNH for increased rent pursuant to our leases. We believe that these sources will be sufficient to meet our operating and capital expenses and debt service obligations for the next 12 months and for the foreseeable future thereafter.

Our future cash flows from operating activities will depend primarily upon our ability to maintain or increase the occupancy of, and the rental rates at, our senior living communities and our ability to control operating expenses at our senior living communities. If occupancy at our senior living communities continues to decline, the rates we receive from residents who pay for our services with private resources decline, government reimbursement rates are reduced and we are unable to generate positive cash flows for an extended period, or for other reasons, we expect that we would explore various alternatives to fund our operations. Such alternatives may include further reducing our costs, incurring debt under or in addition to our new credit facility, engaging in additional sale and leaseback transactions, assuming mortgage debt in connection with acquisitions, mortgage financing our owned senior living communities and issuing other debt or equity securities. We may also elect to pursue such funding sources for other business reasons, including growing our business.

Assets and Liabilities

At December 31, 2016, we had cash and cash equivalents of \$16.6 million compared to \$14.7 million at December 31, 2015. Our total current assets at December 31, 2016 and December 31, 2015 were \$129.4 million and \$112.1 million, respectively. Our total current and long term liabilities were \$173.0 million and \$172.5 million, respectively, at December 31, 2016 compared to \$243.9 million and \$103.4 million, respectively, at December 31, 2015. The increase in our total current assets primarily relates to increased restricted cash at our captive insurance company subsidiary as collateral for an \$11.7 million letter of credit, an increase in due from related persons because of timing differences in when payments were received and an increase in cash and cash equivalents as described further below. The decrease in our total current liabilities primarily relates to our repayment in 2016 of outstanding borrowings under our prior credit facility, a settlement payment we made related to our Arizona litigation matter, a payment we made to the OIG in connection with the settlement of the Compliance Assessment and decreases in our accounts payables and accrued expenses due to timing differences in when payments were made, offset by an increase related to the short term portion of the deferred gain we recorded in connection with the June 2016 sale and leaseback transaction. The increase in our total long term liabilities primarily relates to the long term portion of the deferred gain we recorded in connection with the June 2016 sale and leaseback transaction.

We had cash flows used in operating activities of \$23.5 million for the year ended December 31, 2016 compared to cash flows provided by operating activities of \$40.5 million for the year ended December 31, 2015. The decrease in our cash flows from operating activities for the year ended December 31, 2016 was primarily due to a settlement payment we made related to our Arizona litigation matter, a payment we made to the OIG in connection with the settlement of the Compliance Assessment, and the timing of other payments made by us for payables and other accrued expenses and received by us from related persons, and lower operating income before goodwill and other non-cash charges during the year ended December 31, 2016 compared to the year ended December 31, 2015.

We had cash flows provided by investing activities of \$77.0 million for the year ended December 31, 2016 compared to cash flows used in investing activities of \$53.3 million for the year ended December 31, 2015. The increase in cash provided by investing activities was due to the \$112.4 million of proceeds received from the June 2016 sale and leaseback transaction and an increase in the proceeds from sale of available for sale securities net of purchase of available for sale securities. Acquisitions of property and equipment, on a net basis after considering the proceeds from sales of such assets to SNH, were \$34.0 million and \$36.2 million for the years ended December 31, 2016 and 2015, respectively.

We had cash flows used in financing activities of \$51.6 million compared to cash flows provided by financing activities of \$8.6 million for the years ended December 31, 2016 and 2015, respectively. The increase in cash flows used in financing activities for the year ended December 31, 2016 was due to the net repayment of \$50.0 million of outstanding borrowings under our prior credit facility primarily with proceeds from the June 2016 sale and leaseback transaction.

Table of Contents

Available for Sale Securities

We routinely evaluate our investments in available for sale securities to determine if they have been impaired. If the fair value of an investment is less than its book or carrying value, and we expect that situation to continue for more than a temporary period, we will record an “other than temporary impairment” loss in our consolidated statements of operations. We evaluate the fair value of our available for sale securities by reviewing each security’s current market price, the ratings of the security, the financial condition of the issuer, and our intent and ability to retain the security during temporary market price fluctuations or until maturity. In evaluating the factors described above, we presume a decline in value to be an “other than temporary impairment” if the quoted market price of the security is below the security’s cost basis for an extended period. However, this presumption may be overcome if there is persuasive evidence indicating the value decline is temporary in nature, such as when the operating performance of the obligor is strong or if the market price of the security is historically volatile. Additionally, there may be instances in which impairment losses are recognized even if the decline in value does not meet the criteria described above, such as if we plan to sell the security in the near term and the fair value is below our cost basis. When we believe that a change in fair value of an available for sale security is temporary, we record a corresponding credit or charge to other comprehensive income for any unrealized gains and losses. When we determine that impairment in the fair value of an available for sale security is an “other than temporary impairment”, we record a charge to earnings. We did not record an impairment charge for the years ended December 31, 2016, 2015 or 2014 for our available for sale securities.

Litigation Settlement

We were defendants in a lawsuit filed in the Superior Court of Maricopa County, Arizona by the estate of a former resident of a senior living community operated by us. The complaint asserted claims against us for pain and suffering as a result of improper treatment constituting violations of the Arizona Adult Protective Services Act and wrongful death. In May 2015, the jury rendered a decision in our favor on the wrongful death claim, and against us on the remaining claims, returning verdicts awarding damages of approximately \$19.2 million, which consisted of \$2.5 million for pain and suffering and the remainder in punitive damages. In March 2016, pursuant to a settlement agreement we entered into with the plaintiff, \$7.3 million was paid to the plaintiff, of which \$3.0 million was paid by our liability insurer and the balance by us. We believe our liability insurer may be financially responsible for more than \$3.0 million and we are seeking additional payments from our liability insurer; however, we cannot predict the outcome of our ongoing negotiations or potential future litigation with our liability insurer. As a result, we recorded a \$4.2 million charge during the year ended December 31, 2015, which was included in other senior living operating expenses in our consolidated statements of operations.

Our Leases and Management Agreements with SNH

As of December 31, 2016, we leased 185 senior living communities from SNH under five leases. Our total annual rent payable to SNH as of December 31, 2016 was \$203.8 million, excluding percentage rent based on increases in gross revenues at certain communities. Our total rent expense under all of our leases with SNH, net of lease inducement amortization and the amortization of the deferred gain from the June 2016 sale and leaseback transaction, was \$198.8 million, \$196.3 million and \$195.5 million for the years ended December 31, 2016, 2015 and 2014, respectively, which included approximately \$5.6 million, \$5.7 million and \$5.8 million in estimated percentage rent due to SNH, respectively.

In June 2016, we entered into a transaction agreement and related agreements with SNH pursuant to which, among other things, we sold seven senior living communities to SNH and SNH simultaneously leased these communities back to us under a new long term lease agreement. Under the new lease, we are required to pay SNH initial annual rent of \$8.4 million, plus percentage rent beginning in 2018.

Upon our request, SNH may purchase capital improvements made at the communities we lease from SNH and increase our rent pursuant to contractual formulas; however, SNH is not obligated to purchase these improvements from us. During the year ended December 31, 2016, we sold to SNH \$21.4 million of capital improvements made at the communities we lease from SNH, and these purchases resulted in our annual rent being increased by

approximately \$1.7 million.

We managed 68 senior living communities for the account of SNH as of December 31, 2016, pursuant to long term management agreements and pooling agreements that combine various calculations of revenues and expenses from the operations of the communities covered by the applicable pooling agreement. We earned base management fees from SNH of \$11.5 million, \$10.5 million and \$9.5 million for the years ended December 31, 2016, 2015 and 2014, respectively. In addition, we earned incentive fees of \$108,000 and fees for our management of capital expenditure projects at the communities we managed for the account of SNH of \$432,000 for the year ended December 31, 2016. Also, pursuant to our management agreement with D&R Yonkers LLC, we earned management fees of \$262,000, \$210,000 and \$222,000 for the years ended

Table of Contents

December 31, 2016, 2015 and 2014, respectively, all of which are included in management fee revenue in our consolidated statement of operations.

As part of the June 2016 sale and leaseback transaction described above, we and SNH terminated three of our four then existing pooling agreements and entered into 10 new pooling agreements that combine our management agreements with SNH for senior living communities that include assisted living units.

For more information regarding our leases and management arrangements and other transactions with SNH, see Notes 9, 11 and 16 to our Consolidated Financial Statements included in Part IV, Item 15 in this Annual Report on Form 10-K.

Our Revenues

Our revenues from services to residents at our senior living communities are our primary source of cash to fund our operating expenses, including rent, capital expenditures (net of capital improvements that we sell to SNH for increased rent pursuant to our leases with SNH) and principal and interest payments on our debt.

During the past several years, weak economic conditions in many areas throughout the United States have negatively affected many businesses in these areas. These conditions have resulted in, among other things, a decrease in our communities' occupancy, and it is unclear when these conditions may materially improve. Although many of the services that we provide are needs driven, some of our prospective residents may be deferring their decisions to relocate to senior living communities in light of current economic circumstances. In recent years, economic indicators reflect an improving housing market; however, it is unclear how sustainable the improvements will be and whether any such improvements will result in any increased demand for our services.

For the past two to three years, low capital costs appear to have encouraged increased senior living development, particularly in areas where existing senior living communities have historically experienced high occupancies. As the recently developed senior living communities begin operations, we expect to have continuing challenges to maintain or increase occupancies at our senior living communities.

At some of our senior living communities (principally our SNFs) and our rehabilitation and wellness clinics, Medicare and Medicaid programs provide operating revenues for skilled nursing and rehabilitation and wellness services. We derived approximately 22%, 22% and 23% of our consolidated revenues from continuing operations from these programs for each of the years ended December 31, 2016, 2015 and 2014, respectively. Our net Medicare revenues from services to senior living community residents from continuing operations totaled \$112.1 million, \$122.0 million and \$129.2 million for the years ended December 31, 2016, 2015 and 2014, respectively. Our net Medicaid revenues from services to senior living community residents from continuing operations totaled \$126.2 million, \$122.8 million and \$118.5 million for the years ended December 31, 2016, 2015 and 2014, respectively.

In July 2016, CMS issued a final rule updating Medicare payments to SNFs for federal fiscal year 2017, which CMS estimated will increase payments to SNFs by an aggregate of 2.4%, or approximately \$920.0 million, compared to payments in federal fiscal year 2016. MACRA limits the market basket increase for SNFs to 1.0% in federal fiscal year 2018. It is unclear whether these adjustments in Medicare rates will compensate for the increased costs we may incur for services to our residents whose services are paid for by Medicare.

The Budget Control Act of 2011 and the Bipartisan Budget Act of 2013 allow for automatic reductions in federal spending by means of a process called sequestration, which reduces Medicare payment rates by 2.0% through 2023. In 2014 and 2015, Congress approved two additional one year extensions of Medicare sequestration, through 2025.

Medicaid is exempt from the automatic reductions, as are certain Medicare benefits. The automatic 2.0% payment cuts took effect on April 1, 2013, and had an adverse effect on our operations and financial results. Subsequent legislation appears to have modified some aspects of the sequestration process, but at this time it is unclear what impact this legislation may have on Medicare payments we receive. Any future reductions in Medicare payment rates could be material and adverse to our financial results of operations. Furthermore, the Middle Class Tax Relief and Job Creation Act of 2012, which was enacted in February 2012, incrementally reduced the SNF reimbursement rate for Medicare bad debt from 100% to 65% by federal fiscal year 2015 for beneficiaries dually eligible for Medicare and Medicaid. Because nearly 90% of SNF bad debt has historically been related to dual eligible beneficiaries, this rule

has a substantial negative effect on SNFs, including some that we operate. The same law also reduced the SNF Medicare bad debt reimbursement rate for Medicare beneficiaries not eligible for Medicaid from 70% to 65% in federal fiscal year 2013 and going forward.

Table of Contents

The federal government is seeking to slow the growth of Medicare and Medicaid payments for SNF services by several methods. In 2006, the government implemented limits on Medicare payments for outpatient therapies and then, pursuant to the DRA, created an exception process under which beneficiaries could request an exception from the cap and be granted the amount of services deemed medically necessary by Medicare. On April 1, 2014, PAMA extended the Medicare outpatient therapy cap exception process through March 31, 2015, further postponing the implementation of firm limits on Medicare payments for outpatient therapies. In April 2015, Congress passed MACRA, which extended the outpatient therapy cap exceptions process from March 31, 2015 through December 31, 2017, further postponing the implementation of strict limits on Medicare payments for outpatient therapies. MACRA also repealed the SGR formula for calculating updates to MPFS rates, which would have led to a 21.2% rate reduction effective April 1, 2015, and replaced the SGR formula with a different reimbursement methodology.

In October 2016, CMS issued a final rule to implement the Quality Payment Program. These reforms were mandated under MACRA and replace the SGR methodology for updates to the MPFS to which our Medicare outpatient therapy rates are tied. Starting in 2019, providers may be subject to either MIPS payment adjustments or APM incentive payments.

Additionally, PAMA established a SNF Value-Based Purchasing Program, under which HHS will assess SNFs based on hospital readmissions and make these assessments available to the public by October 1, 2017. Under PAMA, beginning in federal fiscal year 2019, Medicare payment rates will be partially based on SNFs' performance scores on a designated hospital readmissions measure. To fund the program, CMS will reduce Medicare payments to all SNFs by 2.0% through a withhold mechanism starting on October 1, 2018 and then redistribute between 50% and 70% of the withheld payments as incentive payments to those SNFs with the highest rankings on this measure.

In October 2014, President Obama signed into law the IMPACT Act, which requires certain post-acute care providers, including SNFs, to begin collecting and reporting various types of data. Under the SNF Quality Reporting Program, beginning in federal fiscal year 2018, SNFs that fail to timely comply with the reporting requirements will be subject to a 2.0% reduction in their Medicare payment rates for that fiscal year.

Although Medicaid is exempt from the sequestration process described above, some of the states in which we operate either have not raised Medicaid rates by amounts sufficient to offset increasing costs or have frozen or reduced, or are expected to freeze or reduce, Medicaid rates.

In September 2016, CMS issued a final rule to comprehensively update the Conditions of Participation for long term care facilities that participate in Medicare and Medicaid, such as our SNFs. The final rule, which went into effect beginning on November 28, 2016, institutes a broad range of new requirements, some of which stem from statutory modifications under the ACA and the IMPACT Act. These requirements will increase the cost of operations for long term care facilities that participate in Medicare and Medicaid, including our SNFs.

We cannot currently predict the type and magnitude of the potential Medicare and Medicaid policy changes, rate reductions or other changes and the impact on us of the possible failure of these programs to increase rates to match our increasing expenses, but they may be adverse and material to our operations and to our future financial results of operations. Similarly, we are unable to predict the impact on us of the insurance changes, payment changes and healthcare delivery systems changes contained in and to be developed pursuant to the ACA. If the changes implemented under the ACA result in reduced payments for our services, or the failure of Medicare, Medicaid or insurance payment rates to cover our costs of providing required services to residents, our future financial results could be materially and adversely affected. Finally, to the extent the ACA is repealed and replaced under the new Trump Administration and the 115th Congress, additional regulatory risks may arise. Depending upon what aspects of the ACA are repealed and whether and how they are replaced, our future financial results could be adversely and materially affected.

For more information regarding government regulation and their possible impact on us and our business, revenues and operations, see "Business—Government Regulation and Reimbursement" in Part I, Item 1 of this Annual Report on Form

10-K.

Insurance

Increases over time in the costs of insurance, especially professional and general liability insurance, workers' compensation and employee health insurance, have had an adverse impact upon our results of operations. Although we self insure a large portion of these costs, our costs have increased as a result of the higher costs that we incur to settle claims and to purchase insurance for claims in excess of the self insurance amounts. These increased costs may continue in the future. We, RMR LLC and other companies to which RMR LLC provides management services are the shareholders of an insurance

49

Table of Contents

company which has designed and reinsured in part a combined property insurance program in which we and the other shareholders participate. For more information about our existing insurance see “Business—Insurance” in Part I, Item 1 of this Annual Report on Form 10-K.

Discontinued Operations

We have reclassified our consolidated balance sheets and our consolidated statements of operations for all periods presented in our financial statements to show the financial position and results of operations of the senior living communities classified as discontinued operations. Below is a summary of the operating results of these discontinued operations included in the consolidated financial statements for the years ended December 31, 2016, 2015 and 2014 (dollars in thousands):

| | 2016 | 2015 | 2014 |
|--|--------|-----------|------------|
| Revenues | \$932 | \$4,191 | \$22,051 |
| Expenses | (500) | (5,818) | (28,028) |
| Impairment on discontinued assets | (112) | (697) | — |
| Provision for income taxes | (126) | — | (79) |
| Income (loss) from discontinued operations, net of tax | \$194 | \$(2,324) | \$(6,056) |

Contractual Obligations Table

As of December 31, 2016, our contractual obligations from continuing and discontinued operations were as follows (dollars in thousands):

| | Payment due by period | | | | |
|---|-----------------------|------------------|-----------|-----------|-------------------|
| | Total | Less than 1 year | 1-3 years | 3-5 years | More than 5 years |
| Contractual Obligations ⁽¹⁾ | | | | | |
| Debt obligations ⁽²⁾ | \$58,796 | \$1,354 | \$15,422 | \$2,700 | \$39,320 |
| Projected interest on long term debt obligations ⁽³⁾ | 20,098 | 3,694 | 5,866 | 5,045 | 5,493 |
| Operating lease obligations ⁽⁴⁾ | 2,198,107 | 206,513 | 413,187 | 413,411 | 1,164,996 |
| Continuing care contracts ⁽⁵⁾ | 3,157 | 2,126 | 445 | 331 | 255 |
| Accrued self-insurance obligations ⁽⁶⁾ | 56,666 | 20,029 | 17,837 | 5,656 | 13,144 |
| Purchase commitments ⁽⁷⁾ | 9,890 | 2,424 | 3,923 | 3,543 | — |
| Total | \$2,346,714 | \$236,140 | \$456,680 | \$430,686 | \$1,223,208 |

(1) In addition to the amounts discussed below, we also have a business management agreement ending on December 31, 2017, subject to extensions, which requires us to pay management fees to RMR LLC. See Note 15 to our Consolidated Financial Statements included in Part IV, Item 15 of this Annual Report on Form 10-K.

(2) Debt obligations consist of the amounts due under two Federal National Mortgage Association, or FNMA, mortgages, two Federal Home Loan Mortgage Corporation mortgages, and one mortgage from a commercial lender for two communities. Excludes unamortized net premiums and debt issuance costs of \$1.6 million.

(3) Projected interest on debt obligations is interest attributable to only the long term debt obligations listed above at existing rates and is not intended to estimate future interest costs which may result from debt prepayments, new debt issuances or change in interest rates.

(4) Operating lease obligations consist of the annual lease payments to SNH and HCP through the lease terms ending between 2024 and 2032. These amounts do not include percentage rent that may become payable under certain of these leases.

(5) Non refundable resident continuing care contracts. See Note 2 to our Consolidated Financial Statements included in Part IV, Item 15 of this Annual Report on Form 10 K for more information regarding these contracts.

(6) Accrued self insurance obligations reflected on our balance sheet are insurance reserves related to workers' compensation and professional and general liability insurance.

(7) Purchase commitments consist of information technology related support and hosting contracts we have with unrelated third party vendors.

Off Balance Sheet Arrangements

As of December 31, 2016, we have pledged certain of our assets, including accounts receivable, with a carrying value of \$15.5 million, related to our operation of 17 properties we lease from SNH to secure SNH's borrowings from its lender, FNMA. As of December 31, 2016, we had no other off balance sheet arrangements that have had or that we expect would be reasonably likely to have a future material effect on our financial condition, changes in financial condition, revenues or expenses, results of operations, liquidity, capital expenditures or capital resources.

Table of Contents

Debt Financings and Covenants

In February 2017, we replaced our then existing \$100.0 million secured revolving credit facility, which was scheduled to mature in April 2017, with our new \$100.0 million secured revolving credit facility, which is available for general business purposes, including acquisitions. The terms of our new credit facility are substantially similar to those of our prior credit facility. Our new credit facility matures in February 2020. Subject to our payment of extension fees and meeting other conditions, we have options to extend the stated maturity date of our new credit facility for two, one year periods. We pay interest on borrowings under our new credit facility at an annual rate of LIBOR plus a premium of 250 basis points. We also pay a quarterly commitment fee of 0.35% per annum on the unused part of our new credit facility. We can borrow, repay and re-borrow funds available under our new credit facility until maturity, and no principal repayment is due until maturity.

Certain of our subsidiaries guarantee our obligations under our new credit facility. Our new credit facility is secured by real estate mortgages on 10 senior living communities with a combined 1,219 living units owned by our guarantor subsidiaries and our guarantor subsidiaries' accounts receivable and related collateral. The amount of available borrowings under our new credit facility is subject to our having qualified collateral, which is primarily based on the value of the properties securing our obligations under our new credit facility. Accordingly, the availability of borrowings under our new credit facility at any time may be less than \$100.0 million.

Our new credit facility provides for acceleration of payment of all amounts outstanding upon the occurrence and continuation of certain events of default, including a change of control of us, as defined. Our new credit facility contains a number of financial and other covenants, including covenants that restrict our ability to incur indebtedness or to pay dividends or make other distributions under certain circumstances and require us to maintain financial ratios and a minimum net worth.

We previously had a \$25.0 million secured revolving line of credit that matured on March 18, 2016 that we did not extend or replace. We had no borrowings outstanding under this line of credit during the years ended December 31, 2016 or 2015.

We also have mortgage debt that we assumed in connection with our acquisitions of six of our senior living communities. Payments of principal and interest are due monthly under this mortgage debt until maturities at varying dates ranging from June 2018 to September 2032. The weighted average annual interest rate on this mortgage debt was 6.27% as of December 31, 2016.

As of December 31, 2016, we had no outstanding borrowings under our prior credit facility and \$60.4 million in aggregate principal amount of outstanding mortgage debt. As of December 31, 2016, we believe we were in compliance with all applicable covenants under our debt agreements, including under the agreement governing our prior credit facility.

Related Person Transactions

We have relationships and historical and continuing transactions with SNH, RMR LLC, ABP Trust and others related to them. For example: SNH is our former parent company, our largest landlord, the owner of the senior living communities that we manage and a significant stockholder of us; various services we require to operate our business are provided to us by RMR LLC pursuant to our business management agreement with RMR LLC and RMR LLC also provides management services to SNH; RMR LLC employs our President and Chief Executive Officer, our Chief Financial Officer and Treasurer and our Senior Vice President and General Counsel; subsidiaries of ABP Trust, which is owned by one of our Managing Directors, Barry Portnoy, and his son, Adam Portnoy, are our largest stockholder and the landlord for our headquarters; and ABP Trust is the controlling shareholder of RMR Inc., which is the managing member of RMR LLC. We also have relationships and historical and continuing transactions with other companies to which RMR LLC provides management services and which may have trustees, directors and officers who are also trustees, directors or officers of us, SNH, RMR LLC or RMR Inc., including: D&R Yonkers LLC, which is owned by our Chief Financial Officer and Treasurer and SNH's president and chief operating officer and to which we provide management services; and AIC, of which we, ABP Trust, SNH and four other companies to which RMR LLC provides management services each own 14.3% and which arranges and reinsures in part a combined property insurance program for us and its six other shareholders.

For further information about these and other such relationships and related person transactions, see Notes 9, 11, 15 and 16 to our Consolidated Financial Statements included in Part IV, Item 15 of this Annual Report on Form 10-K, which are incorporated herein by reference, our other filings with the SEC, and our definitive Proxy Statement for our 2017 Annual Meeting of Stockholders, or our definitive Proxy Statement, to be filed with the SEC within 120 days after the close of the fiscal year ended December 31, 2016. For further information about these transactions and relationships and about the risks that may arise as a result of these and other related person transactions and relationships, see elsewhere in this Annual Report on

Table of Contents

Form 10-K, including “Warning Concerning Forward Looking Statements”, Part I, Item 1, “Business” and Part I, Item 1A, “Risk Factors.” Our filings with the SEC and copies of certain of our agreements with these related persons, including our leases, forms of management agreements and related pooling agreements with SNH, our business management agreement with RMR LLC, our headquarters lease with a subsidiary of ABP Trust, our consent, standstill, registration rights and lock-up agreement with a subsidiary of ABP Trust, ABP Trust, Barry Portnoy and Adam Portnoy, our management agreement with D&R Yonkers LLC and our shareholders agreement with AIC and its six other shareholders, are available as exhibits to our public filings with the SEC and accessible at the SEC’s website, www.sec.gov. We may engage in additional transactions with related persons, including businesses to which RMR LLC or its affiliates provide management services.

Critical Accounting Policies

Our critical accounting policies concern revenue recognition, including contractual allowances, self insurance reserves, the allowance for doubtful accounts, goodwill, other intangibles and long lived assets and our judgments and estimates concerning our provisions for income taxes.

Our revenue recognition policies involve judgments about Medicare and Medicaid rate calculations. These judgments are based principally upon our experience with these programs and our knowledge of current rules and regulations applicable to these programs. We recognize revenues when services are provided, and these amounts are reported at their estimated net realizable amounts. Some Medicare and Medicaid revenues are subject to audit and retroactive adjustment and sometimes retroactive legislative changes.

Our policies for valuing accounts receivable, including the allowance for doubtful accounts, involve significant judgments based upon our experience, including consideration of the age of the receivables, the terms of the agreements with our residents, their third party payers or other obligors, the residents’ or payers’ stated intent to pay, the residents’ or payers’ financial capacity and other factors which may include litigation or rate and payment appeal proceedings. We periodically review and revise these estimates based on new information and these revisions may be material.

Determining reserves for Medicare repayment obligations and related costs including penalties, and the casualty, liability, workers’ compensation and healthcare losses and costs that we have incurred as of the end of a reporting period involves significant judgments based upon our experience and our expectations of future events, including projected settlements for pending claims, known incidents which we expect may result in claims, estimates of incurred but not yet reported claims, expected changes in premiums for insurance provided by insurers whose policies provide for retroactive adjustments, estimated litigation costs and other factors. Since these reserves are based on estimates, the actual expenses we incur may differ from the amount reserved. We regularly adjust these estimates to reflect changes in the foregoing factors, our actual claims experience, recommendations from our professional consultants, changes in market conditions and other factors; it is possible that such adjustments may be material.

We recorded an impairment charge in the year ended December 31, 2015 for the then full balance of our goodwill. We continue to not have any goodwill recorded on our consolidated balance sheet as of December 31, 2016. Historically, we evaluated the recoverability of goodwill annually in the fourth quarter of each fiscal year, or more frequently, if events or changes in circumstances indicated that goodwill might have been impaired. If our review indicated that the carrying amount of goodwill exceeded its fair value, we would reduce the carrying amount of goodwill to fair value. We evaluated goodwill for impairment at the reporting unit level, which we determined to be our operating segments, by comparing the fair value of the reporting unit as determined by its discounted cash flows and market approaches with its carrying value. The key assumptions used in the discounted cash flow analysis included future revenue growth, gross margins and our weighted average cost of capital. We selected a growth rate based on our view of the growth prospect of each of our reporting units. If the carrying value of the reporting unit exceeded its fair value, we compared the implied fair value of the reporting unit’s goodwill with its carrying amount to measure the amount of the potential impairment loss.

When we acquire a community, we estimate and record the fair value of purchased intangible assets primarily using discounted cash flow analyses of anticipated cash flows reflecting incremental revenues and/or cost savings resulting from the acquired intangible asset, reflecting market participant assumptions. Amortization of intangible assets with

finite lives is recognized over their estimated useful lives using a method of amortization that reflects the pattern in which the economic benefits of the intangible assets are consumed or otherwise realized. We regularly evaluate whether events or changes in circumstances have occurred that could indicate impairment in the value of our other intangible assets. If there is an indication that the carrying value of an asset is not recoverable, we determine the amount of impairment loss, if any, by comparing the historical carrying value of the asset to its estimated fair value. We determine estimated fair value through an evaluation of recent financial performance, recent transactions for similar assets, market conditions and projected cash flows using standard

Table of Contents

industry valuation techniques. This process requires that estimates be made, and, if we misjudge or estimate incorrectly, this could have a material effect on our financial statements.

Our income tax expense, deferred tax assets and liabilities, and liabilities for unrecognized tax benefits reflect our assessment of estimated current and future taxes to be paid. We are subject to income taxes in the United States. Significant judgments and estimates are required in determining our income tax expense.

Deferred income taxes arise from temporary differences between the tax basis of assets and liabilities and their reported amounts in the financial statements, which will result in taxable or deductible amounts in the future. In evaluating our ability to recover our deferred tax assets, we consider all available positive and negative evidence, including scheduled reversals of deferred tax liabilities, projected future taxable income, tax-planning strategies, and results of recent operations. In projecting future taxable income, we begin with historical results adjusted for the results of discontinued operations and incorporate assumptions about the amount of future state and federal pretax operating income adjusted for items that do not have tax consequences. The assumptions about future taxable income require significant judgment and are consistent with the plans and estimates we use to manage the underlying business. In evaluating the objective evidence that historical results provide, we consider three years of cumulative operating income or loss.

As of December 31, 2014, we established a valuation allowance against our deferred tax assets. The decision to establish the valuation allowance was due to our assessment of the available positive and negative evidence to estimate if sufficient future taxable income will be generated to realize the existing deferred tax assets. An important aspect of objective negative evidence evaluated was the significant losses incurred over the two year period ending December 31, 2014 and, as a result of those losses, we expected to be, and it turned out were, in a cumulative loss position for the three year period ending December 31, 2015. This objective negative evidence is difficult to overcome and would require a substantial amount of objectively verifiable positive evidence of future income to support the realizability of our deferred tax assets. For these reasons, we concluded that a full valuation allowance is required and have maintained a full valuation allowance as of December 31, 2016.

Some of our judgments and estimates are based upon published industry statistics and in some cases third party professionals. Any misjudgments or incorrect estimates affecting our critical accounting policies could have a material effect on our financial statements.

In the future we may need to revise the judgments, estimates and assessments we use to formulate our critical accounting policies to incorporate information which is not now known. We cannot predict the effect changes to the premises underlying our critical accounting policies may have on our future results of operations, although such changes could be material and adverse.

Impact of Inflation and Deflation

Inflation in the past several years in the United States has been modest, but recently there have been indications of inflation in the U.S. economy and elsewhere and some market forecasts indicate an expectation of increased inflation in the near to intermediate term. Future inflation might have both positive and negative impacts on our business. Rising price levels might allow us to increase our charges to residents, but might cause our operating costs, including our percentage rent, to increase. Also, our ability to realize rate increases paid by Medicare and Medicaid programs might be limited despite inflation.

Deflation would likely have a negative impact upon us. A large component of our expenses consists of our fixed minimum rental obligations. Accordingly, we believe that a general decline in price levels which could cause our charges to residents to decline would likely not be fully offset by a decline in our expenses.

Seasonality

Our senior living business is subject to modest effects of seasonality. During the calendar fourth quarter holiday periods, residents at such facilities are sometimes discharged to spend time with family and admission decisions are often deferred. The first quarter of each calendar year usually coincides with increased illness among residents which can result in increased costs or discharges to hospitals. As a result of these and other factors, these operations sometimes produce greater earnings in the second and third quarters of a calendar year and lesser earnings in the

fourth and first calendar quarters. We do not expect these seasonal differences to cause fluctuations in our revenues or operating cash flows to such an extent that we will have difficulty paying our expenses, including rent, which do not fluctuate seasonally.

Table of Contents

Impact of Climate Change

The political debate about global climate change has resulted in various treaties, laws and regulations which are intended to limit carbon emissions. We believe these laws being enacted or proposed may cause energy costs at our communities to increase in the future. In the long term, we believe any such increased costs will be passed through and paid by our residents and other customers in higher charges for our services. However, in the short term, these increased costs, if material in amount, could materially and adversely affect our financial condition and results of operations.

Some observers believe severe weather activities in different parts of the country over the last few years is evidence of global climate change. Such severe weather that may result from climate change may have an adverse effect on individual properties we own or lease. We mitigate these risks by owning and leasing a geographically diversified portfolio of properties and by procuring insurance coverage we believe adequate to protect us from material damages and losses from such activities. However, we cannot be sure that our mitigation efforts will be sufficient or that storms that may occur due to future climate change or otherwise could not have a material adverse effect on our business.

Item 7A. Quantitative and Qualitative Disclosures About Market Risk

We are exposed to risks associated with market changes in interest rates. We manage our exposure to this market risk by monitoring available financing alternatives. Other than as described below, we do not currently foresee any significant changes in our exposure to fluctuations in interest rates or in how we manage this exposure in the near future.

At December 31, 2016, our outstanding fixed rate debt consisted of the following (dollars in thousands):

| Debt | Principal Balance ⁽¹⁾ | Annual Interest Rate ⁽¹⁾ | Annual Interest Expense ⁽¹⁾ | Maturity | Interest Payments Due |
|----------|----------------------------------|-------------------------------------|--|----------|-----------------------|
| Mortgage | \$ 13,305 | 6.47 % | \$ 861 | 2018 | Monthly |
| Mortgage | 17,141 | 6.64 % | 1,138 | 2023 | Monthly |
| Mortgage | 17,010 | 5.75 % | 978 | 2022 | Monthly |
| Mortgage | 2,524 | 6.36 % | 161 | 2028 | Monthly |
| Mortgage | 8,816 | 6.20 % | 547 | 2032 | Monthly |
| | \$ 58,796 | | \$ 3,685 | | |

(1) The principal balances, annual interest rates and annual interest expense are, or are determined based upon, the amounts stated in the applicable contracts. In accordance with generally accepted accounting principles in the United States, our carrying values and recorded interest expense may differ from these amounts because of market conditions at the time we assumed certain of these debts.

Our mortgages require principal and interest payments through maturity pursuant to amortization schedules.

Because these debts require interest to be paid at a fixed rate, changes in market interest rates during the term of these debts will not affect our interest obligations. If these debts were refinanced at interest rates which are 100 basis points higher or lower than shown above, our annual interest costs would increase or decrease by approximately \$0.6 million.

Changes in market interest rates would affect the fair value of our fixed rate debt obligations; increases in market interest rates decrease the fair value of our fixed rate debt, while decreases in market interest rates increase the fair value of our fixed rate debt. Based on the balances outstanding at December 31, 2016, and discounted cash flow analyses through the respective maturity dates, and assuming no other changes in factors that may affect the fair value of our fixed rate debt obligations, a hypothetical immediate 100 basis point change in interest rates would increase or decrease the fair value of those obligations by approximately \$2.7 million and \$2.5 million, respectively.

Our mortgages generally contain provisions that allow us to make repayments earlier than the stated maturity date. In some cases, we are not allowed to make early repayment prior to a cutoff date. Where prepayment is permitted, we are generally allowed to make prepayments only at a premium which is often designed to preserve a stated yield to the

note holder. These prepayment rights may afford us opportunities to mitigate the risk of refinancing our debts at maturity at higher rates by refinancing prior to maturity.

At December 31, 2016, we had no floating rate debt as we had no amounts outstanding under our prior credit facility. In February 2017, we replaced our then existing \$100.0 million secured revolving credit facility, which was scheduled to mature in April 2017, with our new \$100.0 million secured revolving credit facility. The terms of our new credit facility are substantially similar to those of our prior credit facility. Our new credit facility matures in February 2020. Subject to our

Table of Contents

payment of extension fees and meeting other conditions, we have options to extend the stated maturity date of our new credit facility for two, one year periods. We can borrow, repay and re-borrow funds available under our new credit facility until maturity, and no principal repayment is due until maturity.

Borrowings under our new credit facility are in U.S. dollars and interest is required to be paid at LIBOR plus a premium of 250 basis points. Accordingly, we are vulnerable to changes in U.S. dollar based short term interest rates, specifically LIBOR. In addition, upon renewal or refinancing of our new credit facility, we are vulnerable to increases in interest rate premiums due to market conditions or our perceived credit risk. Generally, a change in interest rates would not affect the value of debt outstanding under our new credit facility but would affect our operating results. The following table presents the impact a 100 basis point increase in interest rates would have on our annual floating rate interest expense as of December 31, 2016 if we were fully drawn on our then existing prior credit facility (dollars in thousands):

| | Impact of Increase in Interest Rates | | | |
|--------------------------|--------------------------------------|-----------|-----------------------|---------|
| | Weighted | Total | Annual | |
| | Average | Interest | Per | |
| | Interest | Expense | Common | |
| | Rate | Per | Share | |
| | Per Year | Year | Impact ⁽²⁾ | |
| At December 31, 2016 | 3.22 % | \$ 85,332 | \$ 2,748 | \$ 0.06 |
| 100 basis point increase | 4.22 % | \$ 85,332 | \$ 3,601 | \$ 0.07 |

(1) Amount available to borrow on our prior credit facility as of December 31, 2016.

(2) Based on the diluted weighted average shares outstanding for the year ended December 31, 2016.

The foregoing table shows the impact at December 31, 2016 of an immediate increase in interest rates on our prior credit facility. If interest rates were to change gradually over time, the impact would be spread over time. Our exposure to fluctuations in interest rates may increase or decrease in the future with increases or decreases in the outstanding amount under our new credit facility.

Although we have no current plans to do so, we may in the future enter into hedge arrangements from time to time to mitigate our exposure to changes in interest rates.

Item 8. Financial Statements and Supplementary Data

The information required by this Item is included in Part IV, Item 15 of this Annual Report on Form 10 K.

Item 9. Changes in and Disagreements With Accountants on Accounting and Financial Disclosure

None.

Item 9A. Controls and Procedures

As of the end of the period covered by this report, our management carried out an evaluation, under the supervision and with the participation of our President and Chief Executive Officer and our Chief Financial Officer and Treasurer, of the effectiveness of our disclosure controls and procedures pursuant to Rules 13a-15 and 15d-15 under the Exchange Act. Based upon that evaluation, our management, including our President and Chief Executive Officer and our Chief Financial Officer and Treasurer, concluded that our disclosure controls and procedures are effective.

There have been no changes in our internal control over financial reporting during the quarter ended December 31, 2016 that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

Management Report on Assessment of Internal Control Over Financial Reporting

We are responsible for establishing and maintaining adequate internal control over financial reporting. Our internal control system is designed to provide reasonable assurance to our management and Board of Directors regarding the preparation and fair presentation of published financial statements. All internal control systems, no matter how well

designed, have inherent limitations. Therefore, even those systems determined to be effective can provide only reasonable assurance with respect to financial statement preparation and presentation.

Table of Contents

Our management assessed the effectiveness of our internal control over financial reporting as of December 31, 2016. In making this assessment, it used the criteria set forth by the Committee of Sponsoring Organizations of the Treadway Commission in Internal Control-Integrated Framework (2013 framework). Based on this assessment, we believe that, as of December 31, 2016, our internal control over financial reporting is effective.

RSM US LLP, the independent registered public accounting firm that audited the consolidated financial statements included in this Annual Report on Form 10 K, has issued an attestation report on our internal control over financial reporting. The report appears elsewhere herein.

Item 9B. Other Information

Our Board of Directors approved a change of our name from “Five Star Quality Care, Inc.” to “Five Star Senior Living Inc.” on March 2, 2017, and we filed an amendment to our charter with the State Department of Assessments and Taxation of Maryland on that date in order to effect the name change, which amendment was effective at 12:01 AM on March 3, 2017. Concurrently with the amendment to our charter, we also amended our bylaws to reflect the name change.

The foregoing descriptions of the amendments to our charter and bylaws are not complete and are subject to and qualified in their entirety by reference to the full text of the copy of the amendment, a composite copy of our charter, including all amendments to date, and a copy of our amended and restated bylaws, which are attached hereto as Exhibits 3.1, 3.2 and 3.6, respectively, each of which is incorporated herein by reference. In addition, marked versions of the composite copy of our charter and our amended and restated bylaws indicating changes made to these documents, as they existed immediately prior to the adoption of these amendments, are attached as Exhibit 3.3 and Exhibit 3.7, respectively.

Table of Contents

PART III

Item 10. Directors, Executive Officers and Corporate Governance

We have a Code of Business Conduct and Ethics that applies to all our representatives, including our officers, Directors and employees and employees of RMR LLC. Our Code of Business Conduct and Ethics is posted on our website, www.fivestarseniorliving.com. A printed copy of our Code of Business Conduct and Ethics is also available free of charge to any person who requests a copy by writing to our Secretary, Five Star Senior Living Inc., Two Newton Place, 255 Washington Street, Newton, MA 02458. We intend to disclose any amendments or waivers to our Code of Business Conduct and Ethics applicable to our principal executive officer, principal financial officer, principal accounting officer or controller (or any person performing similar functions) on our website.

The remainder of the information required by Item 10 is incorporated by reference to our definitive Proxy Statement.

Item 11. Executive Compensation

The information required by Item 11 is incorporated by reference to our definitive Proxy Statement.

Item 12. Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters

Equity Compensation Plan Information

We may grant common shares to our officers and employees and to employees of RMR LLC under our 2014 Equity Compensation Plan, or the 2014 Plan. In addition, each of our Directors receives common shares as part of his or her annual compensation for serving as a Director and such shares are awarded under the 2014 Plan. The terms of awards made under the 2014 Plan are determined by the Compensation Committee of our Board of Directors at the time of the award. The following table is as of December 31, 2016:

| | Number of securities to be issued upon exercise of outstanding options, warrants and rights (a) | Weighted average exercise price of outstanding options, warrants and rights (b) | Number of securities remaining available for future issuance under equity compensation plans (excluding securities reflected in column (a)) (c) |
|--|--|--|--|
| Equity compensation plans approved by security holders—2014 Plan | None | None | 3,458,920 ⁽¹⁾ |
| Equity compensation plans not approved by security holders | None | None | None |
| Total | None | None | 3,458,920 ⁽¹⁾ |

(1) Consists of common shares available for issuance pursuant to the terms of the 2014 Plan. Share awards that are forfeited will be added to the common shares available for issuance under the 2014 Plan.

Payments by us to RMR LLC and RMR LLC employees are described in Notes 15 and 16 to our Consolidated Financial Statements included in Part IV, Item 15 of this Annual Report on Form 10 K. The remainder of the information required by Item 12 is incorporated by reference to our definitive Proxy Statement.

Item 13. Certain Relationships and Related Transactions, and Director Independence

The information required by Item 13 is incorporated by reference to our definitive Proxy Statement.

Item 14. Principal Accountant Fees and Services

The information required by Item 14 is incorporated by reference to our definitive Proxy Statement.

Table of Contents

PART IV

Item 15. Exhibits and Financial Statement Schedules

(a) Index to Financial Statements

| | Page |
|---|-----------|
| Consolidated Financial Statements of Five Star Senior Living Inc. | |
| <u>Reports of Independent Registered Public Accounting Firm</u> | F_1 / F_2 |
| <u>Consolidated Balance Sheets at December 31, 2016 and 2015</u> | F_3 |
| <u>Consolidated Statements of Operations for the years ended December 31, 2016, 2015 and 2014</u> | F_4 |
| <u>Consolidated Statements of Comprehensive Loss for the years ended December 31, 2016, 2015 and 2014</u> | F_5 |
| <u>Consolidated Statements of Shareholders' Equity for the years ended December 31, 2016, 2015 and 2014</u> | F_6 |
| <u>Consolidated Statements of Cash Flows for the years ended December 31, 2016, 2015 and 2014</u> | F_7 |
| <u>Notes to Consolidated Financial Statements</u> | F_8 |

All other schedules for which provision is made in the applicable accounting regulations of the SEC are not required under the related instructions, or are inapplicable, and therefore have been omitted.

(b) Exhibits

| Exhibit Number | Description |
|-------------------|---|
| 3.1 | Articles of Amendment, dated March 2, 2017. (Filed herewith.) |
| 3.2 | Composite Copy of Articles of Amendment and Restatement, dated December 5, 2001, as amended to date. (Filed herewith.) |
| 3.3 | Composite Copy of Articles of Amendment and Restatement, dated December 5, 2001, as amended to date (marked copy). (Filed herewith.) |
| 3.4 | Articles Supplementary, as corrected by Certificate of Correction, dated March 19, 2004. (Incorporated by reference to the Company's registration statement on Form 8 A dated March 19, 2004 and the Company's Quarterly Report on Form 10-Q for the quarter ended March 31, 2004, respectively, File No. 001-16817.) |
| 3.5 | Articles Supplementary, dated April 16, 2014. (Incorporated by reference to the Company's Current Report on Form 8 K dated April 16, 2014.) |
| 3.6 | Amended and Restated Bylaws of the Company, adopted March 2, 2017. (Filed herewith.) |
| 3.7 | Amended and Restated Bylaws of the Company, adopted March 2, 2017 (marked copy). (Filed herewith.) |
| 4.1 | Form of Common Stock Certificate. (Filed herewith.) |
| 10.1 | 2001 Stock Option and Stock Incentive Plan of the Company, as amended.(+) (Incorporated by reference to the Company's Current Report on Form 8 K dated May 25, 2006, File No. 001 16817.) |
| 10.2 | Form of Restricted Share Agreement.(+) (Incorporated by reference to the Company's Quarterly Report on Form 10 Q for the quarter ended September 30, 2013.) |
| 10.3 | Five Star Senior Living Inc. (f/k/a Five Star Quality Care, Inc.) 2014 Equity Compensation Plan.(+) (Incorporated by reference to the Company's Current Report on Form 8-K dated September 30, 2014.) |
| 10.4 | Form of Restricted Share Agreement.(+) (Incorporated by reference to the Company's Quarterly Report on Form 10-Q for the quarter ended March 31, 2014.) |
| 10.5 | Form of Share Award Agreement.(+) (Filed herewith.) |
| 10.6 | Representative form of Indemnification Agreement.(+) (Incorporated by reference to the Company's Annual Report on Form 10-K for the year ended December 31, 2015.) |
| 10.7 | Summary of Director Compensation.(+) (Incorporated by reference to the Company's Current Report on Form 8-K dated May 23, 2016.) |
| 10.8 | Amended and Restated Credit Agreement, dated as of February 24, 2017, among the Company, the Guarantors party thereto, Citibank, N.A. and the other parties thereto. (Incorporated by reference to the Company's Current Report on Form 8-K dated February 24, 2017.) |

Table of Contents

- Transaction Agreement, dated December 7, 2001, among Senior Housing Properties Trust, certain subsidiaries of Senior Housing Properties Trust, the Company, certain subsidiaries of the Company, FSQ, Inc., Hospitality Properties Trust, Equity Commonwealth (f/k/a HRPT Properties Trust) and The RMR Group LLC (f/k/a Reit Management & Research LLC). (Incorporated by reference to Senior Housing Properties Trust's Current Report on Form 8 K dated December 13, 2001, File No. 001 15319.)
- 10.9
- Transaction Agreement, dated June 29, 2016, between the Company and Senior Housing Properties Trust. (Incorporated by reference to the Company's Current Report on Form 8-K dated June 29, 2016.)
- 10.10
- Purchase and Sale Agreement, dated June 29, 2016, among Senior Housing Properties Trust, as Purchaser, and certain subsidiaries of the Company, as Seller. (Incorporated by reference to the Company's Current Report on Form 8-K dated June 29, 2016.)
- 10.11
- Amended and Restated Master Lease Agreement (Lease No. 1), dated as of August 4, 2009, among certain subsidiaries of Senior Housing Properties Trust, as Landlord, and Five Star Quality Care Trust, as Tenant. (Incorporated by reference to the Company's Quarterly Report on Form 10 Q for the quarter ended June 30, 2009, File No. 001-16817.)
- 10.12
- Partial Termination of and First Amendment to Amended and Restated Master Lease Agreement (Lease No. 1), dated as of October 1, 2009, among certain subsidiaries of Senior Housing Properties Trust, as Landlord, and Five Star Quality Care Trust, as Tenant. (Incorporated by reference to the Company's Quarterly Report on Form 10 Q for the quarter ended September 30, 2009, File No. 001-16817.)
- 10.13
- Second Amendment to Amended and Restated Master Lease Agreement (Lease No. 1), dated as of November 17, 2009, among certain subsidiaries of Senior Housing Properties Trust, as Landlord, and Five Star Quality Care Trust, as Tenant. (Incorporated by reference to the Company's Annual Report on Form 10 K for the year ended December 31, 2009, File No. 001-16817.)
- 10.14
- Third Amendment to Amended and Restated Master Lease Agreement (Lease No. 1), dated as of December 10, 2009, among certain subsidiaries of Senior Housing Properties Trust, as Landlord, and Five Star Quality Care Trust, as Tenant. (Incorporated by reference to the Company's Annual Report on Form 10 K for the year ended December 31, 2009, File No. 001-16817.)
- 10.15
- Partial Termination of and Fourth Amendment to Amended and Restated Master Lease Agreement (Lease No. 1), dated as of August 1, 2010, among certain subsidiaries of Senior Housing Properties Trust, as Landlord, and Five Star Quality Care Trust, as Tenant. (Incorporated by reference to the Company's Quarterly Report on Form 10 Q for the quarter ended September 30, 2010, File No. 001-16817.)
- 10.16
- Fifth Amendment to Amended and Restated Master Lease Agreement (Lease No. 1), dated as of May 1, 2011, among certain subsidiaries of Senior Housing Properties Trust, as Landlord, and Five Star Quality Care Trust, as Tenant. (Incorporated by reference to the Company's Current Report on Form 8 K dated June 8, 2011, File No. 001-16817.)
- 10.17
- Partial Termination of and Sixth Amendment to Amended and Restated Master Lease Agreement (Lease No. 1), dated as of June 1, 2011, among certain subsidiaries of Senior Housing Properties Trust, as Landlord, and Five Star Quality Care Trust, as Tenant. (Incorporated by reference to the Company's Current Report on Form 8 K dated June 8, 2011, File No. 001-16817.)
- 10.18
- Seventh Amendment to Amended and Restated Master Lease Agreement (Lease No. 1), dated as of June 20, 2011, among certain subsidiaries of Senior Housing Properties Trust, as Landlord, and Five Star Quality Care Trust, as Tenant. (Incorporated by reference to the Company's Quarterly Report on Form 10 Q for the quarter ended June 30, 2011, File No. 001-16817.)
- 10.19
- Eighth Amendment to Amended and Restated Master Lease Agreement (Lease No. 1), dated as of August 31, 2012, among certain subsidiaries of Senior Housing Properties Trust, as Landlord, and Five Star Quality Care Trust, as Tenant. (Incorporated by reference to the Company's Quarterly Report on Form 10 Q for the quarter ended September 30, 2012.)
- 10.20
- Partial Termination of and Ninth Amendment to Amended and Restated Master Lease Agreement (Lease No. 1), dated as of August 1, 2013, among certain subsidiaries of Senior Housing Properties Trust, as Landlord, and Five Star Quality Care Trust, as Tenant. (Incorporated by reference to the Company's Quarterly Report on
- 10.21

Form 10 Q for the quarter ended September 30, 2013.)

10.22 Partial Termination of and Tenth Amendment to Amended and Restated Master Lease Agreement (Lease No. 1), dated as of January 22, 2014, among certain subsidiaries of Senior Housing Properties Trust, as Landlord, and Five Star Quality Care Trust, as Tenant. (Incorporated by reference to the Company's Quarterly Report on Form 10 Q for the quarter ended September 30, 2013.)

10.23 Partial Termination of and Eleventh Amendment to Amended and Restated Master Lease Agreement (Lease No. 1), dated as of October 1, 2014, among certain subsidiaries of Senior Housing Properties Trust, as Landlord, and the Company, as Tenant. (Incorporated by reference to the Company's Quarterly Report on Form 10-Q for the quarter ended March 31, 2014.)

10.24 Partial Termination of and Twelfth Amendment to Amended and Restated Master Lease Agreement (Lease No. 1), dated as of October 31, 2014, among certain subsidiaries of Senior Housing Properties Trust, as Landlord, and the Company, as Tenant. (Incorporated by reference to the Company's Annual Report on Form 10-K for the year ended December 31, 2014.)

Table of Contents

- 10.25 Partial Termination of and Thirteenth Amendment to Amended and Restated Master Lease Agreement (Lease No. 1), dated as of February 17, 2015, among certain subsidiaries of Senior Housing Properties Trust, as Landlord, and the Company, as Tenant. (Incorporated by reference to the Company's Annual Report on Form 10-K for the year ended December 31, 2014.)
- 10.26 Partial Termination of and Fourteenth Amendment to Amended and Restated Master Lease Agreement (Lease No. 1), dated as of August 4, 2015, among certain subsidiaries of Senior Housing Properties Trust, as Landlord, and the Company, as Tenant. (Incorporated by reference to the Company's Quarterly Report on Form 10-Q for the quarter ended September 30, 2015.)
- 10.27 Partial Termination of and Fifteenth Amendment to Amended and Restated Master Lease Agreement (Lease No. 1), dated as of December 29, 2015, among certain subsidiaries of Senior Housing Properties Trust, as Landlord, and the Company, as Tenant. (Incorporated by reference to the Company's Annual Report on Form 10-K for the year ended December 31, 2015.)
- 10.28 Amended and Restated Guaranty Agreement (Lease No. 1), dated as of August 4, 2009, made by the Company, as Guarantor, for the benefit of certain subsidiaries of Senior Housing Properties Trust, relating to the Amended and Restated Master Lease Agreement (Lease No. 1), dated as of August 4, 2009, among certain subsidiaries of Senior Housing Properties Trust, as Landlord, and Five Star Quality Care Trust, as Tenant. (Incorporated by reference to the Company's Quarterly Report on Form 10 Q for the quarter ended June 30, 2009, File No. 001-16817.)
- 10.29 Amended and Restated Master Lease Agreement (Lease No. 2), dated as of August 4, 2009, among certain subsidiaries of Senior Housing Properties Trust, as Landlord, and certain subsidiaries of the Company, as Tenant. (Incorporated by reference to the Company's Quarterly Report on Form 10 Q for the quarter ended June 30, 2009, File No. 001-16817.)
- 10.30 Partial Termination of and First Amendment to Amended and Restated Master Lease Agreement (Lease No. 2), dated as of November 1, 2009, among certain subsidiaries of Senior Housing Properties Trust, as Landlord, and certain subsidiaries of the Company, as Tenant. (Incorporated by reference to the Company's Annual Report on Form 10 K for the year ended December 31, 2009, File No. 001-16817.)
- 10.31 Partial Termination of and Second Amendment to Amended and Restated Master Lease Agreement (Lease No. 2), dated as of August 1, 2010, among certain subsidiaries of Senior Housing Properties Trust, as Landlord, and certain subsidiaries of the Company, as Tenant. (Incorporated by reference to the Company's Quarterly Report on Form 10 Q for the quarter ended September 30, 2010, File No. 001-16817.)
- 10.32 Third Amendment to Amended and Restated Master Lease Agreement (Lease No. 2), dated as of June 20, 2011, among certain subsidiaries of Senior Housing Properties Trust, as Landlord, and certain subsidiaries of the Company, as Tenant. (Incorporated by reference to the Company's Quarterly Report on Form 10 Q for the quarter ended June 30, 2011, File No. 001-16817.)
- 10.33 Fourth Amendment to Amended and Restated Master Lease Agreement (Lease No. 2), dated as of July 22, 2011, among certain subsidiaries of Senior Housing Properties Trust, as Landlord, and certain subsidiaries of the Company, as Tenant. (Incorporated by reference to the Company's Quarterly Report on Form 10 Q for the quarter ended June 30, 2011, File No. 001-16817.)
- 10.34 Fifth Amendment to Amended and Restated Master Lease Agreement (Lease No. 2), dated as of August 31, 2012, among certain subsidiaries of Senior Housing Properties Trust, as Landlord, and certain subsidiaries of the Company, as Tenant. (Incorporated by reference to the Company's Quarterly Report on Form 10 Q for the quarter ended September 30, 2012.)
- 10.35 Partial Termination of and Sixth Amendment to Amended and Restated Master Lease Agreement (Lease No. 2), dated as of September 19, 2013, among certain subsidiaries of Senior Housing Properties Trust, as Landlord, and certain subsidiaries of the Company, as Tenant. (Incorporated by reference to the Company's Current Report on Form 8 K dated September 19, 2013.)
- 10.36 Partial Termination of and Seventh Amendment to Amended and Restated Master Lease Agreement (Lease No. 2), dated as of June 1, 2014, among certain subsidiaries of Senior Housing Properties Trust, as Landlord, and certain subsidiaries of the Company, as Tenant. (Incorporated by reference to the Company's Annual Report

on Form 10-K for the year ended December 31, 2013.)

10.37 Partial Termination of and Eighth Amendment to Amended and Restated Master Lease Agreement (Lease No. 2), dated as of July 20, 2015, among certain subsidiaries of Senior Housing Properties Trust, as Landlord, and certain subsidiaries of the Company, as Tenant. (Incorporated by reference to the Company's Quarterly Report on Form 10-Q for the quarter ended June 30, 2015.)

10.38 Partial Termination of and Ninth Amendment to Amended and Restated Master Lease Agreement (Lease No. 2), dated as of September 29, 2016, among certain subsidiaries of Senior Housing Properties Trust, as Landlord, and certain subsidiaries of the Company, as Tenant. (Incorporated by reference to the Company's Quarterly Report on Form 10-Q for the quarter ended September 30, 2016.)

Table of Contents

- 10.39 Amended and Restated Guaranty Agreement (Lease No. 2), dated as of August 4, 2009, made by the Company, as Guarantor, for the benefit of certain subsidiaries of Senior Housing Properties Trust, relating to the Amended and Restated Master Lease Agreement (Lease No. 2), dated as of August 4, 2009, among certain subsidiaries of Senior Housing Properties Trust, as Landlord, and certain subsidiaries of the Company, as Tenant. (Incorporated by reference to the Company's Quarterly Report on Form 10 Q for the quarter ended June 30, 2009, File No.001-16817.)
- 10.40 Amended and Restated Master Lease Agreement (Lease No. 4), dated as of August 4, 2009, among certain subsidiaries of Senior Housing Properties Trust, as Landlord, and certain subsidiaries of the Company, as Tenant. (Incorporated by reference to the Company's Quarterly Report on Form 10 Q for the quarter ended June 30, 2009, File No. 001-16817.)
- 10.41 First Amendment to Amended and Restated Master Lease Agreement (Lease No. 4), dated as of October 1, 2009, among certain subsidiaries of Senior Housing Properties Trust, as Landlord, and certain subsidiaries of the Company, as Tenant. (Incorporated by reference to the Company's Annual Report on Form 10 K for the year ended December 31, 2009, File No. 001-16817.)
- 10.42 Partial Termination of and Second Amendment to Amended and Restated Master Lease Agreement (Lease No. 4), dated as of May 1, 2011, among certain subsidiaries of Senior Housing Properties Trust, as Landlord, and certain subsidiaries of the Company, as Tenant. (Incorporated by reference to the Company's Current Report on Form 8 K dated June 8, 2011, File No. 001-16817.)
- 10.43 Third Amendment to Amended and Restated Master Lease Agreement (Lease No. 4), dated as of June 20, 2011, among certain subsidiaries of Senior Housing Properties Trust, as Landlord, and certain subsidiaries of the Company, as Tenant. (Incorporated by reference to the Company's Quarterly Report on Form 10 Q for the quarter ended June 30, 2011, File No. 001-16817.)
- 10.44 Fourth Amendment to Amended and Restated Master Lease Agreement (Lease No. 4), dated as of August 31, 2012, among certain subsidiaries of Senior Housing Properties Trust, as Landlord, and certain subsidiaries of the Company, as Tenant. (Incorporated by reference to the Company's Quarterly Report on Form 10 Q for the quarter ended September 30, 2012.)
- 10.45 Fifth Amendment to Amended and Restated Master Lease Agreement (Lease No. 4), dated July 10, 2014, among certain subsidiaries of Senior Housing Properties Trust, as Landlord, and certain subsidiaries of the Company, as Tenant. (Incorporated by reference to the Company's Current Report on Form 8 K dated July 10, 2014.)
- 10.46 Amended and Restated Guaranty Agreement (Lease No. 4), dated as of August 4, 2009, made by the Company, as Guarantor, for the benefit of certain subsidiaries of Senior Housing Properties Trust, relating to the Amended and Restated Master Lease Agreement (Lease No. 4), dated as of August 4, 2009, among certain subsidiaries of Senior Housing Properties Trust, as Landlord, and certain subsidiaries of the Company, as Tenant. (Incorporated by reference to the Company's Quarterly Report on Form 10 Q for the quarter ended June 30, 2009, File No. 001-16817.)
- 10.47 Master Lease Agreement (Lease No. 5), dated as of June 29, 2016, between SNH/LTA Properties Trust, as Landlord, and Five Star Quality Care Trust, as Tenant. (Incorporated by reference to the Company's Current Report on Form 8-K dated June 29, 2016.)
- 10.48 Joinder and First Amendment to Master Lease Agreement (Lease No. 5), dated as of December 8, 2016, by and between SNH/LTA Properties Trust and SNH/LTA Properties GA LLC, as Landlord, and Five Star Quality Care Trust, as Tenant. (Filed herewith.)
- 10.49 Guaranty Agreement (Lease No. 5), dated as of June 29, 2016, made by the Company, as Guarantor, for the benefit of SNH/LTA Properties Trust, relating to Master Lease Agreement (Lease No. 5), dated as of June 29, 2016, between SNH/LTA Properties Trust, as Landlord, and Five Star Quality Care Trust, as Tenant. (Incorporated by reference to the Company's Current Report on Form 8-K dated June 29, 2016.)
- 10.50 Amended and Restated Master Lease Agreement, dated as of August 4, 2009, among SNH FM Financing LLC, SNH FM Financing Trust and Ellicott City Land I, LLC, as Landlord, and FVE FM Financing, Inc., as Tenant. (Incorporated by reference to the Company's Quarterly Report on Form 10 Q for the quarter ended June 30,

2009, File No.001-16817.)

10.51 Amendment No. 1 to Amended and Restated Master Lease Agreement, dated as of August 4, 2009, among SNH FM Financing LLC, SNH FM Financing Trust and Ellicott City Land I, LLC, as Landlord, and FVE FM Financing, Inc., as Tenant. (Incorporated by reference to the Company's Quarterly Report on Form 10 Q for the quarter ended June 30, 2009, File No. 001-16817.)

10.52 Partial Termination of and Amendment No. 2 to Amended and Restated Master Lease Agreement, dated as of August 31, 2012, among SNH FM Financing LLC, SNH FM Financing Trust and Ellicott City Land I, LLC, as Landlord, and FVE FM Financing, Inc., as Tenant. (Incorporated by reference to the Company's Quarterly Report on Form 10 Q for the quarter ended September 30, 2012.)

61

Table of Contents

- 10.53 Amended and Restated Guaranty Agreement, dated as of August 4, 2009, made by the Company, as Guarantor, for the benefit of SNH FM Financing LLC, SNH FM Financing Trust and Ellicott City Land I, LLC, relating to the Amended and Restated Master Lease Agreement, dated as of August 4, 2009, among SNH FM Financing LLC, SNH FM Financing Trust and Ellicott City Land I, LLC, as Landlord, and FVE FM Financing, Inc., as Tenant. (Incorporated by reference to the Company's Quarterly Report on Form 10 Q for the quarter ended June 30, 2009, File No. 001-16817.)
- 10.54 Representative form of Subordination, Assignment and Security Agreement. (Incorporated by reference to the Company's Quarterly Report on Form 10 Q for the quarter ended June 30, 2009, File No. 001-16817.)
- 10.55 Lease Realignment Agreement, dated as of August 4, 2009, among Senior Housing Properties Trust and certain of its subsidiaries and the Company and certain of its subsidiaries. (Incorporated by reference to the Company's Quarterly Report on Form 10 Q for the quarter ended June 30, 2009, File No. 001-16817.)
- 10.56 Registration Rights Agreement, dated as of August 4, 2009, between the Company and Senior Housing Properties Trust. (Incorporated by reference to the Company's Quarterly Report on Form 10 Q for the quarter ended June 30, 2009, File No. 001-16817.)
- 10.57 Consent, Standstill, Registration Rights and Lock-Up Agreement, dated October 2, 2016, among the Company, ABP Trust, ABP Acquisition LLC, Barry M. Portnoy and Adam D. Portnoy. (Incorporated by reference to the Company's Current Report on Form 8-K dated October 2, 2016.)
- 10.58 Amended and Restated Shareholders Agreement, dated May 21, 2012, among Affiliates Insurance Company, the Company, Hospitality Properties Trust, Senior Housing Properties Trust, TravelCenters of America LLC, ABP Trust (f/k/a Reit Management & Research Trust), Government Properties Income Trust and Select Income REIT. (Incorporated by reference to the Company's Quarterly Report on Form 10 Q for the quarter ended June 30, 2012.)
- 10.59 Amended and Restated Business Management and Shared Services Agreement, dated as of March 16, 2015, between the Company and The RMR Group LLC.(+) (Incorporated by reference to the Company's Annual Report on Form 10-K for the year ended December 31, 2014.)
- 21.1 Subsidiaries of the Company. (Filed herewith.)
- 23.1 Consent of RSM US LLP. (Filed herewith.)
- 31.1 Rule 13a 14(a) Certification of Chief Executive Officer. (Filed herewith.)
- 31.2 Rule 13a 14(a) Certification of Chief Financial Officer. (Filed herewith.)
- 32.1 Section 1350 Certification of Chief Executive Officer and Chief Financial Officer. (Furnished herewith.)
- 99.1 Amended and Restated Security Agreement (Lease No. 1), dated as of August 4, 2009, among Five Star Quality Care Trust, as Tenant, and the Landlord under the Amended and Restated Master Lease Agreement (Lease No. 1), dated as of August 4, 2009, among certain subsidiaries of Senior Housing Properties Trust, as Landlord, and Five Star Quality Care Trust, as Tenant. (Incorporated by reference to the Company's Quarterly Report on Form 10 Q for the quarter ended June 30, 2009, File No. 001-16817.)
- 99.2 Amended and Restated Subtenant Guaranty Agreement (Lease No. 1), dated as of August 4, 2009, made by certain subsidiaries of the Company, each a Subtenant Guarantor, for the benefit of the Landlord under the Amended and Restated Master Lease Agreement (Lease No. 1), dated as of August 4, 2009, among certain subsidiaries of Senior Housing Properties Trust, as Landlord, and Five Star Quality Care Trust, as Tenant. (Incorporated by reference to the Company's Quarterly Report on Form 10 Q for the quarter ended June 30, 2009, File No. 001-16817.)
- 99.3 Amended and Restated Subtenant Security Agreement (Lease No. 1), dated as of August 4, 2009, made by certain subsidiaries of the Company, as Subtenants, and the Landlord under the Amended and Restated Master Lease Agreement (Lease No. 1), dated as of August 4, 2009, among certain subsidiaries of Senior Housing Properties Trust, as Landlord, and Five Star Quality Care Trust, as Tenant. (Incorporated by reference to the Company's Quarterly Report on Form 10 Q for the quarter ended June 30, 2009, File No. 001-16817.)
- 99.4 Amended and Restated Security Agreement (Lease No. 2), dated as of August 4, 2009, made by certain subsidiaries of the Company, as Tenant, and the Landlord under the Amended and Restated Master Lease Agreement (Lease No. 2), dated as of August 4, 2009, among certain subsidiaries of Senior Housing Properties

- Trust, as Landlord, and certain subsidiaries of the Company, as Tenant. (Incorporated by reference to the Company's Quarterly Report on Form 10 Q for the quarter ended June 30, 2009, File No. 001-16817.)
- 99.5 Amended and Restated Subtenant Guaranty Agreement (Lease No. 2), dated as of August 4, 2009, made by certain subsidiaries of the Company, each a Subtenant Guarantor, for the benefit of the Landlord under the Amended and Restated Master Lease Agreement (Lease No. 2), dated as of August 4, 2009, among certain subsidiaries of Senior Housing Properties Trust, as Landlord, and certain subsidiaries of the Company, as Tenant. (Incorporated by reference to the Company's Quarterly Report on Form 10 Q for the quarter ended June 30, 2009, File No. 001-16817.)
- 99.6 Amended and Restated Subtenant Security Agreement (Lease No. 2), dated as of August 4, 2009, made by certain subsidiaries of the Company, as Subtenants, and the Landlord under the Amended and Restated Master Lease Agreement (Lease No. 2), dated as of August 4, 2009, among certain subsidiaries of Senior Housing Properties Trust, as Landlord, and certain subsidiaries of the Company, as Tenant. (Incorporated by reference to the Company's Quarterly Report on Form 10 Q for the quarter ended June 30, 2009, File No. 001-16817.)

Table of Contents

- Amended and Restated Security Agreement (Lease No. 4), dated as of August 4, 2009, made by certain subsidiaries of the Company, as Tenant, and the Landlord under the Amended and Restated Master Lease
- 99.7 Agreement (Lease No. 4), dated as of August 4, 2009, among certain subsidiaries of Senior Housing Properties Trust, as Landlord, and certain subsidiaries of the Company, as Tenant. (Incorporated by reference to the Company's Quarterly Report on Form 10 Q for the quarter ended June 30, 2009, File No. 001-16817.)
- Amended and Restated Subtenant Guaranty Agreement (Lease No. 4), dated as of August 4, 2009, made by certain subsidiaries of the Company, each a Subtenant Guarantor, for the benefit of the Landlord under the
- 99.8 Amended and Restated Master Lease Agreement (Lease No. 4), dated as of August 4, 2009, among certain subsidiaries of Senior Housing Properties Trust, as Landlord, and certain subsidiaries of the Company, as Tenant. (Incorporated by reference to the Company's Quarterly Report on Form 10 Q for the quarter ended June 30, 2009, File No. 001-16817.)
- Amended and Restated Subtenant Security Agreement (Lease No. 4), dated as of August 4, 2009, made by certain subsidiaries of the Company, as Subtenants, and the Landlord under the Amended and Restated Master
- 99.9 Lease Agreement (Lease No. 4), dated as of August 4, 2009, among certain subsidiaries of Senior Housing Properties Trust, as Landlord, and certain subsidiaries of the Company, as Tenant. (Incorporated by reference to the Company's Quarterly Report on Form 10 Q for the quarter ended June 30, 2009, File No. 001-16817.)
- Amendment to Subtenant Security Agreement, dated as of August 1, 2010, among certain subsidiaries of Senior
- 99.10 Housing Properties Trust and certain subsidiaries of the Company. (Incorporated by reference to the Company's Quarterly Report on Form 10 Q for the quarter ended September 30, 2010, File No. 001-16817.)
- Master Lease Agreement, dated as of September 1, 2008, among certain subsidiaries of Senior Housing
- 99.11 Properties Trust, as Landlord, and Five Star Quality Care RMI, LLC, as Tenant. (Incorporated by reference to the Company's Annual Report on Form 10 K for the year ended December 31, 2008, File No. 001 16817.)
- Guaranty Agreement, dated as of September 1, 2008, made by the Company for the benefit of certain
- 99.12 subsidiaries of Senior Housing Properties Trust. (Incorporated by reference to the Company's Annual Report on Form 10 K for the year ended December 31, 2008, File No. 001 16817.)
- Lease Agreement, dated as of May 12, 2011, between 400 Centre Street LLC and the Company. (Incorporated
- 99.13 by reference to the Company's Current Report on Form 8 K dated May 13, 2011, File No. 001 16817.)
- First Amendment to Lease, dated as of December 23, 2014, between 400 Centre Street LLC and the Company.
- 99.14 (Incorporated by reference to the Company's Annual Report on Form 10-K for the year ended December 31, 2014.)
- Lease Agreement, dated as of June 20, 2011, between SNH/LTA SE McCarthy New Bern LLC, as Landlord,
- 99.15 and FVE SE McCarthy New Bern LLC, as Tenant. (Incorporated by reference to the Company's Quarterly Report on Form 10 Q for the quarter ended June 30, 2011, File No. 001-16817.)
- Guaranty Agreement, dated as of June 20, 2011, from the Company in favor of SNH/LTA SE McCarthy New
- 99.16 Bern LLC. (Incorporated by reference to the Company's Quarterly Report on Form 10 Q for the quarter ended June 30, 2011, File No. 001-16817.)
- Lease Agreement, dated as of June 23, 2011, between SNH/LTA SE Wilson LLC, as Landlord, and FVE SE
- 99.17 Wilson LLC, as Tenant. (Incorporated by reference to the Company's Quarterly Report on Form 10 Q for the quarter ended June 30, 2011, File No. 001-16817.)
- Guaranty Agreement, dated as of June 23, 2011, from the Company in favor of SNH/LTA SE Wilson LLC.
- 99.18 (Incorporated by reference to the Company's Quarterly Report on Form 10 Q for the quarter ended June 30, 2011, File No. 001-16817.)
- Amended and Restated Reimbursement Agreement, dated May 1, 2012, among The RMR Group LLC,
- 99.19 TravelCenters of America LLC and the Company. (Incorporated by reference to the Company's Quarterly Report on Form 10 Q for the quarter ended June 30, 2012.)
- Pooling Agreement No. 1, dated as of June 29, 2016, among FVE Managers, Inc. and certain subsidiaries of
- 99.20 Senior Housing Properties Trust. (Incorporated by reference to the Company's Current Report on Form 8-K dated June 29, 2016.)
- 99.21

Pooling Agreement No. 2, dated as of June 29, 2016, among FVE Managers, Inc. and certain subsidiaries of Senior Housing Properties Trust. (Incorporated by reference to the Company's Current Report on Form 8-K dated June 29, 2016.)

99.22 Pooling Agreement No. 3, dated as of June 29, 2016, among FVE Managers, Inc. and certain subsidiaries of Senior Housing Properties Trust. (Incorporated by reference to the Company's Current Report on Form 8-K dated June 29, 2016.)

99.23 Pooling Agreement No. 4, dated as of June 29, 2016, among FVE Managers, Inc. and certain subsidiaries of Senior Housing Properties Trust. (Incorporated by reference to the Company's Current Report on Form 8-K dated June 29, 2016.)

99.24 Pooling Agreement No. 5, dated as of June 29, 2016, between FVE Managers, Inc. and SNH SE Tenant TRS, Inc. (Incorporated by reference to the Company's Current Report on Form 8-K dated June 29, 2016.)

Table of Contents

| | |
|-------|--|
| 99.25 | Pooling Agreement No. 6, dated as of June 29, 2016, between FVE Managers, Inc. and SNH SE Tenant TRS, Inc. (Incorporated by reference to the Company's Current Report on Form 8-K dated June 29, 2016.) |
| 99.26 | Pooling Agreement No. 7, dated as of June 29, 2016, between FVE Managers, Inc. and SNH SE Tenant TRS, Inc. (Incorporated by reference to the Company's Current Report on Form 8-K dated June 29, 2016.) |
| 99.27 | Pooling Agreement No. 8, dated as of June 29, 2016, between FVE Managers, Inc. and SNH AL AIMO Tenant, Inc. (Incorporated by reference to the Company's Current Report on Form 8-K dated June 29, 2016.) |
| 99.28 | Pooling Agreement No. 9, dated as of June 29, 2016, among FVE Managers, Inc. and certain subsidiaries of Senior Housing Properties Trust. (Incorporated by reference to the Company's Current Report on Form 8-K dated June 29, 2016.) |
| 99.29 | Pooling Agreement No. 10, dated as of June 29, 2016, among FVE Managers, Inc. and certain subsidiaries of Senior Housing Properties Trust. (Incorporated by reference to the Company's Current Report on Form 8-K dated June 29, 2016.) |
| 99.30 | Accession Agreement to Pooling Agreement No. 10, dated as of December 15, 2016, by SNH AL Cumming Tenant LLC. (Filed herewith.) |
| 99.31 | Pooling Agreement No. 11, dated as of December 15, 2016, between FVE Managers, Inc. and SNH AL Georgia Tenant LLC. (Filed herewith.) |
| 99.32 | Representative form of AL Management Agreement, dated March 30, 2015, between FVE Managers, Inc., as Manager, and SNH AL AIMO Tenant, Inc. (Incorporated by reference to the Company's Quarterly Report on Form 10-Q for the quarter ended March 31, 2015.) |
| 99.33 | Amendment to AL Management Agreements, dated July 10, 2014, between FVE Managers, Inc. and certain subsidiaries of Senior Housing Properties Trust. (Incorporated by reference to the Company's Current Report on Form 8 K dated July 10, 2014.) |
| 99.34 | Villa Valencia Agreement, dated July 10, 2014, between SNH SE Tenant Inc. and certain other subsidiaries of Senior Housing Properties Trust and FVE Managers, Inc. (Incorporated by reference to the Company's Current Report on Form 8 K dated July 10, 2014.) |
| 99.35 | Amendment to Villa Valencia Management Agreement, dated June 29, 2016, between FVE Managers, Inc. and SNH SE Tenant TRS, Inc. (Incorporated by reference to the Company's Current Report on Form 8-K dated June 29, 2016.) |
| 99.36 | Pooling Agreement, dated August 31, 2012, between FVE IL Managers, Inc. and certain subsidiaries of Senior Housing Properties Trust. (Incorporated by reference to the Company's Quarterly Report on Form 10 Q for the quarter ended September 30, 2012.) |
| 99.37 | Representative form of IL Management Agreement, dated as of December 15, 2011, between FVE IL Managers, Inc., as Manager, and SNH IL Properties Trust, as Owner. (Incorporated by reference to the Company's Annual Report on Form 10 K for the year ended December 31, 2011, File No. 001-16817.) |
| 99.38 | Amendment to IL Management Agreements, dated July 10, 2014, between FVE IL Managers, Inc. and certain subsidiaries of Senior Housing Properties Trust. (Incorporated by reference to the Company's Current Report on Form 8 K dated July 10, 2014.) |
| 99.39 | Management Agreement, dated as of August 31, 2012, between FVE Managers, Inc., as Manager, and D&R Yonkers LLC, as Licensee. (Incorporated by reference to the Company's Quarterly Report on Form 10 Q for the quarter ended September 30, 2012.) |
| 99.40 | First Amendment to Management Agreement, dated as of August 31, 2012, between FVE Managers, Inc., as Manager, and D&R Yonkers LLC, as Licensee. (Incorporated by reference to the Company's Annual Report on Form 10-K for the year ended December 31, 2014.) |
| 99.41 | FedEx Pricing Agreement, dated June 17, 2015, among the Company, TA Operating LLC, Sonesta International Hotels Corporation and The RMR Group LLC. (Incorporated by reference to the |

- 99.42 Company's Quarterly Report on Form 10-Q for the quarter ended June 30, 2015.)
Letter Agreement, dated October 21, 2016, among the Company and ABP Acquisition LLC, ABP Trust, Barry M. Portnoy and Adam D. Portnoy. (Incorporated by reference to the Company's Current Report on Form 8-K dated October 17, 2016.)
- 99.43 Letter Agreement, dated October 28, 2016, between the Company and Senior Housing Properties Trust. (Incorporated by reference to the Company's Quarterly Report on Form 10-Q for the quarter ended September 30, 2016.)
- 101.1 The following materials from the Company's Annual Report on Form 10 K for the year ended December 31, 2016 formatted in XBRL (eXtensible Business Reporting Language): (i) the Consolidated Balance Sheets, (ii) the Consolidated Statements of Operations, (iii) the Consolidated Statements of Comprehensive Loss, (iv) the Consolidated Statements of Shareholders' Equity, (v) the Consolidated Statements of Cash Flows, and (vi) related notes to these financial statements, tagged as blocks of text and in detail. (Filed herewith.)

(+) Management contract or compensatory plan or arrangement.

Table of Contents

Item 16. Form 10-K Summary

None.

65

Table of Contents

Report of Independent Registered Public Accounting Firm

To the Board of Directors and Shareholders
Five Star Senior Living Inc.

We have audited the accompanying consolidated balance sheets of Five Star Senior Living Inc. (see Note 1) as of December 31, 2016 and 2015, and the related consolidated statements of operations, comprehensive loss, shareholders' equity and cash flows for each of the three years ended December 31, 2016. These financial statements are the responsibility of the Five Star Senior Living Inc.'s management. Our responsibility is to express an opinion on these 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 Five Star Senior Living Inc. as of December 31, 2016 and 2015, and the results of their operations and their cash flows for each of the three years ended December 31, 2016, in conformity with U.S. generally accepted accounting principles.

We have also audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), Five Star Senior Living Inc.'s internal control over financial reporting as of December 31, 2016, based on criteria established in Internal Control - Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission in 2013, and our report dated March 3, 2017 expressed an unqualified opinion on the effectiveness of Five Star Senior Living Inc.'s internal control over financial reporting.

/s/ RSM US LLP

Boston, Massachusetts
March 3, 2017

F-1

Table of Contents

Report of Independent Registered Public Accounting Firm

To the Board of Directors and Shareholders
Five Star Senior Living Inc.

We have audited Five Star Senior Living Inc.'s internal control over financial reporting as of December 31, 2016, based on criteria established in Internal Control - Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission in 2013. Five Star Senior Living Inc.'s management is responsible for maintaining effective internal control over financial reporting and for its assessment of the effectiveness of internal control over financial reporting included in the accompanying Management Report on Assessment of Internal Control Over Financial Reporting. Our responsibility is to express an opinion on the company's internal control over financial reporting based on our audit.

We conducted our audit 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 effective internal control over financial reporting was maintained in all material respects. Our audit included obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, and testing and evaluating the design and operating effectiveness of internal control based on the assessed risk. Our audit also included performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion.

A company's internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company's internal control over financial reporting includes those policies and procedures that (a) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (b) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (c) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company's assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

In our opinion, Five Star Senior Living Inc. maintained, in all material respects, effective internal control over financial reporting as of December 31, 2016, based on criteria established in Internal Control - Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission in 2013.

We have also audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the consolidated financial statements of Five Star Senior Living Inc. and our report dated March 3, 2017 expressed an unqualified opinion.

/s/ RSM US LLP

Boston, Massachusetts
March 3, 2017

F-2

Table of Contents

FIVE STAR SENIOR LIVING INC.
CONSOLIDATED BALANCE SHEETS
(in thousands, except share data)

| | December 31, | |
|---|--------------|------------|
| | 2016 | 2015 |
| ASSETS | | |
| Current assets: | | |
| Cash and cash equivalents | \$ 16,608 | \$ 14,672 |
| Accounts receivable, net of allowance of \$3,191 and \$3,592 at December 31, 2016 and 2015, respectively | 38,324 | 37,829 |
| Due from related persons | 17,010 | 9,731 |
| Prepaid expenses | 11,342 | 9,456 |
| Investments in available for sale securities, of which \$9,659 and \$11,471 are restricted as of December 31, 2016 and 2015, respectively | 24,081 | 26,417 |
| Restricted cash | 15,059 | 3,301 |
| Other current assets | 5,953 | 9,682 |
| Assets of discontinued operations | 1,010 | 981 |
| Total current assets | 129,387 | 112,069 |
| Property and equipment, net | 351,929 | 383,858 |
| Equity investment of an investee | 7,116 | 6,827 |
| Restricted cash | 1,909 | 2,821 |
| Restricted investments in available for sale securities | 16,589 | 23,166 |
| Other long term assets | 2,804 | 3,029 |
| Total assets | \$ 509,734 | \$ 531,770 |
| LIABILITIES AND SHAREHOLDERS' EQUITY | | |
| Current liabilities: | | |
| Revolving credit facilities | \$— | \$ 50,000 |
| Accounts payable and accrued expenses | 68,453 | 93,205 |
| Accrued compensation and benefits | 35,939 | 32,127 |
| Due to related persons | 18,378 | 17,870 |
| Mortgage notes payable | 1,903 | 1,807 |
| Accrued real estate taxes | 12,784 | 12,207 |
| Security deposits and current portion of continuing care contracts | 5,099 | 6,129 |
| Other current liabilities | 30,430 | 30,399 |
| Liabilities of discontinued operations | 7 | 176 |
| Total current liabilities | 172,993 | 243,920 |
| Long term liabilities: | | |
| Mortgage notes payable | 58,494 | 60,396 |
| Accrued self insurance obligations | 36,637 | 37,588 |
| Deferred gain on sale and leaseback transaction with Senior Housing Properties Trust | 72,695 | — |
| Other long term liabilities | 4,649 | 5,414 |
| Total long term liabilities | 172,475 | 103,398 |
| Commitments and contingencies | | |
| Shareholders' equity: | | |
| | 500 | 494 |

Edgar Filing: SEARS HOLDINGS CORP - Form DEF 14A

Common stock, par value \$.01: 75,000,000 shares authorized, 49,995,932 and 49,476,611 shares issued and outstanding at December 31, 2016 and 2015, respectively

| | | |
|--|------------|------------|
| Additional paid in capital | 359,853 | 358,665 |
| Accumulated deficit | (199,521) | (177,622) |
| Accumulated other comprehensive income | 3,434 | 2,915 |
| Total shareholders' equity | 164,266 | 184,452 |
| Total liabilities and shareholders' equity | \$ 509,734 | \$ 531,770 |

See accompanying notes.

F-3

Table of Contents

FIVE STAR SENIOR LIVING INC.
CONSOLIDATED STATEMENTS OF OPERATIONS
(in thousands, except per share data)

| | For the year ended December 31, | | |
|--|---------------------------------|-------------|-------------|
| | 2016 | 2015 | 2014 |
| Revenues: | | | |
| Senior living revenue | \$1,115,551 | \$1,113,971 | \$1,099,228 |
| Management fee revenue | 12,350 | 10,728 | 9,765 |
| Reimbursed costs incurred on behalf of managed communities | 250,207 | 240,711 | 219,082 |
| Total revenues | 1,378,108 | 1,365,410 | 1,328,075 |
| Operating expenses: | | | |
| Senior living wages and benefits | 545,603 | 539,086 | 533,549 |
| Other senior living operating expenses | 284,533 | 293,501 | 292,457 |
| Costs incurred on behalf of managed communities | 250,207 | 240,711 | 219,082 |
| Rent expense | 201,667 | 199,075 | 197,359 |
| General and administrative expenses | 73,516 | 70,757 | 72,385 |
| Depreciation and amortization expense | 38,052 | 33,815 | 31,834 |
| Goodwill impairment | — | 25,344 | — |
| Long lived asset impairment | 502 | 145 | 589 |
| Total operating expenses | 1,394,080 | 1,402,434 | 1,347,255 |
| Operating loss | (15,972) | (37,024) | (19,180) |
| Interest, dividend and other income | 984 | 982 | 867 |
| Interest and other expense | (4,912) | (4,927) | (5,131) |
| Gain on early extinguishment of debt | — | 692 | — |
| Gain on sale of available for sale securities reclassified from accumulated other comprehensive income | 107 | 160 | 392 |
| Loss from continuing operations before income taxes and equity in earnings of an investee | (19,793) | (40,117) | (23,052) |
| Provision for income taxes | (2,351) | (662) | (56,385) |
| Equity in earnings of an investee | 137 | 20 | 87 |
| Loss from continuing operations | (22,007) | (40,759) | (79,350) |
| Income (loss) from discontinued operations, net of tax | 194 | (2,324) | (6,056) |
| Net loss | \$(21,813) | \$(43,083) | \$(85,406) |
| Weighted average shares outstanding—basic and diluted | 48,815 | 48,406 | 48,028 |
| Basic and diluted loss per share from: | | | |
| Continuing operations | \$(0.45) | \$(0.84) | \$(1.65) |
| Discontinued operations | — | (0.05) | (0.13) |
| Net loss per share—basic and diluted | \$(0.45) | \$(0.89) | \$(1.78) |

See accompanying notes.

F-4

Table of Contents

FIVE STAR SENIOR LIVING INC.
 CONSOLIDATED STATEMENTS OF COMPREHENSIVE LOSS
 (in thousands)

| | For the year ended December 31, | | |
|---|------------------------------------|------------|------------|
| | 2016 | 2015 | 2014 |
| Net loss | \$(21,813) | \$(43,083) | \$(85,406) |
| Other comprehensive income (loss): | | | |
| Unrealized gain (loss) on investments in available for sale securities, net of tax of \$273, \$0, and \$151, respectively | 424 | (595) |) 612 |
| Equity in unrealized gain (loss) of an investee, net of tax | 152 | (20) |) 2 |
| Realized gain on investments in available for sale securities reclassified and included in net loss, net of tax of \$50, \$0, and \$150, respectively | (57) |) (160) |) (242) |
| Other comprehensive income (loss) | 519 | (775) |) 372 |
| Comprehensive loss | \$(21,294) | \$(43,858) | \$(85,034) |

See accompanying notes.

F-5

Table of Contents

FIVE STAR SENIOR LIVING INC.
CONSOLIDATED STATEMENTS OF SHAREHOLDERS' EQUITY
(in thousands, except share data)

| | Number of Shares | Common Stock | Additional Paid in Capital | Accumulated Deficit | Accumulated Other Comprehensive Income | Total |
|---|---------------------|-----------------|----------------------------------|------------------------|---|------------|
| Balance at December 31, 2013 | 48,613,442 | \$ 486 | \$ 355,570 | \$ (48,996) | \$ 3,318 | \$ 310,378 |
| Comprehensive loss: | | | | | | |
| Net loss | — | — | — | (85,406) | — | (85,406) |
| Unrealized gain on investments in available for sale securities, net of tax | — | — | — | — | 612 | 612 |
| Realized gain on investments in available for sale securities reclassified and included in net loss, net of tax | — | — | — | — | (242) | (242) |
| Equity in unrealized gain of an investee, net of tax | — | — | — | — | 2 | 2 |
| Total comprehensive loss | — | — | — | (85,406) | 372 | (85,034) |
| Grants under share award plan and share based compensation | 403,050 | 4 | 1,481 | — | — | 1,485 |
| Repurchases under share award plan | (19,177) | — | — | (47) | — | (47) |
| Balance at December 31, 2014 | 48,997,315 | \$ 490 | \$ 357,051 | \$ (134,449) | \$ 3,690 | \$ 226,782 |
| Comprehensive loss: | | | | | | |
| Net loss | — | — | — | (43,083) | — | (43,083) |
| Unrealized loss on investments in available for sale securities, net of tax | — | — | — | — | (595) | (595) |
| Realized gain on investments in available for sale securities reclassified and included in net loss, net of tax | — | — | — | — | (160) | (160) |
| Equity in unrealized loss of an investee, net of tax | — | — | — | — | (20) | (20) |
| Total comprehensive loss | — | — | — | (43,083) | (775) | (43,858) |
| Grants under share award plan and share based compensation | 521,900 | 4 | 1,614 | — | — | 1,618 |
| Repurchases under share award plan | (42,604) | — | — | (90) | — | (90) |
| Balance at December 31, 2015 | 49,476,611 | \$ 494 | \$ 358,665 | \$ (177,622) | \$ 2,915 | \$ 184,452 |
| Comprehensive loss: | | | | | | |
| Net loss | — | — | — | (21,813) | — | (21,813) |
| Unrealized gain on investments in available for sale securities, net of tax | — | — | — | — | 424 | 424 |
| Realized gain on investments in available for sale securities reclassified and included in net loss, net of tax | — | — | — | — | (57) | (57) |
| Equity in unrealized gain of an investee, net of tax | — | — | — | — | 152 | 152 |
| Total comprehensive loss | — | — | — | (21,813) | 519 | (21,294) |
| Grants under share award plan and share based compensation | 569,400 | 6 | 1,188 | — | — | 1,194 |
| Repurchases under share award plan | (50,079) | — | — | (86) | — | (86) |

Edgar Filing: SEARS HOLDINGS CORP - Form DEF 14A

| | | | | | | |
|------------------------------|------------|--------|------------|--------------|----------|-----------|
| Balance at December 31, 2016 | 49,995,932 | \$ 500 | \$ 359,853 | \$(199,521) | \$ 3,434 | \$164,266 |
|------------------------------|------------|--------|------------|--------------|----------|-----------|

See accompanying notes.

F-6

Table of Contents

FIVE STAR SENIOR LIVING INC.
CONSOLIDATED STATEMENTS OF CASH FLOWS
(in thousands)

| | For the year ended December 31, | | |
|--|------------------------------------|------------|------------|
| | 2016 | 2015 | 2014 |
| Cash flows from operating activities: | | | |
| Net loss | \$(21,813) | \$(43,083) | \$(85,406) |
| Adjustments to reconcile net loss to cash (used in) provided by operating activities: | | | |
| Depreciation and amortization expense | 38,052 | 33,815 | 31,834 |
| Gain on early extinguishment of debt | — | (742) | — |
| (Income) loss from discontinued operations before income tax | (194) | 2,324 | 5,977 |
| Gain on sale of available for sale securities reclassified from accumulated other comprehensive income | (107) | (160) | (392) |
| Loss on disposal of property and equipment | 121 | 102 | — |
| Goodwill impairment | — | 25,344 | — |
| Long lived asset impairment | 502 | 145 | 589 |
| Equity in earnings of an investee | (137) | (20) | (87) |
| Stock-based compensation | 1,194 | 1,618 | 1,485 |
| Deferred income taxes | — | — | 55,334 |
| Provision for losses on receivables | 4,033 | 4,646 | 4,777 |
| Amortization of deferred gain on sale and leaseback transaction with Senior Housing Properties Trust | (3,340) | — | — |
| Other non-cash (income) expense adjustments, net | (531) | (143) | 1,636 |
| Changes in assets and liabilities: | | | |
| Accounts receivable | (4,528) | (3,661) | (6,651) |
| Prepaid expenses and other assets | 521 | 2,391 | (279) |
| Accounts payable and accrued expenses | (24,661) | 8,582 | 13,387 |
| Accrued compensation and benefits | 3,812 | (2,044) | 2,283 |
| Due (to) from related persons, net | (7,923) | 809 | (1,601) |
| Other current and long term liabilities | (8,454) | 10,617 | (549) |
| Cash (used in) provided by operating activities | (23,453) | 40,540 | 22,337 |
| Cash flows from investing activities: | | | |
| (Increase) decrease in restricted cash and investment accounts, net | (10,846) | (737) | 13,683 |
| Acquisition of property and equipment | (55,419) | (57,480) | (49,916) |
| Acquisition of senior living communities | — | (9,200) | (5,926) |
| Purchases of intangible assets | — | (191) | — |
| Purchases of available for sale securities | (8,388) | (17,870) | (22,431) |
| Investment in an investee | — | — | (825) |
| Proceeds from sale of property and equipment to Senior Housing Properties Trust | 21,437 | 21,323 | 25,804 |
| Proceeds from sale and leaseback transaction with Senior Housing Properties Trust | 112,350 | — | — |
| Proceeds from sale of available for sale securities | 17,905 | 10,857 | 10,876 |
| Cash provided by (used in) investing activities | 77,039 | (53,298) | (28,735) |
| Cash flows from financing activities: | | | |
| Proceeds from borrowings on credit facilities | 25,000 | 40,000 | 20,000 |
| Repayments of borrowings on credit facilities | (75,000) | (25,000) | (20,000) |
| Repayments of mortgage notes payable | (1,260) | (5,998) | (1,979) |

Edgar Filing: SEARS HOLDINGS CORP - Form DEF 14A

| | | | |
|--|-----------|------------|------------|
| Payment of deferred financing fees | (300) | (300) | — |
| Payment of employee tax obligations on withheld shares | (86) | (90) | (47) |
| Cash (used in) provided by financing activities | (51,646) | 8,612 | (2,026) |
| Cash flows from discontinued operations: | | | |
| Net cash provided by (used in) operating activities | 11 | (2,151) | 5,519 |
| Net cash (used in) provided by investing activities | (15) | (19) | 265 |
| Net cash flows (used in) provided by discontinued operations | (4) | (2,170) | 5,784 |
| Change in cash and cash equivalents | 1,936 | (6,316) | (2,640) |
| Cash and cash equivalents at beginning of period | 14,672 | 20,988 | 23,628 |
| Cash and cash equivalents at end of period | \$16,608 | \$14,672 | \$20,988 |
| Supplemental cash flow information: | | | |
| Cash paid for interest | \$4,855 | \$4,078 | \$3,557 |
| Cash paid for income taxes, net | \$3,213 | \$658 | \$1,179 |
| Non-cash activities: | | | |
| Real estate acquisition | \$— | \$(18,254) | \$(15,518) |
| Assumption of mortgage note payable | \$— | \$18,254 | \$15,518 |
| See accompanying notes. | | | |

F-7

Table of Contents

FIVE STAR SENIOR LIVING INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(dollar amounts in thousands, except per share amounts)

1. Organization and Business

We are a corporation formed under the laws of the State of Maryland in 2001. Effective March 3, 2017, we changed our name from "Five Star Quality Care, Inc." to "Five Star Senior Living Inc." We operate senior living communities, including independent living communities, assisted living communities and skilled nursing facilities, or SNFs. As of December 31, 2016, we operated 283 senior living communities located in 32 states with 31,830 living units, including 253 primarily independent and assisted living communities with 29,229 living units and 30 SNFs with 2,601 living units. As of December 31, 2016, we owned and operated 26 communities (2,703 living units), we leased and operated 189 communities (20,339 living units) and we managed 68 communities (8,788 living units). Our 283 senior living communities, as of December 31, 2016, included 10,772 independent living apartments, 16,179 assisted living suites and 4,879 skilled nursing beds. The foregoing numbers exclude living units categorized as out of service.

2. Summary of Significant Accounting Policies

Basis of Presentation. The accompanying consolidated financial statements include our accounts and those of all of our consolidated subsidiaries. All intercompany transactions and balances with or among our consolidated subsidiaries have been eliminated.

Use of Estimates. Preparation of these financial statements in conformity with accounting principles generally accepted in the United States requires us to make estimates and assumptions that may affect the amounts reported in these financial statements and related notes. Some significant estimates are included in our revenue recognition, including contractual allowances, self insurance reserves, the allowance for doubtful accounts, goodwill, other intangibles and long lived assets.

We are also required to estimate income taxes payable in each of the jurisdictions in which we operate. The process involves estimating actual current tax expense along with assessing temporary differences resulting from differing treatment of items for financial statement and tax purposes. These timing differences result in deferred tax assets and liabilities, which are included in our consolidated balance sheets. We are required to record a valuation allowance to reduce deferred tax assets if we are not able to conclude that it is more likely than not these assets will be realized.

Our actual results could differ from our estimates. We periodically review estimates and assumptions and we reflect the effects of changes, if any, in the consolidated financial statements in the period that they are determined.

Earnings Per Share. We calculate basic earnings per common share, or EPS, by dividing net income (loss) (and income (loss) from continuing operations and income (loss) from discontinued operations) by the weighted average number of common shares outstanding during the year. We calculate diluted EPS using the more dilutive of the two-class method or the treasury stock method.

Cash and Cash Equivalents. Cash and cash equivalents, consisting of short term, highly liquid investments and money market funds with original maturities of three months or less at the date of purchase, are carried at cost plus accrued interest, which approximates market.

Equity Method Investments. As of December 31, 2016, we and six other shareholders each owned approximately 14.3% of the outstanding equity of Affiliates Insurance Company, or AIC. Although we owned less than 20% of AIC, we use the equity method to account for this investment because we believe that we have significant influence over AIC, as all of our Directors are also directors of AIC. Under the equity method, we recorded our percentage share of net earnings from AIC in our consolidated statements of operations. If we determine there is an "other than temporary impairment" in the fair value of this investment, we would record a charge to earnings. In evaluating the fair value of this investment, we have considered, among other things, the assets and liabilities held by AIC, AIC's overall financial condition and earning trends, and the financial condition and prospects for the insurance industry generally. As of December 31, 2016, we have invested \$6,034 in AIC.

Investment Securities. Investment securities that are held principally for resale in the near term are classified as "trading" and are carried at fair value with changes in fair value recorded in earnings. We did not hold any trading securities during the years ended December 31, 2016, 2015 or 2014.

F-8

Table of Contents

Securities not classified as “trading” are classified as “available for sale” and carried at fair value, with unrealized gains and losses reported as a separate component of shareholders’ equity and “other than temporary impairment” losses recorded in our consolidated statements of operations. Realized gains and losses on all available for sale securities are recognized based on specific identification. Our available for sale securities at December 31, 2016 and 2015 consisted primarily of debt and equity securities. Restricted investments in available for sale securities are kept as security for obligations arising from our self insurance programs. At December 31, 2016, these available for sale securities had a fair value of \$40,670 and an unrealized holding gain of \$2,133. At December 31, 2015, these available for sale securities had a fair value of \$49,583 and an unrealized holding gain of \$1,543.

In 2016, 2015 and 2014, our available for sale securities generated interest and dividend income of \$930, \$912 and \$788, respectively, which is included in interest, dividend and other income in our consolidated statements of operations.

The following table summarizes the fair value and gross unrealized losses related to our “available for sale” securities, aggregated by investment category and length of time that individual securities have been in a continuous unrealized loss position for the years ended:

| December 31, 2016 | | | | | |
|-------------------|---------------------|-----------------|------------------------|-----------------|----------------|
| | Less than 12 months | | Greater than 12 months | | Total |
| | Fair Value | Unrealized Loss | Fair Value | Unrealized Loss | Fair Value |
| Investments | \$8,502 | \$ 233 | \$ 937 | \$ 64 | \$9,439 \$ 297 |

| December 31, 2015 | | | | | |
|-------------------|---------------------|-----------------|------------------------|-----------------|-----------------|
| | Less than 12 months | | Greater than 12 months | | Total |
| | Fair Value | Unrealized Loss | Fair Value | Unrealized Loss | Fair Value |
| Investments | \$14,436 | \$ 238 | \$ 1,986 | \$ 332 | \$16,422 \$ 570 |

We routinely evaluate our available for sale securities to determine if they have been impaired. If the fair value of an investment is less than its book or carrying value and we expect that situation to continue for a more than temporary period, we will record an “other than temporary impairment” loss in our consolidated statements of operations. We evaluate the fair value of our available for sale securities by reviewing each security’s current market price, the ratings of the security, the financial condition of the issuer and our intent and ability to retain the security during temporary market price fluctuations or until maturity. In evaluating the factors described above, we presume a decline in value to be an “other than temporary impairment” if the quoted market price of the security is below the security’s cost basis for an extended period. However, this presumption may be overcome if there is persuasive evidence indicating the value decline is temporary in nature, such as when the operating performance of the obligor is strong or if the market price of the security is historically volatile. Additionally, there may be instances in which impairment losses are recognized even if the decline in value does not meet the criteria described above, such as if we plan to sell the security in the near term and the fair value is below our cost basis. When we believe that a change in fair value of an available for sale security is temporary, we record a corresponding credit or charge to other comprehensive income for any unrealized gains and losses. When we determine that impairment in the fair value of an available for sale security is an “other than temporary impairment”, we record a charge to earnings. We did not record such an impairment charge for the years ended December 31, 2016, 2015 and 2014.

Restricted Cash. Restricted cash as of December 31, 2016 and 2015 includes cash that we deposited as security for obligations arising from our self insurance programs and other amounts for which we are required to establish escrows, including: real estate taxes and capital expenditures as required by our mortgages and certain resident security deposits.

Edgar Filing: SEARS HOLDINGS CORP - Form DEF 14A

| | 2016 | | 2015 | |
|---|----------|-----------|---------|-----------|
| | Current | Long term | Current | Long term |
| Insurance reserves | \$1,111 | \$ 1,909 | \$1,397 | \$ 2,821 |
| Real estate taxes and capital expenditures as required by our mortgages | 1,624 | — | 1,279 | — |
| Resident security deposits | 588 | — | 625 | — |
| Workers' compensation letter of credit collateral | \$11,736 | \$ — | \$— | \$ — |
| Total | \$15,059 | \$ 1,909 | \$3,301 | \$ 2,821 |

F-9

Table of Contents

Accounts Receivable and Allowance for Doubtful Accounts. We record accounts receivable at their estimated net realizable value. Included in accounts receivable as of December 31, 2016 and 2015 are amounts due from the Medicare program of \$10,744 and \$9,607, respectively, and amounts due from various state Medicaid programs of \$11,951 and \$12,692, respectively.

We estimate allowances for uncollectible amounts and contractual allowances based upon factors which include, but are not limited to, the age of the receivable and the terms of the agreements, the residents' or third party payers' stated intent to pay, the payers' financial capacity to pay and other factors which may include likelihood and cost of litigation. Accounts receivable allowances are estimates. We periodically review and revise these estimates based on new information and these revisions may be material. Our SNFs record their provision for doubtful accounts as a reduction of revenue, which amounts totaled \$1,162, \$1,963 and \$1,321 during 2016, 2015 and 2014, respectively. Our allowance for doubtful accounts consists of the following:

| | |
|---------------------------------|----------|
| Balance January 1, 2014 | \$4,281 |
| Provision for doubtful accounts | 4,777 |
| Write-offs | (5,642) |
| Balance December 31, 2014 | 3,416 |
| Provision for doubtful accounts | 4,646 |
| Write-offs | (4,470) |
| Balance December 31, 2015 | 3,592 |
| Provision for doubtful accounts | 4,033 |
| Write-offs | (4,434) |
| Balance December 31, 2016 | \$3,191 |

Deferred Finance Costs. We capitalize issuance costs related to our secured credit facilities and amortize the deferred costs over the terms of the respective agreements. Our unamortized balance of deferred finance costs was \$50 and \$100 at December 31, 2016 and 2015, respectively, and was included in other current assets on our consolidated balance sheets. Accumulated amortization related to deferred finance costs was \$175 and \$380 at December 31, 2016 and 2015, respectively. At December 31, 2016, the weighted average amortization period remaining is less than one year. We expect the amortization expense to be incurred during 2017 is approximately \$50.

Property and Equipment. Property and equipment is stated at cost, less accumulated depreciation. We record depreciation on property and equipment on a straight line basis over estimated useful lives of up to 40 years for buildings, up to 15 years for building improvements and up to seven years for personal property. We regularly evaluate whether events or changes in circumstances have occurred that could indicate impairment in the value of our long lived assets. If there is an indication that the carrying value of an asset is not recoverable, we determine the amount of impairment loss, if any, by comparing the historical carrying value of the asset to its estimated fair value. We determine estimated fair value through an evaluation of recent financial performance, recent transactions for similar assets, market conditions and projected cash flows using standard industry valuation techniques.

Goodwill and Other Intangible Assets. Goodwill represents the costs of business acquisitions in excess of the fair value of identifiable net assets acquired. We recorded an impairment charge in the year ended December 31, 2015 for the then full balance of our goodwill (see Note 4 for further discussion). We continue to not have any goodwill recorded on our consolidated balance sheet as of December 31, 2016. Historically, we evaluated the recoverability of goodwill annually in the fourth quarter of each fiscal year, or more frequently, if events or changes in circumstances indicated that goodwill might have been impaired. If our review indicated that the carrying amount of goodwill exceeded its fair value, we would reduce the carrying amount of goodwill to fair value. We evaluated goodwill for impairment at the reporting unit level, which we determined to be our operating segments, by comparing the fair value of the reporting unit as determined by its discounted cash flows and market approaches with its carrying value. The key assumptions used in the discounted cash flow analysis included future revenue growth, gross margins and our

weighted average cost of capital. We selected a growth rate based on our view of the growth prospect of each of our reporting units. If the carrying value of the reporting unit exceeded its fair value, we compared the implied fair value of the reporting unit's goodwill with its carrying amount to measure the amount of the potential impairment loss.

At acquisition, we estimate and record the fair value of purchased intangible assets primarily using discounted cash flow analyses of anticipated cash flows reflecting incremental revenues and/or cost savings resulting from the acquired intangible asset, reflecting market participant assumptions. Amortization of intangible assets with finite lives is recognized over

F-10

Table of Contents

their estimated useful lives using a method of amortization that reflects the pattern in which the economic benefits of the intangible assets are consumed or otherwise realized.

We regularly evaluate whether events or changes in circumstances have occurred that could indicate impairment in the value of our other intangible assets. If there is an indication that the carrying value of an asset is not recoverable, we determine the amount of impairment loss, if any, by comparing the historical carrying value of the asset to its estimated fair value. We determine estimated fair value through an evaluation of recent financial performance, recent transactions for similar assets, market conditions and projected cash flows using standard industry valuation techniques.

Legal Proceedings and Claims. We have been, are currently, and expect in the future to be involved in claims, lawsuits, and regulatory and other government audits, investigations and proceedings arising in the ordinary course of our business, some of which may involve material amounts. Also, the defense and resolution of these claims, lawsuits, and regulatory and other government audits, investigations and proceedings may require us to incur significant expense. We account for claims and litigation losses in accordance with Financial Accounting Standards Board, or FASB, Accounting Standards Codification™, or ASC, Topic 450, Contingencies. Under FASB ASC Topic 450, loss contingency provisions are recorded for probable and estimable losses at our best estimate of a loss or, when a best estimate cannot be made, at our estimate of the minimum loss. These estimates are often developed prior to knowing the amount of the ultimate loss, require the application of considerable judgment, and are refined as additional information becomes known. Accordingly, we are often initially unable to develop a best estimate of loss and therefore the estimated minimum loss amount, which could be zero, is recorded; then, as information becomes known, the minimum loss amount is updated, as appropriate. Occasionally, a minimum or best estimate amount may be increased or decreased when events result in a changed expectation.

Self Insurance. We self insure up to certain limits for workers' compensation, professional and general liability claims, automobile claims and property losses. Claims in excess of these limits are insured up to contractual limits, over which we are self insured. We fully self insure all health related claims for our covered employees. We have established an offshore captive insurance company subsidiary which participates in our workers' compensation and professional and general liability insurance programs. Determining reserves for the casualty, liability, workers' compensation and healthcare losses and costs that we have incurred as of the end of a reporting period involves significant judgments based upon our experience and our expectations of future events, including projected settlements for pending claims, known incidents that we expect may result in claims, estimates of incurred but not yet reported claims, expected changes in premiums for insurance provided by insurers whose policies provide for retroactive adjustments, estimated litigation costs and other factors. Since these reserves are based on estimates, the actual expenses we incur may differ from the amount reserved. We regularly adjust these estimates to reflect changes in the foregoing factors, our actual claims experience, recommendations from our professional consultants, changes in market conditions and other factors; it is possible that such adjustments may be material. Our total self insurance reserves were \$65,526 and \$64,966 as of the year ended December 31, 2016 and 2015, respectively, and are included in accrued compensation and benefits, other current liabilities and accrued self insurance obligations in our consolidated balance sheets.

Continuing Care Contracts. Residents at one of our communities may enter into continuing care contracts with us. We offer one form of continuing care contract to new residents at this community. This form of contract provides that 10% of the resident admission fee becomes non refundable upon occupancy, and the remaining 90% becomes non refundable at the rate of 1.5% per month of the original amount over the subsequent 60 months. Four other forms of continuing care contracts are in effect for existing residents but are not offered to new residents. One historical form of contract provides that the resident admission fee is 10% non refundable upon occupancy and 90% refundable. The second historical form of contract provides that the resident admission fee is 100% refundable. The third historical form of contract provides that the resident admission fee is 1% refundable and 99% non refundable upon admission.

The fourth historical form of contract provides that 30% of the resident admission fee is non refundable upon occupancy and 70% is refundable. In each case, we amortize the non refundable part of these fees into revenue over the actuarially determined remaining life of the resident, which is the expected period of occupancy by the resident. We pay refunds of these admission fees when residents relocate from our communities. We report the refundable amount of these admission fees as current liabilities and the non refundable amount as deferred revenue, a portion of which is classified as a current liability. The balance of our refundable admission fees as of December 31, 2016 and 2015 were \$1,905 and \$2,709, respectively, and were included in security deposits and current portion of continuing care contracts on our consolidated balance sheets. The balance of non-refundable admission fees as of December 31, 2016 and 2015 were \$1,252 and \$1,561, respectively, of which \$1,031 and \$1,267, respectively, were included in other long term liabilities on our consolidated balance sheets.

Leases. On the inception date of a lease and upon any relevant amendments to such lease, we test the classification of such lease as either a capital lease or an operating lease. None of our leases have met any of the criteria to be classified as a capital lease under FASB ASC Topic 840, Leases, and, therefore, we have accounted for all of our leases as operating leases.

F-11

Table of Contents

Other aspects of our lease accounting policies relate to the accounting for sale leaseback transactions, including the appropriate amortization of related deferred liabilities and any deferred gains or losses, and the accounting for lease incentives.

Taxes. FASB ASC Topic 740, Income Taxes, prescribes how we should recognize, measure and present in our consolidated financial statements uncertain tax positions that have been taken or are expected to be taken in a tax return. We can recognize a tax benefit only if it is “more likely than not” that a particular tax position will be sustained upon examination or audit. To the extent the “more likely than not” standard has been satisfied, the benefit associated with a tax position is measured as the largest amount that has a greater than 50% likelihood of being realized.

We pay franchise taxes in certain states in which we have operations. We have included franchise taxes in general and administrative and other senior living operating expenses in our consolidated statements of operations.

We account for income taxes under the asset and liability method, which requires the recognition of deferred tax assets and liabilities for the expected future tax consequences to be included in our financial statements. Under this method, deferred tax assets and liabilities are determined on the basis of the differences between the financial statement and tax bases of assets and liabilities using enacted tax rates in effect for the year in which the differences are expected to reverse, while the effect of a change in tax rates on deferred tax assets and liabilities is recognized in income in the period that includes the enactment date.

We recognize deferred tax assets to the extent that we believe these assets are more likely than not to be realized. In making such a determination, we consider all available positive and negative evidence, including future reversals of existing taxable temporary differences, projected future taxable income, tax-planning strategies and results of recent operations. In the future, if we determine that we would be able to realize our deferred tax assets in excess of their net recorded amount, we would make an adjustment to the deferred tax asset valuation allowance and record an income tax benefit.

Fair Value of Financial Instruments. Our financial instruments are limited to cash and cash equivalents, accounts receivable, available for sale securities, accounts payable and mortgage notes payable. Except for our mortgage debt, the fair value of these financial instruments was not materially different from their carrying values at December 31, 2016 and 2015. We estimate the fair values of our mortgage debt using market quotes when available, discounted cash flow analyses and current prevailing interest rates.

Revenue Recognition. We derive our revenues primarily from services to residents at our senior living communities, and we record revenues when services are provided. We receive payment from governments or other third party payers for some of our services. We derived approximately 22%, 22% and 23% of our senior living revenues in 2016, 2015 and 2014, respectively, from payments under Medicare and Medicaid programs. Revenues under some of these programs are subject to audit and retroactive adjustment.

Medicare revenues from continuing operations at our senior living communities totaled \$112,116, \$122,018 and \$129,212 during 2016, 2015 and 2014, respectively. Medicaid revenues from continuing operations at our senior living communities totaled \$126,209, \$122,821 and \$118,536 during 2016, 2015 and 2014, respectively.

Some of our senior living communities require new private pay residents to pay community fees. Substantially all community fees received are non refundable and are recorded initially as deferred revenue and are included in other current liabilities in our consolidated balance sheets. The deferred amounts are amortized over the life of the contract.

One-time Employee Termination Benefits. FASB ASC Topic 420, Exit or Disposal Cost Obligations, or ASC Topic 420, specifies the criteria for recognizing a one-time employee termination arrangement. In December 2015, we

entered into a letter agreement with our former chief financial officer and treasurer in connection with the termination of his employment. Pursuant to that letter agreement, we agreed to pay severance in the amount of \$604 beginning in February 2016 through December 2017 with no future services required after the termination date, which was December 31, 2015. Our arrangement with our former chief financial officer and treasurer meets the criteria in ASC Topic 420, and, as a result, we recorded the full severance amount of \$604 in the year ended December 31, 2015, which is included in general and administrative expenses in our consolidated statements of operations.

In accordance with the letter agreement, our Compensation Committee of our Board of Directors also awarded our former Chief Financial Officer and Treasurer a stock grant of 35,000 common shares and agreed to accelerate the vesting of his unvested common shares including those awarded in prior years. In accordance with FASB ASC Topic 718, Stock Compensation, we recorded non-cash stock compensation expense of approximately \$234 in the year ended December 31, 2015, which is included in general and administrative expenses in our consolidated statements of operations.

F-12

Table of Contents

Reclassifications. We have made reclassifications to the prior years' financial statements to conform to the current year's presentation. These reclassifications had no effect on net income or shareholders' equity.

Recent Accounting Pronouncements. In December 2015, we early adopted FASB Accounting Standards Update, or ASU, No. 2015-17, Balance Sheet Classification of Deferred Taxes, which requires that deferred tax assets and liabilities be classified as noncurrent in a consolidated balance sheet rather than the former presentation of separating deferred tax assets and liabilities into current and noncurrent amounts. We adopted this ASU using prospective application. Since we have recognized a full deferred tax valuation allowance since 2014, and our deferred tax assets and liabilities net to zero, the implementation of this ASU did not have a material impact on our consolidated financial statements.

On January 1, 2016, we adopted FASB ASU No. 2015-03, Simplifying the Presentation of Debt Issuance Costs, which requires debt issuance costs to be presented in the balance sheet as a direct deduction from the associated debt liability, and ASU No. 2015-15, Presentation and Subsequent Measurement of Debt Issuance Costs Associated with Line-of-Credit Arrangements - Amendments to SEC Paragraphs Pursuant to Staff Announcement at June 18, 2015 EITF Meeting, which addresses the presentation of debt issuance costs related to line of credit arrangements. The implementation of ASU No. 2015-03 did not have a material impact on our consolidated financial statements and the adoption of ASU No. 2015-15 did not result in any changes in the classification of capitalized debt issuance costs related to our secured revolving credit facility.

On January 1, 2016, we adopted FASB ASU No. 2015-16, Simplifying the Accounting for Measurement-Period Adjustments, which eliminates the requirement for an acquirer in a business combination to account for measurement period adjustments retrospectively. Instead, acquirers must recognize measurement period adjustments during the period in which they determine the amounts, including the effect on earnings of any amounts that would have been recorded in previous periods if the accounting had been completed at the acquisition date. The implementation of this ASU did not have a material impact on our consolidated financial statements.

On January 1, 2016, we adopted FASB ASU 2014-15, Presentation of Financial Statements - Going Concern: Disclosure of Uncertainties about an Entity's Ability to Continue as a Going Concern, which requires an entity to evaluate whether there are conditions or events that raise substantial doubt about the entity's ability to continue as a going concern within one year after the date that the financial statements are issued (or within one year after the financial statements are available to be issued when applicable) and to provide related footnote disclosures in certain circumstances. The implementation of this ASU did not have an impact on our consolidated financial statements.

In January 2016, the FASB issued ASU No. 2016-01, Recognition and Measurement of Financial Assets and Financial Liabilities, which changes how entities measure certain equity investments and present changes in the fair value of financial liabilities measured under the fair value option that are attributable to their own credit. This ASU is effective for interim and annual periods beginning after December 15, 2017, with early adoption permitted subject to certain conditions. Currently, changes in fair value of these investments are recorded through other comprehensive income. Under this ASU, these changes will be recorded through earnings. We are continuing to evaluate this ASU, but we expect the implementation of this ASU will affect how we record changes in fair value of the available for sale securities that we hold.

In February 2016, the FASB issued ASU No. 2016-02, Leases (Topic 842), which sets out the principles for the recognition, measurement, presentation and disclosure of leases for both parties to a contract (i.e., lessees and lessors). ASU No. 2016-02 requires lessees to apply a dual approach, classifying leases as either finance or operating leases based on the principle of whether or not the lease is effectively a financed purchase of the leased asset by the lessee. This classification will determine whether the lease expense is recognized based on an effective interest method or on a straight line basis over the term of the lease. A lessee is also required to record a right of use asset and a lease

liability for all leases with a term of greater than 12 months regardless of their classification. Leases with a term of 12 months or less will be accounted for similar to existing guidance for operating leases today. The new standard requires lessors to account for leases using an approach that is substantially equivalent to existing guidance for sales type leases, direct financing leases and operating leases. ASU No. 2016-02 is effective for reporting periods beginning after December 15, 2018, with early adoption permitted. We are in the process of evaluating the effects the adoption of this update may have on our consolidated financial statements. We believe the adoption of this update will have a material impact on our consolidated balance sheets due to the recognition of the lease rights and obligations as assets and liabilities. While the adoption will have no effect on the cash we pay, we expect amounts within our statements of operations and comprehensive (loss) income to change materially.

In March 2016, the FASB issued ASU No. 2016-09, Compensation - Stock Compensation (Topic 718), which identifies areas for simplification involving several aspects of accounting for share based payment transactions, including the income tax consequences, classification of awards as either equity or liabilities, an option to recognize gross stock compensation expense with actual forfeitures recognized as they occur, as well as certain classifications on the statement of

F-13

Table of Contents

cash flows. This ASU is effective for reporting periods beginning after December 15, 2016. We will adopt the new standard as required effective January 1, 2017. The new standard requires prospective recognition of excess tax benefits and deficiencies resulting from share based compensation awards vesting and exercises be recognized in our consolidated statements of operations. Previously, these amounts were recognized in additional paid in capital, and were not material to our consolidated financial statements. Excess tax benefits from share based compensation awards will continue to be reported as an operating activity, and cash paid on employees' behalf related to shares withheld for tax purposes will continue to be classified as a financing activity on the statement of cash flows. In addition, forfeitures will be recognized as they occur as permitted by the new standard. We do not expect that the adoption of this ASU will have a material impact on our consolidated financial statements.

In May 2014, the FASB issued ASU No. 2014-09, Revenue from Contracts with Customers (Topic 606), which outlines a comprehensive model for entities to use in accounting for revenue arising from contracts with customers. This ASU clarifies the principles for recognizing revenue by, among other things, removing inconsistencies in revenue requirements, improving comparability of revenue recognition practices across entities and industries and providing improved disclosure requirements. In July 2015, the FASB approved a one year deferral of the effective date for this ASU to interim and annual reporting periods beginning after December 15, 2017. In March 2016, the FASB issued ASU No. 2016-08, Revenue from Contracts with Customers (Topic 606): Principal versus Agent Considerations (Reporting Revenue Gross versus Net), which clarifies how an entity should identify the unit of accounting for the principal versus agent evaluation and how it should apply the control principle to certain types of arrangements, such as service transactions. These ASUs may be applied retrospectively to each prior period (full retrospective) or retrospectively with the cumulative effect recognized as of the date of initial application (modified retrospective). We will adopt the new ASUs as required effective January 1, 2018 and currently expect to apply the modified retrospective approach. While we are continuing to assess the impact adopting these ASUs (and related clarifying guidance issued by the FASB) will have on our consolidated financial statements, we currently believe its adoption will not have a material impact on the timing of our revenue recognition. We do expect the adoption will result in expanded disclosures related to the nature, amount, timing, and uncertainty of revenue and cash flows arising from our contracts with customers that are included in the scope of these ASUs. A substantial portion of our revenue relates to contracts with residents that are generally short term in nature and fall under ASC Topic 840, Leases, which are specifically excluded from the scope of ASU No. 2014-09. Our contracts with residents and other customers that are included in the scope of these ASUs are also generally short term in nature and revenue is recognized when services are provided. As we complete our evaluation of these ASUs, new information may arise that could change our current understanding of the impact to revenue recognized. Additionally, we will continue to monitor industry activities and any additional guidance provided by regulators, standards setters and the accounting profession and will adjust our assessment and implementation plans accordingly.

In June 2016, the FASB issued ASU No. 2016-13, Financial Instruments-Credit Losses (Topic 326), which requires a financial asset or a group of financial assets measured at amortized cost basis, to be presented at the net amount expected to be collected. This ASU eliminates the probable initial recognition threshold and instead reflects an entity's current estimate of all expected credit losses. In addition, this ASU amends the current available for sale security other-than-temporary impairment model for debt securities. The length of time that the fair value of an available for sale debt security has been below the amortized cost will no longer impact the determination of whether a credit loss exists and credit losses will now be limited to the difference between a security's amortized cost basis and its fair value. This ASU is effective for reporting periods beginning after December 15, 2019. We are currently assessing the potential impact the adoption of this ASU will have on our consolidated financial statements.

In August 2016, the FASB issued ASU No. 2016-15, Statement of Cash Flows (Topic 230): Classification of Certain Cash Receipts and Cash Payments, which clarifies how companies present and classify certain cash receipts and cash payments in the statement of cash flows. ASU No. 2016-15 is effective for reporting periods beginning after December 15, 2017. We are currently assessing the potential impact the adoption of this ASU will have on our

consolidated financial statements.

In November 2016, the FASB issued ASU No. 2016-18, Statement of Cash Flows (Topic 230): Restricted Cash, which requires that the reconciliation of the beginning-of-period and end-of-period amounts shown in the statement of cash flows include restricted cash and restricted cash equivalent. In the event restricted cash is presented separately from cash and cash equivalents on the balance sheet, companies will be required to reconcile the amounts presented on the statement of cash flows to the amounts on the balance sheet and disclose information about the nature of the restrictions. ASU No. 2016-18 is effective for reporting periods beginning after December 15, 2017. We are currently assessing the potential impact the adoption of this ASU will have on our consolidated financial statements.

In January 2017, the FASB issued ASU No. 2017-01, Business Combinations (Topic 805), which clarifies the definition of a business to assist entities with evaluating whether transactions should be accounted for as acquisitions (or disposals) of assets or of businesses. The amendments in this ASU provide a screen to determine when an acquired set of

F-14

Table of Contents

activities is not a business. The screen requires that when substantially all of the fair value of the gross assets acquired (or disposed of) is concentrated in a single identifiable asset or a group of similar identifiable assets, the set is not a business. This ASU is effective for reporting periods beginning after December 15, 2017, with early adoption permitted. We are currently evaluating the impact adopting this ASU will have on our consolidated financial statements, but we expect that most future acquisitions, if completed with terms similar to historical transactions, will be treated as acquisitions of assets rather than as business combinations, as substantially all of the fair value of the assets we typically acquire is concentrated in real estate. In an acquisition of assets, certain acquisition costs are capitalized as opposed to expensed under business combination guidance.

Segment Information. We have two operating segments: (i) senior living communities and (ii) rehabilitation and wellness. In the senior living community segment, we operate for our own account or manage for the account of other independent living communities, assisted living communities and SNFs that are subject to centralized oversight and provide housing and services to elderly residents. In the rehabilitation and wellness operating segment we provide services in the inpatient setting and in outpatient clinics. We have determined that our two operating segments meet the aggregation criteria as prescribed under FASB ASC Topic 280, Segment Reporting, and therefore, we have determined that our business is comprised of one reportable segment, senior living. All of our operations and assets are located in the United States, except for the operations of our Cayman Islands organized captive insurance company subsidiary, which participates in our workers' compensation and professional and general liability insurance programs.

3. Property and Equipment

Property and equipment consists of the following:

| | December 31, 2016 | December 31, 2015 |
|-----------------------------------|-------------------------|-------------------------|
| Land | \$22,261 | \$25,410 |
| Buildings and improvements | 304,044 | 338,522 |
| Furniture, fixtures and equipment | 193,286 | 165,497 |
| Property and equipment, at cost | 519,591 | 529,429 |
| Accumulated depreciation | (167,662) | (145,571) |
| Property and equipment, net | \$351,929 | \$383,858 |

We recorded depreciation expense relating to our property and equipment of \$36,462, \$33,129 and \$29,434 for the years ended December 31, 2016, 2015 and 2014, respectively.

We review the carrying value of long lived assets for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. If there is an indication that the carrying value of an asset is not recoverable, we determine the amount of impairment loss, if any, by comparing the historical carrying value of the asset to its estimated fair value. We determine estimated fair value based on input from market participants, our experience selling similar assets, market conditions and internally developed cash flow models that our assets or asset groups are expected to generate, and we consider these estimates to be a Level 3 fair value measurement. As a result of our long lived assets impairment review, we recorded \$502, \$145 and \$589 of impairment charges to certain of our long lived assets in continuing operations for the years ended December 31, 2016, 2015 and 2014, respectively. The fair values of the impaired assets were \$337, \$319 and \$478 as of December 31, 2016, 2015 and 2014, respectively.

As of December 31, 2015, we had \$8,289 of assets related to our leased senior living communities included in our property and equipment that we subsequently sold during the year ended December 31, 2016 to Senior Housing Properties Trust or its subsidiaries, or SNH, for increased rent pursuant to the terms of our leases with SNH. As of December 31, 2016, we had \$7,255 of assets related to our leased senior living communities included in our property and equipment that we currently expect to request that SNH purchase from us for an increase in future rent; however,

SNH is not obligated to purchase such amounts. See Note 9 for more information regarding our leases with SNH.

4. Other Intangible Assets and Goodwill

Other Intangible assets. The other intangible assets balance is made up of management agreements, trademarks, resident agreements, liquor licenses and other intangible assets that we primarily acquired in connection with our acquisitions of senior living communities. The changes in the carrying amount of our other intangible assets for the years ended December 31, 2016 and 2015 are as follows:

F-15

Table of Contents

| | December 31, 2016 | | | December 31, 2015 | | |
|------------------------------------|-----------------------|--------------------------|-----|-----------------------|--------------------------|-------|
| | Gross Carrying Amount | Accumulated Amortization | Net | Gross Carrying Amount | Accumulated Amortization | Net |
| Indefinite lived intangible assets | 191 | — | 191 | 191 | — | 191 |
| Definite lived intangible assets | 1,866 | (1,590) | 276 | 2,469 | (726) | 1,743 |
| | 2,057 | (1,590) | 467 | 2,660 | (726) | 1,934 |

We amortize definite lived intangible assets using the straight line method over the useful lives of the assets which have identifiable useful lives commencing on the date of acquisition. Total amortization expense for definite lived intangible assets for the years ended December 31, 2016, 2015 and 2014 was \$1,590, \$726 and \$2,440, respectively. At December 31, 2016, the weighted average amortization period remaining for these intangible assets is approximately one year. Amortization expense is estimated to be approximately \$196 in 2017 and \$80 in 2018.

Goodwill. We evaluated the recoverability of goodwill annually in the fourth quarter of each fiscal year, or more frequently if events or changes in circumstances indicated that goodwill might have been impaired. We evaluated goodwill for impairment at the reporting unit level; our reporting units are equivalent to our two operating segments. All of our goodwill was included in our senior living reporting unit. As part of the preparation of our 2015 third quarter financial statements, we determined that, as a result of the significant decline in our stock price subsequent to the announcement of our financial and operating results for the second quarter of 2015 and the overall decline in values of other comparable publicly traded senior living operating companies, potential indicators of impairment existed and an interim assessment of goodwill for impairment was completed.

In step one of the goodwill impairment test, or Step 1, the carrying value of a reporting unit is compared to its estimated fair value. We estimated the fair value of the senior living reporting unit using a weighting of fair values derived from the income approach and the market approach. The results of the Step 1 analysis indicated that the carrying value of the senior living reporting unit exceeded its estimated fair value. Accordingly, we performed step two of the goodwill impairment test, or Step 2.

In Step 2, the fair value of a reporting unit is allocated to all of the assets and liabilities of the reporting unit, including any unrecognized intangible assets, in a hypothetical analysis that calculates the implied fair value of goodwill as if the reporting unit had been acquired in a business combination. If the implied fair value of goodwill is less than the carrying value of goodwill, an impairment loss is recognized for the difference. As a result of our Step 2 analysis, the goodwill in our senior living reporting unit was determined to have an implied fair value of zero, and therefore we recorded a non-cash charge for goodwill impairment of \$25,344 for the year ended December 31, 2015, which is included in goodwill impairment in our consolidated statements of operations, and which amount represents the then full balance of our goodwill included in our continuing operations immediately prior to recording the charge. We also recorded additional goodwill impairment of \$63, which is included in loss from discontinued operations in our consolidated statements of operations. These non-cash charges for goodwill impairment did not impact our compliance with our then existing debt covenants or our borrowing capacity under our then existing secured revolving credit facility.

Fair values used in our goodwill impairment analysis were determined primarily using discounted cash flow models that incorporate assumptions for short and long term revenue growth rates, operating margins and discount rates, which represented our best estimates of the then current and forecasted market conditions, our cost structure, and the implied rate of return that our management believed a market participant would require for an investment in a company having similar risks and business characteristics to the reporting unit being assessed, all of which are considered to be Level 3 fair value measurements.

We continue to not have any goodwill recorded on our consolidated balance sheet as of December 31, 2016.

F-16

Table of Contents

5. Income Taxes

Significant components of our deferred tax assets and liabilities at December 31, 2016 and 2015, were as follows:

| | 2016 | 2015 |
|--|-----------|----------|
| Non-current deferred tax assets: | | |
| Continuing care contracts | 491 | 621 |
| Allowance for doubtful accounts | 1,254 | 1,448 |
| Deferred gains on sale lease back transactions | 33,121 | 2,236 |
| Insurance reserves | 3,976 | 4,303 |
| Tax credits | 21,647 | 19,426 |
| Tax loss carry forwards | 41,160 | 61,911 |
| Impairment of securities | 360 | 371 |
| Depreciable assets | 1,795 | 975 |
| Goodwill | 6,478 | 6,699 |
| Other | 1,152 | 4,272 |
| Total non-current deferred tax assets before valuation allowance | 111,434 | 102,262 |
| Valuation allowance: | (100,524) | (90,726) |
| Total non-current deferred tax assets | 10,910 | 11,536 |
| Non-current deferred tax liabilities: | | |
| Lease expense | (9,660) | (10,531) |
| Employee stock grants | (72) | (88) |
| Identifiable intangibles/other liabilities | (1,178) | (917) |
| Total non-current deferred tax liabilities | (10,910) | (11,536) |
| Net deferred tax asset (liabilities) | \$ — | \$ — |

As of December 31, 2016, our federal net operating loss carry forwards, which are scheduled to begin expiring in 2026 if unused, were approximately \$71,156, and our tax credit carry forwards, which begin expiring in 2022 if unused, were approximately \$21,647. We have an additional \$518 of federal net operating loss carry forwards not reflected in the deferred taxes table above attributable to unvested stock grants which will be recorded as an increase to additional paid in capital once they are realized in accordance with FASB ASC Topic 718. The Internal Revenue Service, or IRS, has completed its examination of our 2014 federal income tax return and there were no adjustments. At December 31, 2016, our federal tax returns filed for the 2013 and 2015 tax years are subject to examination and our net operating loss carry forwards and tax credit carry forwards are subject to adjustment by the IRS. Management assessed the available positive and negative evidence to estimate if sufficient future taxable income will be generated to realize the existing deferred tax assets. An important piece of objective negative evidence evaluated was the significant losses incurred over the two year period ending December 31, 2014 and that, as a result of those losses, we expected to be, and it turned out were, in a cumulative loss position for the three year period ending December 31, 2015. That objective negative evidence is difficult to overcome and would require a substantial amount of objectively verifiable positive evidence beyond projections of future income to support the realizability of our deferred tax assets. Accordingly, on the basis of that assessment, as of December 31, 2014, we determined it was more likely than not that our net deferred tax assets would not be realized and concluded that a full valuation allowance was required. As of and for the years ended December 31, 2016 and 2015, management continued to assess the available positive and negative evidence to estimate if sufficient future taxable income would be generated to realize the existing deferred tax assets. On the basis of that assessment we determined it was more likely than not that our net deferred tax assets would not be realized and concluded that a full valuation allowance was required. In the future, if we believe that we will more likely than not realize the benefit of these deferred tax assets, we will adjust our valuation allowance and recognize an income tax benefit, which may affect our results of operations.

Table of Contents

The changes in our valuation allowance for deferred tax assets were as follows:

| | Balance at Beginning of Period | Amounts Charged To Expense | Amounts Charged Off, Net of Recoveries | Amounts Charged (Credited) to Equity | Balance at End of Period |
|------------------------------|--|-------------------------------------|--|--|-----------------------------|
| Year Ended December 31, 2014 | \$ 3,603 | \$ 73,470 | \$ | — \$ (152) | \$ 76,921 |
| Year Ended December 31, 2015 | \$ 76,921 | \$ 13,491 | \$ | — \$ 314 | \$ 90,726 |
| Year Ended December 31, 2016 | \$ 90,726 | \$ 10,021 | \$ | — \$ (223) | \$ 100,524 |

For the year ended December 31, 2016, we recognized a provision for income taxes from continuing operations of \$2,351, which consists of current state tax expense of \$2,670, related primarily to the gain on sale for tax purposes associated with our June 2016 sale and leaseback transaction with SNH, net of federal intraperiod tax allocation benefits totaling \$319 related to the unrealized gains on our available for sale securities and discontinued operations. We have not recognized any federal income tax expense attributable to federal taxable income because in the year ended December 31, 2016, such income and expense were offset by our federal net operating loss carry forwards and tax credit carry forwards. We recognized an immaterial amount of tax expense from discontinued operations in 2016 and 2014 and did not recognize any income tax expense or benefit from our discontinued operations in 2015. See Note 9 for further information regarding the June 2016 sale and leaseback transaction with SNH.

The provision for income taxes from continuing operations is as follows:

| | Years Ended December 31, | | |
|--|-----------------------------|---------|----------|
| | 2016 | 2015 | 2014 |
| Current tax provision: | | | |
| Federal | \$(319) | \$— | \$— |
| State | \$2,670 | \$1,018 | \$848 |
| Total current tax provision | 2,351 | 1,018 | 848 |
| Deferred tax (benefit) provision: | | | |
| Federal | — | 114 | 43,040 |
| State | — | (470) | 12,497 |
| Total deferred tax (benefit) provision | — | (356) | 55,537 |
| Total tax provision | \$2,351 | \$662 | \$56,385 |

The principal reasons for the difference between our effective tax rate on continuing operations and the U.S. federal statutory income tax rate are as follows:

| | For the years ended December 31, | | |
|--|-------------------------------------|---------|---------|
| | 2016 | 2015 | 2014 |
| Taxes at statutory U.S. federal income tax rate | (35.0)% | (35.0)% | (35.0)% |
| State and local income taxes, net of federal tax benefit | (0.7)% | 1.0 % | (6.5)% |
| Tax credits | (9.1)% | (3.4)% | (5.4)% |
| Change in valuation allowance | 55.6 % | 32.7 % | 287.5 % |
| Goodwill | — % | 4.1 % | — % |
| Other differences, net | 1.3 % | 2.2 % | 4.9 % |
| Effective tax rate | 12.1 % | 1.6 % | 245.6 % |

We utilize a two step process for the measurement of uncertain tax positions that have been taken or are expected to be taken on a tax return. The first step is a determination of whether the tax position should be recognized in the financial statements. The second step determines the measurement of the tax position. A reconciliation of the beginning and ending amount of unrecognized tax benefits is summarized as follows for the years ended December 31, 2016, 2015 and 2014:

Table of Contents

| | For the years ended December 31, | |
|---|--|---------|
| | 2015 | 2014 |
| Unrecognized tax benefits at January 1 | \$-1,379 | \$1,245 |
| Decreases for tax positions of prior years | —(1,379) | — |
| Additions for tax positions of current year | — | 134 |
| Unrecognized tax benefits at December 31 | \$-— | \$1,379 |

As of December 31, 2016, there are no unrecognized tax benefits.

We recognize interest and penalties related to uncertain tax positions in income tax expense and such amounts were not material for the years ended December 31, 2016, 2015 and 2014.

6. Earnings Per Share

We calculated EPS for the years ended December 31, 2016, 2015 and 2014 using the weighted average number of common shares outstanding during the periods. When applicable, diluted EPS reflects the more dilutive earnings per common share amount calculated using the two class method or the treasury stock method. The years ended December 31, 2016, 2015 and 2014 had 866,041, 604,200 and 482,844, respectively, of potentially dilutive restricted unvested common shares that were not included in the calculation of diluted EPS because to do so would have been antidilutive.

7. Fair Values of Assets and Liabilities

Our assets recorded at fair value have been categorized based upon a fair value hierarchy in accordance with FASB ASC Topic 820, Fair Value Measurements and Disclosures. We apply the following fair value hierarchy, which prioritizes the inputs used to measure fair value into three levels.

Level 1 inputs are quoted prices (unadjusted) in active markets for identical assets or liabilities that we have the ability to access at the measurement date.

Level 2 inputs are inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly or indirectly. Level 2 inputs include quoted prices for similar assets and liabilities in active markets and quoted prices in inactive markets.

Level 3 inputs are unobservable inputs for the asset or liability in which there is little, if any, market activity for the asset or liability at the measurement date.

Recurring Fair Value Measures

The tables below present the assets measured at fair value at December 31, 2016 and 2015 categorized by the level of inputs used in the valuation of each asset.

Table of Contents

| Description | As of December 31, 2016 | | | |
|---|-------------------------|---|---|--|
| | Total | Quoted Prices in Active Markets for Identical (Level 1) | Significant Other Observable Inputs (Level 2) | Significant Unobservable Inputs (Level 3) |
| Cash equivalents ⁽¹⁾ | \$17,702 | \$17,702 | \$ | —\$ |
| Available for sale securities: ⁽²⁾ | | | | — |