

SECURITIES AND EXCHANGE COMMISSION

FORM 10-Q

Quarterly report pursuant to sections 13 or 15(d)

Filing Date: **2012-11-13** | Period of Report: **2012-09-30**  
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FILER

**ADCARE HEALTH SYSTEMS INC**

CIK: [1004724](#) | IRS No.: [311332119](#) | State of Incorporation: **OH** | Fiscal Year End: **1231**  
Type: **10-Q** | Act: **34** | File No.: [001-33135](#) | Film No.: [121199846](#)  
SIC: **8051** Skilled nursing care facilities

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# UNITED STATES SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

## FORM 10-Q

(Mark One)

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

For the quarterly period ended September 30, 2012

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

For the transition period from \_\_\_\_\_ to \_\_\_\_\_

Commission File Number 001-33135

### AdCare Health Systems, Inc.

(Exact name of registrant as specified in its charter)

**Ohio**

(State or other jurisdiction  
of incorporation)

**31-1332119**

(I.R.S. Employer Identification Number)

**1145 Hembree Road, Roswell, GA 30076**

(Address of principal executive offices)

**(678) 869-5116**

(Registrant's telephone number, including area code)

**Not Applicable**

(Former name, former address and former fiscal year, if changed since last report)

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

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes  No

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

Large accelerated filer

Accelerated filer

Non-accelerated filer

Smaller reporting company

(Do not check if a smaller reporting company)

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

Indicate the number of shares outstanding of each of the issuer’s classes of common stock, as of the latest practicable date.

As of October 31, 2012: 14,658,361 shares of common stock with no par value were outstanding.

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**AdCare Health Systems, Inc.**  
**Form 10-Q**  
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**Part I. Financial Information**

## Item 1. Financial Statements

**ADCARE HEALTH SYSTEMS, INC. AND SUBSIDIARIES**  
**CONDENSED CONSOLIDATED BALANCE SHEETS**  
*(Amounts in 000s)*

	<u>September 30,</u> <u>2012</u>	<u>December 31,</u> <u>2011</u>
	<u>(Unaudited)</u>	
<b><u>ASSETS</u></b>		
Current Assets:		
Cash and cash equivalents	\$ 9,884	\$ 7,364
Restricted cash and cash equivalents	2,825	1,883
Accounts receivable, net of allowance of \$3,099 and \$1,346	30,397	18,759
Prepaid expenses and other	892	663
Assets of disposal group held for sale	–	47
Total current assets	<u>43,998</u>	<u>28,716</u>
Restricted cash and investments	5,748	4,870
Property and equipment, net	166,708	105,143
Intangible assets – bed licenses, net	2,558	1,189
Intangible assets – lease rights, net	7,658	8,460
Goodwill	906	906
Escrow deposits for acquisitions	812	3,172
Lease deposits	1,704	1,685
Deferred loan costs, net	6,630	4,818
Other assets	169	122
Total assets	<u>\$ 236,891</u>	<u>\$ 159,081</u>
<b><u>LIABILITIES AND STOCKHOLDERS' EQUITY</u></b>		
Current Liabilities:		
Current portion of notes payable and other debt	\$ 11,991	\$ 4,567
Revolving credit facilities and lines of credit	1,363	7,343
Accounts payable	20,324	12,075
Accrued expenses	12,615	9,858
Liabilities of disposal group held for sale	–	240
Total current liabilities	<u>46,293</u>	<u>34,083</u>
Notes payable and other debt, net of current portion:		
Senior debt, net of discounts	134,003	87,771
Convertible debt, net of discounts	22,746	14,614
Revolving credit facilities	9,076	1,308
Other debt	887	1,400

Derivative liability	3,231	1,889
Other liabilities	1,728	2,437
Deferred tax liability	99	86
Total liabilities	<u>218,063</u>	<u>143,588</u>
Commitments and contingencies (Note 14)	–	–
Stockholders' equity:		
Preferred stock, no par value; 1,000 shares authorized; no shares issued or outstanding	–	–
Common stock and additional paid-in capital, no par value; 29,000 shares authorized; 14,657 and 12,802 shares issued and outstanding	41,002	35,047
Accumulated deficit	<u>(19,943)</u>	<u>(18,713)</u>
Total stockholders' equity	21,059	16,334
Noncontrolling interest in subsidiaries	<u>(2,231)</u>	<u>(841)</u>
Total equity	18,828	15,493
Total liabilities and stockholders' equity	<u>\$ 236,891</u>	<u>\$ 159,081</u>

See accompanying notes to condensed consolidated financial statements

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

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2012	2011	2012	2011
<b>Revenues:</b>				
Patient care revenues	\$ 61,342	\$ 40,192	\$ 165,793	\$ 104,596
Management revenues	428	330	1,154	1,312
Total revenues	<u>61,770</u>	<u>40,522</u>	<u>166,947</u>	<u>105,908</u>
<b>Expenses:</b>				
Cost of services (exclusive of facility rent, depreciation and amortization)	49,164	32,637	131,514	84,916
General and administrative	4,328	3,267	13,188	9,358
Facility rent expense	2,080	1,937	6,196	5,787
Depreciation and amortization	2,112	836	5,370	2,188
Salary retirement and continuation costs	38	–	38	622
Total expenses	<u>57,722</u>	<u>38,677</u>	<u>156,306</u>	<u>102,871</u>
Income from Operations	<u>4,048</u>	<u>1,845</u>	<u>10,641</u>	<u>3,037</u>
<b>Other Income (Expense):</b>				
Interest expense, net	(3,992)	(2,223)	(10,312)	(5,511)

Acquisition costs, net of gains	(342)	(1,147)	(1,160)	(789)
Derivative gain (loss)	(2,105)	4,745	(1,342)	807
Loss on extinguishment of debt	–	(58)	–	(136)
Other income (expense)	271	(20)	242	567
Total other income (expense), net	(6,168)	1,297	(12,572)	(5,062)
Income (Loss) from Continuing Operations Before Income Taxes				
Taxes	(2,120)	3,142	(1,931)	(2,025)
Income Tax Expense	(118)	(204)	(217)	(414)
Income (Loss) from Continuing Operations	(2,238)	2,938	(2,148)	(2,439)
Loss from discontinued operations	(202)	(158)	(472)	(285)
Net Income (Loss)	(2,440)	2,780	(2,620)	(2,724)
Net Loss Attributable to Noncontrolling Interests	738	748	1,390	1,090
Net Income (Loss) Attributable to AdCare Health Systems	\$ (1,702)	\$ 3,528	\$ (1,230)	\$ (1,634)
Net Income (Loss) per Common Share – Basic:				
Continuing Operations	\$ (0.10)	\$ 0.33	\$ (0.05)	\$ (0.14)
Discontinued Operations	(0.01)	(0.01)	(0.03)	(0.03)
	\$ (0.11)	\$ 0.32	\$ (0.08)	\$ (0.17)
Net Income (Loss) per Common Share – Diluted:				
Continuing Operations	\$ (0.10)	\$ 0.28	\$ (0.05)	\$ (0.14)
Discontinued Operations	(0.01)	(0.01)	(0.03)	(0.03)
	\$ (0.11)	\$ 0.27	\$ (0.08)	\$ (0.17)

See accompanying notes to condensed consolidated financial statements

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

	Common Stock and Additional	Common Stock Shares	Paid-in Capital	Accumulated Deficit	Total Stockholders' Equity	Noncontrolling Interests	Total Equity
Balance, January 1, 2012		12,802	\$ 35,047	\$ (18,713)	\$ 16,334	\$ (841)	\$ 15,493
Common stock dividend adjustment		88					
Nonemployee warrants for services		–	441	–	441	–	441

Stock based compensation expense		615	–	615	–	615
Public stock offering, net	1,165	3,837	–	3,837	–	3,837
Exercises of options and warrants	95	137	–	137	–	137
Stock issued in acquisition	187	750		750		750
Issuance of restricted stock	320	175	–	175	–	175
Net loss	–	–	(1,230)	(1,230)	(1,390)	(2,620)
Balance, September 30, 2012	14,657	\$ 41,002	\$ (19,943)	\$ 21,059	\$ (2,231)	\$ 18,828

See accompanying notes to condensed consolidated financial statements

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

	Nine Months Ended September 30,	
	2012	2011
Cash flows from operating activities:		
Net Loss	\$ (2,620)	\$ (2,724)
Net Loss from discontinued operations	472	285
Net Loss from continuing operations	(2,148)	(2,439)
Adjustments to reconcile net loss from continuing operations to net cash provided by operating activities:		
Depreciation and amortization	5,370	2,188
Non cash settlement gain	(361)	–
Warrants issued for services	1	162
Stock based compensation expense	615	579
Provision for leases in excess of cash	419	558
Amortization of deferred financing costs	1,742	599
Amortization of debt discounts	646	663
Derivative (gain) loss	1,342	(807)
Loss on debt extinguishment	–	136
Deferred tax expense	13	163
(Gain) loss on disposal of assets	(2)	126
Gain on acquisitions	–	(898)
Provision for bad debts	2,021	593
Other noncash items	40	59
Changes in certain assets and liabilities, net of acquisitions:		
Accounts receivable	(13,199)	(8,305)
Prepaid expenses and other	(229)	(159)
Other assets	133	(525)
Accounts payable and accrued expenses	9,368	8,433
Net cash provided by operating activities – continuing operations	5,771	1,126

Net cash used in operating activities – discontinued operations	(648)	(96)
Net cash provided by operating activities	5,123	1,030
Cash flows from investing activities:		
Change in restricted cash and investments	677	546
Acquisitions	(13,467)	(11,050)
Proceeds from sale of assets	50	–
Purchase of property and equipment	(4,191)	(2,732)
Net cash used in investing activities	(16,931)	(13,236)
Cash flows from financing activities:		
Proceeds from debt	13,261	7,313
Debt issuance costs	(740)	(389)
Change in line of credit	1,600	5,770
Exercise of warrants and options	137	6,798
Proceeds from stock issuances, net	3,837	–
Repayment of notes payable	(3,620)	(1,013)
Net cash provided by financing activities – continuing operations	14,475	18,479
Net cash used in financing activities – discontinued operations	(147)	(134)
Net cash provided by financing activities	14,328	18,345
Net Change in Cash	2,520	6,139
Cash, Beginning	7,364	3,911
Cash, Ending	\$ 9,884	\$ 10,050
Supplemental Disclosure of Cash Flow Information:		
Cash paid during the period for:		
Interest	\$ 7,633	\$ 4,246
Income Taxes	\$ 217	\$ 197
Supplemental Disclosure of Non-cash Activities:		
Acquisitions in exchange for debt and equity instruments	\$ 46,605	\$ 48,826
Warrants issued for financing costs	\$ 439	\$ 330
Restricted stock issued for financing costs	\$ 175	\$ –
Other assets acquired in exchange for debt	\$ 4,908	\$ 5,063

See accompany notes to condensed consolidated financial statements.

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## ADCARE HEALTH SYSTEMS, INC. AND SUBSIDIARIES

Notes to Condensed Consolidated Financial Statements  
(Unaudited)

### NOTE 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

#### *Basis of Presentation*



The accompanying unaudited condensed consolidated financial statements have been prepared in accordance with U.S. generally accepted accounting principles for interim financial information and with the instructions to Form 10-Q and Rule 8-03 of Regulation S-X. Accordingly, they do not include all of the information or notes required for complete annual financial statements and should be read in conjunction with the AdCare Health Systems, Inc.'s audited consolidated financial statements and notes included in AdCare Health Systems, Inc.'s Annual Report on Form 10-K for the year ended December 31, 2011 (the "Annual Report"). These statements include the accounts of AdCare Health Systems, Inc. ("AdCare") and its controlled subsidiaries (collectively with AdCare, the "Company" or "we"). Controlled subsidiaries include AdCare's majority owned subsidiaries and variable interest entities ("VIE") in which AdCare has control as primary beneficiary.

All inter-company accounts and transactions were eliminated in the consolidation. In the opinion of the Company's management, all adjustments considered for a fair presentation are included and are of a normal recurring nature. The preparation of interim financial statements requires management to make estimates and assumptions that affect certain reported amounts. Operating results for the three and nine months ended September 30, 2012 are not necessarily indicative of the results that may be expected for the year ending December 31, 2012. Certain prior year amounts have been reclassified to conform to the current year presentation.

### *Earnings per Share*

Basic earnings per share is computed by dividing net income or loss by the weighted-average number of common shares outstanding during the period.

Diluted earnings per share is similar to basic earnings per share except net income or loss is adjusted by the impact of the assumed issuance of common shares upon conversion or exercise of convertible or exercisable securities and the weighted-average number of common shares outstanding includes potentially dilutive securities, such as options, warrants, non-vested shares, and additional shares issuable under convertible notes outstanding during the period when such potentially dilutive securities are not anti-dilutive. Potentially dilutive securities from options, warrants and non-vested shares are calculated in accordance with the treasury stock method, which assumes that proceeds from the exercise of all options and warrants with exercise prices exceeding the average market value are used to repurchase common stock at market value. The incremental shares remaining after the proceeds are exhausted represent the potentially dilutive effect of the securities. Potentially dilutive securities from convertible debt are calculated based on the assumed issuance at the beginning of the period, as well as any adjustment to income that would result from their assumed issuance.

	Three Months Ended September 30,					
	2012			2011		
	Income (loss)	Shares (1)	Per Share	Income (loss)	Shares (1)	Per Share
<b>(Amounts in 000s, except per share data)</b>						
<b>Continuing Operations:</b>						
Income (loss) from continuing operations	\$ (2,238)			\$ 2,938		
Net loss attributable to noncontrolling interests	738			748		
Basic income (loss) from continuing operations	\$ (1,500)	14,508	\$ (0.10)	\$ 3,686	11,275	\$ 0.33
Effect from options, warrants and non-vested shares	-	-		-	1,111	
Effect from assumed issuance of convertible shares (2)	-	-		-	938	
Diluted net income (loss) from continuing operations	\$ (1,500)	14,508	\$ (0.10)	\$ 3,686	13,324	\$ 0.28

**Discontinued Operations:**

Basic loss from discontinued operations	\$	(202)	14,508	\$	(0.01)	\$	(158)	11,275	\$	(0.01)
Diluted loss from discontinued operations	\$	(202)	14,508	\$	(0.01)	\$	(158)	11,275	\$	(0.01)

**Net Income (Loss) Attributable to AdCare:**

Basic net income (loss)	\$	(1,702)	14,508	\$	(0.11)	\$	3,528	11,275	\$	0.32
Diluted net income (loss)	\$	(1,702)	14,508	\$	(0.11)	\$	3,528	13,324	\$	0.27

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(Amounts in 000s, except per share data)	Nine Months Ended September 30,					
	2012			2011		
	Income (loss)	Shares (1)	Per Share	Income (loss)	Shares (1)	Per Share
<b>Continuing Operations:</b>						
Loss from continuing operations	\$	(2,148)		\$	(2,439)	
Net loss attributable to noncontrolling interests		1,390			1,090	
Basic loss from continuing operations	\$	(758)	13,820	\$	(1,349)	9,923
Effect from options, warrants and non-vested shares		-	-		-	-
Effect from assumed issuance of convertible shares (2)		-	-		-	-
Diluted loss from continuing operations	\$	(758)	13,820	\$	(1,349)	9,923
<b>Discontinued Operations:</b>						
Basic loss from discontinued operations	\$	(472)	13,820	\$	(0.03)	9,923
Diluted loss from discontinued operations	\$	(472)	13,820	\$	(0.03)	9,923
<b>Net Income (Loss) Attributable to AdCare:</b>						
Basic loss	\$	(1,230)	13,820	\$	(0.08)	9,923
Diluted loss	\$	(1,230)	13,820	\$	(0.08)	9,923

(1) The weighted average shares outstanding include retroactive adjustments for the stock dividends paid on October 22, 2012 and October 1, 2011 (See Note 10).

(2) The impact of the conversion of the subordinated convertible notes issued in 2010, 2011 and 2012 were excluded in those periods where the impact would be anti-dilutive.

**Intangible Assets and Goodwill**

There have been no required impairment adjustments to intangible assets and goodwill during the nine months ended September 30, 2012.

Intangible assets consist of the following:

September 30, 2012

December 31, 2011

Amounts in (000s)	Gross		Net	Gross		Net
	Carrying Amount	Accumulated Amortization	Carrying Amount	Carrying Amount	Accumulated Amortization	Carrying Amount
Lease Rights	\$ 9,545	\$ 1,887	\$ 7,658	\$ 9,545	\$ 1,085	\$ 8,460
Bed Licenses (included in property and equipment)	41,061	1,412	39,649	26,149	533	25,616
Bed Licenses - Separable	2,558	–	2,558	1,189	–	1,189
Totals	\$ 53,164	\$ 3,299	\$ 49,865	\$ 36,883	\$ 1,618	\$ 35,265

For the nine months ended September 30, 2012, amortization expense was approximately \$0.9 million for bed licenses included in property and equipment. For the nine months ended September 30, 2012 and 2011, amortization expense was \$0.8 million and \$0.7 million, respectively, for lease rights. Estimated amortization expense for each of the following years ending December 31 is as follows:

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(Amounts in 000s)	Lease Rights	Bed Licenses
2012 (remainder)	\$ 267	\$ 358
2013	1,069	1,433
2014	1,010	1,433
2015	885	1,433
2016	885	1,433
Thereafter	3,542	33,559
	\$ 7,658	\$ 39,649

### *Compensated Absences*

In 2012, the Company removed the ability for employees to accumulate earned but unused vacation beyond the current calendar year. As a result, vacation time previously accumulated must be used by the employee by December 31, 2012 or it will be forfeited. Management has estimated the potential forfeitures and has adjusted the vacation accrual accordingly.

### **NOTE 2. LIQUIDITY AND PROFITABILITY**

The Company had operating income of approximately \$4.0 million and \$10.6 million for the three and nine months ended September 30, 2012, respectively, compared to operating income of approximately \$1.8 million and \$3.0 million for the three and nine months ended September 30, 2011, respectively. The Company had a net loss of approximately \$1.7 million and \$1.2 million for the three and nine months ended September 30, 2012, respectively, and net income of \$3.5 million and a net loss of \$1.6 million for the three and nine months ended September 30, 2011, respectively. The Company had negative working capital of approximately \$2.3 million at September 30, 2012. Approximately \$3.0 million of the negative working capital ratio is related to short term debt under a VIE which the Company does not guarantee. (See Note 12). The Company's ability to sustain profitable operations is dependent on continued growth in revenue and controlling costs.

Management's plans for increasing liquidity and profitability in future years include the following:

- increasing facility occupancy and improving the quality mix by increasing Medicare patients and further optimizing our newly acquired facilities;

- acquiring additional long term care facilities with existing cash flowing operations to expand our operations; and
- refinancing debt where possible on longer terms to obtain more favorable terms.

Management believes that the foregoing actions, if taken by the Company, should provide the opportunity for the Company to improve liquidity and profitability; however, there is no assurance that such actions will occur or, if they do occur, that they will result in improved liquidity or profitability. The consolidated financial statements do not include any adjustments that might result from the outcome of this uncertainty.

### NOTE 3. DISCONTINUED OPERATIONS

As part of the Company's strategy to focus on the growth of its skilled nursing segment, the Company decided in the fourth quarter of 2011 to exit the home health segment of the business. This segment represents less than 2% of total revenues for the Company over the past year. During the quarter ended September 30, 2012, the Company sold all the equipment of the home health segment for approximately \$50,000 and discontinued providing services resulting in an immaterial gain on sale.

### NOTE 4. SEGMENTS

The Company reports its operations in three segments: Skilled Nursing Facility ("SNF"), Assisted Living Facility ("ALF"), and Corporate & Other. The SNF and ALF segments provide services to individuals needing long-term care in a nursing home or assisted living setting, and the management of those facilities. The Corporate & Other segment engages in the management of facilities and accounting and IT services. We evaluate financial performance and allocate resources primarily based upon segment operating income (loss). Segment operating results excludes interest expense and other non-operating income and expenses. The table below sets forth our segment information for the three and nine months ended September 30, 2012 and 2011.

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(Amounts in 000s)	SNF	ALF	Corporate & Other	Eliminations	Total
<b>Three months ended</b>					
<b>September 30, 2012</b>					
Net revenues	\$ 57,978	\$ 3,364	\$ 3,505	\$ (3,077)	\$ 61,770
Cost of services	49,812	2,441	(12)	(3,077)	49,164
General and administrative	–	–	4,328	–	4,328
Facility rent expense	2,039	–	41	–	2,080
Depreciation and amortization	1,590	224	298	–	2,112
Salary retirement and continuation costs	–	–	38	–	38
Operating income/(loss)	\$ 4,537	\$ 699	\$ (1,188)	\$ –	\$ 4,048
<b>Three months ended</b>					
<b>September 30, 2011</b>					
Net revenues	\$ 37,729	\$ 2,463	\$ 2,349	\$ (2,019)	\$ 40,522
Cost of services	32,887	1,885	(116)	(2,019)	32,637
General and administrative	–	–	3,267	–	3,267
Facility rent expense	1,906	–	31	–	1,937
Depreciation and amortization	631	158	47	–	836

Operating income/(loss)	\$ 2,305	\$ 420	\$ (880)	\$ –	\$ 1,845
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**Nine months ended**

**September 30, 2012**

Net revenues	\$ 155,753	\$ 10,038	\$ 9,487	\$ (8,331)	\$ 166,947
Cost of services	132,582	7,362	(99)	(8,331)	131,514
General and administrative	–	–	13,188	–	13,188
Facility rent expense	6,065	–	131	–	6,196
Depreciation and amortization	4,075	654	641	–	5,370
Salary retirement and continuation costs	–	–	38	–	38
Operating income/(loss)	\$ 13,031	\$ 2,022	\$ (4,412)	\$ –	\$ 10,641
Total assets	\$ 169,546	\$ 29,181	\$ 38,164	\$ –	\$ 236,891

**Nine months ended**

**September 30, 2011**

Net revenues	\$ 97,382	\$ 7,214	\$ 7,646	\$ (6,334)	\$ 105,908
Cost of services	85,495	5,740	15	(6,334)	84,916
General and administrative	–	–	9,358	–	9,358
Facility rent expense	5,711	–	76	–	5,787
Depreciation and amortization	1,595	470	123	–	2,188
Salary retirement and continuation costs	–	–	622	–	622
Operating income/(loss)	\$ 4,581	\$ 1,004	\$ (2,548)	\$ –	\$ 3,037
Total assets	\$ 105,620	\$ 21,490	\$ 31,176	\$ –	\$ 158,286

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**NOTE 5. PROPERTY AND EQUIPMENT**

(Amounts in 000s)	Estimated Useful Lives (Years)	September 30, 2012	December 31, 2011
Buildings and improvements	5-40	\$ 151,951	\$ 96,065
Equipment	2-10	12,776	7,108
Land	–	11,274	7,636
Computer related	2-10	2,573	2,414
Construction in process	–	811	77
		179,385	113,300
Less: accumulated depreciation expense		11,265	7,624
Less: accumulated amortization expense		1,412	533
Property and equipment, net		\$ 166,708	\$ 105,143

For the nine months ended September 30, 2012 and 2011, depreciation and amortization expense was approximately \$4.6 million and \$1.5 million, respectively.

**NOTE 6. RESTRICTED CASH AND INVESTMENTS**

The following table sets forth the Company's various restricted cash, escrow deposits and investments:

(Amounts in 000s)	September 30, 2012	December 31, 2011
HUD escrow deposits	\$ 202	\$ 326
Funds held in trust for residents	21	45
Principal and interest escrow	247	-
Refundable escrow deposit	-	500
Collateral certificates of deposit	2,355	1,012
Total current portion	<u>2,825</u>	<u>1,883</u>
HUD reserve replacements	1,157	1,130
Reserves for capital improvements	2,292	1,767
Restricted investments for other debt obligations	2,299	1,973
Total noncurrent portion	<u>5,748</u>	<u>4,870</u>
Total restricted cash and investments	<u>\$ 8,573</u>	<u>\$ 6,753</u>

#### NOTE 7. ACCRUED EXPENSES

Accrued expenses consist of the following:

(Amounts in 000s)	September 30, 2012	December 31, 2011
Accrued payroll related	\$ 6,358	\$ 5,040
Accrued employee benefits	1,766	2,023
Real estate and other taxes	1,650	982
Other accrued expenses	2,841	1,813
	<u>\$ 12,615</u>	<u>\$ 9,858</u>

#### NOTE 8. NOTES PAYABLE AND OTHER DEBT

Notes payable and other debt consist of the following:

(Amounts in 000s)	September 30, 2012	December 31, 2011
Revolving credit facilities and lines of credit	\$ 10,439	\$ 8,651
Senior debt HUD	15,734	15,738
Senior debt USDA	38,158	38,717
Senior debt SBA	6,247	5,087
Senior debt bonds, net of discount	15,889	6,176
Senior debt other mortgage indebtedness	63,610	23,823
Other debt	7,243	4,197
Convertible debt issued in 2010, net of discount	10,737	10,105
Convertible debt issued in 2011	4,509	4,509
Convertible debt issued in 2012	7,500	-
Total	<u>180,066</u>	<u>117,003</u>

Less current portion of notes payable and other debt	11,991	4,567
Less current portion of revolving credit facility and lines of credit	1,363	7,343
Notes payable and other debt, net of current portion	<u>\$ 166,712</u>	<u>\$ 105,093</u>

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### ***Scheduled Maturities***

The following is a summary of the scheduled maturities of indebtedness as of September 30, 2012 for each of the next five years and thereafter:

<b>(Amounts in 000s)</b>		
2013	\$	13,354
2014		26,323
2015		24,531
2016		15,193
2017		26,316
Thereafter		75,693
		<u>181,410</u>
Less: unamortized discounts		(1,344)
	\$	<u>180,066</u>

Approximately \$23.7 million of the scheduled maturities in 2012, 2014 and 2015, relate to the subordinated convertible notes issued in 2010, 2011 and 2012. While management cannot predict with certainty, we anticipate that some holders of the subordinated convertible notes will elect to convert their subordinated convertible notes into common stock provided the common stock continues to trade above the applicable conversion price for such notes. The conversion prices are \$3.73, \$4.80 and \$3.97 for the subordinated convertible notes issued in 2010, 2011 and 2012, respectively. If all of the subordinated convertible notes had been converted to common stock at September 30, 2012, then the Company would have been required to issue approximately 6.0 million shares of common stock.

### ***Revolving Credit Facilities***

#### *Gemino Credit Agreement*

At December 31, 2011, the outstanding balance of approximately \$7.3 million for the revolving credit agreement was classified as current as a result of the required lockbox arrangement and subjective acceleration clauses.

On September 20, 2012, AdCare terminated and paid off all amounts outstanding under that certain Credit Agreement, dated October 29, 2010, between Gemino Healthcare Finance, LLC (“Gemino”) and AdCare (the “Gemino credit facility”). The Gemino credit facility was a secured credit facility for borrowings up to \$7.5 million, which was to mature on October 29, 2013. As of September 20, 2012, the amount outstanding in principal balance was approximately \$4.2 million which was paid from funds made available to AdCare from a new credit facility entered into with the PrivateBank and Trust Company (“PrivateBank”). Interest accrued on the principal balance outstanding of the Gemino credit facility at an annual rate equal to LIBOR rate plus the applicable margin of 4.75% to 5.00%, depending on the principal amount outstanding. The Gemino credit facility contained various financial covenants and other restrictions, including a fixed charge cover ratio and maximum

loan turn days, as well as borrowing base restrictions. No material early termination penalties were incurred by AdCare as a result of the termination.

#### *Gemino-Bonterra Amendment*

On September 20, 2012, ADK Bonterra/Parkview, LLC, a wholly owned subsidiary of AdCare (“Bonterra”), entered into a Second Amendment to the Credit Agreement with Gemino, which amended that certain Credit Agreement, dated April 27, 2011, between Bonterra and Gemino (the “Gemino-Bonterra credit facility”). The Gemino-Bonterra credit facility is a secured credit facility for borrowings up to \$2.0 million. The amendment extends the term of the Gemino-Bonterra credit facility from October 29, 2013 to January 31, 2014 and amends certain financial covenants regarding Bonterra’s fixed charge coverage ratio, maximum loan turn days and applicable margin. Interest accrues on the principal balance outstanding at an annual rate equal to LIBOR plus the applicable margin of 4.75% to 5.00%, depending upon the principal amount outstanding. As of September 30, 2012, approximately \$1.4 million was outstanding under the Gemino-Bonterra credit facility.

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#### *PrivateBank Credit Facility*

On September 20, 2012, in connection with the payoff of the Gemino credit facility, AdCare entered into a Loan and Security Agreement with PrivateBank. The PrivateBank credit facility provides for a three-year \$10.6 million principal amount senior secured revolving credit facility limited to certain borrowing base restrictions and offset by a \$0.1 million letter of credit.

The PrivateBank credit facility matures on September 20, 2015. Interest accrues on the principal balance thereof at an annual rate of the greater of 1% plus the prime interest rate per annum, or 5% per annum, and payments for the interest are payable monthly, commencing on October 1, 2012. In addition, there is a non-utilization fee of 0.5% of the unused portion of the available credit. The PrivateBank credit facility may be prepaid at any time without premium or penalty, provided that such prepayment is accompanied by a simultaneous payment of all accrued but unpaid interest through the date of prepayment. The PrivateBank credit facility is secured by a first priority security interest in the real property and improvements constituting nursing facilities owned and operated by AdCare. AdCare has unconditionally guaranteed all amounts owing under the PrivateBank credit facility.

Proceeds from the PrivateBank credit facility were used to pay off all amounts outstanding under (i) a separate \$2.0 million credit facility with PrivateBank under which certain subsidiaries of AdCare were borrowers and (ii) the Gemino credit facility.

The PrivateBank credit facility was modified in October 2012. (See Note 16.)

#### ***Mortgage Notes***

##### *Hearth and Home of Vandalia*

In connection with the Company’s January 2012 refinance of the assisted living facility located in Vandalia, Ohio known as Hearth and Home of Vandalia, a wholly owned subsidiary of AdCare obtained a term loan insured by U.S. Department of Housing and Urban Development (“HUD”) with a financial institution for a total amount of \$3.7 million that matures in 2041. The HUD term loan requires monthly principal and interest payments with a fixed interest rate of 3.74%. Deferred financing costs incurred on the term loan amounted to approximately \$0.2 million and are being amortized to interest expense



over the life of the loan. The HUD term loan has a prepayment penalty of 8% starting in 2014 declining by 1% each year through 2022.

#### *Woodland Manor*

In connection with the Company's January 2012 acquisition of the skilled nursing facility located in Springfield, Ohio, known as Woodland Manor, a wholly owned subsidiary of the Company entered into a loan agreement for \$4.8 million. The loan matures in December 2016 with a required final payment of approximately \$4.3 million and accrues interest at the LIBOR rate plus 4% with a minimum rate of 6% per annum. The loan requires monthly payments of principal and interest. Deferred financing costs incurred on the loan amounted to approximately \$0.1 million and are being amortized to interest expense over the life of the loan. The loan has a prepayment penalty of 5% through 2012 declining by 1% each year through 2015. The loan is secured by the Woodland Manor facility and guaranteed by AdCare.

#### *Little Rock, Northridge and Woodland Hills*

In connection with the Company's April 2012 acquisition of three skilled nursing facilities located in Arkansas known as Little Rock, Northridge and Woodland Hills, certain wholly owned subsidiaries of AdCare entered into a loan agreement for \$21.8 million with PrivateBank. The loan originally matured in March 2017 with a required final payment of approximately \$19.7 million and accrues interest at the LIBOR rate plus 4% with a minimum rate of 6% per annum. The loan requires monthly principal payments plus interest for total current monthly payments of approximately \$0.2 million. Deferred financing costs incurred on the loan amounted to approximately \$0.4 million and are being amortized to interest expense over the life of the loan. The loan has a prepayment penalty of 5% through 2012 declining by 1% each year through 2015. The loan is secured by the three facilities and guaranteed by AdCare. The Company has approximately \$1.8 million of restricted assets related to this loan.

On June 15, 2012, certain wholly owned subsidiaries of AdCare entered into a modification agreement with PrivateBank to modify the terms of the loan agreement. The loan modification agreement, among other things, amended the loan agreement to reflect a maturity date of March 30, 2013. The Company intends on refinancing this loan to a longer term. PrivateBank has informed us in writing that, in the event the loan was not refinanced through the U.S. Small Business Administration (the "SBA"), it would be the

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intent of PrivateBank to reinstate the March 30, 2017 maturity date.

#### *Abington Place*

In connection with the Company's June 2012 acquisition of the skilled nursing facility located in Little Rock, Arkansas known as Abington Place, a wholly owned subsidiary of AdCare entered into a short-term loan agreement for \$3.4 million with Metro City Bank. In August 2012, the maturity date was amended from September 2012 to January 2014. The note accrues interest at the prime rate plus 2.25% with a minimum rate of 6.25% per annum. Deferred financing costs incurred on the loan amounted to approximately \$0.1 million and are being amortized to interest expense over the life of the loan. The loan may be prepaid at any time without penalty. The loan was secured by the Abington Place facility and guaranteed by AdCare.

#### *Stone County*

In June 2012, a wholly owned subsidiary of AdCare, entered into each of: (i) a Loan Agreement with Metro City Bank (“Metro”) in the amount of \$1.3 million; (ii) a Loan Agreement with Metro in the amount of \$1.8 million; and (iii) a Loan Agreement with the Economic Development Corporation of Fulton County (the “CDC”), an economic development corporation working with the SBA. The purpose of these agreements was to refinance existing debt in the original principal amount of \$3.1 million used to acquire select assets of a 97-bed skilled nursing facility located in Arkansas known as the Stone County Nursing and Rehabilitation Facility.

The funding of the Metro loans for \$1.3 million and \$1.8 million occurred on June 8, 2012. The funding of the SBA loan for \$1.3 million occurred in July 2012, and the proceeds were used to satisfy the \$1.3 million Metro loan.

The \$1.8 million Metro loan matures in June 2022 and accrues interest an annual variable rate equal to the published Wall Street Journal prime rate plus 2.25% (with a minimum rate of 6.25% per annum). Deferred financing costs incurred on this loan amounted to approximately \$0.1 million and are being amortized to interest expense over the life of the loan. The Metro loan has a prepayment penalty of 10% for any prepayment through June 2013. The penalty is reduced by 1% each year thereafter until the tenth anniversary, after which there is no prepayment penalty. The Metro loan is secured by the Stone County Nursing and Rehabilitation Facility and is guaranteed by AdCare.

The SBA loan matures in July 2032 and accrues interest at a rate of 2.42% per annum. The SBA Loan is payable in equal monthly installments of principal and interest based on a twenty (20) year amortization schedule. The SBA loan may be prepaid, subject to prepayment premiums during the first 10 years. There are also annual fees associated with the SBA loan, including an SBA guarantee fee. The SBA Loan is secured by a second in priority security deed on the Stone County Nursing and Rehabilitation Facility and guarantees from AdCare, the SBA and a wholly owned subsidiary of AdCare.

#### *Glenvue*

In July 2012, a wholly owned subsidiary of AdCare financed the skilled nursing facility located in Glennville, Georgia known as Glenvue Health & Rehabilitation by entering into a loan agreement for \$6.6 million with PrivateBank . The loan matures in July 2014 with a required final payment of approximately \$6.4 million and accrues interest at an annual rate of the greater of 6.0% per annum; or the LIBOR rate plus 4.0% per annum. The loan requires monthly principal payments and interest. Deferred financing costs incurred on the loan amounted to approximately \$0.1 million and are being amortized to interest expense over the life of the loan. The loan is secured by the Glenvue facility and guaranteed by AdCare.

#### *Companions Specialized Care*

In August 2012, a wholly owned subsidiary of AdCare financed the skilled nursing facility located in Tulsa, Oklahoma known as Companions Specialized Care Center by entering into a loan agreement for \$5.0 million with Contemporary Healthcare Capital. The loan matures in August 2015 with a required final payment of \$5.0 million and accrues interest at a fixed rate of 8.5% per annum. Deferred financing costs incurred on the loan amounted to approximately \$0.2 million and are being amortized to interest expense over the life of the loan. The loan has a prepayment penalty of 5% during the first year of the term and 1% during the second year of the term. The loan is secured by the Companions Specialized Care facility and guaranteed by AdCare.

### ***Bonds***

#### *Eaglewood Village Bonds*

In April 2012, a wholly owned subsidiary of AdCare entered into a loan agreement with the City of Springfield in the State of Ohio (“City of Springfield”) pursuant to which City of Springfield lent to such subsidiary the proceeds from the sale of City of Springfield’ s Series 2012 Bonds. The Series 2012 Bonds consist of \$6.6 million in Series 2012A First Mortgage Revenue Bonds and \$0.6 million in Taxable Series 2012B First Mortgage Revenue Bonds. The Series 2012 Bonds were issued pursuant to an April 2012 Indenture of Trust between the City of Springfield and the Bank of Oklahoma. The Series 2012A Bonds mature in May 2042 and accrue interest at a fixed rate of 7.65% per annum. The Series 2012B Bonds mature in May 2021 and accrue interest at a fixed rate of 8.5% per annum. Deferred financing costs incurred on the loan amounted to approximately \$0.6 million and are being amortized to interest expense over the life of the loan. The loan is secured by the Company’ s assisted living facility located in Springfield, Ohio known as Eaglewood Village and guaranteed by AdCare. There is an original issue discount of approximately \$0.3 million and restricted assets of \$0.3 million related to this loan.

#### *Quail Creek*

In July 2012, a wholly owned subsidiary of AdCare financed the skilled nursing facility located in Oklahoma City, Oklahoma known as Quail Creek Nursing by the assumption of existing indebtedness under that certain Loan Agreement and Indenture of First Mortgage with The Bank of New York Mellon Global Corporate Trust, as assignee of The Liberty National Bank and Trust of that certain Bond Indenture, dated September 1, 1986, as amended as of September 1, 2001. The indebtedness under the Loan Agreement and Indenture consists of a principal amount of \$2.8 million. The loan matures in August 2016 and, accrues interest at a fixed rate of 10.25% per annum. The loan is secured by the Quail Creek facility.

#### **Other Debt**

##### *Eaglewood Village Promissory Note*

In January 2012, two wholly owned subsidiaries of AdCare issued a promissory seller note in the amount of \$0.5 million in connection with the January 2012 acquisition of the assisted living facility located in Springfield, Ohio. The note matures in January 2014 and requires a final payment of approximately \$0.5 million. The note bears interest at 6.5% per annum payable monthly beginning February 2012. The note requires monthly principal and interest payment. The note may be prepaid without penalty at any time.

##### *Cantone Promissory Notes*

In March 2012, AdCare issued an unsecured promissory note to Cantone Asset Management LLC in the amount of \$3.5 million. In April 2012, AdCare issued another promissory note to Cantone Asset Management LLC in the amount of \$1.5 million. In July 2012, these two promissory notes were refinanced through the issuance to Cantone Asset Management LLC in July 2012 of an 8% subordinated convertible note in principal amount of \$5.0 million.

##### *Strome Note*

On April 1, 2012, AdCare issued an unsecured promissory note in the amount of \$5.0 million to Strome Alpha Offshore Ltd. The promissory note matures in November 2012, and the Company anticipates paying off the promissory note with proceeds from the preferred stock offering discussed in Note 16. Interest accrues at a fixed rate of 10% per annum. The promissory note requires interest payments of approximately \$0.1 million on July 1, 2012 and October 1, 2012. The promissory note may be prepaid at any time without penalty.

#### **Convertible Debt**

##### *Convertible Debt Issued in July 2012*

AdCare entered into a Securities Purchase Agreement, dated as of June 28, 2012, with certain accredited investors pursuant to which the Company issued and sold such investors on July 2, 2012 an aggregate of \$7.5 million in principal amount of the Company's 8.0% subordinated convertible notes. The notes bear interest at 8% per annum and such interest is payable quarterly in cash in arrears beginning on September 30, 2012. The notes mature on July 31, 2015. The notes are unsecured and subordinated in right of payment to existing and future senior indebtedness of the Company. The \$7.5 million principal amount of the notes includes a refinance of existing indebtedness of \$5.0 million of promissory notes issued to Cantone Asset Management LLC.

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At any time on or after the six-month anniversary of the date of issuance of the notes, the notes are convertible at the option of the holder into shares of the Company's common stock at an initial conversion price equal to \$3.97 per share (adjusted for a 5% stock dividend paid on October 22, 2012 as further discussed in Note 10) and subject to adjustment for stock dividends, stock splits, combination of shares, recapitalization and other similar events.

If at any time on or after the six-month anniversary date, the weighted average price of the common stock for any 20 trading days within a period of 30 consecutive trading days equals or exceeds 200% of the conversion price and the average daily trading volume of the common stock during such 20 days exceeds 50,000 shares, then the Company may, subject to the satisfaction of certain other conditions, redeem the notes in cash at a redemption price equal to the sum of 100% of the principal amount being redeemed plus any accrued and unpaid interest on such principal.

In addition, the holders of a majority of the aggregate principal amount of notes then outstanding may require the Company to redeem all or any portion of the notes upon a change of control transaction, as described in the Notes, at a redemption price in cash equal to 110% of the redemption amount.

## **NOTE 9. ACQUISITIONS**

### ***Summary of 2012 Acquisitions***

During the nine months ended September 30, 2012, the Company acquired a total of eight skilled nursing facilities and one assisted living facility described further below. The Company has incurred a total of approximately \$1.2 million of acquisition costs related to these acquisitions and has recorded the cost in the "Other Income (Expense)" section of the Condensed Consolidated Statements of Operations.

#### *Eaglewood Care Center and Eaglewood Village*

On January 1, 2012, the Company obtained effective control of the Eaglewood Care Center, a skilled nursing facility and the Eaglewood Village facility, an assisted living facility each located in Springfield, Ohio. The total purchase price was \$12.4 million after final closing adjustments.

#### *Little Rock, Northridge and Woodland Hills*

On April 1, 2012, the Company obtained effective control of the Little Rock, Northridge and Woodland Hills facilities, three skilled nursing facilities located in Little Rock, Arkansas. The total purchase price was \$27.2 million after final closing adjustments.

### *Abington Place*

On June 1, 2012, the Company obtained effective control of Abington Place, a skilled nursing facility located in Little Rock, Arkansas. The total purchase price was \$3.6 million after final closing adjustments.

### *Glenvue Nursing Home*

On July 2, 2012, the Company obtained effective control of Glenvue Nursing, a skilled nursing facility located in Glenville, Georgia. The total purchase price was \$8.2 million.

### *Quail Creek Health and Rehab*

On July 3, 2012, the Company obtained effective control of Quail Creek Health and Rehab a skilled nursing facility located in Oklahoma City, Oklahoma, contingent upon final approval and transfer of the operating license to AdCare. The total purchase price was \$5.8 million

### *Companion Specialized Care Center*

On August 17, 2012, the Company obtained effective control of Companions Specialized Care Center, a skilled nursing facility located in Tulsa, Oklahoma, contingent upon final approval and transfer of the operating license to AdCare. The total purchase price was approximately \$5.8 million.

The preliminary purchase price allocation of all 2012 acquisitions is summarized as follows:

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(Amounts in 000s)

<b>Consideration transferred:</b>	
Net proceeds from loans	\$ 38,805
Seller notes	5,000
Cash (including prepaid deposits)	15,577
Common stock issued	750
Total consideration transferred	<u>\$ 60,132</u>
<b>Assets acquired:</b>	
Land	\$ 3,567
Buildings	39,945
Equipment and furnishings	3,906
Intangible assets – bed licenses	15,905
Total assets acquired	63,323
<b>Liabilities assumed:</b>	
Assumed indebtedness	(2,800)
Real estate taxes and other	(391)
Total identifiable net assets	<u>\$ 60,132</u>

The purchase price allocations for Glenvue Nursing, Quail Creek Health and Rehab and Companion Specialized Care Center are recorded on a preliminary basis. The fair value estimates of assets acquired and liabilities are pending completion of various

elements. The Quail Creek Health and Rehab and Companion Specialized Care Center acquisitions are preliminary subject to finalization of independent valuations of fair value of the assets acquired and liabilities assumed and final review by our management. The Companion Specialized Care Center consideration transferred is also subject to evaluation of the value of the stock transferred for restriction discounts. The Glenvue Nursing purchase price allocation is subject to final review by management of the independent valuations. Accordingly, there could be adjustments to our financial statements, including changes in our depreciation and amortization expense related to the valuation of building, equipment and furnishings and intangible assets acquired and their respective useful lives among other adjustments.

### ***Unaudited Pro forma Financial Information***

The above acquisitions have been included in the consolidated financial statements since the dates the Company gained effective control. Combined revenue for all 2012 acquisitions since gaining effective control is approximately \$ 21.5 million and resulted in income from operations of approximately \$ 2.1 million for the nine months ended September 30, 2012.

The following table represents pro forma results of consolidated operations as if all of the 2011 and 2012 acquisitions had occurred at the beginning of the earliest fiscal year being presented, after giving effect to certain adjustments.

<b>(Amounts in 000s)</b>	<b>Nine Months Ended September 30,</b>	
	<b>2012</b>	<b>2011</b>
Pro forma revenue	\$ 182,647	\$ 181,437
Pro forma operating expenses	\$ 171,591	\$ 171,859
Pro forma income from operations	\$ 11,056	\$ 9,578

The forgoing pro forma information is not indicative of what the results of operations would have been if the acquisitions had actually occurred at the beginning of the periods presented and is not intended as a projection of future results or trends.

## **NOTE 10. STOCKHOLDERS' EQUITY**

### *Stock Dividend*

On September 6, 2012, the Company's Board of Directors declared a 5% stock dividend issued on October 22, 2012 to holders of the common stock as of October 8, 2012. As a result of the stock dividend, the number of outstanding shares of common stock increased by approximately 0.7 million shares in 2012. As the Company is in a deficit position, there is no recorded impact to the reported amounts of stockholders' equity in the accompanying condensed consolidated balance sheet. As the dividend was declared before the release of the accompanying condensed consolidated financial statements,

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all references to the number of common shares and per-share amounts are restated based on the increased number of shares giving retroactive effect to the stock dividend on prior period amounts.

### *2012 Public Common Stock Offering*

In March 2012, the Company closed a firm commitment underwritten public offering of 1.1 million shares of common stock at an offering price to the public of \$3.75 per share. The Company also granted the underwriter in the offering an option for 45 days to purchase up to an additional 165,000 shares of common stock to cover over-allotments, if any. In connection with the underwriter's partial exercise of this option, the Company issued an additional 65,000 shares of common stock at an

offering price to the public of \$3.75 per share on May 22, 2012. The Company received net proceeds of approximately \$3.8 million after deducting underwriting discounts and other offering-related expenses of approximately \$0.6 million. This transaction occurred prior to the 2012 stock dividend and the share amounts, as disclosed, have not been restated as a result.

### *Shares Reserved*

At September 30, 2012, the Company had reserved approximately 12.1 million shares (after the 2012 stock dividend) of its authorized but unissued common stock for possible future issuance in connection with the following approximate number of shares (in thousands):

(Amounts in 000s)	Shares
Exercise and future grants of stock options under plans	1,274
Exercise of outstanding stock warrants—employee	563
Exercise of outstanding stock warrants—non-employee	3,154
Convertible debt shares issuable (including additional 20% required under agreements)	7,124
Total authorized shares reserved	<u>12,115</u>

## **NOTE 11. STOCK BASED COMPENSATION**

### ***Employee Common Stock Warrants & Options (Shares and Strike Prices Adjusted for the 2012 Stock Dividend-See Note 10)***

In February 2012, the Company granted non-qualified stock options to Christopher Brogdon, the Company's Vice Chairman, pursuant to the Company's 2011 Stock Incentive Plan (the "2011 Plan"). A total of 52,500 options were granted with an exercise price per share of \$6.67 and 105,000 options were granted with an exercise price of \$7.62. The options vest in September of 2013 and 2014, respectively. The options are exercisable until February 2022. The fair value of the options at the date of grant was estimated at \$1.19 and \$1.03 per share, respectively, and is being recognized as share-based compensation expense over the requisite service period of the awards.

In March 2012, the Company granted incentive stock options to certain members of management pursuant to the 2011 Plan. A total of 461,160 options were granted with an exercise price per share of \$3.93. The options vest ratably on the day before each of the three subsequent anniversaries. The options are exercisable until March 2017. The fair value of the options at the date of grant was estimated at \$1.34 per share and is being recognized as share-based compensation expense over the requisite service period of the awards.

On June 1, 2012, at the Annual Meeting of Shareholders of the Company, the shareholders approved an amendment to the 2011 Plan to increase the maximum number of shares of common stock that may be issued under the 2011 Plan to an aggregate of 2.0 million shares from 1.0 million. The Company's management, key employees (including the Company's principal executive officer, principal financial officer and named executive officers), directors and consultants are eligible to participate in the 2011 Plan.

In August 2012, the Company granted incentive stock options to certain members of management pursuant to the 2011 Plan. A total of 248,850 options were granted with an exercise price per share of \$3.93. The options vest ratably over

three years. The options are exercisable until August 2022. The fair value of the options on the date of grant was estimated at \$1.55 per share and is being recognized as share-based compensation expense over the requisite service period of the awards.

### ***Nonemployee Common Stock Warrants***

On March 29, 2012, in connection with the issuance of the \$3.5 million promissory note to Cantone Asset Management LLC, the Company granted to Cantone Asset Management LLC a warrant to purchase 315,000 shares of common stock at an exercise price per share of \$3.81. The warrant is exercisable until March 2015. The fair value of the warrant at the date of grant was estimated at \$0.64 per share and is included in deferred loan costs and is being amortized as interest expense over the life of the promissory note.

On April 1, 2012, in connection with the issuance of the \$5.0 million promissory note to Strome Alpha Offshore Ltd., the Company granted to Strome Alpha Offshore Ltd. a warrant to purchase 328,125 shares of common stock at an exercise price per share of \$3.81. The warrant is exercisable until April 2015. The fair value of the warrant at the date of grant was estimated at \$0.64 per share and is included in deferred loan costs and is being amortized as interest expense over the life of the promissory note.

On July 2, 2012 in connection with the issuance of the \$7.5 million principal amount of 8% subordinated convertible notes, the Company granted a warrant to purchase 105,000 shares of common stock at an exercise price per share of \$3.81 to the placement agent as partial consideration for its service in the offering. The warrant is exercisable until July 2015. The fair value of the warrant at the date of grant was estimated at \$0.49 per share and is included in deferred loan costs and is being amortized as interest expense over the life of the 8% subordinated convertible notes.

On August 31, 2012 the Company granted a warrant to purchase 15,750 shares of common stock at an exercise price per share of \$4.37 to a vendor. The warrant is exercisable until August 2015. The fair value of the warrant at date of grant was estimated at \$0.89 per share and is being recognized as non-employee share –based compensation expense over the requisite service period of the awards.

### ***Restricted Stock***

In June 2012, the Company, approved issuing, pursuant to the 2011 Plan, 283,500 shares of common stock with a three year restriction on transfer to its nine directors. The restricted stock has all the rights of a shareholder from the date of grant, including, without limitation the right to receive dividends and the right to vote. The Company determined the fair value of the restricted stock at date of grant to be equal to the grant date closing stock price of \$3.36. The related compensation expense is being recognized over the three year restricted period. The compensation expense for the three months ended September 30, 2012 was approximately \$0.2 million with unrecognized compensation expense of approximately \$0.7 million remaining at September 30, 2012.

On July 2, 2012 in connection with the issuance of the \$7.5 million principal amount of 8% subordinated convertible notes, the Company granted 52,500 shares of restricted common stock with a one year restriction on transferability to the placement agent as partial consideration for its service on the offering. The Company determined the fair value of the restricted stock at the date of grant to be equal to the grant date closing stock price of \$3.50. The related compensation expense is included in deferred loan costs and is being amortized as interest expense over the term of the 8% subordinated convertible notes. The expense for the three months ended September 30, 2012 was less than \$0.1 million with unrecognized expense of approximately \$0.2 million remaining at September 30, 2012.

The following summarizes the Company's restricted stock activity for the period ended September 30, 2012:



	Number of Shares	Weighted Avg. Grant Date Fair Value
Nonvested at January 1, 2012	–	–
Stock Dividend	16,000	\$ 3.38
Granted	320,000	\$ 3.38
Vested	(336,000)	\$ 3.38
Forfeited	–	–
Nonvested at September 30, 2012	–	–

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**NOTE 12. VARIABLE INTEREST ENTITIES**

As further described in Note 19 to the consolidated financial statements in the Annual Report, the Company has certain variable interest entities that are required to be consolidated because AdCare has control as primary beneficiary. A “primary beneficiary” is the party in a VIE that has both of the following characteristics: (a.) The power to direct the activities of the VIE that most significantly impact the VIE’s economic performance and (b.) The obligation to absorb losses of the VIE that could potentially be significant to the VIE or the right to receive benefits from the VIE that could potentially be significant to the VIE.

In June 2012, the Company amended the Option Agreement to purchase Riverchase Village Facility to extend the option exercise period to June 22, 2013. There have been no significant changes in these relationships in 2012. The following summarizes the assets and liabilities of the variable interest entities included in the consolidated balance sheets:

Riverchase Village Facility - Assets and Liabilities:

(Amounts in 000s)	September 30, 2012	December 31, 2011
Cash	\$ 10	\$ 16
Accounts receivable	7	10
Restricted investments	326	451
Property and equipment, net	5,993	5,999
Other assets	411	432
Total assets	<u>\$ 6,747</u>	<u>\$ 6,908</u>
Accounts payable	\$ 1,112	\$ 740
Accrued expenses	130	174
Current portion of notes payable	99	99
Notes payable, net of current portion	6,010	6,077
Noncontrolling interest	(604)	(182)
Total liabilities	<u>\$ 6,747</u>	<u>\$ 6,908</u>

Oklahoma Facilities - Assets and Liabilities:

(Amounts in 000s)	September 30, 2012	December 31, 2011
Cash	\$ 191	\$ 181

Accounts receivable	1,219	800
Property and equipment, net	10,916	11,111
Other assets	586	642
<b>Total assets</b>	<b>\$ 12,912</b>	<b>\$ 12,734</b>

Accounts payable	\$ 1,672	\$ 458
Accrued expenses	428	357
Current portion of notes payable	2,998	189
Notes payable, net of current portion	9,441	12,389
Noncontrolling interest	(1,627)	(659)
<b>Total liabilities</b>	<b>\$ 12,912</b>	<b>\$ 12,734</b>

In March 2012, a wholly owned subsidiary of AdCare entered into a purchase agreement for a skilled nursing home facility in Tulsa, Oklahoma and agreed to provide back office services for the facility until the earlier of its acquisition by the Company or the termination of the purchase agreement. It was determined that in this arrangement, the Company had a variable interest. The current owner of the facility was obligated for the outstanding debt of the facility and the Company did not provided any guarantee of the debt. The Company can terminate the current arrangement without any requirement to provide future financial support. As such, it was determined that under this arrangement the Company was not the primary beneficiary and, consolidation was not required. The arrangement terminated on August 17, 2012 when the Company acquired effective control of Companion Specialized Care Center (See Note 9).

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**NOTE 13. FAIR VALUE MEASUREMENTS**

The following are the major categories of assets and liabilities measured at fair value on a recurring basis during the nine months ended September 30, 2012, using quoted prices in active markets for identical assets (Level 1); significant other observable inputs (Level 2); and significant unobservable inputs (Level 3).

	Level 1:	Level 2:	Level 3:	Total at September 30, 2012
Derivative Liability	\$ -	\$ -	\$ 3.2 million	\$ 3.2 million

Set forth below is a reconciliation of the beginning and ending balances for the derivative liability measured at fair value on a recurring basis using significant unobservable inputs (Level 3) during the nine months ended September 30, 2012:

(Amounts in 000s)	Derivative Liability
Beginning Balance	\$ 1.9 million
Total loss	1.3 million
Ending Balance	<u>\$ 3.2 million</u>

The derivative liability is the result of the Company issuing subordinated convertible notes in 2010. The notes are convertible into shares of common stock of the Company at a current conversion price of \$3.73 (adjusted for various stock dividends) that is subject to future reductions if the Company issues equity instruments at a lower price. Because there is no minimum conversion price, an indeterminate number of shares may be issued in the future. Accordingly, the Company

determined an embedded derivative existed that was required to be bifurcated from the subordinated convertible notes and accounted for separately as a derivative liability recorded at fair value. The Company estimates the fair value of the derivative liability using the Black-Scholes Merton option-pricing model with changes in fair value being reported in the condensed consolidated statement of operations. This model requires certain key inputs that are significant unobservable inputs (Level 3).

The Company currently has no plans to issue equity instruments at a price lower than the conversion price of \$3.73, the current conversion price of the subordinated convertible notes issued in 2010. The derivative liability is a non-cash item. Upon conversion to common stock, the debt and derivative liability will be extinguished, the current fair market value of the common stock will be reflected as common stock and additional paid-in capital, and there may be a resulting gain or loss on the debt extinguishment. If not converted to common stock, upon settlement at the date of maturity, the debt and derivative liability will result in a gain on debt extinguishment for the remaining fair value of the derivative.

## **NOTE 14. COMMITMENTS AND CONTINGENCIES**

### ***Legal Matters***

The skilled nursing and assisted living business involves a significant risk of liability given the age and health of the Company's patients and residents and the services the Company provides. The Company and others in the industry are subject to an increasing number of claims and lawsuits, including professional liability claims, which may allege that services have resulted in personal injury, elder abuse, wrongful death or other related claims. The defense of these lawsuits may result in significant legal costs, regardless of the outcome, and can result in large settlement amounts or damage awards.

In addition to the potential lawsuits and claims described above, the Company and others in the industry are also subject to potential lawsuits under the Federal False Claims Act and comparable state laws alleging submission of fraudulent claims for services to any healthcare program (such as Medicare) or payor. A violation may provide the basis for exclusion from federally-funded healthcare programs. As of September 30, 2012, the Company does not have any material loss contingencies recorded based on management's evaluation of the probability of loss from known claims.

In 2012, the Company was named as a defendant in two related lawsuits asserting breach of contract claims arising out of consulting agreements executed in 2010 in connection with the Company's becoming the operator of certain leased facilities that were previously operated by a third-party. The same transaction was already the subject of litigation commenced by the Company in 2011 against several entities which had previously operated the leased facilities. After becoming the operator of the lease facilities, the Company incurred certain losses for pre-closing activities for which the Company was entitled to indemnification. The Company sought to enforce its rights to indemnity by filing a lawsuit

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against the former operators of the leased facilities for breach of contract and related tort claims, and the Company proceeded to set off its losses against payment due under the consulting agreements referenced above. The defendants filed counterclaims against the Company. In the third quarter of 2012, a settlement was reached with respect to the three lawsuits that permitted the Company to eliminate a previously accrued liability in light of the lower than expected settlement amount of approximately \$1.0 million resulting in a non-cash settlement gain of approximately \$0.4 million recognized in the third quarter. During the third quarter, approximately \$0.3 million of the settlement was paid and the majority of the remaining balance will be paid within one year.

### ***Commitments***

#### Oklahoma (Harty) PSA Amendment

On April 17, 2012, a wholly owned subsidiary of AdCare amended the Purchase and Sale Agreement with First Commercial Bank to acquire five skilled nursing facilities located in Oklahoma. The amendment requires an additional deposit of \$50,000 into escrow to be used as earnest money; amends the closing date to the date which is sixty (60) days after all required licenses are received, but in no event later than September 30, 2012; and releases \$200,000 from escrow to First Commercial Bank. Upon the closing of the purchase, the Company shall receive a \$200,000 credit against the purchase price; however, if the transaction fails to be consummated for any reason other than (i) default by First Commercial Bank; (ii) the failure of a condition to closing to be satisfied; or (iii) an event of casualty or condemnation, First Commercial Bank shall be entitled to retain the \$200,000 disbursed from escrow. If the transaction fails to be consummated for any reason other than as described in the preceding sentence, First Commercial Bank shall return the \$200,000 to the Company upon demand. (See Note 16).

#### Sumter Valley PSA

On April 27, 2012, a wholly owned subsidiary of AdCare entered into a Purchase and Sale Agreement with 1761 Pinewood Holdings, LLC to acquire a 96-bed skilled nursing facility located in Sumter, South Carolina for an aggregate purchase price of \$5.5 million. The purchase price consists of: (i) \$5.3 million cash consideration; and (ii) a \$0.2 million promissory note to be issued by one of AdCare's subsidiaries that shall bear interest at a fixed rate of 6% based on a 15-year amortization schedule. Pursuant to the purchase and sale agreement, as amended, the Company deposited \$0.1 million into escrow and delivered approximately \$0.2 million to the seller to be held as earnest money.

On September 27, 2012, under the Third Amendment to the Purchase and Sale Agreement, the closing date was extended to December 28, 2012, although, upon 14 days written notice by the Company, the closing day may be moved to the last business day of November 2012. The Company has paid approximately \$0.9 million in earnest money that will be credited against the purchase price at closing.

#### Georgetown PSA

On August 9, 2012, a wholly owned subsidiary of AdCare entered into a Purchase and Sale Agreement with Winyah Nursing Home, Inc. to acquire certain land, buildings, improvements, furniture, fixtures and equipment comprising an 84-bed skilled nursing facility known as Georgetown Healthcare & Rehabilitation Center located in Georgetown, South Carolina for an aggregate purchase price of \$4.2 million. The Company deposited \$0.1 million into escrow which will be refunded if an inspection of the facility is deemed unsatisfactory. The closing date is expected to be on or before November 30, 2012. (See Note 16).

#### Cabot PSA

On September 25, 2012, a wholly owned subsidiary of AdCare entered into a Purchase and Sale Agreement with John B. Montgomery and Michael Morton to acquire all the issued and outstanding membership interests of LJL Properties, LLC for an aggregate purchase price of \$6.3 million consisting of: (a) approximately \$0.8 million payable in cash; and (b) the assumption of indebtedness of LJL Properties, LLC in the original principle amount of approximately \$5.5 million subject to the terms and conditions of the Purchase and Sale Agreement. LJL Properties, LLC has applied for a Permit of Approval from the Arkansas Health Services Permit Agency permitting construction of a 70-bed nursing facility identified as Lonoke County Nursing and Rehab Center in Cabot, Arkansas. LJL Properties, LLC has caused the facility to be constructed with licensure of the new facility pending. AdCare has deposited \$0.1 million into escrow as earnest money. The closing is expected to occur on December 1, 2012 and the closing may be extended until December 15, 2012 with an additional payment of earnest money.

On June 4, 2012, the Company entered into a purchase agreement with JRT Group Properties, LLC (“JRT Group

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Properties”) to acquire property comprising Building 1145 of the Offices at Hembree, a condominium, located in Roswell, Georgia, for an aggregate purchase price of \$1.1 million. The lender which the Company anticipates using to finance this acquisition has received a third party appraisal with respect to the property which is consistent with the purchase price. One member of JRT Group Properties is a non-officer employee of the Company and another member of JRT is the son of Christopher Brogdon, the Company’s Vice Chairman and Chief Acquisition officer.

Benefit Plans

In the second quarter of 2012, it was determined that the Company has potential obligations related to the Company sponsored 401(k) plan. The Company has recorded an obligation based on an estimated amount of approximately \$0.1 million. The Company is pursuing remedial actions under the Voluntary Correction Programs (“VCP”). The Internal Revenue Service and the Federal Department of Labor may not accept the Company’s VCP proposal. Thus the obligation may be adjusted in the future. However, management does not believe the ultimate impact of the resolution will be material to its results of operations and expects this issue to be resolved before the end of 2012.

**NOTE 15. RELATED PARTY TRANSACTIONS**

On January 17, 2012, a wholly owned subsidiary of AdCare entered into a Purchase and Sale Agreement with Gyman Properties, LLC to acquire a 141-bed skilled nursing facility located in Lonoke, Arkansas, known as Golden Years Manor, for an aggregate purchase price of \$6.5 million. Pursuant to the Purchase and Sale Agreement, we deposited approximately \$0.3 million into escrow to be held as earnest money. On May 9, 2012, AdCare assigned all of its rights under the Purchase and Sale Agreement to GL Nursing, LLC, an entity affiliated with Christopher Brogdon, AdCare’s Vice Chairman and a beneficial owner of more than 10% of the common stock. GL Nursing, LLC has agreed to reimburse us the \$0.3 million deposit and all of our out-of-pocket costs relating to Golden Years Manor upon the closing of the acquisition, which occurred on May 31, 2012. The Company has recorded a receivable for this amount.

On June 4, 2012, a wholly owned subsidiary of AdCare entered into a Purchase Agreement with JRT Group Properties to acquire property comprising Building 1145 of the Offices at Hembree, a condominium, located in Roswell, Georgia for an aggregate purchase price of approximately \$1.1 million. The closing of the Hembree Purchase is expected to occur before the end of 2012. One member of JRT Group Properties is a non-officer employee of AdCare and another member of JRT Group Properties is the son of Christopher Brogdon, the Company’s Vice Chairman. As previously disclosed in the Annual Report, AdCare leases the Hembree property for use as administrative offices.

On July 26, 2012, Hearth & Home of Ohio, Inc. (“Hearth & Home”), a wholly owned subsidiary of AdCare, entered into an Amendment with Christopher Brogdon, the Company’s Vice Chairman, which amends that certain Option Agreement, as previously amended, between Hearth & Home and Mr. Brogdon, dated June 22, 2010, to extend the last date on which the option provided for thereby may be exercised from June 22, 2012 to June 22, 2013. Pursuant to the option agreement, AdCare has an exclusive and irrevocable option, exercisable until June 22, 2013 to purchase from Mr. Brogdon 100% of the issued and outstanding membership interests of Riverchase Village ADK, LLC (“Riverchase”) for a purchase price of \$0.1 million. As previously disclosed, AdCare: (i) entered into a five-year management contract with Riverchase on June 22,

2010 to manage the 105-bed assisted living facility located in Hoover, Alabama, known as Riverchase Village; and (ii) guaranteed the repayment by Riverchase of certain bonds owing to The Medical Clinic Board of the City of Hoover.

On October 12, 2012, the Company executed an Assignment of Purchase and Sale Agreement in favor of Edwards Redeemer Property Holdings, LLC (“Edwards Redeemer”) and ER Nursing, LLC (both indirect, wholly owned subsidiaries of the Company and, collectively, the “Edwards Assignees”) pursuant to which AdCare assigned all of its right to purchase the Edwards Redeemer Nursing Center located in Oklahoma under that certain Purchase and Sale Agreement, dated May 5, 2011 and as subsequently amended and assigned. The Edwards Assignees have agreed to assume all obligations of the Company under the Purchase and Sale Agreement with respect to the Edwards Redeemer Nursing facility, including reimbursement for out-of-pocket costs. AdCare, the owner of all of the issued and outstanding membership interests of Edward Redeemer, also has executed a Membership Interest Power pursuant to which it assigns all such interests to Chris Brogdon, the Company’s Vice Chairman.

The Company also executed an Assignment of Purchase and Sale Agreement in favor of WP Oklahoma Nursing, LLC, an entity owned and controlled by Chris Brogdon, the Company’s Vice Chairman, pursuant to which the Company assigns all of its right to purchase the Whispering Pines Nursing Center located in Oklahoma under the Purchase and Sale Agreement dated May 5, 2011 and as subsequently amended and assigned. WP Oklahoma Nursing, LLC has agreed to assume all obligations of AdCare under the Purchase and Sale Agreement with respect to the Whispering Pines Nursing Center facility. Related to this agreement, the Company has recorded a receivable of less than \$0.1 million.

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**NOTE 16. SUBSEQUENT EVENTS**

*Self-Insurance*

Effective October 1, 2012, the Company began providing self-insured medical healthcare benefits to employees. To protect itself against loss exposure with this policy, the Company has purchased individual stop-loss insurance coverage that insures individual claims that exceed \$0.2 million for each covered person per year with an aggregate annual stop-loss level of approximately \$7.5 million. In addition, the Company entered into a large deductible worker’s compensation plan for the majority of its employees with a \$0.3 million deductible limit for each occurrence with an aggregate limit of approximately \$6.5 million.

*Oklahoma (Harty) PSA Amendment*

On October 8, 2012, a wholly owned subsidiary of AdCare amended the Purchase and Sale Agreement, dated May 5, 2011, and as subsequently amended and assigned pursuant to which the Company would acquire five skilled nursing facilities located in Oklahoma. The amendment extends the closing date to 60 days after AdCare receives all required licenses and permits necessary to complete the purchase but by no later than November 30, 2012. In consideration for extending the closing date, the Company agrees to pay certain real estate taxes and assessments relating to the facilities in Oklahoma for fiscal year 2011 (which the seller represents to total approximately \$0.2 million) and fiscal year 2012.

On October 12, 2012, the Company executed an Assignment of Purchase and Sale Agreement in favor of the Edwards Assignees, pursuant to which AdCare assigns all of its right to purchase the Edwards Redeemer Nursing Center located in Oklahoma under that certain Purchase and Sale Agreement, dated May 5, 2011 and as subsequently amended and assigned. The Edwards Assignees have agreed to assume all obligations of AdCare under the Purchase and Sale Agreement with respect to the Edwards Redeemer Nursing Center facility, including reimbursement for out-of-pocket costs. AdCare Holdings, the owner of all of the issued and outstanding membership interests of Edward Redeemer (a wholly owned subsidiary of the Company) also has

executed a Membership Interest Power pursuant to which it assigns all such interests to Chris Brogdon, the Company's Vice Chairman.

The Company also executed an Assignment of Purchase and Sale Agreement in favor of WP Oklahoma Nursing, LLC, an entity owned and controlled by Mr. Brogdon, pursuant to which the Company assigns all of its right to purchase the Whispering Pines Nursing Center located in Oklahoma under the Purchase and Sale Agreement, dated May 5, 2011 and as subsequently amended and assigned. WP Oklahoma Nursing, LLC has agreed to assume all obligations of the Company under the Oklahoma Facilities Purchase Agreement with respect to the WP Facility.

### Ohio ALFs Sale

On October 11, 2012, the Company and certain subsidiaries entered into an Agreement of Sale with CHP Acquisition Company, LLC ("CHP") pursuant to which the Company may sell certain land, buildings, improvements, furniture, fixtures, operating agreements and equipment comprising the following six assisted living facilities: Community's Hearth & Home located in Springfield, Ohio; Community's Hearth & Home also located in Springfield, Ohio; Hearth & Home of Van Wert located in Van Wert, Ohio; Community's Hearth & Home located in Urbana, Ohio; Hearth & Home of Vandalia located in Vandalia, Ohio; and Lincoln Lodge Retirement Residence located in Columbus, Ohio (collectively, the "Ohio ALFs"), for an aggregate purchase price of approximately \$22.3 million, subject to the terms and conditions of the Agreement of Sale.

The purchase price consists of: (i) \$0.2 million to be deposited by CHP into escrow to be held as earnest money (the "Deposit"); (ii) CHP's satisfaction of the principal balance of United States Department of Housing and Urban Development ("HUD") loans for certain of the Ohio ALFs (the "HUD Loan Payoff"); (iii) CHP's assumption of a HUD loan secured by one of the Ohio ALFs (the "HUD Loan Assumption"); (iv) a promissory note issued by CHP to the Company in the amount of \$3.6 million (the "CHP Promissory Note"); and (v) cash consideration in an amount equal to the purchase price minus the amount of the Deposit, the HUD Loan Payoff, the HUD Loan Assumption and the CHP Promissory Note. The Company estimates that the cash consideration to be received at closing would be approximately \$6.7 million.

The closing of the Ohio ALFs Sale may take place at any such time as mutually agreed upon by the Company and CHP, but in no event later than December 31, 2012, unless such closing date has been extended by mutual agreement of the Company and CHP. The closing of the Ohio ALFs Sale is subject to customary closing conditions, indemnification provisions and termination provisions.

At September 30, 2012, the Company did not meet the criteria to classify the Ohio ALFs as held for sale or to present the related operations as discontinued operations because management, although having the authority to approve the action had

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not yet committed to sell the assets, there was no active plan to locate a buyer was and the disposal of the Ohio ALFs probable. Therefore, the related assets and liabilities of the Ohio ALFs were classified as held and used at September 30, 2012. The major assets that will be held as part of the disposal group include the property and equipment with a carrying value of approximately \$12.0 million and the liabilities that are expected to be extinguished consisting of debt was approximately \$11.5 million at September 30, 2012. There are no indications of potential impairment of assets.

### PrivateBank Credit Facility Amendment

On October 26, 2012, the Company and certain of its wholly owned subsidiaries, on the one hand, and PrivateBank entered into a Modification Agreement which amends that certain Loan and Security Agreement, dated as of September 20, 2012,

between certain of the Company's wholly owned subsidiaries and PrivateBank. The modification agreement amends the loan agreement to: (i) allow PrivateBank to issue additional letters of credit for the account of the borrowers under the loan agreement; and (ii) change the total amount that may be issued under any letters of credit to \$2.5 million. The modification agreement did not change the maximum amount that may be borrowed under the loan agreement by the borrowers, which remains at \$10.6 million.

#### Georgetown PSA Amendment

On November 5, 2012, the Company amended its Purchase and Sale Agreement with Winyah Nursing Home, LLC relating to the acquisition of the Georgetown Healthcare & Rehabilitation Center, an 84-bed skilled nursing facility in Georgetown, South Carolina. The amendment extends the closing date to December 27, 2012 and required the Company to deliver an additional \$50,000 extension fee to the seller.

#### Preferred Stock

On November 7, 2012, the Company announced a "best efforts" public offering of 450,000 shares of its newly designated series of its preferred stock, designated as its 10.875% Series A Cumulative Redeemable Preferred Stock ("Series A Preferred Stock"). The Series A Preferred Stock is offered at \$23 per share. Subject to the closing of the offering and sale of the 450,000 shares of Series A Preferred Stock, the Company expects to receive net proceeds of approximately \$9.3 million after deducting underwriting discounts and other offering-related expenses of approximately \$1.1 million.

## **Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations.**

### **Special Note Regarding Forward Looking Statements**

Certain statements in this Quarterly Report on Form 10-Q (this "Quarterly Report") constitute "forward-looking statements." These forward-looking statements involve known or unknown risks, uncertainties and other factors that may cause the actual results, performance, or achievements of the Company to be materially different from any future results, performance or achievements expressed or implied by the forward-looking statements. Specifically, the actions of our competitors and customers, our ability to execute our business plan and our ability to increase revenues is dependent upon our ability to continue to expand our current business and to expand into new markets, general economic conditions, and other factors. You can identify forward-looking statements by terminology such as "may," "will," "should," "expects," "intends," "plans," "anticipates," "believes," "estimates," "predicts," "potential," "continues," or the negative of these terms or other comparable terminology. Although we believe that the expectations reflected in the forward-looking statements are reasonable, we do not guarantee future results, levels of activity, performance or achievements. We undertake no obligation to publicly update or review any forward-looking statements, whether as a result of new information, future developments or otherwise. You should read this Management's Discussion and Analysis of Financial Condition and Results of Operations in conjunction with the financial statements and related notes included in this Quarterly Report and included in the Annual Report.

#### **Overview**

We own and manage skilled nursing facilities and assisted living facilities. We deliver skilled nursing and assisted living services through wholly owned separate operating subsidiaries.

	September 30, 2012	June 30, 2012	December 31, 2011	September 30, 2011	December 31, 2010
Cumulative number of facilities	51	48	42	40	27
Cumulative number of operational beds	4,791	4,427	3,737	3,579	2,428



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State	Number of Operational Beds/Units	Number of Facilities at September 30, 2012					Total
		Owned	VIE	Leased	Managed for Third Parties		
Arkansas	1,041	10	–	–	–	10	
Alabama	408	2	1	–	–	3	
Georgia	1,631	4	–	10	–	14	
Missouri	80	–	–	1	–	1	
North Carolina	106	1	–	–	–	1	
Ohio	981	10	–	1	4	15	
Oklahoma	544	2	5	–	–	7	
<b>Total</b>	<b>4,791</b>	<b>29</b>	<b>6</b>	<b>12</b>	<b>4</b>	<b>51</b>	
<b>Facility Type</b>							
Skilled Nursing	4,296	21	5	12	3	41	
Assisted Living*	412	8	1	–	–	9	
Independent Living	83	–	–	–	1	1	
<b>Total</b>	<b>4,791</b>	<b>29</b>	<b>6</b>	<b>12</b>	<b>4</b>	<b>51</b>	

\*The above table includes six owned assisted living facilities in Ohio consisting of 196 beds. The Company has entered into an agreement of sale to sell these facilities by December 31, 2012. See Note 16 in the “Notes to Condensed Consolidated Financial Statements” section of Part I, Item 1 of this Quarterly Report.

### Acquisitions

We have embarked on a strategy to grow our business through acquisitions and leases of senior care facilities. During the first nine months of 2012, we acquired nine facilities (eight skilled nursing facilities and one assisted living facility), bringing our total bed count to 4,791 at September 30, 2012.

- On December 30, 2011, we acquired a skilled nursing facility and an assisted living facility both located in Springfield, Ohio, for an aggregate adjusted purchase price of approximately \$12.4 million. We obtained effective control and commenced operating these facilities on January 1, 2012.
- On March 30, 2012, we acquired three skilled nursing facilities located in Little Rock, Arkansas. The total purchase price was approximately \$27.2 million. We obtained effective control and operations commenced on April 1, 2012.
- On April 30, 2012, we acquired a skilled nursing facility located in Little Rock, Arkansas for an aggregate purchase price of approximately \$3.6 million. We obtained effective control and operations commenced on June 1, 2012.
- On July 2, 2012 we acquired a skilled nursing facility in Glennville, Georgia for an aggregate purchase price of approximately \$8.2 million. We obtained effective control and operations commenced on July 2, 2012.
- On July 2, 2012 we acquired a skilled nursing facility in Oklahoma City, Oklahoma for an aggregate purchase price of approximately \$5.8 million. We obtained effective control and operations commenced on July 3, 2012.

- On August 17, 2012, we acquired a skilled nursing facility in Tulsa, Oklahoma for an aggregate purchase price of approximately \$5.8 million. We obtained effective control and operations commenced on August 17, 2012.

In addition, the following potential acquisitions have been announced during the nine months ended September 30, 2012:

- On April 17, 2012, we amended a Purchase and Sale Agreement with First Commercial Bank to acquire five skilled nursing facilities located in Oklahoma. On October 12, 2012, we assigned our rights to purchase two of these facilities to a related party. We expect closing to occur no later than December 31, 2012. See Notes 14, 15 and 16 in the “Notes to Condensed Consolidated Financial Statements” section of Part I, Item 1 of this Quarterly Report.
- On April 27, 2012, we entered into a Purchase and Sale Agreement with 1761 Pinewood Holdings, LLC to acquire a 96-bed

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skilled nursing facility located in Sumter, South Carolina for an aggregate purchase price of approximately \$5.5 million. We expect the closing of the acquisition to occur on December 31, 2012.

- On August 9, 2012, we entered into a Purchase and Sale Agreement with Winyah Nursing Home, Inc. to acquire an 84-bed skilled nursing facility located in Georgetown, South Carolina for an aggregate purchase price of approximately \$4.2 million. We expect closing to occur on or before December 27, 2012.
- On September 25, 2012, we entered into a Purchase and Sale Agreement with John B. Montgomery and Michael Morton. to acquire all the issued and outstanding membership interests in LJL Properties, LLC for an aggregate purchase price of approximately \$6.3 million. LJL Properties, LLC has applied for a Permit of Approval permitting construction of a 70-bed nursing facility in Cabot, Arkansas. We expect closing to occur no later than December 15, 2012.

The Company is currently evaluating potential acquisition opportunities in addition to those described above, and we continue to seek new opportunities to further our growth strategy. No assurance is made that any of these potential acquisition opportunities will be determined to be appropriate for us or that we will complete any of such acquisitions on terms acceptable to us, or at all.

### *Segments*

The Company reports its operations in three segments: SNF, ALF and Corporate & Other. The Company delivers services through wholly owned separate operating subsidiaries. The SNF and ALF segments provide services to individuals needing long-term care in a nursing home or assisted living setting and management of those facilities. The Corporate & Other segment engages in the management of facilities and accounting and IT services. We evaluate financial performance and allocate resources primarily based on segment operating income (loss). Segment operating results excludes interest expense and other non-operating income and expenses. See Note 4 in the “Notes to Condensed Consolidated Financial Statements” section of Part I, Item 1 of this Quarterly Report.

### *Skilled Nursing Facilities*

We focus on two primary indicators in evaluating the financial performance in this segment. Those indicators are facility occupancy and patient mix. Facility occupancy is important because higher occupancy generally leads to higher revenues. In addition, concentrating on increasing the number of Medicare covered admissions (the “patient mix”) helps in increasing revenues. We continue our work towards maximizing the number of patients covered by Medicare where, typically, our operating margins are higher. We

include commercial insurance covered admissions that are reimbursed at the same level as those covered by Medicare in our Medicare utilization percentages and analysis.

For the three and nine months ended September 30, 2012, revenue in our skilled nursing segment increased approximately \$ 20.2 million and \$58.4 million, respectively, compared to September 30, 2011, as a result of acquisition growth. For the three and nine months ended September 30, 2012, this segment had income from operations of \$4.5 million and \$13.0 million respectively, as a result of optimization of occupancy and quality mix as well as expense controls. We expect to continue to implement and refine strategies designed to sustain these goals. Total assets increased \$63.9 million due to acquisitions made since September 30, 2011 and other building improvements.

### Average Occupancy

	Three Months Ended September 30,	
	2012	2011
Same Facilities (1)	84.9%	87.3%
All Facilities	77.2%	85.4%

  

	Nine Months Ended September 30,	
	2012	2011
Same Facilities (1)	85.1%	87.0%
All Facilities	78.1%	86.2%

(1) "Same Facilities" results represent those owned and leased facilities we began operating on and prior to January 1, 2011.

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### Patient Mix

Three Months Ended September 30,

	Same Facilities		All Facilities	
	2012	2011	2012	2011
Medicare	13.8%	14.4%	12.8%	12.9%
Medicaid	74.8%	74.5%	74.2%	76.3%
Other	11.4%	11.1%	13.0%	10.8%
Total	100.0%	100.0%	100.0%	100.0%

Nine Months Ended September 30

	Same Facilities		All Facilities	
	2012	2011	2012	2011
Medicare	14.7%	15.0%	13.6%	14.2%
Medicaid	73.5%	75.4%	73.8%	76.2%
Other	11.8%	9.6%	12.6%	9.6%
Total	100.0%	100.0%	100.0%	100.0%

**For the Three Months Ended September 30, 2012:**

Region (SNF Only)	Operational Beds at Period End(1)	Period' s Average Operational Beds	Occupancy (Operational Beds)	Medicare Utilization (Skilled %ADC)(2)	2012 QTD Total Revenues	Medicare (Skilled) SPPD(3)	Medicaid SPPD(3)
Alabama	304	304	78.1%	8.6%	\$ 4,566	\$ 402.10	\$ 183.60
Arkansas	1,009	1,009	61.9%	12.5%	\$ 11,976	\$ 395.18	\$ 173.60
Georgia	1,631	1,631	86.7%	13.3%	\$ 27,942	\$ 457.55	\$ 166.86
Missouri	80	80	63.8%	12.6%	\$ 852	\$ 444.90	\$ 135.04
North Carolina	106	106	84.9%	19.8%	\$ 1,870	\$ 446.67	\$ 162.67
Ohio	293	293	85.7%	14.9%	\$ 5,409	\$ 472.49	\$ 167.02
Oklahoma	544	483	72.3%	10.7%	\$ 5,363	\$ 403.65	\$ 127.85
<b>Total</b>	<b>3,967</b>	<b>3,906</b>	<b>77.2%</b>	<b>12.8%</b>	<b>\$ 57,978</b>	<b>\$ 437.54</b>	<b>\$ 164.42</b>

**For the Nine Months Ended September 30, 2012:**

Region (SNF Only)	Period' s Average Operational Beds	Occupancy (Operational Beds)	Medicare Utilization (Skilled %ADC)(2)	2012 YTD Total Revenues	Medicare (Skilled) SPPD(3)	Medicaid SPPD(3)
Alabama	304	81.4%	10.9%	\$ 14,469	\$ 390.53	\$ 186.16
Arkansas	822	63.4%	12.0%	\$ 29,297	\$ 385.94	\$ 172.28
Georgia	1,542	86.3%	14.4%	\$ 76,053	\$ 463.27	\$ 154.03
Missouri	80	62.7%	17.5%	\$ 2,594	\$ 413.79	\$ 132.37
North Carolina	106	84.5%	18.6%	\$ 5,485	\$ 454.37	\$ 160.27
Ohio	293	84.4%	16.2%	\$ 16,024	\$ 472.48	\$ 161.70
Oklahoma	371	70.4%	10.0%	\$ 11,830	\$ 412.55	\$ 125.72
<b>Total</b>	<b>3,518</b>	<b>78.1%</b>	<b>13.6%</b>	<b>\$ 155,752</b>	<b>\$ 440.95</b>	<b>\$ 158.09</b>

(1) Excludes managed beds which are not consolidated.

(2) ADC is the Average Daily Census

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(3) PPD is the Per Patient Day equivalent

*Assisted Living Facilities*

For the three and nine months ended September 30, 2012, revenue in our ALF segment increased approximately \$ 0.9 million and \$ 2.8 million, respectively, compared to September 30, 2011 as a result of increased revenue from acquisitions, an annual increase in rates charged to privately paying residents and increasing occupancy. For the three and nine months ended September 30, 2012, this segment had income from operations of approximately \$0.7 million and \$2.0 million, respectively. Total assets increased \$ 7.7 million primarily due to acquisitions since September 30, 2011 and other building improvements made during the last twelve months.

**Average Occupancy**

**Three Months Ended**

**September 30,**

2012	2011
------	------

85.1%	77.5%
-------	-------

**Nine Months Ended**

**September 30,**

2012	2011
------	------

83.4%	75.9%
-------	-------

Residents of our assisted living facilities rely on their personal investments and wealth to pay for their stay. Although many of the risks still remain, such as declines in market values of investments, depressed market for the sale of private homes, and adult children caring for their elderly at home, we have seen an increase in census.

In October 2012, the Company entered into a an Agreement of Sale pursuant to which the Company may sell ALFs in Ohio (the "Ohio ALFs"). Management expects the sale to close on or before December 31, 2012. We estimate the cash proceeds from the sale will be approximately \$6.7 million. For the nine months ended September 30, 2012, the Ohio ALF' s had revenues of approximately \$6.8 million and operating income of approximately \$1.7 million. At September 30, 2012, the Ohio ALFs had approximately \$15.4 million in assets that will likely be sold and \$12.6 million in debt that will likely be extinguished as a result of the sale.

*Corporate & Other*

We manage three skilled nursing facilities and one independent living campus for third party owners under management agreements that either are for a fixed monthly fee or for a percentage of revenue generated by the managed facility. Depending on the type of management agreement, our revenues increase annually according to inflationary adjustments stipulated in our management agreements or they increase as the facility' s revenue increases for the management agreements that are based on a percentage of revenue. This segment includes our corporate overhead expenses, which are made up of salaries of our senior management team members and various other corporate expenses, including, but not limited to, corporate office operating expenses, audit fees, legal fees and board activities. Additionally, non-cash charges for compensation expense related to warrants, restricted stock and stock options are included in corporate overhead. We do not allocate these expenses to the divisions or separate them from the management business for management review purposes.

**Results of Operations**

<b>(Amounts in 000s)</b>	<b>Total Patient Care Revenues</b>			
	<b>Three Months Ended September 30,</b>		<b>Nine Months Ended September 30,</b>	
	<b>2012</b>	<b>2011</b>	<b>2012</b>	<b>2011</b>
<b>Skilled Nursing</b>				
Same Facilities	\$ 29,431	\$ 29,657	\$ 87,886	\$ 87,020
Other Facilities	28,547	8,072	67,867	10,362
<b>Total</b>	<b>\$ 57,978</b>	<b>\$ 37,729</b>	<b>\$ 155,753</b>	<b>\$ 97,382</b>

<b>(Amounts in 000s)</b>	<b>Total Patient Care Revenues</b>			
	<b>Three Months Ended September 30,</b>		<b>Nine Months Ended September 30,</b>	
	<b>2012</b>	<b>2011</b>	<b>2012</b>	<b>2011</b>
<b>Assisted Living</b>				
Same Facilities	\$ 2,699	\$ 2,463	\$ 8,010	\$ 7,214
Other Facilities	665	n/a	2,028	n/a
<b>Total</b>	<b>\$ 3,364</b>	<b>\$ 2,463</b>	<b>\$ 10,038</b>	<b>\$ 7,214</b>

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[Table of Contents](#)**Comparison for the three months ended September 30, 2012 and 2011**

*Patient Care Revenues* - For the periods presented, total patient care revenues increased \$21.2 million, or 53%.

Revenue in our SNF segment increased approximately \$20.2 million when compared to the three months ended September 30, 2011, primarily as a result of additional facilities acquired since September 2011. This segment had net income from operations of approximately \$4.5 million which is \$2.2 million higher compared to the three months ended September 30, 2011 as a result of higher revenue due to acquisitions and improved reimbursement. We are seeking to increase facility occupancy and to increase the number of patients covered by Medicare. We seek to continue to implement and refine strategies designed to achieve these goals.

Revenue in our ALF segment increased approximately \$0.9 million when compared to the three months ended September 30, 2011, as a result of increased census and levels of care as well as the addition of one new facility in 2012 and one new facility in the fourth quarter of 2011. This segment had income from operations of \$0.7 million which is \$0.3 million more than the same period in 2011 from an annual increase in rates charged to residents of the facilities.

*Management Revenue* - For the periods presented, management revenues (net of eliminations) increased \$0.1 million, or 30%, as a result of a net increase of one managed facility.

*Cost of Services* - For the periods presented, cost of services was approximately \$49.2 million or 80% of patient care revenue compared to \$32.6 million or 81% of patient care revenue for the same period a year ago. This increase in overall cost is the result of numerous acquisitions over the past 12 months.

*General and Administrative* - For the three months ended September 30, 2012, general and administrative expenses were approximately \$4.3 million in 2012 compared to \$3.3 million in 2011, an increase of \$1.0 million, or 32%. As a percent of total revenues, general and administration expenses were approximately 7.0% for the three months ended September 30, 2012 compared to 8.0% for the three months ended September 30, 2011. Our performance-based incentive expense increased by \$0.5 million reflecting the improvement in the Company's financial results. Wage and other employee related costs increased \$0.2 million as a result of additional staffing needed to support the growth in operations. Investor relations expenses increased by approximately \$0.1 million. Datacenter cost has increased by \$0.2 million as a result of outsourcing our IT department.

*Facility Rent Expense* - For the periods presented, lease expenses increased \$0.1 million due to annual increases and the addition of the one new leased facility in the fourth quarter of 2011.

*Depreciation and Amortization* - For the periods presented, depreciation and amortization increased \$1.3 million. The depreciation increase is directly related to acquisition activity that was not included in the 2011 results as it occurred in later periods. In addition, the acquisitions resulted in intangibles that are being amortized during the period.

*Interest Expense, net* - For the periods presented, interest expense, net increased \$1.8 million, or 80%. We have entered into numerous debt instruments in relation to our growth strategy for the acquisition of the facilities which began in the third quarter of 2010. In addition, several of the arrangements are short term in nature resulting in higher interest rates than previously experienced and an increase in the amortization of deferred loan costs associated with the new debt agreements.

*Acquisition Costs, net of Gains* - For the three months ended September 30, 2012, acquisition costs, net of gains was an expense of \$0.3 million, compared to \$1.1 million for the comparative period. For the three months ended September 30, 2012, the total acquisition costs were legal fees directly related to acquisitions and other costs incurred on potential future acquisitions.

*Derivative Gain/Loss* - For the three months ended September 30, 2012, the derivative loss was \$2.1 million, compared to a gain of \$4.7 million for the same period in 2011. The derivative results from the subordinated notes issued in the third quarter of 2010. The expense associated with the derivative increases as the stock price climbs, and conversely decreases as the stock price declines. The price of the common stock increased during the three-month period ended September 30, 2012, from June 30, 2012 to September 30, 2012.

### **Comparison for the nine months ended September 30, 2012 and 2011**

*Patient Care Revenues* - For the periods presented, total patient care revenues increased \$61.2 million, or 59%.

Revenue in our SNF segment increased approximately \$58.4 million when compared to the nine months ended September 30, 2011, primarily as a result of additional facilities acquired since September, 2011. This segment had net income from operations of \$13.0 million which is \$8.5 million higher compared to the nine months ended September 30, 2011 as a result of higher revenue due to acquisitions and improved reimbursement. We are seeking to increase facility occupancy and to increase the number of patients covered by Medicare. We seek to continue to implement and refine strategies designed to achieve these goals.

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Revenue in our ALF segment increased approximately \$2.8 million when compared to the nine months ended September 30, 2011, as a result one new facility in 2012 and one new facility in the fourth quarter of 2011. This segment had income from operations of \$2.0 million which is \$1.0 million more than the same period in 2011.

*Management Revenue* - For the periods presented, management revenues (net of eliminations) decreased \$0.2 million, or 12%, as a result of fewer managed facilities.

*Cost of Services* - For the periods presented, cost of services was approximately \$131.5 million or 79% of patient care revenue compared to \$84.9 million or 81% of patient care revenue for the same period a year ago. This increase in overall cost is the result of numerous acquisitions over the past 12 months. The improvement as a percent of patient care revenue reflects the implementation of consolidated purchasing programs and other cost reduction efforts. In 2012, the Company eliminated the ability for employees to accumulate earned but unused vacation beyond the current calendar year. As a result, vacation time previously accumulated must be used by the employee by December 31, 2012 or it will be forfeited. Management has estimated the potential forfeitures and has adjusted the vacation accrual accordingly.

*General and Administrative* - For the nine month period ended September 30, 2012, general and administrative expenses were approximately \$13.2 million in 2012 compared to \$9.4 million in 2011, an increase of \$3.8 million, or 41%. As a percent of total revenues, general and administration expenses were approximately 7.9% for the nine months ended September 30, 2012 compared to 8.8% for the nine months ended September 30, 2011. Our performance-based incentive expense increased by \$1.5 million reflecting the improvement in the Company's financial results. Wage and other employee related costs increased \$0.6 million as a result of additional staffing needed to support the growth in operations. Travel costs have increased approximately \$0.3 million as a result of acquisitions and more geographically dispersed operations. Investor relations expenses increased by approximately \$0.2 million. Non-employee Board compensation increased approximately \$0.2 million. This increase is to align Board compensation with the Company's peer group and to provide appropriate remuneration for their services. Datacenter cost has increased by \$0.2 million as a result of outsourcing our IT department.

*Facility Rent Expense* - For the periods presented, lease expenses increased \$0.5 million due to annual increases and the addition of the one new leased facility in the fourth quarter of 2011.

*Depreciation and Amortization* - For the periods presented, depreciation and amortization increased \$3.2 million. The depreciation increase is directly related to acquisition activity that was not included in the 2011 results as it occurred in later periods. In addition, the acquisitions resulted in intangibles that are being amortized during the period.

*Interest Expense, net* - For the periods presented, interest expense, net increased \$4.8 million or 87%. We have entered into numerous debt instruments in relation to our growth strategy for the acquisition of the facilities which began in the third quarter of 2010. In addition, several of the arrangements are short term in nature resulting in higher interest rates than previously experienced and an increase in the amortization of deferred loan costs associated with the new debt agreements.

*Acquisition Costs, net of Gains* - For the nine months ended September 30, 2012, acquisition costs, net of gains was an expense of \$1.2 million, compared to an expense of \$0.8 million for the comparative period. For the nine months ended September 30, 2012, the total acquisition costs were legal fees directly related to acquisitions during the nine months ended September 30, 2012 and other costs incurred on potential future acquisitions.

*Derivative Gain/Loss* - For the nine months ended September 30, 2012, the derivative loss was \$1.3 million, compared to a gain of \$0.8 million for the same period in 2011. The derivative results from the subordinated convertible notes issued during the third quarter of 2010. The expense associated with the derivative increases as the stock price climbs, and conversely decreases as the stock price declines. The price of the common stock of the Company increased during the nine-month period ended September 30, 2012 from December 31, 2011 to September 30, 2012.

*Other Income/(Expense)* - For the periods presented, other income decreased \$0.3 million. There was a recovery of receivables recorded in the prior year. In the nine months ended September 30, 2012, there was a \$0.4 million non-cash settlement gain as a result of the litigation settlement partially offset by other expenses.

### **Critical Accounting Policies and Use of Estimates**

There have been no significant changes during the nine months ended September 30, 2012 to the items that we disclosed as our critical accounting policies and use of estimates in our discussion and analysis of financial condition and results of operation contained in the Annual Report.

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### **Liquidity and Capital Resources**

#### **Overview**

Liquidity is the measure of the Company's ability to have adequate cash or access to cash at all times in order to meet financial obligations when due, as well as to fund corporate expansion and other activities. Historically, the Company has met its liquidity requirements through a combination of net cash flow from operations, debt from third party lenders and issuances of other debt and equity securities.

We have negative working capital of approximately \$2.3 million at September 30, 2012. Our ability to sustain profitable operations is dependent on continued growth in revenues and controlling costs. Approximately \$3.0 million of the negative working capital ratio is



related to short term debt under a VIE which the Company does not guarantee. (See Note 12 in the “Notes to Condensed Consolidated Financial Statements” section of Part I, Item 1 of this Quarterly Report).

During the next twelve months, the Company believes it will require additional financing to satisfy its financial obligations and implement its expansion strategy. The Company is currently exploring several financing alternatives and may seek to raise additional capital through the sale of additional debt or equity securities, although there is no assurance that the Company will be able to raise additional capital through the issuance of debt or equity securities on terms acceptable to it, or at all. If the Company is unable to secure such additional financing, then the Company may be required to restructure its outstanding indebtedness and delay or modify its expansion plans.

### *Adjusted EBITDA from continuing operations and Adjusted EBITDAR from continuing operations*

Adjusted Earnings Before Interest, Taxes, Depreciation and Amortization from continuing operations (“Adjusted EBITDA from continuing operations”) and adjusted Earnings Before Interest, Taxes, Depreciation, Amortization and Rent from continuing operations (“Adjusted EBITDAR from continuing operations”) are measures of operating performance that are not calculated in accordance with U.S. generally accepted accounting principles (“GAAP”). The Company believes these non-GAAP measures reflect an additional way of viewing aspects of our operations that, when viewed with our GAAP results and the accompanying quantitative reconciliations to net income (loss) (the most directly comparable GAAP financial measures), provide a more complete understanding of factors or trends affecting our business.

(Amounts in 000s)	Three Months Ended		Nine Months Ended	
	September 30,		September 30,	
	2012	2011	2012	2011
<b>Condensed Consolidated Statement of Operations Data:</b>				
Net income (loss)	\$ (2,440)	\$ 2,780	\$ (2,620)	\$ (2,724)
Impact of discontinued operations	202	158	472	285
Net income (loss) from continuing operations	(2,238)	2,938	(2,148)	(2,439)
Interest expense (net)	3,992	2,223	10,312	5,511
Income tax (benefit) expense	118	204	217	414
Amortization of stock based compensation	269	184	616	741
Depreciation and amortization	2,112	836	5,370	2,188
Acquisition costs, net of gain	342	1,147	1,160	789
Loss on extinguishment of debt	–	58	–	136
Derivative (gain) loss	2,105	(4,745)	1,342	(807)
Other non-routine adjustments	(282)	–	(282)	(632)
Salary retirement and continuation costs	38	–	38	622
Adjusted EBITDA from continuing operations	6,456	2,845	16,625	6,523
Facility rent expense	2,080	1,937	6,196	5,787
Adjusted EBITDAR from continuing operations	\$ 8,536	\$ 4,782	\$ 22,821	\$ 12,310

The Company defines: (i) “Adjusted EBITDA from continuing operations” as net income (loss) from continuing operations before interest expense, income tax expense; depreciation and amortization (including amortization of non-cash stock-based compensation), acquisition costs (net of gains), loss on extinguishment of debt, derivative loss or gain, other non-routine adjustments (primarily a recovery of a receivable and a non-cash settlement gain), and retirement and salary continuation costs; and (ii) “Adjusted EBITDAR from continuing operations” as net income (loss) from continuing operations before interest expense; income tax expense, depreciation and amortization (including amortization of non-cash stock-based compensation), acquisition costs (net of gains), loss on extinguishment of debt, derivative loss; other non-routine adjustments (primarily a recovery of a receivable and a non-cash settlement gain), retirement and salary continuation costs and rent cost.

Adjusted EBITDA from continuing operations and Adjusted EBITDAR from continuing operations should not be considered in isolation or as a substitute for net income, income from operations or cash flows provided by, or used in, operations as determined in accordance with GAAP. Adjusted EBITDA from continuing operations and Adjusted EBITDAR from continuing operations are used by management to focus on operating performance and management without mixing in items of income and expense that relate to the financing and capitalization of the business, fixed rent or lease payments of facilities, derivative loss or gain, and certain

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acquisition related charges.

The Company believes these measures are useful to investors in evaluating the Company' s performance, results of operations and financial position for the following reasons:

- They are helpful in identifying trends in the Company' s day-to-day performance because the items excluded have little or no significance to the Company' s day-to-day operations;
- They provide an assessment of controllable expenses and afford management the ability to make decisions which are expected to facilitate meeting current financial goals as well as achieve optimal financial performance; and
- They are an indication to determine whether or not adjustments to current spending decisions are needed.

AdCare believes that the use of the measures provides a meaningful and consistent comparison of the Company' s underlying business between periods by eliminating certain items required by GAAP, which have little or no significance in the Company' s day-to-day operations.

### Woodland Manor Financing

In connection with the Company' s January 2012 acquisition of the skilled nursing facility located in Springfield, Ohio, known as Woodland Manor, a wholly owned subsidiary of the Company entered into a loan agreement for \$4.8 million. The loan matures in December 2016 with a required final payment of approximately \$4.3 million and accrues interest at the LIBOR rate plus 4% with a minimum rate of 6% per annum. The loan requires monthly payments of principal and interest. Deferred financing costs incurred on the loan amounted to approximately \$0.1 million and are being amortized to interest expense over the life of the loan. The loan has a prepayment penalty of 5% through 2012 declining by 1% each year through 2015. The loan is secured by the Woodland Manor facility and guaranteed by AdCare.

### Eaglewood Village Financings

In April 2012, a wholly owned subsidiary of AdCare entered into a loan agreement with the City of Springfield in the State of Ohio ("City of Springfield") pursuant to which City of Springfield lent to such subsidiary the proceeds from the sale of City of Springfield' s Series 2012 Bonds. The Series 2012 Bonds consist of \$6.6 million in Series 2012A First Mortgage Revenue Bonds and \$0.6 million in Taxable Series 2012B First Mortgage Revenue Bonds. The Series 2012 Bonds were issued pursuant to an April 2012 Indenture of Trust between the City of Springfield and the Bank of Oklahoma. The Series 2012A Bonds mature in May 2042 and accrue interest at a fixed rate of 7.65% per annum. The Series 2012B Bonds mature in May 2021 and accrue interest at a fixed rate of 8.5% per annum. Deferred financing costs incurred on the loan amounted to approximately \$0.6 million and are being amortized to interest expense over the life of the loan. The loan is secured by the Company' s assisted living facility located in Springfield, Ohio known as Eaglewood

Village and guaranteed by AdCare. There is an original issue discount of approximately \$0.3 million and restricted assets of \$0.3 million related to this loan.

In January 2012, two wholly owned subsidiaries of AdCare issued a promissory seller note in the amount of \$0.5 million in connection with the January 2012 acquisition of the assisted living facility located in Springfield, Ohio. The note matures in January 2014 and requires a final payment of approximately \$0.5 million. The note bears interest at 6.5% per annum payable monthly beginning February 2012. The note requires monthly principal and interest payment. The note may be prepaid without penalty at any time.

#### Vandalia HUD Financing

In connection with the Company's January 2012 refinance of the assisted living facility located in Vandalia, Ohio known as Hearth and Home of Vandalia, a wholly owned subsidiary of AdCare obtained a term loan insured by U.S. Department of Housing and Urban Development ("HUD") with a financial institution for a total amount of \$3.7 million that matures in 2041. The HUD term loan requires monthly principal and interest payments with a fixed interest rate of 3.74%. Deferred financing costs incurred on the term loan amounted to approximately \$0.2 million and are being amortized to interest expense over the life of the loan. The HUD term loan has a prepayment penalty of 8% starting in 2014 declining by 1% each year through 2022.

#### Cantone Promissory Notes

In March 2012, AdCare issued an unsecured promissory note to Cantone Asset Management LLC in the amount of \$3.5 million. In April 2012, AdCare issued another promissory note to Cantone Asset Management LLC in the amount of \$1.5 million. In July 2012, these two promissory notes were refinanced through the issuance to Cantone Asset Management LLC in July 2012 of an 8% subordinated convertible note in principal amount of \$5.0 million.

#### Convertible Debt Issued in July 2012

AdCare entered into a Securities Purchase Agreement, dated as of June 28, 2012, with certain accredited investors pursuant to which the Company issued and sold such investors on July 2, 2012 an aggregate of \$7.5 million in principal amount of the Company's 8.0% subordinated convertible notes. The notes bear interest at 8% per annum and such interest is payable quarterly in cash in arrears beginning on September 30, 2012. The notes mature on July 31, 2015. The notes are unsecured and subordinated in right of payment to existing and future senior indebtedness of the Company. The \$7.5 million principal amount of the notes includes a refinance of

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existing indebtedness of \$5.0 million of promissory notes issued to Cantone Asset Management LLC.

At any time on or after the six-month anniversary of the date of issuance of the notes, the notes are convertible at the option of the holder into shares of the Company's common stock at an initial conversion price equal to \$3.97 per share (adjusted for a 5% stock dividend paid on October 22, 2012 as further discussed in Note 10) and subject to adjustment for stock dividends, stock splits, combination of shares, recapitalization and other similar events.

If at any time on or after the six-month anniversary date, the weighted average price of the common stock for any 20 trading days within a period of 30 consecutive trading days equals or exceeds 200% of the conversion price and the average daily trading volume of the common stock during such 20 days exceeds 50,000 shares, then the Company may, subject to the satisfaction of certain other conditions, redeem the notes in cash at a redemption price equal to the sum of 100% of the principal amount being redeemed plus any accrued and unpaid interest on such principal.

In addition, the holders of a majority of the aggregate principal amount of notes then outstanding may require the Company to redeem all or any portion of the notes upon a change of control transaction, as described in the notes, at a redemption price in cash equal to 110% of the redemption amount.

#### Little Rock, Northridge and Woodland Hills Financings

In connection with the Company's April 2012 acquisition of three skilled nursing facilities located in Arkansas known as Little Rock, Northridge and Woodland Hills, certain wholly owned subsidiaries of AdCare entered into a loan agreement for \$21.8 million with PrivateBank. The loan originally matured in March 2017 with a required final payment of approximately \$19.7 million and accrues interest at the LIBOR rate plus 4% with a minimum rate of 6% per annum. The loan requires monthly principal payments plus interest for total current monthly payments of approximately \$0.2 million. Deferred financing costs incurred on the loan amounted to approximately \$0.4 million and are being amortized to interest expense over the life of the loan. The loan has a prepayment penalty of 5% through 2012 declining by 1% each year through 2015. The loan is secured by the three facilities and guaranteed by AdCare. The Company has approximately \$1.8 million of restricted assets related to this loan.

On June 15, 2012, certain wholly owned subsidiaries of AdCare entered into a modification agreement with PrivateBank to modify the terms of the loan agreement. The loan modification agreement, among other things, amended the loan agreement to reflect a maturity date of March 30, 2013. The Company intends on refinancing the loan to long-term. PrivateBank has informed us in writing that, in the event the loan was not refinanced through the U.S. Small Business Administration ("SBA"), it would be the intent of PrivateBank to reinstate the March 30, 2017 maturity date.

#### Abington Place Financing

In connection with the Company's June 2012 acquisition of the skilled nursing facility located in Little Rock, Arkansas known as Abington Place, a wholly owned subsidiary of AdCare entered into a short-term loan agreement for \$3.4 million with Metro City Bank. In August 2012, the maturity date was amended from September 2012 to December 2014. The note accrues interest at the prime rate plus 2.25% with a minimum rate of 6.25% per annum. Deferred financing costs incurred on the loan amounted to approximately \$0.1 million and are being amortized to interest expense over the life of the loan. The loan may be prepaid at any time without penalty. The loan was secured by the Abington Place facility and guaranteed by AdCare.

#### Stone County Financing

In June 2012, a wholly owned subsidiary of AdCare, entered into each of: (i) a Loan Agreement with Metro City Bank ("Metro") in the amount of \$1.3 million; (ii) a Loan Agreement with Metro in the amount of \$1.8 million; and (iii) a Loan Agreement with the Economic Development Corporation of Fulton County (the "CDC"), an economic development corporation working with the SBA. The purpose of these agreements was to refinance existing debt in the original principal amount of \$3.1 million used to acquire select assets of a 97-bed skilled nursing facility located in Arkansas known as the Stone County Nursing and Rehabilitation Facility.

The funding of the Metro loans for \$1.3 million and \$1.8 million occurred on June 8, 2012. The funding of the SBA loan for \$1.3 million occurred in July 2012, and the proceeds were used to satisfy the \$1.3 million Metro loan.

The \$1.8 million Metro loan matures in June 2022 and accrues interest an annual variable rate equal to the published Wall Street Journal prime rate plus 2.25% (with a minimum rate of 6.25% per annum). Deferred financing costs incurred on this loan amounted to approximately \$0.1 million and are being amortized to interest expense over the life of the loan. The Metro loan has a prepayment penalty of 10% for any prepayment through June 2013. The penalty is reduced by 1% each year thereafter until the tenth anniversary, after which there is no prepayment penalty. The Metro loan is secured by the Stone County Nursing and Rehabilitation Facility and is guaranteed by AdCare.

The SBA loan matures in July 2032 and accrues interest at a rate of 2.42% per annum. The SBA Loan is payable in equal monthly installments of principal and interest based on a twenty (20) year amortization schedule. The SBA loan may be prepaid, subject to prepayment premiums during the first 10 years. There are also annual fees associated with the SBA loan, including an SBA guarantee fee. The SBA Loan is secured by a second in priority security deed on the Stone County Nursing and Rehabilitation Facility and guarantees from AdCare, the SBA and a wholly owned subsidiary of AdCare.

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### 2012 Public Common Stock Offering

In March 2012, the Company closed a firm commitment underwritten public offering of 1.1 million shares of common stock at an offering price to the public of \$3.75 per share. The Company also granted the underwriter in the offering an option for 45 days to purchase up to an additional 165,000 shares of common stock to cover over-allotments, if any. In connection with the underwriter's partial exercise of this option, the Company issued an additional 65,000 shares of common stock at an offering price to the public of \$3.75 per share on May 22, 2012. The Company received net proceeds of approximately \$3.8 million after deducting underwriting discounts and other offering-related expenses of approximately \$0.6 million. This transaction occurred prior to the 2012 stock dividend and the share amounts, as disclosed, have not been restated as a result.

### Gemino Credit Agreement

At December 31, 2011, the outstanding balance of approximately \$7.3 million for the revolving credit agreement was classified as current as a result of the required lockbox arrangement and subjective acceleration clauses.

On September 20, 2012, AdCare terminated and paid off all amounts outstanding under that certain Credit Agreement, dated October 29, 2010, between Gemino Healthcare Finance, LLC ("Gemino") and AdCare (the "Gemino credit facility"). The Gemino credit facility was a secured credit facility for borrowings up to \$7.5 million, which was to mature on October 29, 2013. As of September 20, 2012, the amount outstanding in principal balance was approximately \$4.2 million which was paid from funds made available to AdCare from a new credit facility entered into with the PrivateBank and Trust Company ("PrivateBank"). Interest accrued on the principal balance outstanding of the Gemino credit facility at an annual rate equal to LIBOR rate plus the applicable margin of 4.75% to 5.00%, depending on the principal amount outstanding. The Gemino credit facility contained various financial covenants and other restrictions, including a fixed charge cover ratio and maximum loan turn days, as well as borrowing base restrictions. No material early termination penalties were incurred by AdCare as a result of the termination.

### Gemino-Bonterra Amendment

On September 20, 2012, ADK Bonterra/Parkview, LLC, a wholly owned subsidiary of AdCare ("Bonterra"), entered into a Second Amendment to the Credit Agreement with Gemino, which amended that certain Credit Agreement, dated April 27, 2011, between Bonterra and Gemino (the "Gemino-Bonterra credit facility"). The Gemino-Bonterra credit facility is a secured credit facility for borrowings up to \$2.0 million. The amendment extends the term of the Gemino-Bonterra credit facility from October 29, 2013 to January 31, 2014 and amends certain financial covenants regarding Bonterra's fixed charge coverage ratio, maximum loan turn days and applicable margin. Interest accrues on the principal balance outstanding at an annual rate equal to LIBOR plus the applicable margin of 4.75% to 5.00%, depending upon the principal amount outstanding. As of September 30, 2012, approximately \$1.4 million was outstanding under the Gemino-Bonterra credit facility.

### PrivateBank Credit Facility

On September 20, 2012, in connection with the payoff of the Gemino credit facility, AdCare entered into a Loan and Security Agreement with PrivateBank. The PrivateBank credit facility provides for a three-year \$10.6 million principal amount senior secured revolving credit facility limited to certain borrowing base restrictions and offset by a \$0.1 million letter of credit.

The PrivateBank credit facility matures on September 20, 2015. Interest accrues on the principal balance thereof at an annual rate of the greater of 1% plus the prime interest rate per annum, or 5% per annum, and payments for the interest are payable monthly, commencing on October 1, 2012. In addition, there is a non-utilization fee of 0.00% of the unused portion of the available credit. The PrivateBank credit facility may be prepaid at any time without premium or penalty, provided that such prepayment is accompanied by a simultaneous payment of all accrued but unpaid interest through the date of prepayment. The PrivateBank credit facility is secured by a first priority security interest in the real property and improvements constituting nursing facilities owned and operated by AdCare. AdCare has unconditionally guaranteed all amounts owing under the PrivateBank credit facility.

Proceeds from the PrivateBank credit facility were used to pay off all amounts outstanding under (i) a separate \$2.0 million credit facility with PrivateBank under which certain subsidiaries of AdCare were borrowers and (ii) the Gemino credit facility.

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The PrivateBank credit facility was modified in October 2012. See Note 16 in the “Notes to the Condensed Consolidated Financial Statements” section of Part 1, Item 1 of this Quarterly Report.

### *Glenvue*

In July 2012, a wholly owned subsidiary of AdCare financed the skilled nursing facility located in Glennville, Georgia known as Glenvue Health & Rehabilitation by entering into a loan agreement for \$6.6 million with PrivateBank. The loan matures in July 2014 with a required final payment of approximately \$6.4 million and accrues interest at an annual rate of the greater of 6.0% per annum; or the LIBOR rate plus 4.0% per annum. The loan requires monthly principal payments and interest. Deferred financing costs incurred on the loan amounted to approximately \$0.1 million and are being amortized to interest expense over the life of the loan. The loan is secured by the Glenvue facility and guaranteed by AdCare.

### *Companions Specialized Care*

In August 2012, a wholly owned subsidiary of AdCare financed the skilled nursing facility located in Tulsa, Oklahoma known as Companions Specialized Care Center by entering into a loan agreement for \$5.0 million with Contemporary Healthcare Capital. The loan matures in August 2015 with a required final payment of \$5.0 million and accrues interest at a fixed rate of 8.5% per annum. Deferred financing costs incurred on the loan amounted to approximately \$0.2 million and are being amortized to interest expense over the life of the loan. The loan has a prepayment penalty of 5% during the first year of the term and 1% during the second year of the term. The loan is secured by the Companions Specialized Care facility and guaranteed by AdCare.

### *Quail Creek*

In July 2012, a wholly owned subsidiary of AdCare financed the skilled nursing facility located in Oklahoma City, Oklahoma known as Quail Creek Nursing by the assumption of existing indebtedness under that certain Loan Agreement and Indenture of First Mortgage with The Bank of New York Mellon Global Corporate Trust, as assignee of The Liberty National Bank and Trust of that certain Bond Indenture, dated September 1, 1986, as amended by that certain First Amendment to the Loan Agreement and Indenture of First Mortgage dated as of September 1, 2001. The indebtedness under the Loan Agreement and Indenture consists of a principal amount of \$2.8 million. The loan matures in August 2016, accrues interest at a fixed rate of 10.25% per annum. The loan is secured by the Quail Creek facility.

For information on financings that have been entered into subsequent to September 30, 2012, see Note 16 in the “Notes to Condensed Consolidated Financial Statements” section of Part I, Item 1 of this Quarterly Report.

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

	<u>Nine Months Ended September 30</u>	
	<u>2012</u>	<u>2011</u>
Net cash provided by operating activities - continuing operations	\$ 5,771	\$ 1,126
Net cash used in operating activities - discontinued operations	(648)	(96)
Net cash used in investing activities - continuing operations	(16,931)	(13,236)
Net cash provided by financing activities - continuing operations	14,475	18,479
Net cash used in financing activities - discontinued operations	(147)	(134)
Net change in cash and cash equivalents	2,520	6,139
Cash and cash equivalents at beginning of period	7,364	3,911
Cash and cash equivalents at end of period	<u>\$ 9,884</u>	<u>\$ 10,050</u>

*Nine months ended September 30, 2012*

Net cash provided by operating activities for the nine months ended September 30, 2012, was approximately \$5.1 million consisting primarily of our net income from operations, changes in working capital, and noncash charges (primarily depreciation and amortization, share-based compensation, difference between straight-line rent and rent paid, provision for bad debt and amortization of debt discounts and related deferred financing costs); all primarily the result of routine operating activities.

Net cash used in investing activities for the nine months ended September 30, 2012, was approximately \$16.9 million. This is primarily the result of funding our acquisitions, including making escrow deposits and investments in equipment and other facility improvements.

Net cash provided by financing activities was approximately \$14.3 million for the nine months ended September 30, 2012. This is primarily the result of cash proceeds received from public stock offering, and proceeds from debt financings to primarily to fund our

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acquisitions and to increase borrowings in our revolving credit facilities, partially offset by repayments of existing debt obligations.

*Nine months ended September 30, 2011*

Net cash provided by operating activities for the nine months ended September 30, 2011 was approximately \$1.0 million consisting primarily of our income from operations less the noncash gain on acquisitions, and changes in working capital, and noncash charges (primarily depreciation and amortization, the derivative loss, share-based compensation, difference between straight-line rent and rent paid, provisions for bad debts and amortization of debt discounts and related deferred financing costs); all primarily the result of routine operating activities.

Net cash used in investing activities for the nine months ended September 30, 2011, was approximately \$13.2 million. This is primarily the result of funding our acquisitions, including making escrow deposits and investments in equipment and other facility improvements.

Net cash provided by financing activities was approximately \$18.3 million for the nine months ended September 30, 2011. This is primarily the result of increases in borrowings on the line of credit, proceeds from debt financings primarily to fund our acquisitions and proceeds from exercises of warrants and options, partially offset by repayments of existing debt obligations.

### Item 3. Quantitative and Qualitative Disclosure About Market Risk

Not required.

### Item 4. Controls and Procedures

We maintain disclosure controls and procedures that are designed to ensure that information required to be disclosed in our reports filed pursuant to the Securities Exchange Act of 1934, as amended (the "Exchange Act"), is recorded, processed, summarized and reported within the time periods specified in the rules and forms of the Securities and Exchange Commission and that such information is accumulated and communicated to our management, including our Chief Executive Officer and Chief Financial Officer, as appropriate, to allow for timely decisions regarding required disclosure. In designing and evaluating the disclosure controls and procedures, management recognizes that any controls and procedures, no matter how well designed and operated, can provide only reasonable assurance of achieving the desired control objectives, and management is required to apply its judgment in evaluating the cost-benefit relationship of possible controls and procedures.

Our management, with the participation of our Chief Executive Officer and Chief Financial Officer, has evaluated the effectiveness of our disclosure controls and procedures (as such term is defined in Rules 13a-15(e) and 15d-15(e) under the Exchange Act) as of the end of the period covered by this Quarterly Report (the "Evaluation Date"). Based on such evaluation, our Chief Executive Officer and Chief Financial Officer have concluded that, as of the Evaluation Date, our disclosure controls and procedures are effective.

There have not been any changes in our internal control over financial reporting (as such term is defined in Rules 13a-15(f) and 15d-15(f) under the Exchange Act) during the nine months ended September 30, 2012 that have been materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

## **Part II. Other Information**

### Item 1. Legal Proceedings

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

We operate in an industry that is extremely regulated. As such, in the ordinary course of business, we are continuously subject to state and federal regulatory scrutiny, supervision and control. Such regulatory scrutiny often includes inquiries, investigations, examinations, audits, site visits and surveys, some of which are non-routine. In addition to being subject to direct regulatory oversight of state and federal regulatory agencies, our industry is frequently subject to the regulatory practices, which could subject us to civil, administrative or criminal fines, penalties or restitutionary relief, and reimbursement authorities could also seek the suspension or exclusion of the provider or individual from participation in their program. We believe that there has been, and will continue to be, an increase in governmental investigations of long-term care providers, particularly in the area of Medicare/Medicaid false claims, as well as an increase in enforcement actions resulting from these investigations. Adverse determinations in legal proceedings or governmental investigations against or involving us, whether currently asserted or arising in the future, could have a material adverse effect on our financial position, results of operations and cash flows.



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Item 1A. Risk Factors

Our operations and financial results are subject to various risks and uncertainties that could adversely affect our business, financial condition, results of operations, cash flows, and trading price of our common stock. Please refer to our Annual Report for additional information concerning these and other uncertainties that could negatively impact the Company.

Item 5. Other Information

On August 31, 2012, the Company issued to a vendor a warrant to purchase 15,750 shares of common stock at an exercise price of \$4.37 per share. The warrant was issued (and if the warrant is exercised, then the underlying shares of common stock will be issued) without registration under the Securities Act of 1933, as amended, in reliance upon the exemption set forth in Section 4(2) thereof. The Company relied on this exemption based upon the private nature of the transaction and representations made by the vendor as to its sophistication and intent to hold the securities for its own account and without a view to distribute, among other things. The warrant has a three-year term and may be exercised on a cashless basis.

Item 6. Exhibits

The agreements included as exhibits to this Quarterly Report are included to provide information regarding the terms of these agreements and are not intended to provide any other factual or disclosure information about the Company, its business or the other parties to these agreements. These agreements may contain representations and warranties by each of the parties to the applicable agreement. These representations and warranties have been made solely for the benefit of the other parties to the applicable agreement and:

- should not in all instances be treated as categorical statements of fact, but rather as a way of allocating the risk to one of the parties if those statements prove to be inaccurate;
- have been qualified by disclosures that were made to the other party in connection with the negotiation of the applicable agreement, which disclosures are not necessarily reflected in the agreement;
- may apply standards of materiality in a way that is different from what may be viewed as material to investors; and
- were made only as of the date of the applicable agreement or such other date or dates as may be specified in the agreement and are subject to more recent developments.

Accordingly, these representations and warranties may not describe the actual state of affairs as of the date they were made or at any other time, and should not be relied upon by investors.

**EXHIBIT INDEX**

Exhibit No.	Description	Method of Filing
2.1	Amendment to Purchase Agreement, dated July 19, 2012, between 1761 Pinewood Holdings, LLC and AdCare Property Holdings, LLC	Filed herewith

2.2	Purchase and Sale Agreement, dated as of August 9, 2012, between Winyah Nursing Home, Inc. and AdCare Property Holdings, LLC	Incorporated by reference from Exhibit 2.1 to the Registrant' s Current Report on Form 8-K filed August 15, 2012
2.3	Second Amendment to Purchase Agreement, dated as of August 31, 2012, between Winyah Nursing Home, Inc. and AdCare Property Holdings, LLC	Filed herewith
2.4	Third Amendment to Purchase Agreement, dated as of September 27, 2012, between 1761 Pinewood Holdings, LLC and AdCare Property Holdings, LLC	Filed herewith
2.5	Agreement of Sale, dated October 11, 2012, between AdCare Health Systems, Inc., certain of its subsidiaries named therein and CHP Acquisition Company, LLC	Filed herewith

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<u>Exhibit No.</u>	<u>Description</u>	<u>Method of Filing</u>
2.6	Assignment of Purchase and Sale Agreement, dated October 12, 2012, executed by AdCare Property Holdings, LLC in favor of Edwards Redeemer Property Holdings, LLC and ER Nursing, LLC	Filed herewith
2.7	Assignment of Purchase and Sale Agreement, dated October 12, 2012, executed by AdCare Property Holdings, LLC in favor of WP Oklahoma Nursing, LLC	Filed herewith
2.8	Membership Interest Power, dated October 12, 2012	Filed herewith
2.9	Fourth Amendment to Purchase and Sale Agreement, dated October 8, 2012, between AdCare Property Holdings, LLC and First Commercial Bank	Incorporated by reference from Exhibit 2.5 to the Registrant' s Current Report on Form 8-K filed October 10, 2012
2.10	Membership Interest Purchase Agreement, dated as of September 25, 2012, by and between John B. Montgomery and Michael Morton and AdCare Property Holdings, LLC	Incorporated by reference from Exhibit 2.1 to the Registrant' s Current Report on Form 8-K filed October 1, 2012
2.11	Addendum to Membership Interest Purchase Agreement, dated as of September 26, 2012, by and between John B. Montgomery and Michael Morton and AdCare Property Holdings, LLC	Incorporated by reference from Exhibit 2.2 to the Registrant' s Current Report on Form 8-K filed October 1, 2012
2.12	First Amendment to Purchase and Sale Agreement, effective as of October 31, 2012, between AdCare Property Holdings, LLC and Winyah Nursing Home, LLC	Filed herewith

3.1	Amended and Restated Articles of Incorporation	Incorporated by reference from Exhibit 3.1 of the Registrant's Registration Statement Form SB (Registration No. 333-131542) filed February 3, 2006
3.2	Code of Regulations	Incorporated by reference from Exhibit 3.2 of the Registrant's Registration Statement Form SB (Registration No. 333-131542) filed February 3, 2006
3.3	Amendment to Amended and Restated Articles of Incorporation	Incorporated by reference to Exhibit 3.3 of the Registrant's Quarterly Report on Form 10-Q for the quarter ended September 30, 2011
3.4	Affidavit, dated June 28, 2012	Incorporated by reference to Exhibit 3.1 of the Registrant's Current Report on Form 8-K filed on July 5, 2012
3.5	Certificate of Amendment to Amended and Restated Articles of Incorporation of AdCare Health Systems, Inc.	Incorporated by reference to Exhibit 3.5 of the Registrant's Registration Statement on Form 8-A filed on November 7, 2012
4.1	Warrant to Purchase 312,500 Shares of Common Stock, dated April 1, 2012, issued by AdCare Health Systems, Inc. to Strome Alpha Offshore Ltd.	Incorporated by reference to Exhibit 4.1 of the Registrant's Quarterly Report on Form 10-Q for the quarter ended March 30, 2012
4.2	Warrant to Purchase 300,000 Shares of Common Stock, dated March 30, 2012, issued by AdCare Health Systems, Inc. to Cantone Asset Management LLC	Incorporated by reference to Exhibit 4.2 of the Registrant's Quarterly Report on Form 10-Q for the quarter ended March 30, 2012
4.3	Warrant to Purchase 100,000 Shares of Common Stock, dated July 2, 2012, issued by AdCare Health Systems, Inc. to Cantone Research, Inc.	Incorporated by reference to Exhibit 4.3 of the Registrant's Quarterly Report on Form 10-Q for the quarter ended June 30, 2012

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<u>Exhibit No.</u>	<u>Description</u>	<u>Method of Filing</u>
10.1	Form of Securities Purchase Agreement, dated as of June 28, 2012, between AdCare Health Systems, Inc. and the Buyers signatory thereto	Incorporated by reference from Exhibit 99.1 to the Registrant's Current Report on Form 8-K filed July 5, 2012

10.2	Form of Registration Rights Agreement, dated as of June 28, 2012, between AdCare Health Systems, Inc. and the Buyers signatory thereto	Incorporated by reference from Exhibit 99.2 to the Registrant' s Current Report on Form 8-K filed July 5, 2012
10.3	Form of 8% Subordinated Convertible Note Due 2015 issued by AdCare Health Systems, Inc.	Incorporated by reference from Exhibit 99.3 to the Registrant' s Current Report on Form 8-K filed July 5, 2012
10.4	Loan Agreement, dated as of July 2, 2012, by and between Glenvue H&R Property Holdings, LLC and the PrivateBank and Trust Company	Incorporated by reference to Exhibit 10.32 of the Registrant' s Quarterly Report on Form 10-Q for the quarter ended June 30, 2012
10.5	Promissory Note, dated July 2, 2012, issued by Glenvue H&R Property Holdings, LLC in favor of the PrivateBank and Trust Company in the amount of \$6,600,000	Incorporated by reference to Exhibit 10.33 of the Registrant' s Quarterly Report on Form 10-Q for the quarter ended June 30, 2012
10.6	Deed to Secure Debt, Security Agreement and Assignment of Leases and Rents, dated as of July 2, 2012, from Glenvue H&R Property Holdings, LLC to the PrivateBank and Trust Company	Incorporated by reference to Exhibit 10.34 of the Registrant' s Quarterly Report on Form 10-Q for the quarter ended June 30, 2012
10.7	Assignment of Leases and Rents, dated as of July 2, 2012, from Glenvue H&R Property Holdings, LLC to the PrivateBank and Trust Company	Incorporated by reference to Exhibit 10.35 of the Registrant' s Quarterly Report on Form 10-Q for the quarter ended June 30, 2012
10.8	Guaranty of Payment and Performance, dated as of July 2, 2012, issued by Glenvue H&R Property Holdings, LLC and AdCare Health Systems, Inc. for the benefit of The PrivateBank and Trust Company	Incorporated by reference to Exhibit 10.36 of the Registrant' s Quarterly Report on Form 10-Q for the quarter ended June 30, 2012
10.9	Assignment and Assumption Agreement, dated as of July 1, 2012, by and between Westlake Nursing Home Limited Partnership and QC Property Holdings, LLC	Incorporated by reference to Exhibit 10.37 of the Registrant' s Quarterly Report on Form 10-Q for the quarter ended June 30, 2012
10.10	Loan Agreement and Indenture of First Mortgage, dated as of September 1, 1986, by and among Oklahoma County Industrial Authority, Westlake Nursing Home Limited Partnership and The Liberty National Bank and Trust Company of Oklahoma City, as Trustee	Incorporated by reference to Exhibit 10.38 of the Registrant' s Quarterly Report on Form 10-Q for the quarter ended June 30, 2012
10.11	First Amendment to Loan Agreement and Indenture of First Mortgage, dated September 1, 2001, by and among Oklahoma	Incorporated by reference to Exhibit 10.39 of the Registrant' s

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<u>Exhibit No.</u>	<u>Description</u>	<u>Method of Filing</u>
	County Industrial Authority, Westlake Nursing Home, L.P. and Bank One Trust Company, N.A., as Trustee	Quarterly Report on Form 10-Q for the quarter ended June 30, 2012
10.12	Loan Agreement, made as of August 17, 2012, by and among CSCC Property Holdings, LLC, CSCC Nursing, LLC and Contemporary Healthcare Senior Lien Fund I, L.P.	Filed herewith
10.13	Loan Agreement, made as of August 17, 2012, by and among CSCC Property Holdings, LLC, CSCC Nursing, LLC and Contemporary Healthcare Fund I, L.P.	Filed herewith
10.14	Promissory Note, dated August 17, 2012, issued by CSCC Nursing, LLC and CSCC Property Holdings, LLC in favor of Contemporary Healthcare Senior Lien Fund I, L.P. in the amount of \$5,000,000	Filed herewith
10.15	Revolving Loan Promissory Note, made as of August 17, 2012, by and among CSCC Nursing, LLC and CSCC Property Holdings, LLC in favor of Contemporary Healthcare Fund I, L.P. in the amount of \$600,000	Filed herewith
10.16	Assignment of Leases and Rents, dated as of August 17, 2012, by and among CSCC Property Holdings, LLC, CSCC Nursing, LLC and Contemporary Healthcare Senior Lien Fund I, L.P.	Filed herewith
10.17	Mortgage, Assignment of Rents and Leases, Security Agreement and Fixture Filing, dated August 17, 2012, made and entered into by CSCC Property Holdings, LLC in favor of Contemporary Healthcare Senior Lien Fund I, L.P.	Filed herewith
10.18	Guaranty of Payment and Performance, made as of August 17, 2012, by AdCare Health Systems, Inc. in favor of Contemporary Healthcare Fund I, L.P.	Filed herewith
10.19	Guaranty of Payment and Performance, made as of August 17, 2012, by AdCare Oklahoma Management, LLC in favor of Contemporary Healthcare Fund I, L.P.	Filed herewith
10.20	Guaranty of Payment and Performance, made as of August 17, 2012, by AdCare Health Systems, Inc. in favor of Contemporary Healthcare Senior Lien Fund I, L.P.	Filed herewith
10.21	Guaranty of Payment and Performance, made as of August 17, 2012, by AdCare Oklahoma Management, LLC in favor of Contemporary Healthcare Senior Lien Fund I, L.P.	Filed herewith

10.22	Security Agreement, made as of August 17, 2012, by and among CSCC Property Holdings, LLC, CSCC Nursing, LLC and Contemporary Healthcare Fund I, L.P.	Filed herewith
10.23	Security Agreement, made as of August 17, 2012, by and among CSCC Property Holdings, LLC, CSCC Nursing, LLC and Contemporary Healthcare Senior Lien Fund I, L.P.	Filed herewith
10.24	Loan and Security Agreement, dated as of September 20, 2012, by and among The PrivateBank and Trust Company and the Borrowers named therein	Filed herewith

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<b>Exhibit No.</b>	<b>Description</b>	<b>Method of Filing</b>
10.25	Modification Agreement, dated as of October 26, 2012, by and among The PrivateBank and Trust Company and the Borrowers named therein	Filed herewith
10.26	Promissory Note, dated September 20, 2012, issued by the subsidiaries of AdCare Health Systems, Inc. named therein in favor of The PrivateBank and Trust Company in the amount of \$10,600,000	Filed herewith
10.27	Guaranty of Payment and Performance, made as of September 20, 2012, by AdCare Health Systems, Inc. in favor of The PrivateBank and Trust Company	Filed herewith
10.28	Payoff Confirmation Letter, dated September 20, 2012, from Gemino Healthcare Finance, LLC to AdCare Health Systems, Inc. and certain of its subsidiaries named therein	Filed herewith
10.29	Release of Guarantees, dated September 20, 2012, from Gemino Healthcare Finance, LLC to certain subsidiaries of AdCare Health Systems, Inc. named therein	Filed herewith
10.30	Second Amendment to Credit Agreement, dated September 20, 2012, by and between ADK Bonterra/Parkview, LLC and Gemino Healthcare Finance, LLC	Filed herewith
10.31	Temporary Extension Agreement, dated August 29, 2012, by and between APH & R Property Holdings, LLC and Metro City Bank	Filed herewith
10.32	Loan Agreement, dated as of April 12, 2012, between the City of Springfield, Ohio and Eaglewood Property Holdings, LLC	Incorporated by reference to Exhibit 10.18 of the Registrant' s Quarterly Report on Form 10-Q for the quarter ended March 30, 2012

10.33	Guaranty Agreement, dated as of April 12, 2012, made and entered into by AdCare Health Systems, Inc., to and for the benefit of BOKF, NA dba Bank of Oklahoma	Incorporated by reference to Exhibit 10.19 of the Registrant' s Quarterly Report on Form 10-Q for the quarter ended March 30, 2012
10.34	Land Use Restriction Agreement, dated as of April 12, 2012, by and between BOKF, NA dba Bank of Oklahoma and Eaglewood Property Holdings, LLC	Incorporated by reference to Exhibit 10.20 of the Registrant' s Quarterly Report on Form 10-Q for the quarter ended March 30, 2012
10.35	Open-End Mortgage, Assignment of Leases and Security Agreement, dated April 12, 2012, from Eaglewood Property Holdings, LLC to BOKF, NA dba Bank of Oklahoma	Incorporated by reference to Exhibit 10.21 of the Registrant' s Quarterly Report on Form 10-Q for the quarter ended March 30, 2012
10.36	Loan Agreement, dated April 30, 2012, by and between APH&R Property Holdings, LLC and Metro City Bank	Incorporated by reference from Exhibit 99.1 to the Registrant' s Current Report on Form 8-K filed May 3, 2012
10.37	Promissory Note, dated April 30, 2012, issued by APH&R Property Holdings, LLC in favor of Metro City Bank in the amount of \$3,425,500	Incorporated by reference from Exhibit 99.2 to the Registrant' s Current Report on Form 8-K filed May 3, 2012
10.38	Mortgage and Security Agreement, dated April 30, 2012, between APH&R Property Holdings, LLC and Metro City Bank	Incorporated by reference from Exhibit 99.3 to the Registrant' s Current Report on Form 8-K filed May 3, 2012
10.39	Security Agreement, dated April 30, 2012, between APH&R Property Holdings, LLC and Metro City Bank	Incorporated by reference from Exhibit 99.4 to the Registrant' s Current Report on Form 8-K filed May 3, 2012
10.40	Guaranty, dated as of April 30, 2012, between APH&R Property Holdings, LLC in favor of Metro City Bank	Incorporated by reference from Exhibit 99.5 to the Registrant' s Current Report on Form 8-K filed May 3, 2012
10.41	Guaranty, dated as of April 30, 2012, between AdCare Health Systems, Inc. in favor of Metro City Bank	Incorporated by reference from Exhibit 99.6 to the Registrant' s Current Report on Form 8-K filed May 3, 2012
10.42	Collateral Assignment of Certificate of Deposit, dated April 30, 2012, by and between APH&R Property Holdings, LLC	Incorporated by reference from Exhibit 99.7 to the Registrant' s

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Exhibit No.	Description	Method of Filing
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	and Metro City Bank	Current Report on Form 8-K filed May 3, 2012
10.43	Promissory Note, dated April 27, 2012, issued by Cantone Asset Management LLC in favor of AdCare Health Systems, Inc. in the amount of \$1,500,000	Incorporated by reference from Exhibit 99.8 to the Registrant' s Current Report on Form 8-K filed May 3, 2012
10.44	Promissory Note, dated June 8, 2012, issued by Mt. V Property Holdings, LLC in favor of Metro City Bank in the amount of \$1,800,000	Incorporated by reference from Exhibit 10.13 of the Registrant' s Quarterly Report on Form 10-Q for the quarter ended June 30, 2012
10.45	Loan Agreement, dated June 8, 2012, by and between Mt. V Property Holdings, LLC and Metro City Bank	Incorporated by reference from Exhibit 10.14 of the Registrant' s Quarterly Report on Form 10-Q for the quarter ended June 30, 2012
10.46	Mortgage and Security Agreement, dated June 8, 2012, by and between Mt. V Property Holdings, LLC and Metro City Bank	Incorporated by reference from Exhibit 10.15 of the Registrant' s Quarterly Report on Form 10-Q for the quarter ended June 30, 2012
10.47	Assignment of Leases and Rents, dated June 8, 2012, by and between Mt. V Property Holdings, LLC and Metro City Bank	Incorporated by reference from Exhibit 10.16 of the Registrant' s Quarterly Report on Form 10-Q for the quarter ended June 30, 2012
10.48	Security Agreement, dated June 8, 2012, by and between Mt. V Property Holdings, LLC and Metro City Bank	Incorporated by reference from Exhibit 10.17 of the Registrant' s Quarterly Report on Form 10-Q for the quarter ended June 30, 2012
10.49	Guaranty, dated June 8, 2012, made by AdCare Health Systems, Inc. in favor of Metro City Bank	Incorporated by reference from Exhibit 10.18 of the Registrant' s Quarterly Report on Form 10-Q for the quarter ended June 30, 2012
10.50	Promissory Note, dated June 8, 2012, issued by Mt. V Property Holdings, LLC in favor of Metro City Bank in the amount of \$1,267,000	Incorporated by reference from Exhibit 10.19 of the Registrant' s Quarterly Report on Form 10-Q for the quarter ended June 30, 2012
10.51	Loan Agreement, dated June 8, 2012, by and between Mt. V Property Holdings, LLC and Metro City Bank	Incorporated by reference from Exhibit 10.20 of the Registrant' s Quarterly Report on Form 10-Q for the quarter ended June 30, 2012
10.52	Mortgage and Security Agreement, dated June 8, 2012, by and between Mt. V Property Holdings, LLC and Metro City Bank	Incorporated by reference from Exhibit 10.21 of the Registrant' s Quarterly



10.53 Assignment of Leases and Rents, dated June 8, 2012, by and  
Incorporated by reference from  
Exhibit 10.22 of the Registrant' s

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<u>Exhibit No.</u>	<u>Description</u>	<u>Method of Filing</u>
	between Mt. V Property Holdings, LLC and Metro City Bank	Quarterly Report on Form 10-Q for the quarter ended June 30, 2012
10.54	Security Agreement, dated June 8, 2012, by and between Mt. V Property Holdings, LLC and Metro City Bank	Incorporated by reference from Exhibit 10.23 of the Registrant' s Quarterly Report on Form 10-Q for the quarter ended June 30, 2012
10.55	Guaranty, dated June 8, 2012, made by AdCare Health Systems, Inc. in favor of Metro City Bank	Incorporated by reference from Exhibit 10.24 of the Registrant' s Quarterly Report on Form 10-Q for the quarter ended June 30, 2012
10.56	Promissory Note, dated June 8, 2012, issued by Mt. V Property Holdings, LLC in favor of Economic Development Corporation of Fulton County in the amount of \$1,304,000	Incorporated by reference from Exhibit 10.25 of the Registrant' s Quarterly Report on Form 10-Q for the quarter ended June 30, 2012
10.57	Loan Agreement, dated June 8, 2012, by and between Mt. V Property Holdings, LLC, Mountain View Nursing, LLC and Economic Development Corporation of Fulton County	Incorporated by reference from Exhibit 10.26 of the Registrant' s Quarterly Report on Form 10-Q for the quarter ended June 30, 2012
10.58	Security Agreement, dated June 8, 2012, by and between Mt. V Property Holdings, LLC and Economic Development Corporation of Fulton County	Incorporated by reference from Exhibit 10.27 of the Registrant' s Quarterly Report on Form 10-Q for the quarter ended June 30, 2012
10.59	Mortgage and Security Agreement, dated June 8, 2012, by and between Mt. V Property Holdings, LLC and Economic Development Corporation of Fulton County	Incorporated by reference from Exhibit 10.28 of the Registrant' s Quarterly Report on Form 10-Q for the quarter ended June 30, 2012
10.60	Assignment of Leases and Rents, dated June 8, 2012, by and between Mt. V Property Holdings, LLC and Economic Development Corporation of Fulton County	Incorporated by reference from Exhibit 10.29 of the Registrant' s Quarterly

		Report on Form 10-Q for the quarter ended June 30, 2012
10.61	Unconditional Guarantee, dated June 8, 2012, issued by Mountain View Nursing, LLC in favor of Economic Development Corporation of Fulton County	Incorporated by reference from Exhibit 10.30 of the Registrant' s Quarterly Report on Form 10-Q for the quarter ended June 30, 2012
10.62	Unconditional Guarantee, dated June 8, 2012, issued by AdCare Health Systems, Inc. in favor of Economic Development Corporation of Fulton County	Incorporated by reference from Exhibit 10.31 of the Registrant' s Quarterly Report on Form 10-Q for the quarter ended June 30, 2012
10.63	Bond Purchase Agreement, dated April 10, 2012, among Lawson Financial Corporation, The City of Springfield, Ohio and Eaglewood Property Holdings, LLC	Incorporated by reference from Exhibit 10.40 of the Registrant' s Quarterly Report on Form 10-Q for the quarter ended June 30, 2012
10.64	Note Purchase Agreement, dated April 12, 2012, by and between Cantone Asset Management LLC and AdCare Health	Incorporated by reference from Exhibit 10.41 of the Registrant' s

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<u>Exhibit No.</u>	<u>Description</u>	<u>Method of Filing</u>
	Systems, Inc.	Quarterly Report on Form 10-Q for the quarter ended June 30, 2012
10.65	Employment Agreement, dated August 7, 2012, between AdCare Health Systems, Inc. and Martin D. Brew	Incorporated by reference from Exhibit 10.42 of the Registrant' s Quarterly Report on Form 10-Q for the quarter ended June 30, 2012
10.66	Modification Agreement, dated June 15, 2012, among Little Rock HC&R Property Holdings, LLC, Northridge HC&R Property Holdings, LLC, Woodland Hills HC Property Holdings, LLC and The PrivateBank and Trust Company	Incorporated by reference from Exhibit 10.43 of the Registrant' s Quarterly Report on Form 10-Q for the quarter ended June 30, 2012
10.67	Amendment, entered into as of July 26, 2012, by and between Christopher F. Brogdon and Hearth & Home of Ohio, Inc.	Incorporated by reference from Exhibit 10.47 of the Registrant' s Quarterly Report on Form 10-Q for the quarter ended June 30, 2012
10.68	Employment Agreement, dated August 6, 2012, between AdCare Health Systems, Inc. and Melissa L. Green	Incorporated by reference from Exhibit 10.48 of the Registrant' s Quarterly Report on Form 10-Q for the quarter ended June 30, 2012

31.1	Certification of CEO pursuant to Section 302 of the Sarbanes-Oxley Act	Filed herewith
31.2	Certification of CFO pursuant to Section 302 of the Sarbanes-Oxley Act	Filed herewith
32.1	Certification of CEO pursuant to Section 906 of the Sarbanes-Oxley Act	Filed herewith
32.2	Certification of CFO pursuant to Section 906 of the Sarbanes-Oxley Act	Filed herewith
101	The following financial information from AdCare Health Systems, Inc. Quarterly Report on Form 10-Q for the quarter ended September 30, 2012, formatted in XBRL (eXtensible Business Reporting Language): (i) Consolidated Statements of Operations for the three months ended September 30, 2012 and 2011 and for the nine months ended September 30, 2012 and 2011, (ii) Consolidated Balance Sheets as of September 30, 2012 and December 31, 2011, (iii) Consolidated Statements of Cash Flows for the nine months ended September 30, 2012 and 2011, (iv) Consolidated Statements of Stockholders' Equity for the nine months ended September 30, 2012 and (v) the Notes to Consolidated Financial Statements.	Filed herewith

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**SIGNATURES**

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused the report to be signed on its behalf by the undersigned, thereunto duly authorized.

**ADCARE HEALTH SYSTEMS, INC.  
(Registrant)**

Date: November 13, 2012

/s/Boyd P. Gentry  
Boyd P. Gentry  
Chief Executive Officer  
(Principal Executive Officer)

Date: November 13, 2012

/s/Martin D. Brew  
Martin D. Brew  
Chief Financial Officer  
(Principal Financial and Accounting Officer)

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**EXHIBIT INDEX**

<b>Exhibit No.</b>	<b>Description</b>	<b>Method of Filing</b>
2.1	Amendment to Purchase Agreement, dated July 19, 2012, between 1761 Pinewood Holdings, LLC and AdCare Property Holdings, LLC	Filed herewith
2.2	Purchase and Sale Agreement, dated as of August 9, 2012, between Winyah Nursing Home, Inc. and AdCare Property Holdings, LLC	Incorporated by reference from Exhibit 2.1 to the Registrant' s Current Report on Form 8-K filed August 15, 2012
2.3	Second Amendment to Purchase Agreement, dated as of August 31, 2012, between Winyah Nursing Home, Inc. and AdCare Property Holdings, LLC	Filed herewith
2.4	Third Amendment to Purchase Agreement, dated as of September 27, 2012, between 1761 Pinewood Holdings, LLC and AdCare Property Holdings, LLC	Filed herewith
2.5	Agreement of Sale, dated October 11, 2012, between AdCare Health Systems, Inc., certain of its subsidiaries named therein and CHP Acquisition Company, LLC	Filed herewith
2.6	Assignment of Purchase and Sale Agreement, dated October 12, 2012, executed by AdCare Property Holdings, LLC in favor of Edwards Redeemer Property Holdings, LLC and ER Nursing, LLC	Filed herewith
2.7	Assignment of Purchase and Sale Agreement, dated October 12, 2012, executed by AdCare Property Holdings, LLC in favor of WP Oklahoma Nursing, LLC	Filed herewith
2.8	Membership Interest Power, dated October 12, 2012	Filed herewith
2.9	Fourth Amendment to Purchase and Sale Agreement, dated October 8, 2012, between AdCare Property Holdings, LLC and First Commercial Bank	Incorporated by reference from Exhibit 2.5 to the Registrant' s Current Report on Form 8-K filed October 10, 2012
2.10	Membership Interest Purchase Agreement, dated as of September 25, 2012, by and between John B. Montgomery and Michael Morton and AdCare Property Holdings, LLC	Incorporated by reference from Exhibit 2.1 to the Registrant' s Current Report on Form 8-K filed

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<b>Exhibit No.</b>	<b>Description</b>	<b>Method of Filing</b>
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		October 1, 2012
2.11	Addendum to Membership Interest Purchase Agreement, dated as of September 26, 2012, by and between John B. Montgomery and Michael Morton and AdCare Property Holdings, LLC	Incorporated by reference from Exhibit 2.2 to the Registrant' s Current Report on Form 8-K filed October 1, 2012
2.12	First Amendment to Purchase and Sale Agreement, effective as of October 31, 2012, between AdCare Property Holdings, LLC and Winyah Nursing Home, LLC	Filed herewith
3.1	Amended and Restated Articles of Incorporation	Incorporated by reference from Exhibit 3.1 of the Registrant' s Registration Statement Form SB (Registration No. 333-131542) filed February 3, 2006
3.2	Code of Regulations	Incorporated by reference from Exhibit 3.2 of the Registrant' s Registration Statement Form SB (Registration No. 333-131542) filed February 3, 2006
3.3	Amendment to Amended and Restated Articles of Incorporation	Incorporated by reference to Exhibit 3.3 of the Registrant' s Quarterly Report on Form 10-Q for the quarter ended September 30, 2011
3.4	Affidavit, dated June 28, 2012	Incorporated by reference to Exhibit 3.1 of the Registrant' s Current Report on Form 8-K filed on July 5, 2012
3.5	Certificate of Amendment to Amended and Restated Articles of Incorporation of AdCare Health Systems, Inc.	Incorporated by reference to Exhibit 3.5 of the Registrant' s Registration Statement on Form 8-A filed on November 7, 2012
4.1	Warrant to Purchase 312,500 Shares of Common Stock, dated April 1, 2012, issued by AdCare Health Systems, Inc. to Strome Alpha Offshore Ltd.	Incorporated by reference to Exhibit 4.1 of the Registrant' s Quarterly Report on Form 10-Q for the quarter ended March 30, 2012
4.2	Warrant to Purchase 300,000 Shares of Common Stock, dated March 30, 2012, issued by AdCare Health Systems, Inc. to Cantone Asset Management LLC	Incorporated by reference to Exhibit 4.2 of the Registrant' s Quarterly Report on Form 10-Q for the quarter ended March 30, 2012
4.3	Warrant to Purchase 100,000 Shares of Common Stock, dated July 2, 2012, issued by AdCare Health Systems, Inc. to Cantone Research, Inc.	Incorporated by reference to Exhibit 4.3 of the Registrant' s Quarterly Report on Form 10-Q for the quarter ended June 30, 2012

10.1	Form of Securities Purchase Agreement, dated as of June 28, 2012, between AdCare Health Systems, Inc. and the Buyers signatory thereto	Incorporated by reference from Exhibit 99.1 to the Registrant' s Current Report on Form 8-K filed July 5, 2012
10.2	Form of Registration Rights Agreement, dated as of June 28, 2012, between AdCare Health Systems, Inc. and the Buyers signatory thereto	Incorporated by reference from Exhibit 99.2 to the Registrant' s Current Report on Form 8-K filed July 5, 2012
10.3	Form of 8% Subordinated Convertible Note Due 2015 issued by AdCare Health Systems, Inc.	Incorporated by reference from Exhibit 99.3 to the Registrant' s Current Report on Form 8-K filed

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Exhibit No.	Description	Method of Filing
		July 5, 2012
10.4	Loan Agreement, dated as of July 2, 2012, by and between Glenvue H&R Property Holdings, LLC and the PrivateBank and Trust Company	Incorporated by reference to Exhibit 10.32 of the Registrant' s Quarterly Report on Form 10-Q for the quarter ended June 30, 2012
10.5	Promissory Note, dated July 2, 2012, issued by Glenvue H&R Property Holdings, LLC in favor of the PrivateBank and Trust Company in the amount of \$6,600,000	Incorporated by reference to Exhibit 10.33 of the Registrant' s Quarterly Report on Form 10-Q for the quarter ended June 30, 2012
10.6	Deed to Secure Debt, Security Agreement and Assignment of Leases and Rents, dated as of July 2, 2012, from Glenvue H&R Property Holdings, LLC to the PrivateBank and Trust Company	Incorporated by reference to Exhibit 10.34 of the Registrant' s Quarterly Report on Form 10-Q for the quarter ended June 30, 2012
10.7	Assignment of Leases and Rents, dated as of July 2, 2012, from Glenvue H&R Property Holdings, LLC to the PrivateBank and Trust Company	Incorporated by reference to Exhibit 10.35 of the Registrant' s Quarterly Report on Form 10-Q for the quarter ended June 30, 2012
10.8	Guaranty of Payment and Performance, dated as of July 2, 2012, issued by Glenvue H&R Property Holdings, LLC and AdCare Health Systems, Inc. for the benefit of The PrivateBank and Trust Company	Incorporated by reference to Exhibit 10.36 of the Registrant' s Quarterly Report on Form 10-Q for the quarter ended June 30, 2012
10.9	Assignment and Assumption Agreement, dated as of July 1, 2012, by and between Westlake Nursing Home Limited Partnership and QC Property Holdings, LLC	Incorporated by reference to Exhibit 10.37 of the Registrant' s Quarterly Report on Form 10-Q for the quarter ended June 30, 2012

10.10	Loan Agreement and Indenture of First Mortgage, dated as of September 1, 1986, by and among Oklahoma County Industrial Authority, Westlake Nursing Home Limited Partnership and The Liberty National Bank and Trust Company of Oklahoma City, as Trustee	Incorporated by reference to Exhibit 10.38 of the Registrant' s Quarterly Report on Form 10-Q for the quarter ended June 30, 2012
10.11	First Amendment to Loan Agreement and Indenture of First Mortgage, dated September 1, 2001, by and among Oklahoma County Industrial Authority, Westlake Nursing Home, L.P. and Bank One Trust Company, N.A., as Trustee	Incorporated by reference to Exhibit 10.39 of the Registrant' s Quarterly Report on Form 10-Q for the quarter ended June 30, 2012
10.12	Loan Agreement, made as of August 17, 2012, by and among CSCC Property Holdings, LLC, CSCC Nursing, LLC and Contemporary Healthcare Senior Lien Fund I, L.P.	Filed herewith
10.13	Loan Agreement, made as of August 17, 2012, by and among CSCC Property Holdings, LLC, CSCC Nursing, LLC and Contemporary Healthcare Fund I, L.P.	Filed herewith
10.14	Promissory Note, dated August 17, 2012, issued by CSCC Nursing, LLC and CSCC Property Holdings, LLC in favor of Contemporary Healthcare Senior Lien Fund I, L.P. in the amount of \$5,000,000	Filed herewith
10.15	Revolving Loan Promissory Note, made as of August 17, 2012, by and among CSCC Nursing, LLC and CSCC Property Holdings, LLC in favor of Contemporary Healthcare Fund I,	Filed herewith

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<b>Exhibit No.</b>	<b>Description</b>	<b>Method of Filing</b>
	L.P. in the amount of \$600,000	
10.16	Assignment of Leases and Rents, dated as of August 17, 2012, by and among CSCC Property Holdings, LLC, CSCC Nursing, LLC and Contemporary Healthcare Senior Lien Fund I, L.P.	Filed herewith
10.17	Mortgage, Assignment of Rents and Leases, Security Agreement and Fixture Filing, dated August 17, 2012, made and entered into by CSCC Property Holdings, LLC in favor of Contemporary Healthcare Senior Lien Fund I, L.P.	Filed herewith
10.18	Guaranty of Payment and Performance, made as of August 17, 2012, by AdCare Health Systems, Inc. in favor of Contemporary Healthcare Fund I, L.P.	Filed herewith

10.19	Guaranty of Payment and Performance, made as of August 17, 2012, by AdCare Oklahoma Management, LLC in favor of Contemporary Healthcare Fund I, L.P.	Filed herewith
10.20	Guaranty of Payment and Performance, made as of August 17, 2012, by AdCare Health Systems, Inc. in favor of Contemporary Healthcare Senior Lien Fund I, L.P.	Filed herewith
10.21	Guaranty of Payment and Performance, made as of August 17, 2012, by AdCare Oklahoma Management, LLC in favor of Contemporary Healthcare Senior Lien Fund I, L.P.	Filed herewith
10.22	Security Agreement, made as of August 17, 2012, by and among CSCC Property Holdings, LLC, CSCC Nursing, LLC and Contemporary Healthcare Fund I, L.P.	Filed herewith
10.23	Security Agreement, made as of August 17, 2012, by and among CSCC Property Holdings, LLC, CSCC Nursing, LLC and Contemporary Healthcare Senior Lien Fund I, L.P.	Filed herewith
10.24	Loan and Security Agreement, dated as of September 20, 2012, by and among The PrivateBank and Trust Company and the Borrowers named therein	Filed herewith
10.25	Modification Agreement, dated as of October 26, 2012, by and among The PrivateBank and Trust Company and the Borrowers named therein	Filed herewith
10.26	Promissory Note, dated September 20, 2012, issued by the subsidiaries of AdCare Health Systems, Inc. named therein in favor of The PrivateBank and Trust Company in the amount of \$10,600,000	Filed herewith
10.27	Guaranty of Payment and Performance, made as of September 20, 2012, by AdCare Health Systems, Inc. in favor of The PrivateBank and Trust Company	Filed herewith
10.28	Payoff Confirmation Letter, dated September 20, 2012, from Gemino Healthcare Finance, LLC to AdCare Health Systems, Inc. and certain of its subsidiaries named therein	Filed herewith
10.29	Release of Guarantees, dated September 20, 2012, from Gemino Healthcare Finance, LLC to certain subsidiaries of	Filed herewith

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<b>Exhibit No.</b>	<b>Description</b>	<b>Method of Filing</b>
	AdCare Health Systems, Inc. named therein	



10.30	Second Amendment to Credit Agreement, dated September 20, 2012, by and between ADK Bonterra/Parkview, LLC and Gemino Healthcare Finance, LLC	Filed herewith
10.31	Temporary Extension Agreement, dated August 29, 2012, by and between APH & R Property Holdings, LLC and Metro City Bank	Filed herewith
10.32	Loan Agreement, dated as of April 12, 2012, between the City of Springfield, Ohio and Eaglewood Property Holdings, LLC	Incorporated by reference to Exhibit 10.18 of the Registrant' s Quarterly Report on Form 10-Q for the quarter ended March 30, 2012
10.33	Guaranty Agreement, dated as of April 12, 2012, made and entered into by AdCare Health Systems, Inc., to and for the benefit of BOKF, NA dba Bank of Oklahoma	Incorporated by reference to Exhibit 10.19 of the Registrant' s Quarterly Report on Form 10-Q for the quarter ended March 30, 2012
10.34	Land Use Restriction Agreement, dated as of April 12, 2012, by and between BOKF, NA dba Bank of Oklahoma and Eaglewood Property Holdings, LLC	Incorporated by reference to Exhibit 10.20 of the Registrant' s Quarterly Report on Form 10-Q for the quarter ended March 30, 2012
10.35	Open-End Mortgage, Assignment of Leases and Security Agreement, dated April 12, 2012, from Eaglewood Property Holdings, LLC to BOKF, NA dba Bank of Oklahoma	Incorporated by reference to Exhibit 10.21 of the Registrant' s Quarterly Report on Form 10-Q for the quarter ended March 30, 2012
10.36	Loan Agreement, dated April 30, 2012, by and between APH&R Property Holdings, LLC and Metro City Bank	Incorporated by reference from Exhibit 99.1 to the Registrant' s Current Report on Form 8-K filed May 3, 2012
10.37	Promissory Note, dated April 30, 2012, issued by APH&R Property Holdings, LLC in favor of Metro City Bank in the amount of \$3,425,500	Incorporated by reference from Exhibit 99.2 to the Registrant' s Current Report on Form 8-K filed May 3, 2012
10.38	Mortgage and Security Agreement, dated April 30, 2012, between APH&R Property Holdings, LLC and Metro City Bank	Incorporated by reference from Exhibit 99.3 to the Registrant' s Current Report on Form 8-K filed May 3, 2012
10.39	Security Agreement, dated April 30, 2012, between APH&R Property Holdings, LLC and Metro City Bank	Incorporated by reference from Exhibit 99.4 to the Registrant' s Current Report on Form 8-K filed May 3, 2012
10.40	Guaranty, dated as of April 30, 2012, between APH&R Property Holdings, LLC in favor of Metro City Bank	Incorporated by reference from Exhibit 99.5 to the Registrant' s Current Report on Form 8-K filed May 3, 2012

10.41	Guaranty, dated as of April 30, 2012, between AdCare Health Systems, Inc. in favor of Metro City Bank	Incorporated by reference from Exhibit 99.6 to the Registrant' s Current Report on Form 8-K filed May 3, 2012
10.42	Collateral Assignment of Certificate of Deposit, dated April 30, 2012, by and between APH&R Property Holdings, LLC	Incorporated by reference from Exhibit 99.7 to the Registrant' s

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<u>Exhibit No.</u>	<u>Description</u>	<u>Method of Filing</u>
	and Metro City Bank	Current Report on Form 8-K filed May 3, 2012
10.43	Promissory Note, dated April 27, 2012, issued by Cantone Asset Management LLC in favor of AdCare Health Systems, Inc. in the amount of \$1,500,000	Incorporated by reference from Exhibit 99.8 to the Registrant' s Current Report on Form 8-K filed May 3, 2012
10.44	Promissory Note, dated June 8, 2012, issued by Mt. V Property Holdings, LLC in favor of Metro City Bank in the amount of \$1,800,000	Incorporated by reference from Exhibit 10.13 of the Registrant' s Quarterly Report on Form 10-Q for the quarter ended June 30, 2012
10.45	Loan Agreement, dated June 8, 2012, by and between Mt. V Property Holdings, LLC and Metro City Bank	Incorporated by reference from Exhibit 10.14 of the Registrant' s Quarterly Report on Form 10-Q for the quarter ended June 30, 2012
10.46	Mortgage and Security Agreement, dated June 8, 2012, by and between Mt. V Property Holdings, LLC and Metro City Bank	Incorporated by reference from Exhibit 10.15 of the Registrant' s Quarterly Report on Form 10-Q for the quarter ended June 30, 2012
10.47	Assignment of Leases and Rents, dated June 8, 2012, by and between Mt. V Property Holdings, LLC and Metro City Bank	Incorporated by reference from Exhibit 10.16 of the Registrant' s Quarterly Report on Form 10-Q for the quarter ended June 30, 2012
10.48	Security Agreement, dated June 8, 2012, by and between Mt. V Property Holdings, LLC and Metro City Bank	Incorporated by reference from Exhibit 10.17 of the Registrant' s Quarterly Report on Form 10-Q for the quarter ended June 30, 2012
10.49	Guaranty, dated June 8, 2012, made by AdCare Health Systems, Inc. in favor of Metro City Bank	Incorporated by reference from Exhibit 10.18 of the Registrant' s Quarterly Report on Form 10-Q for the quarter ended June 30, 2012

10.50	Promissory Note, dated June 8, 2012, issued by Mt. V Property Holdings, LLC in favor of Metro City Bank in the amount of \$1,267,000	Incorporated by reference from Exhibit 10.19 of the Registrant' s Quarterly Report on Form 10-Q for the quarter ended June 30, 2012
10.51	Loan Agreement, dated June 8, 2012, by and between Mt. V Property Holdings, LLC and Metro City Bank	Incorporated by reference from Exhibit 10.20 of the Registrant' s Quarterly Report on Form 10-Q for the quarter ended June 30, 2012
10.52	Mortgage and Security Agreement, dated June 8, 2012, by and between Mt. V Property Holdings, LLC and Metro City Bank	Incorporated by reference from Exhibit 10.21 of the Registrant' s Quarterly Report on Form 10-Q for the quarter ended June 30, 2012
10.53	Assignment of Leases and Rents, dated June 8, 2012, by and	Incorporated by reference from Exhibit 10.22 of the Registrant' s

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Exhibit No.	Description	Method of Filing
	between Mt. V Property Holdings, LLC and Metro City Bank	Quarterly Report on Form 10-Q for the quarter ended June 30, 2012
10.54	Security Agreement, dated June 8, 2012, by and between Mt. V Property Holdings, LLC and Metro City Bank	Incorporated by reference from Exhibit 10.23 of the Registrant' s Quarterly Report on Form 10-Q for the quarter ended June 30, 2012
10.55	Guaranty, dated June 8, 2012, made by AdCare Health Systems, Inc. in favor of Metro City Bank	Incorporated by reference from Exhibit 10.24 of the Registrant' s Quarterly Report on Form 10-Q for the quarter ended June 30, 2012
10.56	Promissory Note, dated June 8, 2012, issued by Mt. V Property Holdings, LLC in favor of Economic Development Corporation of Fulton County in the amount of \$1,304,000	Incorporated by reference from Exhibit 10.25 of the Registrant' s Quarterly Report on Form 10-Q for the quarter ended June 30, 2012
10.57	Loan Agreement, dated June 8, 2012, by and between Mt. V Property Holdings, LLC, Mountain View Nursing, LLC and Economic Development Corporation of Fulton County	Incorporated by reference from Exhibit 10.26 of the Registrant' s Quarterly Report on Form 10-Q for the quarter ended June 30, 2012

10.58	Security Agreement, dated June 8, 2012, by and between Mt. V Property Holdings, LLC and Economic Development Corporation of Fulton County	Incorporated by reference from Exhibit 10.27 of the Registrant' s Quarterly Report on Form 10-Q for the quarter ended June 30, 2012
10.59	Mortgage and Security Agreement, dated June 8, 2012, by and between Mt. V Property Holdings, LLC and Economic Development Corporation of Fulton County	Incorporated by reference from Exhibit 10.28 of the Registrant' s Quarterly Report on Form 10-Q for the quarter ended June 30, 2012
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10.61	Unconditional Guarantee, dated June 8, 2012, issued by Mountain View Nursing, LLC in favor of Economic Development Corporation of Fulton County	Incorporated by reference from Exhibit 10.30 of the Registrant' s Quarterly Report on Form 10-Q for the quarter ended June 30, 2012
10.62	Unconditional Guarantee, dated June 8, 2012, issued by AdCare Health Systems, Inc. in favor of Economic Development Corporation of Fulton County	Incorporated by reference from Exhibit 10.31 of the Registrant' s Quarterly Report on Form 10-Q for the quarter ended June 30, 2012
10.63	Bond Purchase Agreement, dated April 10, 2012, among Lawson Financial Corporation, The City of Springfield, Ohio and Eaglewood Property Holdings, LLC	Incorporated by reference from Exhibit 10.40 of the Registrant' s Quarterly Report on Form 10-Q for the quarter ended June 30, 2012
10.64	Note Purchase Agreement, dated April 12, 2012, by and between Cantone Asset Management LLC and AdCare Health	Incorporated by reference from Exhibit 10.41 of the Registrant' s

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<b>Exhibit No.</b>	<b>Description</b>	<b>Method of Filing</b>
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10.65	Employment Agreement, dated August 7, 2012, between AdCare Health Systems, Inc. and Martin D. Brew	Incorporated by reference from Exhibit 10.42 of the Registrant' s Quarterly Report on Form 10-Q for the quarter ended June 30, 2012
10.66	Modification Agreement, dated June 15, 2012, among Little Rock HC&R Property Holdings, LLC, Northridge HC&R Property	Incorporated by reference from Exhibit 10.43 of the Registrant' s Quarterly

	Holdings, LLC, Woodland Hills HC Property Holdings, LLC and The PrivateBank and Trust Company	Report on Form 10-Q for the quarter ended June 30, 2012
10.67	Amendment, entered into as of July 26, 2012, by and between Christopher F. Brogdon and Hearth & Home of Ohio, Inc.	Incorporated by reference from Exhibit 10.47 of the Registrant' s Quarterly Report on Form 10-Q for the quarter ended June 30, 2012
10.68	Employment Agreement, dated August 6, 2012, between AdCare Health Systems, Inc. and Melissa L. Green	Incorporated by reference from Exhibit 10.48 of the Registrant' s Quarterly Report on Form 10-Q for the quarter ended June 30, 2012
31.1	Certification of CEO pursuant to Section 302 of the Sarbanes-Oxley Act	Filed herewith
31.2	Certification of CFO pursuant to Section 302 of the Sarbanes-Oxley Act	Filed herewith
32.1	Certification of CEO pursuant to Section 906 of the Sarbanes-Oxley Act	Filed herewith
32.2	Certification of CFO pursuant to Section 906 of the Sarbanes-Oxley Act	Filed herewith
101	The following financial information from AdCare Health Systems, Inc. Quarterly Report on Form 10-Q for the quarter ended September 30, 2012, formatted in XBRL (eXtensible Business Reporting Language): (i) Consolidated Statements of Operations for the three months ended September 30, 2012 and 2011 and for the nine months ended September 30, 2012 and 2011, (ii) Consolidated Balance Sheets as of September 30, 2012 and December 31, 2011, (iii) Consolidated Statements of Cash Flows for the nine months ended September 30, 2012 and 2011, (iv) Consolidated Statements of Stockholders' Equity for the nine months ended September 30, 2012 and (v) the Notes to Consolidated Financial Statements.	Filed herewith

## AMENDMENT TO PURCHASE AGREEMENT

This Amendment to Purchase Agreement (the “**Amendment**”) is made as of the 19th day of July 2012, by and between 1761 Pinewood Holdings, LLC, a Delaware limited liability company (“**Seller**”), and AdCare Property Holdings, LLC, an Ohio limited liability company (“**Purchaser**”). Seller and Purchaser are hereinafter jointly referred to as the “**Parties**” and individually as a “**Party**”.

**WHEREAS**, the Seller and the Purchaser entered into a Purchase Agreement (the “**Agreement**”) dated as of April 27, 2012; and

**WHEREAS**, the Parties wish to amend the Agreement as described herein;

**NOW, THEREFORE**, in consideration of the mutual premises and covenants contained herein, the adequacy and sufficiency of which are hereby acknowledged, it is agreed between the Parties as follows:

1. Defined Terms. Unless otherwise indicated herein, capitalized terms used herein shall have the meanings ascribed to them in the Agreement.
2. Additional Earnest Money. Simultaneously with the execution of this Amendment, Purchaser shall wire an additional One Hundred Fifty Thousand Dollars and 00/100 (\$150,000.00) (the “Additional Earnest Money”) to Seller pursuant to the wire instructions set forth on Exhibit A attached hereto. For the purposes of clarification and notwithstanding anything to the contrary contained in the Agreement, the Additional Earnest Money shall not be held in escrow pursuant to the Escrow Agreement, but shall be delivered directly to Seller as set forth in the preceding sentence. For the purposes of Section 2(b) of the Agreement, the Additional Earnest Money shall be deemed to be “Earnest Money” and shall be credited against the Purchase Price at Closing, unless the Closing does not occur due to a default by Seller in accordance with Section 17 of the Agreement, in which event the Additional Earnest Money shall be returned to Purchaser.
3. Date of Closing. The Parties agree that the Closing Date shall be August 31, 2012, and the transaction shall be effective as of 12:00 a.m. September 1, 2012. Section 8 of the Agreement shall be amended as follows:
  - a. The date “August 1, 2012” in line 10 of Section 8 shall be deleted and replaced with “September 1, 2012”.
  - b. The date “July 31, 2012” in line 11 of Section 8 shall be deleted and replaced with “August 31, 2012”.
4. Counterparts. This Amendment may be executed in counterparts, each of which will be an original and all of which taken together shall constitute one and the

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same agreement, and any Party hereto may execute this Agreement by signing any such counterpart.

5. Miscellaneous. This Amendment and the obligations of the Parties hereunder shall be binding upon and inure to the benefit of the Parties hereto and their respective successors and assigns and shall be governed by and construed in accordance with the laws governing the Agreement. This Amendment may not be modified or amended in any manner other than by a written agreement signed by all Parties. Except as otherwise expressly provided in this Amendment, the provisions of the Agreement are hereby ratified and confirmed and remain in full force and effect.

The Recitals are correct and are incorporated as a substantive part of this Amendment. Delivery of this Amendment by facsimile or electronic mail by any party shall represent a valid and binding execution and delivery of this Amendment by such party.

**[Signature Page Follows]**

2

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IN WITNESS WHEREOF, each of the Parties hereto and in the capacity indicated below has executed this Amendment as of the day and year first above written.

**PURCHASER:**

**ADCARE PROPERTY HOLDINGS, LLC**  
an Ohio limited liability company

By: /s/ Christopher F. Brogdon  
Christopher F. Brogdon,  
Vice Chairman and Chief Acquisition Officer

**SELLER:**

**1761 PINWOOD HOLDINGS, LLC**  
a Delaware limited liability company

By: /s/ Abraham Shaulson  
Name: Abraham Shaulson  
Title: President

3

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## SECOND AMENDMENT TO PURCHASE AGREEMENT

This Second Amendment to Purchase Agreement (the “**Amendment**”) is made as of the 31<sup>st</sup> day of August 2012, by and between 1761 Pinewood Holdings LLC, a Delaware limited liability company (“**Seller**”), and AdCare Property Holdings, LLC, an Ohio limited liability company (“**Purchaser**”). Seller and Purchaser are hereinafter jointly referred to as the “**Parties**” and individually as a “**Party**”.

**WHEREAS**, the Seller and the Purchaser entered into a Purchase Agreement dated as of April 27, 2012, as amended pursuant to that certain Amendment to Purchase Agreement dated as of July 19, 2012 (as amended, the “**Agreement**”); and

**WHEREAS**, the Parties wish to further amend the Agreement as described herein;

**NOW, THEREFORE**, in consideration of the mutual premises and covenants contained herein, the adequacy and sufficiency of which are hereby acknowledged, it is agreed between the Parties as follows:

1. Defined Terms. Unless otherwise indicated herein, capitalized terms used herein shall have the meanings ascribed to them in the Agreement.
2. Partial Disbursement of Earnest Money. By the execution of this Amendment, Purchaser hereby authorizes and directs Escrow Agent to promptly wire the sum of One Hundred Thousand and 00/100 Dollars (\$100,000.00) (the “**Disbursed Earnest Money**”) to Seller pursuant to the wire instructions set forth on Exhibit A attached hereto. For the purposes of clarification and notwithstanding anything to the contrary contained in the Agreement, the remaining balance of the Earnest Money (i.e. \$50,000.00) shall be held in escrow pursuant to the Escrow Agreement. For the purposes of Section 2(b) of the Agreement, the Disbursed Earnest Money shall be deemed to be “Earnest Money” and shall be credited against the Purchase Price at Closing, unless the Closing does not occur due to a default by Seller in accordance with Section 17 of the Agreement, in which event the Disbursed Earnest Money shall be returned to Purchaser.
3. Extension Fee. Simultaneously with the execution of this Amendment, Purchaser shall wire the sum of Twenty-Five Thousand and 00/100 Dollars (\$25,000.00) (the “**Extension Fee**”) to Seller pursuant to wire instructions set forth on Exhibit “A” attached hereto. The Extension Fee shall be non-refundable and shall not be credited against the Purchase Price at Closing.
4. Date of Closing. The Parties agree that the Closing Date shall be September 28, 2012, the transaction shall fund on October 1, 2012 and shall be effective as of 12:00 a.m. October 1, 2012. Section 8 of the Agreement shall be amended as follows:

- 
- a. The date “September 1, 2012” in line 10 of Section 8 shall be deleted and replaced with “October 1, 2012”.
  - b. The date “August 31, 2012” in line 11 of Section 8 shall be deleted and replaced with “September 30, 2012”.
5. Like Kind Exchange. Seller may desire to effectuate a like-kind exchange pursuant to Section 1031 of the Internal Revenue Service Code in connection with the sale of the Facility. Purchaser agrees to use reasonable efforts to accommodate Seller in effectuating a like-kind exchange pursuant to Section 1031 of the Internal Revenue Service



Code in connection with the transfer of the Facility; provided however, that (a) such exchange does not directly or indirectly increase the Purchase Price, (b) such exchange will not delay or otherwise adversely affect the Closing and (c) all documents to be executed by Purchaser in connection with such exchange shall be subject to the reasonable approval of Purchaser, which approval shall not be unreasonably withheld or delayed.

6. Counterparts. This Amendment may be executed in counterparts, each of which will be an original and all of which taken together shall constitute one and the same agreement, and any Party hereto may execute this Agreement by signing any such counterpart.
  
7. Miscellaneous. This Amendment and the obligations of the Parties hereunder shall be binding upon and inure to the benefit of the Parties hereto and their respective successors and assigns and shall be governed by and construed in accordance with the laws governing the Agreement. This Amendment may not be modified or amended in any manner other than by a written agreement signed by all Parties. Except as otherwise expressly provided in this Amendment, the provisions of the Agreement are hereby ratified and confirmed and remain in full force and effect. The Recitals are correct and are incorporated as a substantive part of this Amendment. Delivery of this Amendment by facsimile or electronic mail by any party shall represent a valid and binding execution and delivery of this Amendment by such party.

**[Signature Page Follows]**

2

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IN WITNESS WHEREOF, each of the Parties hereto and in the capacity indicated below has executed this Amendment as of the day and year first above written.

**PURCHASER:**

**ADCARE PROPERTY HOLDINGS, LLC,**  
an Ohio limited liability company

By: /s/ Christopher F. Brogdon

Name: Christopher F. Brogdon

Title: Vice Chairman and Chief Acquisition Officer

**SELLER:**

**1761 PINWOOD HOLDINGS LLC,**  
a Delaware limited liability company

By: /s/ Abraham Shaulson

Name: Abraham Shaulson

Title: President

3



**THIRD AMENDMENT TO PURCHASE AGREEMENT**

This Third Amendment to Purchase Agreement (the “**Amendment**”) is made as of the 27<sup>th</sup> day of September 2012, by and between 1761 Pinewood Holdings LLC, a Delaware limited liability company (“**Seller**”), and AdCare Property Holdings, LLC, an Ohio limited liability company (“**Purchaser**”). Seller and Purchaser are hereinafter jointly referred to as the “**Parties**” and individually as a “**Party**”.

**WHEREAS**, the Seller and the Purchaser entered into a Purchase Agreement dated as of April 27, 2012, as amended pursuant to that certain Amendment to Purchase Agreement dated as of July 19, 2012, as further amended pursuant to that certain Second Amendment to Purchase Agreement dated as of August 31, 2012 (as amended, the “**Agreement**”); and

**WHEREAS**, the Parties wish to further amend the Agreement as described herein;

**NOW, THEREFORE**, in consideration of the mutual premises and covenants contained herein, the adequacy and sufficiency of which are hereby acknowledged, it is agreed between the Parties as follows:

1. Defined Terms. Unless otherwise indicated herein, capitalized terms used herein shall have the meanings ascribed to them in the Agreement.
2. Additional Earnest Money; Partial Disbursement of Earnest Money. Within three (3) business days of the date hereof, Purchaser shall wire the sum of Five Hundred Fifty Thousand and 00/100 Dollars (\$550,000.00) to Escrow Agent as additional Earnest Money (the “**Additional Earnest Money**”). By the execution of this Amendment, Purchaser hereby authorizes and directs Escrow Agent to promptly wire the sum of Six Hundred Thousand and 00/100 Dollars (\$600,000.00) (the “**Additional Disbursed Earnest Money**,” being the sum of the Additional Earnest Money plus the \$50,000 Earnest Money that the Escrow Agent is holding as of the date of this Agreement) to Seller pursuant to the wire instructions set forth on Exhibit A attached hereto. For the purposes of clarification and notwithstanding anything to the contrary contained in the Agreement, once the Additional Disbursed Earnest Money has been disbursed by the Escrow Agent, the Escrow Agent shall not be holding any remaining Earnest Money pursuant to the Escrow Agreement. For the purposes of Section 2(b) of the Agreement, the Additional Disbursed Earnest Money shall be deemed to be “Earnest Money” (such that the total amount of Earnest Money shall be Eight Hundred Fifty Thousand and 00/100 Dollars [\$850,000.00]) and shall be credited against the Purchase Price at Closing, unless the Closing does not occur due to a default by Seller in accordance with Section 17 of the Agreement, in which event all Earnest Money (comprised of the Additional Earnest Money, the Disbursed Earnest Money and the Additional Disbursed Earnest Money) shall be returned to Purchaser. In the event the Closing does not occur due to a default by Buyer

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under the Agreement, including, without limitation the failure of Buyer to close the transaction contemplated under the Agreement on or before the Walk-Away Date, all Earnest Money shall remain the property of Seller and Purchaser shall have no rights whatsoever with respect thereto.

3. Date of Closing. The Parties agree that the Closing Date shall be on or before December 28, 2012, and shall be effective as of 12:00 a.m. January 1, 2013. Section 8 of the Agreement shall be amended as follows:
  - a. The date “October 1, 2012” in line 10 of Section 8 shall be deleted and replaced with “January 1, 2013”.

- b. The date “September 30, 2012” in line 11 of Section 8 shall be deleted and replaced with “December 31, 2012”.

Notwithstanding anything to the contrary contained in the Agreement, upon fourteen (14) days written notice by Purchaser to Seller (the “Closing Date Notice”), Purchaser shall have the right to close the transaction contemplated under the Agreement on the last business day of October or November, with the transition of operations at the Facility to occur and to be effective as of 12:00 a.m. on the first day of the month following the Closing. The Closing Date Notice shall be irrevocable by Purchaser and the date set forth in the Closing Date Notice for the Closing to occur shall be deemed to be the Walk-Away Date.

4. Counterparts. This Amendment may be executed in counterparts, each of which will be an original and all of which taken together shall constitute one and the same agreement, and any Party hereto may execute this Agreement by signing any such counterpart.
5. Miscellaneous. This Amendment and the obligations of the Parties hereunder shall be binding upon and inure to the benefit of the Parties hereto and their respective successors and assigns and shall be governed by and construed in accordance with the laws governing the Agreement. This Amendment may not be modified or amended in any manner other than by a written agreement signed by all Parties. Except as otherwise expressly provided in this Amendment, the provisions of the Agreement are hereby ratified and confirmed and remain in full force and effect. The Recitals are correct and are incorporated as a substantive part of this Amendment. Delivery of this Amendment by facsimile or electronic mail by any party shall represent a valid and binding execution and delivery of this Amendment by such party.

[Signature Page Follows]

IN WITNESS WHEREOF, each of the Parties hereto and in the capacity indicated below has executed this Amendment as of the day and year first above written.

**PURCHASER:**

**ADCARE PROPERTY HOLDINGS, LLC,**  
an Ohio limited liability company

By: /s/ Christopher F. Brogdon

Name: Christopher F. Brogdon

Title: Vice Chairman and Chief Acquisition Officer

**SELLER:**

**1761 PINWOOD HOLDINGS LLC,**  
a Delaware limited liability company

By: /s/ Abraham Shaulson

Name: Abraham Shaulson

Title: President

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**AGREEMENT OF SALE**

By and among  
**ADCARE HEALTH SYSTEMS, INC.,**  
an Ohio corporation and its subsidiaries identified on the signature page hereto  
(collectively, *“Seller”*)

and

**CHP ACQUISITION COMPANY LLC**  
an Ohio limited liability company  
(*“Buyer”*)

**Dated as of October 11, 2012**

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**AGREEMENT OF SALE**

THIS AGREEMENT OF SALE (this “*Agreement*”), is made this 11<sup>TH</sup> day of October, 2012, by and among ADCARE HEALTH SYSTEMS, INC., an Ohio corporation ( “*ADK*”) and its subsidiaries identified on the signature page hereto (hereinafter, ADK and such subsidiaries are collectively referred to as “*Seller*”), and CHP ACQUISITION COMPANY LLC, an Ohio limited liability company (or its nominee, designee or assignee), (hereinafter, “*Buyer*”).

**RECITALS**

A. Seller is the owner of the following six (6) senior citizens’ housing, assisted living and/or independent living facilities commonly known by the following names and located in the cities and states indicated below:

<u>Name of Facility</u>	<u>Location</u>
Community’ s Hearth & Home	Springfield, Ohio
Community’ s Hearth & Home	Springfield, Ohio
Hearth & Home of Van Wert	Van Wert, Ohio
Community’ s Hearth & Home	Urbana, Ohio
Hearth & Home of Vandalia	Vandalia, Ohio
Lincoln Lodge Retirement Residence	Columbus, Ohio

Collectively, the above seniors’ housing facilities are referred to as the “*Facilities*” and each individually as a “*Facility*”.

B. Seller desires to sell to Buyer, and Buyer desires to purchase from Seller, all of the Facilities and the assets related to the Facilities on the terms and conditions hereinafter set forth.

NOW, THEREFORE, in consideration of the foregoing and the respective promises, representations, warranties and covenants herein contained, the parties hereto, intending to be legally bound hereby, do agree as follows:

**ARTICLE I  
DEFINITIONS**

1.1. **Definitions.** For purposes of this Agreement the following terms shall have the means ascribed below:

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“*Affiliate*” shall mean with respect to any Person, any Person that directly or indirectly, through one or more intermediaries, controls, is controlled by, or is under common control with, such first Person.

“*Agreement*” shall mean this Agreement of Sale including all Exhibits and Schedules attached hereto or referred to herein.

“*Approvals*” shall have the meaning set forth in Section 3.1(h).

**“Assets”** shall have the meaning set forth in Section 3.1.

**“Assignment and Assumption Agreement”** shall have the meaning set forth in Section 7.2(e).

**“Assumed Obligations”** shall have the meaning set forth in Section 4.1.

**“Assumed Service Contracts”** shall mean those certain executory contracts that Buyer elects to assume pursuant to and in accordance with Section 4.1.

**“Awards”** shall have the meaning set forth in Section 3.1(g).

**“Balance Sheet”** shall have the meaning set forth in Section 13.1(p).

**“Bill of Sale”** shall have the meaning set forth in Section 7.2(c).

**“Building Service Equipment”** shall have the meaning set forth in Section 3.1(c).

**“Business”** shall have the meaning set forth in Section 2.1.

**“Business Day”** shall mean any day other than a Saturday or Sunday, or other day recognized as a holiday by the U.S. Government or the government of the State of Ohio, or on which banks or similar financial institutions in the State of Ohio are generally closed.

**“Buyer’s A/Rs”** shall have the meaning set forth in Section 12.1.

**“Cap Ex Obligations”** shall have the meaning set forth in Section 6.4(f)(i).

**“Cash”** shall mean all cash and bank deposits, investments in so-called “money market” funds, certificates of deposit, treasury bills and any accrued interest thereon excluding any Resident Trust Funds.

**“Closing”** shall mean the settlement of the conveyance of the Assets under this Agreement.

**“Closing Date”** shall mean the date of the Closing.

**“COBRA”** shall have the meaning set forth in Section 11.4.

**“Consents”** shall mean all consents, approvals, licenses, permits, orders or authorizations.

**“Contract”** shall mean any contract, lease, license, indenture, agreement, commitment or other legally binding arrangement to which the Seller is a party or by which any of its properties or assets is or are bound, including the Service Contracts and the Resident occupancy agreements.

**“Damages”** shall have the meaning set forth in Section 21.1.

**“Deed”** shall have the meaning set forth in Section 7.1.

**“Deposit”** shall have the meaning set forth in Section 6.1(a).

**“Environmental Laws”** shall have the meaning set forth in Section 13.1(k).

**“Escrow Agent”** shall mean Hummel Title Agency.

**“Escrow Agreement”** shall have the meaning set forth in Section 6.1(a).

**“ERISA”** shall have the meaning set forth in Section 13.1(t).

**“Excluded Assets”** shall have the meaning set forth in Section 3.2.

**“Existing Cap Ex Obligations”** shall have the meaning set forth in Section 6.4(f)(i).

**“Facilities”** shall have the meaning set forth in Paragraph A of the Recitals to this Agreement.

**“Facility Employees”** shall have the meaning set forth in Section 11.2.

**“Financial Statements”** shall have the meaning set forth in Section 13.1(p).

**“Governmental Authority”** shall mean any Federal, state, local or foreign government or any court of competent jurisdiction, administrative agency or commission or other governmental or quasi-governmental authority or instrumentality, domestic or foreign.

**“Health Care Providers”** shall have the meaning set forth in Section 13.1(u).

**“Hired Employees”** shall have the meaning set forth in Section 11.3.

**“Improvements”** shall have the meaning set forth in Section 3.1(b).

**“Indemnified Party”** shall have the meaning set forth in Section 21.4.

**“Indemnifying Party”** shall have the meaning set forth in Section 21.4.

**“Insurance Policies”** shall have the meaning set forth in Section 13.1(l).

**“Inventory”** shall have the meaning set forth in Section 3.1(e).

**“Intangible Property”** shall have the meaning set forth in Section 3.1(i)

**“Knowledge of Seller”** or words of similar import shall mean the actual knowledge of Buyer’s officers and directors, including but not limited to, Andy Wade, Martin Brew or Boyd P. Gentry, without any duty of investigation or inquiry.

**“Land”** shall have the meaning set forth in Section 3.1.

**“Law”** shall mean any law (including decisional law), statute, regulation, code, ordinance or interpretation of any Federal, state or local agency, government, authority, commission, board, bureau, administrative or other entity or body, including any Program participation or certification requirement.

**“Licensure Approvals”** shall have the meaning set forth in Section 9.1.

**“Material Adverse Change”** shall have the meaning set forth in Section 16.1(j).

**“Material Adverse Effect”** shall mean a material adverse effect (i) on the Business, Assets or results of operations of the Seller or Buyer, or (ii) on the ability of the Seller or Buyer, as the case may be, to consummate this Agreement and the other transactions contemplated hereby.

**“Medical Equipment”** shall have the meaning set forth in Section 3.1(d).

**“New Cap Ex Obligations”** shall have the meaning set forth in Section 6.4(f)(i).

**“Obligations”** shall mean any claim, debt, liability, judgment, commitment or obligation of any nature, whether secured, recourse, nonrecourse, liquidated, unliquidated, accrued, absolute, fixed, contingent, ascertained, unascertained, known, unknown or otherwise.

**“Outside Closing Date”** shall have the meaning set forth in Section 5.1.

**“Permitted Encumbrances”** shall have the meaning set forth in Section 7.1(c).

**“Person”** shall mean a natural person, a trustee, and any form of legal entity.

**“Personal Property”** shall have the meaning set forth in Section 7.2(c).

**“Plan”** shall have the meaning set forth in Section 13.1(t).

**“Programs”** shall have the meaning set forth in Section 13.1(x).

**“Program Agreements”** shall have the meaning set forth in Section 13.1(x).

**“Property”** shall have the meaning set forth in Section 3.1(b).

**“Property Information”** shall mean: (a) each then-effective certificate of occupancy and other license issued by any Governmental Authority and covering the Business and the Property; (b) all, if any, of Seller’s and its agents’ books and records relating to the operation, maintenance and management of the Facilities, including but not limited to income and expense statements for the Facilities; (c) all, if any, plans and specifications covering the Property which are in Seller’s possession, custody or control; (d) all, if any, guarantees or warranties then in effect and covering the Assets; (e) the benefit of all, if any, maintenance or other Contracts relating to the Facilities to which Seller or any of its predecessors in title is a party; (f) any third-party reports of any kind in its possession relating to the Property (e.g., appraisals, studies undertaken by insurers in underwriting or considering potential insurance coverage involving the Property, title commitments and policies, surveys, environmental studies, and engineering studies); (g) all Residents’ occupancy agreements, and (h) the most recent title commitment and survey for the Property, together with copies of all title exceptions.

***“Proposed Settlement”*** shall have the meaning set forth in Section 21.6.

***“Purchase Price”*** shall have the meaning set forth in Section 6.1.

***“Records”*** shall have the meaning set forth in Section 3.1(f).

***“Required Permits”*** shall have the meaning set forth in Section 13.1(e).

***“Resident”*** shall mean an individual living and residing in any of the Facilities.

***“Resident Trust Funds”*** shall have the meaning set forth in Section 10.1.

***“Seller’s A/Rs”*** shall have the meaning set forth in Section 12.1.

***“Seller’s Medicare Provider Agreements”*** shall have the meaning set forth in Section 8.1.

***“Service Contracts”*** shall have the meaning set forth in Section 4.1.

***“Seller’s Obligations”*** shall have the meaning set forth in Section 4.2.

***“Study Period”*** shall have the meaning set forth in Section 15.1.

***“Tax”*** or ***“Taxes”*** shall mean all Federal, state, local, foreign and other taxes, assessments, duties or similar charges of any kind whatsoever, including all corporate franchise, income, sales, use, ad valorem, receipts, value added, profits, license, withholding, payroll, employment, excise, property, net worth, capital gains, transfer, stamp, documentary, social security, payroll, environmental, alternative minimum, occupation, recapture, unclaimed property and other taxes, and including any interest, penalties and additions imposed with respect to such amounts.

***“Title Insurer”*** shall mean the First American Title Insurance Company.

***“WARN Act”*** shall meaning set forth in Section 11.5.

***“Warranties”*** shall have the meaning set forth in Section 3.1(j).

## ARTICLE II SALE AND PURCHASE OF ASSETS

**2.1. Agreement to Sell and Purchase.** Subject to the terms and conditions of this Agreement and in consideration of the Purchase Price, on the Closing Date, Seller shall sell, transfer, convey and assign to Buyer (or its assignee as provided in Section 2.2), and Buyer (or its assignee) shall purchase from Seller, all of the Assets, other than the Excluded Assets, maintained or acquired by or on behalf of Seller in its ownership of the Facilities as well as all personal property used in the assisted living and independent living business currently being conducted by Seller at the Facilities (the ***“Business”***), free and clear of any and all liens, claims, charges, pledges, security interests or other encumbrances of any kind or nature whatsoever, except for the Permitted Liens.

**ARTICLE III**  
**ASSETS AND EXCLUDED ASSETS**

**3.1. Assets.** The assets to be purchased by Buyer at the Closing include all of Seller' s right, title and interest in the following (collectively, the "**Assets** "):

(a) The six (6) parcels of real property described in **Exhibit A** attached hereto, together with all of Seller' s right, title and interest in any real property contiguous thereto which lies within the dedicated area of any public road or alley, open or closed, to the center line there at, and all rights, ways, appurtenances and advantages belonging to the real property (collectively, the "**Land**").

(b) All buildings and other improvements on the Land (collectively, the "Improvements" and together with the Land, the "**Property**").

(c) All apparatus, computer equipment and hardware, machinery, vehicles, furniture, fixtures, equipment and other items of personal property whether or not located on the Property which is utilized for the operation and maintenance of the Facilities or the Business (other than any personal property of a Resident), including, but not limited to, all interior and exterior window treatments and floor, wall and ceiling coverings; partitions, doors and hardware; elevators, heating, plumbing and ventilating apparatus; gas, electric and steam fixtures; chutes, ducts and tanks; heaters, incinerators and boilers; air-cooling and air-conditioning equipment; lavatory fixtures; tools, building supplies, lobby decorations, kitchen appliances; and all additions thereto and replacements of the same (collectively, the "**Building Service Equipment**").

(d) All medical apparatus, furniture, fixtures, equipment and other items of personal property owned by Seller and located at and used in connection with the operation of the Facilities on the Closing Date (the "**Medical Equipment**").

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(e) All consumable inventories of every kind and nature whatsoever, including, but not limited to, all pharmacy supplies, medical supplies, prescription and non-prescription drugs or equipment, office supplies, other supplies and foodstuffs, which are located at the Facility on the Closing Date (collectively, the "**Inventory**").

(f) All files, charts, other Resident information in Seller' s possession or control relating to all Residents occupying or using the Facilities on the Closing Date, including, but not limited to, all patient records, medical records, therapy records, pharmacy records, including, a complete computer printout of all clinical records and financial and accounting records, Resident Trust Funds records, litigation records, maintenance records, employment records for the Hired Employees (including all medical and health records and all non-medical records including evaluations, etc.), administrative compliance records, including, but not limited to, all state surveys and plans of correction, correspondence and any other written data which was utilized in connection with the operation of the Facilities or the Business (collectively, the "**Records**"). To the extent that any Records have been removed from the Facilities, such Records shall be made available to Buyer at a convenient location or returned to the Facilities prior to the Closing. Any deliveries made by Seller to Buyer shall be made in full compliance with all applicable Laws, including, but not limited to, HIPAA.

(g) All proceeds of any award made for a taking of all or any part of the Land or the Improvements by any governmental authority pursuant to the exercise of its power of eminent domain (collectively, the "**Awards**").

(h) All assignable or transferable licenses, authorizations, approvals and permits issued by any Governmental Authority relating to the operation, ownership, use, occupancy or maintenance of the Facilities (collectively, the "**Approvals**").

(i) All assignable or transferable intangible property, benefits, and privileges relating or pertaining to the Facilities and the Business, including all of Seller' s right, title and interest in and to all environmental reports, hydrology studies, ADA

surveys, soil reports, utility agreements (excluding Seller's utility deposits which shall be returned to Seller at Closing), construction, equipment, and other indemnities, contractual and other rights, trademarks, service marks, trade names, applications, development rights and approvals, permits, approvals, plans, drawings, specifications, surveys, maps, engineering reports, assignable insurance proceeds, and all other intangible rights used in connection with or relating or pertaining to the ownership or operation of the Facilities or the Business (collectively, the "**Intangible Property**").

(j) All assignable or transferable warranties and guaranties presently in effect from contractors, suppliers or manufacturers of personal property installed in or used in connection with the Property or any work performed or improvements included as a part of the Property which are listed on **Exhibit D** attached hereto (collectively, the "**Warranties**").

(k) All Assumed Service Contracts.

(l) All telephone numbers, telephone directory listings and advertisements used in or at the Facilities (the prepaid expenses of which shall be prorated at Closing).

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(m) All assignable or transferable goodwill relating to or arising in connection with the ownership or operation of the Facilities or the Business.

(n) All Resident Trust Funds.

(o) All claims, causes of action and other legal rights and remedies of Seller, but not Seller's Obligations, whether or not known as of the Closing Date, relating to or in connection with (i) Seller's ownership of the Assets, or (ii) the operation of the Facilities or the Business that are reasonably necessary to preserve or obtain for the benefit of Buyer full rights to the Assets, but excluding causes of action and other legal rights and remedies of Seller (A) against Buyer with respect to the transactions contemplated by this Agreement, or (B) relating exclusively to the Excluded Assets.

**3.2 Excluded Assets.** It is expressly agreed that Seller shall retain and Buyer shall not acquire the following assets (the "**Excluded Assets**"):

(a) All Cash and all cash-like assets, excluding all Resident Trust Funds, as of the Closing Date.

(b) All minute books, charter documents, stock record books, books and records pertaining to the organization, existence or capitalization of Seller, including, for the avoidance of doubt, all financial, accounting and tax records of or relating to Seller.

(c) All books and records relating to any Excluded Assets.

(d) All assets transferred or otherwise disposed of by Seller in the ordinary course of business and in accordance with this Agreement prior to the Closing.

(e) All prepaid assets or refunds or credits of Taxes, as of the Closing Date.

(f) All files, charts, and other information relating to all Residents who previously occupied or used the Facilities prior to the Closing Date and who are not Residents of the Facilities on the Closing Date.

(g) All accounts receivable as of the Closing Date.



**ARTICLE IV**  
**ASSUMED OBLIGATIONS**

**4.1. Assumed Service Contracts.** Set forth on **Exhibit B** is a list of all material vendor, lease, service and other Contracts to which third-party vendors provide goods or services to the Facilities and to which Seller is a party (the “**Service Contracts**”). Notwithstanding the preceding sentence, the term “Service Contracts” shall expressly exclude all Contracts entered into by ADK pursuant to which third-party vendors provide goods or services to the Facilities including, without limitation, ADK’s participation agreement with Forum Purchasing, LLC and the right to purchase goods and services thereunder. During the Study Period, Seller shall make available to Buyer at the Facilities copies or originals of all such Service Contracts. At or prior to the end of the Study Period, Buyer shall notify Seller which of the Service Contracts it desires

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Seller to assign to Buyer, and, unless any such Service Contracts shall have expired or been terminated by Seller for cause prior to the Closing, Seller shall assign all of its rights in such Service Contracts to Buyer effective as of the Closing Date. After the end of the Study Period, Seller shall not terminate any such Service Contracts without the consent of Buyer. If, as a condition to the assignment of any of the Service Contracts so designated by Buyer, it shall be necessary to cure any defaults thereunder, then, as a condition to such assignment, Seller may either perform such acts and/or pay such sums (if any) as shall be required to cure any such default. If Buyer desires a Service Contract to be assigned and Seller does not cure a default with respect thereto, such Service Contract shall not be assigned to Buyer. To the extent that any Consent is needed to assign any of the Service Contracts to Buyer, Seller shall use its reasonable efforts to obtain such Consent at its cost. If such Consent has not been obtained on or prior to the Closing Date and the Closing occurs, this Agreement shall not constitute an assignment or attempted assignment thereof if such assignment or attempted assignment would constitute a breach thereof and no Obligations under such Service Contract shall be assumed by Buyer. If any Consent shall not be obtained on or prior to the Closing Date and the Closing occurs: (a) Seller shall use its reasonable efforts to obtain such Consent as promptly as practicable thereafter, and (b) if, in the reasonable judgment of Seller, such Consent cannot be obtained, such Service Contract shall not be assigned to Buyer. The Service Contracts assigned by Seller to Buyer hereunder are referred to as the “**Assumed Service Contracts.**” Buyer shall assume and undertake to perform any and all obligations under the Assumed Service Contracts assigned to it as aforesaid only with respect to Obligations arising after the Closing Date (the “**Assumed Obligations**”). Except for the Assumed Obligations and those Obligations assumed by Buyer under Section 6.4(f) (with respect to New Cap Ex Obligations), Buyer shall not assume, perform or be responsible for any Obligations of Seller whether or not relating to the Assets or the Business. Seller shall take whatever steps as may be required to terminate or cancel as of the Closing those Service Contracts which are not assigned to Buyer and Seller shall remove (or cause to be removed) from the Facilities any machinery or equipment which is subject to the unassigned Service Contracts. Notwithstanding the foregoing, Seller shall not terminate or cancel any Service Contract which Buyer desires to assume but which is not assigned to Buyer at the Closing (because the requisite Consent has not been obtained), until such time as Seller determines that such Consent cannot be obtained. In the event such Consent is obtained, then promptly thereafter, Seller shall assign such Service Contract to Buyer by an appropriate assignment and assumption agreement.

**4.2. Seller’s Obligations.** Notwithstanding anything to the contrary contained herein, in no event shall Buyer assume, perform or be responsible for any of the following (collectively, “**Seller’s Obligations**”): (a) any Obligation of Seller under Medicaid or any provider or other agreement relating to the Facilities, including, any amounts determined as a result of an audit or denial of a claim to be due by Seller under Medicaid because Seller has been overpaid during the period prior to the Closing Date or has received payments for which it is not entitled, (b) any Obligation under any Assumed Service Contract resulting from an act or omission of Seller occurring prior to the Closing Date, (c) any Obligation under any Service Contract not assumed by Buyer pursuant to and in accordance with Section 4.1, (d) any malpractice or other tort claim to the extent such claim is based upon acts or omissions of Seller occurring prior to the Closing Date, (e) any claim for breach of contract to the extent based on acts or omissions of Seller occurring prior to the Closing Date, (f) any accounts payable, Taxes, or other Obligation of Seller to pay money arising prior to the Closing Date, (g) any Obligations regarding the Resident

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Trust Funds arising prior to the Closing Date or occurring or relating to occurrences prior to the Closing Date, (h) any payment in full of any costs associated with the prepayment of any existing debt, and (i) any other Obligation of Seller with respect to the Assets or the Business arising prior to the Closing Date or based on acts or omissions of Seller (or on behalf of Seller) occurring prior to the Closing Date.

## ARTICLE V CLOSING

**5.1. Closing.** The Closing shall take place by the release of documents and funds held in escrow by the Escrow Agent at such time as may be mutually agreed upon by the parties hereto, but no later than December 31, 2012, unless Closing shall have been extended by mutual agreement of the parties.

## ARTICLE VI PURCHASE PRICE; ALLOCATION; RECORDATION COSTS; PRORATIONS

**6.1. Purchase Price.** Buyer shall pay Twenty Two Million Three Hundred Seven Thousand Four Hundred Ninety and 00/100 Dollars (\$22,307,490.00) to Seller as the purchase price for the Assets (the "**Purchase Price**"); as follows:

(a) Within three (3) Business Days after the execution of this Agreement by both parties, Buyer shall deposit with the Title Insurer, as Escrow Agent, the sum of Fifty Thousand and 00/100 Dollars (\$50,000.00) (the "**Deposit**") which shall be held by the Title Insurer in an interest-bearing account. The Deposit and any interest thereon shall be fully refundable to Buyer until the end of the Study Period or shall, along with the Additional Deposit and any interest thereon, be applied towards the Purchase Price at the time of Closing. In the event the purchase of the Assets does not occur for any reason, the party entitled to the Deposit shall be entitled to any interest earned thereon. The Deposit shall be held by the Title Insurer pursuant to an Escrow Agreement in the form attached hereto as **Exhibit D** (the "**Escrow Agreement**"). If Buyer does not terminate this Agreement on or before the expiration of the Study Period, Buyer shall, within two (2) Business Days after the expiration of the Study Period, deposit the sum of One Hundred Fifty Thousand and 00/100 Dollars (\$150,000.00) with the Escrow Agent (the "Additional Deposit"). The Additional Deposit shall be held and disbursed as part of the Deposit.

(b) At Closing, Buyer shall satisfy the principal balance of the HUD Loans for the Facilities (the "**HUD Loans**"), excluding the Vandalia HUD Loan.

(c) At Closing, Buyer shall assume the HUD Loan secured by Hearth & Home of Vandalia, located in Vandalia, Ohio (the "**Vandalia HUD Loan**"). All reserves held in connection with the Vandalia HUD Loan shall be for the benefit of Buyer.

(d) At Closing, Buyer shall execute and deliver to Seller a promissory note in the principal amount of Three Million Six Hundred Thousand and 00/100 Dollars (\$3,600,000.00) bearing interest at the rate of Five Percent (5%) per annum with a maturity date of the earlier of (i) Buyer's refinancing of the Vandalia HUD Loan or (ii) September 1, 2014 in the form attached hereto as **Exhibit E** (the "**Seller Note**"). Interest on the Seller Note shall be paid monthly in arrears

and the Seller Note shall be secured by Buyer's pledge of the equity interest in the entity which will hold fee simple title to Hearth & Home of Vandalia, located in Vandalia, Ohio in the form attached hereto as **Exhibit F** (the "**Pledge Agreement**"). The Seller Note shall be subject to set off by Buyer against any claims for indemnification from Seller pursuant to §21.1(a), (b), (c), (d), (e) or (f).

(e) At Closing, Buyer shall pay to Seller the Purchase Price less (i) the principal balances of the HUD Loans, (ii) the Vandalia HUD Loan, (iii) the Seller Note and (iv) the Deposit (and all accrued interest thereon) (hereinafter referred to as the "**Cash Consideration**"), by wired funds received by the Title Insurer at or before 4:00 p.m., Eastern Standard Time, on the Closing Date in accordance with written wiring instructions provided to Buyer by the Title Insurer. All reserves held in connection with the HUD Loans (other than the Vandalia HUD Loan) shall be first applied to any prepayment penalties due in connection with the payoff of the HUD Loans (other than the Vandalia Loan) and Cap Ex Obligations that are agreed to by the parties and identified as such on **Exhibit G** and the remaining balance of such reserves shall be returned to Seller at or following the Closing and Seller shall be entitled to retain such reserves without reduction to the Purchase Price.

**6.2. Recordation Costs.** Seller shall pay the cost of any recording fee and any state or county recordation tax or other transfer fee incurred in recording the deed or any related documents among the real property records of the applicable counties in which the Facilities reside. Buyer shall pay for (i) one-half the costs of any title insurance, (ii) the costs of real property surveys and other inspections or tests with respect to the Facilities, (iii) its own legal fees, and (iv) the amount of net adjustments (as described below), if any, to be paid to Seller. Seller shall pay (i) one-half the costs of title insurance, (ii) any amounts expressly assumed in this Agreement, (iii) its own legal fees and (iv) the amount of net adjustments (as described below), if any, to be paid to Buyer.

**6.3. Prorations.** In addition to any other customary items, the following items are to be apportioned on a *pro-rata* basis as to ownership as of Closing Date:

(a) Any real property tax or assessment affecting the Property as of the Closing Date that is payable in one or more annual installments shall be apportioned between the parties as of Closing, based on the tax or installment due for the taxing period in which Closing occurs.

(b) Water, gas, electric and other utility charges, and sewer and waste water charges, shall be adjusted as of the Closing Date. If there are meters measuring the consumption of any utility or other service to the Property, then Seller shall cause the meters to be read not more than one (1) day before the Closing Date. For metered service, Seller shall pay the utility bills for services rendered prior to the readings, and Buyer shall pay the utility bills for the services rendered after the readings.

(c) Costs under the Assumed Service Contracts shall be paid through the Closing Date by Seller, and shall otherwise be terminated or assumed as described in Section 4.1.

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(d) Buyer shall reimburse Seller for the costs of fuel oil, if any, purchased by Seller for use at the Facilities, on the Closing Date.

(e) Rent/Residents' Occupancy Fees.

(i) Any rent or Residents' occupancy fees accrued for any period ending before the Closing Date (1) which is paid to Seller before Closing shall be retained by Seller, or (2) which is due but unpaid as of Closing shall not be adjusted between Seller and Buyer, and Seller shall bear and retain the risk and the burden of collecting the same; provided, that if after Closing Buyer is actually paid any such rent or fees, Buyer shall (after first applying such payment to the payment of any rent or Residents' occupancy fees which has then accrued) remit to Seller the balance remaining after such application.

(ii) Any rent or Residents' occupancy fees accruing for the month during which Closing occurs (1) which is paid before Closing, shall be adjusted between Seller and Buyer, at and as of Closing, or (2) which is paid to either party hereto after Closing, shall be adjusted if, as and when collected, between Seller and Buyer as of Closing, and the respective amounts thereof due to the parties hereto shall be paid to them promptly thereafter by the party to which such rent or fees was remitted.

(iii) At Closing, Seller shall deliver to Buyer a schedule of any and all unpaid rent or Residents' occupancy fees accrued before Closing, and shall by such delivery be deemed to have warranted to Buyer the truth, completeness and accuracy of such schedule, which warranty shall survive Closing.

(f) Capital Improvement Costs.

(i) Capital improvement repairs and expenses, including without limitation construction costs, insurance premiums related to the construction, construction bond fees and all other out-of-pocket costs which are the obligation of Seller under any capital improvement or repair contract ("**Cap Ex Obligations**"), shall be allocated between the parties according to whether such obligations arose prior to Closing, regardless of the expected completion date for such repairs. Cap Ex Obligations that exist as of the date of this Agreement are the "**Existing Cap Ex Obligations**," and are set forth on **Exhibit G** attached hereto. Cap Ex Obligations that arise prior to the Closing but after the date of the Study Period Agreement or capital repairs that commence during the pendency of this Agreement, and are approved by Buyer upon notice from Seller, are the "**New Cap Ex Obligations**."

(ii) Existing Cap Ex Obligations, to the extent not previously paid for by Seller, shall be withheld from the Purchase Price at Closing, and placed in escrow with the Escrow Agent. Seller shall be responsible for paying such Existing Cap Ex Obligations which work will be performed by or on behalf of Buyer. Seller shall be entitled to utilize the Existing Cap Ex Obligations escrow for payment of the Existing Cap Ex Obligations and, upon written request from Seller, the Escrow Agent shall make such disbursements provided Buyer shall have approved such disbursements (not to be unreasonably withheld or delayed). If Seller fails to pay within ten (10) days after the submission of an invoice for such Cap Ex Obligations, then the Escrow Agent shall release funds to Buyer sufficient to pay such invoice. If there are any funds

remaining in the escrow after the payment, in full, of such Existing Cap Ex Obligations, such excess shall be paid to Seller. If the amount in escrow is insufficient for such purpose, then Seller shall, within fifteen (15) Business Days, pay for such deficiency upon request, accompanied by evidence of the deficiency. Seller shall cause all Cap Ex Obligations related repairs, improvements and construction that are performed prior to Closing, to be done in a workmanlike manner, free and clear of all liens and encumbrances.

(iii) Buyer shall reimburse Seller for the costs of New Cap Ex Obligations properly performed and paid for by Seller to the extent such New Cap Ex Obligations were approved in writing by Buyer. Buyer shall assume the obligation to perform and pay for all New Cap Ex Obligations not paid for by Seller.

(iv) After the end of the Study Period, Seller agrees that it shall not consent to or permit to occur any change order or addition to Cap Ex Obligations or changes in the cost, timing or scope of work or specifications with respect to Existing Cap Ex Obligations or New Cap Ex Obligations without Buyer's prior written consent, which shall not be unreasonably withheld or delayed. If Buyer is responsible for completing capital improvements pursuant to the foregoing provisions of this subsection (f), then at Closing Seller shall assign to Buyer all contracts related to such construction, pursuant to an assignment in form and substance acceptable to both parties.

Buyer and Seller shall cooperate to produce prior to Closing a schedule of prorations to be made under this Section 6.4 on Closing as complete and accurate as reasonably possible. All prorations which can be accurately or reasonably estimated as of Closing shall be made at Closing. All other prorations, and adjustments to initial estimated prorations, shall be made by the parties

with due diligence and cooperation within thirty (30) days following Closing, or such later time as may be required to obtain necessary information for proration, by immediate cash payment to the party yielding a net credit from such prorations from the other party.

## ARTICLE VII TITLE AND POSSESSION

7.1. **Deed.** At Closing, Seller shall convey the Property to Buyer in fee simple, by a limited warranty deed in the form attached as **Exhibit H**, subject only to the operation and effect of the following:

- (a) Any restrictions or regulations affecting the Property by virtue of any zoning, administrative or other law or regulation of any Governmental Authority having jurisdiction over the same, whether now or hereafter in effect;
- (b) The lien of real estate taxes for 2012 and subsequent years, not yet due and payable; and
- (c) Those items set forth in Section B-II of Buyer's approved title commitment for the Property to be issued by the Title Insurer. The items listed in clauses (a) through (c) are, collectively, the **"Permitted Encumbrances."**

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7.2. **Title.**

(a) Seller shall transfer fee simple, good and marketable title to the Property to Buyer, subject only to the Permitted Encumbrances, which title shall be insurable by the Title Insurer at its standard rates. If the title commitment issued to Buyer during the Study Period contains any lien or encumbrance other than a Permitted Encumbrance, or reveals any matter which causes Seller's fee simple title to the Property to not be good and marketable of record, then Buyer shall give Seller written notice of the same within ten (10) days after Buyer's receipt of the title commitment or proforma from the Title Insurer. Subject to the provisions of Sections 6.1(b) and (c) above, Seller shall discharge any mortgage liens, monetary liens, mechanics liens, judgment liens or any lien, encumbrance, covenant or restriction at or prior to Closing, or extend the Outside Closing Date for such time as is reasonably necessary to cure or remove the objection, not to exceed thirty (30) days.

(b) If Seller is unable to cure an objection, Seller shall give Buyer written notice of Seller's inability to cure. In such event, Buyer shall have the option to either (i) waive its objection and proceed to Closing (without any reduction in the Purchase Price), or (ii) in addition to its other rights and remedies under Section 19.3, to terminate this Agreement by giving Seller written notice of such termination within five (5) days after receipt of the non-cure notice from Seller. If Buyer terminates this Agreement, then the Deposit, and any interest thereon, shall be returned to Buyer and neither party shall have any further obligation to the other except as provided in Sections 15.1(c) (relating to damages to property) and 22.1 (relating to broker's commissions).

(c) **Bill of Sale.** At Closing, Seller shall sell, assign, convey, transfer, and set over to Buyer good and marketable title to the Building Service Equipment, Medical Equipment, Inventory, Records, Awards, Approvals, Intangible Property, Warranties, Property Information, goodwill and other Assets being sold hereunder (other than the Property) (collectively, the **"Personal Property"**), by a bill of sale in substantially the form attached hereto as **Exhibit I** (the **"Bill of Sale"**). Seller hereby agrees to indemnify and hold Buyer harmless against any liability incurred because of any non-payment of any Tax which may be imposed upon the sale of any Personal Property. The parties' rights and obligations under this Section 7.2(c) shall survive Closing.

(d) **Possession and Burden of Risk.** At Closing, Seller shall deliver to Buyer possession of the Personal Property, subject to all rights of occupancy under the Residents' occupancy agreements, in substantially the same condition as the condition on the date hereof, subject to reasonable wear and tear. Until Closing, Seller shall bear the risk of any damage to or destruction of any Personal Property.

(e) **Assignment and Assumption Agreement.** At Closing, Seller and Buyer shall execute and deliver an Assignment and Assumption Agreement covering all Resident Trust Funds and the Assumed Service Contracts, substantially in the form attached hereto as **Exhibit J** (the “*Assignment and Assumption Agreement*”), by which Seller assigns to Buyer all of Seller’s right, title and interest in and to the Resident Trust Funds and Assumed Service Contracts.

**ARTICLE VIII  
MEDICAID PROVIDER AGREEMENTS**

**8.1. Seller’s Medicaid Provider Agreements.** Buyer hereby elects not to assume and shall not assume Seller’s right and interest in and to Seller’s Medicaid provider numbers and Medicaid provider reimbursement agreements with respect to Facilities. Seller shall terminate its Medicaid Provider Agreements and surrender its Medicaid provider numbers as of the Closing Date. Promptly after the execution of this Agreement, Seller and Buyer shall each notify the Ohio Department of Job & Family Services advising of the change in ownership of the Business and the Facilities from Seller to Buyer, and shall include in such notices all information required to be provided to the Department in connection with said change in ownership, in sufficient time to permit the Closing to occur on or before the intended Closing Date

**ARTICLE IX  
CHANGE OF OWNERSHIP OF THE FACILITIES**

**9.1. Licensure Approvals.** Promptly after the receipt of a fully executed copy of this Agreement, Buyer shall file all applications and other documents required by the State of Ohio for the issuance of all licenses and permits necessary to operate the Facilities under the laws of the State of Ohio (the “*Licensure Approvals*”). Seller hereby agrees to cooperate with Buyer in obtaining the Licensure Approvals. Buyer shall, from time to time, upon request of Seller, advise Seller of the status of Buyer’s efforts to secure the Licensure Approvals. Seller shall be solely responsible for any and all costs (not to exceed \$100,000.00) associated with the change of ownership process including, but not limited to, any physical plant or other changes required to bring the Facilities into compliance with the currently effective licensure and certification or other legal requirements if and to the extent it is not currently in such compliance and such compliance is required as a matter of State or Federal law. To the extent the costs referenced in the preceding sentence exceed \$100,000.00 and Seller refuses to pay such excess costs after receipt of written notice from Buyer, Buyer may (i) pay such costs in excess of \$100,000.00 or (ii) terminate this Agreement and receive a refund of the Deposit together with accrued interest.

**9.2. Cooperation in Transition of the Business.** Seller and Buyer shall cooperate with each other to effectuate a smooth and orderly transition of the ownership and operation of the Facilities and the Business.

**ARTICLE X  
TRANSFER OF RESIDENT TRUST FUNDS**

**10.1. Resident Trust Funds.** On the Closing Date, Seller shall deliver to Buyer an accounting and inventory of (a) any and all sums which Seller is holding, or is charged with holding, for or for the account of the Residents of the Facilities on the Closing Date, (b) any interest or payment in lieu of interest accruing before Closing on any such sums under the provisions of any occupancy agreement or instrument related thereto, or under applicable law, for which Seller is liable to the Residents and which has not been paid to the Residents before Closing, and (c) any and all property of the Residents being held by Seller as of the Closing Date in trust for Residents (collectively, “*Resident Trust Funds*”), together with a schedule listing each such Resident, the amount of Cash being held by Seller for or on account of such Resident,

the respective Resident occupancy agreement under which it is being held and the manner in which the amount thereof was calculated, which schedule shall be certified by Seller to Buyer as being true, accurate and complete in all respects. On the Closing Date, Seller shall transfer the Resident Trust Funds to Buyer and Buyer shall accept the same in trust for the Residents and be solely accountable to the Residents for such Resident Trust Funds in accordance with the terms of this Agreement, the Residents' occupancy agreements and applicable statutory and regulatory requirements. Buyer shall have no responsibility to the applicable Resident or regulatory authority with respect to any Resident Trust Funds delivered by Seller to Buyer for claims which arise or from actions or omissions of Seller with respect to the Resident Trust Funds occurring before the Closing Date. Seller shall have no responsibility to the applicable Resident or regulatory authority with respect to any Resident Trust Funds delivered to Buyer for claims which arise from actions or omissions of Buyer with respect to the Resident Trust Funds occurring on or after the Closing Date. Buyer shall indemnify Seller against any liability to any such Resident or Tenant or other Person for any Resident Trust Funds delivered to Buyer, as aforesaid, and Seller shall indemnify Buyer against any liability to any Resident for any Resident Trust Funds not delivered to Buyer, as aforesaid, each of which obligations shall survive Closing.

## **ARTICLE XI EMPLOYEES**

**11.1. Termination of Seller's Employees.** Seller shall terminate all of the employees of the Facilities effective as of 11:59 p.m. on the day immediately prior to the Closing Date. Unless otherwise agreed by Seller and Buyer, Seller shall pay directly to such employees any unpaid wages and/or accrued benefits which are due and payable to the employees of the Facilities as of the Closing Date. Seller shall provide Buyer with a list of employees at least fifteen (15) Business Days prior to the Closing Date and shall permit Buyer, in cooperation and coordination with Seller, to meet with the employees of the Facilities prior to the Closing Date and to advise them of Buyer's proposed plans with respect to the hiring of the employees of the Facilities and the benefits which will be offered to the employees of the Facilities. Except as set forth on Exhibit K, Seller has not terminated the employment of any employee of the Facilities within sixty (60) days prior to the date hereof, and, after expiration of the Study Period, except after notice to Buyer, Seller will not terminate any employee's employment.

**11.2. Hired Employees.** Buyer agrees to cooperate with Seller to provide information concerning which Facilities employees ("**Facilities Employees**") are retained by Buyer and the service descriptions and salary levels for any such Facilities Employees. Such employees whose employment is continued shall be referred to as the "**Hired Employees.**" Seller or its Affiliates shall have the right (but not the obligation) to employ or offer to employ any employee who Buyer does not offer employment to or who declines Buyer's offer of employment; provided, however, that Seller shall not actively solicit such employees. For a period of three (3) year after the Closing Date, Seller agrees not to solicit any of the Hired Employees while they remain in the employment of Buyer for employment at any other facility owned or operated by Seller or its Affiliates; provided, however, for purposes hereof the placement of an advertisement in a publication of general circulation which is seen by such Hired Employees shall be not be deemed to be solicitation of such employees.

**11.3. Employee Benefits.** Seller shall offer and provide, as appropriate, group health plan continuation coverage pursuant to the requirements of Section 601, *et seq.* of the Employee Retirement Income Security Act of 1974 ("**ERISA**") and Section 4980B of the Internal Revenue Code ("**COBRA**") to all of the employees of the Facilities to whom it is required to offer the same under applicable law. Seller acknowledges and agrees that Buyer is not assuming any of Seller's obligations to its employees under COBRA or otherwise. As of the Closing Date, all Hired Employees who participate as of the Closing Date in group health insurance coverage sponsored by Seller shall be eligible (subject to the terms and conditions of Buyer's health and welfare plans) for participation in a group health plan (as defined for purposes of Internal Revenue Code Section 4980B) established and maintained by Buyer for the general benefit of its employees but shall be subject to all such deductibles as if they become new members on the Closing Date unless

(x) they are under a waiting period with Seller at the Closing Date, in which case they shall be required to complete their waiting period while under Buyer's group health plan or in accordance with the terms of Buyer's benefit plan, or (y) they were subject to a pre-existing condition exclusion while under Seller's group-health plan, in which case they shall be subject to the same exclusion while in Buyer's group health plan or in accordance with the terms of Buyer's benefit plans, which exclusion shall, if applicable, be subject to the same time limitation while said employees are in Buyer's employ as was applicable thereto while said employees were in Seller's employ, with the time limit calculated from the date the same commenced while said employees were in Seller's employ.

**11.4. Compliance With WARN Act.** Seller and Buyer acknowledge and agree that the provisions of this Article XI are designed solely to ensure that Seller is not required to give notice to the employees of the Facilities of the "closure" thereof under the Worker Adjustment and Retraining Act (the "*WARN Act*") or any other comparable state laws. Nothing in this Article X shall create any rights in favor of any Person not a party hereto, including the Facilities Employees, or constitute an employment agreement or condition of employment for any employee of Seller or any Affiliate of Seller.

## ARTICLE XII ACCOUNTS RECEIVABLE

**12.1. Accounts Receivable.** Seller shall retain whatever right, title and interest it may have in and to all outstanding accounts receivable with respect to the Facilities which relate to the period prior to the Closing Date, including, but not limited to, any accounts receivable arising from rate adjustments which relate to the period prior to the Closing Date even if such adjustments occur after the Closing Date ("*Seller's A/Rs*"). Seller acknowledges that Buyer owns all accounts receivable arising from services provided by or at the Facilities on or after the Closing Date ("*Buyer's A/Rs*").

**12.2. Receipts by Buyer.** In furtherance and not in limitation of the requirements set forth in Section 12.1, payments received by Buyer on or after the Closing Date from third-party payors, including, but not limited to, Medicaid, VA, managed care and health insurance, shall be handled as follows:

(a) If such payments either specifically indicate on the accompanying remittance advice, or if the parties agree that they relate to the period prior to the Closing Date,

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they shall be forwarded by Buyer to Seller, along with the applicable remittance advice, within seven (7) Business Days after receipt thereof; and

(b) If such payments indicate on the accompanying remittance advice, or if the parties agree that they relate to the period on or after the Closing Date, they shall be retained by Buyer.

**12.3. Receipts by Seller.** Payments received by Seller on or after the Closing Date from third-party payors, including, but not limited to, Medicaid, VA, managed care and health insurance, shall be handled as follows:

(a) If such payments either specifically indicate on the accompanying remittance advice, or if the parties agree that they relate to the period on or after the Closing Date, they shall be forwarded by Seller to Buyer, along with the applicable remittance advice, within seven (7) Business Days after receipt thereof; and

(b) If such payments indicate on the accompanying remittance advice, or if the parties agree that they relate to the period prior to the Closing Date, they shall be retained by Seller.



**12.4. Other Receipts.** If the remittance advice indicates or the parties agree that any payment relates to periods both prior to and on or after the Closing Date, the party receiving the payment shall forward the amount relating to the other party's operation, along with the applicable remittance advice, within seven (7) Business Days after receipt thereof. If the remittance advice does not indicate the period to which a payment relates or whether it is for Seller or Buyer, or if there is no accompanying remittance advice, or the payment is not otherwise identifiable using commercially reasonable efforts, and if the parties do not otherwise agree as to how to apply such payment, then 100% of such payments received within the first one hundred eighty (180) days after the Closing Date shall be deemed to have been collected in respect of Seller's A/R due from the payee in respect of services provided prior to the Closing Date. All such payments received in excess of the amount of Seller's A/R due from said payee and all such payments received after the 180<sup>th</sup> day after the Closing Date shall be deemed to have been collected in respect of Buyer's A/R from said payee. All such payments received by Buyer but which are deemed to be due Seller under this Section 12.4 shall be forwarded by Buyer to Seller within seven (7) Business Days after receipt thereof, and all such payments received by Seller but which are deemed to be due Buyer under this Section 12.4 shall be forwarded by Seller to Buyer within seven (7) Business Days after receipt thereof. All such payments received by Seller which are deemed to have been collected in respect of Seller's A/R shall be retained by Seller and all such payments received by Buyer which are deemed to have been collected in respect of Buyer's A/R shall be retained by Buyer.

**12.5. Accounting for Accounts Receivable.**

(a) As soon as reasonably possible but not later than twenty (20) Business Days after the Closing Date, Seller shall provide Buyer with a schedule of Seller's A/Rs listing by patient the amounts due as of the Closing Date and the respective payees.

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(b) For a period of six (6) months following the Closing Date, Buyer shall provide Seller with (i) an accounting by the 20<sup>th</sup> day of each month setting forth all amounts received by Buyer during the preceding month with respect to Seller's A/Rs which are listed on the schedule provided by Seller pursuant to Section 12.5(a), and (ii) copies of all remittance advices relating to such amounts received and any other reasonable supporting documentation as may be required for Seller to determine the Seller's A/Rs that has been paid. Buyer shall deliver such accounting to Seller at Seller's record address in this Agreement.

(c) For a period of six (6) months following the Closing Date or until Seller receives payment of all accounts receivable attributed to the operation of the Facility prior to the Closing Date, whichever is sooner, Seller shall provide Buyer (no less frequently than monthly) with (i) an accounting setting forth all amounts received by Seller with respect to Buyer's A/Rs using the same type of schedule as that provided by Seller pursuant to Section 12.5(a), and (ii) copies of all remittance advices relating to such amounts received and any other reasonable supporting documentation as may be required for Buyer to determine the Buyer's A/Rs that have been paid. Seller shall deliver such accounting to Buyer at the following address: Easton Town Center, 4100 Regent St., Suite F., Columbus, Ohio 43219, Attention: Roger C. Vincent, President.

(d) For a period of one (1) year following the Closing Date, Buyer and Seller shall, upon reasonable notice and during normal business hours, have the right to inspect all cash receipts of the other party in order to confirm the other party's compliance with the obligations imposed on it under this Article XII. Notwithstanding the foregoing, if such information can be transmitted through electronic mail, then Buyer and Seller may satisfy their obligations under this Section 12.5 in that manner.

**ARTICLE XIII  
REPRESENTATIONS AND WARRANTIES**

**13.1. Seller's Representations.** To induce Buyer to enter into this Agreement, Seller (jointly and severally) hereby represents and warrants to Buyer as of the date of this Agreement and re-states as of the Closing Date, as follows:

(a) Seller has been duly organized and is validly existing, is in good standing in Ohio, its state of formation, and is qualified to do business and is in good standing in each of the states in which it owns property or does business. Seller has full power and authority and possesses all material governmental Approvals necessary to enable it to own, license, possess, lease or otherwise hold its properties and assets and to carry on the Business and to operate the Facilities as presently conducted.

(b) Seller has the full right, power and authority to execute this Agreement and to consummate the sale of Assets and the other transactions contemplated by this Agreement. The Person executing this Agreement on behalf of Seller is authorized to do so. Seller has duly executed and delivered this Agreement, and this Agreement constitutes the legal, valid and binding obligation of Seller, enforceable against it in accordance with its terms. The execution and delivery by Seller of this Agreement and the other documents contemplated hereby do not, and the consummation of transactions contemplated by this Agreement and

compliance by Seller with the terms hereof, do not, and will not, conflict with, or result in any violation of or default under (with or without notice or lapse of time, or both), or result in the creation of any lien or encumbrance upon any of the assets or properties of Seller under, any provision of (i) the organizational documents of Seller, (ii) any Contract to which Seller is a party or by which any of its assets or properties is bound, or (iii) any judgment, writ, order or decree or Law that is applicable to Seller or its assets or properties. No Consent of, or registration, declaration or filing with (A) any Governmental Authority, or (B) any other Person, is required to be obtained or made by or with respect to Seller, in connection with the execution, delivery and performance of this Agreement or the consummation of the transactions contemplated hereby.

(c) Seller has good and marketable title to the Property free and clear of all liens and encumbrances except for the Permitted Encumbrances and the Vandalia HUD Loan. Seller has neither created, nor authorized any other party to create, any lien or encumbrances on the Property, other than the Permitted Encumbrances. To Seller's knowledge, there are no pending real estate assessment protests or proceedings with respect to the Property. Seller has title to all Personal Property and the execution and delivery to Buyer of the Bill of Sale shall vest title to all the Personal Property in Buyer, free and clear of liens and encumbrances. No Person has the right to purchase all or any of the Assets or any interest in Seller (except for the securities of ADK).

(d) The Assets are sufficient to permit the conduct of the Business immediately following the Closing in substantially the same manner as currently conducted.

(e) Except as set forth on Exhibit L attached hereto, there are no Approvals or Consents necessary or required to own, operate or use the Facilities or to operate the Business ("**Required Permits**"). Seller has a current certificate of occupancy and it and/or Seller's agents have all the other Required Permits necessary or required for the ownership and operation of the Facilities and the Business. All Required Permits are in full force and effect and are not subject to any claim, default, condition, sanction or penalty. Seller has delivered to Buyer true, correct and complete copies of the most recent Required Permits necessary or required for the ownership and operation of the Facilities and the Business.

(f) Except as described on Exhibit M attached hereto, there are no deficiencies described in any survey of the Facilities conducted by any Governmental Authority that has not been corrected or otherwise remedied.

(g) No taking by power of eminent domain or condemnation proceeding has been instituted or threatened for the permanent or temporary taking or condemnation of all or any portion of the Property.

(h) No labor has been performed or materials furnished at the request or direction of Seller that could result in a materialman's or mechanic's lien filed against the Property except as shall be fully paid or released prior to Closing. All real estate taxes on the Property that have become due and payable prior to Closing have been or will be paid by Closing.

(i) Except as set forth in **Exhibit N**, as of the date hereof, there are no actions, suits, material labor disputes or arbitrations, legal or administrative proceedings or investigations pending against Seller, the Business or the Facilities, and to the Knowledge of Seller, no actions, suits, material labor disputes or arbitrations, legal or administrative proceedings or investigations are contemplated or threatened against Seller in connection with the Facilities, nor is any basis known by Seller to exist for any such action or for any governmental investigations relating to the Business or the Facilities. Except as set forth on Exhibit O, there are no pending actions against Seller or relating to the Assets or the Business and no such actions have been commenced within the last three (3) years.

(j) Seller has complied in all material respects with each, and is not in violation of any, Law, to which it or the Facilities or the Business is subject, and has not failed to obtain any permit, or other governmental authorization or inspection necessary to the ownership or use of the Assets or to the conduct of the Business, including, the Federal Medicaid Statutes. Except as set forth on **Exhibit M**, Seller has not received any notice of any violations of any Law, nor does Seller have Knowledge of any such violations, including, without limitation, violations of: state licensing requirements for operation of the Facilities as nursing facilities, safety, handicapped accessibility, ADA, health, environmental, fire, zoning or subdivision laws, ordinances, codes and regulations. To Seller's knowledge, the Improvements are not presently in violation of any applicable building codes or other applicable laws.

(k) All environmental and property condition reports that are in Seller's possession have been delivered to Buyer and Seller has not received any notice of litigation, condemnation or violation of governmental or environmental requirements relating to the Property. Seller has received no notice that hazardous or toxic substances, materials or wastes, pollutants or contaminants (including, without limitation, petroleum and petroleum products, asbestos and PCBs) have been released, spilled, leaked, discharged, disposed of, pumped, poured, emitted, emptied, dumped or allowed to escape or threaten to release on, at, under or from the Property, and to Seller's knowledge, the Property is in material compliance with all Environmental Laws, and there have been no environmental proceedings with respect to the Property. As used herein, "**Environmental Law**" means all federal, state, or local laws, ordinances, requirements and regulations relating to waste disposal or protecting the environment, including without limitation. (i) the Comprehensive Environmental Response, Compensation, and Liability Act of 1980 (42 U.S.C. §§ 9601, et seq.), as amended ("CERCLA"); (ii) the Solid Waste Disposal Act (42 U.S.C. §§ 6901, et seq.), as amended; (iii) the Clean Air Act (42 U.S.C. §§ 7401, et seq.), as amended; (iv) the Clean Water Act (33 U.S.C. § 1251), as amended; (v) the Hazardous Materials Transportation Act (49 U.S.C. §§ 1801, et seq.), as amended; (vi) the Federal Insecticide, Fungicide and Rodenticide Act (7 U.S.C. § 136, et seq.), as amended; (vii) the Safe Drinking Water Act (41 U.S.C. § 300f, et seq.), as amended; (viii) the Federal Water Pollution Control Act (33 U.S.C. § 1251, et seq.) and (ix) the Toxic Substances Control Act (15 U.S.C. § 2601, et seq.).

(l) Within the last three (3) years, Seller has not made or pursued any claim under any insurance contracts, binders or policies relating to the Assets or the Business (the "**Insurance Policies**") except as otherwise listed within **Exhibit O**. Seller has not received from any insurance company which carries insurance on any of the Facilities or the Business, or any board of fire underwriters, any notice of any defect or inadequacy in connection with the

Facilities or the Business, or its operation, or request for the performance of any repairs, alterations or other work, and Seller has no knowledge of any such defect or inadequacy which might increase the premium or cause the cancellation of any of the Insurance Policies.

(m) [Intentionally Omitted]

(n) Seller is a "United States person" within the meaning of Sections 1445(f)(3) and 7701(a)(30) of the Internal Revenue Code of 1986, as amended.

(o) The Resident roll attached hereto as **Exhibit P** is a complete and accurate schedule of all the Residents as of the date hereof. Seller has not accepted any advance payment of more than thirty (30) days from any Resident.

(p) Attached as **Exhibit Q** is a copy of the audited balance sheet of Seller as of December 31, 2011 (the "**Balance Sheet**"), the audited statement of income and cash flows of Seller for the fiscal year ended December 31, 2011, and the unaudited statement of income and cash flows of Seller for the period ended September 31, 2102 (the financial statements described in this sentence, collectively, the "**Financial Statements**").

(i) The Financial Statements have been prepared, in all material respects, in conformity with accounting principles generally accepted in the United States of America, consistently applied (so-called "GAAP") (except in each case as described in the notes thereto and, in the case of the unaudited financial statements, subject to normal year-end audit adjustments) and reflects the financial condition, results of operations, cash flows and changes in partners' equity of Seller and as of the respective dates thereof and for the respective periods indicated. Since December 31, 2011, there have been no changes in Seller's methods of accounting for tax or financial statement purposes. Other than as set forth in the Financial Statements or arising in the ordinary course of business since such date, there are no other material Obligations of Seller.

(ii) Since December 31, 2011, to the date of this Agreement, Seller has caused the Business to be conducted in the ordinary course and in substantially the same manner as previously conducted. From the date of the Balance Sheet to the date of this Agreement and except as disclosed on **Exhibit Q**, Seller has not taken any action that, if taken after the date of this Agreement without the consent of Buyer, would constitute a breach of Section 14.2.

(q) Seller, has not received any notification as of the date of this Agreement from any party to a Contract that such party intends to terminate, discontinue or not proceed with such Contract or otherwise received any notification as of the date of this Agreement of any possible disruption to the Business as a result of the execution of this Agreement or the sale of the Assets.

(r) Seller has complied with and performed all of its Obligations required to be performed under all material Service Contracts relating to or in connection with the Facilities, or the Business or to which Seller is a party or by which it or the Assets are bound (whether as an original party or as an assignee or successor) as of the date hereof, and is not in default in any material respect under any Service Contract, undertaking, commitment or other Obligation; and no event has occurred which, with or without the giving of notice, lapse of time or both, would

constitute a default thereunder in any material respect. No party has failed to comply with or perform the Obligations required to be performed under any material Contract to which Seller is a party (whether as an original party or as an assignee or successor) as of the date hereof, and no event has occurred which, with or without the giving of notice, lapse of time or both, would constitute a default by such party thereunder. Except as set forth on **Exhibit B**, all Service Contracts are valid, binding and in full force and effect and are enforceable by Seller in accordance with their terms. In addition, except as disclosed on **Exhibit B**, there are no facts or circumstances which make a default by any party to any material contract or obligation likely to occur subsequent to the date hereof.

(s) Seller has not (i) made a general assignment for the benefit of its creditors, (ii) instituted, or been the subject of, any proceeding to be adjudicated bankrupt or insolvent or consented to the institution of bankruptcy or insolvency proceedings against it, (iii) filed a petition, answer or consent seeking reorganization or relief under any applicable Federal or state bankruptcy law or consented to the filing of any such petition or to the appointment of a receiver, liquidator, assignee, trustee, sequestrator or other similar official of it or of any part of its property, or (iv) admitted in writing its inability to pay its debts generally as they become due.

(t) Seller is not an employee benefit plan as defined in Section 3 (3) of the Employee Retirement Income Act of 1974, as amended (“**ERISA**”), which is subject to Title I of ERISA, nor a plan as defined in Section 4975(e)(1) of the Internal Revenue Code of 1986, as amended (each of the foregoing hereinafter referred to collectively as a “**Plan**”), and none of the Assets constitute “plan assets” as defined in Department of Labor Regulation Section 2510.3-101.

(u) In connection with the Facilities and the Business, Seller and each employee or individual or entity furnishing healthcare related services under arrangement (collectively, the “**Health Care Providers**”), to the extent required, is, to the Knowledge of the Seller, licensed under the applicable Laws of their state and, to the Knowledge of the Seller, each Health Care Provider has complied with all Laws, relating to the rendering of health care services. To the Knowledge of the Seller, no Health Care Provider has:

(i) had his or her professional license, Drug Enforcement Agency number or Medicare or Medicaid provider status, or participation in any other healthcare plan of a third-party payor suspended, relinquished, terminated or revoked;

(ii) been reprimanded, sanctioned or disciplined by any licensing board or any Federal, state or local society, agency, regulatory body, Governmental Authority, hospital, third-party payor or specialty board;

(iii) had a final judgment or settlement entered against him or her in connection with a malpractice or similar action; or

(iv) has engaged in, undertaken or accused, charged or convicted of criminal conduct or act.

(v) Neither Seller nor any of its respective partners, officers, directors, employees, agents or Affiliates has offered, paid, or agreed to pay to any Person, including any

governmental official, or solicited, received or agreed to receive from any such Person, directly or indirectly, any money or anything of value for the purpose or with the intent of obtaining or maintaining business for Seller or any Affiliate or otherwise affecting the business, operations, prospects, properties, or condition (financial or otherwise) of Seller, and which is or was in violation of any Law, or not properly and correctly recorded or disclosed on the books and records of Seller. Seller has not engaged in any transaction, maintained any bank account or used any other funds except for transactions, bank accounts and funds which have been and are properly and correctly reflected in the normally maintained books and records of Seller.

(w) To Seller’s knowledge, Seller is in compliance in all material respects with all Laws respecting employment and employment practices, terms and conditions of employment, compensation, wages and hours, health and safety, labor relations and plant closings, including all applicable foreign laws, the Americans with Disabilities Act, the Age Discrimination in Employment Act, the Equal Pay Act, the Fair Labor Standards Act, the National Labor Relations Act, Occupational Safety and Health Act, Title VII of the Civil Rights Act of 1964, as amended, the Family and Medical Leave Act, the Worker Adjustment and Retraining Notification Act, the Consolidated Omnibus Budget Reconciliation Act, and ERISA. Seller is not a party to any collective bargaining agreement or labor contract.

(x) In connection with the Facilities, Seller participates in the Medicaid Waiver Program (the “**Program**”). With respect to the Facilities, Seller does not participate in the Medicare Program. A list of and copy of its existing Medicaid Waiver contract and reimbursement agreements and all business and provider numbers pertaining to Seller or, if such contracts do not exist, other documentation evidencing such participation (collectively, the “**Program Agreement**”) is set forth on **Exhibit R** attached hereto. Seller is in material compliance with all of the terms, conditions and provisions of the Program Agreements. Seller is in compliance with rules and policies respecting the Program Agreement and third-party payor contract, including all certification, billing, reimbursement

and documentation requirements, and there is no threatened or pending revocation, suspension, termination, probation, restriction, limitation or non-renewal affecting the Program Agreement or third-party payor contracts.

**(y)** In connection with the Facilities, no notice of suspension, cross-recoupment, sanction or any other material offsets against future reimbursements under or pursuant to the Program has been received by Seller, nor is there any basis therefor. With respect to the Program, there are no pending appeals, adjustments, challenges, audits, litigation, notices of intent to recoup past or present reimbursements for any material amounts. Seller has not been subject to or threatened with any loss as a result of any utilization review denials with respect to the Program or any third-party payors during the past twelve (12) months, nor has Seller received notice of any pending, threatened or possible decertification or other loss of participation in, any of the Program.

**(z)** Seller has filed all material Tax Returns that it was required to file for any taxable period beginning before the Closing Date for which the statutory period of limitations for the assessment of Tax has not yet expired and all material Taxes owed by Seller for such taxable periods (whether or not shown as due on such Tax Returns) have been paid. Seller has withheld and paid all Taxes required to have been withheld and paid in connection with amounts paid or owing to any employee or independent contractor for all periods for which the statutory period of

limitations for the assessment of such Tax has not yet expired and all IRS Tax Returns required with respect thereto have been properly completed and timely filed. If at the Closing Date all or any part of the Assets is or has been affected by any one or more assessments which are or may become payable in annual installments of which the first installment is then a charge or lien, or has been paid, for the purpose of this Agreement all of the unpaid installments of any such assessment, including those that are due and payable after the Closing Date, Seller acknowledges that it shall be deemed to be due and payable and shall be paid and discharged by Seller at the Closing Date.

**(aa)** To Knowledge of Seller, except as set forth in those certain Environmental Phase I Assessments previously delivered to Buyer or to be delivered to Buyer during the Study Period, there currently is no lead paint, mold, asbestos, or material containing asbestos present in the common areas, or elsewhere on, in or under the Property.

**(bb)** The Property is not designated as historical, and there is no historical designation pending.

**(cc)** Seller has not made any commitments or representations to the applicable Governmental Authorities, any adjoining or surrounding property owners, any civic association, any utility, or any other Person that would in any manner be binding upon Buyer or upon the Property. Seller has received no notice which would refute that no such commitments or representations were made by any of Seller's predecessors in title.

**(dd)** Seller has received no notice that the heating, ventilation, air-conditioning, electrical, plumbing, water, fire alarm and structural systems or components of the Property are not in good working order and condition or are not in compliance with applicable requirements.

**(ee)** To Seller's knowledge, the parking spaces on the Property are all the parking spaces required by Law with respect to the Property and the Facilities and such spaces comply with applicable Laws. There are no contracts or other arrangements allowing persons who are not affiliated with the Facilities any parking rights at the Property and no Person other than the employees at the Facilities and visitors to the Facilities has the right to park on the Property.

**(ff)** No representation or warranty by Seller in this Agreement, any Exhibit attached hereto or in any list, certificate, document or written statement delivered by Seller to Buyer pursuant hereto, to the Knowledge of Seller, contains any untrue statement of fact or omits to state any material fact necessary to make any statement herein or therein, in the light of the circumstances

under which it was made, not misleading. Except as described in the Exhibits hereto or to be delivered, all documents and agreements described in such Exhibits are valid and effective in accordance with their respective terms and there is not under any of such documents or agreements, or any obligation, covenant or condition contained therein, any existing default by Seller or any other party, or event which with notice, lapse of time, or both constitute a default.

(gg) AS-IS SOLEY WITH RESPECT TO THE PROPERTY, EXCEPT AS OTHERWISE EXPRESSLY PROVIDED IN THIS AGREEMENT, SELLER HAS NOT MADE, AND BUYER HAS NOT RELIED UPON, ANY INFORMATION, PROMISE,

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REPRESENTATION OR WARRANTY, EXPRESS OR IMPLIED, REGARDING THE PROPERTY, WHETHER OR NOT MADE BY SELLER, INCLUDING, WITHOUT LIMITATION, ANY INFORMATION, PROMISE, REPRESENTATION OR WARRANTY REGARDING THE PHYSICAL CONDITION OR VALUE OF THE PROPERTY, TITLE TO OR THE BOUNDARIES OF ANY OF THE LAND OR THE FACILITIES, PEST CONTROL MATTERS, SOIL CONDITIONS, THE PRESENCE, EXISTENCE OR ABSENCE OF HAZARDOUS SUBSTANCES, TOXIC SUBSTANCES OR OTHER ENVIRONMENTAL MATTERS, COMPLIANCE WITH BUILDING, HEALTH, SAFETY, LAND USE AND ZONING LAWS, REGULATIONS AND ORDERS, STRUCTURAL AND OTHER ENGINEERING CHARACTERISTICS, TRAFFIC PATTERNS, MARKET DATA, ECONOMIC CONDITIONS OR PROJECTIONS, AND ANY OTHER INFORMATION PERTAINING TO ANY OF THE PROPERTY OR THE MARKET AND PHYSICAL ENVIRONMENTS IN WHICH THEY MAY BE LOCATED AND SELLER EXPRESSLY DISCLAIMS ALL WARRANTIES RELEVANT TO THE PROPERTY, EITHER EXPRESS OR IMPLIED, INCLUDING MERCHANTABILITY, FITNESS FOR A PARTICULAR PURPOSE, AND SUITABILITY FOR ITS INTENDED USE. BUYER ACKNOWLEDGES THAT (A) BUYER IS A SOPHISTICATED OWNER AND OPERATOR OF FACILITIES SIMILAR TO THE FACILITIES, (B) BUYER HAS ENTERED INTO THIS AGREEMENT WITH THE INTENTION OF MAKING AND RELYING UPON ITS OWN INVESTIGATION OR THAT OF THIRD PARTIES WITH RESPECT TO THE PHYSICAL, ENVIRONMENTAL, ECONOMIC AND LEGAL CONDITION OF THE PROPERTY AND (C) BUYER IS NOT RELYING UPON ANY STATEMENTS, REPRESENTATIONS OR WARRANTIES OF ANY KIND, AND IS ACQUIRING THE PROPERTY IN "AS IS, WHERE IS" CONDITION, EXCEPT AS SPECIFICALLY SET FORTH IN THIS AGREEMENT. WITHOUT LIMITING THE GENERALITY OF THE FOREGOING, BUYER ACKNOWLEDGES THAT ANY ESTIMATES OF FUTURE PROFITABILITY OF THE PROPERTY (OR ANY OF THEM) MADE BY BUYER, BASED ON INFORMATION (INCLUDING RESULTS OF PAST PERFORMANCE) PROVIDED TO BUYER BY SELLER ARE INHERENTLY UNCERTAIN AND ARE SUBJECT TO A VARIETY OF VARIABLES WHICH ARE DIFFICULT, IF NOT IMPOSSIBLE, TO PREDICT.

**13.2. Buyer's Representations.** To induce Seller to enter into this Agreement, Buyer hereby represents and warrants to Seller as of the date of this Agreement and the Closing Date, as follows:

(a) Buyer has been duly organized and is validly existing as a limited liability company in the State of Ohio, is in good standing in the state of its organization and it, or any assignee of Buyer that will acquire title to any of the Assets, will be qualified to do business, and will be in good standing, in the State of Ohio at the time of Closing. Buyer has the full right and authority to consummate or cause to be consummated the sale of the Assets, and to make or cause to be made the transfers and assignments contemplated herein. The person signing this Agreement on behalf of Buyer is authorized to do so.

(b) To the Knowledge of Buyer, there is no agreement to which Buyer is a party or which is binding upon Buyer which is in conflict with this Agreement.

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(c) There is no action or proceeding pending, or, to the Knowledge of Buyer, threatened against Buyer which would challenge or have a Material Adverse Effect upon Buyer's ability to perform its obligations under this Agreement.

**13.3. Survival of Representations and Warranties.** All representations, warranties, covenants and agreements made by each party in this Agreement, in any Exhibit attached hereto or in any list, certificate, document or written statement furnished or delivered by any such party pursuant hereto shall survive the Closing, and shall remain in full force notwithstanding any investigation conducted before or after the Closing, or the decision of any party to complete the Closing until September 1, 2014; provided, however, that: (i) the representations and warranties set forth in Sections 13.1(j), (k), (t), (u), (w), (x), (z), and (aa) shall survive until expiration of the relevant statute of limitations; (ii) the representations and warranties set forth in Sections 13.1(a), (b) and (c) shall survive indefinitely; and (iii) if at the expiration of the appropriate period any claim or assessment for indemnification has been asserted but not fully determined, or any audit or other proceeding with respect to any Tax matter has been initiated, such period will be extended as to such claim, assessment, audit or other proceeding until it is finally determined or concluded, and each party hereto shall be entitled to rely upon the representations and warranties of the other party set forth in this Agreement.

#### **ARTICLE XIV INTERIM OPERATIONS AND UNDERTAKINGS**

**14.1. Conduct of Business Pending Closing.** From the date of this Agreement until the Closing Date, Seller shall:

- (a) Maintain the Business and the Facilities in existence and in good standing and in material compliance with all Laws;
- (b) Maintain the general character of the Facilities and the Business and conduct the Business in the ordinary and usual manner;
- (c) Maintain all licenses and permits necessary for the ownership and operation of the Facilities in full force and effect, and will timely file all reports, statements, renewal applications and other filings, and will timely pay all fees and charges in connection therewith that are required to keep such permits in full force and effect;
- (d) Maintain the Property in good repair and condition subject to ordinary wear and tear;
- (e) Maintain in full force and effect substantially the same public liability and casualty insurance coverage and other Insurance Policies now in effect with respect to the Property and the Business;
- (f) Make all necessary repairs to, and replacement of, the Assets as are reasonably necessary for the continued operation of the Business and the Facilities;
- (g) Comply in all material respects with all Environmental Laws applicable to the Property;

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- (h) Continue to perform all Obligations under all Service Contracts;
- (i) Maintain adequate food and medical supplies and other Inventory at the Facilities as required by the State of Ohio and Federal laws, standards rules and regulations; and
- (j) Provide for and/or cure deficiencies and all violations which may be cited by the State of Ohio or any other Governmental Authority having jurisdiction over the Facilities.



**14.2. Prohibited Actions Pending Closing.** Unless otherwise expressly provided for herein or approved by Buyer in writing, from the date of this Agreement until the Closing Date, Seller shall not:

- (a) Induce, solicit or entice any Residents to transfer or discontinue any relationships with Seller prior to the Closing Date or Buyer after the Closing Date;
- (b) Remove any Personal Property necessary for the operation of the Business from the Facilities unless the same is replaced by property of substantially equal or greater value, or unless the removal is authorized pursuant to the provisions of this Agreement;
- (c) Interfere with or disrupt Buyer's relationship with any employee or Resident of Seller;
- (d) Accept any advance payment for more than thirty (30) days of any rent or Residents' occupancy fees under any Lease or occupancy agreement; or waive, reduce or forgive any rent or occupancy fees required to be paid under any occupancy agreement, or grant any lease or other concessions or free rent periods under any occupancy agreement;
- (e) After the expiration of the Study Period, renew, extend, terminate, modify or waive any term or condition of any of the Service Contracts or Resident occupancy agreement, nor, after the expiration of the Study Period, enter into any new Contracts relating to the Facilities or the Business, if such Contracts would survive the Closing;
- (f) Make any capital improvements to the Property in excess of \$10,000;
- (g) Make any commitments or representations to any applicable Governmental Authority, any adjoining or surrounding property owners, any civic association, any utility or any other person or entity that would in any manner be binding upon Buyer or upon the Property or the Business;
- (h) Sell or otherwise dispose of, or agree to sell or dispose of any of the Assets, except in the ordinary course of business as permitted by this Agreement; and
- (i) Take any action prior to the Closing Date which would breach any of the representations and warranties contained in this Agreement or otherwise take any action outside of the ordinary course of business of Seller.

**14.3. Notice.** From the date of this Agreement to the Closing Date, promptly (but in any event within two (2) Business Days) after Seller's discovery or receipt of notice of (A) any

default under any Contract, (B) any violation or non-compliance with any applicable Law, (C) any threatened or pending action by any Governmental Authority, (D) any claim made by any Governmental Authority or third-party relating to any Environmental Laws, or (E) any other matter or event that has or could have a Material Adverse Effect upon the Assets or the Business, Seller shall deliver to Buyer a copy of all non-privileged correspondence, notice or legal pleading in connection therewith, together with a certificate of the chief executive officer of Seller specifying the nature and period of the existence thereof and what actions Seller has taken and proposes to take with respect thereto.

**14.4. Access.** From the date of this Agreement until the Closing, Seller shall afford Buyer and its independent certified public accountants, counsel and other representatives, free and full access at all reasonable times to the properties, books and records of the Business and the right to consult with the officers, employees, accountants, counsel and other representatives of the Business in

order that Buyer may have full opportunity to make such investigations as it shall reasonably desire to make of the affairs of the Business; provided, however, that any such investigation, including, without limitation, pursuant to Article XV, shall not affect or otherwise diminish or obviate in any way any of the representations and warranties of Seller hereunder. Seller shall (and Seller shall ensure that its agents shall), upon reasonable notice from Buyer from time to time before Closing, permit Buyer or Buyer's agents to inspect at Seller's business office during regular business hours Seller's and Seller's agent's books and records for the Facilities.

## ARTICLE XV FEASIBILITY/DUE DILIGENCE

**15.1. Study Period.** Buyer, acting in its sole and absolute discretion, shall have a sixty (60) calendar day period after the date hereof (the "**Study Period**") which Study Period shall end on or about at 5:00 p.m., Eastern Standard Time on December 12, 2012, during which Buyer may make its own investigation of the Assets and the Business, including, but not limited to, examination of all books of account and records related to the business related to operating the Assets, and property-level diligence such as investigations with regard to zoning, building code and other legal requirements, obtaining such third party reports or studies as Buyer deems necessary, investigation of the status of the receivables, service contracts, Medicare/Medicaid provider agreements and compliance with all applicable regulatory requirements such as state or federal permits, licenses, and healthcare survey matters. Buyer shall have a continuing right of access, as described in Section 15.1(b), to conduct such studies. At any time prior to the expiration of the Study Period, Buyer may notify Seller in writing that Buyer has determined, for any or no reason, in its sole discretion that it will not complete the proposed acquisition of the Assets, and is thereby terminating this Agreement. If Buyer gives such notice to Seller, this Agreement shall automatically terminate and Seller shall instruct the Title Insurer to remit the Deposit, and all interest thereon, to Buyer. In the event Buyer terminates this Agreement on the basis of any of Seller's representations proving untrue, or because Seller refuses to cure due diligence deficiencies reasonably identified by Buyer, then (i) the Escrow Agent shall return the Deposit to Buyer together with accrued interest thereon, without any setoff or deduction, and neither party shall have any further obligation to the other hereunder except for Buyer's and Seller's obligations under Sections 15.1(c) (relating to damages to property) and 22.1 (relating to broker's commissions) which shall survive such termination. If Buyer does not deliver such

notice to Seller prior to the end of the Study Period, Buyer shall be deemed to have elected to proceed under this Agreement and to consummate the transaction contemplated hereunder.

**(a)** From and after the date of this Agreement, but as soon as possible, during the Study Period and provided that Buyer does not terminate this Agreement pursuant to Section 4.1, Seller shall provide to Buyer or make available to Buyer at the location(s) where such information is stored, any of the Property Information that is in the possession, custody or control of Seller or Seller's agents. Seller shall instruct its agents to cooperate with Buyer. In the event the Property Information is in the possession or control of the management company for the Property or its counsel, Seller shall direct such entities to provide the Property Information or make it available to Buyer. Seller shall provide to Buyer any further Property Information coming into Seller's possession or produced by Seller or its property manager after the initial delivery or availability, and shall continue to make available the same during the pendency of this Agreement.

**(b)** Buyer and its agents may at any time (after giving Seller reasonable written notice) enter onto the Property during the Study Period and, while thereon, make surveys, tests, investigations and appraisals, take measurements, test borings, other tests of surface and subsurface conditions and soil tests, make structural, mechanical, architectural, zoning, land use, market and engineering studies, and make any other inspections of the Property and other Assets deemed appropriate by Buyer, all at Buyer's expense.

(c) To expedite work on items requiring substantial lead time, Seller has provided Buyer with copies of each policy of title insurance covering the Assets and declaration pages and certificates of insurance coverage for each property/casualty and general liability/professional liability policy maintained by Seller in connection with the Business and the Assets.

(d) If Buyer exercises its rights under Section 15.1(b) to enter onto the Property, Buyer shall keep the Property free and clear of any liens or claims resulting therefrom, and defend, indemnify and hold harmless Seller against and from any liability or expense actually incurred by Seller for loss or damage to property and/or injuries to or death of Persons proximately caused by the actions of Buyer other than those caused in whole or in part as the result of acts or omissions by or on behalf of Seller. If Closing does not occur for any reason, Buyer shall restore any portion of the Property damaged by such exercise to its condition immediately before such exercise. If Buyer exercises this right of entry, it shall not unreasonably disturb any Resident in its use and enjoyment of the Facilities. The rights and obligations of the parties under this Section 15.1(c) shall survive Closing or any earlier termination of this Agreement.

**15.2. Special Assessments.** Seller shall provide Buyer, within ten (10) Business Days of receipt, but in no event later than Closing, copies of any notices Seller or its agents receive with respect to any special assessments or proposed increases in the valuation of the Property. After expiration of the Study Period, Buyer shall have the right to contest, in the name of Seller, any proposed increase in the assessment of the Property, provided that Buyer pays all costs and

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expenses in connection therewith. Buyer shall promptly advise Seller in writing prior to the filing of any contest and shall provide Seller copies of all relevant documents in connection with such contest. Seller shall cooperate with Buyer in connection with any such contest.

## ARTICLE XVI CONDITIONS PRECEDENT

**16.1. Conditions Precedent to Buyer's Obligations.** All obligations of Buyer under this Agreement are subject to the fulfillment or satisfaction in the sole discretion of Buyer, prior to or at the Closing, of each of the following conditions precedent (any of which may be waived in writing in whole or in part by Buyer):

(a) Seller's representations and warranties contained in this Agreement, the Exhibits attached hereto and any list, certificate, document or written statement specifically referred to herein or furnished by Seller to Buyer at the Closing shall be true on and as of the date of this Agreement and shall be true in all material respects on and as of the Closing Date with the same effect as though such representations and warranties were made on and as of the Closing Date.

(b) Seller shall have performed and complied in all material respects with all agreements and conditions contained in this Agreement that are required to be performed or complied with by it prior to or at the Closing.

(c) Buyer shall have received all the Seller deliveries described in Section 17.1. All Assumed Service Contracts shall have been assigned to Buyer and Seller shall have obtained all Consents required therefor.

(d) Buyer shall have received Bill of Sale, the Assignment and Assumption Agreement, and a certificate dated as of the Closing Date and signed by Seller certifying that the conditions specified in this Section 14.1 have been fulfilled and all such other documents required to be delivered by Seller hereunder.

(e) The Property shall not have been and shall not be threatened to be adversely affected as a result of fire, explosion, earthquake, disaster, accident, flood, drought, embargo, riot, civil disturbance, uprising, activity of the armed forces or act of

God or public enemy or any other event or circumstance that would have any Material Adverse Affect upon Seller. There shall not be pending or threatened any strike or any action by any Governmental Authority which would or could have a Material Adverse Effect on the Business.

(f) No suit, action, proceeding, or investigation shall have been instituted or threatened by any Governmental Authority, and no injunction shall have been issued and then outstanding, to restrain, prohibit or otherwise challenge the legality or validity of the transactions contemplated by this Agreement.

(g) Buyer shall have received any and all Consents and Licensure Approvals required or necessary to permit Buyer to purchase the Assets and to operate the Business and the Facility as presently being conducted and to participate (and be entitled to reimbursement) as a

provider in the Medicare and Medicaid Programs for the number of beds currently certified under such Programs.

(h) On the Closing Date, Buyer's title company shall be irrevocably committed to deliver to Buyer (or its permitted assignee) an ALTA Form 1970 Owner's Policy in the amount of not less than the Purchase Price insuring Buyer (or its permitted assignee) as the owner of the Property, and removing all exceptions other than the Permitted Liens, together with such endorsements as Buyer (or its permitted assignee) may require.

(i) There not having occurred any Material Adverse Change in: (A) the physical condition of the Assets (reasonable wear and tear excepted); (B) the economic condition of the Facilities (including any material reduction in the census of Residents prior to Closing); (C) the Assets' individual or aggregate financial performance between the expiration of the Study Period and Closing and (D) the environmental condition of the Property. As used herein, a "**Material Adverse Change**" in the physical condition of the Property or Assets (reasonable wear and tear excepted) or environmental condition of the Property or Assets shall mean a change in the physical condition of the Property or Assets (reasonable wear and tear excepted) or an environmental condition that either (i) costs in excess of Two Hundred Fifty Thousand Dollars (\$250,000.00) in the aggregate to cure, or (ii) costs less than Two Hundred Fifty Thousand Dollars (\$250,000.00) in the aggregate to cure, but has not been repaired or remediated by Seller prior to Closing. Seller shall have the right to extend the Closing for thirty (30) days to complete any required repair or remediation. In either event, if Buyer elects to close notwithstanding the failure of the condition in this Section 16.1(i) being satisfied, Seller shall escrow an amount to be mutually agreed upon to address such matters post-Closing, which amount shall be deposited with the Escrow Agent and held in accordance with the Escrow Agreement.

(j) Buyer shall have received a certificate in the form attached hereto as **Exhibit S**, executed by Seller, and such other evidence as Buyer may require that the Property is being acquired in a manner consistent with the Foreign Investment in Property Tax Act, as amended.

**16.2. Conditions Precedent to Seller' Obligations.** All obligations of Seller under this Agreement are subject to the fulfillment or satisfaction, prior to or at the Closing, of each of the following conditions precedent (any of which may be waived in writing in whole or in part by Seller):

(a) The representations and warranties of Buyer contained in this Agreement and in any list, certificate, document or written statement furnished by it to Seller in connection with the negotiation, execution or performance of this Agreement shall be true as of the date of execution of this Agreement and shall be true in all material respects at and as of the Closing Date with the same effect as though such representations and warranties were made on and as of the Closing Date.

(b) Buyer shall have performed and complied in all material respects with all agreements and conditions contained in this Agreement that are required to be performed or complied with by it prior to or at the Closing.

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(c) Seller shall have received all the Buyer deliveries described in Section 17.2.

(d) Seller shall have received the Cash Consideration balance of the Purchase Price, the Seller Note, the Pledge Agreement, the fully executed assumption of the Vandalia HUD Loan, the Assignment and Assumption Agreement signed by Buyer and a certificate dated the Closing Date and signed by Buyer certifying that the conditions specified in Section 16.2 have been fulfilled.

(e) No suit, action, proceeding or investigation shall have been instituted or threatened by any Governmental Authority, and no injunction shall have been issued and then be outstanding to restrain, prohibit or otherwise challenge the legality or validity of any of the transactions contemplated by this Agreement.

**16.3. Waiver of Conditions Precedent.** Except as otherwise provided herein, so long as a party is not in default under this Agreement, if any condition to that party's obligations to proceed with the Closing has not be satisfied as of the Closing Date, the party having the benefit of such condition may, in its sole discretion, terminate this Agreement by delivering written notice to the other party on or before the Closing Date, or elect to close, notwithstanding the non-satisfaction of such condition. If the party having the benefit of such condition elects to proceed with the Closing, notwithstanding the non-satisfaction of such condition, then, except as provided in Section 16.1(j), the non-satisfied condition shall be deemed to have been waived by the party having the benefit of said condition.

## ARTICLE XVII DELIVERIES AT CLOSING

**17.1. Seller's Deliveries.** At Closing, Seller shall deliver to Buyer:

- (a) the Deeds referenced in Section 7.1;
- (b) the Bills of Sale referenced in Section 7.2(c);
- (c) the Assignment and Assumption Agreement referenced in Section 7.2(e);
- (d) a schedule, certified by Seller, of rent or Resident occupancy payment arrearages as of Closing;
- (e) a closing statement setting forth the prorations and adjustments to be made pursuant to the provisions of this Agreement;
- (f) the FIRPTA Affidavit referenced in Section 16.1(k);
- (g) the owner's affidavit required by the Title Insurer in order to permit the Title Insurer to omit from Buyer's policy the exceptions for (i) parties in possession, (ii) mechanic's liens and (iii) any other standard exceptions;
- (h) all Records and Property Information;

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- (i) any and all keys, locks and safe combinations, training and instruction manuals in Seller' s possession, custody or control relating to the maintenance and operation of the Facilities;
- (j) the Resident Trust Funds;
- (k) letters addressed to the Residents and to parties under the Assumed Service Contracts, advising them of the transfer of the Facilities to Buyer, the letters to the Residents which shall be in form that meets with the reasonable satisfaction of Seller and Buyer;
- (l) evidence of the termination of such Service Contracts not assumed by Buyer;
- (m) evidence of the authority of the incumbency of any individuals to execute any instruments executed and delivered by Seller at Closing;
- (n) a certificate executed by Seller that all of the representations and warranties set forth in Section 13.1 of this Agreement are true and correct in all material respects of the Closing Date; and
- (o) such other documents as shall be required to consummate the transactions contemplated herein.

**17.2. Buyer' s Deliveries.** At Closing, Buyer shall deliver to Seller:

- (a) the Purchase Price;
- (b) the Seller Note and Pledge Agreement;
- (c) the Bills of Sale referenced in Section 17.1 (b);
- (d) the Assignment and Assumption Agreement referenced in Section 17.1(c);
- (e) the Assumption of the Vandalia HUD Loan;
- (f) a certificate executed by Buyer that all of the representations and warranties set forth in Section 13.2 of this Agreement are true and correct in all material respects of the Closing Date; and
- (g) such other documents as shall be required to consummate the transactions contemplated herein.

**ARTICLE XVIII  
CASUALTY AND CONDEMNATION**

**18.1. Casualty.** In the event that the Property is damaged or destroyed by any fire, flood or other casualty after the date of this Agreement or prior to Closing, Seller shall give Buyer prompt written notice of the damage. If the damage is not material, then Seller shall use its commercially reasonable efforts to commence repairs prior to the Closing. If such repairs

have not been completed prior to Closing, Buyer shall complete such repairs subsequent to Closing, at Seller' s expense. The parties shall agree on an amount to be escrowed prior to closing in connection with such repairs. If the casualty causes material damage, then Buyer may elect by notice to Seller within ten (10) days after Buyer is notified of such damage to either (A) proceed in the same manner

as in the case of damage that is not material, (B) to terminate this Agreement or (C) proceed to Closing, provided that Seller shall then assign to Buyer its rights to all insurance proceeds and any other claims or rights with respect to such damage, and any difference between such proceeds and the estimated cost of repair of the damage (as reasonably estimated by Seller's insurance company) shall be credited to Buyer at the Closing against the Purchase Price. If Buyer terminates this Agreement pursuant to this Section 18.1, then the Deposit and all interest thereon shall be returned to Buyer and neither party shall have any further obligation to each other except as provided in Sections 15.1(c) (relating to damages to property) and 22.1 (relating to broker's commissions). Damage as to any one or more occurrences is "material" if the cost to repair the damage, as reasonably estimated by Seller's engineer or expert, exceeds Two Hundred Fifty Thousand Dollars (\$250,000.00) in the aggregate. Buyer shall have the right to participate in the negotiations and settlement of any casualty-related claim in the event Buyer elects or is otherwise obligated to proceed with Closing.

**18.2. Condemnation.** If before Closing any of the Property is taken by condemnation or if any formal notice of a condemnation is issued to Seller, Seller shall promptly notify Buyer. If the condemnation is of a significant portion of the Property or would materially and adversely affect Buyer's ability to use and enjoy the Property, Buyer may, within fifteen (15) days after Seller notifies Buyer of any condemnation, terminate this Agreement by giving Seller written notice thereof, in which event the Deposit shall be returned to Buyer and the parties shall have no further liability to each other hereunder, except for Buyer's obligations under Sections 15.1(c) (relating to damages to property) and 22.1 (relating to broker's commissions) which shall survive such termination. If Seller gives notice to Buyer and Buyer does not terminate this Agreement, the Purchase Price shall not be reduced, but at Closing Seller shall pay to Buyer any award made for such condemnation which is received by Seller before Closing, and assign to Buyer all of Seller's interest in any award made for condemnation after Closing. Buyer shall have the right to participate in the negotiations and settlement of any condemnation claim in the event Buyer elects or is otherwise obligated to proceed with Closing.

## **ARTICLE XIX DEFAULT**

**19.1. Rights.** On any default, the non-defaulting party may, by notifying the defaulting party, either postpone Closing for as long as is necessary for such default to be cured, but not beyond the Outside Closing Date, or declare such default and exercise its rights under this Section.

**19.2. Buyer Default.** If Buyer is the defaulting party, Seller shall be entitled, as its sole and exclusive remedy on account of such default, to terminate this Agreement and receive payment of the Deposit as liquidated damages, the parties hereby agreeing that they have considered carefully the loss to Seller that would be a consequence of such default and that such sum is a reasonable estimate of that loss. Without limiting the foregoing, Seller shall under no

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circumstances have, and Seller hereby waives any right to seek against Buyer or any other person, damages or specific performance of any or all of Buyer's obligations hereunder. If Seller terminates this Agreement pursuant to this Section, this Agreement shall automatically terminate and the parties shall have no further obligation to each other, except for Buyer's and Seller's obligations under Sections 15.1(c) (relating to damages to property) and 22.1 (relating to broker's commissions), which shall survive such termination.

**19.3. Seller Default.** If Seller is the defaulting party, Buyer shall be entitled, after such declaration of default to (a) to seek specific performance and compel Seller to convey the Property as required hereunder, or (b) terminate this Agreement. If Buyer terminates this Agreement pursuant to this Section, Seller shall pay to Buyer the reasonable out-of-pocket costs it has incurred in connection with this Agreement and the attempted acquisition of the Property, including all third-party costs incurred before, during and after the Study Period as well as its reasonable attorneys' fees (including fees of both outside and in-house counsel). If the parties determine prior to Closing that Seller has breached a representation set forth in Section 13.1, the parties may close without prejudice to any remedies Buyer may have with respect to same.

**ARTICLE XX**  
**FURTHER ASSURANCES AND AGREEMENTS TO MODIFY**

**20.1. Further Assurances and Agreements to Modify Transaction Structure.** From and after the Closing, Seller, on the one hand, and Buyer, on the other hand, agree to execute and deliver such further documents and instruments and to do such other acts and things (including the making of filings), as Buyer or Seller, as the case may be, may reasonably request in order to effectuate the transactions contemplated by this Agreement. In the event any party shall be involved in litigation, threatened litigation or government inquires with respect to a matter involving Seller, the other parties shall also make available to such first party, at reasonable times and subject to the reasonable requirements of their or its own business, such of their or its personnel as may have information relevant to the matters. Following the Closing, the parties will cooperate with each other in connection with Tax audits and in the defense of any legal proceedings, consistent with the other provisions for defense of claims provided in Sections 21.4 or 21.5 of this Agreement, and to facilitate the collection of any accounts receivable, to the extent such cooperation does not cause unreasonable expense, unless such expense is borne by the requesting party.

**20.2. Access to the Records.** From and after the Closing Date, Buyer shall allow Seller and its agents and representatives to have reasonable access to (upon reasonable prior notice and during normal business hours), and to make copies of the Records, to the extent reasonably necessary to enable Seller to among other things investigate and defend malpractice, employee or other claims, to support medical review requests from Medicare, to support Medicare claims appeals, to file or defend cost reports and tax returns, to complete/revise, as needed, any patient assessments which may be required for Seller to seek reimbursement for services rendered prior to the Closing Date, to verify accounts receivable collections due Seller, to file exceptions to the Medicare routine cost limits for the cost reporting periods prior to the Closing Date and to enable Seller to complete, in accordance with Seller's policies and procedures, any and all post Closing Date accounting, reconciliation and closing procedures, including, but not limited to, a month end close out of all accounts, including but not limited to

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accounts payable and Medicare billing. Seller agrees not to use or disclose any of the information obtained from Buyer except solely for the purposes described herein and further agrees to maintain this information confidential. Likewise, from and after the Closing Date, Seller shall allow Buyer and its agents reasonable access to the Records, to the extent Buyer reasonably requires such access in connection with, without limitation, accounting, billing, tax filings or securities filings, Medicare and/or Medicaid filings and appeals. Buyer agrees not to use or disclose any of the information obtained from Seller except solely for the purposes described herein and further agrees to maintain this information as confidential.

**ARTICLE XXI**  
**INDEMNIFICATION**

**21.1. Indemnification by Seller.** Seller shall indemnify, defend and hold Buyer and each of the directors, officers, shareholders, agents and employees of Buyer and any Affiliate thereof harmless at all times from and after the Closing Date against and in respect of any and all damages, losses, liabilities, taxes and deficiencies and penalties and interest thereon and costs and expenses (including attorneys fees and costs) (collectively, "**Damages**") resulting from:

- (a) any misrepresentation or breach of any representation or warranty or non-fulfillment of any covenant or provision on the part of Seller under this Agreement;
- (b) any Obligations of Seller or any Obligation with respect to the Assets or the Business, except for Obligations arising on or after the Closing Date or that are expressly assumed by Buyer hereunder;
- (c) any claim or litigation relating to the Excluded Assets;



(d) any claim or litigation relating to any of Seller' s Obligations;

(e) any claims or litigation relating to Seller now pending or threatened or which may hereafter be brought against Buyer based upon events occurring prior to the Closing Date; and

(f) any and all actions, suits, proceedings, claims, demands, assessments, judgment, costs (including reasonable attorneys fees), losses, liabilities and reasonable legal fees and other expenses incurred by Buyer incident to any of the foregoing.

**21.2. Indemnification by Buyer.** Buyer shall indemnify, defend and hold Seller and each of the directors, officers, shareholders, agents and employees of Seller and any Affiliates thereof harmless at all times from and after the Closing Date against and in respect of any and all Damages resulting from:

(a) any misrepresentation or breach of any representation or warranty or non-fulfillment of any covenant or provision on the part of Buyer under this Agreement;

(b) any Obligations expressly assumed by Buyer hereunder;

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(c) any claims or litigation relating to Buyer which may hereafter be brought against Seller, based upon events occurring on or after the Closing Date and not directly caused by Seller or relating to a matter for which Seller provides indemnification under Section 21.1; and

(d) any and all actions, suits, proceedings, claims, demands, assessments, judgment, costs (including reasonable attorneys fees), losses, liabilities and reasonable legal fees and other expenses incurred by Seller incident to any of the foregoing.

**21.3. Period of Indemnity.** The aforesaid indemnities under Sections 21.1 and 21.2, shall remain in full force and effect: (a) as they relate to a third-party claim against the indemnified party for a period equal to the applicable statute of limitation for such claim; and (b) as they relate to breaches of representations, warranties or covenants made by Indemnifying Party for the period provided in Section 13.3 provided, however, if at the expiration of the appropriate period any claim or assessment for indemnification has been asserted but not fully determined, or any audit or other proceeding with respect to any tax matter has been initiated, such period will be extended as to such claim, assessment, audit or other proceeding until it is finally determined or concluded.

**21.4. Notice to the Indemnifying Party.** Within thirty (30) days after the assertion of any claim by a third-party or occurrence of any event which may give rise to a claim for indemnification from a party (the "***Indemnifying Party***") under this Article XXI, the other party (the "***Indemnified Party***") shall notify the Indemnifying Party in writing of such claim and, with respect to claims by third parties, advise the Indemnifying Party whether the Indemnified Party intends to contest same; provided, however, failure to provide such notice shall not in any way serve to waive or diminish the indemnification rights of the Indemnified Party. Notwithstanding the foregoing, any inadvertent delay in notifying the Indemnifying Party shall in no case prejudice the rights of the Indemnified Party under this Agreement except to the extent the Indemnifying Party shall actually be prejudiced by such failure.

**21.5. Rights of Parties to Settle or Defend.** If the Indemnified Party determines not to contest such claim, the Indemnifying Party shall have the right, at its own expense, to contest and defend against such claim. If the Indemnified Party determines to contest such claim, the Indemnifying Party shall have the right to be represented, at its own expense by its own counsel and accountants, their participation to be subject to the reasonable direction of the Indemnified Party. In either case, the Indemnified Party shall make available to the Indemnifying Party and its attorneys and accountants, at all reasonable times during normal business hours, all books, records, and other documents in its possession relating to such claim. The party contesting any such claim shall be

furnished all reasonable assistance in connection therewith by the other party. If the Indemnifying Party fails to undertake the defense of, or settle or pay, any such third-party claim within ten (10) days after the Indemnified Party has given written notice to the Indemnifying Party advising that the Indemnified Party does not intend to contest such claim, or the Indemnifying Party, after having received such notification from the Indemnified Party, fails forthwith to defend, settle or pay such claim, then the Indemnified Party may take any and all necessary action to dispose of such claim, including, without limitation, the settlement or full payment thereof upon such terms as it shall deem appropriate, in its sole discretion, subject to the following with respect to any proposed settlement thereof.

**21.6. Settlement Proposals.** In the event the Indemnified Party desires to settle any such third-party claim (whether or not contested by the Indemnifying Party), the Indemnified Party shall advise the Indemnifying Party of the amount it proposes to pay in settlement thereof and the terms of the settlement thereof (the “**Proposed Settlement**”). If such Proposed Settlement is unsatisfactory to the Indemnifying Party, it shall have the right, at its own expense, to contest such claim by giving written notice of such election to the Indemnified Party within ten (10) days after the Indemnifying Party has been advised of the Proposed Settlement. If the Indemnifying Party does not deliver such written notice within ten (10) days after the Indemnifying Party has been advised of the Proposed Settlement, the Indemnified Party may offer the Proposed Settlement to the third-party making such claim. If the Proposed Settlement is not accepted by the party making such claim, any new Proposed Settlement figure which the Indemnified Party may wish to present to the party making such claim shall first be presented to the Indemnifying Party who shall have the right, subject to the conditions hereinabove set forth in this Section 21.6, to contest such claim. In all such events, the Indemnifying Party shall indemnify the Indemnified Party and hold it harmless against and from any and all costs of defense, payment or settlement, including reasonable attorneys’ fees incurred in connection therewith.

**21.7. Reimbursement.** At the time that the Indemnified Party shall suffer a loss because of a breach of any warranty, representation or covenant by the Indemnifying Party or at the time the amount of any liability on the part of the Indemnifying Party under this Article XXI is determined (which in the case of payments to third persons shall be the earlier of: (a) the date of such payments; or (b) the date that a court of competent jurisdiction shall enter a final judgment, order or decree (after exhaustion of appeal rights establishing such liability), the Indemnifying Party shall forthwith, upon notice from the Indemnified Party, pay to the Indemnified Party, the amount of the indemnity claim. If such amount is not paid forthwith, then the Indemnified Party may, at its option, take legal action against the Indemnifying Party for reimbursement in the amount of its indemnity claim.

**21.8. Limitations on Indemnification Obligations of Seller.** Seller’ s indemnification obligations pursuant to this Article XXI are subject to the following conditions precedent and limitations:

(a) Buyer shall not be entitled to recover under Section 21.1 until the aggregate amount which Buyer would recover under Section 21.1, but for this Section 21.8, exceeds One Hundred Thousand Dollars (\$100,000.00) in the aggregate, in which event, subject to the further limitations of this Section, Buyer shall be entitled to recovery for all Damages up to a maximum amount of Three Million Six Hundred Thousand Dollars (\$3,600,000.00) including the first One Hundred Thousand Dollars (\$100,000.00). Buyer shall be entitled to offset such Damages up to the maximum amount set forth in the preceding sentence against amounts otherwise due Seller under the Seller Note. Notwithstanding the foregoing, there shall be no maximum amount for any Damages incurred by Buyer as a result of Seller’ s fraud, bad faith or intentional misconduct.

(b) For purposes of Section 21.8, in computing any individual or aggregate amounts of Damages to which Buyer is entitled, the amount of such Damages shall be an

amount: (i) net of any tax benefit actually recognized by Buyer; and (ii) net of any cash insurance proceeds actually received by Buyer with respect thereto.

## ARTICLE XXII COMMISSIONS

**22.1. Commissions.** Seller represents that, in connection with the sale of the Property, it has not used the services of any broker. Buyer represents that, in connection with the sale of the Property, it has not used the services of any broker. Subject to the foregoing, each party represents to the other that, in connection with such sale, the party so representing has not dealt with any other real estate broker, agent or finder, and there is no commission or other compensation due on account thereof. Each party shall indemnify and hold harmless the other against and from any inaccuracy in such party's representation. The rights and obligations of the parties under this Section shall survive Closing or any termination of this Agreement before Closing. Each party shall be responsible for the fees of their respective advisors and consultants.

## ARTICLE XXIII MISCELLANEOUS

**23.1. Effectiveness.** This Agreement shall become effective on its execution and delivery by each party.

**23.2. Complete Understanding.** This Agreement represents the complete understanding between the parties as to the sale of the Property, and supersedes all prior written or verbal negotiations or agreements as to the Assets, the condition thereof or any other matter whatsoever, made by any broker, agent, employee or other person representing or purporting to represent either party.

**23.3. Waiver.** No party shall be deemed to have waived the exercise of any right which it holds under this Agreement unless such waiver is made expressly and in writing. No delay or omission by any party in exercising any right shall be deemed a waiver of its future exercise. No waiver made as to any instance involving the exercise of any right shall be deemed a waiver as to any other instance, or any other right.

**23.4. Applicable Law.** This Agreement shall be given effect and construed by application of the law of the State of Ohio. Any action arising hereunder shall be brought in the courts of Ohio, except that if it is to be brought in a United States District Court, it shall be brought in the United States District Court for the Southern District of Ohio.

**23.5. Notices.** Any notice to be provided hereunder to a party or the Title Insurer, as Escrow Agent, shall be in writing, and shall be deemed to have been provided forty-eight (48) hours after being sent as certified or registered mail in the United States mails, postage prepaid, return receipt requested, or the next Business Day after having been deposited with a national courier service, or on having been sent by immediate electronic communication, in each case if receipt is acknowledged or confirmed or delivery is first refused, to the persons and addresses set forth below, as such address may be changed from time to time by notice to the other party.

If intended for Seller to:

AdCare Health Systems, Inc.  
Two Buckhead Plaza  
3050 Peachtree Road NW, Suite 355  
Atlanta, GA 30305  
Attention: Boyd P. Gentry

with a copy to:

Holt Ney Zatcoff & Wasserman, LLP  
100 Galleria Parkway, Suite 1800  
Atlanta, Georgia 30339  
Attention: Gregory P. Youra, Esq.

If intended for Buyer to:

CHP Acquisition Company LLC  
Easton Town Center  
4100 Regent St., Suite F  
Columbus, Ohio 43219  
Attention: Roger C. Vincent, President

with a copy to:

Roetzel & Andress, LPA  
155 East Broad Street, 12<sup>th</sup> Floor  
Columbus, Ohio 43215  
Attention: Jeffrey Fromson, Esq.

If intended for the Escrow Agent, to:

Hummel Title Agency  
2154 East Main Street, Suite 301  
Columbus, Ohio 43209  
Attention: Jeffrey D. Meyer, Esq.

**23.6. Waiver of Jury Trial. THE PARTIES HEREBY IRREVOCABLY WAIVE ANY AND ALL RIGHT TO TRIAL BY JURY IN ANY LEGAL PROCEEDING ARISING OUT OF OR RELATING TO THIS AGREEMENT OR THE TRANSACTIONS CONTEMPLATED HEREBY.**

**23.7. Construction.** All references made in the neuter, masculine or feminine gender shall be deemed to have been made in all such genders; and in the singular or plural number shall be deemed to have been made, respectively, in the plural or singular number as well.

**23.8. Exhibits.** Each writing or plat referred to as being attached as an Exhibit is hereby made a part of this Agreement.

**23.9. Severability.** No determination that any provision of this Agreement is invalid or unenforceable in any instance shall affect the validity or enforceability of any other such provision, or that provision in any circumstance not controlled by such determination. Each provision shall be valid and enforceable to the fullest extent allowed by, and shall be construed wherever possible as being consistent with, applicable law.

**23.10. Time of essence.** Time shall be of the essence of this Agreement.

23.11. **Counterparts.** This Agreement may be signed in counterparts, all of which when taken together shall constitute the one and same original.

23.12. **Facsimile Signatures.** The exchange of copies of this Agreement and of signature pages by facsimile transmission shall constitute effective execution and delivery of this Agreement as to the parties and may be used in lieu of the original Agreement for all purposes. Signatures of the parties transmitted by facsimile shall be deemed to be their original signatures for all purposes.

23.13. **Construction.** Each party hereto hereby acknowledges that all parties hereto participated equally in the negotiation and drafting of this Agreement and that, accordingly, no court construing this Agreement shall construe it more stringently against one party than against the other.

23.14. **Headings.** The headings are used herein for convenience of reference only, and shall not be deemed to vary the content of this Agreement.

23.15. **Attorneys' Fees.** If either party hereto institutes any proceeding, claim or action, at law or in equity, in connection with or arising out of the terms, conditions, covenants and agreements contained in this Agreement, the non-prevailing party in any such action, claim or proceeding shall reimburse the prevailing party for reasonable attorneys' fees, costs and other expenses incurred in connection with such proceeding or action.

23.16. **Exclusivity.** Until and unless this Agreement is terminated by Buyer, Seller will not solicit any offers or proposals, or enter into letters of intent, negotiations or contracts with any third-party with respect to a transaction relating to the sale, transfer, conveyance, merger or any other transaction of similar import with respect to Seller or any of the Assets.

23.17. **Assignment.** Buyer shall not assign any of its rights under this Agreement without first obtaining the Seller's written consent. Notwithstanding, if Buyer provides Seller with written notice at least four (4) Business Days prior to Closing, Buyer may assign this Agreement to any entity controlled by Buyer as evidenced by documentation reasonably acceptable to Seller. Subject to the foregoing provisions of this subsection, this Agreement shall be binding on and inure to the benefit of the parties and their respective successors and assigns in interest hereunder.

*[Signature Page on Following Page]*

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*[Remainder of page intentionally left blank]*

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IN WITNESS WHEREOF, each party has executed this Agreement by its duly authorized representatives, the day and year first above written.

**BUYER:**

**CHP ACQUISITION COMPANY LLC,**  
an Ohio limited liability Company

By: /s/ Roger C. Vincent

Name: Roger C. Vincent

Title: President

**SELLER:**

**ADCARE HEALTH SYSTEMS, INC,**  
an Ohio Corporation

By: /s/ Boyd P. Gentry

Name: Boyd P. Gentry

Title: Chief Executive Officer

**HEARTH & HOME OF OHIO, INC.,**  
an Ohio corporation

By: /s/ Martin D. Brew

Name: Martin D. Brew

Title: CFO

**NEW LINCOLN LTD., LP,**  
an Ohio limited partnership

By: /s/ Martin D. Brew

Its General Partner

By: /s/ Martin D. Brew

Name: Martin D. Brew

Title: CFO

**COMMUNITY' S HEARTH & HOME, LTD.,**  
an Ohio

By: /s/ Martin D. Brew

Name: Martin D. Brew

Title: CFO

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**COMMUNITY' S HEARTH & HOME**  
**AT EL CAMINO,**  
an Ohio

By: /s/ Martin D. Brew

Name: Martin D. Brew

Title: CFO

**LINCOLN LODGE RETIREMENT RESIDENCE,**  
an Ohio

By: /s/ Martin D. Brew  
Name: Martin D. Brew  
Title: CFO

**HEARTH & HOME OF VAN WERT,**  
an Ohio

By: /s/ Martin D. Brew  
Name: Martin D. Brew  
Title: CFO

**COMMUNITY' S HEARTH AT VANDALIA,**  
an Ohio

By: /s/ Martin D. Brew  
Name: Martin D. Brew  
Title: CFO

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**ASSIGNMENT OF PURCHASE AND SALE AGREEMENT**

FOR VALUE RECEIVED, ADCARE PROPERTY HOLDINGS, LLC, a Georgia limited liability company (“Assignor”) hereby transfers and assigns unto EDWARDS REDEEMER PROPERTY HOLDINGS, LLC and ER NURSING, LLC, each a Georgia limited liability company (collectively “Assignee”), all of Assignor’s right, title and interest in and to that certain Purchase and Sale Agreement effective as of May 5, 2011, as the same has been amended and assigned through the date hereof (the “Agreement”), relating to the Facility (as defined in the Agreement) commonly known as “Edwards Redeemer Nursing Center” and located at 1530 Northeast Grand Blvd., Oklahoma City, Oklahoma. Assignee hereby assumes all obligations of Assignor under the Agreement with respect to such Facility. Assignor and Assignee acknowledge that the Purchase Price for the Facility shall be \$2,100,000.00.

IN WITNESS WHEREOF, Assignor and Assignee have caused this Assignment of Purchase and Sale Agreement to be duly executed and delivered as of the 12th day of October, 2012.

**ASSIGNOR:**

ADCARE PROPERTY HOLDINGS, LLC

By: /s/ Boyd P. Gentry  
Boyd P. Gentry, Manager

**ASSIGNEE:**

EDWARDS REDEEMER PROPERTY HOLDINGS, LLC

By: /s/ Boyd P. Gentry  
Boyd P. Gentry, Manager

ER NURSING, LLC

By: /s/ Boyd P. Gentry  
Boyd P. Gentry, Manager





**ASSIGNMENT OF PURCHASE AND SALE AGREEMENT**

FOR VALUE RECEIVED, ADCARE PROPERTY HOLDINGS, LLC, a Georgia limited liability company (“**Assignor**”) hereby transfers and assigns unto WP OKLAHOMA NURSING, LLC, a Georgia limited liability company (“**Assignee**”), all of Assignor’s right, title and interest in and to that certain Purchase and Sale Agreement effective as of May 5, 2011, as the same has been amended and assigned through the date hereof (the “**Agreement**”), relating to the Facility (as defined in the Agreement) commonly known as “Whispering Pines Nursing Center” and located at 501 East Robinson, Norman, Oklahoma. Assignee hereby assumes all obligations of Assignor under the Agreement with respect to such Facility.

IN WITNESS WHEREOF, Assignor and Assignee have caused this Assignment of Purchase and Sale Agreement to be duly executed and delivered as of the 12th day of October, 2012.

**ASSIGNOR:**

**ASSIGNEE:**

ADCARE PROPERTY HOLDINGS, LLC

WP OKLAHOMA NURSING, LLC

By: /s/ Boyd P. Gentry  
Boyd P. Gentry, Manager

By: /s/ Christopher F. Brogdon  
Christopher F. Brogdon, Manager

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**MEMBERSHIP INTEREST POWER**

For value received, AdCare Property Holdings, LLC (“Transferor”) is the owner of 100% of the issued and outstanding membership units of Edwards Redeemer Property Holdings, LLC, a Georgia limited liability company (the “Company”) does hereby assign and transfer to Christopher F. Brogdon, an individual resident of the State of Georgia, any and all of the right, title and interest that Transferor has or may have in and to its 100% interest in the Company (the “Transferred Interests”). Transferor hereby irrevocably constitutes and appoints \_\_\_\_\_ or any other duly authorized officer or attorney of the Company to transfer such right, title and interest of the Transferred Interests on the books of the Company with full power of substitution in the premises.

Transferor represents and warrants that: (i) Transferor is the owners of the Transferred Interests free and clear of any and all liens, pledges, encumbrances, charges, assessments, agreements, options or claims (collectively, “Adverse Interests”); (ii) Transferor has the full right, power and authority to transfer, convey, assign and deliver the Transferred Interests; (iii) the Transferred Interests are hereby transferred free and clear of all Adverse Interests; and (iv) the Transferred Interests constitute, 100% of all membership interests in the Company.

*[Signatures on next page]*

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Executed as of the 12th day of October, 2012.

**TRANSFEROR:**

**ADCARE PROPERTY HOLDINGS, LLC**

By: /s/ Boyd P. Gentry

Boyd P. Gentry, Manager

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**FIRST AMENDMENT TO PURCHASE AND SALE AGREEMENT**

This First Amendment to Purchase and Sale Agreement (this "Assignment and Amendment") is made and entered into as of October 31, 2012 (the "Effective Date") by and between **WINYAH NURSING HOME, LLC** ("Seller") and **ADCARE PROPERTY HOLDINGS, LLC**, an Ohio limited liability company or its permitted assigns ("Purchaser").

**WITNESSETH:**

**WHEREAS**, Seller (incorrectly named as Winyah Nursing Home, Inc.) and Purchaser are parties to that certain Purchase and Sale Agreement dated as of August 9, 2012 (the "Agreement"); and

**WHEREAS**, Purchaser and Seller desire to amend the Agreement to extend the Closing Date on the terms hereinafter set forth.

In consideration of the mutual covenants and agreements contained herein, and other good and valuable consideration paid by Purchaser to Seller, the receipt and sufficiency of which are hereby acknowledged, Seller and Purchaser agree as follows:

1. **Capitalized Terms**. Capitalized but undefined terms used in this Amendment shall have the meanings set forth in the Agreement.
2. **Seller**. Seller hereby confirms that the original Agreement erroneously identified "Winyah Nursing Home, Inc." as the seller and owner of the Facility. Seller confirms that it is the current owner of the Facility. Accordingly, from and after the date hereof, the defined term "Seller" as set forth in the Agreement is amended to be "Winyah Nursing Home, LLC."
3. **Closing Date**. The Agreement is hereby amended to provide that the Closing Date is extended to and shall be December 27, 2012.
4. **Extension Fee**. Notwithstanding the provisions of Section 2.2 of the Agreement, in exchange for Seller's agreement to extend the Closing Date as set forth herein, Purchaser shall deliver \$50,000.00 (the "Extension Fee") to Seller in accordance with the wire instructions attached hereto as **Exhibit A**. Notwithstanding the delivery of the Extension Fee to Seller in accordance with this Amendment, the parties acknowledge and agree that the Extension Fee shall be a credit against the Cash Consideration portion of the Purchase Price (in addition to the existing \$50,000 Deposit currently being held by the Escrow Agent) at Closing (or in the event of a Seller default resulting in the failure of the transaction contemplated by the Agreement to close, returned to Purchaser).
5. **Ratification**. Except to the extent amended hereby, Purchaser and Seller ratify and confirm that all other terms and conditions of the Agreement remain in full force and effect.
6. **Counterparts**. This Amendment may be executed in any number of counterparts, each of which shall be deemed an original, and all of which shall be taken to be one and the same Amendment, for the same effect as if all parties hereto had signed the same signature page, and an electronic PDF or facsimile copy of an executed counterpart shall constitute the same as delivery of the original of such executed counterpart. Any signature page of this Amendment (whether original or facsimile) may be detached from any counterpart of this Amendment (whether original or facsimile) without impairing the legal effect of any signatures thereof and may be attached to another counterpart of this Amendment (whether original, PDF or facsimile) identical in form hereto but having attached to it one or more additional signature pages (whether original, PDF or facsimile).

IN WITNESS WHEREOF, each party has caused this instrument to be executed as of the date set forth hereinabove.

**SELLER:**

**WINYAH NURSING HOME, LLC**, a South Carolina limited liability company

By: /s/ Martha F. Tatum  
Martha F. Tatum, Chief Executive Officer

**PURCHASER:**

**ADCARE PROPERTY HOLDINGS, LLC**, an Ohio limited liability company

By: /s/ Boyd P. Gentry  
Boyd P. Gentry, Manager

**LOAN AGREEMENT**

**THIS LOAN AGREEMENT** (this “**Agreement**”) is made as of August 17, 2012, by and among **CSCC PROPERTY HOLDINGS, LLC**, a Georgia limited liability company (“**Owner**”) and **CSCC NURSING, LLC**, a Georgia limited liability company (“**Operator**”) and together with the Owner and with their respective successors and assigns, being collectively referred to herein as, the “**Borrowers,**” and each, a “**Borrower**”), and **CONTEMPORARY HEALTHCARE SENIOR LIEN FUND I, L.P.**, a Delaware limited partnership (together with its successors and assigns, the “**Lender**”).

**RECITALS**

**WHEREAS**, Borrowers have requested that Lender make a loan to Borrowers in the principal sum of \$5,000,000.

**WHEREAS**, Lender has agreed to make such loan on the terms and conditions hereinafter set forth.

**AGREEMENT**

**NOW, THEREFORE**, it is hereby agreed as follows:

**ARTICLE I.**

**DEFINITIONS, ACCOUNTING PRINCIPLES, UCC TERMS.**

1.1 **Definitions.** As used in this Agreement, the following terms shall have the following meanings unless the context hereof shall otherwise indicate:

“**Accounts**” means all accounts arising from the business of each of the Borrowers, and all rights to payment from patients, residents, private insurers, and others arising from the business of each of the Borrowers, including rights to payment pursuant to Reimbursement Contracts, including rights to payment from Medicare and Medicaid programs or similar state or federal programs, boards, bureaus or agencies. “Accounts” shall also include the proceeds thereof (whether cash or noncash, moveable or immoveable, tangible or intangible) received from the sale, exchange, transfer, collection or other disposition or substitution thereof and any amounts deposited with Lender pursuant to Sections 4.13, Section 4.14 or Section 4.31 and any reserve account required hereunder.

“**Affiliate**” shall mean, with respect to any Person, (a) each Person that controls, is controlled by or is under common control with such Person, (b) each Person that, directly or indirectly, owns or controls, whether beneficially or as a trustee, guardian or other fiduciary, any of the Stock of such Person, and (c) each of such Person’s officers, directors, members, joint venturers and partners.

“**Anti Terrorism Laws**” shall mean any Laws relating to terrorism or money laundering, including Executive Order No. 13224 (effective September 24, 2001), the United States Patriot Act, the laws comprising or implementing the Bank Secrecy Act, and the laws administered by OFAC.

“**Application Fee**” shall have the meaning set forth in Section 2.9.

“**AR Lender**” shall mean Contemporary Healthcare Fund I, L.P.

“**AR Loan**” shall mean all loan obligations, the AR Loan Agreement and the other AR Loan Documents.

“**AR Loan Agreement**” shall mean that certain Loan Agreement dated the date hereof, by and between AR Lender and the Borrowers, as such agreement may be amended.

“**AR Loan Documents**” shall mean the AR Loan Agreement and all documents, instruments and agreements executed in connection with such AR Loan Agreement.

“**Assignee**” shall have the meaning set forth in Section 7.9.

“**Assignment and Pledge Agreement**” shall have the meaning set forth in Section 2.2(b)(iii).

“**Assignment of Acquisition Contracts and Documents**” shall have the meaning set forth in Section 2.2(b)(xi).

“**Assignment of Leases and Rents**” shall have the meaning set forth in Section 2.2(b)(iv).

“**Assumed Management Fees**” shall mean five percent (5%) of total revenues net of contractual adjustments.

“**Bankruptcy Default**” means an Event of Default pursuant to Section 6.1(e) or Section 6.1(f) of this Agreement.

“**Borrower**” or “**Borrowers**” has the meaning set forth in the introductory paragraph of this Agreement.

“**Borrower Environmental Indemnity Agreement**” shall have the meaning set forth in Section 2.2(c)(v) of this Agreement.

“**Business Day**” means a day, other than Saturday or Sunday and legal holidays, when the Lender or national banks in New Jersey are open for business.

“**Capital Improvements Escrow and Security Agreement**” shall have the meaning set forth in Section 2.2(b)(v).

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“**Capital Improvements Reserve Fund**” shall have the meaning set forth in Section 4.16.

“**Capital Improvements Reserve Requirement**” shall be an amount equal to \$600 per licensed bed per year, which amount shall be payable as provided for in the Capital Improvements Escrow and Security Agreement.

“**Capitalized Interest Reserve Account**” shall have the meaning given in Section 4.30.

“**Certificate of Occupancy**” shall mean a final and unconditional Certificate of Occupancy (or its equivalent) permitting the lawful occupancy of the Facility from the appropriate Governmental Authority having jurisdiction over the Property.

“**Change in Control**” shall mean (i) a merger or consolidation of either of the Borrowers where any of the Borrowers, as the case may be, is not the surviving entity, or if it is the surviving entity, such transaction resulted in a change in its governing body, such that a majority of the individuals who comprise the governing body immediately prior to such transaction (or series of related transactions) do not constitute a majority of the governing body after such transaction, (or if such individuals continue to constitute a majority of the governing body the transaction vested in another person(s) and/or entity(ies) any super-majority voting rights); (b) a cumulative change in the ownership of a Borrower exceeding, on a fully diluted basis and on an as if converted basis, twenty five

percent (25%) of the equity interest issued and outstanding at the Closing Date; (c) the termination of employment or any material change in the duties and responsibilities of Christopher F. Brogdon or the material failure to perform his duties, as determined by the Lender; or (d) any change of the "Manager," as defined in each of the Borrower's operating agreements, as designated as of the date hereof.

"**Closing Date**" shall have the meaning set forth in Section 2.1(b).

"**Closing Fee**" shall have the meaning set forth in Section 2.9.

"**Closing Statement**" means the Lender's Closing Statement dated the date hereof, executed by the Borrowers and the Lender.

"**Collateral**" means, collectively, all collateral assigned, hypothecated, pledged, or otherwise granted to Lender under the Loan Documents all whether now owned or hereafter acquired, including replacements, additions, accessions, substitutions, and products thereof and thereto, and all other property which is or hereafter may become subject to a Lien in favor of Lender as security for any of the Loan Obligations.

"**Contemporary Debt**" shall mean any indebtedness now or hereafter owing to Lender or any Affiliate of Lender by Borrowers (or any of them) or any Affiliate of a Borrower, whether primary or secondary, fixed or contingent, individually or jointly with others, including, but not limited to debt owing to Lender or any Affiliate of Lender that is guaranteed by any Guarantor. Such Contemporary Debt shall include the AR Loan.

"**Control Agreement**" shall have the meaning set forth in Section 2.2(b)(x).

"**Corporate Guarantor**" means, jointly and severally, AdCare Oklahoma Management, LLC, a Georgia limited liability company, and AdCare Health Systems, Inc., an Ohio corporation.

"**Current Assets**" shall have the meaning set forth in Section 4.13(a).

"**Current Liabilities**" shall have the meaning set forth in Section 4.13(a).

"**Current Ratio**" shall have the meaning set forth in Section 4.13(a).

"**Debt Service Coverage Ratio**" means a ratio of the first number to the second number in which:

(i) the first number is the sum of:

(a) net income from operations of the Facility (without deduction for actual management fees paid in connection with the operation of the Facility) calculated based upon the applicable period,

(b) interest expense with respect to the Facility, to the extent deducted in determining net income,

(c) lease expense pursuant to a lease of the Facility from one Borrower to another, if any, to the extent deducted in determining net income,

(d) non-cash expenses or allowances for depreciation and amortization of the Facility for such period to the extent deducted in determining net income, and

(e) any monies in the Capitalized Interest Reserve Account,

less:

(a) non- operating or extraordinary income,

(b) Assumed Management Fees,

(c) required Capital Improvements Reserve Fund deposits for such period, and

(d) unfinanced capital expenditures in excess of the year-to-date sum of Capital Improvements Reserve Fund deposits,

(ii) and the second number is the sum of:

(a) the total Installment Payments, as defined in the Note, due for such period, and

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(b) other secured and unsecured debt payments (principal and interest) for such period relating to the Facility, including, without limitation, payments with respect to any Contemporary Debt relating to the Facility, provided, however, that such debt shall not include the AR Loan, unless provided for herein.

In calculating “net income,” any extraordinary income shall be excluded.

“**Default**” means the occurrence or existence of any event which, but for the giving of notice or expiration of time or both, would constitute an Event of Default.

“**Default Rate**” means a per annum rate equal to the lesser of five (5%) percent above the Note Rate as set forth in the Note or the maximum rate permitted by applicable law.

“**Equipment**” means all beds, linen, televisions, carpeting, telephones, cash registers, computers, lamps, glassware, rehabilitation equipment, restaurant and kitchen equipment, and other fixtures and equipment of each of the Borrowers located on, attached to or used or useful in connection with any of the Property or the Facility and all renewals and replacements thereof and substitutions therefor; provided, however, that with respect to any items which are leased for the benefit of the Facility and not owned by any Borrower, the Equipment shall include the leasehold interest only of a Borrower together with any options to purchase any of said items and any additional or greater rights with respect to such items which any Borrower may hereafter acquire, but the foregoing shall not be construed to mean that such leasing shall be permitted hereunder and under the other Loan Documents.

“**ERISA**” shall have the meaning set forth in Section 3.23.

“**Event of Default**” means any “Event of Default” as defined in Article VI hereof.

“**Exhibit**” means an Exhibit to this Agreement, unless the context refers to another document, and each such Exhibit shall be deemed a part of this Agreement to the same extent as if it were set forth in its entirety wherever reference is made thereto.



“**Facility**” means that certain facility known as Companions Specialized Care Center, a 121-bed licensed skilled nursing facility located at 6201 East 36<sup>th</sup> Street, Tulsa, OK 74135, as it may now or hereafter exist, together with any other general or specialized care facility, if any, now or hereafter operated on the Property.

“**Facility Bank**” means The PrivateBank and Trust Company.

“**Force Majeure**” means any happening or occurrence such as strikes, acts of God or nature or similar unanticipated events beyond the control of the party affected thereby, which prevents such party’s compliance with certain obligations hereunder, other than a Borrower’s financial inability to perform.

“**GAAP**” means, as in effect from time to time, generally accepted accounting principles consistently applied as promulgated by the American Institute of Certified Public Accountants.

“**General Intangibles**” means all intangible personal property of any of the Borrowers arising out of or connected with the Property or the Facility and all renewals and replacements thereof and substitutions therefor (other than Accounts, Rents, Instruments, Inventory, Money, Permits, and Reimbursement Contracts), including, without limitation, things in action, contract rights and other rights to payment of money.

“**Governmental Authority**” means any board, commission, department or body of any municipal, county, state or federal governmental unit, or any subdivision of any of them, that has or acquires jurisdiction over the Property and/or the Improvements or the use, operation or improvement of the Property.

“**Guarantor**” means, jointly and severally, any Corporate Guarantor and each other party who executes and delivers a Guaranty Agreement in accordance with the terms of this Agreement.

“**Guaranty Agreement**” means any Payment and Performance Guaranty.

“**Health Regulatory Authority**” means any Governmental Authority administering, overseeing, or regulating any certificates of need and other licensure and regulatory approvals required for the operation of the Facility (including any approvals required to obtain reimbursement under Medicare, Medicaid and CHAMPUS, and other Department of Veterans Affairs benefits, as applicable.)

“**Improvements**” means all buildings, structures and improvements of every nature whatsoever now or hereafter situated on the Property, including, but not limited to, all gas and electric fixtures, radiators, heaters, engines and machinery, boilers, ranges, elevators and motors, plumbing and heating fixtures, carpeting and other floor coverings, water heaters, awnings and storm sashes, and cleaning apparatus which are or shall be attached to the Property or said buildings, structures or improvements.

“**Indebtedness**” means any (a) obligations for borrowed money, (b) obligations, payment for which is being deferred by more than thirty (30) days, representing the deferred purchase price of property other than accounts payable arising in connection with the purchase of inventory and materials customary in the trade and in the ordinary course of each Borrower’s business, (c) obligations, whether or not assumed, secured by Liens or payable out of the proceeds or production from the Accounts and/or property now or hereafter owned or acquired, and (d) the amount of any other obligation (including obligations under financing leases) which would be shown as a liability on a balance sheet prepared in accordance with GAAP.

“**Indemnified Parties**” shall have the meaning set forth in Section 7.4.

“**Inspection Fee**” shall have the meaning set forth in Section 4.17(c).

“**Installment Payments**” shall have the meaning given to such term in the Note.

“**Instruments**” means all instruments, chattel paper, documents or other writings obtained from or in connection with the operation of the Property or the construction and operation of the Facility (including, without limitation, all ledger sheets, computer records and

printouts, data bases, programs, books of account, trademarks or trade names, utility contracts, maintenance and service contracts, and files relating thereto).

“**Inventory**” means all inventories of food, beverages and other consumables held by any of the Borrowers for sale or use at or from the Property or the Facility, and soap, paper supplies, medical supplies, drugs and all other such goods, wares and merchandise held by any of the Borrowers for sale to or for consumption by guests, patients or residents of the Property or the Facility and all such other goods returned to or repossessed by any Borrower.

“**Knowledge**” means that any Borrower will be deemed to have “Knowledge” of a particular fact or other matter if any executive officer of such Borrower is aware of such fact or other matter where a prudent individual could be expected to discover or otherwise become aware of such fact or other matter in the course of operating the business.

“**Lease Agreement**” shall mean that certain Facility Lease dated June 25, 2012 and effective on the Operations Closing Date, between Owner and the Operator.

“**Legal Requirements**” means all governmental statutes, laws, rules, orders, regulations, ordinances, judgments, decrees and injunctions of any Governmental Authority affecting either Borrower or the Property or any portion of or the construction, rehabilitation, ownership, use, alteration or operation of, or any portion of the Property (whether now or hereafter enacted and in force), and all permits, licenses and authorizations and regulations relating thereto.

“**Lender**” shall mean Contemporary Healthcare Senior Lien Fund I, L.P.

“**Lender’s Approval**” shall have the meaning set forth in Section 7.12.

“**Lien**” means any voluntary or involuntary mortgage, security deed, deed of trust, lien, pledge, assignment, security interest, title retention agreement, financing lease, levy, execution, seizure, judgment, attachment, garnishment, charge, lien or other encumbrance of any kind, including those contemplated by or permitted in this Agreement and the other Loan Documents.

“**Loan**” shall mean the loan in a maximum amount of the Original Loan Amount made by Lender to Borrowers as evidenced by the Note.

“**Loan Documents**” means, collectively:

- (i) this Agreement,
- (ii) Assignment and Pledge Agreement (with, if applicable, Waiver and Consent),

(iii) Assignment of Acquisition Contracts and Documents,

(iv) Assignment of Leases and Rents,

(v) Borrower Environmental Indemnity Agreement,

(vi) Capital Improvements Escrow and Security Agreement,

(vii) Closing Statement,

(viii) Control Agreement,

(ix) Management Company Environmental Indemnity Agreement,

(x) Mortgage,

(xi) Note,

(xii) Operations Seller Subordination and Assignment of Lease Agreement,

(xiii) Operations Seller SNDA,

(xiv) Payment and Performance Guaranty,

(xv) Security Agreement,

(xvi) Subordination and Assignment of Lease Agreement,

(xvii) Subordination and Assignment of Management Agreement,

(xviii) Subordination and Attornment Agreement,

(xix) Subordination and Standstill Agreement,

(xx) Subsidiary Guaranty,

(xxi) Tax and Insurance Escrow and Security Agreement, and

(xxii) ZBA Agreement.

each as further amended, modified, supplemented or restated, together with any and all other documents executed by any Borrower or others, evidencing, securing or otherwise relating to the Loan.

“**Loan Obligations**” means the aggregate of all principal and interest owing from time to time under the Note and all expenses, charges and other amounts from time to time owing under the Note, this Agreement, or the other Loan Documents and all covenants, agreements and other obligations from time to time owing to, or for the benefit of, Lender pursuant to the Loan Documents.

“**Loan-to-Value Ratio**” means a ratio of the first number to the second number in which:

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- (a) the first number is the sum of the Loan Obligations, and
- (b) the second number is the sum of the:
  - (i) net income from operations of the Facility (without deduction for actual management fees paid in connection with the operation of the Facility) calculated based upon a trailing twelve (12) month period,
  - (ii) interest expense with respect to the Facility, to the extent deducted in determining net income,
  - (iii) lease expense pursuant to a lease of the Facility from one Borrower to another, if any, to the extent deducted in determining net income,
  - (iv) non-cash expenses or allowances for depreciation and amortization of the Facility for such period to the extent deducted in determining net income, and

*less:*

- (i) non- operating or extraordinary income,
- (ii) Assumed Management Fees,
- (iii) required Capital Improvements Reserve Fund deposits for such period, and
- (iv) unfinanced capital expenditures in excess of the sum of Capital Improvements Reserve Fund deposits for such period,

divided by:

- (i) fourteen percent (14.00%).

“**Management Agreement**” means that certain Management Agreement dated January 1, 2012, between Operator and Management Company.

“**Management Company**” shall mean AdCare Oklahoma Management, LLC, a Georgia limited liability company.

“**Management Company Environmental Indemnity Agreement**” shall have the meaning set forth in Section 2.2(c)(vi) of this Agreement.

“**Material Adverse Effect**” shall have the meaning set forth in Section 3.1.

“**Maturity Date**” shall have the meaning given such term in the Note.

“**Medicaid**” means that certain program of medical assistance, funded jointly by the federal government and the states, for impoverished individuals who are aged, blind and/or

disabled, and/or members of families with dependent children, which program is more fully described in Title XIX of the Social Security Act (42 U.S.C. §§ 1396 *et seq.*) and the regulations promulgated thereunder.

“**Medicare**” means that certain federal program providing health insurance for eligible elderly and other individuals, under which physicians, hospitals, independent living and assisted living facilities, skilled nursing homes, home health care and other providers are reimbursed for certain covered services they provide to the beneficiaries of such program, which program is more fully described in Title XVIII of the Social Security Act (42 U.S.C. §§ 1395 *et seq.*) and the regulations promulgated thereunder.

“**Money**” means all monies, cash, rights to deposit or savings accounts or other items of legal tender obtained from or for use in connection with the operation of the Facility.

“**Mortgage**” means that certain Mortgage, Assignment of Leases and Rents, Security Agreement and Fixture Filing of even date herewith from the Owner in favor of or for the benefit of Lender as set forth in Section 2.2(b)(i).

“**Note**” means the Promissory Note dated the date hereof in the principal amount of the Original Loan Amount payable by Borrowers to the order of Lender.

“**Note Rate**” shall have the meaning given such term in the Note.

“**Operations Closing Date**” shall have the meaning given such term in Section 3.39(i).

“**Operations Seller**” means Tulsa Christian Care, Inc.

“**Operations Seller Lease Agreement**” means the Facility Lease dated the date hereof, between Operations Seller and Owner.

“**Operations Seller Management Agreement**” means the Management Agreement dated June 25, 2012, as amended, between Operations Seller and Management Company.

“**Operations Seller SNDA**” shall have the meaning set forth in Section 2.2(c)(vii).

“**Operations Seller Subordination and Assignment of Lease Agreement**” shall have the meaning set forth in Section 2.2(c)(viii).

“**Operations Seller Transfer Agreement**” means the Operations Transfer Agreement dated the date hereof, between the Operations Seller and the Operator.

“**Original Loan Amount**” shall mean \$5,000,000.

“**Payment and Performance Guaranty**” shall have the meaning set forth in Section 2.2(b)(viii).

“**Permits**” means all licenses, permits and certificates used or necessary in connection with the ownership, operation, construction, use or occupancy of the Property and/or the Facility, including, without limitation, business licenses, state health department licenses, food service licenses, licenses to conduct business, certificates of need and all such other permits, licenses and rights, obtained from any governmental, quasi-governmental or private person or entity whatsoever concerning ownership, construction, operation, use or occupancy.

“**Permitted Encumbrances**” has the meaning given to that term in Section 5.2 hereof.

“**Person**” means any natural person, firm, trust, corporation, partnership, limited liability company, trust and any other form of legal entity.

“**Physical Plant Standard**” shall have the meaning set forth in Section 3.15.

“**Proceeds**” means all awards, payments, earnings, royalties, issues, profits, liquidated claims, and proceeds (including proceeds of insurance and condemnation or any conveyance in lieu thereof) from the sale, conversion (whether voluntary or involuntary), exchange, transfer, collection, loss, damage, condemnation, disposition, substitution or replacement of any of the Collateral.

“**Property**” means the real estate which is more particularly described in Exhibit A hereto, upon which the Facility is located, and which, concurrent with the Closing Date, was owned by Owner.

“**Purchase Agreement**” means the Purchase and Sale Agreement, with exhibits, dated March 14, 2012, as amended April 19, 2012 and June 19, 2012, as amended, between Seller and AdCare Property Holdings, LLC, as assigned to the Owner.

“**Reimbursement Contracts**” means all third party reimbursement contracts for the Facility which are now or hereafter in effect with respect to residents or patients qualifying for coverage under the same, including Medicare, Medicaid, other government programs and private insurance agreements, and any successor program or other similar reimbursement program and/or private insurance agreements.

“**Rents**” means all rent and other payments of whatever nature from time to time payable pursuant to leases of the Property or the Facility, or for retail space or other space at the Property (including, without limitation, rights to payment earned under leases for space in the Improvements for the operation of ongoing retail businesses such as newsstands, barbershops, beauty shops, physicians’ offices, pharmacies and specialty shops).

“**Security Agreement**” shall have the meaning set forth in Section 2.2(b)(ii).

“**Seller**” means, collectively, F&F Ventures, LLC and Tulsa Christian Care, Inc.

“**Single Purpose Entity**” means a Person which owns no interest or property other than the Property and the Improvements or has a business purpose limited solely to the leasing and operation of the Facility.

“**Stabilization**” means the date upon which the Facility demonstrates a Total Debt Service Coverage Ratio of 1.15 to 1.00 for three consecutive calendar months.

“**Standstill Notice**” shall have the meaning set forth in Section 6.4.

“**Stock**” shall mean all shares, options, warrants, general or limited partnership interests, membership interests, participations or other equivalents (regardless of how designated) in a corporation, limited liability company, partnership or any equivalent entity, whether voting or nonvoting, including, without limitation, common stock, preferred stock, or any other “equity security” (as such term is defined in Rule 3a11-1 of the General Rules and Regulations promulgated by the Securities and Exchange Commission under the Securities Exchange Act of 1934, as amended).

“**Subordination and Assignment of Lease Agreement**” shall have the meaning set forth in Section 2.2(c)(iii).

“**Subordination and Assignment of Management Agreement**” shall have the meaning set forth in Section 2.2(c)(ii).

“**Subordination and Attornment Agreement**” shall have the meaning set forth in Section 2.2(c)(i).

“**Subordination and Standstill Agreement**” shall have the meaning set forth in Section 2.2(c)(iv).

“**Subsidiary Guaranty**” shall have the meaning set forth in Section 2.2(b)(ix).

“**Tax**” (including, with correlative meaning, the terms “**Taxes**” and “**Taxable**”) means, with respect to any Person, (a) all taxes, domestic or foreign, including without limitation any income (net, gross or other, including recapture of any tax items such as investment tax credits), alternative or add-on minimum tax, gross income, gross receipts, gains, sales, use, leasing, lease, user, ad valorem, transfer, recording, franchise, profits, property (real or personal, tangible or intangible), fuel, license, withholding on amounts paid to or by such Person, payroll, employment, unemployment, social security, excise, severance, stamp, occupation, premium, environmental or windfall profit tax, custom, duty or other tax, or other like assessment or charge of any kind whatsoever, together with any interest, levies, assessments, charges, penalties, additions to tax or additional amounts imposed by any Taxing Authority, (b) any joint or several liability of such Person with any other Person for the payment of any amounts of the type described in (a) of this definition and (c) any liability of such Person for the payment of any amounts of the type described in (a) as a result of any express or implied obligation to indemnify any other Person.

“**Tax and Insurance Escrow and Security Agreement**” shall mean that certain Tax and Insurance Escrow and Security Agreement in the form attached hereto as Schedule 2.2(b)(vi).

“**Tax and Insurance Reserve Fund**” shall have the meaning set forth in Section 4.4(g).

“**Tax and Insurance Report**” shall mean the report required by Section 4.6(o) of this Agreement.

“**Tax Return(s)**” mean all returns, consolidated or otherwise (including without limitation informational returns), required to be filed with any Taxing Authority.

“**Taxing Authority**” means any authority responsible for the imposition or collection of any Tax.

“**Third Party Payors’ Programs**” shall have the meaning set forth in Section 3.13.

“**Title Policy**” means the policy for title insurance issued by First American Title Insurance Company.

“**Total Debt Service Coverage Ratio**” means the Debt Service Coverage Ratio including the AR Loan.

“**Trade Rights**” shall have the meaning set forth in Section 3.32.

“**UCC**” shall mean the Uniform Commercial Code.

“**ZBA Agreement**” means the agreement by and among the Facility Bank, each Borrower and the AR Lender, governing the operation of the Government Receivables Account and Payroll Account and transfer to the Loan Account.

1.2 **Singular vs. Plural**. Singular terms shall include the plural forms and vice versa, as applicable, related to the terms defined.

1.3 **Uniform Commercial Code**. Terms contained in this Agreement shall, unless otherwise defined herein or unless the context otherwise indicates, have the meanings, if any, assigned to them by the Uniform Commercial Code in effect in the state in which the Collateral for the Loan Obligations is deemed located, as such Uniform Commercial Code may be amended from time to time (provided, no amendment shall have the effect of releasing any security interest previously granted.)

1.4 **GAAP**. All accounting terms used in this Agreement shall be construed in accordance with GAAP, except as otherwise specified.

1.5 **References Generally**. All references to other documents or instruments shall be deemed to refer to such documents or instruments as they may hereafter be extended, renewed, modified, or amended and all replacements and substitutions therefor.

1.6 **References to Medicaid and Medicare**. All references herein to “Medicaid” and “Medicare” shall be deemed to include any successor program thereto.

## ARTICLE II. TERMS OF THE LOAN

### 2.1 **The Loan**.

(a) **Loan**. Borrowers have agreed to borrow the Loan from Lender and Lender has agreed to make the Loan to Borrowers, subject to each Borrower’s compliance with and observance of the terms, conditions, covenants, and provisions of this Agreement and the other Loan Documents, and Borrowers have made the covenants, representations, and warranties herein and therein as a material inducement to Lender to make the Loan.

(b) **Closing Date**. The date of the closing related to the disbursing of any portion of the Loan and delivery of the Loan Documents shall be referred to herein as the “**Closing Date**.”

### 2.2 **Loan Documents**.

(a) The Loan will be evidenced by the Loan Documents, including, but not limited to, the Note;

(b) The Loan will be secured and guaranteed by the following:



- (i) a first lien deed of trust/mortgage lien to secure debt and security agreement, assignment of rents, and fixture filing relating to all of Owner' s right, title and interest in and to the Facility including the real property, the improvements thereon, and all Equipment, fixtures, and Inventory used in connection therewith in form and substance satisfactory to Lender delivered by the Owner on the Closing Date in the form of which attached hereto as Schedule 2.2(b)(i) (the "**Mortgage**");
- (ii) except for accounts receivable for which Lender shall have a second lien subject only to AR Lender' s interest in same, a first lien security interest and an assignment of Borrowers' interest in all General Intangibles, including, but not limited to, licenses, Permits, Reimbursement Contracts, leases and other contracts used in connection with or relating to operation of the Facility, and a second lien, subject only to AR Lender' s lien, on Accounts, as evidenced by the Security Agreement delivered by Borrowers on the Closing Date, in the forms attached hereto as Schedule 2.2(b)(ii) (the "**Security Agreement**");
- (iii) a first lien security interest in all of the issued and outstanding membership interests or capital stock, as the case may be, of Owner and Operator, evidenced by the form of Assignment and Pledge Agreement executed and

delivered by all the members of each of the Borrowers on the Closing Date, along with a Waiver and Consent, if applicable, in the form attached hereto as Schedule 2.2(b)(iii) (each, an "**Assignment and Pledge Agreement**");

- (iv) a first lien security interest and an assignment of all of Borrowers' interest in all of the rights related to any rents and leases relating to the Facility as evidenced by the Assignment of Leases and Rents delivered on the Operations Closing Date in the form attached hereto as Schedule 2.2(b)(iv) (the "**Assignment of Leases and Rents**");
- (v) a first lien security interest in the Capital Improvements Reserve Fund as evidenced and as required by the form of capital improvements escrow and security agreement attached hereto as Schedule 2.2(b)(v) (the "**Capital Improvements Escrow and Security Agreement**");
- (vi) a first lien security interest in the Tax and Insurance Reserve Fund as evidenced and as required by the form of tax and insurance escrow and security agreement attached hereto as Schedule 2.2(b)(vi) (the "**Tax and Insurance Escrow and Security Agreement**");
- (vii) a first lien on the Capitalized Interest Reserve Account;
- (viii) a guaranty by each Corporate Guarantor, through the delivery to Lender on the Closing Date, of a payment and performance guaranty agreement in the form attached hereto as Schedule 2.2(b)(viii) (each a "**Payment and Performance Guaranty**");
- (ix) a guaranty by each subsidiary of any Borrower which may be hereafter acquired or formed by a Borrower, it being understood and agreed that as of the Loan Closing Date, no such entities exist, through the delivery to Lender at the time of the acquisition or formation of

such subsidiary by each such subsidiary, a Guaranty in the form attached hereto as Schedule 2.2(b)(ix) (each, a “**Subsidiary Guaranty**”);

- (x) a Control Agreement by and among the Facility Bank, Borrowers and AR Lender for the “Loan Account,” as defined in the AR Loan Agreement, delivered to AR Lender on within 10 Business Days of the Closing Date or

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at a later date as agreed to by AR Lender in the form attached to the AR Loan Agreement (the “**Control Agreement**”); and

- (xi) an Assignment of Acquisition Contracts and Documents dated the Closing Date executed and delivered by the Owner in the form attached hereto as Schedule 2.2(b)(xi) (the “**Assignment of Acquisition Contracts and Documents**”).
- (c) Additional terms and conditions of the Loan will be evidenced by the following documents:
- (i) a Subordination and Attornment Agreement executed and delivered by Operator, Owner and Lender on the Operations Closing Date in the form attached hereto as Schedule 2.2(c)(i) (the “**Subordination and Attornment Agreement**”);
  - (ii) a Subordination and Assignment of Management Agreement executed and delivered by Borrowers and the Management Company on the Operations Closing Date in the form attached hereto as Schedule 2.2(c)(ii) (the “**Subordination and Assignment of Management Agreement**”);
  - (iii) a Subordination and Assignment of Lease Agreement executed and delivered by Borrowers on the Operations Closing Date in the form attached hereto as Schedule 2.2(c)(iii) (the “**Subordination and Assignment of Lease Agreement**”);
  - (iv) a Subordination and Standstill Agreement executed and delivered by Lender and AR Lender, and acknowledged by each Borrower on the Closing Date in the form attached hereto as Schedule 2.2(c)(iv)(A) (the “**Subordination and Standstill Agreement**”);
  - (v) a Borrower Environmental Indemnity Agreement dated the Closing Date executed and delivered by Borrowers in the form attached hereto as Schedule 2.2(c)(v) (the “**Borrower Environmental Indemnity Agreement**”);
  - (vi) a Management Company Environmental Indemnity Agreement dated the Closing Date executed and delivered by the Management Company in the form attached hereto as Schedule 2.2(c)(vi) (the “**Management Company Environmental Indemnity Agreement**”);

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- (vii) a Subordination and Attornment Agreement executed and delivered by Operations Seller, Owner and Lender on the Closing Date in the form attached hereto as Schedule 2.2(c)(vii) (the “**Operations Seller SNDA**”); and
- (viii) a Subordination and Assignment of Lease Agreement executed and delivered by Owner on the Closing Date in the form attached hereto as Schedule 2.2(c)(viii) (the “**Operations Seller Subordination and Assignment of Lease Agreement**”).

2.3 **Closing Deliverables by Borrowers.** Borrowers shall deliver or cause to be delivered to Lender the following:

(a) **Borrower’s Officers’ Certificates.** On the Closing Date, a certificate executed by the Chief Executive Officer and Chief Financial Officer or other party acceptable to Lender of each Borrower certifying to Lender, among other things, that, as of the Closing Date: (i) the transactions have been duly authorized, (ii) true, correct and complete copies of the organizational documents of Borrowers have been delivered to Lender, (iii) to the Borrowers’ Knowledge, no part of the Facility shall have been damaged and not repaired to Lender’s satisfaction or taken in condemnation or other like proceedings nor shall any such proceeding be pending, (iv) to the Borrowers’ Knowledge, the Facility shall be unimpaired and not reduced in value and shall be free from settling and other structural defects, (v) neither the Borrowers nor the Guarantors, nor any of Borrowers’ or Guarantors’ principals shall be involved in any bankruptcy, reorganization or insolvency proceeding and (vi) that since the date or dates, as the case may be, of the financial information last provided to the Lender with respect to the Borrowers, any ownership interest in the Borrowers, the Facility or the Guarantors, there has been no material adverse change in the financial condition thereof;

(b) **Legal Opinion.** On the Closing Date, a legal opinion of Borrowers’, the Borrowers’ members and any Guarantor’s counsel, in form and content satisfactory to Lender and its counsel;

(c) **Reports.** The following reports and other documents all of which shall be in Lender’s name:

- (i) **Title Commitment.** From a title company acceptable to Lender, at no cost to Lender, the current title commitment or binder and, on the Closing Date, an ALTA mortgagee’s Loan Policy - 2006 Form, with such changes as Lender may request, naming as an insured “Contemporary Healthcare Senior Lien Fund I, L.P., together with its successors and/or assigns as their interests may appear,” together with such coinsurance and/or reinsurance, exceptions, and other endorsements as may be required by Lender, showing Owner as title holder and insuring the amount and priority of Lender’s lien. If such commitment

and/or policy is not in electronic form, please provide and send two copies of each to Lender and one copy to the Lender’s counsel. On the Closing Date, the title commitment must be marked as a pro forma binder or a Title Policy must be issued, in either case subject to Lender’s approval. The status of title is subject to Lender’s approval.

- (ii) **Survey.** On the Closing Date, three (3) copies of a survey with a licensed surveyor’s certificate, all in form and substance acceptable to and certified to Lender, Lender’s counsel and the title insurance company. Such survey and surveyor’s certificate shall not be dated more than thirty (30) days prior to the date of the Closing Date and shall attest to the existence or nonexistence of a special flood hazard area with respect to the Facility. The survey shall also be prepared in accordance with ALTA 2011 standards and be certified

to the Lender and the title insurance company. Such survey shall provide evidence to Lender that all streets adjoining the Property underlying the Facility have been completed, dedicated and accepted for maintenance and public ingress and egress to the Property.

- (iii) Environmental Report. On the Closing Date, a Phase I Environmental Report indicating that the Facility and the Property are free from toxic chemicals and environmentally hazardous substances and that surrounding land uses do not pose an environmental threat.
- (iv) Engineering Report. On the Closing Date, an engineering report of the Facility from an engineering firm acceptable to Lender in its sole discretion, which report shall be in substance acceptable to Lender
- (v) Appraisal. (a) On the Closing Date, an appraisal of the Property “as is” acceptable to Lender, in its sole discretion dated no more than thirty (30) days prior to the Closing Date, and (b) as otherwise may be required hereunder.
- (vi) Termite Inspection Report. On the Closing Date, a termite inspection report of the Facility dated no more than thirty (30) days prior to the Closing Date in form and substance satisfactory to the Lender or, in lieu thereof, a current pest control contract for the Facility.

(d) Zoning Letter. A copy of a letter from local zoning authority or some other evidence acceptable to Lender, addressed to the Lender, confirming that the Facility is zoned for its intended use.

(e) Sprinkler Systems. On the Closing Date, Borrowers shall provide evidence to Lender, acceptable to Lender in its sole discretion, that all buildings that comprise the Facility have sprinkler systems.

(f) Evidence of Insurance. Evidence, acceptable to Lender in its sole discretion, of insurance required by Section 4.5 herein, in form and substance acceptable to Lender. Such evidence shall be: (i) the original, or a copy certified by the insurance agent, of the policy(ies) of insurance, or (ii) the insurance binder (Acord Form 25 provided by the insurance carrier) or (iii) a certificate of insurance (Acord Form 27 or 28, at Lender’s discretion, provided by the insurance agent), or (iv) an original letter from the insurance carrier on the primary layer, signed by an officer of such carrier, attaching the form of insurance policy pursuant to which coverage is being provided, and, if applicable, an original letter from each insurance carrier on the excess layers, signed by an officer of such carrier(s) agreeing that such carrier is bound to the form of insurance policy delivered by the primary carrier (i.e., agreeing to “follow form” to the primary carrier). The letter must set forth the date by which the policy will be delivered to the Lender. All mortgagee/loss payee/additional insured endorsements must be attached to such letter.

(g) Evidence of Payment of Taxes. Evidence, acceptable to the Lender in its sole discretion, that Borrowers have timely and appropriately paid all Taxes associated with the Facility.

(h) Licenses and Permits. On the Closing Date, a copy of the Facility license to permit it to be operated as a skilled nursing facility prior to the Operations Closing Date.

(i) Certificate of Occupancy. On the Closing Date or post Closing Date at Lender’s discretion, a copy of the Facility’s Certificate of Occupancy.

(j) Loan Documents. On the Closing Date, executed copies of each of the Loan Documents required on such date.

(k) Other Agreements. On the Closing Date, a copy of the executed Operations Seller Management Agreement, Operations Seller Lease Agreement and the Operations Seller Transfer Agreement.

(l) Further Assurances. Such other information of Borrowers, each Guarantor and/or the Facility, as Lender shall reasonably deem necessary.

#### 2.4 **Interest and Interest Rate.**

(a) The outstanding principal balance of the Loan will bear interest at the Note Rate as set forth in the Note and payments of principal and interest on the Loan, including any prepayment premium, shall be made in accordance with the terms and provisions

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of the Note and this Agreement. Payments of principal and interest on the Loan shall be made in accordance with the terms and provisions of the Note and the amortization schedule attached hereto as Schedule 2.4(a) (which amortization schedule may be adjusted during the term of the Loan in accordance with the Note).

(b) All interest on the outstanding principal balance of the Loan shall be calculated on the basis of a 360-day year by multiplying the outstanding principal amount by the applicable per annum rate, multiplying the product thereof by the actual number of days elapsed and dividing the product so obtained by 360.

2.5 **Repayment of Loan.** Each payment of the Loan Obligations shall be paid directly to Lender in lawful money of the United States of America at the following address:

Contemporary Healthcare Senior Lien Fund I, L.P.  
1040 Broad Street  
Suite 103  
Shrewsbury, New Jersey 07702  
Attention: Mr. Eric Smith

or such other place as Lender shall designate in writing to Borrowers. Each such payment shall be paid in immediately available funds by 2:00 p.m. Eastern time on the date such payment is due, except if such date is not a Business Day such payment shall then be due on the first Business Day after such date, but interest shall continue to accrue until the date payment is received. Any payment received after 2:00 p.m. Eastern time shall be deemed to have been received on the immediately following Business Day for all purposes, including, without limitation, the accrual of interest on principal.

#### 2.6 **Prepayment.**

(a) The Loan may be prepaid in whole or in part at any time upon not less than thirty (30) days prior written notice to Lender and not more than forty (40) days prior written notice to Lender specifying the scheduled payment date on which such prepayment will be made and the amount of such prepayment, and provided further that all prepayments must include all unpaid interest and any other amounts owed to Lender relating to the Loan amount prepaid, plus a premium equal to a percentage of the Loan principal balance outstanding and being prepaid as of the prepayment date equal to five percent (5%) in the first Loan year, one percent (1%) in the second Loan year and no prepayment premium thereafter until the Maturity Date.

(b) If a prepayment is made in which the Loan shall be prepaid in whole, the AR Loan shall also be repaid in full together with all interest, fees, expenses and other amounts owed to Lender under the documents executed in connection with such accounts receivable loan.

(c) Borrowers shall not be entitled to re-borrow any amounts so prepaid.

2.7 **Late Charges on Overdue Installments; Collection Costs.**

(a) If any scheduled payment of principal or interest as set forth in the Note, or any other agreed charge, is not made as the same becomes due, Borrowers agree to pay to Lender a late charge as required by the Note.

(b) The imposition of such late charges shall not preclude Lender from exercising any other remedies which it may have.

(c) Borrowers will also pay to Lender, in addition to the amount due, all reasonable costs of collecting, securing, or attempting to collect or secure the Note, including, without limitation, court costs and reasonable attorneys' fees, including, without limitation, attorneys' fees for preparation of litigation and in any appellate and bankruptcy proceedings.

2.8 **Usury Provisions.** In no event shall the amount of interest due or payable hereunder or pursuant to any of the Loan Documents exceed the maximum rate of interest allowed by applicable law, and in the event any such payment is inadvertently paid by Borrowers or inadvertently received by Lender, then such excess sum shall be credited as a payment of principal. It is the express intent hereof that Borrowers not pay and Lender not receive, directly or indirectly, interest in excess of that which may be legally paid by Borrowers under applicable law.

2.9 **Fees.**

(a) **Application Fee.** On the Closing Date, Borrowers shall pay to Lender a non-refundable Application Fee of one percent (1.00%) of the Original Loan Amount, which fee may be paid for from Loan proceeds (the "**Application Fee**").

(b) **Closing Fee.** On the Closing Date, Borrowers shall pay to Lender a Closing Fee of one percent (1.00%) of the Original Loan Amount, which fee may be paid for from Loan proceeds (the "**Closing Fee**").

All fees provided for in this Section 2.9 are deemed fully earned on the date due.

2.10 **Use of Loan; Disbursement of Proceeds.**

(a) Borrowers agree to use the Loan for the following:

(i) To acquire the Facility;

(ii) To provide funds to pay for the costs, expenses and fees due in connection with the Loan as noted on the Lender's Closing Statement;

(iii) To fund Loan reserves; and

- (iv) The balance of the Loan, if any, shall be used for working capital, including, but not limited to, towards satisfaction of the covenants set forth herein and in the other Loan Documents.

(b) All proceeds of the Loan will be disbursed through a title company selected by Lender pursuant to closing instructions to be provided by Lender and/or Lender's counsel.

(c) Borrowers further agree to make an equity contribution of \$550,000. The required equity contribution amount excludes any other fee the Borrowers or any of their Affiliates would pay themselves for services with respect to the acquisition or improvement of the Facility.

(d) Lender acknowledges that Borrowers have agreed to provide \$750,000 of stock in AdCare Health Systems, Inc. to Seller in accordance with the Purchase Agreement.

2.11 **Miscellaneous.** With respect to the amounts due under the Note, each Borrower waives the following to the fullest extent permitted by law:

(a) All rights of exemption of any of the Collateral from levy or sale under execution or other process for the collection of debts under the Constitution or laws of the United States or any state thereof;

(b) Demand, presentment, protest, notice of dishonor, notice of non-payment, diligence in collection, and all other requirements necessary to enforce the Note; and

(c) Any further receipt by Lender or acknowledgment by Lender of any Collateral now or hereafter deposited with Lender as security for the Loan.

2.12 **Application of Payment.** Note payments shall be applied as set forth in the Note.

### **ARTICLE III. BORROWERS' REPRESENTATIONS AND WARRANTIES**

To induce Lender to enter into this Agreement, and to make the Loan to Borrowers, each Borrower, jointly and severally, represents and warrants to Lender as follows:

3.1 **Existence, Power and Qualification.** Each Borrower is a duly organized and validly existing in the jurisdiction of its formation having the power to own its properties and to carry on its business as is now being conducted, and is duly qualified to do business and is in good standing in every jurisdiction in which the failure to be so qualified would have a material adverse effect on the results of operations, conditions (financial or otherwise), assets, properties, business or prospects of Borrowers (a "**Material Adverse Effect**").

3.2 **Power and Authority.** Each Borrower has full power and authority to borrow the indebtedness evidenced by the Note and to incur the Loan Obligations provided for herein, all of which have been authorized by all proper and necessary action. All consents, approvals authorizations, orders or filings of or with any court or governmental agency or body, if any, required for the execution, delivery and performance of the Loan Documents by each Borrower has been obtained or made.

3.3 **Due Execution and Enforcement.** Each of the Loan Documents to which each Borrower is a party constitutes a valid and legally binding obligation of each Borrower, enforceable in accordance with its respective terms (except as such enforcement may be limited by bankruptcy, insolvency, reorganization, receivership, moratorium, or other laws relating to the rights of creditors generally and by general principles of equity) and does not violate, conflict with, or constitute any default under any law, government regulation, decree, judgment, each Borrower's articles of organization or operating agreement or any other agreement or instrument binding upon each Borrower.

3.4 **Capitalization.** The owners of any issued and outstanding equity interests of a Borrower and the amount of such equity interests held by such owners as of the Closing Date is set forth on Exhibit C attached hereto. All such issued and outstanding equity interests of the Borrowers have been duly and validly issued and are fully paid and non-assessable and were issued in full compliance with all federal and state securities laws. There are no outstanding (a) options, warrants or other rights to purchase from any Borrower any securities of a Borrower, (b) securities convertible into or exchangeable for shares of such equity interests, or (c) other commitments of any kind for the issuance of additional equity interests or options, warrants or other securities of the Borrowers except as set forth on Exhibit C. Except as set forth on Exhibit C, the Borrowers are not, pursuant to the terms of any other agreement currently in existence, under any obligation to register under the Securities Act of 1933, as amended, any of their presently outstanding securities or any of their securities which may be hereafter issued.

3.5 **Subsidiaries.** Neither Borrower presently owns or controls, directly or indirectly, any interest in any other corporations, associations or other business entities and neither Borrower is a participant in any joint venture, partnerships or similar arrangements.

3.6 **Non-Contravention.** Neither the execution and delivery by the Borrowers of this Agreement or the other Loan Documents, nor the consummation by the Borrowers of the transactions contemplated hereby and thereby, will (a) conflict with or violate the provisions of any law, rule or regulation applicable to the Borrowers or any of their respective properties or assets, (b) conflict with or violate the provisions of the organizational or governing documents, including but not limited to, the operating agreements of the Borrowers, (c) require on the part of any Borrower any notice to or filing with, or any permit, authorization, consent or approval of, any Governmental Authority other than the filing of UCC financing statements as required by the Loan Documents, (d) require on the part of any Borrower, any notice to or filing with or any permit authorization, consent or approval of any Person, (e) violate any judgment, decree, order or award of any Governmental Authority by which the Borrowers or their properties are bound, or (f) conflict with, result in material breach of, constitute (with or without due notice or lapse of time or both) a material default under, result in the acceleration of obligations under, create in any party any right to terminate, modify or cancel, or require any notice, consent or waiver under, any material contract or instrument to which a Borrower is a party or by which they are bound (individually or collectively) or to which any of its assets are subject.

3.7 **Absence of Undisclosed Liabilities.** Except as set forth on Schedule 3.7 neither of the Borrowers have any liability or obligation, secured or unsecured, whether accrued, absolute, contingent, unasserted or otherwise, that is material to the condition (financial or

otherwise) of the assets, properties, business or prospects of such Borrower, except as and to the extent any such liability or obligation is reflected and reserved against in the current balance sheet delivered to Lender prior to the Closing Date. Except as set forth on Schedule 3.7 the Facility will not have any liability or obligation, secured or unsecured, whether accrued, absolute, contingent, unasserted or otherwise, that is material to the condition (financial or otherwise) of the assets, properties, business or prospects of the Facility, except as and to the extent any such liability or obligation is reflected and reserved against in the balance sheet delivered to Lender on the Closing Date.



### 3.8 **Pending Matters.**

(a) **Operations; Financial Condition.** No action or investigation is pending or threatened before or by any court or administrative agency which might result in any material adverse change in the financial condition, operations or prospects of any Borrower or any lower reimbursement rate under the Reimbursement Contracts. Neither Borrower is in violation of any agreement, the violation of which might reasonably be expected to have a Material Adverse Effect on its business or assets, and neither Borrower is in violation of any order, judgment, or decree of any court, or any statute or governmental regulation to which it is subject.

(b) **Property Improvements.** There are no proceedings pending, or, to the best of either Borrower's knowledge, threatened, to acquire through the exercise of any power of condemnation, eminent domain or similar proceeding any part of the Property, the Improvements or any interest therein, or to enjoin or similarly prevent or restrict the use of the Property or the operation of the Facility in any manner. None of the Improvements is subject to any unrepaired casualty or other damage.

3.9 **Financial Statements Accurate.** All financial statements heretofore or hereafter provided by either Borrower are and will be true and complete in all material respects as of their respective dates and fairly present the respective financial condition of such Borrower, and there are no material liabilities, direct or indirect, fixed or contingent, as of the respective dates of such statements which are not reflected therein or in the notes thereto or in a written certificate delivered with such statements. The financial statements of each Borrower have been prepared in accordance with GAAP. There has been no material adverse change in the financial condition, operations, or prospects of either Borrower since the dates of such statements except as fully disclosed in writing with the delivery of such statements. All financial statements of the operations of the Facility heretofore or hereafter provided to Lender are and will be true and complete in all material respects as of their respective dates.

### 3.10 **Compliance with Facility Laws.**

(a) Commencing on the Operations Closing Date, Borrowers shall be in compliance, as applicable, in all material respects with the applicable provisions of skilled nursing facility laws, rules, regulations and published interpretations to which Borrowers are subject.

(b) At all times:

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- (i) the Facility is and will be duly licensed and operated as a skilled nursing facility under the applicable laws of the state where the Property is located;
  - (ii) Commencing on the Operations Closing Date, with respect to the Facility, Borrowers will be the lawful owners of all applicable operating Permits for the Facility, including, without limitation, the Certificate of Need, as applicable, which (A) is and will be in full force and effect, (B) constitutes all of the permits, licenses and certificates required for the use, operation and occupancy thereof, (C) has not been pledged as collateral for any other loan or Indebtedness except to Lender or AR Lender or their Affiliates, (D) is and will be free from restrictions or any encumbrance which would materially adversely affect the use or operation of the Facility, and (E) will not be provisional, probationary or restricted in any way;

- (iii) No waivers of any laws, rules, regulations, or requirements (including, but not limited to, minimum square foot requirements per bed) is or will be required for the Facility to operate at the current licensed bed capacity;
- (iv) all Reimbursement Contracts are and will be in full force and effect with respect to the Facility, and each Borrower is in good standing with all the respective agencies governing such skilled nursing facility licenses, program certification, and Reimbursement Contracts;
- (v) each Borrower is and will be current in the payment of all applicable so-called provider specific taxes or other applicable assessments with respect to such Reimbursement Contracts; and
- (vi) in the event Lender acquires the Facility through foreclosure, to the Borrowers' knowledge as of the Closing Date, no receiver appointed by the court in connection with such foreclosure shall have to obtain a Certificate of Need in connection with such foreclosure.

3.11 **Maintain Bed Capacity.** Neither Borrower has granted to any third party the right to reduce the number of licensed beds in the Facility or to apply for approval to transfer the right to any and all of the licensed Facility beds to any other location.

3.12 **Medicare and Medicaid Compliance.** The Facility is in substantial compliance with all requirements for participation in Medicare and Medicaid, including without limitation, the Medicare and Medicaid Patient Protection Act of 1987. The Facility is in

conformance in all material respects with all insurance, reimbursement and cost reporting requirements and has a current provider agreement which is in full force and effect under Medicaid and Medicare.

3.13 **Third-Party Payors.** To the Borrowers' Knowledge, there is no threatened or pending revocation, suspension, termination, probation, restriction, limitation, or nonrenewal affecting either Borrower or the Facility or any participation or provider agreement with any third-party payor, including Medicare, Medicaid and any private commercial insurance managed care and employee assistance program (such programs, the "**Third-Party Payors' Programs**") to which such Borrower presently is subject. All Medicare, Medicaid and private insurance cost reports and financial reports submitted by Borrowers or any Guarantor are and will be materially accurate and complete and have not been and will not be misleading in any material respects. No cost reports for the Facility remain "open" or unsettled, except as otherwise disclosed. Borrowers further covenant to sweep, on a daily basis, all accounts containing Medicaid or Medicare receivables into a Borrowers' account that is subject to the Control Agreement.

3.14 **Governmental Proceedings and Notices.** No Borrower nor the Facility is currently the subject of any proceeding by any governmental agency, and no notice of any violation has been received from a governmental agency that would, directly or indirectly, or with the passage of time:

- (a) Have a material adverse impact on such Borrower' s ability to accept and/or retain patients or result in the imposition of a fine, a sanction, a lower rate certification or a lower reimbursement rate for services rendered to eligible patients;
- (b) Modify, limit or annul or result in the transfer, suspension, revocation or imposition of probationary use of any of the Permits; or

(c) Affect such Borrower's continued participation in the Medicare or Medicaid programs or any other Third-Party Payors' Programs, or any successor programs thereto, at current rate certifications.

(d) Affect such Borrower's prospective participation in the Medicare or Medicaid programs or any other Third-Party Payors' Programs, or any successor programs thereto, at current rate certifications.

The Facility is not the subject of any proceeding by any Governmental Authority, and no notice of any violation has been received by the Facility from a Governmental Authority that would, directly or indirectly, or with the passage of time:

(a) Have a material adverse impact on such Borrower's ability to accept and/or retain residents or result in the imposition of a fine, a sanction, a lower rate certification, if applicable, or a lower reimbursement rate for services rendered, if applicable, to eligible residents;

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(b) Modify, limit or annul or result in the transfer, suspension, revocation or imposition of probationary use of any of the Permits; or

(c) Affect such Borrowers' continued participation in the Medicare or Medicaid programs or any other Third-Party Payors' Programs, or any successor programs thereto, at current rate certifications.

3.15 **Physical Plant Standards.** The Facility and the use thereof complies in all material respects with all applicable local, state and federal building codes, fire codes, health care, nursing facility and other similar regulatory requirements (the "**Physical Plant Standards**"), and no waivers of Physical Plant Standards exist at the Facility.

3.16 **Pledges of Receivables.** Except as set forth in Schedule 3.16, neither Borrower has pledged its Accounts as collateral security for any loan or Indebtedness other than, as applicable, the Loan and the AR Loan.

3.17 **Payment of Taxes and Property Impositions.** Each Borrower has filed all federal, state, and local tax returns which it is required to file and has paid, or made adequate provision for the payment of, all taxes which are shown pursuant to such returns or are required to be shown thereon or to assessments received by each Borrower, including, without limitation, provider taxes. All such returns are complete and accurate in all respects. Each Borrower has paid or made adequate provision for the payment of all applicable water and sewer charges, ground rents (if applicable) and Taxes with respect to the Property.

3.18 **Title to Collateral.** Each Borrower has good and marketable title to all of the Collateral it has pledged as security for the Loan, subject to no Lien, except Permitted Encumbrances which do not and will not materially interfere with the security intended to be provided by the Mortgage or the current use or operation of the Property and the Improvements or the current ability of the Facility to generate net operating income sufficient to service the Loan. All Improvements situated on the Property are situated wholly within the boundaries of the Property.

3.19 **Priority of Mortgages; Liens; Other Obligations.** The Mortgage constitutes a valid first lien against the real and personal property described therein, prior to all other liens or encumbrances, including those which may hereafter accrue, excepting only Permitted Encumbrances (as defined in Section 5.2 (No Liens; Exceptions)) which do not and will not materially and adversely affect (a) the ability of any Borrower to pay in full the principal of and interest on the Note when due, (b) the security (and its value) intended to be provided by the Mortgage, or (c) the current use of the Property and the Improvements. No Borrower nor any Guarantor is liable, primarily or secondarily, upon any Indebtedness other than as described in its financial statements or in the AR Loan Documents, or has any fixed or contingent obligation to make any loan or contribution of capital to any other entity that has not been fully paid. No Borrower nor any Guarantor owes any debt to its members, shareholders, partners or affiliates.

3.20 **Location of Chief Executive Offices.** The location of each Borrower's principal place of business and chief executive office is set forth on Exhibit B hereto.

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3.21 **Disclosure.** All information furnished or to be furnished by each Borrower to Lender in connection with the Loan or any of the Loan Documents, is, or will be at the time the same is furnished, accurate and correct in all material respects and complete insofar as completeness may be necessary to provide Lender with true and accurate knowledge of the subject matter.

3.22 **Trade Names.** No Borrower nor the Facility have changed their names, been known by any other name, or been a party to a merger, reorganization or similar transaction within the last five (5) years.

3.23 **ERISA.** To the Borrower's Knowledge, each Borrower is in compliance with all applicable provisions of the Employee Retirement Income Security Act of 1974, as amended ("**ERISA**").

3.24 **Ownership.** The ownership interests of the Persons comprising each Borrower and each of the respective interests in each Borrower as of the Closing Date is correctly and accurately set forth on Exhibit C, attached hereto.

3.25 **Proceedings Pending.** There are no proceedings pending, or, to the best of each Borrower's knowledge, threatened, to acquire any power of condemnation or eminent domain with respect to any part of the Property, or to enjoin or similarly prevent or restrict the use of any Property or the operation of the Facility in any manner.

3.26 **Compliance With Other Applicable Laws.** To the best of each Borrower's knowledge, each Property and Improvements comply with all covenants and restrictions of record and applicable laws, ordinances, rules and regulations, including, without limitation, all laws, ordinances, rules and regulations relating to zoning, setback requirements and building codes. No Improvements constitute a nonconforming structure and the operation of the Facility is not a nonconforming use under current zoning, and there are no waivers of any current building code requirements for the Property or Improvements. The Facility is in compliance in all material respects with the Americans With Disabilities Act and regulations thereunder and the Federal Housing Act and regulations thereunder, each to the extent applicable. Each Borrower agrees to indemnify and hold Lender harmless from any fines or penalties assessed or any corrective costs incurred by Lender if any Improvements or any Property, or any part thereof, is hereafter determined to be in violation of any covenants or restrictions of record or any applicable laws, ordinances, rules or regulations, and such indemnity shall survive any foreclosure or deed in lieu of foreclosure.

3.27 **Solvency.** Each Borrower is solvent for purposes of 11 U.S.C. §548, and the borrowing of the Loan will not render such Borrower insolvent for purposes of 11 U.S.C. §548. Neither of the Borrowers nor any of the Guarantors nor any of the Borrowers' principals, partners and/or members are involved in any bankruptcy, reorganization or insolvency proceeding.

3.28 **Lease Agreement.** The Operations Seller Lease Agreement is in full force and effect and, there are no defaults (either monetarily or non-monetarily) by the Operations Seller or Owner, as applicable, thereunder. Commencing on the Operations Closing

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Date, the Lease Agreement is in full force and effect and, there are no defaults (either monetarily or non-monetarily) by the Owner or Operator, as applicable, thereunder.

3.29 **Management Agreement.** The Operations Seller Management Agreement is in full force and effect and, there are no defaults (either monetarily or non-monetarily) by the Operations Seller or Management Company, as applicable, thereunder. Commencing on the Operations Closing Date, the Management Agreement is in full force and effect and, there are no defaults (either monetarily or non-monetarily) by the Operator or Management Company, as applicable, thereunder.

3.30 **Single Purpose Entity.** Each Borrower is a Single Purpose Entity.

3.31 **Fraudulent Conveyances.** No Borrower (a) has entered into this Agreement or any of the other Loan Documents with the actual intent to hinder, delay, or defraud any creditor, nor (b) has received reasonably equivalent value in exchange for its obligations under the Loan Documents. Giving effect to the transactions contemplated by the Loan Documents, the fair saleable value of each Borrower's assets exceeds and will, immediately following the execution and delivery of the Loan Documents, be greater than each Borrower's probable liabilities, including the maximum amount of its contingent liabilities or its debts as such debts become absolute and mature. Each Borrower's assets do not and, immediately following the execution and delivery of the Loan Documents will not, constitute unreasonably small capital to carry out its business as conducted or as proposed to be conducted. None of the Borrowers intend to, nor do they believe that they will, incur debts and liabilities (including, without limitation, contingent liabilities and other commitments) beyond their ability to pay such debts as they mature (taking into account the timing and amounts to be payable on or in respect of obligations of each Borrower).

3.32 **Trademarks, Patents and Other Rights.** Set forth in Schedule 3.32 is a list and brief description of all patents, patent rights, patent applications, trademarks, trademark applications, service marks, service mark applications, trade names and copyrights, and all applications for such which are in the process of being prepared, are owned by, or are registered in the name of either Borrower, or of which any Borrower is a licensor or licensee, or in which any Borrower has any right, and in each case a brief description of the nature of such right. Each Borrower owns or possesses adequate licenses or other rights to use all patents, patent applications, trademarks, trademark applications, service marks, service mark applications, trade names, copyrights, manufacturing processes, formulae, trade secrets, and know how (collectively, "**Trade Rights**") necessary or desirable to the conduct of its business as conducted and as proposed to be conducted. No claim is pending or, to the knowledge of either Borrower, threatened to the effect that the operations of either Borrower infringe upon or conflict with the asserted rights of any other Person under any Trade Rights, and, to the knowledge of either Borrower, there is no basis for any such claim (whether or not pending or threatened). No claim is pending or, to the knowledge of either Borrower, threatened to the effect that any such Trade Rights owned or licensed by either Borrower or which such Borrower otherwise has the right to use, is invalid or unenforceable by such Borrowers, and there is no known basis for any such claim (whether or not pending or threatened). All technical information developed by and belonging to each Borrower has been patented or has been kept confidential or has otherwise been established as a trade secret. Neither Borrower has granted or assigned to any other Person

any right to sell or produce the products or proposed products or provide the services or proposed services of Borrowers. No officer, director, equity-holder or employee of Borrower has an ownership interest in any of the trademarks, patents, or other rights set forth in Schedule 3.32.

3.33 **Proprietary Information of Third Parties.** To the knowledge of each Borrower, no third party has claimed or has any reason to claim that any Person employed by either Borrower has: (i) violated or may be violating any of the material terms or conditions of his or her employment, non-competition, or non-disclosure agreement with such third party; (ii) disclosed or may be disclosing or utilized or may be utilizing any trade secret or proprietary information or documentation of such third party; or (iii) interfered or may be interfering in the employment relationship between such third party and any of its current or former employees. To the knowledge of either Borrower, no third party has requested information from either Borrower that suggests that such a claim might be contemplated. To the knowledge of either Borrower, no Person employed by either Borrower has employed or proposes to employ any trade secret or any information or documentation proprietary to any former employer, and no Person employed by either Borrower

has violated any confidential relationship which such Person may have had with any third party in connection with the development or sale of any product or proposed product or the development or sale of any service or proposed service of either Borrower, and such Borrowers does not have any reason to believe there will be any such employment or violation. To the knowledge of either Borrower, none of the execution, delivery or performance of this Agreement, or the carrying on of the business of either Borrower as officers, employees, or agents by any officer, director, or key employee, or the conduct of the businesses of such Borrowers, will conflict with or result in a material breach of the terms, conditions, or provisions of, or constitute a default under any material contract, covenant, or instrument under which such Person is obligated.

3.34 **Insider Interests.** No present officer, director, equity holder or employee of, or supplier to, any Borrower: (i) owns, other than by virtue of a membership interest in a Borrower, directly or indirectly, in whole or in part, any of the properties used in the businesses of any Borrower; (ii) has received a loan or advance from either Borrower which is currently outstanding; (iii) has any obligation to make any loan to either Borrower other than as may be specifically contemplated by each Borrower's limited liability company operating agreement; or (iv) has any other business relationship with Borrowers other than in his, her or its capacity as an officer, director, equity holder or employee. No present officer, director, equity holder or employee of either Borrower owns, in whole or in part, directly or indirectly, any interest in excess of five percent (5%) in, or controls, or is an employee, officer, director, or partner of, or participant in, or consultant to, any corporation, association, partnership, limited partnership, joint venture, or other entity which is operating as a nursing facility or residential care facility within ten (10) miles of the Facility, of either Borrower.

3.35 **Fraud and Abuse.** Neither Borrower nor either Borrower's members, managers, officers, directors, or senior executives, or, to the knowledge of either Borrower, Persons who provide professional services under agreements with such Borrower, have engaged in any activities on behalf of or attributable to either Borrower which are prohibited under federal Medicare and Medicaid statutes, 42 U.S.C. § 1320a-7b, or the regulations promulgated pursuant to such statutes or related state or local statutes or regulations or which are prohibited by rules of professional conduct, including but not limited to the following: (i) knowingly and

willfully making or causing to be made a false statement or representation of a material fact in any application for any benefit or payment; (ii) knowingly and willfully making or causing to be made any false statement or representation of a material fact for use in determining rights to any benefit or payment; (iii) failing to disclose knowledge by a claimant of the occurrence of any event affecting the initial or continued right to any benefit or payment on its own behalf or on behalf of another, with intent to fraudulently secure such benefit or payment; (iv) knowingly and willfully soliciting or receiving any remuneration (including any kickback, bribe, or rebate), directly or indirectly, overtly or covertly, in cash or in kind or offering to pay such remuneration (a) in return for referring an individual to a Person for the furnishing or arranging for the furnishing of any item or service for which payment may be made in whole or in part by Medicare or Medicaid, or (b) in return for purchasing, leasing, or ordering or arranging for or recommending purchasing, leasing, or ordering any good, facility, service, or item for which payment may be made in whole or in part by Medicare or Medicaid, as applicable.

3.36 **Brokerage Commission.** Any brokerage commission or similar compensation amounts or fees due in connection with the purchase of the Property and in connection with the transactions contemplated hereby have been paid in full and any such commissions coming due in the future as related to any act of or on behalf of the Borrower will promptly be paid by Borrowers. Borrowers agree to and shall indemnify Lender from any liability, claims or losses (including reasonable attorneys' fees) incurred by Lender and arising by reason of any claim from any such brokerage commission that are the result of any action by or on behalf of the Borrowers. This provision shall survive the repayment of the Loan and shall continue in full force and effect so long as the possibility of such liability, claims or losses exists.

3.37 **Labor Matters.** As of the Closing Date, there are no strikes or other labor disputes pending or, to any Borrower's knowledge, threatened against Borrowers or any Guarantor. Hours worked and payments made to the employees of any Borrower and Guarantors have not been in violation of the Fair Labor Standards Act or any other applicable Law dealing with such matters. All payments due from Borrowers and Guarantors, or for which any claim may be made against any of them, on account of

wages and employee and retiree health and welfare insurance and other benefits have been paid or accrued as a liability on their books, as the case may be. The consummation of the transactions contemplated by this Agreement and the other Loan Documents will not give rise to a right of termination or right of renegotiation on the part of any union under any collective bargaining agreement to which it is a party or by which it is bound.

3.38 **No Litigation**. There is no action, suit, claim, investigation or proceeding pending against, or to any Borrower's knowledge threatened against or affecting any Borrower or the Facility.

3.39 **Post Closing Date Covenants**. Borrower warrants and covenants to provide or cause to be provided to Lender:

(i) On a date to occur within five months after the Closing Date, deliver all of the following to the Lender or AR Lender, as applicable (such date, the "**Operations Closing Date**"):

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- (a) Facility license in the name of the Operator;
  - (b) Medicare number for the Operator;
  - (c) Management Agreement, effective as of the Operations Closing Date;
  - (d) Lease Agreement, effective as of the Operations Closing Date;
  - (e) Assignment of Leases and Rents dated the Operations Closing Date;
  - (f) Subordination and Attornment Agreement dated the Operations Closing Date;
  - (g) Subordination and Assignment of Lease Agreement dated the Operations Closing Date;
  - (h) Subordination and Assignment of Management Agreement dated the Operations Closing Date; and
  - (i) Opinion of counsel dated the Operations Closing Date, addressing those matters required by Lender.
- (ii) No later than seven months after the Closing Date, a new Medicaid provider number for the Operator;
- (iii) Within ninety days of the Closing Date, a copy of the Certificate of Occupancy;
- (iv) Within ten Business Days after the Closing Date, deliver to Lender the executed Control Agreement;
- (v) Within ten Business Days after the Closing Date, deliver to Lender the executed ZBA Agreement.

**ARTICLE IV.  
AFFIRMATIVE COVENANTS OF BORROWERS**

Each Borrower, jointly and severally, agrees with and covenants unto the Lender that until the Loan Obligations have been paid in full, Borrowers shall:

4.1 **Payment of Loan/Performance of Loan Obligations.** Duly and punctually pay or cause to be paid the principal and interest of the Note in accordance with its terms and duly and punctually pay and perform or cause to be paid or performed all Loan Obligations hereunder and under the other Loan Documents.

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4.2 **Maintenance of Existence.** Maintain its existence as a limited liability company, and, in each jurisdiction in which the character of the property owned by it or in which the transaction of its business makes qualification necessary, maintain good standing.

4.3 **Maintenance of Single Purpose.** Maintain its existence as a Single Purpose Entity.

4.4 **Accrual and Payment of Taxes.**

(a) Borrowers shall pay, on or before the due date thereof, all Taxes, levies, license fees, permit fees and all other charges (in each case whether general or special, ordinary or extraordinary, or foreseen or unforeseen) of every character whatsoever (including all penalties and interest thereon) now or hereafter levied, assessed, confirmed or imposed on, or in respect of, or which may be a lien upon the Collateral or the Facility, or any part thereof, or any estate, right or interest therein, or upon the rents, issues, income or profits thereof, and shall submit to Lender such evidence of the due and punctual payment of all such Taxes, assessments and other fees and charges as may be required by law. Borrowers shall have the right before they become delinquent to contest or object to the amount or validity of any such Tax, assessment, fee or charge by appropriate legal proceedings, but this shall not be deemed or construed in any way as relieving, modifying or extending Borrowers' covenant to pay any such Tax, assessment, fee or charge at the time and in the manner provided herein, unless Borrowers have given prior written notice to Lender of Borrowers' intent to so contest or object, and unless (i) Borrowers shall demonstrate to Lender's satisfaction that the legal proceedings shall conclusively operate to prevent the sale of the Collateral and Facility, or any part thereof, to satisfy such Tax, assessment, fee or charge prior to final determination of such proceedings; and (ii) if required by Lender, Borrowers shall furnish a good and sufficient bond or surety as requested by and satisfactory to Lender in an amount sufficient to fully pay the contested amount, with penalties, interest and other charges if Borrowers should be unsuccessful in such contest; and (iii) Borrowers shall diligently pursue such contest.

(b) Borrowers shall pay, on or before the due date thereof, all Taxes, assessments, charges, expenses, costs and fees which may now or hereafter be levied upon, or assessed or charged against, or incurred in connection with, the Note, the Mortgage or any other Loan Documents.

(c) Operator shall pay, on or before the due date thereof, all rents and other payments due under the Lease Agreement; and Borrowers shall pay all utility charges with respect to the Collateral and Facility, or which may become a charge or lien against the Collateral and the Facility, for gas, electricity, water and sewer services and the like furnished to the Collateral or the Facility, and all other public or private assessments or charges of a similar nature affecting the Collateral or the Facility or any portion thereof, whether or not the nonpayment of same may result in a lien thereon. Borrowers shall submit to Lender such evidence of the due and punctual payment of all such premiums, charges and other sums as Lender may require.

(d) Borrowers shall not suffer any mechanic's, materialman's, laborer's, statutory or other lien (except as expressly permitted by this Agreement) to be created

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or remain outstanding against the Collateral or the Facility; provided, however, that Borrowers may contest any such lien in good faith by appropriate legal proceedings provided the lien is bonded off and removed as an encumbrance upon the Collateral or the Facility. Lender has not consented and will not consent to the performance of any work or the furnishing of any materials which might be deemed to create a lien or liens superior to the lien hereof.

(e) In the event of the passage of any state, federal, municipal or other governmental law, order, rule or regulation, subsequent to the date hereof, in any manner changing or modifying the laws now in force governing the taxation of mortgages or security agreements or debts secured thereby or the manner of collecting such Taxes so as to adversely affect Lender, Borrower will pay any such Tax on or before the due date thereof. If Borrowers fail to make such prompt payment or if, in the opinion of Lender, any such state, federal, municipal, or other governmental law, order, rule or regulation prohibits Borrowers from making such payment or would penalize Lender if Borrowers makes such payment or if, in the opinion of Lender, the making of such payment might result in the imposition of interest beyond the maximum amount permitted by applicable law, then the entire balance of the Loan Obligations shall, at the option of Lender, become immediately due and payable.

(f) Each Borrower hereby, jointly and severally, indemnifies and holds Lender harmless from any sales or use Tax that may be imposed on the Lender by virtue of Lender' s Loan to Borrowers.

(g) During each fiscal year, make accurate provision for the payment of all current tax liabilities of all kinds (including, without limitation, federal and state income taxes, franchise taxes, payroll taxes, provider taxes (to the extent necessary to participate in and receive maximum funding pursuant to Reimbursement Contracts) and Taxes, all required withholding of income taxes of employees, all required old age and unemployment contributions, and all required payments to employee benefit plans, and pay the same when they become due including, but not limited to, making all required deposits into an escrow fund (the "**Tax and Insurance Reserve Fund**") in accordance with the terms of the Tax and Insurance Escrow and Security Agreement.

4.5 **Insurance**. Maintain the following insurance coverages with respect to the Property and the Facility:

(a) **Property Insurance**. Insurance against loss or damage by fire, casualty and other hazards as now are or subsequently may be covered by an "all risk" policy or a policy covering "special" causes of loss, with such endorsements as Lender may from time to time reasonably require and which are customarily required by institutional lenders of similar properties similarly situated, including, without limitation, building, ordinance or law, lightning, windstorm, civil commotion, hail, riot, strike, water damage, sprinkler leakage, collapse, malicious mischief, explosion, smoke, aircraft, vehicles, vandalism, falling objects and weight of snow, ice or sleet, and covering the Facility in an amount equal to one hundred percent (100%) of the full insurable replacement value of the Facility (exclusive of footings and foundations below the lowest basement floor) without deduction for depreciation. The determination of the replacement cost amount shall be adjusted annually to comply with the requirements of the insurer issuing the coverage or, at Lender' s election, by reference to such indexes, appraisals or

information as Lender determines in its reasonable discretion, and, unless the insurance required by this paragraph shall be effected by blanket and/or umbrella policies in accordance with these terms, the policy shall include inflation guard coverage that ensures that the policy limits will be increased over time to reflect the effect of inflation. Each policy shall, subject to Lender' s approval, contain (i) a replacement cost endorsement, without deduction for depreciation, (ii) either an agreed amount endorsement or a waiver of any co-insurance provisions, and (iii) an ordinance or law coverage or enforcement endorsement if the Improvements or the use of the Property constitutes any legal nonconforming structures or uses, and shall provide for deductibles in such amounts as Lender may permit in its sole discretion. The property insurance policy shall not contain an exclusion endorsement for mold.

(b) Commercial General Liability Insurance. Commercial general liability insurance under a policy containing “Comprehensive General Liability Form” of coverage on an occurrence or claims made basis with retroactive date to prior occurrence form, which policy shall include, without limitation, coverage against claims for personal injury, bodily injury, death and property damage liability with respect to the Facility and the operations related thereto, whether on or off the Property, and the following coverages: Employee as Additional Insured, Employee Benefits, Product Liability/Completed Operations; Broad Form Contractual Liability, Independent Contractor, Personal Injury and Advertising Injury Protection, Medical Payment (with a minimum limit of \$5,000 per person), hired and non-owned automobile coverage (including rented and leased vehicles), and, if any alcoholic beverages shall be sold, manufactured or distributed in the Facility, liquor liability coverage, all of which shall be in such amounts as Lender may from time to time reasonably require, but not less than One Million Dollars (\$1,000,000) per occurrence, Three Million Dollars (\$3,000,000) in the aggregate. If such policy shall cover more than one property, such limits shall apply on a “per location” basis. If any elevators, health club facilities or swimming pools are located at the Facility at any time during the Loan, the foregoing amounts shall be increased to Three Million Dollars (\$3,000,000) and Five Million Dollars (\$5,000,000), respectively, unless other amounts are approved in writing by Lender in its sole discretion. Such liability policy shall delete the contractual exclusion under the personal injury coverage, if possible, and if available, shall include the following endorsements: Notice of Accident, Knowledge of Occurrence, and Unintentional Error and Omission. Absent written consent from Lender, Borrowers shall not change, cancel or renew the terms of such policy in any manner that would materially lessen the amount and scope of such insurance coverage applicable to the Property and Facility. The commercial general liability policy shall not contain an exclusion endorsement for mold.

(c) Professional Liability Insurance. Professional liability insurance, whenever possible provided by the same carrier as the Commercial General Liability coverage, in an amount equal to One Million Dollars (\$1,000,000) per occurrence and Three Million Dollars (\$3,000,000) in the aggregate and insuring Borrowers from acts occurring prior to the date of the Loan, unless other amounts are approved by Lender in writing at its sole discretion.

(d) Business Interruption Insurance/Extra Expense Coverage. Business interruption income insurance (i) covering the same perils of loss as are required to be covered by the property insurance described above, (ii) in an amount equal to the greater of: (1) the projected annual net income from the Facility plus carrying costs and extraordinary expenses of the Property for a period of twenty-four (24) months, based upon Borrower’s reasonable

estimate thereof as approved by Lender; provided, however, that if fifty-percent (50%) of the estimated annual expenses of the Facility is greater than such calculation of net income, then Borrowers shall, for purposes of this test, use such amount, or (2) or actual loss sustained, in either case with no cap, (iii) including either an agreed amount endorsement or a waiver of any co-insurance provisions, so as to prevent any Borrower, Lender and any other insured thereunder from being a coinsurer, and (iv) providing that any covered loss thereunder shall be payable to Lender.

(e) Construction Insurance. During the period of any new construction on the Property, a so-called “Builder’s All-Risk Completed Value” or “Course of Construction” insurance policy in non-reporting form for any improvements under construction, including, without limitation, for demolition and increased cost of construction or renovation, in an amount equal to one hundred percent (100%) of the estimated replacement cost value on the date of completion, including “soft cost” coverage, FF&E and Workers’ Compensation Insurance covering all persons engaged in such construction, in an amount at least equal to the minimum required by law. In addition, each contractor and subcontractor shall be required to provide Lender with a certificate of insurance for (i) Workers’ Compensation insurance covering all persons engaged by such contractor or subcontractor in such construction in an amount at least equal to the minimum required by law, (ii) General Liability insurance showing minimum limits of at least One Million Dollars (\$1,000,000) per occurrence and Two Million Dollars (\$2,000,000) in the aggregate, where Borrowers and Lender have additional insured status on a primary and non-contributory basis with both forms CG 2010 (ongoing operations) and CG 2037 (completed operations) or its equivalent including coverage for products and completed operations, (iii) Automobile Liability insurance showing minimum limits of at least One Million Dollars (\$1,000,000) covering all owned autos, hired and non-owned autos (including rented

and leased vehicles).and (iv) statutory Workers Compensation with Employers Liability limits of \$1,000,000 for each accident, each disease and each disease policy limit. Each contractor and subcontractor also shall cover Borrowers and Lender as an additional insured under hall liability policies (excluding Professional Liability, Workers Compensation & Employers Liability) and shall indemnify and hold Borrowers and Lender harmless from and against any and all claims, damages, liabilities, costs and expenses arising out of, relating to or otherwise in connection with its performance of such construction. Each contractor shall waive all rights of recovery and shall cause its insurance carriers to waive their subrogation rights against the Lender, Borrowers and affiliated entities, for damages covered by the insurance required.

(f) Boiler and Machinery Equipment Breakdown Coverage. If the Facility contains steam boilers, steam pipes, steam engines, steam turbines or other high pressure vessels, insurance covering the major components of the central heating, air conditioning and ventilating systems, boilers, other pressure vessels, high pressure piping and machinery, elevators and escalators, if any, and other similar equipment installed in the Improvements, in an amount equal to the coverage as defined under the Property Insurance, which policies shall insure against physical damage to and loss of occupancy and use of the improvements arising out of an accident or breakdown covered thereunder.

(g) Flood. If the Facility is located in a High Risk Flood Area, as defined by FEMA, flood coverage in the amount of \$1,000,000 is required. If the Facility is located in an area covered by the National Flood Insurance Program, the Borrowers shall carry

the maximum federal amount of \$500,000 and additionally will carry a Differences in Conditions policy.

(h) Wind and Hurricane Insurance. If the Facility is located in Wind Zone 3 or 4, there must be no policy restrictions with regard to “Wind”, “Windstorm”, “Hail”, “Named Storm” and “Hurricane”. Any restrictions in coverage and/or deductibles must be reviewed and approved by Lender.

(i) Earthquake Insurance. If the Facility is located in Seismic Zone 3 or 4, earthquake coverage must be obtained in an amount equal to the coverage as defined under the Property Insurance.

(j) Workers’ Compensation/Employer’ s Liability Insurance. Workers’ compensation insurance or other similar insurance which may be required by governmental authorities or applicable Legal Requirements in an amount at least equal to the minimum required by law, and employer’ s liability insurance with a limit of One Million Dollars (\$1,000,000) per accident and per disease per employee, and One Million Dollars (\$1,000,000) in the aggregate for disease arising in connection with the operation of the Property. If the Facility is located in a monopolistic state, a Stop Gap Endorsement must be added to the General Liability policy.

(k) Automobile Liability Insurance. Borrowers must obtain Automobile Liability Insurance coverage in the amount of \$1,000,000. If the Facility does not own any vehicles, then hired and non-owned automobile endorsement (including rented and leased vehicles) must be obtained.

(l) Term and Other Requirements. All insurance required under this Agreement must have a term of not less than one year and shall be in the form and amount and with deductibles as, from time to time, shall be acceptable to Lender in its sole discretion, under valid and enforceable policies issued by financially responsible insurers either licensed to transact business in the state where the Facility is located, or obtained through a duly authorized surplus lines insurance agent or otherwise in conformity with the laws of such state, with a (i) rating of not less than the fourth (4<sup>th</sup>) highest rating category by either Standard & Poor’ s Ratings Group, Duff & Phelps Credit Rating Co., Moody’ s Investors Service, Inc., Fitch Investors Service, Inc. or any successors thereto, or (ii) an A-V rating in Best’ s Key Rating Guide. Originals or certified copies of all insurance policies shall be delivered to and held by

Lender. All such policies shall name Lender as an additional insured, shall provide for loss payable solely to Lender and shall contain: (A) a standard “non-contributory mortgagee endorsement or its equivalent relating, inter alia, to recovery by Lender notwithstanding the negligent or willful acts or omissions of Borrowers and notwithstanding (1) occupancy or use of the Facility for purposes more hazardous than those permitted by the terms of such policy, (2) any foreclosure or other action taken by Lender pursuant to the Mortgage upon the occurrence of a default, or (3) any change in title or ownership of the Facility; and (B) a provision that such policies shall not be canceled or amended, including, without limitation, any amendment reducing the scope or limits of coverage, or failed to be renewed, without at least thirty (30) days prior written notice to Lender in each instance. With respect to insurance policies which require payment of premiums annually, not less than thirty (30) days prior to the expiration dates of the insurance policies

obtained pursuant to this Agreement, Borrowers shall pay such amounts; provided, however, to the extent Lender has required Borrowers to deposit funds in an escrow therefor, Borrowers shall instead fund such escrow, as directed by Lender. Not less than thirty (30) days prior to the expiration dates of the insurance policies obtained pursuant to this Agreement, originals or certified copies of renewals of such policies (or certificates evidencing such renewals) bearing notations evidencing the payment of premiums or accompanied by other evidence satisfactory to Lender of such payment, which premiums shall not be paid by Borrowers through or by any financing arrangement, shall be delivered by Borrowers to Lender. Borrowers shall carry separate insurance, concurrent in kind or form or contributing in the event of loss with any insurance required by this Section 4.5. If the limits of any policy required hereunder are reduced or eliminated due to a covered loss, Borrowers shall pay the additional premium, if any, in order to have the original limits of insurance reinstated, or Borrowers shall purchase new insurance in the same type and amount that existed immediately prior to the loss.

(m) Lender’s Right to Procure Insurance. If Borrowers fail to maintain and deliver to Lender the original policies and/or certificates of insurance required, Lender may, at its option, procure such insurance and Borrowers shall pay or, as the case may be, reimburse Lender for, all premiums thereon promptly, upon demand by Lender, with interest thereon at the Default Rate from the date paid by Lender to the date of repayment and such sum shall constitute a part of all obligations related to the Loan.

(n) Use of Blanket and Umbrella Policies. The insurance required may, at the option of Borrowers, be effected by blanket and/or umbrella policies issued to Borrowers or to an Affiliate of Borrowers covering the Facility and the properties of such Affiliate; provided that, in each case, the policies otherwise comply with the provisions of this Agreement and allocate to the Facility, from time to time, the coverage specified by this Agreement, without possibility of reduction or coinsurance by reason of, or damage to, any other property (real or personal) named therein. If the insurance required by this Agreement shall be affected by any such blanket or umbrella policies, Borrowers shall furnish to Lender original policies or certified copies thereof, with schedules attached thereto showing the amount of the insurance provided under such policies which are applicable to the Facility. Additionally, umbrella coverage of no less than Five Million Dollars (\$5,000,000) in the aggregate, will extend over General Liability, Professional Liability, Automobile Liability, and Employer’s Liability.

(o) Subrogation Rights. Neither Lender nor its agents or employees shall be liable for any loss or damage insured by the insurance policies required to be maintained under this Agreement; it being understood that (i) Borrowers shall look solely to their insurance company for the recovery of such loss or damage, (ii) such insurance company shall have no rights of subrogation against Lender, its agents or employees, and (iii) Borrowers shall use their best efforts to procure from such insurance company a waiver of subrogation rights against Lender. If, however, such insurance policies do not provide for a waiver of subrogation rights against Lender (whether because such a waiver is unavailable or otherwise), then Borrowers hereby agree, to the extent permitted by law and to the extent not prohibited by such insurance policies, to waive their respective rights of recovery, if any, against Lender, its agents and employees, whether resulting from any damage to the Facility, any liability claim in connection with the Facility or otherwise. If any such insurance policy shall prohibit Borrowers from

waiving such claims, then Borrowers must obtain from such insurance company a waiver of subrogation rights against Lender.

(p) Condemnation and Casualty Loss. In the event of condemnation or casualty loss, the entire award of insurance proceeds as a result thereof will be assigned to Lender with authorization, at Lender's option, to apply all or a portion thereof up to the outstanding principal balance of the Loan and to any other Loan Obligations or to release amounts in excess of such outstanding obligations related to the Loan to Borrowers, at Lender's option in its sole discretion.

(q) Use of Proceeds of Insurance or Condemnation. At its option, Lender agrees that Lender shall make the net proceeds of insurance or condemnation (after payment of Lender's reasonable costs and expenses) available to Borrowers for Borrowers' repair, restoration and replacement of the improvements on the Property, the equipment and the inventory damaged or taken on the following terms and subject to Borrowers' satisfaction of the following conditions:

- (i) The aggregate amount of all such proceeds shall not exceed the aggregate amount of all such Loan Obligations;
- (ii) At the time of such loss or damage and at all times thereafter while Lender is holding any portion of such proceeds, there shall exist no Default or Event of Default;
- (iii) The Improvements, Equipment, and Inventory for which loss or damage has resulted shall be capable of being restored to its preexisting condition and utility in all material respects with a value equal to or greater than that which existed prior to such loss or damage and such restoration shall be capable of being completed prior to the earlier to occur of (A) the expiration of business interruption insurance as determined by an independent inspector or (B) the Maturity Date;
- (iv) Within thirty (30) days from the date of such loss or damage Borrowers shall have given Lender a written notice electing to have the proceeds applied for such purpose;
- (v) Within sixty (60) days following the date of notice under the preceding subparagraph (c) and prior to any proceeds being disbursed to Borrowers, Borrowers shall have provided to Lender all of the following:
  - (A) complete plans and specifications for restoration, repair and replacement of the Improvements, Equipment and Inventory damaged to the condition, utility and value required by (a) above,

(B) if loss or damage exceeds \$50,000, fixed-price or guaranteed maximum cost bonded construction contracts for completion of the repair and restoration work in accordance with such plans and specifications,

(C) builder's risk insurance for the full cost of construction with Lender named under a standard mortgagee loss-payable clause,

(D) such additional funds as in Lender's reasonable opinion are necessary to complete such repair, restoration and replacement, and

- (E) copies of all permits and licenses necessary to complete the work in accordance with the plans and specifications;
- (vi) Lender may, at Borrowers' expense, retain an independent inspector to review and approve plans and specifications and completed construction and to approve all requests for disbursement, which approvals shall be conditions precedent to release of proceeds as work progresses;
- (vii) No portion of such proceeds shall be made available by Lender for architectural reviews or for any other purposes which are not directly attributable to the cost of repairing, restoring or replacing the Improvements, Equipment and Inventory for which a loss or damage has occurred unless the same are covered by such insurance;
- (viii) Borrowers shall diligently pursue such work and shall complete such work prior to the earlier to occur of the expiration of business interruption insurance or the Maturity Date;
- (ix) Each disbursement by Lender of such proceeds and deposits shall be funded subject to conditions and in accordance with disbursement procedures which a commercial construction lender would typically establish in the exercise of sound banking practices and shall be made only upon receipt of disbursement requests on an AIA G702/703 form (or similar form approved by the Lender) signed and certified by Borrowers and, if required by Lender, its architect and general contractor with appropriate invoices and lien waivers as required by Lender; and
- (x) Lender shall have a first lien and security interest in all building materials and completed repair and restoration work and in all fixtures and equipment acquired with such proceeds, and each Borrower shall, as applicable, execute and deliver such mortgages, deeds of trust, security

agreements, financing statements and other instruments as Lender shall request to create, evidence, or perfect such lien and security interest.

(r) Use of Insurance Proceeds to Set Off Loan Obligations. In the event and to the extent such proceeds are not required or used for the repair, restoration and replacement of the Improvements, Equipment and Inventory for which a loss or damage has occurred, or in the event Lender does not permit Borrowers to have the insurance proceeds applied to the restoration of the Improvements, Equipment, or Inventory, or, if the conditions set forth herein for such application are otherwise not satisfied, then Lender shall be entitled without notice to or consent from Borrowers to apply such proceeds, or the balance thereof, at Lender' s option either (i) to the full or partial payment or prepayment of the Loan Obligations (without premium) in the manner aforesaid, or (ii) to the repair, restoration and/or replacement of all or any part of such Improvements, Equipment and Inventory for which a loss or damage has occurred.

(s) Appointment as Attorney-in-Fact. Each Borrower appoints Lender as such Borrower' s attorney-in-fact to cause the issuance of or an endorsement of any insurance policy to bring Borrowers into compliance herewith and, as limited above, at Lender' s sole option, to make any claim for, receive payment for, and execute and endorse any documents, checks or other

instruments in payment for loss, theft, or damage covered under any such insurance policy; provided, however, in no event will Lender be liable for failure to collect any amounts payable under any insurance policy.

(t) Changes in Insurance Coverage. Lender acknowledges that certain coverage amounts described above may not be commercially reasonable or available to attain or maintain. Lender reserves the right in its sole discretion to approve lesser amounts of coverage or approve modifications to the required types of insurance. Notwithstanding the foregoing, if the Lender determines in its reasonable discretion based on its experience with the long term care industry, generally, that insurance coverage in excess of the amounts currently maintained by the Borrowers or on an “occurrence” basis or any other modification to the insurance requirements are necessary and are available for the Borrowers at premiums not materially in excess of the premiums then being paid by Borrowers, then Borrowers shall be obligated to procure coverage as determined by Lender.

(u) Other Insurance. Lender may require such other insurance coverages, in such amounts, and such other forms and endorsements, as may from time to time be required by Lender and which are customarily required by institutional lenders to similar properties in the state the Facility is located in, similarly situated, including, without limitation, coverages against other insurable hazards, which at the time are commonly insured against and generally available at commercially reasonable premiums.

(v) Escrow for Insurance. Borrowers shall deposit funds for payment of insurance premium in accordance with the Tax and Insurance Escrow and Security Agreement.

4.6 Financial and Other Information. Provide Lender the following financial statements and information on a continuing basis during the term of the Loan:

(a) Annual Financial Statements. Within ninety (90) days after the end of each fiscal year of the Facility, for each Borrower and Management Company, reviewed financial statements, and for AdCare Health Systems, Inc., audited financial statements (including a balance sheet, a cash flow statement and a statement of income and expenses for the reporting year) prepared by a nationally recognized accounting firm or independent certified public accountant acceptable to Lender and certified to by the respective financial officer as being true and correct.

(b) Annual Disclosure Certificate. Within thirty (30) days after the end of each fiscal year, an annual disclosure certificate in the form provided for in Exhibit D attached hereto certified by the chief financial officer of each Borrower.

(c) Quarterly Compliance Certificate. Within forty-five (45) days after the end of each fiscal quarter of the Facility, furnish to Lender a quarterly compliance certificate in the form attached hereto as Exhibit E certified by the chief financial officer of each Borrower.

(d) Quarterly Financial Statements. Within forty-five (45) days after the end of each fiscal quarter of the Facility, for each Borrower, the Management Company and any Corporate Guarantor, financial statements (including a balance sheet, cash flow statement and a statement of income and expenses for the reporting quarter) certified to by the respective financial officer as being true and correct.

(e) Monthly Financial Statements. Within thirty (30) days after the end of each month current financial statements for the Facility, prepared in accordance with GAAP consistently applied, which statements shall include a balance sheet, cash flow statement, a statement of income and expenses for the month then ended and a statement of the number of bed days available and the actual patient days incurred for the month, together with monthly census information of the Facility as of the end of such month in sufficient detail to show patient-mix on a daily average basis for such year through the end of such month, certified by a financial officer of each Borrower to be true and correct.

(f) Copies of Tax Returns. As soon as available, but in no event more than thirty (30) days after the filing deadline, as may be extended from time to time, copies of all federal, state and local tax returns of each Borrower and each Guarantor, together with all supporting documentation and required schedules.

(g) Copies of Medicare and Medicaid Cost Reports. As applicable, within ten (10) Business Days of filing or receipt, (i) all Medicaid and Medicare cost reports and any amendments thereto filed with respect to the Facility and all responses, audit reports, or other inquiries with respect to such cost reports and (ii) copies of all licensure and state and federal inspection reports, if applicable, with an attached plan of correction.

(h) Copies of Medicaid and Medicare Rate Calculation Worksheet. As applicable, within ten (10) Business Days of receipt, a copy of the Medicaid and Medicare Rate

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Calculation Worksheet (or the equivalent thereof) issued by the appropriate agency for the Facility.

(i) Copies of Downgrade Notices. Within three (3) days of receipt, any and all notices (regardless of form) from any and all licensing and/or certifying agencies that license the Facility and/or the Medicare and/or Medicaid certification of the Facility that the Facility is being downgraded to a substandard category, revoked, or suspended or that any such action is pending or being considered to downgrade to a substandard category, revoke or suspend the Facility's license.

(j) Evidence of Payment of Bed Taxes. Upon request by Lender, evidence of payment by Borrowers of any applicable provider bed taxes or similar taxes with respect to the Facility, which taxes Borrowers agree to pay or cause to be paid.

(k) Aged Accounts Receivable/Payable Report. Within thirty (30) days after the end of each calendar month, (i) an aged accounts receivable report of the Facility in sufficient detail to show amounts due from each class of unit or patient-mix (i.e., private, Medicare, Medicaid and V.A.) by the account age classifications of 30 days, 60 days, 90 days, 120 days, and over 120 days, (ii) monthly census information of the Facility in sufficient detail to show unit or patient mix on a daily average basis for such month and (iii) an accounts payable report of the Facility.

(l) Report Regarding Resident Days and Medicare or Medicaid Default Rate. As applicable, within ten (10) Business Days of receipt, a statement of the number of patient days for which the Facility has received the Medicare default rate for any applicable period. For purposes herein, "default rate" shall have the meaning ascribed to it in that certain Medicare or Medicaid rate notification letter prepared in connection with any review or survey of the Facility.

(m) Copies of Inspection Reports. Within ten (10) Business Days of receipt, copies of all licensure and state or federal inspection reports, if applicable, with attached plan of correction. Borrowers shall correct any deficiency on any report delivered pursuant to this Section 4.6 or otherwise received by Borrowers within the date required by the Health Regulatory Authority or other such government agency.

(n) Payment of Taxes and Insurance. Borrowers shall deliver to Lender on a monthly or quarterly basis (as determined by Lender in accordance with the requirements of the applicable taxing authorities) evidence that Borrowers have paid or caused to be paid all insurance premiums and all Taxes, charges, claims for labor, supplies, rent or other obligations which, if unpaid, might give rise to a Lien against the property of Borrowers (except Liens permitted by this Agreement), that were due and payable by Borrowers during such previous month or quarter, as the case may be (each a "**Tax and Insurance Report**").



(o) SBA Requirements. Within twenty (20) days after the end of each fiscal quarter, a completed SBA Form 468/Economic Data Portfolio Concern in the form attached hereto as Exhibit F and such other documents and agreements as may be required to be delivered to the Small Business Administration, all as directed by the Lender.

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(p) Insurance Captive. Within ninety (90) days after the end of each fiscal year, a loss run history on the entire insurance captive, if an insurance captive is utilized for the Facility.

(q) Independent Audit of Accounts Receivable. Upon Lender's request, but no often than once per year, and/or, upon an Event of Default, Borrowers shall submit the results of an audit of its accounts receivable and cash collections in form and substance acceptable to Lender, in Lender's sole discretion, and performed by an independent third party auditor approved by Lender, which audits will be performed at Borrowers' expense.

(r) Reports Regarding Claims. Within three (3) Business Days of being (a) presented with a claim or claims in an amount in excess of Fifty Thousand Dollars (\$50,000) against any insurance policy for the Facility related any facility under that policy or (b) presented with any claim against the Facility, a report and/or notice identifying the amount and related loss of such claim.

(s) Affiliates Facilities Reports. Should a health care facility owned by an Affiliate of any Borrower (whether or not financed by Lender or its Affiliate) be either decertified (or action taken in pursuance thereof) or is subject to a denial of new admissions, the Borrowers or the applicable Affiliate shall provide Lender with a written notice of such events.

(t) Accounts List. Within thirty (30) days after the end of each fiscal year, within five (5) Business Days of opening or closure of any account or upon Lender's request, deliver a comprehensive list of all bank accounts associated with any Borrower or the Facility and all subsidiaries thereof including, without limitation: (i) the designated number associated with each account; (ii) the name of the bank or financial institution where the account is held; and (iii) the type of account.

(u) Audited Financials. If not already required, the Lender reserves the right to require that the annual financial statements of each Borrower and the Management Company be audited and prepared by a nationally recognized accounting firm or independent certified public accountant acceptable to Lender, at Borrowers' respective cost and expense, if (i) an Event of Default has occurred or (ii) if Lender has reasonable grounds to believe that the unaudited financial statements do not accurately represent the financial condition of each Borrower, the Management Company or any Corporate Guarantor, as the case may be.

(v) Additional Information. Lender further reserves the right to require such other information of Borrowers, the Management Company, Guarantors and/or the Facility, in such form and at such other times (including monthly or more frequently) as Lender shall deem necessary, and Borrowers agree promptly to provide or to cause to be provided, such information to Lender.

(w) Statutory Rights. The provisions of this Section 4.6 shall not be in limitation of any rights which the Lender may have under any applicable law with respect to the books and records of the Borrowers or to inspect the Facility of to discuss its affairs, finances and accounts.

4.7 Reserved.

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4.8 **Books and Records.** Keep and maintain at all times at the Facility or the Management Company' s offices, and upon Lender' s request shall make available at the Facility, complete and accurate books of account and records (including copies of supporting bills and invoices) adequate to reflect correctly the results of the operation of the Facility, and copies of all written contracts, subleases (if any), and other instruments which affect the Property, which books, records, contracts, leases (if any) and other instruments shall be subject to examination and inspection at any reasonable time by Lender (upon reasonable advance notice, which for such purposes only may be given orally, except in the case of an emergency or following an Event of Default, in which case no advance notice shall be required); provided, however, that if an Event of Default has occurred and is continuing, Borrowers shall deliver to Lender upon written demand all books, records, contracts, subleases (if any) and other instruments relating to such Facility or its operation and Borrowers authorize Lender to obtain a credit report on Borrowers at any time at Borrowers' sole cost and expense.

4.9 **Payment of Indebtedness.** Duly and punctually pay or cause to be paid all other Indebtedness now owing or hereafter incurred by Borrowers in accordance with the terms of such Indebtedness, except such Indebtedness owing to those other than Lender which is being contested in good faith and with respect to which any execution against properties of Borrowers has been effectively stayed and for which reserves and collateral for the payment and security thereof have been established as determined by Lender in its sole discretion.

4.10 **Notice of Loss.** Immediately notify the Lender of any event causing a loss or depreciation in value of either Borrower' s assets in excess of \$10,000 or any Guarantor' s assets in excess of the amount required by their Guaranty Agreement and the amount of such loss or depreciation, except Borrowers shall not be required to notify Lender of depreciation in Equipment resulting from ordinary use thereof.

4.11 **Records of Accounts.** Maintain all records, including records pertaining to the Accounts of each Borrower, at the chief executive office of each Borrower as set forth in this Agreement.

4.12 **Conduct of Business.** Conduct the operation of the Facility at all times in a manner consistent with the level of operation of the Facility as of the date hereof, including without limitation, the following:

- (a) to maintain the standard of care for the patients of the Facility at all times at a level necessary to ensure quality care for the patients of the Facility in accordance with customary and prudent industry standards;
- (b) to operate the Facility in a prudent manner and in compliance with applicable laws and regulations relating thereto and cause all Permits, Reimbursement Contracts, and any other agreements necessary for the use and operation of the Facility or as may be necessary for participation in the Medicaid, Medicare or other applicable reimbursement programs to remain in effect without reduction in the number of licensed beds authorized for use in the Medicaid, Medicare or other applicable reimbursement programs;

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(c) to maintain sufficient Inventory and Equipment of types and quantities at the Facility to enable Borrowers adequately to perform operations of the Facility;

(d) to keep all Improvements and Equipment located on or used or useful in connection with the Facility in good repair, working order and condition, reasonable wear and tear excepted, and from time to time make all needed and proper repairs, renewals, replacements, additions, and improvements thereto to keep the same in good operating condition;

(e) to maintain sufficient cash in the operating accounts of the Facility in order to satisfy the working capital needs of the Facility and not to comingle funds of the Facility and the Borrowers with any other funds; provided, however, that

any cash or equity contributions shall not be deemed commingled funds and provided further, however, that any of such contributions that are deemed loans must be subject to a subordination agreement approved by the Lender; and

(f) to keep all required Permits current and in full force and effect.

4.13 **Minimum Financial Covenants.** Borrowers on a consolidated basis shall maintain the following:

(a) Current Ratio.

(i) Borrowers shall maintain a Current Ratio (as defined below) of 1.0 to 1.0 commencing at the end of the first fiscal quarter after the Closing Date and thereafter as tested on a quarterly basis at the end of each quarter for the term of the Loan; and

(ii) For the purposes of this Agreement, “**Current Ratio**” shall mean Current Assets divided by Current Liabilities. “**Current Assets**” shall mean, only with respect to the Facility, cash, accounts receivable aged less than 90 days (any other receivable in such calculation to be approved by Lender), inventory, marketable securities, prepaid expenses and other assets that can be converted to cash within one year, excluding, at the sole discretion of the Lender, accounts or Indebtedness due to or from Affiliates of the Borrowers. “**Current Liabilities**” shall mean, only with respect to the Facility, accounts payable, short term loans, expenses incurred but unpaid and other debts due within one year, excluding, at the sole discretion of the Lender, accounts or Indebtedness due to or from Affiliates of the Borrowers.

(b) Liquidity. Borrowers on a consolidated basis shall at all times during the term of the Loan maintain cash, or availability under a line of credit, including availability under the AR Loan and the Capitalized Interest Account, of no less than Two Hundred Fifty Thousand and no/100 Dollars (\$250,000.00).

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(c) If any Borrower fails to achieve or provide evidence of achievement of the Current Ratio for the Facility, provided there is no continuing Default or Event of Default under the Loan Documents and provided, further, that there has never been a default under Section 6.1(a) of this Agreement, Borrowers may deposit with Lender, at Borrowers’ option within thirty (30) days of such failure, additional cash or other liquid collateral in an amount which would have resulted in the noncomplying Current Ratio requirement having been satisfied. If after Borrowers have deposited such additional cash or liquid collateral, any Borrower again fails to achieve or provide evidence of the achievement of the Current Ratio for the Facility requirements set forth above and such failure continues for a second consecutive quarter, Borrowers may deposit with Lender, at Borrowers’ option within thirty (30) days of such failure, additional cash or other liquid collateral (with credit for amounts currently being held by Lender pursuant to the foregoing sentence), in an amount which would have resulted in the noncomplying Current Ratio requirement for such quarter having been satisfied. Borrowers shall not have the option to cure for failure to comply for any additional consecutive quarters and such an event will constitute an Event of Default under this Agreement. Any additional cash or liquid collateral deposited by Borrowers hereunder in order to achieve the required Current Ratio for the Facility and cure any existing default with respect thereto will be held by Lender in a standard custodial account and shall constitute additional collateral for the obligations related to the Loan and an “Account” as defined in this Agreement, and, upon the occurrence of a default, may be applied by Lender, in such order and manner as Lender may elect, to the reduction of the obligations related to the Loan. Borrowers shall not be entitled to any interest earned on such additional collateral. Provided that there is no outstanding Default or Event of Default, such additional collateral which has not been applied to the Loan Obligations will be released by Lender at such time as Borrowers provided Lender with evidence that the required minimum Current

Ratio requirement set forth above has been achieved and maintained (without regard to any cash or liquid collateral deposited pursuant to this section) for two (2) consecutive fiscal quarters.

Notwithstanding anything herein to the contrary, any additional liquid collateral posted by Borrowers under the AR Loan Agreement for purposes of satisfying this covenant, if the lender thereof is an Affiliate of the Lender, shall be deemed to satisfy the requirements herein.

Borrowers shall be required to supply Lender with a certificate evidencing compliance with the requirements of this Section, which certificate shall be signed by an officer or manager as appropriate.

#### 4.14 **Debt Service Coverage Requirements.**

(a) **Debt Service Coverage Ratio.** Borrowers on a consolidated basis shall maintain and provide evidence to Lender of the achievement of a Debt Service Coverage Ratio and Total Debt Service Coverage Ratio for the Facility of (i) not less than 1.00 to 1.00 as tested on a quarterly basis at the end of the first full fiscal quarter ending December 31, 2012 and the second fiscal quarter ending March 31, 2013, and thereafter, (ii) 1.15 to 1.00 as tested on a quarterly basis at the end of each quarter, beginning with the last day of the third fiscal quarter after the Closing Date and continuing thereafter for the term of the Loan. Borrowers may include any outstanding amounts in the Capitalized Interest Reserve Account in such calculations.

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This Debt Service Coverage Ratio and Total Debt Service Coverage Ratio will be measured as follows: (A) for a trailing three month period tested at the end of the first fiscal quarter following the Closing Date, (B) for the second fiscal quarter following the Closing Date and for a trailing six month period tested at the end of such quarter, (C) for the third fiscal quarter following the Closing Date, and for a trailing nine month period tested at the end of such quarter, and (iv) thereafter, tested quarterly and for a trailing twelve month period from the end of such quarter.

(b) If any Borrower fails to achieve or provide evidence of achievement of the Debt Service Coverage Ratio or Total Debt Service Coverage Ratio for the Facility, provided there is no continuing Default or Event of Default under the Loan Documents and provided, further, that there has never been a Default under Section 6.1(a) of this Agreement, Borrowers may deposit with Lender, at Borrowers' option within thirty (30) days of such failure, additional cash or other liquid collateral in an amount which would have resulted in the noncomplying Debt Service Coverage Ratio or noncomplying Total Debt Service Coverage Ratio requirement having been satisfied. If after Borrowers have deposited such additional cash or liquid collateral, any Borrower again fails to achieve or provide evidence of the achievement of the Debt Service Coverage Ratio or Total Debt Service Coverage Ratio for the Facility requirements set forth above and such failure continues for a second consecutive quarter, Borrowers may deposit with Lender, at Borrowers' option within thirty (30) days of such failure, additional cash or other liquid collateral (with credit for amounts currently being held by Lender pursuant to the foregoing sentence), in an amount which would have resulted in the noncomplying Debt Service Coverage Ratio or Total Debt Service Coverage Ratio requirement for such quarter having been satisfied. Borrowers shall not have the option to cure for failure to comply for any additional consecutive quarters and such an event will constitute an Event of Default under this Agreement. Any additional cash or liquid collateral deposited by Borrowers hereunder in order to achieve the required Debt Service Coverage Ratio or Total Debt Service Coverage Ratio for the Facility and cure any existing default with respect thereto will be held by Lender in a standard custodial account and shall constitute additional collateral for the obligations related to the Loan and an "Account" as defined in this Agreement, and, upon the occurrence of and during the continuance of an Event of Default, may be applied by Lender, in such order and manner as Lender may elect, to the reduction of the obligations related to the Loan. Borrowers shall not be entitled to any interest earned on such additional collateral. Provided that there is no outstanding Default or Event of Default, such additional collateral which has not been applied to the Loan Obligations will be released by Lender at such time as Borrowers provide Lender with evidence that the required minimum Debt Service Coverage Ratio and minimum Total Debt Service Coverage Ratio requirements set

forth above have been achieved and maintained (without regard to any cash or liquid collateral deposited pursuant to this section) for two (2) consecutive fiscal quarters.

Notwithstanding anything herein to the contrary, any additional liquid collateral posted by Borrowers under the AR Loan Agreement for purposes of satisfying this covenant, if the lender thereof is an Affiliate of the Lender, shall be deemed to satisfy the requirements herein.

Borrowers shall be required to supply Lender with a certificate evidencing compliance with the requirements of this Section, which certificate shall be signed by an officer

or manager as appropriate.

4.15 **Occupancy.** Starting with the quarter ending March 31, 2013, maintain or cause to be maintained, an average annual occupancy of the Facility as tested quarterly (on the basis of a fiscal year) of seventy percent (70%) or greater (based on 102 in-service beds).

4.16 **Capital Expenditures.**

(a) On the Closing Date, Borrowers shall establish with Lender a capital improvements reserve fund to pay for the completion, renovation or remediation of certain capital improvements identified by Lender as deferred maintenance costs for the Facility and to deposit other funds as described below (the “**Capital Improvements Reserve Fund**”).

(b) Commencing September 20, 2012 and during the term of the Loan, Borrowers shall deposit a monthly minimum annual capital expenditure equal to the Capital Improvements Reserve Requirement into the Capital Improvements Reserve Fund as provided for in the Capital Improvements Escrow and Security.

(c) Withdrawals from the Capital Improvements Reserve Fund may be made by Borrowers from time to time during the term of the Loan to cover ordinary repairs needed to maintain or improve the condition of the Facility or to cover repairs and replacements as required by professional building inspectors engaged by Lender all in accordance with the terms and conditions of the Capital Improvements Escrow and Security Agreement.

(d) In the event that any inspection report delivered during the term of the Loan indicates that repairs or replacements are necessary over and above the amount then held in the Capital Improvements Reserve Fund, Lender may require that additional funds be deposited in the Capital Improvements Reserve Fund to cover any such shortfall plus an amount determined by Lender to cover any cost overruns to complete such necessary improvements and/or repairs.

(e) Borrowers grant to Lender a right of setoff against all moneys in the Capital Improvements Reserve Fund, and Borrowers shall not permit any other Lien to exist upon such fund.

(f) Upon Borrowers’ failure to adequately maintain the Facility in good condition, Lender may, but shall not be obligated to, make such capital expenditures and may apply the moneys in the Capital Improvements Reserve Fund for such purpose. To the extent there are insufficient moneys in the Capital Improvements Reserve Fund for such purposes, all funds advanced by Lender to make such capital expenditures shall constitute a portion of the Loan Obligations, shall be secured by the Mortgage and shall accrue interest at the Default Rate until paid. Upon an Event of Default, Lender may apply any moneys in the Capital Improvements Reserve Fund to the Loan Obligations, in such order and manner as Lender may elect.

(g) All fees and costs associated with any inspections, reports, subsequent inspections and other matters set forth in this Section 4.16 shall be paid by Borrowers.

4.17 **Updated Appraisals; Inspections.**

(a) Appraisals. For so long as the Loan remains outstanding, if any Event of Default shall occur hereunder, or if, in Lender's judgment, a material depreciation in the value of the Property shall have occurred, then in any such event, Lender, may cause the Property to be appraised by an appraiser selected by Lender, and in accordance with Lender's appraisal guidelines and procedures then in effect, and Borrowers agree to cooperate in all respects with such appraisals and furnish to the appraisers all requested information regarding the Property and the Facility. Borrowers agree to pay all reasonable costs incurred by Lender in connection with such appraisal which costs shall be secured by the Mortgage and shall accrue interest at the Default Rate until paid.

(b) Inspection Fee. Borrowers shall pay to Lender an Inspection Fee equal to \$1,500 per year on each anniversary of the Closing Date during the term of the Loan (the "Inspection Fee").

(c) Access; Inspections. Borrowers shall authorize and permit Lender and its representatives (which term shall be deemed to include its independent accountants and counsel) to have reasonable access during normal business hours, upon reasonable notice and in such manner as will not unreasonably interfere with the conduct of business of Borrowers, to the Facility as Lender may from time to time reasonably request. Upon an Event of Default under the Loan Documents, Lender shall have access to the Facility at any hour without notice. Borrowers will agree to allow Lender or Lender's representative access to conduct inspections of the Facility upon reasonable notice to Borrowers. In cases of an emergency, Lender shall have the right to access the Facility to conduct inspections without notice. In addition to and not in substitution for Lender's rights under Section 4.8 (Books and Records), Borrowers agree to provide Lender, for any such inspection purposes, any data necessary for Lender to complete its inspection. Borrowers shall reimburse Lender for reasonable travel costs associated with one Facility visit per year.

(d) Reports. If any inspector's report indicates that repairs or replacements are necessary over and above such capital expenditure requirement, Lender shall require a non-interest bearing repair escrow fund to ensure completion of the repairs. The amount of any repair escrow shall be one hundred twenty five percent (125%) of the estimated cost of repairs as determined by the inspector and Lender. Lender also shall require an agreement satisfactory to Lender, which will provide for completion of the repairs and the disbursement of the escrow funds. All fees and costs associated with any inspection, any report and any subsequent inspections (if required) shall be paid by Borrowers.

(e) Clinical Inspection Fee for Facility. Borrowers shall pay to Lender the reasonable fees associated with a third party clinician that is engaged by Lender to inspect the Facility for clinical issues if the Facility's plan of correction following any survey is not approved after the first revisit or where the Facility has been decertified or given a Denial of Payment.

4.18 **Comply with Covenants and Laws.** Comply, in all material respects, with all applicable covenants and restrictions of record and all laws, ordinances, rules and

regulations and keep the Facility and the Property in compliance with all applicable laws, ordinances, rules and regulations, including, without limitation, the Americans with Disabilities Act and regulations promulgated thereunder, the Fair Housing Act and regulations thereunder, and laws, ordinances, rules and regulations relating to zoning, health, building codes, setback requirements, Medicaid and

Medicare laws and keep the Permits for the Facility in full force and effect (and if any material noncompliance is discovered during the term of the Loan, Borrowers will promptly remedy such noncompliance).

4.19 **Reserved.**

4.20 **Certificate.** Upon Lender' s written request, furnish Lender with a certificate stating that Borrowers have complied with and is in compliance with all terms, covenants and conditions of the Loan Documents to which Borrowers are a party and that there exists no Default or Event of Default or, if such is not the case, that one or more specified events have occurred, and that the representations and warranties contained herein are true and correct with the same effect as though made on the date of such certificate.

4.21 **Notice of Fees or Penalties.** Immediately notify Lender, upon Borrower' s knowledge thereof, of the assessment by any state or any Medicare, Medicaid, health or licensing agency of any fines or penalties against either Borrower or the Facility.

4.22 **Notice of Representations and Warranties.** Borrowers shall immediately notify Lender in writing, in the event any representation or warranty contained in the Loan Documents becomes untrue or there shall have been any material adverse change in any such representation or warranty.

4.23 **Lease Agreement; Management Agreement.**

(a) Maintain any lease agreement, any management agreement and any other services agreement, excluding those cancelable within thirty days or less than \$10,000 per annum (including, without limitation, the Operations Seller Lease Agreement, Lease Agreement, Operations Seller Management Agreement and Management Agreement) in full force and effect and timely perform all of its obligations thereunder and not permit the termination or amendment of such lease agreement, management agreement or other services agreement (including, without limitation, the Operations Seller Lease Agreement, Lease Agreement, Operations Seller Management Agreement and Management Agreement) or enter into any replacement or additional lease agreements, management agreements or other services agreements (including, without limitation, food service management agreements) unless the prior written consent of Lender is first obtained (which consent will not be unreasonably withheld and may be presumed a response in the affirmative if not received by the Borrowers within fifteen days of Lender' s receipt of the initial request for consent); provided, however, that Lender' s prior consent shall not be required for termination of any such lease agreement, management agreement or other services agreement (including, without limitation, the Operations Seller Lease Agreement, Lease Agreement, Operations Seller Management Agreement and Management Agreement) in the event of emergency situations (i.e., termination of the Facility' s license or decertification of the Facility from participation in Medicare and/or Medicaid) as set forth below;

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(b) In the event that proceedings are instituted to terminate the Facility' s license or to terminate the Facility' s Medicaid or Medicare certification, upon request of Lender immediately terminate any lease agreement, any management agreement or any other services agreement (including, without limitation, the Operations Seller Lease Agreement, Lease Agreement, Operations Seller Management Agreement and Management Agreement) relating to the Facility and engage oversight management services from a replacement lessee, management company or operator, as the case may be, reasonably acceptable to the Lender;

(c) In the event that bankruptcy or insolvency proceedings are instituted by or against the Operator, Management Company or Operations Seller, Owner shall (to the extent permitted by the applicable bankruptcy court having jurisdiction over such proceedings), upon written instruction received from Lender, to terminate any applicable lease agreement, management agreement or other services agreement (including, without limitation, the Operations Seller Lease Agreement, Lease Agreement, Operations Seller Management Agreement and Management Agreement);

(d) In the event that Borrowers fail to satisfy any covenants in the Loan Documents, Lender shall have the right, but not the obligation, to terminate any lease agreement, any management agreement and any other services agreement (including, without limitation, the Operations Seller Lease Agreement, Lease Agreement, Operations Seller Management Agreement and Management Agreement) and engage oversight management services and other relevant services from a replacement lessee, management company or operator, as the case may be, reasonably acceptable to Lender;

(e) In the event that at any time during the term of the Loan, any lessee, management company or operator materially defaults under the then applicable lease agreement, management agreement or other services agreement (including, without limitation the Operations Seller Lease Agreement, Lease Agreement, Operations Seller Management Agreement and Management Agreement) in effect (which default is not cured within the applicable cure period, if any) Borrowers shall terminate such lease agreement, management agreement or other services agreement (including, without limitation the Operations Seller Lease Agreement, Lease Agreement, Operations Seller Management Agreement and Management Agreement) and replace such lessee, management company or operator pursuant to a replacement lease agreement, management agreement or other services agreement in form and substance acceptable to Lender, within thirty (30) days of such material default; and

(f) In any instance where a replacement manager or operator is appointed by the Borrowers and/or Owner and/or Operator or Operations Seller, as applicable, or as required by the Lender, such replacement manager or operator shall be required to enter into a replacement Subordination and Assignment of Management Agreement, environmental indemnity agreement and/or Subordination and Assignment of Lease Agreement, as applicable, and any other agreement reasonably required by the Lender, in each instance in form and substance substantially similar to those same agreements executed on the Closing Date or the Operations Closing Date.

4.24 **Required Payment.** At any time upon: (i) a sale of twenty-five percent (25%) or more of the assets of either of the Borrowers (in a single transaction or a series of

transactions not in the ordinary course of business), (ii) a repayment in full of the AR Loan, or (iii) a Change in Control of any Borrower, the Loan shall be required to be prepaid in full with accrued interest plus the appropriate prepayment premium, as set forth in Section 6.3 (Default Rate) and Section 2.6 (Prepayment) at the option of Lender in its sole discretion; provided, however, that no prepayment penalty shall be required for a prepayment due to a Change in Control.

4.25 **Other Debt Agreements.** Maintain, and cause each Affiliate to maintain, compliance with the terms, covenants and conditions of the loan agreements, notes, mortgages, deeds of trust, security agreements, assignments and/or other documents and instruments evidencing or securing Indebtedness upon which such Person is obligated or which encumbers any property of such Person, including, without limitation, the AR Loan and all other Contemporary Debt.

4.26 **Access.** Borrowers shall authorize and permit Lender and its representatives (which term shall be deemed to include its independent accountants and counsel) to have reasonable access during normal business hours, upon reasonable notice and in such manner as will not unreasonably interfere with the conduct of business of Borrowers, to the Facility as Lender may from time to time reasonably request. Upon an Event of Default under the Loan Documents, Lender shall have access to the Facility at any hour without notice.

4.27 **USA Patriot Act Verification Information.** On the Closing Date, provide evidence of its legal name, tax identification number and street address, and, if either Borrower is an individual, a driver' s license and date of birth, satisfactory to and sufficient for Lender to verify the identity of such Borrower, as required under the USA Patriot Act. Each Borrower shall notify Lender, promptly, of any change to such information.



4.28 **Lien Searches.** Upon Lender's request and at Borrowers' sole cost and expense, deliver to Lender the results of complete lien and judgment searches for each Borrower or any Guarantor at the applicable county and at the Secretary of State's Office.

4.29 **License to Operate.** Maintain or cause to be maintained the required Facility licenses, Medicaid and Medicare Reimbursement Contracts and/or Permits at all times.

4.30 **Capitalized Interest Reserve Account.** Borrowers shall establish with Lender on the Closing Date, a capitalized interest reserve account (the "**Capitalized Interest Reserve Account**") in an amount equal to \$300,000 to pay Loan capitalized interest if and to the extent Facility revenues are insufficient therefore. Such funds shall be for the benefit of the AR Loan, as well, at the discretion of the Lender. Borrowers hereby grant to Lender a first Lien, subject to Permitted Encumbrances and AR Lender's second lien, security interest in such Capitalized Interest Reserve Account as Collateral for repayment of the Loan. Borrowers grant to Lender a right of setoff against all moneys in the Capitalized Interest Reserve Account and Borrowers shall not permit any other Lien, other than Permitted Encumbrances, to exist upon such fund. The Capitalized Interest Reserve Account shall be a non-interest bearing account. Borrowers may request disbursements from the Capitalized Interest Reserve Account by delivering to Lender in writing a notice to such effect. Lender may grant or deny any such disbursement request at its discretion; provided, however, that if there is an Event of Default

continuing or if there has ever been a monetary Event of Default, such monies shall be retained by Lender as additional security for the Loan and applied at the Lender's discretion. The Capitalized Interest Reserve Account shall terminate upon Stabilization and any monies remaining shall be used to prepay the Loan without prepayment premium.

4.31 **Loan-to-Value Ratio.**

(a) Borrowers on a consolidated basis shall maintain a Loan-to-Value Ratio of not more than eighty percent (80.00%) starting December 31, 2014 and continuing thereafter for the term of the Loan. This Loan-to-Value Ratio will be measured for a trailing twelve month period as tested at the end of each fiscal quarter starting December 31, 2014 and continuing to test at the end of each fiscal quarter thereafter for the term of the Loan.

(b) If Borrowers fail to maintain or provide evidence of maintaining the required Loan-to-Value Ratio for the Facility, provided there is no continuing Default or Event of Default under the Loan Documents and provided, further, that there has never been a Default under Section 6.1(a) of this Agreement, Borrowers may deposit with Lender, at Borrowers' option within thirty (30) days of such failure, additional cash or other liquid collateral in an amount which when added to the second number in the Loan-to-Value Ratio definition would have resulted in the noncomplying Loan-to-Value Ratio requirement having been satisfied. If after Borrowers have deposited such additional cash or liquid collateral, Borrowers again fail to achieve or provide evidence of the achievement of the Loan-to-Value Ratio requirements set forth above and such failure continues for a second consecutive quarter, Borrowers may deposit with Lender, at Borrowers' option within thirty (30) days of such failure, additional cash or other liquid collateral (with credit for amounts currently being held by Lender pursuant to the foregoing sentence), in an amount which when added to the second number in the Loan-to-Value Ratio definition would have resulted in the noncomplying Loan-to-Value Ratio requirement having been satisfied. Borrowers shall not have the option to cure for failure to comply for any additional consecutive quarters and such an event will constitute an Event of Default under this Agreement. Any additional cash or liquid collateral deposited by Borrowers hereunder in order to achieve the required Loan-to-Value Ratio for the Facility and cure any existing default with respect thereto will be held by Lender in a standard custodial account and shall constitute additional collateral for the obligations related to the Loan and an "Account" as defined in this Agreement, and, upon the occurrence of and during the continuance of an Event of Default, may be applied by Lender, in such order and manner as Lender may elect, to the reduction of the obligations related to the Loan. Borrowers shall not be entitled to any interest earned on such additional collateral. Provided that there is no outstanding Default or Event of Default, such

additional collateral which has not been applied to the Loan Obligations will be released by Lender at such time as Borrowers provide Lender with evidence that the required Loan-to-Value Ratio set forth above has been achieved and maintained (without regard to any cash or liquid collateral deposited pursuant to this section) for two (2) consecutive fiscal quarters.

**ARTICLE V.**  
**NEGATIVE COVENANTS OF BORROWERS**

Until the Loan Obligations have been paid in full, each Borrower jointly and severally agrees it shall not:

5.1 **Assignment of Licenses and Permits.** Assign or transfer any of its interest in any Permits or Reimbursement Contracts (including rights to payment thereunder) pertaining to the Facility, or assign, transfer, or remove or permit any other person to assign, transfer, or remove any records pertaining to the Facility including, without limitation, patient records, medical and clinical records (except for removal of such patient records as directed by the patients owning such records), without Lender's prior written consent, which consent may be granted or refused in Lender's sole discretion.

5.2 **No Liens; Exceptions.** Create, incur, assume or suffer to exist any Lien upon or with respect to the Facility or any of any Borrower's properties, rights, income or other assets relating thereto, including, without limitation, the Collateral, whether now owned or hereafter acquired, other than the following permitted Liens ("**Permitted Encumbrances**"):

- (a) Liens at any time existing in favor of the Lender or its Affiliates,
- (b) Liens which are listed in Exhibit G attached hereto,
- (c) Inchoate Liens arising by operation of law for the purchase of labor, services, materials, equipment or supplies, provided payment shall not be delinquent and, if such Lien is a lien upon any of the Property or Improvements, such Lien must be fully disclosed to Lender and bonded off and removed from the Property and Improvements, within thirty (30) days of its creation, in a manner satisfactory to Lender,
- (d) Liens incurred in the ordinary course of business in connection with workers' compensation, unemployment insurance or other forms of governmental insurance or benefits, or to secure performance of tenders, statutory obligations, leases and contracts (other than for money borrowed or for credit received with respect to property acquired) entered into in the ordinary course of business as presently conducted or to secure obligations for surety or appeal bonds, and
- (e) Liens for current year's taxes, assessments or governmental charges or levies provided payment thereof shall not be delinquent.
- (f) Liens in favor of AR Lender or any Contemporary Debt.

5.3 **Indebtedness and Other Obligations.**

(a) Incur or become obligated upon any other Indebtedness, secured or unsecured, or become obligated to make any capital contribution or loan to any other entity other than the following:

- (i) Indebtedness to Lender including Contemporary Debt;

- (ii) Indebtedness to AR Lender;
- (iii) Indebtedness to trade creditors in the ordinary course of business as reflected on the financial statements; and
- (iv) Accrued debt for current payroll taxes and similar taxes not yet due.

(b) Other than in accordance with the terms of the Subordination and Standstill Agreement, Borrowers will not permit any increase in the AR Loan or change in the interest rate (other than changes occurring automatically under a note having a floating rate as an index), payment terms or other material terms of any of such debt and will not enter into any agreement amending the documents evidencing such debt in any of the foregoing respects.

5.4 **Merger, Consolidation, Etc.** Consummate any Change in Control, merger, consolidation or similar transaction, or sell, assign, lease or otherwise dispose of substantially all of its assets (whether now or hereafter acquired), without the prior written consent of the Lender, which consent may be granted or refused in Lender' s sole discretion.

5.5 **Maintain Single-Purpose Entity Status.**

- (a) Borrowers shall not:
  - (i) engage in any business or activity other than the ownership, operation and maintenance of the Property and activities incidental thereto;
  - (ii) acquire or own any material assets other than (A) the Property, Facility, Equipment, General Intangibles, Accounts and Inventory, and (B) such incidental machinery, equipment, fixtures and other personal property as may be necessary for the operation of the Property;
  - (iii) fail to preserve its existence as a limited liability company, validly existing and in good standing (if applicable) under the laws of the jurisdiction of its organization or formation, or without the prior written consent of Lender, amend, modify, terminate or fail to comply with the provisions of its articles of organization, operating agreement or similar organizational document, as same may be further amended or supplemented, if such amendment, modification, termination or failure to comply would adversely affect its ability to perform its obligations hereunder, under the Note or any other document evidencing or securing the Loan;
  - (iv) incur any debt, secured or unsecured, direct or contingent (including guaranteeing any obligation), other than the

Loan and trade payables incurred in the ordinary course of business, provided same are paid when due;

- (v) fail to maintain its records, books of account and bank accounts separate and apart from those of its members and affiliates, the affiliates of any of its members, and any other person; and
- (vi) fail either to hold itself out to the public as a legal person separate and distinct from any other person or to conduct its business solely in its own name in order not (A) to mislead others as to the identity with which such other party is transacting business, or (B) to suggest that it is responsible for the debts of any third party (including any of its members or affiliates, or any general partner, principal or affiliate thereof).

5.6 **Dividends, Distributions and Redemptions.**

- (a) Except as otherwise consented to by Lender in writing, none of the Borrowers may declare or pay any dividends, or purchase, redeem, retire, or otherwise acquire for value, any of its membership interests or shares of capital stock, as the case may be, now or hereafter outstanding, or return any capital to its members (each a “**Distribution**”).
- (b) Notwithstanding the foregoing, the Borrowers may declare and pay Distributions quarterly provided that:
  - (1) the Borrowers have demonstrated satisfactory compliance, as determined by Lender in Lender’ s sole discretion, with all covenants of the Loan Documents,
  - (2) the Borrowers have demonstrated satisfactory compliance, as determined by Lender in Lender’ s sole discretion, with all financial covenants of the Loan Documents including that the Borrowers have maintained a Total Debt Service Coverage Ratio of 1.35 to 1.00 for two consecutive fiscal quarters immediately prior to any Distribution, provided, however, that if the Facility falls below such coverage requirements for any quarter after meeting the immediately provided for test, all Distributions shall cease until the Facility again meets such requirements for another two consecutive quarters,
  - (3) there has not existed a payment Event of Default on the Loan or the AR Loan;
  - (4) neither the Loan nor the AR Loan is in Default which Default has not been cured or waived;

- (5) the making of such Distribution would not cause an Event of Default on the Loan or the AR Loan;
- (6) at no time has the Lender accelerated the Loan,

otherwise there shall be no Distributions.

5.7 **Change of Business.** Make any material change in the nature of its business as it is being conducted as of the date hereof.

5.8 **Changes in Accounting.** Change its methods of accounting, unless such change is permitted by GAAP, and provided such change does not have the effect of curing or preventing what would otherwise be an Event of Default or Default had such change not taken place.

5.9 **ERISA Funding and Termination.** Permit (a) the funding requirements of ERISA with respect to any employee plan to be less than the minimum required by ERISA at any time, or (b) any employee plan to be subject to involuntary termination proceedings at any time.

5.10 **Transactions with Affiliates.** Unless previously approved by the Lender, enter into any transaction with a Person which is an Affiliate of any Borrower other than in the ordinary course of its business and on fair and reasonable terms no less favorable to Borrowers, than those they could obtain in a comparable arms-length transaction with a Person not an Affiliate.

5.11 **Transfer of Ownership Interests.** Permit a change in the Persons holding the ownership interests or capital stock of any Borrower unless the written consent of the Lender is first obtained, which consent may be granted or refused in Lender's sole discretion.

5.12 **Change of Use.** Alter or change the use of the Facility or permit to exist any management agreement for the Facility or enter into any operating lease for the Facility (other than the Lease Agreement, Operations Seller Lease Agreement, Operations Seller Management Agreement and Management Agreement), unless Borrowers first notify Lender and provide Lender a copy of the proposed lease agreement or management agreement, obtains Lender's written consent thereto, which consent may be withheld in Lender's sole discretion, and obtains and provides Lender with a subordination agreement in form satisfactory to Lender, as determined by Lender in its sole discretion, from such manager or lessee subordinating to all rights of Lender.

5.13 **Domicile and Place of Business.** Change its chief executive office or its principal place of business without first giving Lender at least thirty (30) days prior written notice thereof and promptly providing Lender such information and amendatory financing statements as Lender may request in connection therewith.

5.14 **Acquisitions.** Directly or indirectly, purchase, lease, manage, own, operate, or otherwise acquire any property or other assets (or any interest therein) which are not used in connection with the operation of the Facility.

5.15 **Change in Organizational Documents.** Permit any change in the articles of organization articles of incorporation, bylaws or operating agreement of any Borrower or the Management Company, as the case may be, without in each case the prior written consent of Lender, or permit the change in the manager or managing member of any Borrower or the Management Company, as the case may be, or the admission of any other manager or managing member of any Borrower or the Management Company, as the case may be.

5.16 **Facility Status.** Borrowers shall not close the Facility.

5.17 **Compliance With Anti-Terrorism Orders.** Borrowers will not permit the transfer of any interest in any Borrower to any person or entity (or any beneficial owner of such entity) who is listed on those certain lists referred to as the OFAC Lists developed in connection with the Anti-Terrorism Laws (the "OFAC Lists"). Borrowers will not knowingly enter into a lease with any party who is listed on the OFAC Lists. Borrowers shall immediately notify Lender if any Borrower has knowledge that any principal, or any member or beneficial owner of any Borrower or principal of any Borrower is listed on the OFAC Lists or is indicted on or arraigned and held over on charges involving money laundering or predicate crimes to money laundering. Borrowers shall immediately notify Lender if any Borrower knows that any tenant of the Facility is listed on the OFAC Lists, or is convicted on, pleads

nolo contendere to, is indicted on, or is arraigned and held over on charges involving money laundering or predicate crimes to money laundering.

5.18 **Involvement of Key Management.** Permit Christopher F. Brogdon to cease to be actively involved on a full time basis in the senior management of Borrowers or the Management Company, as the case may be, except with consent of Lender, which consent shall be given or withheld in its sole discretion, unless replaced by a replacement executive acceptable to Lender acting in good faith within sixty (60) days of such cessation.

5.19 **Intercompany Indebtedness Prohibited.** In addition to and not in substitution for the covenants and obligations set for in Article V and the Permitted Encumbrances set forth herein, except as noted in Schedule 5.19, no Borrower shall incur or become obligated upon any other Indebtedness, secured or unsecured, or become obligated to make any capital contribution or loan to any Affiliate of any Borrower, including, but not limited to (i) advancing or loaning funds, (ii) engaging in any actions that generate any accounts receivable due from and/or (iii) distribution of any funds of any Borrower to any other affiliate businesses of Borrowers or Guarantors which are not a Borrower hereunder, except as allowable under Section 5.6. Borrowers are prohibited from commingling Facility funds with any other funds not attributable to the Borrowers and/or the Facility.

## ARTICLE VI. EVENTS OF DEFAULT AND REMEDIES

6.1 **Events of Default.** The occurrence of any one or more of the following shall constitute an “**Event of Default**” hereunder:

(a) The failure by Borrowers to pay any installment of principal, interest, or other payments required under the Note, as and when due;

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(b) Either Borrower’ s violation of any covenant set forth in Section 3.39 (Post Closing Date Covenants), Section 4.24 (Required Payment), Section 4.29 (License to Operate) and Article V hereof;

(c) Either Borrower’ s or any Guarantor’ s failure to deliver or cause to be delivered the financial statements and information set forth in Section 4.6 (Financial and Other Information) within the times required, either Borrower’ s ability to maintain the financial covenants set forth in Section 4.13 (Minimum Financial Covenants), Section 4.14 (Debt Service Coverage Ratio Requirements) or Section 4.31 (Loan-To-Value Ratio) in the applicable period, or either Borrower’ s timely or proper performance or observance of the covenants set forth in Section 4.5 (Insurance), and such failure is not cured within thirty (30) days following Lender’ s written notice to Borrowers thereof;

(d) The failure of either Borrower properly and timely to perform or observe any covenant or condition set forth in this Agreement (other than those specified in this Section 6.1) or any other Loan Documents which is susceptible of being cured and is not cured within any applicable cure period as set forth herein or, if no cure period is specified therefor, is not cured within thirty (30) days of Lender’ s notice to Borrowers of such Default; provided, however, that if such default cannot be cured within such thirty (30) day period, such cure period shall be extended for an additional sixty (60) days, as long as Borrowers are diligently and in good faith prosecuting said cure to completion and as long as such extension is approved by Lender in its sole discretion;

(e) The filing by either Borrower or any Guarantor of a voluntary petition, or the adjudication of any of the aforesaid Persons, or the filing by any of the aforesaid Persons of any petition or answer seeking or acquiescing, in any reorganization, arrangement, composition, readjustment, liquidation, dissolution or similar relief for itself under any present or future federal, state or other statute, law or regulation relating to bankruptcy, insolvency or other relief for debtors, or if any of the aforesaid

Persons should seek or consent to or acquiesce in the appointment of any trustee, receiver or liquidator for itself or of all or any substantial part of its property or of any or all of the rents, revenues, issues, earnings, profits or income thereof, or the mailing of any general assignment for the benefit of creditors or the admission in writing by any of the aforesaid Persons of its inability to pay its debts generally as they become due;

(f) The entry by a court of competent jurisdiction of an order, judgment, or decree approving a petition filed against either Borrower or any Guarantor which such petition seeks any reorganization, arrangement, composition, readjustment, liquidation, dissolution or similar relief under any present or future federal, state or other statute, law or regulation relating to bankruptcy, insolvency, or other relief for debtors, which order, judgment or decree remains unvacated and unstayed for an aggregate of sixty (60) days (whether or not consecutive) from the date of entry thereof, or the appointment of any trustee, receiver or liquidator of any of the aforesaid Persons or of all or any substantial part of its properties or of any or all of the rents, revenues, issues, earnings, profits or income thereof which appointment shall remain unvacated and unstayed for an aggregate of sixty (60) days (whether or not consecutive);

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(g) Unless otherwise permitted hereunder or under any other Loan Documents, the sale, transfer, lease, assignment, or other disposition, voluntarily or involuntarily, of the Collateral, or any part thereof, or, except for Permitted Encumbrances as described in Section 5.2 (No Liens; Exceptions) above, any further encumbrance of the Collateral, unless the prior written consent of Lender is obtained, which consent may be withheld in Lender's sole discretion;

(h) The death or incompetence of any individual Guarantor or, if such Guarantor is a joint and several guarantor with a spouse, such Guarantor and spouse, unless replaced by a replacement Guarantor acceptable to Lender acting in good faith within four (4) months of such death or any legal determination of incompetence.

(i) Any certificate, statement, representation, warranty or audit heretofore or hereafter furnished by or on behalf of either Borrower or any Guarantor pursuant to or in connection with this Agreement (including, without limitation, representations and warranties contained herein or in any Loan Documents) or as an inducement to Lender to make the Loan to Borrowers, (i) proves to have been false in any material respect at the time when the facts therein set forth were stated or certified, (ii) proves to have omitted any substantial contingent or unliquidated liability or claim against either Borrower or any Guarantor, or (iii) on the date of execution of this Agreement there shall have been any materially adverse change in any of the acts previously disclosed by any such certificate, statement, representation, warranty or audit, which change shall not have been disclosed to Lender in writing at or prior to the time of such execution;

(j) The failure of either Borrower to correct within the time deadlines set by any applicable Medicare, Medicaid or licensing agency, any deficiency which would result in the following actions by such agency with respect to the Facility:

- (i) a termination of any Reimbursement Contract or any Permit; or
- (ii) a ban on new admissions generally or on admission of patients otherwise qualifying for Medicare or Medicaid coverage; or
- (iii) a ban on new beds, generally.

(k) Either Borrower or the Facility should be assessed fines or penalties by any state or any Medicare, Medicaid, health or licensing agency having jurisdiction over such Persons or the Facility in excess of \$10,000;

(l) A final judgment shall be rendered by a court of law or equity against either Borrower or any Guarantor in excess of \$10,000, and the same shall remain undischarged for a period of thirty (30) days, unless such judgment is either (i) fully covered by collectible insurance and such insurer has within such period acknowledged such coverage in writing, or (ii) although not fully covered by insurance, enforcement of such judgment has been effectively stayed, such judgment is being contested or appealed by appropriate proceedings and such Borrower or Guarantor, as the case may be, has established reserves adequate for payment

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in the event such Person is ultimately unsuccessful in such contest or appeal and evidence thereof is provided to Lender and such evidence is satisfactory as determined by Lender in its sole discretion;

(m) The occurrence of any "Event of Default" under any of the AR Loan Documents or any Contemporary Debt in existence on the date hereof;

(n) The occurrence of any material default that is not cured within any applicable cure period under any other deed to secure debt or related financing documents evidencing or securing debt with respect to the Facility;

(o) The occurrence of any materially adverse change in the financial condition or prospects of either Borrower or any Guarantor, or the existence of any other condition which constitutes a material impairment of any such Person's ability to operate the Facility or of such Person's ability to perform their respective obligations under the Loan Documents, which is not remedied within thirty (30) days after written notice;

(p) Borrowers shall execute (other than to Lender) any conditional bill of sale, chattel mortgage, security agreement or other security instrument covering any materials, fixtures, machinery, equipment, articles, and/or Personal Property intended to be incorporated in the Facility or the appurtenances thereto or placed in the Facility, or if a financing statement (for collateral greater than \$10,000 in value) giving notice of a security interest created under any such security instrument shall be filed, or if any of such materials, fixtures, machinery, equipment, articles, and/or Personal Property shall not be purchased so that the ownership thereof will vest unconditionally in Borrowers, free from encumbrances other than to Lender, on delivery at the Property, or if Borrowers shall not produce to Lender upon demand the contracts, bills of sale, statements, receipted vouchers or agreements, or any of them, under which Borrower claims title to any thereof; or

(q) Any survey, report or examination discloses that the Property or any portion thereof encroaches upon or projects over a street or upon or over adjoining property or violates any setback or other restriction, however created, or any building, zoning, subdivision, land-use, health, sanitation, or environmental protection ordinance, regulation or law of any Governmental Authority having jurisdiction over the Property or any other Legal Requirements; provided, however, that if such default cannot be cured within such thirty (30) day period, such cure period shall be extended for an additional sixty (60) days, as long as Borrowers are diligently and in good faith prosecuting said cure to completion and as long as such extension is approved by Lender.

Notwithstanding anything in this Section 6.1, all requirements of notice shall be deemed eliminated if Lender is prevented from declaring an Event of Default by bankruptcy or other applicable law. The cure period, if any, shall then run from the occurrence of the event or condition of Default rather than from the date of notice.

6.2 **Remedies.** In addition to other remedies under this Agreement, upon the occurrence of any one or more of the foregoing Events of Default, the Lender may, at its option:

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(a) Declare the entire unpaid principal of the Loan Obligations to be, and the same shall thereupon become, immediately due and payable, without presentment, protest or further demand or notice of any kind, all of which are hereby expressly waived; provided, however, if a Bankruptcy Default occurs, then all such amounts shall become immediately due and payable automatically without any election by the Lender; and/or

(b) Proceed to protect and enforce its rights by action at law (including, without limitation, bringing suit to reduce any claim to judgment), suit in equity and other appropriate proceedings including, without limitation, for specific performance of any covenant or condition contained in this Agreement; and/or

(c) Exercise any and all rights and remedies afforded by the laws of the United States, the states in which any of the Property or other Collateral is located or any other appropriate jurisdiction as may be available for the collection of debts and enforcement of covenants and conditions such as those contained in this Agreement and the Loan Documents; and/or

(d) Exercise the rights and remedies of setoff and/or banker's lien against the interest of Borrowers in and to every account and other property of either Borrower which is in the possession of the Lender or any person who then owns a participating interest in the Loan, to the extent of the full amount of the Loan; and/or

(e) Appoint a management company, in Lender's sole discretion, to assume and manage the business of the each Borrower, as such relates to the Facility secured by the Loan Documents; and/or

(f) Exercise its rights and remedies pursuant to any other Loan Documents; and/or

(g) All rights and remedies of Lender under the terms of this Agreement, the Note, any of the other Loan Documents, and any applicable statutes or rules of law shall be cumulative and may be exercised successively or concurrently; and/or

(h) If there is no control agreement for the Borrowers' accounts, require Borrowers and Borrowers' bank to enter into a control agreement, in a commercially reasonable form, allowing Lender to have control of the Borrowers' bank account or require Borrowers to immediately and for so long as such Event of Default or Default exists, sweep any monies in any other bank account of Borrowers into an account subject to a control agreement.

### 6.3 **Default Rate; Prepayment Premium.**

(a) In addition to and not in substitution for the penalties set forth in Section 6.3(b) and Section 6.3(c), upon the occurrence and during the continuance of any Event of Default, the Note Rate shall be increased by the Default Rate, at the option of Lender.

(b) In addition to and not in substitution for the penalties set forth in Section 6.3(a) and Section 6.3(c), if an Event of Default occurs and the Loan is declared to be

immediately due and payable, there shall be added to the principal balance of the Loan then due an amount equal to the prepayment premium, as set forth in Section 2.6.

(c) In addition to and not in substitution for the penalties set forth in Section 6.3(a) and Section 6.3(b), upon the occurrence of any Event of Default, Borrowers shall be liable to the Lender for all costs paid or incurred for the acquisition,

renovating, improving and/or equipping of the Facility, whether the same shall be paid or incurred pursuant to the provisions of this section or otherwise, and all payments made or liabilities incurred by the Lender hereunder or any kind whatsoever shall be secured by the Loan Documents and shall immediately become due and payable to the Lender without notice or demand and shall be paid by Borrowers to the Lender on demand, with interest thereon at the Default Rate to the date of payment..

6.4 **Standstill Remedy.** Upon the occurrence of any Event of Default, Lender shall have the right, but not the obligation, to issue to Borrowers a standstill notice (the “**Standstill Notice**”) which notice shall set forth any or all of the following provisions:

(a) Each Borrower, jointly and severally, covenants and agrees that after receipt of this Standstill Notice, without the prior written consent of Lender:

- (i) each Borrower’s business, including the Facility, will be conducted only in the ordinary course of business and in compliance with applicable laws, regulations, and contractual obligations;
- (ii) Neither Borrower will merge, amalgamate or consolidate with any corporation, or acquire all or substantially all of the business or assets of any other Person, business organization, entity or enterprise, or acquire ownership or control of any capital stock, bonds, or other securities of, or any property interest in, any business organization, entity or enterprise or acquire control of the management or policies thereof;
- (iii) Each Borrower shall not:
  - (A) enter into any transaction with or create or assume any obligation or liability to any Affiliate, agent or relative of any Borrower or such Affiliates;
  - (B) cancel or compromise any claim, except in the ordinary course of business, or waive any rights of substantial value;
  - (C) make any Tax election or settle or compromise any Tax liability;
  - (D) make any capital expenditures, except those made in the ordinary course of business which do not exceed \$10,000 in the aggregate;
  - (E) enter into or assume any contract, agreement or commitment which, by reason of its size, term or other factor, is not in the ordinary course of business;
  - (F) delay the payment of its accounts payable or take any actions to accelerate the payment of its accounts receivable; or
  - (G) take any action, or omit to take any action, which would have, or could reasonably be expected to have, a Material Adverse Effect.
- (iv) Each Borrower shall use its respective commercially reasonable efforts in a manner consistent with past practice to preserve the business organization of the Facility intact and

to keep available the services of the present employees and agents of the Facility and to preserve the good will of customers, suppliers, referral sources, employees, agents, third-party payors and others having business relations with the Facility;

- (v) Each Borrower shall use its respective reasonable efforts to maintain the Facility in good operating condition and repair, ordinary wear and tear excepted, and will maintain existing insurance coverage on the Facility as well as other existing insurance coverage;
- (vi) Each Borrower shall pay all registration, maintenance and renewal fees that are due or past due in connection with each item of Intellectual Property relating to the Facility; and

Upon receipt of the Standstill Notice, Borrowers shall comply with all of the provisions set forth herein.

## ARTICLE VII. MISCELLANEOUS

7.1 **Waiver.** No remedy conferred upon, or reserved to, the Lender in this Agreement or any of the other Loan Documents is intended to be exclusive of any other remedy or remedies, and each and every remedy shall be cumulative and shall be in addition to every other remedy given hereunder or now or hereafter existing in law or in equity. Exercise of or omission to exercise any right of the Lender shall not affect any subsequent right of Lender to exercise the same. No course of dealing between Borrowers and Lender or any delay on the Lender's part in exercising any rights shall operate as a waiver of any of the Lender's rights. No waiver of any Default under this Agreement or any of the other Loan Documents shall extend to or shall affect any subsequent or other then existing Default or shall impair any rights, remedies or powers of Lender.

7.2 **Costs and Expenses.** Borrowers will bear all taxes, fees, charges and expenses, including, but not limited to, in connection with the Loan, the Note, the preparation and servicing of this Agreement and the other Loan Documents (including any amendments hereafter made), and in connection with any modifications thereto after the Closing Date, the recording or re-recording of any of the Loan Documents, surveillance of the Borrowers' operations and evaluation of Lender's, Borrowers', or any Guarantor's respective rights, obligations, actions or in-actions under the Loan Documents, including, any waivers or consents, all (a) out of pocket expenses of Borrowers and Lender; (b) recording fees, recording taxes, intangibles taxes, documentary taxes or similar taxes; (c) title insurance premiums, (d) costs of third party reports, including, but not limited to, environmental, engineering, appraisal, survey, title report, lien search, inspections, drawing of papers, architects, and Engineers expenses and charges; (e) attorneys' fees of the Lender's counsel; (f) fees and expenses of consultants and advisors of Lender, including financial advisors; and (g) expenses related to the employment of watchmen to protect the Property from injury in the event that after request Borrowers do not provide such protection, the amount of which taxes, fees, charges and expenses shall constitute additional Loan Obligations of Borrowers to Lender payable on demand of Lender. If, at any time, a Default occurs or Lender becomes a party to any suit or proceeding in order to protect its interests or priority in any collateral for any of the Loan Obligations or its rights under this Agreement or any of the Loan Documents, or if Lender is made a party to any suit or proceeding by virtue of the Loan, this Agreement or any Collateral and as a result of any of the foregoing, Lender employs or engages counsel, consultants or other advisors to advise, consult or provide other representation with respect to the Loan Documents, or to collect the balance of the Loan Obligations, or to take any action in or with respect to any suit or proceeding relating to this Agreement, any of the other Loan Documents, any Collateral, Borrowers or any Guarantor or operator, or to protect, collect, or liquidate any of the security for the Loan Obligations, or attempt to enforce any security interest or lien granted to Lender by any of the Loan Documents, then in any such events, all of the reasonable attorney's fees, consultant fees, or other advisor fees arising from such services, including any fees for preparation of litigation and in any appellate or bankruptcy proceedings, and any expenses, costs and charges relating thereto shall constitute additional Loan Obligations of Borrowers to Lender payable on demand of Lender. Without limiting the foregoing, the Borrowers have undertaken the obligation for payment of, and shall pay, all recording and

filing fees, revenue or documentary stamps or taxes, intangibles taxes, and other taxes, expenses and charges payable in connection with this Agreement, any of

the Loan Documents, the Loan Obligations, or the filing of any financing statements or other instruments required to effectuate the purposes of this Agreement and any record searches, lien searches or other similar searches performed by Lender during the term of the Loan as determined by Lender to be necessary or appropriate, in its sole discretions, and should the Borrowers fail to do so, the Borrowers agree to reimburse Lender for the amounts paid by Lender, together with penalties or interest, if any, incurred by Lender as a result of underpayment or nonpayment. Such amounts shall constitute a portion of the Loan Obligations, shall be secured by the Mortgage and shall bear interest at the Default Rate (as defined in the Note) from the date advanced until repaid.

7.3 **Performance of Lender.** At its option, upon Borrowers' failure to do so, the Lender may make any payment or do any act on Borrowers' behalf that Borrowers or others are required to do to remain in compliance with this Agreement or any of the other Loan Documents, and Borrowers, jointly and severally, agree to reimburse the Lender, on demand, for any payment made or expense incurred by Lender pursuant to the foregoing authorization, including, without limitation, attorneys' fees, and until so repaid any sums advanced by Lender shall constitute a portion of the Loan Obligations, shall be secured by the Mortgage and shall bear interest at the Default Rate from the date advanced until repaid. Further, upon the occurrence and during the continuation of an Event of Default, Lender shall have the right to notify all account debtors to make payment directly to Lender until such time as (i) Lender has determined in its sole discretion, applied in good faith, that such Event of Default has been cured by Borrowers, (ii) Lender has waived such Event of Default, or (iii) all amounts due hereunder have been fully paid and discharged, whichever occurs first.

7.4 **Indemnification.** Borrowers shall, at their sole cost and expense, protect, defend, indemnify and hold harmless the Indemnified Parties from and against any and all claims, suits, liabilities (including, without limitation, strict liabilities), actions, proceedings, obligations, debts, damages, losses, costs, expenses, diminutions in value, fines, penalties, charges, fees, expenses, judgments, awards, amounts paid in settlement, punitive damages, foreseeable and unforeseeable consequential damages, of whatever kind or nature (including but not limited to reasonable attorneys' fees and other costs of defense) imposed upon or incurred by or asserted against Lender by reason of:

- (a) ownership of the Note, the Mortgage, the Property or any interest therein or receipt of any Rents (as defined in the Mortgage);
- (b) any amendment to, or restructuring of, the Loan Obligations and/or any of the Loan Documents;
- (c) any and all lawful action that may be taken by Lender in connection with the enforcement of the provisions of the Mortgage or the Note or any of the other Loan Documents, whether or not suit is filed in connection with same, or in connection with either Borrower, any Guarantor, and/or any partner, joint venturer, member or shareholder thereof becoming a party to a voluntary or involuntary federal or state bankruptcy, insolvency or similar proceeding;

(d) any accident, injury to or death of persons or loss of or damage to property occurring in, on or about the Property, the Improvements or any part thereof or on the adjoining sidewalks, curbs, adjacent property or adjacent parking areas, streets or ways;

(e) any use, nonuse or condition in, on or about the Property, the Improvements or any part thereof or on the adjoining sidewalks, curbs, adjacent property or adjacent parking areas, streets or ways;

- (f) any failure on the part of either Borrower or any Guarantor to perform or comply with any of the terms of this Agreement or any of the other Loan Documents;
- (g) any claims by any broker, person or entity claiming to have participated in arranging the making of the Loan evidenced by the Note;
- (h) any failure of the Property to be in compliance with any applicable laws;
- (i) any and all claims and demands whatsoever which may be asserted against Lender by reason of any alleged obligations or undertakings on its part to perform or discharge any of the terms, covenants, or agreements contained in the Lease Agreement, Operations Seller Lease Agreement or any replacement or renewal thereof or substitution therefor;
- (j) performance of any labor or services or the furnishing of any materials or other property with respect to the Property, the Improvements or any part thereof;
- (k) the failure of any person to file timely with the Internal Revenue Service an accurate Form 1099-b, statement for recipients of proceeds from real estate, broker and barter exchange transactions, which may be required in connection with the Mortgage, or to supply a copy thereof in a timely fashion to the recipient of the proceeds of the transaction in connection with which the Loan is made;
- (l) any misrepresentation made to Lender in this Agreement or in any of the other Loan Documents;
- (m) any tax on the making and/or recording of the Mortgage, the Note or any of the other Loan Documents;
- (n) the violation of any requirements of ERISA;
- (o) any fines or penalties assessed or any corrective costs incurred by Lender if the Facility or any part of the Property is determined to be in violation of any covenants, restrictions of record, or any applicable laws, ordinances, rules or regulations; or
- (p) the enforcement by any of the Indemnified Parties of the provisions of this Section 7.4.

Any amounts payable to Lender by reason of the application of this Section 7.4 shall become immediately due and payable, and shall constitute a portion of the Loan Obligations, shall be secured by the Mortgage and shall accrue interest at the Default Rate. The obligations and liabilities of Borrowers under this Section 7.4 shall survive any termination, satisfaction, assignment, entry of a judgment of foreclosure or exercise of a power of sale or delivery of a deed in lieu of foreclosure of the Mortgage. For purposes of this Section 7.4, the term “**Indemnified Parties**” means Lender and any Person who is or will have been involved in the origination of the Loan, any Person who is or will have been involved in the servicing of the Loan, any Person in whose name the encumbrance created by any of the Mortgage is or will have been recorded, any Person who may hold or acquire or will have held a full or partial interest in the Loan (including, without limitation, any investor in any securities backed in whole or in part by the Loan) as well as the respective directors, officers, shareholder, partners, members, employees, agents, servants, representatives, contractors, subcontractors, affiliates, subsidiaries, participants, successors and assigns of any and all of the foregoing (including, without limitation, any other Person who holds or acquires or will have held a participation or other full or partial interest in the Loan or the Property, whether during the term of

the Mortgage or as a part of or following a foreclosure of the Loan and including, without limitation, any successors by merger, consolidation or acquisition of all or a substantial portion of Lender's assets and business).

7.5 **Headings.** The headings of the Sections of this Agreement are for convenience of reference only, are not to be considered a part hereof, and shall not limit or otherwise affect any of the terms hereof.

7.6 **Survival of Covenants.** All covenants, agreements, representations and warranties made herein and in certificates or reports delivered pursuant hereto shall be deemed to have been material and relied on by Lender, notwithstanding any investigation made by or on behalf of Lender, and shall survive the execution and delivery to Lender of the Note and this Agreement.

7.7 **Notices, Etc.** Any notice or other communication required or permitted to be given by this Agreement or the other Loan Documents or by applicable law shall be in writing and shall be deemed received (a) on the date delivered, if sent by hand delivery (to the person or department if one is specified below) with receipt acknowledged by the recipient thereof, (b) three (3) Business Days following the date deposited in U.S. mail, certified or registered, with return receipt requested, or (c) one (1) Business Day following the date deposited with Federal Express or other national overnight carrier, and in each case addressed as follows:

If to Borrowers:

CSCC Property Holdings, LLC  
CSCC Nursing, LLC  
Two Buckhead Plaza  
3050 Peachtree Road NW, Suite 355  
Atlanta, Georgia 30305

with a copy to:

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Ellen W. Smith, Esq.  
Holt Ney Zatzoff & Wasserman, LLP  
100 Galleria Parkway, Suite 1800  
Atlanta, Georgia 30339  
Fax: (770) 956-1490

If to Lender:

Eric Smith  
Contemporary Healthcare Capital, LLC  
1040 Broad Street  
Suite 103  
Shrewsbury, New Jersey 07702

with a copy to:

Law Offices of Thomas K. Slattery, P.L.L.C.  
1250 24<sup>th</sup> Street NW, Suite 300  
Washington, DC 20037

Either party may change its address to another single address by notice given as herein provided, except any change of address notice must be actually received in order to be effective.

7.8 **Benefits.** All of the terms and provisions of this Agreement shall bind and inure to the benefit of the parties hereto and their respective successors and assigns. No Person other than Borrowers or Lender shall be entitled to rely upon this Agreement or be entitled to the benefits of this Agreement.

7.9 **Participation.** Borrowers acknowledge that Lender may, at its option, sell participation interests in the Loan or to other participating banks or Lender may (but shall not be obligated to) assign its interest in the Loan to its affiliates, or to other assignees (the “Assignee”). Borrowers agree with each present and future participant in the Loan or Assignee of the Loan that if an Event of Default should occur, each present and future participant or Assignee shall have all of the rights and remedies of Lender with respect to any deposit due from Borrowers. The execution by a participant of a participation agreement with Lender, and the execution by Borrowers of this Agreement, regardless of the order of execution, shall evidence an agreement between Borrowers and said participant in accordance with the terms of this Section 7.9.

7.10 **Supersedes Prior Agreements; Counterparts.** This Agreement and the instruments referred to herein supersede and incorporate all representations, promises, and statements, oral or written, made by Lender in connection with the Loan. This Agreement may not be varied, altered, or amended except by a written instrument executed by an authorized officer of the Lender. This Agreement may be executed in any number of counterparts, each of which, when executed and delivered, shall be an original, but such counterparts shall together constitute one and the same instrument.

7.11 **Loan Agreement Governs.** The Loan is governed by terms and provisions set forth in this Agreement and the other Loan Documents and in the event of any irreconcilable conflict between the terms of the other Loan Documents and the terms of this Agreement, the terms of this Agreement shall control; provided, however, in the event there is any apparent conflict between any particular term or provision which appears in both this Agreement and the other Loan Documents and it is possible and reasonable for the terms of both this Agreement and the Loan Documents to be performed or complied with then notwithstanding the foregoing both the terms of this Agreement and the other Loan Documents shall be performed and complied with.

7.12 **Construction of Provisions of this Agreement.** Lender has not agreed to make any loan other than that specifically described herein. All requirements herein shall be deemed material to Lender. Except as specified herein, all conditions and requirements must be satisfied by Borrowers prior to the Closing Date. Whenever any of the Loan Documents refers to a matter being “satisfactory” to Lender, subject to Lender’s “approval” or “consent,” at Lender’s “option,” at Lender’s “determination,” “required” by Lender, may be “granted” or “denied” at Lender’s “request,” as Lender shall “deem necessary,” or similar terminology, it is deemed that each of the aforesaid shall be in the sole discretion of the Lender (except as otherwise expressly provided), and if any term or condition requires Lender’s approval, consent, or satisfaction (the “Lender’s Approval”), the Lender’s Approval shall not be implied, but shall be evidenced only by a written notice from Lender specifically addressed to the particular requirement or condition and expressing Lender’s Approval. If “Borrower” or “Guarantor” consists of more than one Person, all obligations of Borrowers or Guarantors are joint and several and all references herein to “Borrower” or “Guarantor” shall apply both individually to each Person and in the alternative to all of them collectively, whether or not so stated.

7.13 **Advertising.** Borrowers acknowledge and agree that Lender is authorized to state in advertising or other press releases the fact that the type and amount of financing contemplated under the Loan Documents has been provided to Borrowers and Guarantor for the Facility by Lender. Lender agrees not to include any confidential information of the Borrowers or any Guarantor in such advertisements.

7.14 **CONTROLLING LAW.** THE PARTIES HERETO AGREE THAT THE VALIDITY, INTERPRETATION, ENFORCEMENT AND EFFECT OF THIS AGREEMENT AND THE OTHER LOAN DOCUMENTS SHALL BE GOVERNED BY, AND CONSTRUED IN ACCORDANCE WITH, THE LAWS OF THE STATE OF NEW JERSEY AND THE PARTIES HERETO SUBMIT (AND WAIVE ALL RIGHTS TO OBJECT) TO NON-EXCLUSIVE PERSONAL JURISDICTION IN THE STATE OF NEW JERSEY, FOR THE ENFORCEMENT OF ANY AND ALL OBLIGATIONS UNDER THIS AGREEMENT AND THE OTHER LOAN DOCUMENTS EXCEPT THAT IF ANY SUCH ACTION OR PROCEEDING ARISES UNDER THE CONSTITUTION, LAWS OR TREATIES OF THE UNITED STATES OF AMERICA, OR IF THERE IS A DIVERSITY OF CITIZENSHIP BETWEEN THE PARTIES THERETO, SO THAT IT IS TO BE BROUGHT IN A UNITED STATES DISTRICT COURT, IT SHALL BE BROUGHT IN THE UNITED STATES DISTRICT COURT FOR THE DISTRICT OF NEW JERSEY OVER SHREWSBURY, NEW JERSEY OR ANY SUCCESSOR FEDERAL COURT HAVING ORIGINAL JURISDICTION.

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7.15 **WAIVER OF JURY TRIAL.** EACH BORROWER HEREBY WAIVES ANY RIGHT THAT IT MAY HAVE TO A TRIAL BY JURY ON ANY CLAIM, COUNTERCLAIM, SETOFF, DEMAND, ACTION OR CAUSE OF ACTION (A) ARISING OUT OF OR IN ANY WAY RELATED TO THIS AGREEMENT, THE OTHER LOAN DOCUMENTS OR THE LOAN, OR (B) IN ANY WAY CONNECTED WITH OR PERTAINING OR RELATED TO OR INCIDENTAL TO ANY DEALINGS OF LENDER AND/OR BORROWERS WITH RESPECT TO THE LOAN DOCUMENTS OR IN CONNECTION WITH THIS AGREEMENT OR THE EXERCISE OF ANY PARTY' S RIGHTS AND REMEDIES UNDER THIS AGREEMENT OR OTHERWISE, OR THE CONDUCT OR THE RELATIONSHIP OF THE PARTIES HERETO, IN ALL OF THE FOREGOING CASES WHETHER NOW EXISTING OR HEREAFTER ARISING AND WHETHER SOUNDING IN CONTRACT, TORT OR OTHERWISE. EACH BORROWER AGREES THAT LENDER MAY FILE A COPY OF THIS AGREEMENT AND WILL BE ABLE TO FILE A COPY OF ALL LOAN DOCUMENTS WITH ANY COURT AS WRITTEN EVIDENCE OF THE KNOWING, VOLUNTARY, AND BARGAINED AGREEMENT OF EACH BORROWER IRREVOCABLY TO WAIVE ITS RIGHTS TO TRIAL BY JURY AS AN INDUCEMENT OF LENDER TO MAKE THE LOAN, AND THAT, TO THE EXTENT PERMITTED BY APPLICABLE LAW, ANY DISPUTE OR CONTROVERSY WHATSOEVER (WHETHER OR NOT MODIFIED HEREIN) BETWEEN BORROWERS AND LENDER SHALL INSTEAD BE TRIED IN A COURT OF COMPETENT JURISDICTION BY A JUDGE SITTING WITHOUT A JURY.

7.16 **Joint and Several Obligations.** All obligations of Borrowers hereunder are joint and several. All obligations of each Guarantor under the Loan Documents are joint and several. The use of the phrases "either Borrower" or "each Borrower" or "any Guarantor" in some sentences herein is for clarity only; the failure to use such phrases elsewhere shall not alter the fact that each reference to either Borrower and any Guarantor hereunder is intended to mean each party included within such defined term, both jointly and severally.

7.17 **Time is of the Essence.** Time is of the essence of the Loan Documents and of each provision hereof.

7.18 **Seniority; Subordination.** Notwithstanding anything to the contrary contained in this Agreement, the indebtedness, rights, remedies and obligations evidenced hereby are senior and/or subordinate, if at all, in the manner and to the extent set forth in the Subordination and Standstill Agreement and each signatory hereto shall be bound by the provisions of the Subordination and Standstill Agreement.

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**IN WITNESS WHEREOF**, Borrowers and the Lender have caused this Agreement to be properly executed, by their respective duly authorized representatives, as of the date first above written.

**BORROWERS:**

**CSCC PROPERTY HOLDINGS, LLC**, a Georgia limited liability company

By: /s/ Christopher F. Brogdon

Name: Christopher F. Brogdon

Title: Manager

**CSCC NURSING, LLC**, a Georgia limited liability company

By: /s/ Christopher F. Brogdon

Name: Christopher F. Brogdon

Title: Manager

**LENDER:**

**CONTEMPORARY HEALTHCARE SENIOR LIEN FUND I, L.P.**, a Delaware limited partnership

By: CHSL-GP, LLC,  
a Delaware limited liability company

Its: General Partner

By: /s/ Eric Smith

Eric Smith, Member

SIGNATURE PAGE TO LOAN AGREEMENT – ADCARE - SENIOR

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## LOAN AGREEMENT

**THIS LOAN AGREEMENT** (this “**Agreement**”) is made as of August 17, 2012, by and among **CSCC PROPERTY HOLDINGS, LLC**, a Georgia limited liability company (“**Owner**”) and **CSCC NURSING, LLC**, a Georgia limited liability company (“**Operator**”) and together with the Owner and with their respective successors and assigns, being collectively referred to herein as, the “**Borrowers,**” and each, a “**Borrower**”), and **CONTEMPORARY HEALTHCARE FUND I, L.P.**, a Delaware limited partnership (together with its successors and assigns, the “**Lender**”).

### RECITALS

**WHEREAS**, Borrowers have requested that Lender make a loan to Borrowers in the principal sum of \$600,000.

**WHEREAS**, Lender has agreed to make such loan on the terms and conditions hereinafter set forth.

### AGREEMENT

**NOW, THEREFORE**, it is hereby agreed as follows:

#### ARTICLE I.

##### DEFINITIONS, ACCOUNTING PRINCIPLES, UCC TERMS.

1.1 **Definitions.** As used in this Agreement, the following terms shall have the following meanings unless the context hereof shall otherwise indicate:

“**Accounts**” means all accounts arising from the business of each of the Borrowers, and all rights to payment from patients, residents, private insurers, and others arising from the business of each of the Borrowers, including rights to payment pursuant to Reimbursement Contracts, including rights to payment from Medicare and Medicaid programs or similar state or federal programs, boards, bureaus or agencies. “Accounts” shall also include the proceeds thereof (whether cash or noncash, moveable or immoveable, tangible or intangible) received from the sale, exchange, transfer, collection or other disposition or substitution thereof and any amounts deposited with Lender pursuant to Sections 4.13 and 4.14 and any reserve account required hereunder.

“**Account Debtor**” means “account debtor,” as defined in Article 9 of the UCC, and any other obligor in respect of an Account.

“**Advance**” shall have the meaning given such term in Section 2.1(c).

“**Advance Rate**” shall be 80% as applied to the Borrowing Base as defined below.

“**Affiliate**” shall mean, with respect to any Person, (a) each Person that controls, is controlled by or is under common control with such Person, (b) each Person that, directly or indirectly, owns or controls, whether beneficially or as a trustee, guardian or other fiduciary, any of the Stock of such Person, and (c) each of such Person’s officers, directors, members, joint venturers and partners.

“**Anti Terrorism Laws**” shall mean any Laws relating to terrorism or money laundering, including Executive Order No. 13224 (effective September 24, 2001), the United States Patriot Act, the laws comprising or implementing the Bank Secrecy Act, and the laws administered by OFAC.

“**Application Fee**” shall have the meaning set forth in Section 2.9.

“**Assignee**” shall have the meaning set forth in Section 7.9.

“**Assignment and Pledge Agreement**” shall have the meaning set forth in Section 2.2(b)(iii).

“**Assumed Management Fees**” shall mean five percent (5%) of total revenues net of contractual adjustments.

“**Bankruptcy Default**” means an Event of Default pursuant to Section 6.1(e) or Section 6.1(f) of this Agreement.

“**Borrower**” or “**Borrowers**” has the meaning set forth in the introductory paragraph of this Agreement.

“**Borrower Environmental Indemnity Agreement**” shall have the meaning set forth in Section 2.2(c)(v) of this Agreement.

“**Borrowing Base**” shall mean the product of: (i) net billings outstanding less Ineligible Accounts Receivable, times (ii) the Liquidity Factor, times (iii) the Advance Rate.

“**Borrowing Base Certificate**” means the certificate attached as Exhibit I.

“**Business Day**” means a day, other than Saturday or Sunday and legal holidays, when the Lender or national banks in New Jersey are open for business.

“**Capital Improvements Escrow and Security Agreement**” shall have the meaning set forth in Section 2.2(b)(v).

“**Certificate of Occupancy**” shall mean a final and unconditional Certificate of Occupancy (or its equivalent) permitting the lawful occupancy of the Facility from the appropriate Governmental Authority having jurisdiction over the Property.

“**Change in Control**” shall mean (i) a merger or consolidation of either of the Borrowers where any of the Borrowers, as the case may be, is not the surviving entity, or if it is the surviving entity, such transaction resulted in a change in its governing body, such that a majority of the individuals who comprise the governing body immediately prior to such transaction (or series of related transactions) do not constitute a majority of the governing body after such transaction, (or if such individuals continue to constitute a majority of the governing body the transaction vested in another person(s) and/or entity(ies) any super-majority voting rights); (b) a cumulative change in the ownership of a Borrower exceeding, on a fully diluted basis and on an as if converted basis, twenty five percent (25%) of the equity interest issued and outstanding at the Closing Date; (c) the termination of employment or any material change in the duties and responsibilities of Christopher F. Brogdon or the material failure to perform his duties, as determined by the Lender; or (d) any change of the “Manager,” as defined in each of the Borrower’ s operating agreements, as designated as of the date hereof.

“**Chattel Paper**” shall mean all chattel paper, as that term is defined in Article 9 of the UCC, and includes, without limitation, a record or records (including, without limitation, electronic chattel paper) which evidence both a monetary obligation and a security interest in specific goods, a security interest in specific goods and software used in the goods, or a lease of specific goods; all

Supporting Obligations (as defined below) with respect thereto; any returned, rejected or repossessed goods and software covered by any such record or records and all proceeds (in any form including, without limitation, accounts, contract rights, documents, chattel paper, instruments and general intangibles) of such returned, rejected or repossessed goods; and all proceeds (Cash proceeds and non-cash proceeds) of the foregoing, whether now or hereafter held by any Borrower.

“**Closing Date**” shall have the meaning set forth in Section 2.1(b).

“**Closing Fee**” shall have the meaning set forth in Section 2.9.

“**Closing Statement**” means the Lender’s Closing Statement dated the date hereof, executed by the Borrowers and the Lender.

“**Collateral**” means, collectively, all collateral assigned, hypothecated, pledged, or otherwise granted to Lender under the Loan Documents all whether now owned or hereafter acquired, including replacements, additions, accessions, substitutions, and products thereof and thereto, and all other property which is or hereafter may become subject to a Lien in favor of Lender as security for any of the Loan Obligations.

“**Contemporary Debt**” shall mean any indebtedness now or hereafter owing to Lender or any Affiliate of Lender by Borrowers (or any of them) or any Affiliate of a Borrower, whether primary or secondary, fixed or contingent, individually or jointly with others, including, but not limited to debt owing to Lender or any Affiliate of Lender that is guaranteed by any Guarantor. Such Contemporary Debt shall include the Senior Loan.

“**Control Agreement**” shall have the meaning set forth in Section 2.2(b)(x).

“**Corporate Guarantor**” means, jointly and severally, AdCare Oklahoma Management, LLC, a Georgia limited liability company, and AdCare Health Systems, Inc., an Ohio corporation.

“**Current Assets**” shall have the meaning set forth in Section 4.13(a).

“**Current Liabilities**” shall have the meaning set forth in Section 4.13(a).

“**Current Ratio**” shall have the meaning set forth in Section 4.13(a).

“**Debt Service Coverage Ratio**” means a ratio of the first number to the second number in which:

- (i) the first number is the sum of:
  - (a) net income from operations of the Facility (without deduction for actual management fees paid in connection with the operation of the Facility) calculated based upon the applicable period,
  - (b) interest expense with respect to the Facility, to the extent deducted in determining net income,
  - (c) lease expense pursuant to a lease of the Facility from one Borrower to another, if any, to the extent deducted in determining net income,

(d) non-cash expenses or allowances for depreciation and amortization of the Facility for such period to the extent deducted in determining net income, and

(e) any monies in the Capitalized Interest Reserve Account held with the Senior Loan,

less:

(a) non- operating or extraordinary income,

(b) Assumed Management Fees,

(c) required Capital Improvements Reserve Fund deposits for such period, and

(d) unfinanced capital expenditures in excess of the year-to-date sum of Capital Improvements Reserve Fund deposits,

(ii) and the second number is the sum of:

(a) the total Installment Payments, as defined in the Note, due for such period, and

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(b) other secured and unsecured debt payments (principal and interest) for such period relating to the Facility, including, without limitation, payments with respect to any Contemporary Debt relating to the Facility, provided, however, that such debt shall not include the Senior Loan, unless provided for herein.

In calculating “net income,” any extraordinary income shall be excluded.

“**Default**” means the occurrence or existence of any event which, but for the giving of notice or expiration of time or both, would constitute an Event of Default.

“**Default Rate**” means a per annum rate equal to the lesser of five (5%) percent above the Note Rate as set forth in the Note or the maximum rate permitted by applicable law.

“**Equipment**” means all beds, linen, televisions, carpeting, telephones, cash registers, computers, lamps, glassware, rehabilitation equipment, restaurant and kitchen equipment, and other fixtures and equipment of each of the Borrowers located on, attached to or used or useful in connection with any of the Property or the Facility and all renewals and replacements thereof and substitutions therefor; provided, however, that with respect to any items which are leased for the benefit of the Facility and not owned by any Borrower, the Equipment shall include the leasehold interest only of a Borrower together with any options to purchase any of said items and any additional or greater rights with respect to such items which any Borrower may hereafter acquire, but the foregoing shall not be construed to mean that such leasing shall be permitted hereunder and under the other Loan Documents.

“**ERISA**” shall have the meaning set forth in Section 3.23.

“**Event of Default**” means any “Event of Default” as defined in Article VI hereof.

“**Exhibit**” means an Exhibit to this Agreement, unless the context refers to another document, and each such Exhibit shall be deemed a part of this Agreement to the same extent as if it were set forth in its entirety wherever reference is made thereto.

“**Exit Fee**” shall have the meaning set forth in Section 2.9(d).

“**Facility**” means that certain facility known as Companions Specialized Care Center, a 121-bed licensed skilled nursing facility located at 6201 East 36<sup>th</sup> Street, Tulsa, OK 74135, as it may now or hereafter exist, together with any other general or specialized care facility, if any, now or hereafter operated on the Property.

“**Facility Bank**” means The PrivateBank and Trust Company.

“**Force Majeure**” means any happening or occurrence such as strikes, acts of God or nature or similar unanticipated events beyond the control of the party affected thereby, which prevents such party’s compliance with certain obligations hereunder, other than a Borrower’s financial inability to perform.

“**GAAP**” means, as in effect from time to time, generally accepted accounting principles consistently applied as promulgated by the American Institute of Certified Public Accountants.

“**General Intangibles**” means all intangible personal property of any of the Borrowers arising out of or connected with the Property or the Facility and all renewals and replacements thereof and substitutions therefor (other than Accounts, Rents, Instruments, Inventory, Money, Permits, and Reimbursement Contracts), including, without limitation, things in action, contract rights and other rights to payment of money.

“**Government Receivables Account**” means the bank deposit account for Borrowers maintained at the Facility Bank into which all Medicaid and Medicare Reimbursement Contracts payments are to be deposited.

“**Governmental Authority**” means any board, commission, department or body of any municipal, county, state or federal governmental unit, or any subdivision of any of them, that has or acquires jurisdiction over the Property and/or the Improvements or the use, operation or improvement of the Property.

“**Guarantor**” means, jointly and severally, any Corporate Guarantor and each other party who executes and delivers a Guaranty Agreement in accordance with the terms of this Agreement.

“**Guaranty Agreement**” means any Payment and Performance Guaranty.

“**Health Regulatory Authority**” means any Governmental Authority administering, overseeing, or regulating any certificates of need and other licensure and regulatory approvals required for the operation of the Facility (including any approvals required to obtain reimbursement under Medicare, Medicaid and CHAMPUS, and other Department of Veterans Affairs benefits, as applicable.)

“**Improvements**” means all buildings, structures and improvements of every nature whatsoever now or hereafter situated on the Property, including, but not limited to, all gas and electric fixtures, radiators, heaters, engines and machinery, boilers, ranges, elevators and motors, plumbing and heating fixtures, carpeting and other floor coverings, water heaters, awnings and storm sashes, and cleaning apparatus which are or shall be attached to the Property or said buildings, structures or improvements.

“**Indebtedness**” means any (a) obligations for borrowed money, (b) obligations, payment for which is being deferred by more than thirty (30) days, representing the deferred purchase price of property other than accounts payable arising in connection with the purchase of inventory and materials customary in the trade and in the ordinary course of each Borrower’s business, (c) obligations, whether or not assumed, secured by Liens or payable out of the proceeds or production from the Accounts and/or property now or hereafter owned or acquired, and (d) the amount of any other obligation (including obligations under financing leases) which would be shown as a liability on a balance sheet prepared in accordance with GAAP.

“**Indemnified Parties**” shall have the meaning set forth in Section 7.4.

“**Ineligible Accounts Receivable**” shall mean the sum of:

- (i) self-pay billings and direct patient obligations not directly collectible from commercial or government payors;
- (ii) gross patient billings outstanding to government payors aged greater than 90 days;
- (iii) gross patient billings outstanding to commercial payors aged greater than 90 days;
- (iv) net billings not directly owned by or in the name of and payable to the Borrower or subject to a priority lien in favor of any entity other than the Lender;
- (v) net billings made under any provider or payor agreement of which the Borrower is not directly the receiving party or Seller in accordance with the Purchase Agreement; and
- (vi) other billings so deemed ineligible by the Lender based on the collection experience with respect to the Accounts or other factually based credit criteria upon an audit of cash collections by an independent auditor acceptable to the Lender.

“**Installment Payments**” shall have the meaning given to such term in the Note.

“**Instruments**” means all instruments, Chattel Paper, documents or other writings obtained from or in connection with the operation of the Property or the construction and operation of the Facility (including, without limitation, all ledger sheets, computer records and printouts, data bases, programs, books of account, trademarks or trade names, utility contracts, maintenance and service contracts, and files relating thereto).

“**Inventory**” means all inventories of food, beverages and other consumables held by any of the Borrowers for sale or use at or from the Property or the Facility, and soap, paper supplies, medical supplies, drugs and all other such goods, wares and merchandise held by any of the Borrowers for sale to or for consumption by guests, patients or residents of the Property or the Facility and all such other goods returned to or repossessed by any Borrower.

“**Investment Property**” shall mean all property, as such term is defined in the UCC, and includes, without limitation, a security, whether certificated or uncertificated, security entitlement, securities account, commodity, or commodity account, and all proceeds (Cash proceeds and non-cash proceeds) of, and Supporting Obligations with respect to, the foregoing.

“**Knowledge**” means that any Borrower will be deemed to have “Knowledge” of a particular fact or other matter if any executive officer of such Borrower is aware of such fact or other matter where a prudent individual could be expected to discover or otherwise become aware of such fact or other matter in the course of operating the business.

“**Lease Agreement**” shall mean that certain Facility Lease dated June 25, 2012 and effective on the Operations Closing Date, between Owner and the Operator.

“**Legal Requirements**” means all governmental statutes, laws, rules, orders, regulations, ordinances, judgments, decrees and injunctions of any Governmental Authority affecting either Borrower or the Property or any portion of or the construction, rehabilitation, ownership, use, alteration or operation of, or any portion of the Property (whether now or hereafter enacted and in force), and all permits, licenses and authorizations and regulations relating thereto.

“**Lender**” shall mean Contemporary Healthcare Fund I, L.P.

“**Lender’s Approval**” shall have the meaning set forth in Section 7.12.

“**Lien**” means any voluntary or involuntary mortgage, security deed, deed of trust, lien, pledge, assignment, security interest, title retention agreement, financing lease, levy, execution, seizure, judgment, attachment, garnishment, charge, lien or other encumbrance of any kind, including those contemplated by or permitted in this Agreement and the other Loan Documents.

“**Liquidity Factor**” shall mean a percentage representative of cash collections to net billings by payor, by site, or by other classification as determined by an independent auditor acceptable to Lender. The Liquidity Factor shall be subject to change during the term of this Agreement at the sole discretion of Lender based upon factually based credit criteria, including, among other things, actual monthly cash collections recognized on gross patient billings as determined by an independent auditor acceptable to Lender. The Liquidity Factor as of the Closing Date will be 90%.

“**Loan**” shall mean the loan in a maximum amount of the Original Loan Amount made by Lender to Borrowers as evidenced by the Note.

“**Loan Account**” means the Borrowers’ deposit account maintained at the Facility Bank and subject to the Control Agreement and ZBA Agreement.

“**Loan Documents**” means, collectively:

- (i) this Agreement,
- (ii) Assignment and Pledge Agreement (with, if applicable, Waiver and Consent),
- (iii) Borrower Environmental Indemnity Agreement,
- (iv) Closing Statement,
- (v) Control Agreement,
- (vi) Management Company Environmental Indemnity Agreement,



- (vii) Note,
- (viii) Payment and Performance Guaranty,
- (ix) Security Agreement,
- (x) Subordination and Assignment of Lease Agreement,
- (xi) Subordination and Assignment of Management Agreement,
- (xii) Subordination and Standstill Agreement,
- (xiii) Subsidiary Guaranty,
- (xiv) ZBA Agreement.

each as further amended, modified, supplemented or restated, together with any and all other documents executed by any Borrower or others, evidencing, securing or otherwise relating to the Loan.

“**Loan Obligations**” means the aggregate of all principal and interest owing from time to time under the Note and all expenses, charges and other amounts from time to time owing under the Note, this Agreement, or the other Loan Documents and all covenants, agreements and other obligations from time to time owing to, or for the benefit of, Lender pursuant to the Loan Documents.

“**Management Agreement**” means that certain Management Agreement dated January 1, 2012, between Operator and Management Company.

“**Management Company**” shall mean AdCare Oklahoma Management, LLC, a Georgia limited liability company.

“**Management Company Environmental Indemnity Agreement**” shall have the meaning set forth in Section 2.2(c)(vi) of this Agreement.

“**Material Adverse Effect**” shall have the meaning set forth in Section 3.1.

“**Maturity Date**” shall have the meaning given such term in the Note.

“**Medicaid**” means that certain program of medical assistance, funded jointly by the federal government and the states, for impoverished individuals who are aged, blind and/or disabled, and/or members of families with dependent children, which program is more fully described in Title XIX of the Social Security Act (42 U.S.C. §§ 1396 *et seq.*) and the regulations promulgated thereunder.

“**Medicare**” means that certain federal program providing health insurance for eligible elderly and other individuals, under which physicians, hospitals, independent living and assisted living facilities, skilled nursing homes, home health care and other providers are reimbursed for certain covered services they provide to the beneficiaries of such program, which

program is more fully described in Title XVIII of the Social Security Act (42 U.S.C. §§ 1395 *et seq.*) and the regulations promulgated thereunder.

“**Money**” means all monies, cash, rights to deposit or savings accounts or other items of legal tender obtained from or for use in connection with the operation of the Facility.

“**Note**” means the Promissory Note dated the date hereof in the principal amount of the Original Loan Amount payable by Borrowers to the order of Lender.

“**Note Rate**” shall have the meaning given such term in the Note.

“**Operations Closing Date**” shall have the meaning given such term in Section 3.39(i).

“**Operations Seller**” means Tulsa Christian Care, Inc.

“**Operations Seller Lease Agreement**” means the Facility Lease dated the date hereof, between Operations Seller and Owner.

“**Operations Seller Management Agreement**” means the Management Agreement dated June 25, 2012, as amended, between Operations Seller and Management Company.

“**Operations Seller SNDA**” shall have the meaning set forth in Section 2.2(c)(vii).

“**Operations Seller Subordination and Assignment of Lease Agreement**” shall have the meaning set forth in Section 2.2(c)(viii).

“**Operations Seller Transfer Agreement**” means the Operations Transfer Agreement dated the date hereof, between the Operations Seller and the Operator.

“**Original Loan Amount**” shall mean \$600,000.

“**Payment and Performance Guaranty**” shall have the meaning set forth in Section 2.2(b)(viii).

“**Payroll Account**” means the Borrowers’ payroll account maintained at the Facility Bank and subject to the ZBA Agreement.

“**Permits**” means all licenses, permits and certificates used or necessary in connection with the ownership, operation, construction, use or occupancy of the Property and/or the Facility, including, without limitation, business licenses, state health department licenses, food service licenses, licenses to conduct business, certificates of need and all such other permits, licenses and rights, obtained from any governmental, quasi-governmental or private person or entity whatsoever concerning ownership, construction, operation, use or occupancy.

“**Permitted Encumbrances**” has the meaning given to that term in Section 5.2 hereof.

“**Person**” means any natural person, firm, trust, corporation, partnership, limited liability company, trust and any other form of legal entity.

“**Physical Plant Standard**” shall have the meaning set forth in Section 3.15.

“**Proceeds**” means all awards, payments, earnings, royalties, issues, profits, liquidated claims, and proceeds (including proceeds of insurance and condemnation or any conveyance in lieu thereof) from the sale, conversion (whether voluntary or involuntary), exchange, transfer, collection, loss, damage, condemnation, disposition, substitution or replacement of any of the Collateral.

“**Property**” means the real estate which is more particularly described in Exhibit A hereto, upon which the Facility is located, and which, concurrent with the Closing Date, was owned by Owner.

“**Purchase Agreement**” means the Purchase and Sale Agreement, with exhibits, dated March 14, 2012, as amended April 19, 2012 and June 19, 2012, as amended, between Seller and AdCare Property Holdings, LLC, as assigned to the Owner.

“**Reimbursement Contracts**” means all third party reimbursement contracts for the Facility which are now or hereafter in effect with respect to residents or patients qualifying for coverage under the same, including Medicare, Medicaid, other government programs and private insurance agreements, and any successor program or other similar reimbursement program and/or private insurance agreements.

“**Rents**” means all rent and other payments of whatever nature from time to time payable pursuant to leases of the Property or the Facility, or for retail space or other space at the Property (including, without limitation, rights to payment earned under leases for space in the Improvements for the operation of ongoing retail businesses such as newsstands, barbershops, beauty shops, physicians’ offices, pharmacies and specialty shops).

“**Security Agreement**” shall have the meaning set forth in Section 2.2(b)(ii).

“**Seller**” means, collectively, F&F Ventures, LLC and Tulsa Christian Care, Inc.

“**Senior Lender**” shall mean Contemporary Healthcare Senior Lien Fund I, L.P.

“**Senior Loan**” shall mean all loan obligations, the Senior Loan Agreement and the other Senior Loan Documents.

“**Senior Loan Agreement**” shall mean that certain Loan Agreement dated the date hereof, by and between Senior Lender and the Borrowers, as such agreement may be amended.

“**Senior Loan Documents**” shall mean the Senior Loan Agreement and all documents, instruments and agreements executed in connection with such Senior Loan Agreement.

“**Senior Mortgage**” means that certain Mortgage, Assignment of Leases and Rents, Security Agreement and Fixture Filing of even date herewith from the Owner in favor of or for the benefit of the Senior Lender.

“**Single Purpose Entity**” means a Person which owns no interest or property other than the Property and the Improvements or has a business purpose limited solely to the leasing and operation of the Facility.

“**Stabilization**” means the date upon which the Facility demonstrates a Total Debt Service Coverage Ratio of 1.15 to 1.00 for three consecutive calendar months.

“**Standstill Notice**” shall have the meaning set forth in Section 6.4.

“**Stock**” shall mean all shares, options, warrants, general or limited partnership interests, membership interests, participations or other equivalents (regardless of how designated) in a corporation, limited liability company, partnership or any equivalent entity, whether voting or nonvoting, including, without limitation, common stock, preferred stock, or any other “equity security” (as such term is defined in Rule 3a11-1 of the General Rules and Regulations promulgated by the Securities and Exchange Commission under the Securities Exchange Act of 1934, as amended).

“**Subordination and Assignment of Lease Agreement**” shall have the meaning set forth in Section 2.2(c)(iii).

“**Subordination and Assignment of Management Agreement**” shall have the meaning set forth in Section 2.2(c)(ii).

“**Subordination and Attornment Agreement**” shall have the meaning set forth in Section 2.2(c)(i).

“**Subordination and Standstill Agreement**” shall have the meaning set forth in Section 2.2(c)(iv).

“**Subsidiary Guaranty**” shall have the meaning set forth in Section 2.2(b)(ix).

“**Supporting Obligation**” shall mean all supporting obligations as such term is defined in the UCC, and in any event shall include, without limitation, a letter-of-credit right, secondary obligation, or obligation of a secondary obligor, or secondary obligation that supports the payment or performance of an Account, Chattel Paper, a document, a General Intangible, an Instrument, or Investment Property.

“**Tax**” (including, with correlative meaning, the terms “**Taxes**” and “**Taxable**”) means, with respect to any Person, (a) all taxes, domestic or foreign, including without limitation any income (net, gross or other, including recapture of any tax items such as investment tax

credits), alternative or add-on minimum tax, gross income, gross receipts, gains, sales, use, leasing, lease, user, ad valorem, transfer, recording, franchise, profits, property (real or personal, tangible or intangible), fuel, license, withholding on amounts paid to or by such Person, payroll, employment, unemployment, social security, excise, severance, stamp, occupation, premium, environmental or windfall profit tax, custom, duty or other tax, or other like assessment or charge of any kind whatsoever, together with any interest, levies, assessments, charges, penalties, additions to tax or additional amounts imposed by any Taxing Authority, (b) any joint or several liability of such Person with any other Person for the payment of any amounts of the type described in (a) of this definition and (c) any liability of such Person for the payment of any amounts of the type described in (a) as a result of any express or implied obligation to indemnify any other Person.

“**Tax and Insurance Escrow and Security Agreement**” shall mean that certain Tax and Insurance Escrow and Security Agreement in the form attached hereto as Schedule 2.2(b)(vi).

“**Tax and Insurance Report**” shall mean the report required by Section 4.6(o) of this Agreement.

“**Tax Return(s)**” mean all returns, consolidated or otherwise (including without limitation informational returns), required to be filed with any Taxing Authority.

“**Taxing Authority**” means any authority responsible for the imposition or collection of any Tax.

“**Third Party Payors’ Programs**” shall have the meaning set forth in [Section 3.13](#).

“**Total Debt Service Coverage Ratio**” means the Debt Service Coverage Ratio including the Senior Loan.

“**Trade Rights**” shall have the meaning set forth in [Section 3.32](#).

“**UCC**” shall mean the Uniform Commercial Code.

“**Unused Fee**” shall have the meaning set forth in [Section 2.9\(d\)](#).

“**ZBA Agreement**” means the agreement by and among the Facility Bank, each Borrower and the Lender, governing the operation of the Government Receivables Account and Payroll Account and transfer to the Loan Account.

1.2 **Singular vs. Plural**. Singular terms shall include the plural forms and vice versa, as applicable, related to the terms defined.

1.3 **Uniform Commercial Code**. Terms contained in this Agreement shall, unless otherwise defined herein or unless the context otherwise indicates, have the meanings, if any, assigned to them by the Uniform Commercial Code in effect in the state in which the Collateral for the Loan Obligations is deemed located, as such Uniform Commercial Code may

be amended from time to time (provided, no amendment shall have the effect of releasing any security interest previously granted.)

1.4 **GAAP**. All accounting terms used in this Agreement shall be construed in accordance with GAAP, except as otherwise specified.

1.5 **References Generally**. All references to other documents or instruments shall be deemed to refer to such documents or instruments as they may hereafter be extended, renewed, modified, or amended and all replacements and substitutions therefor.

1.6 **References to Medicaid and Medicare**. All references herein to “Medicaid” and “Medicare” shall be deemed to include any successor program thereto.

## ARTICLE II. TERMS OF THE LOAN

### 2.1 **The Loan**.

(a) **Loan**. Borrowers have agreed to borrow the Loan from Lender and Lender has agreed to make the Loan to Borrowers, subject to each Borrower’s compliance with and observance of the terms, conditions, covenants, and provisions of this Agreement and the other Loan Documents, and Borrowers have made the covenants, representations, and warranties herein and therein as a material inducement to Lender to make the Loan.

(b) Closing Date. The date of the closing related to the disbursing of any portion of the Loan and delivery of the Loan Documents shall be referred to herein as the “**Closing Date**.”

(c) Advances. Borrowers shall have the option to request up to one advance of Loan proceeds (an “**Advance**”) per week during the term of the Loan upon presentation to Lender of a current Borrowing Base Certificate, in form attached as Exhibit I hereto, and such other supporting documentation as Lender shall require. All such requests for Advances shall be submitted to Lender not less than three (3) Business Days prior to the date of the desired funding of the Advance. Each such Advance shall be subject to receipt of a signed certificate from an authorized officer of the Borrowers in a form acceptable to Lender, which certificate shall demonstrate Borrowers’ compliance with the conditions of the Advance set forth herein certifying to such items as Lender shall require, including without limitation the following:

(i) Lender has the capacity to fund the Advance, and such Advance, when combined with the aggregate unpaid principal amount of all other Advances does not violate any of the Lender’ s concentration rules or requirements relating to the maximum aggregate financing Lender may advance to any one Borrower, as determined by Lender in accordance with SBA regulations;

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(ii) No monetary Event of Default shall have occurred and no other Default or Event of Default shall exist and be continuing under the Loan or the Senior Loan;

(iii) Borrowers shall demonstrate to Lender that the aggregate principal balance outstanding of the Loan, giving effect to the requested Advance, is equal to the lesser of (A) \$600,000, or (B) the Borrowing Base;

(iv) All representations and warranties made by Borrowers in this Agreement and the other Loan Documents are true and correct as of the date of making such Advance except as otherwise specifically approved by Lender in writing or permitted under the Loan Documents;

(v) There shall have been no material adverse change in the financial condition of the Borrowers or any Guarantor as determined by Lender in its sole discretion;

(vi) Borrowers shall pay all reasonable fees and expenses incurred by Lender in connection with making such Advance;

(vii) Borrowers’ minimum balance on any date shall be the lesser of (A) \$450,000 or (B) the Borrowing Base;

(viii) Borrowers shall deliver to Lender any and all documents and information to evidence the conditions set forth herein as determined by Lender, in its sole discretion;

(ix) Borrowers shall execute any and all documents reasonably deemed necessary by Lender;

(x) Borrowers shall be current under all payroll and payroll tax obligations for the Facility unless subject to a good faith contest adequately reserved for in the judgment of the Lender; and

(xi) Each Advance shall be in a minimum amount of \$25,000.

2.2 **Loan Documents.**

- (a) The Loan will be evidenced by the Loan Documents, including, but not limited to, the Note;
- (b) The Loan will be secured and guaranteed by the following:
  - (i) reserved;

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- (ii) a second lien security interest., subject only to Senior Lender' s lien, and an assignment of Borrowers' interest in all General Intangibles, including, but not limited to, licenses, Permits, Reimbursement Contracts, leases and other contracts used in connection with or relating to operation of the Facility, and a first lien security interest and an assignment of Borrowers' interest in all Accounts, as evidenced by the Security Agreement delivered by Borrowers on the Closing Date, in the forms attached hereto as Schedule 2.2(b)(ii) (the "**Security Agreement**");
- (iii) a second lien security interest in all of the issued and outstanding membership interests or capital stock, as the case may be, of Owner and Operator, evidenced by the form of Assignment and Pledge Agreement executed and delivered by all the members of each of the Borrowers on the Closing Date, along with a Waiver and Consent, if applicable, in the form attached hereto as Schedule 2.2(b)(iii) (each, an "**Assignment and Pledge Agreement**");
- (iv) reserved;
- (v) a second lien security interest in the Capital Improvements Reserve Fund as evidenced and as required by the form of capital improvements escrow and security agreement attached to the Senior Loan Agreement (the "**Capital Improvements Escrow and Security Agreement**");
- (vi) a second lien security interest in the Tax and Insurance Reserve Fund as evidenced and as required by the form of tax and insurance escrow and security agreement attached to the Senior Loan Agreement (the "**Tax and Insurance Escrow and Security Agreement**");
- (vii) a second lien on the Capitalized Interest Reserve Account held by the Senior Lender and as defined in the Senior Loan Agreement;
- (viii) a guaranty by each Corporate Guarantor, through the delivery to Lender on the Closing Date, of a payment and performance guaranty agreement in the form attached hereto as Schedule 2.2(b)(viii) (each a "**Payment and Performance Guaranty**");
- (ix) a guaranty by each subsidiary of any Borrower which may be hereafter acquired or formed by a Borrower, it being

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understood and agreed that as of the Loan Closing Date, no such entities exist, through the delivery to Lender at the time of the acquisition or formation of such subsidiary by each such subsidiary, a Guaranty in the form attached hereto as Schedule 2.2(b)(ix) (each, a “**Subsidiary Guaranty**”); and

- (x) a Control Agreement by and among the Facility Bank, Borrowers and Lender for the “Loan Account,” delivered to Lender within 10 Business Days of the Closing Date in the form attached hereto as Schedule 2.2(b)(x) (the “**Control Agreement**”);
  - (xi) reserved.
- (c) Additional terms and conditions of the Loan will be evidenced by the following documents:
- (i) reserved;
  - (ii) a Subordination and Assignment of Management Agreement executed and delivered by Borrowers and the Management Company on the Operations Closing Date in the form attached hereto as Schedule 2.2(c)(ii) (the “**Subordination and Assignment of Management Agreement**”);
  - (iii) a Subordination and Assignment of Lease Agreement executed and delivered by Borrowers on the Operations Closing Date in the form attached hereto as Schedule 2.2(c)(iii) (the “**Subordination and Assignment of Lease Agreement**”);
  - (iv) a Subordination and Standstill Agreement executed and delivered by Lender and Senior Lender, and acknowledged by each Borrower on the Closing Date in the form attached hereto as Schedule 2.2(c)(iv)(A) (the “**Subordination and Standstill Agreement**”);
  - (v) a Borrower Environmental Indemnity Agreement dated the Closing Date executed and delivered by Borrowers in the form attached hereto as Schedule 2.2(c)(v) (the “**Borrower Environmental Indemnity Agreement**”);
  - (vi) a Management Company Environmental Indemnity Agreement dated the Closing Date executed and delivered by the Management Company in the form attached hereto

as Schedule 2.2(c)(vi) (the “**Management Company Environmental Indemnity Agreement**”);

- (vii) a Subordination and Attornment Agreement executed and delivered by Operations Seller, Owner and Senior Lender, under which Lender is a third party beneficiary, on the Closing Date in the form attached hereto as Schedule 2.2(c)(vii) (the “**Operations Seller SNDA**”); and



- (viii) a Subordination and Assignment of Lease Agreement executed and delivered by Owner, Operations Seller, Senior Lender and Lender on the Closing Date in the form attached hereto as Schedule 2.2(c)(viii) (the “**Operations Seller Subordination and Assignment of Lease Agreement**”).

2.3 **Closing Deliverables by Borrowers.** Borrowers shall deliver or cause to be delivered to Lender the following:

- (a) Borrower’s Officers’ Certificates. On the Closing Date, a certificate executed by the Chief Executive Officer and Chief Financial Officer or other party acceptable to Lender of each Borrower certifying to Lender, among other things, that, as of the Closing Date: (i) the transactions have been duly authorized, (ii) true, correct and complete copies of the organizational documents of Borrowers have been delivered to Lender, (iii) to the Borrowers’ Knowledge, no part of the Facility shall have been damaged and not repaired to Lender’s satisfaction or taken in condemnation or other like proceedings nor shall any such proceeding be pending, (iv) to the Borrowers’ Knowledge, the Facility shall be unimpaired and not reduced in value and shall be free from settling and other structural defects, (v) neither the Borrowers nor the Guarantors, nor any of Borrowers’ or Guarantors’ principals shall be involved in any bankruptcy, reorganization or insolvency proceeding and (vi) that since the date or dates, as the case may be, of the financial information last provided to the Lender with respect to the Borrowers, any ownership interest in the Borrowers, the Facility or the Guarantors, there has been no material adverse change in the financial condition thereof;

- (b) Legal Opinion. On the Closing Date, a legal opinion of Borrowers’, the Borrowers’ members and any Guarantor’s counsel, in form and content satisfactory to Lender and its counsel;

- (c) Reports. The following reports and other documents all of which shall be in Lender’s name:

- (i) Reserved.

- (ii) Survey. On the Closing Date, three (3) copies of a survey with a licensed surveyor’s certificate, all in form and substance acceptable to and certified to Lender, Lender’s counsel and the title insurance company. Such survey and surveyor’s certificate shall not be dated more than thirty

(30) days prior to the date of the Closing Date and shall attest to the existence or nonexistence of a special flood hazard area with respect to the Facility. The survey shall also be prepared in accordance with ALTA 2011 standards and be certified to the Lender and the title insurance company. Such survey shall provide evidence to Lender that all streets adjoining the Property underlying the Facility have been completed, dedicated and accepted for maintenance and public ingress and egress to the Property.

- (iii) Environmental Report. On the Closing Date, a Phase I Environmental Report indicating that the Facility and the Property are free from toxic chemicals and environmentally hazardous substances and that surrounding land uses do not pose an environmental threat.

- (iv) Engineering Report. On the Closing Date, an engineering report of the Facility from an engineering firm acceptable to Lender in its sole discretion, which report shall be in substance acceptable to Lender

(v) Appraisal. (a) On the Closing Date, an appraisal of the Property “as is” acceptable to Lender, in its sole discretion dated no more than thirty (30) days prior to the Closing Date, and (b) as otherwise may be required hereunder.

(vi) Termite Inspection Report. On the Closing Date, a termite inspection report of the Facility dated no more than thirty (30) days prior to the Closing Date in form and substance satisfactory to the Lender or, in lieu thereof, a current pest control contract for the Facility.

(d) Zoning Letter. A copy of a letter from local zoning authority or some other evidence acceptable to Lender, addressed to the Lender, confirming that the Facility is zoned for its intended use.

(e) Sprinkler Systems. On the Closing Date, Borrowers shall provide evidence to Lender, acceptable to Lender in its sole discretion, that all buildings that comprise the Facility have sprinkler systems.

(f) Evidence of Insurance. Evidence, acceptable to Lender in its sole discretion, of insurance required by Section 4.5 herein, in form and substance acceptable to Lender. Such evidence shall be: (i) the original, or a copy certified by the insurance agent, of the policy(ies) of insurance, or (ii) the insurance binder (Acord Form 25 provided by the insurance carrier) or (iii) a certificate of insurance (Acord Form 27 or 28, at Lender’ s discretion, provided by the insurance agent), or (iv) an original letter from the insurance carrier on the primary layer, signed by an officer of such carrier, attaching the form of insurance policy pursuant to which

coverage is being provided, and, if applicable, an original letter from each insurance carrier on the excess layers, signed by an officer of such carrier(s) agreeing that such carrier is bound to the form of insurance policy delivered by the primary carrier (i.e., agreeing to “follow form” to the primary carrier). The letter must set forth the date by which the policy will be delivered to the Lender. All mortgagee/loss payee/additional insured endorsements must be attached to such letter.

(g) Evidence of Payment of Taxes. Evidence, acceptable to the Lender in its sole discretion, that Borrowers have timely and appropriately paid all Taxes associated with the Facility.

(h) Licenses and Permits. On the Closing Date, a copy of the Facility license to permit it to be operated as a skilled nursing facility prior to the Operations Closing Date.

(i) Certificate of Occupancy. On the Closing Date or post Closing Date at Lender’ s discretion, a copy of the Facility’ s Certificate of Occupancy.

(j) Loan Documents. On the Closing Date, executed copies of each of the Loan Documents required on such date.

(k) Other Agreements. On the Closing Date, a copy of the executed Operations Seller Management Agreement, Operations Seller Lease Agreement and the Operations Seller Transfer Agreement.

(l) Further Assurances. Such other information of Borrowers, each Guarantor and/or the Facility, as Lender shall reasonably deem necessary.

## 2.4 **Interest and Interest Rate.**

(a) The outstanding principal balance of the Loan will bear interest at the Note Rate as set forth in the Note and payments of principal and interest on the Loan, including any fees payable in Section 2.9, shall be made in accordance with the terms and provisions of the Note and this Agreement. Payments of principal and interest on the Loan shall be made in accordance with the terms and provisions of the Note and the amortization schedule attached hereto as Schedule 2.4(a) (which amortization schedule may be adjusted during the term of the Loan in accordance with the Note).

(b) All interest on the outstanding principal balance of the Loan shall be calculated on the basis of a 360-day year by multiplying the outstanding principal amount by the applicable per annum rate, multiplying the product thereof by thirty days and dividing the product so obtained by 360.

2.5 **Repayment of Loan.** Each payment of the Loan Obligations shall be paid directly to Lender in lawful money of the United States of America at the following address:

Contemporary Healthcare Fund I, L.P.  
1040 Broad Street  
Suite 103  
Shrewsbury, New Jersey 07702  
Attention: Mr. Eric Smith

or such other place as Lender shall designate in writing to Borrowers. Each such payment shall be paid in immediately available funds by 2:00 p.m. Eastern time on the date such payment is due, except if such date is not a Business Day such payment shall then be due on the first Business Day after such date, but interest shall continue to accrue until the date payment is received. Any payment received after 2:00 p.m. Eastern time shall be deemed to have been received on the immediately following Business Day for all purposes, including, without limitation, the accrual of interest on principal.

2.6 **Prepayment.**

(a) During the term of the Loan, the Borrowers may borrow, repay, and reborrow the Loan in accordance with the terms hereof and subject to the limitations set forth herein and in the Note.

(b) The Borrowers shall prepay the Loan in full upon any repayment in whole of the Senior Loan.

2.7 **Late Charges on Overdue Installments; Collection Costs.**

(a) If any scheduled payment of principal or interest as set forth in the Note, or any other agreed charge, is not made as the same becomes due, Borrowers agree to pay to Lender a late charge as required by the Note.

(b) The imposition of such late charges shall not preclude Lender from exercising any other remedies which it may have.

(c) Borrowers will also pay to Lender, in addition to the amount due, all reasonable costs of collecting, securing, or attempting to collect or secure the Note, including, without limitation, court costs and reasonable attorneys' fees, including, without limitation, attorneys' fees for preparation of litigation and in any appellate and bankruptcy proceedings.

2.8 **Usury Provisions.** In no event shall the amount of interest due or payable hereunder or pursuant to any of the Loan Documents exceed the maximum rate of interest allowed by applicable law, and in the event any such payment is inadvertently

paid by Borrowers or inadvertently received by Lender, then such excess sum shall be credited as a payment of principal. It is the express intent hereof that Borrowers not pay and Lender not receive, directly or indirectly, interest in excess of that which may be legally paid by Borrowers under applicable law.

2.9 **Fees.**

(a) **Application Fee.** Borrowers shall pay to Lender a non-refundable Application Fee of one percent (1.00%) of the Original Loan Amount, which fee may be paid for from Loan proceeds (the “**Application Fee**”). The Application Fee is due upon the earlier of the Closing Date or August 31, 2012 and is deemed fully earned upon the execution of such term sheet.

(b) **Closing Fee.** Borrowers shall pay to Lender a non-refundable transaction fee of one percent (1%) of the initial Advance to be made on the first Closing Date and one percent (1%) on each subsequent Advance (the “**Closing Fee**”). Such Closing Fee is deemed fully earned on the date due. Notwithstanding the foregoing, the total Closing Fee paid by the Borrowers over the term of the Loan shall not exceed 1% of the Original Loan Amount (the “**Closing Fee**”).

(c) **Monitoring Fee.** Borrowers shall pay to Lender a Monitoring Fee of one-half of a percent (0.5%) per annum of the Original Loan Amount, payable monthly on the 20<sup>th</sup> day of each month commencing the 20<sup>th</sup> day of the month next succeeding the Operations Closing Date (the “**Monitoring Fee**”).

(d) **Exit Fee.** Upon the Maturity Date or if the Borrowers shall decide to terminate a portion or all of the Lender’s commitment to provide the Loan hereunder, the Borrowers shall pay an exit fee (the “**Exit Fee**”) to the Lender equal to 1.5% of the Original Loan Amount; subject, however, to the following: (i) any cash sweeps upon an Event of Default shall not be considered prepayments subject to the Exit Fee so long as the aggregate outstanding principal balance of the Loan at all times equals or exceeds \$450,000; (ii) if at any time the aggregate outstanding principal balance of the Loan shall be less than \$450,000, then the Exit Fee shall be equal to 1.5% of the difference between \$450,000 and the aggregate outstanding principal balance on such date; and (iii) any permanent full or partial termination of Lender’s commitment for the Original Loan Amount shall require payment of the Exit Fee equal to 1.5% of the principal amount so terminated; provided, that the aggregate amount of Exit Fees payable during the term of the Loan shall not exceed 1.5% of the Original Loan Amount.

(e) **Non-Use Fee.** Borrower shall pay to Lender a Non-Use Fee of one half of a percent (0.5%) per annum on the average monthly Loan amount that has not been advanced, payable monthly on the 20<sup>th</sup> day of each month commencing the 20<sup>th</sup> day of the month next succeeding the Operations Closing Date.

All fees provided for in this Section 2.9 are deemed fully earned on the date due.

2.10 **Use of Loan; Disbursement of Proceeds.**

(a) Borrowers agree to use the Loan for the following:

(i) To provide funds to pay for the costs, expenses and fees due in connection with the Loan as noted on the Lender’s Closing Statement; and

(ii) The balance of the Loan, if any, shall be used for working capital, including, but not limited to, towards satisfaction of the covenants set forth herein and in the other Loan Documents.

(b) reserved.

(c) Borrowers further agree to make an equity contribution of \$550,000. The required equity contribution amount excludes any other fee the Borrowers or any of their Affiliates would pay themselves for services with respect to the acquisition or improvement of the Facility.

(d) Lender acknowledges that Borrowers have agreed to provide \$750,000 of stock in AdCare Health Systems, Inc. to Seller in accordance with the Purchase Agreement.

2.11 **Miscellaneous.** With respect to the amounts due under the Note, each Borrower waives the following to the fullest extent permitted by law:

(a) All rights of exemption of any of the Collateral from levy or sale under execution or other process for the collection of debts under the Constitution or laws of the United States or any state thereof;

(b) Demand, presentment, protest, notice of dishonor, notice of non-payment, diligence in collection, and all other requirements necessary to enforce the Note; and

(c) Any further receipt by Lender or acknowledgment by Lender of any Collateral now or hereafter deposited with Lender as security for the Loan.

2.12 **Application of Payment.** Note payments shall be applied as set forth in the Note.

### **ARTICLE III. BORROWERS' REPRESENTATIONS AND WARRANTIES**

To induce Lender to enter into this Agreement, and to make the Loan to Borrowers, each Borrower, jointly and severally, represents and warrants to Lender as follows:

3.1 **Existence, Power and Qualification.** Each Borrower is a duly organized and validly existing in the jurisdiction of its formation having the power to own its properties and to carry on its business as is now being conducted, and is duly qualified to do business and is in good standing in every jurisdiction in which the failure to be so qualified would have a material adverse effect on the results of operations, conditions (financial or otherwise), assets, properties, business or prospects of Borrowers (a "**Material Adverse Effect**").

3.2 **Power and Authority.** Each Borrower has full power and authority to borrow the indebtedness evidenced by the Note and to incur the Loan Obligations provided for herein, all of which have been authorized by all proper and necessary action. All consents,

approvals authorizations, orders or filings of or with any court or governmental agency or body, if any, required for the execution, delivery and performance of the Loan Documents by each Borrower has been obtained or made.

3.3 **Due Execution and Enforcement.** Each of the Loan Documents to which each Borrower is a party constitutes a valid and legally binding obligation of each Borrower, enforceable in accordance with its respective terms (except as such enforcement may be limited by bankruptcy, insolvency, reorganization, receivership, moratorium, or other laws relating to the rights of creditors generally and by general principles of equity) and does not violate, conflict with, or constitute any default under any law, government regulation, decree, judgment, each Borrower's articles of organization or operating agreement or any other agreement or instrument binding upon each Borrower.

3.4 **Capitalization.** The owners of any issued and outstanding equity interests of a Borrower and the amount of such equity interests held by such owners as of the Closing Date is set forth on Exhibit C attached hereto. All such issued and outstanding equity interests of the Borrowers have been duly and validly issued and are fully paid and non-assessable and were issued in full compliance with all federal and state securities laws. There are no outstanding (a) options, warrants or other rights to purchase from any Borrower any securities of a Borrower, (b) securities convertible into or exchangeable for shares of such equity interests, or (c) other commitments of any kind for the issuance of additional equity interests or options, warrants or other securities of the Borrowers except as set forth on Exhibit C. Except as set forth on Exhibit C, the Borrowers are not, pursuant to the terms of any other agreement currently in existence, under any obligation to register under the Securities Act of 1933, as amended, any of their presently outstanding securities or any of their securities which may be hereafter issued.

3.5 **Subsidiaries.** Neither Borrower presently owns or controls, directly or indirectly, any interest in any other corporations, associations or other business entities and neither Borrower is a participant in any joint venture, partnerships or similar arrangements.

3.6 **Non-Contravention.** Neither the execution and delivery by the Borrowers of this Agreement or the other Loan Documents, nor the consummation by the Borrowers of the transactions contemplated hereby and thereby, will (a) conflict with or violate the provisions of any law, rule or regulation applicable to the Borrowers or any of their respective properties or assets, (b) conflict with or violate the provisions of the organizational or governing documents, including but not limited to, the operating agreements of the Borrowers, (c) require on the part of any Borrower any notice to or filing with, or any permit, authorization, consent or approval of, any Governmental Authority other than the filing of UCC financing statements as required by the Loan Documents, (d) require on the part of any Borrower, any notice to or filing with or any permit authorization, consent or approval of any Person, (e) violate any judgment, decree, order or award of any Governmental Authority by which the Borrowers or their properties are bound, or (f) conflict with, result in material breach of, constitute (with or without due notice or lapse of time or both) a material default under, result in the acceleration of obligations under, create in any party any right to terminate, modify or cancel, or require any notice, consent or waiver under, any material contract or instrument to which a Borrower is a party or by which they are bound (individually or collectively) or to which any of its assets are subject.

3.7 **Absence of Undisclosed Liabilities.** Except as set forth on Schedule 3.7 neither of the Borrowers have any liability or obligation, secured or unsecured, whether accrued, absolute, contingent, unasserted or otherwise, that is material to the condition (financial or otherwise) of the assets, properties, business or prospects of such Borrower, except as and to the extent any such liability or obligation is reflected and reserved against in the current balance sheet delivered to Lender prior to the Closing Date. Except as set forth on Schedule 3.7 the Facility will not have any liability or obligation, secured or unsecured, whether accrued, absolute, contingent, unasserted or otherwise, that is material to the condition (financial or otherwise) of the assets, properties, business or prospects of the Facility, except as and to the extent any such liability or obligation is reflected and reserved against in the balance sheet delivered to Lender on the Closing Date.

3.8 **Pending Matters.**

(a) Operations; Financial Condition. No action or investigation is pending or threatened before or by any court or administrative agency which might result in any material adverse change in the financial condition, operations or prospects of any Borrower or any lower reimbursement rate under the Reimbursement Contracts. Neither Borrower is in violation of any agreement, the violation of which might reasonably be expected to have a Material Adverse Effect on its business or assets, and neither Borrower is in violation of any order, judgment, or decree of any court, or any statute or governmental regulation to which it is subject.

(b) Property Improvements. There are no proceedings pending, or, to the best of either Borrower's knowledge, threatened, to acquire through the exercise of any power of condemnation, eminent domain or similar proceeding any part of the Property, the Improvements or any interest therein, or to enjoin or similarly prevent or restrict the use of the Property or the operation of the Facility in any manner. None of the Improvements is subject to any unrepaired casualty or other damage.

3.9 Financial Statements Accurate. All financial statements heretofore or hereafter provided by either Borrower are and will be true and complete in all material respects as of their respective dates and fairly present the respective financial condition of such Borrower, and there are no material liabilities, direct or indirect, fixed or contingent, as of the respective dates of such statements which are not reflected therein or in the notes thereto or in a written certificate delivered with such statements. The financial statements of each Borrower have been prepared in accordance with GAAP. There has been no material adverse change in the financial condition, operations, or prospects of either Borrower since the dates of such statements except as fully disclosed in writing with the delivery of such statements. All financial statements of the operations of the Facility heretofore or hereafter provided to Lender are and will be true and complete in all material respects as of their respective dates.

3.10 Compliance with Facility Laws.

(a) Commencing on the Operations Closing Date, Borrowers shall be in compliance, as applicable, in all material respects with the applicable provisions of skilled

nursing facility laws, rules, regulations and published interpretations to which Borrowers are subject.

(b) At all times:

- (i) the Facility is and will be duly licensed and operated as a skilled nursing facility under the applicable laws of the state where the Property is located;
- (ii) Commencing on the Operations Closing Date, with respect to the Facility, Borrowers will be the lawful owners of all applicable operating Permits for the Facility, including, without limitation, the Certificate of Need, as applicable, which (A) is and will be in full force and effect, (B) constitutes all of the permits, licenses and certificates required for the use, operation and occupancy thereof, (C) has not been pledged as collateral for any other loan or Indebtedness except to Lender or Senior Lender or their Affiliates, (D) is and will be free from restrictions or any encumbrance which would materially adversely affect the use or operation of the Facility, and (E) will not be provisional, probationary or restricted in any way;
- (iii) No waivers of any laws, rules, regulations, or requirements (including, but not limited to, minimum square foot requirements per bed) is or will be required for the Facility to operate at the current licensed bed capacity;

- (iv) all Reimbursement Contracts are and will be in full force and effect with respect to the Facility, and each Borrower is in good standing with all the respective agencies governing such skilled nursing facility licenses, program certification, and Reimbursement Contracts;
- (v) each Borrower is and will be current in the payment of all applicable so-called provider specific taxes or other applicable assessments with respect to such Reimbursement Contracts; and
- (vi) in the event Lender acquires the Facility through foreclosure, to the Borrowers' knowledge as of the Closing Date, no receiver appointed by the court in connection with such foreclosure shall have to obtain a Certificate of Need in connection with such foreclosure.

3.11 **Maintain Bed Capacity.** Neither Borrower has granted to any third party the right to reduce the number of licensed beds in the Facility or to apply for approval to transfer the right to any and all of the licensed Facility beds to any other location.

3.12 **Medicare and Medicaid Compliance.** The Facility is in substantial compliance with all requirements for participation in Medicare and Medicaid, including without limitation, the Medicare and Medicaid Patient Protection Act of 1987. The Facility is in conformance in all material respects with all insurance, reimbursement and cost reporting requirements and has a current provider agreement which is in full force and effect under Medicaid and Medicare.

3.13 **Third-Party Payors.** To the Borrowers' Knowledge, there is no threatened or pending revocation, suspension, termination, probation, restriction, limitation, or nonrenewal affecting either Borrower or the Facility or any participation or provider agreement with any third-party payor, including Medicare, Medicaid and any private commercial insurance managed care and employee assistance program (such programs, the "**Third-Party Payors' Programs**") to which such Borrower presently is subject. All Medicare, Medicaid and private insurance cost reports and financial reports submitted by Borrowers or any Guarantor are and will be materially accurate and complete and have not been and will not be misleading in any material respects. No cost reports for the Facility remain "open" or unsettled, except as otherwise disclosed. Borrowers further covenant to sweep, on a daily basis, all accounts containing Medicaid or Medicare receivables into a Borrowers' account that is subject to the Control Agreement.

3.14 **Governmental Proceedings and Notices.** No Borrower nor the Facility is currently the subject of any proceeding by any governmental agency, and no notice of any violation has been received from a governmental agency that would, directly or indirectly, or with the passage of time:

- (a) Have a material adverse impact on such Borrower' s ability to accept and/or retain patients or result in the imposition of a fine, a sanction, a lower rate certification or a lower reimbursement rate for services rendered to eligible patients;
- (b) Modify, limit or annul or result in the transfer, suspension, revocation or imposition of probationary use of any of the Permits; or
- (c) Affect such Borrower' s continued participation in the Medicare or Medicaid programs or any other Third-Party Payors' Programs, or any successor programs thereto, at current rate certifications.
- (d) Affect such Borrower' s prospective participation in the Medicare or Medicaid programs or any other Third-Party Payors' Programs, or any successor programs thereto, at current rate certifications.



The Facility is not the subject of any proceeding by any Governmental Authority, and no notice of any violation has been received by the Facility from a Governmental Authority that would, directly or indirectly, or with the passage of time:

(a) Have a material adverse impact on such Borrower's ability to accept and/or retain residents or result in the imposition of a fine, a sanction, a lower rate

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certification, if applicable, or a lower reimbursement rate for services rendered, if applicable, to eligible residents;

(b) Modify, limit or annul or result in the transfer, suspension, revocation or imposition of probationary use of any of the Permits; or

(c) Affect such Borrowers' continued participation in the Medicare or Medicaid programs or any other Third-Party Payors' Programs, or any successor programs thereto, at current rate certifications.

3.15 **Physical Plant Standards.** The Facility and the use thereof complies in all material respects with all applicable local, state and federal building codes, fire codes, health care, nursing facility and other similar regulatory requirements (the "**Physical Plant Standards**"), and no waivers of Physical Plant Standards exist at the Facility.

3.16 **Pledges of Receivables.** Except as set forth in Schedule 3.16, neither Borrower has pledged its Accounts as collateral security for any loan or Indebtedness other than, as applicable, the Loan and the Senior Loan.

3.17 **Payment of Taxes and Property Impositions.** Each Borrower has filed all federal, state, and local tax returns which it is required to file and has paid, or made adequate provision for the payment of, all taxes which are shown pursuant to such returns or are required to be shown thereon or to assessments received by each Borrower, including, without limitation, provider taxes. All such returns are complete and accurate in all respects. Each Borrower has paid or made adequate provision for the payment of all applicable water and sewer charges, ground rents (if applicable) and Taxes with respect to the Property.

3.18 **Title to Collateral.** Each Borrower has good and marketable title to all of the Collateral it has pledged as security for the Loan, subject to no Lien, except Permitted Encumbrances which do not and will not materially interfere with the security intended to be provided by the Security Agreement or the current use or operation of the Property and the Improvements or the current ability of the Facility to generate net operating income sufficient to service the Loan. All Improvements situated on the Property are situated wholly within the boundaries of the Property.

3.19 **Priority of Mortgages; Liens; Other Obligations.** The Security Agreement and UCC financing statements constitute a valid lien against the personal property described therein, prior to all other liens or encumbrances, including those which may hereafter accrue, excepting only Permitted Encumbrances (as defined in Section 5.2 (No Liens; Exceptions)) which do not and will not materially and adversely affect (a) the ability of any Borrower to pay in full the principal of and interest on the Note when due, (b) the security (and its value) intended to be provided by the Security Agreement and UCC financing statements, or (c) the current use of the Property and the Improvements. No Borrower nor any Guarantor is liable, primarily or secondarily, upon any Indebtedness other than as described in its financial statements or in the Senior Loan Documents, or has any fixed or contingent obligation to make any loan or contribution of capital to any other entity that has not been fully paid. No Borrower nor any Guarantor owes any debt to its members, shareholders, partners or affiliates.

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3.20 **Location of Chief Executive Offices.** The location of each Borrower's principal place of business and chief executive office is set forth on Exhibit B hereto.

3.21 **Disclosure.** All information furnished or to be furnished by each Borrower to Lender in connection with the Loan or any of the Loan Documents, is, or will be at the time the same is furnished, accurate and correct in all material respects and complete insofar as completeness may be necessary to provide Lender with true and accurate knowledge of the subject matter.

3.22 **Trade Names.** Except as disclosed in Schedule 3.22, no Borrower nor the Facility have changed their names, been known by any other name, or been a party to a merger, reorganization or similar transaction within the last five (5) years.

3.23 **ERISA.** To the Borrower's Knowledge, each Borrower is in compliance with all applicable provisions of the Employee Retirement Income Security Act of 1974, as amended ("**ERISA**").

3.24 **Ownership.** The ownership interests of the Persons comprising each Borrower and each of the respective interests in each Borrower as of the Closing Date is correctly and accurately set forth on Exhibit C, attached hereto.

3.25 **Proceedings Pending.** There are no proceedings pending, or, to the best of each Borrower's knowledge, threatened, to acquire any power of condemnation or eminent domain with respect to any part of the Property, or to enjoin or similarly prevent or restrict the use of any Property or the operation of the Facility in any manner.

3.26 **Compliance With Other Applicable Laws.** To the best of each Borrower's knowledge, each Property and Improvements comply with all covenants and restrictions of record and applicable laws, ordinances, rules and regulations, including, without limitation, all laws, ordinances, rules and regulations relating to zoning, setback requirements and building codes. No Improvements constitute a nonconforming structure and the operation of the Facility is not a nonconforming use under current zoning, and there are no waivers of any current building code requirements for the Property or Improvements. The Facility is in compliance in all material respects with the Americans With Disabilities Act and regulations thereunder and the Federal Housing Act and regulations thereunder, each to the extent applicable. Each Borrower agrees to indemnify and hold Lender harmless from any fines or penalties assessed or any corrective costs incurred by Lender if any Improvements or any Property, or any part thereof, is hereafter determined to be in violation of any covenants or restrictions of record or any applicable laws, ordinances, rules or regulations, and such indemnity shall survive any foreclosure or deed in lieu of foreclosure.

3.27 **Solvency.** Each Borrower is solvent for purposes of 11 U.S.C. §548, and the borrowing of the Loan will not render such Borrower insolvent for purposes of 11 U.S.C. §548. Neither of the Borrowers nor any of the Guarantors nor any of the Borrowers' principals, partners and/or members are involved in any bankruptcy, reorganization or insolvency proceeding.

3.28 **Lease Agreement.** The Operations Seller Lease Agreement is in full force and effect and, there are no defaults (either monetarily or non-monetarily) by the Operations Seller or Owner, as applicable, thereunder. Commencing on the Operations Closing Date, the Lease Agreement is in full force and effect and, there are no defaults (either monetarily or non-monetarily) by the Owner or Operator, as applicable, thereunder.

3.29 **Management Agreement.** The Operations Seller Management Agreement is in full force and effect and, there are no defaults (either monetarily or non-monetarily) by the Operations Seller or Management Company, as applicable, thereunder. Commencing on the Operations Closing Date, the Management Agreement is in full force and effect and, there are no defaults (either monetarily or non-monetarily) by the Operator or Management Company, as applicable, thereunder.

3.30 **Single Purpose Entity.** Each Borrower is a Single Purpose Entity.

3.31 **Fraudulent Conveyances.** No Borrower (a) has entered into this Agreement or any of the other Loan Documents with the actual intent to hinder, delay, or defraud any creditor, nor (b) has received reasonably equivalent value in exchange for its obligations under the Loan Documents. Giving effect to the transactions contemplated by the Loan Documents, the fair saleable value of each Borrower's assets exceeds and will, immediately following the execution and delivery of the Loan Documents, be greater than each Borrower's probable liabilities, including the maximum amount of its contingent liabilities or its debts as such debts become absolute and mature. Each Borrower's assets do not and, immediately following the execution and delivery of the Loan Documents will not, constitute unreasonably small capital to carry out its business as conducted or as proposed to be conducted. None of the Borrowers intend to, nor do they believe that they will, incur debts and liabilities (including, without limitation, contingent liabilities and other commitments) beyond their ability to pay such debts as they mature (taking into account the timing and amounts to be payable on or in respect of obligations of each Borrower).

3.32 **Trademarks, Patents and Other Rights.** Set forth in Schedule 3.32 is a list and brief description of all patents, patent rights, patent applications, trademarks, trademark applications, service marks, service mark applications, trade names and copyrights, and all applications for such which are in the process of being prepared, are owned by, or are registered in the name of either Borrower, or of which any Borrower is a licensor or licensee, or in which any Borrower has any right, and in each case a brief description of the nature of such right. Each Borrower owns or possesses adequate licenses or other rights to use all patents, patent applications, trademarks, trademark applications, service marks, service mark applications, trade names, copyrights, manufacturing processes, formulae, trade secrets, and know how (collectively, "**Trade Rights**") necessary or desirable to the conduct of its business as conducted and as proposed to be conducted. No claim is pending or, to the knowledge of either Borrower, threatened to the effect that the operations of either Borrower infringe upon or conflict with the asserted rights of any other Person under any Trade Rights, and, to the knowledge of either Borrower, there is no basis for any such claim (whether or not pending or threatened). No claim is pending or, to the knowledge of either Borrower, threatened to the effect that any such Trade Rights owned or licensed by either Borrower or which such Borrower otherwise has the right to use, is invalid or unenforceable by such Borrowers, and there is no known basis for any such

claim (whether or not pending or threatened). All technical information developed by and belonging to each Borrower has been patented or has been kept confidential or has otherwise been established as a trade secret. Neither Borrower has granted or assigned to any other Person any right to sell or produce the products or proposed products or provide the services or proposed services of Borrowers. No officer, director, equity-holder or employee of Borrower has an ownership interest in any of the trademarks, patents, or other rights set forth in Schedule 3.32.

3.33 **Proprietary Information of Third Parties.** To the knowledge of each Borrower, no third party has claimed or has any reason to claim that any Person employed by either Borrower has: (i) violated or may be violating any of the material terms or conditions of his or her employment, non-competition, or non-disclosure agreement with such third party; (ii) disclosed or may be disclosing or utilized or may be utilizing any trade secret or proprietary information or documentation of such third party; or (iii) interfered or may be interfering in the employment relationship between such third party and any of its current or former employees. To the knowledge of either Borrower, no third party has requested information from either Borrower that suggests that such a claim might be contemplated. To the knowledge of either Borrower, no Person employed by either Borrower has employed or proposes to employ any trade secret or any information or documentation proprietary to any former employer, and no Person employed by either Borrower has violated any confidential relationship which such Person may have had with any third party in connection with the development or sale of any product or proposed product or the development or sale of any service or proposed service of either Borrower, and such Borrowers does not have any reason to believe there will be any such employment or violation. To the knowledge of either Borrower, none of the execution, delivery or performance of this Agreement, or the carrying on of the business of either Borrower as officers, employees, or agents by any officer, director, or key employee, or the conduct of the businesses of such Borrowers, will conflict with or result in a material breach of the terms, conditions, or provisions of, or constitute a default under any material contract, covenant, or instrument under which such Person is obligated.

3.34 **Insider Interests.** No present officer, director, equity holder or employee of, or supplier to, any Borrower: (i) owns, other than by virtue of a membership interest in a Borrower, directly or indirectly, in whole or in part, any of the properties used in the businesses of any Borrower; (ii) has received a loan or advance from either Borrower which is currently outstanding; (iii) has any obligation to make any loan to either Borrower other than as may be specifically contemplated by each Borrower's limited liability company operating agreement; or (iv) has any other business relationship with Borrowers other than in his, her or its capacity as an officer, director, equity holder or employee. No present officer, director, equity holder or employee of either Borrower owns, in whole or in part, directly or indirectly, any interest in excess of five percent (5%) in, or controls, or is an employee, officer, director, or partner of, or participant in, or consultant to, any corporation, association, partnership, limited partnership, joint venture, or other entity which is operating as a nursing facility or residential care facility within ten (10) miles of the Facility, of either Borrower.

3.35 **Fraud and Abuse.** Neither Borrower nor either Borrower's members, managers, officers, directors, or senior executives, or, to the knowledge of either Borrower, Persons who provide professional services under agreements with such Borrower, have engaged in any activities on behalf of or attributable to either Borrower which are prohibited under

federal Medicare and Medicaid statutes, 42 U.S.C. § 1320a-7b, or the regulations promulgated pursuant to such statutes or related state or local statutes or regulations or which are prohibited by rules of professional conduct, including but not limited to the following: (i) knowingly and willfully making or causing to be made a false statement or representation of a material fact in any application for any benefit or payment; (ii) knowingly and willfully making or causing to be made any false statement or representation of a material fact for use in determining rights to any benefit or payment; (iii) failing to disclose knowledge by a claimant of the occurrence of any event affecting the initial or continued right to any benefit or payment on its own behalf or on behalf of another, with intent to fraudulently secure such benefit or payment; (iv) knowingly and willfully soliciting or receiving any remuneration (including any kickback, bribe, or rebate), directly or indirectly, overtly or covertly, in cash or in kind or offering to pay such remuneration (a) in return for referring an individual to a Person for the furnishing or arranging for the furnishing of any item or service for which payment may be made in whole or in part by Medicare or Medicaid, or (b) in return for purchasing, leasing, or ordering or arranging for or recommending purchasing, leasing, or ordering any good, facility, service, or item for which payment may be made in whole or in part by Medicare or Medicaid, as applicable.

3.36 **Brokerage Commission.** Any brokerage commission or similar compensation amounts or fees due in connection with the purchase of the Property and in connection with the transactions contemplated hereby have been paid in full and any such commissions coming due in the future as related to any act of or on behalf of the Borrower will promptly be paid by Borrowers. Borrowers agree to and shall indemnify Lender from any liability, claims or losses (including reasonable attorneys' fees) incurred by Lender and arising by reason of any claim from any such brokerage commission that are the result of any action by or on behalf of the Borrowers. This provision shall survive the repayment of the Loan and shall continue in full force and effect so long as the possibility of such liability, claims or losses exists.

3.37 **Labor Matters.** As of the Closing Date, there are no strikes or other labor disputes pending or, to any Borrower's knowledge, threatened against Borrowers or any Guarantor. Hours worked and payments made to the employees of any Borrower and Guarantors have not been in violation of the Fair Labor Standards Act or any other applicable Law dealing with such matters. All payments due from Borrowers and Guarantors, or for which any claim may be made against any of them, on account of wages and employee and retiree health and welfare insurance and other benefits have been paid or accrued as a liability on their books, as the case may be. The consummation of the transactions contemplated by this Agreement and the other Loan Documents will not give rise to a right of termination or right of renegotiation on the part of any union under any collective bargaining agreement to which it is a party or by which it is bound.

3.38 **No Litigation**. There is no action, suit, claim, investigation or proceeding pending against, or to any Borrower's knowledge threatened against or affecting any Borrower or the Facility.

3.39 **Post Closing Date Covenants**. Borrower warrants and covenants to provide or cause to be provided to Lender:

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(i) On a date to occur within five months after the Closing Date, deliver all of the following to the Lender (such date, the "**Operations Closing Date**"):

- (a) Facility license in the name of the Operator;
- (b) Medicare number for the Operator;
- (c) Management Agreement, effective as of the Operations Closing Date;
- (d) Lease Agreement, effective as of the Operations Closing Date;
- (e) Assignment of Leases and Rents dated the Operations Closing Date;
- (f) Subordination and Attornment Agreement dated the Operations Closing Date;
- (g) Subordination and Assignment of Lease Agreement dated the Operations Closing Date;
- (h) Subordination and Assignment of Management Agreement dated the Operations Closing Date; and
- (i) Opinion of counsel dated the Operations Closing Date, addressing those matters required by Lender.

(ii) No later than seven months after the Closing Date, a new Medicaid provider number for the Operator;

(iii) Within ninety days of the Closing Date, a copy of the Certificate of Occupancy;

(iv) Within ten Business Days after the Closing Date, deliver to Lender the executed Control Agreement;

(v) Within ten Business Days after the Closing Date, deliver to Lender the executed ZBA Agreement.

#### **ARTICLE IV. AFFIRMATIVE COVENANTS OF BORROWERS**

Each Borrower, jointly and severally, agrees with and covenants unto the Lender that until the Loan Obligations have been paid in full, Borrowers shall:

4.1 **Payment of Loan/Performance of Loan Obligations.** Duly and punctually pay or cause to be paid the principal and interest of the Note in accordance with its

terms and duly and punctually pay and perform or cause to be paid or performed all Loan Obligations hereunder and under the other Loan Documents.

4.2 **Maintenance of Existence.** Maintain its existence as a limited liability company, and, in each jurisdiction in which the character of the property owned by it or in which the transaction of its business makes qualification necessary, maintain good standing.

4.3 **Maintenance of Single Purpose.** Maintain its existence as a Single Purpose Entity.

4.4 **Accrual and Payment of Taxes.**

(a) Borrowers shall pay, on or before the due date thereof, all Taxes, levies, license fees, permit fees and all other charges (in each case whether general or special, ordinary or extraordinary, or foreseen or unforeseen) of every character whatsoever (including all penalties and interest thereon) now or hereafter levied, assessed, confirmed or imposed on, or in respect of, or which may be a lien upon the Collateral or the Facility, or any part thereof, or any estate, right or interest therein, or upon the rents, issues, income or profits thereof, and shall submit to Lender such evidence of the due and punctual payment of all such Taxes, assessments and other fees and charges as may be required by law. Borrowers shall have the right before they become delinquent to contest or object to the amount or validity of any such Tax, assessment, fee or charge by appropriate legal proceedings, but this shall not be deemed or construed in any way as relieving, modifying or extending Borrowers' covenant to pay any such Tax, assessment, fee or charge at the time and in the manner provided herein, unless Borrowers have given prior written notice to Lender of Borrowers' intent to so contest or object, and unless (i) Borrowers shall demonstrate to Lender's satisfaction that the legal proceedings shall conclusively operate to prevent the sale of the Collateral and Facility, or any part thereof, to satisfy such Tax, assessment, fee or charge prior to final determination of such proceedings; and (ii) if required by Lender, Borrowers shall furnish a good and sufficient bond or surety as requested by and satisfactory to Lender in an amount sufficient to fully pay the contested amount, with penalties, interest and other charges if Borrowers should be unsuccessful in such contest; and (iii) Borrowers shall diligently pursue such contest.

(b) Borrowers shall pay, on or before the due date thereof, all Taxes, assessments, charges, expenses, costs and fees which may now or hereafter be levied upon, or assessed or charged against, or incurred in connection with, the Note, the Security Agreement or any other Loan Documents.

(c) Operator shall pay, on or before the due date thereof, all rents and other payments due under the Lease Agreement; and Borrowers shall pay all utility charges with respect to the Collateral and Facility, or which may become a charge or lien against the Collateral and the Facility, for gas, electricity, water and sewer services and the like furnished to the Collateral or the Facility, and all other public or private assessments or charges of a similar nature affecting the Collateral or the Facility or any portion thereof, whether or not the nonpayment of same may result in a lien thereon. Borrowers shall submit to Lender such evidence of the due and punctual payment of all such premiums, charges and other sums as Lender may require.

(d) Borrowers shall not suffer any mechanic's, materialman's, laborer's, statutory or other lien (except as expressly permitted by this Agreement) to be created or remain outstanding against the Collateral or the Facility; provided, however, that Borrowers may contest any such lien in good faith by appropriate legal proceedings provided the lien is bonded off and removed as

an encumbrance upon the Collateral or the Facility. Lender has not consented and will not consent to the performance of any work or the furnishing of any materials which might be deemed to create a lien or liens superior to the lien hereof.

(e) In the event of the passage of any state, federal, municipal or other governmental law, order, rule or regulation, subsequent to the date hereof, in any manner changing or modifying the laws now in force governing the taxation of mortgages or security agreements or debts secured thereby or the manner of collecting such Taxes so as to adversely affect Lender, Borrower will pay any such Tax on or before the due date thereof. If Borrowers fail to make such prompt payment or if, in the opinion of Lender, any such state, federal, municipal, or other governmental law, order, rule or regulation prohibits Borrowers from making such payment or would penalize Lender if Borrowers makes such payment or if, in the opinion of Lender, the making of such payment might result in the imposition of interest beyond the maximum amount permitted by applicable law, then the entire balance of the Loan Obligations shall, at the option of Lender, become immediately due and payable.

(f) Each Borrower hereby, jointly and severally, indemnifies and holds Lender harmless from any sales or use Tax that may be imposed on the Lender by virtue of Lender's Loan to Borrowers.

(g) During each fiscal year, make accurate provision for the payment of all current tax liabilities of all kinds (including, without limitation, federal and state income taxes, franchise taxes, payroll taxes, provider taxes (to the extent necessary to participate in and receive maximum funding pursuant to Reimbursement Contracts) and Taxes, all required withholding of income taxes of employees, all required old age and unemployment contributions, and all required payments to employee benefit plans, and pay the same when they become due including, but not limited to, making all required deposits into an escrow fund (the "**Tax and Insurance Reserve Fund**") in accordance with the terms of the Tax and Insurance Escrow and Security Agreement for the Senior Loan.

4.5 **Insurance.** Maintain the following insurance coverages with respect to the Property and the Facility:

(a) **Property Insurance.** Insurance against loss or damage by fire, casualty and other hazards as now are or subsequently may be covered by an "all risk" policy or a policy covering "special" causes of loss, with such endorsements as Lender may from time to time reasonably require and which are customarily required by institutional lenders of similar properties similarly situated, including, without limitation, building, ordinance or law, lightning, windstorm, civil commotion, hail, riot, strike, water damage, sprinkler leakage, collapse, malicious mischief, explosion, smoke, aircraft, vehicles, vandalism, falling objects and weight of snow, ice or sleet, and covering the Facility in an amount equal to one hundred percent (100%) of the full insurable replacement value of the Facility (exclusive of footings and foundations below the lowest basement floor) without deduction for depreciation. The determination of the

replacement cost amount shall be adjusted annually to comply with the requirements of the insurer issuing the coverage or, at Lender's election, by reference to such indexes, appraisals or information as Lender determines in its reasonable discretion, and, unless the insurance required by this paragraph shall be effected by blanket and/or umbrella policies in accordance with these terms, the policy shall include inflation guard coverage that ensures that the policy limits will be increased over time to reflect the effect of inflation. Each policy shall, subject to Lender's approval, contain (i) a replacement cost endorsement, without deduction for depreciation, (ii) either an agreed amount endorsement or a waiver of any co-insurance provisions, and (iii) an ordinance or law coverage or enforcement endorsement if the Improvements or the use of the Property constitutes any legal nonconforming structures or uses, and shall provide for deductibles in such amounts as Lender may permit in its sole discretion. The property insurance policy shall not contain an exclusion endorsement for mold.

(b) **Commercial General Liability Insurance.** Commercial general liability insurance under a policy containing "Comprehensive General Liability Form" of coverage on an occurrence or claims made basis with retroactive date to prior occurrence form, which policy shall include, without limitation, coverage against claims for personal injury, bodily injury, death and

property damage liability with respect to the Facility and the operations related thereto, whether on or off the Property, and the following coverages: Employee as Additional Insured, Employee Benefits, Product Liability/Completed Operations; Broad Form Contractual Liability, Independent Contractor, Personal Injury and Advertising Injury Protection, Medical Payment (with a minimum limit of \$5,000 per person), hired and non-owned automobile coverage (including rented and leased vehicles), and, if any alcoholic beverages shall be sold, manufactured or distributed in the Facility, liquor liability coverage, all of which shall be in such amounts as Lender may from time to time reasonably require, but not less than One Million Dollars (\$1,000,000) per occurrence, Three Million Dollars (\$3,000,000) in the aggregate. If such policy shall cover more than one property, such limits shall apply on a “per location” basis. If any elevators, health club facilities or swimming pools are located at the Facility at any time during the Loan, the foregoing amounts shall be increased to Three Million Dollars (\$3,000,000) and Five Million Dollars (\$5,000,000), respectively, unless other amounts are approved in writing by Lender in its sole discretion. Such liability policy shall delete the contractual exclusion under the personal injury coverage, if possible, and if available, shall include the following endorsements: Notice of Accident, Knowledge of Occurrence, and Unintentional Error and Omission. Absent written consent from Lender, Borrowers shall not change, cancel or renew the terms of such policy in any manner that would materially lessen the amount and scope of such insurance coverage applicable to the Property and Facility. The commercial general liability policy shall not contain an exclusion endorsement for mold.

(c) Professional Liability Insurance. Professional liability insurance, whenever possible provided by the same carrier as the Commercial General Liability coverage, in an amount equal to One Million Dollars (\$1,000,000) per occurrence and Three Million Dollars (\$3,000,000) in the aggregate and insuring Borrowers from acts occurring prior to the date of the Loan, unless other amounts are approved by Lender in writing at its sole discretion.

(d) Business Interruption Insurance/Extra Expense Coverage. Business interruption income insurance (i) covering the same perils of loss as are required to be covered by the property insurance described above, (ii) in an amount equal to the greater of: (1)

the projected annual net income from the Facility plus carrying costs and extraordinary expenses of the Property for a period of twenty-four (24) months, based upon Borrower’s reasonable estimate thereof as approved by Lender; provided, however, that if fifty-percent (50%) of the estimated annual expenses of the Facility is greater than such calculation of net income, then Borrowers shall, for purposes of this test, use such amount, or (2) or actual loss sustained, in either case with no cap, (iii) including either an agreed amount endorsement or a waiver of any co-insurance provisions, so as to prevent any Borrower, Lender and any other insured thereunder from being a coinsurer, and (iv) providing that any covered loss thereunder shall be payable to Lender.

(e) Construction Insurance. During the period of any new construction on the Property, a so-called “Builder’s All-Risk Completed Value” or “Course of Construction” insurance policy in non-reporting form for any improvements under construction, including, without limitation, for demolition and increased cost of construction or renovation, in an amount equal to one hundred percent (100%) of the estimated replacement cost value on the date of completion, including “soft cost” coverage, FF&E and Workers’ Compensation Insurance covering all persons engaged in such construction, in an amount at least equal to the minimum required by law. In addition, each contractor and subcontractor shall be required to provide Lender with a certificate of insurance for (i) Workers’ Compensation insurance covering all persons engaged by such contractor or subcontractor in such construction in an amount at least equal to the minimum required by law, (ii) General Liability insurance showing minimum limits of at least One Million Dollars (\$1,000,000) per occurrence and Two Million Dollars (\$2,000,000) in the aggregate, where Borrowers and Lender have additional insured status on a primary and non-contributory basis with both forms CG 2010 (ongoing operations) and CG 2037 (completed operations) or its equivalent including coverage for products and completed operations, (iii) Automobile Liability insurance showing minimum limits of at least One Million Dollars (\$1,000,000) covering all owned autos, hired and non-owned autos (including rented and leased vehicles).and (iv) statutory Workers Compensation with Employers Liability limits of \$1,000,000 for each accident, each disease and each disease policy limit. Each contractor and subcontractor also shall cover Borrowers and Lender as an additional insured under all liability policies (excluding Professional Liability, Workers Compensation & Employers Liability) and shall



indemnify and hold Borrowers and Lender harmless from and against any and all claims, damages, liabilities, costs and expenses arising out of, relating to or otherwise in connection with its performance of such construction. Each contractor shall waive all rights of recovery and shall cause its insurance carriers to waive their subrogation rights against the Lender, Borrowers and affiliated entities, for damages covered by the insurance required.

(f) Boiler and Machinery Equipment Breakdown Coverage. If the Facility contains steam boilers, steam pipes, steam engines, steam turbines or other high pressure vessels, insurance covering the major components of the central heating, air conditioning and ventilating systems, boilers, other pressure vessels, high pressure piping and machinery, elevators and escalators, if any, and other similar equipment installed in the Improvements, in an amount equal to the coverage as defined under the Property Insurance, which policies shall insure against physical damage to and loss of occupancy and use of the improvements arising out of an accident or breakdown covered thereunder.

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(g) Flood. If the Facility is located in a High Risk Flood Area, as defined by FEMA, flood coverage in the amount of \$1,000,000 is required. If the Facility is located in an area covered by the National Flood Insurance Program, the Borrowers shall carry the maximum federal amount of \$500,000 and additionally will carry a Differences in Conditions policy.

(h) Wind and Hurricane Insurance. If the Facility is located in Wind Zone 3 or 4, there must be no policy restrictions with regard to “Wind”, “Windstorm”, “Hail”, “Named Storm” and “Hurricane”. Any restrictions in coverage and/or deductibles must be reviewed and approved by Lender.

(i) Earthquake Insurance. If the Facility is located in Seismic Zone 3 or 4, earthquake coverage must be obtained in an amount equal to the coverage as defined under the Property Insurance.

(j) Workers’ Compensation/Employer’s Liability Insurance. Workers’ compensation insurance or other similar insurance which may be required by governmental authorities or applicable Legal Requirements in an amount at least equal to the minimum required by law, and employer’s liability insurance with a limit of One Million Dollars (\$1,000,000) per accident and per disease per employee, and One Million Dollars (\$1,000,000) in the aggregate for disease arising in connection with the operation of the Property. If the Facility is located in a monopolistic state, a Stop Gap Endorsement must be added to the General Liability policy.

(k) Automobile Liability Insurance. Borrowers must obtain Automobile Liability Insurance coverage in the amount of \$1,000,000. If the Facility does not own any vehicles, then hired and non-owned automobile endorsement (including rented and leased vehicles) must be obtained.

(l) Term and Other Requirements. All insurance required under this Agreement must have a term of not less than one year and shall be in the form and amount and with deductibles as, from time to time, shall be acceptable to Lender in its sole discretion, under valid and enforceable policies issued by financially responsible insurers either licensed to transact business in the state where the Facility is located, or obtained through a duly authorized surplus lines insurance agent or otherwise in conformity with the laws of such state, with a (i) rating of not less than the fourth (4<sup>th</sup>) highest rating category by either Standard & Poor’s Ratings Group, Duff & Phelps Credit Rating Co., Moody’s Investors Service, Inc., Fitch Investors Service, Inc. or any successors thereto, or (ii) an A-V rating in Best’s Key Rating Guide. Originals or certified copies of all insurance policies shall be delivered to and held by Lender. All such policies shall name Lender as an additional insured, shall provide for loss payable solely to Lender and shall contain: (A) a standard “non-contributory mortgagee endorsement or its equivalent relating, inter alia, to recovery by Lender notwithstanding the negligent or willful acts or omissions of Borrowers and notwithstanding (1) occupancy or use of the Facility for purposes more hazardous than those permitted by the terms of such policy, (2) any foreclosure or other action taken by Lender pursuant to the Security

Agreement or the other Loan Documents upon the occurrence of a default, or (3) any change in title or ownership of the Facility; and (B) a provision that such policies shall not be canceled or amended, including, without limitation, any

amendment reducing the scope or limits of coverage, or failed to be renewed, without at least thirty (30) days prior written notice to Lender in each instance. With respect to insurance policies which require payment of premiums annually, not less than thirty (30) days prior to the expiration dates of the insurance policies obtained pursuant to this Agreement, Borrowers shall pay such amounts; provided, however, to the extent Lender has required Borrowers to deposit funds in an escrow therefor, Borrowers shall instead fund such escrow, as directed by Lender. Not less than thirty (30) days prior to the expiration dates of the insurance policies obtained pursuant to this Agreement, originals or certified copies of renewals of such policies (or certificates evidencing such renewals) bearing notations evidencing the payment of premiums or accompanied by other evidence satisfactory to Lender of such payment, which premiums shall not be paid by Borrowers through or by any financing arrangement, shall be delivered by Borrowers to Lender. Borrowers shall carry separate insurance, concurrent in kind or form or contributing in the event of loss with any insurance required by this Section 4.5. If the limits of any policy required hereunder are reduced or eliminated due to a covered loss, Borrowers shall pay the additional premium, if any, in order to have the original limits of insurance reinstated, or Borrowers shall purchase new insurance in the same type and amount that existed immediately prior to the loss.

(m) Lender's Right to Procure Insurance. If Borrowers fail to maintain and deliver to Lender the original policies and/or certificates of insurance required, Lender may, at its option, procure such insurance and Borrowers shall pay or, as the case may be, reimburse Lender for, all premiums thereon promptly, upon demand by Lender, with interest thereon at the Default Rate from the date paid by Lender to the date of repayment and such sum shall constitute a part of all obligations related to the Loan.

(n) Use of Blanket and Umbrella Policies. The insurance required may, at the option of Borrowers, be effected by blanket and/or umbrella policies issued to Borrowers or to an Affiliate of Borrowers covering the Facility and the properties of such Affiliate; provided that, in each case, the policies otherwise comply with the provisions of this Agreement and allocate to the Facility, from time to time, the coverage specified by this Agreement, without possibility of reduction or coinsurance by reason of, or damage to, any other property (real or personal) named therein. If the insurance required by this Agreement shall be affected by any such blanket or umbrella policies, Borrowers shall furnish to Lender original policies or certified copies thereof, with schedules attached thereto showing the amount of the insurance provided under such policies which are applicable to the Facility. Additionally, umbrella coverage of no less than Five Million Dollars (\$5,000,000) in the aggregate, will extend over General Liability, Professional Liability, Automobile Liability, and Employer's Liability.

(o) Subrogation Rights. Neither Lender nor its agents or employees shall be liable for any loss or damage insured by the insurance policies required to be maintained under this Agreement; it being understood that (i) Borrowers shall look solely to their insurance company for the recovery of such loss or damage, (ii) such insurance company shall have no rights of subrogation against Lender, its agents or employees, and (iii) Borrowers shall use their best efforts to procure from such insurance company a waiver of subrogation rights against Lender. If, however, such insurance policies do not provide for a waiver of subrogation rights against Lender (whether because such a waiver is unavailable or otherwise), then Borrowers hereby agree, to the extent permitted by law and to the extent not prohibited by such insurance

policies, to waive their respective rights of recovery, if any, against Lender, its agents and employees, whether resulting from any damage to the Facility, any liability claim in connection with the Facility or otherwise. If any such insurance policy shall prohibit Borrowers from waiving such claims, then Borrowers must obtain from such insurance company a waiver of subrogation rights against Lender.

(p) Condemnation and Casualty Loss. In the event of condemnation or casualty loss, the entire award of insurance proceeds as a result thereof will be assigned to Lender with authorization, at Lender's option, to apply all or a portion thereof up to the outstanding principal balance of the Loan and to any other Loan Obligations or to release amounts in excess of such outstanding obligations related to the Loan to Borrowers, at Lender's option in its sole discretion.

(q) Use of Proceeds of Insurance or Condemnation. At its option, Lender agrees that Lender shall make the net proceeds of insurance or condemnation (after payment of Lender's reasonable costs and expenses) available to Borrowers for Borrowers' repair, restoration and replacement of the improvements on the Property, the equipment and the inventory damaged or taken on the following terms and subject to Borrowers' satisfaction of the following conditions:

- (i) The aggregate amount of all such proceeds shall not exceed the aggregate amount of all such Loan Obligations;
- (ii) At the time of such loss or damage and at all times thereafter while Lender is holding any portion of such proceeds, there shall exist no Default or Event of Default;
- (iii) The Improvements, Equipment, and Inventory for which loss or damage has resulted shall be capable of being restored to its preexisting condition and utility in all material respects with a value equal to or greater than that which existed prior to such loss or damage and such restoration shall be capable of being completed prior to the earlier to occur of (A) the expiration of business interruption insurance as determined by an independent inspector or (B) the Maturity Date;
- (iv) Within thirty (30) days from the date of such loss or damage Borrowers shall have given Lender a written notice electing to have the proceeds applied for such purpose;
- (v) Within sixty (60) days following the date of notice under the preceding subparagraph (c) and prior to any proceeds being disbursed to Borrowers, Borrowers shall have provided to Lender all of the following:

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(A) complete plans and specifications for restoration, repair and replacement of the Improvements, Equipment and Inventory damaged to the condition, utility and value required by (a) above,

(B) if loss or damage exceeds \$50,000, fixed-price or guaranteed maximum cost bonded construction contracts for completion of the repair and restoration work in accordance with such plans and specifications,

(C) builder's risk insurance for the full cost of construction with Lender named under a standard mortgagee loss-payable clause,

(D) such additional funds as in Lender's reasonable opinion are necessary to complete such repair, restoration and replacement, and

(E) copies of all permits and licenses necessary to complete the work in accordance with the plans and specifications;

- (vi) Lender may, at Borrowers' expense, retain an independent inspector to review and approve plans and specifications and completed construction and to approve all requests for disbursement, which approvals shall be conditions precedent to release of proceeds as work progresses;
- (vii) No portion of such proceeds shall be made available by Lender for architectural reviews or for any other purposes which are not directly attributable to the cost of repairing, restoring or replacing the Improvements, Equipment and Inventory for which a loss or damage has occurred unless the same are covered by such insurance;
- (viii) Borrowers shall diligently pursue such work and shall complete such work prior to the earlier to occur of the expiration of business interruption insurance or the Maturity Date;
- (ix) Each disbursement by Lender of such proceeds and deposits shall be funded subject to conditions and in accordance with disbursement procedures which a commercial construction lender would typically establish in the exercise of sound banking practices and shall be made only upon receipt of disbursement requests on an AIA G702/703 form (or similar form approved by the Lender) signed and certified by Borrowers and, if required by Lender, its architect and general contractor with appropriate invoices and lien waivers as required by Lender; and

- (x) Lender shall have a second lien and security interest in all building materials and completed repair and restoration work and in all fixtures and equipment acquired with such proceeds, and each Borrower shall, as applicable, execute and deliver such mortgages, deeds of trust, security agreements, financing statements and other instruments as Lender shall request to create, evidence, or perfect such lien and security interest.

(r) Use of Insurance Proceeds to Set Off Loan Obligations. In the event and to the extent such proceeds are not required or used for the repair, restoration and replacement of the Improvements, Equipment and Inventory for which a loss or damage has occurred, or in the event Lender does not permit Borrowers to have the insurance proceeds applied to the restoration of the Improvements, Equipment, or Inventory, or, if the conditions set forth herein for such application are otherwise not satisfied, then Lender shall be entitled without notice to or consent from Borrowers to apply such proceeds, or the balance thereof, at Lender' s option either (i) to the full or partial payment or prepayment of the Loan Obligations (without premium) in the manner aforesaid, or (ii) to the repair, restoration and/or replacement of all or any part of such Improvements, Equipment and Inventory for which a loss or damage has occurred.

(s) Appointment as Attorney-in-Fact. Each Borrower appoints Lender as such Borrower' s attorney-in-fact to cause the issuance of or an endorsement of any insurance policy to bring Borrowers into compliance herewith and, as limited above, at Lender' s sole option, to make any claim for, receive payment for, and execute and endorse any documents, checks or other instruments in payment for loss, theft, or damage covered under any such insurance policy; provided, however, in no event will Lender be liable for failure to collect any amounts payable under any insurance policy.

(t) Changes in Insurance Coverage. Lender acknowledges that certain coverage amounts described above may not be commercially reasonable or available to attain or maintain. Lender reserves the right in its sole discretion to approve lesser amounts of coverage or approve modifications to the required types of insurance. Notwithstanding the foregoing, if the Lender

determines in its reasonable discretion based on its experience with the long term care industry, generally, that insurance coverage in excess of the amounts currently maintained by the Borrowers or on an “occurrence” basis or any other modification to the insurance requirements are necessary and are available for the Borrowers at premiums not materially in excess of the premiums then being paid by Borrowers, then Borrowers shall be obligated to procure coverage as determined by Lender.

(u) Other Insurance. Lender may require such other insurance coverages, in such amounts, and such other forms and endorsements, as may from time to time be required by Lender and which are customarily required by institutional lenders to similar properties in the state the Facility is located in, similarly situated, including, without limitation, coverages against other insurable hazards, which at the time are commonly insured against and generally available at commercially reasonable premiums.

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(v) Escrow for Insurance. Borrowers shall deposit funds for payment of insurance premium in accordance with the Tax and Insurance Escrow and Security Agreement.

4.6 **Financial and Other Information**. Provide Lender the following financial statements and information on a continuing basis during the term of the Loan:

(a) Annual Financial Statements. Within ninety (90) days after the end of each fiscal year of the Facility, for each Borrower and Management Company, reviewed financial statements, and for AdCare Health Systems, Inc., audited financial statements (including a balance sheet, a cash flow statement and a statement of income and expenses for the reporting year) prepared by a nationally recognized accounting firm or independent certified public accountant acceptable to Lender and certified to by the respective financial officer as being true and correct.

(b) Annual Disclosure Certificate. Within thirty (30) days after the end of each fiscal year, an annual disclosure certificate in the form provided for in Exhibit D attached hereto certified by the chief financial officer of each Borrower.

(c) Quarterly Compliance Certificate. Within forty-five (45) days after the end of each fiscal quarter of the Facility, furnish to Lender a quarterly compliance certificate in the form attached hereto as Exhibit E certified by the chief financial officer of each Borrower.

(d) Quarterly Financial Statements. Within forty-five (45) days after the end of each fiscal quarter of the Facility, for each Borrower, the Management Company and any Corporate Guarantor, financial statements (including a balance sheet, cash flow statement and a statement of income and expenses for the reporting quarter) certified to by the respective financial officer as being true and correct.

(e) Monthly Financial Statements. Within thirty (30) days after the end of each month current financial statements for the Facility, prepared in accordance with GAAP consistently applied, which statements shall include a balance sheet, cash flow statement, a statement of income and expenses for the month then ended and a statement of the number of bed days available and the actual patient days incurred for the month, together with monthly census information of the Facility as of the end of such month in sufficient detail to show patient-mix on a daily average basis for such year through the end of such month, certified by a financial officer of each Borrower to be true and correct.

(f) Copies of Tax Returns. As soon as available, but in no event more than thirty (30) days after the filing deadline, as may be extended from time to time, copies of all federal, state and local tax returns of each Borrower and each Guarantor, together with all supporting documentation and required schedules.

(g) Copies of Medicare and Medicaid Cost Reports. As applicable, within ten (10) Business Days of filing or receipt, (i) all Medicaid and Medicare cost reports and any amendments thereto filed with respect to the Facility and all responses, audit reports, or other inquiries with respect to such cost reports and (ii) copies of all licensure and state and federal inspection reports, if applicable, with an attached plan of correction.

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(h) Copies of Medicaid and Medicare Rate Calculation Worksheet. As applicable, within ten (10) Business Days of receipt, a copy of the Medicaid and Medicare Rate Calculation Worksheet (or the equivalent thereof) issued by the appropriate agency for the Facility.

(i) Copies of Downgrade Notices. Within three (3) days of receipt, any and all notices (regardless of form) from any and all licensing and/or certifying agencies that license the Facility and/or the Medicare and/or Medicaid certification of the Facility that the Facility is being downgraded to a substandard category, revoked, or suspended or that any such action is pending or being considered to downgrade to a substandard category, revoke or suspend the Facility's license.

(j) Evidence of Payment of Bed Taxes. Upon request by Lender, evidence of payment by Borrowers of any applicable provider bed taxes or similar taxes with respect to the Facility, which taxes Borrowers agree to pay or cause to be paid.

(k) Aged Accounts Receivable/Payable Report. Within thirty (30) days after the end of each calendar month, (i) an aged accounts receivable report of the Facility in sufficient detail to show amounts due from each class of unit or patient-mix (i.e., private, Medicare, Medicaid and V.A.) by the account age classifications of 30 days, 60 days, 90 days, 120 days, and over 120 days, (ii) monthly census information of the Facility in sufficient detail to show unit or patient mix on a daily average basis for such month and (iii) an accounts payable report of the Facility.

(l) Report Regarding Resident Days and Medicare or Medicaid Default Rate. As applicable, within ten (10) Business Days of receipt, a statement of the number of patient days for which the Facility has received the Medicare default rate for any applicable period. For purposes herein, "default rate" shall have the meaning ascribed to it in that certain Medicare or Medicaid rate notification letter prepared in connection with any review or survey of the Facility.

(m) Copies of Inspection Reports. Within ten (10) Business Days of receipt, copies of all licensure and state or federal inspection reports, if applicable, with attached plan of correction. Borrowers shall correct any deficiency on any report delivered pursuant to this Section 4.6 or otherwise received by Borrowers within the date required by the Health Regulatory Authority or other such government agency.

(n) Payment of Taxes and Insurance. Borrowers shall deliver to Lender on a monthly or quarterly basis (as determined by Lender in accordance with the requirements of the applicable taxing authorities) evidence that Borrowers have paid or caused to be paid all insurance premiums and all Taxes, charges, claims for labor, supplies, rent or other obligations which, if unpaid, might give rise to a Lien against the property of Borrowers (except Liens permitted by this Agreement), that were due and payable by Borrowers during such previous month or quarter, as the case may be (each a "**Tax and Insurance Report**").

(o) SBA Requirements. Within twenty (20) days after the end of each fiscal quarter, a completed SBA Form 468/Economic Data Portfolio Concern in the form

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attached hereto as Exhibit F and such other documents and agreements as may be required to be delivered to the Small Business Administration, all as directed by the Lender.

(p) Insurance Captive. Within ninety (90) days after the end of each fiscal year, a loss run history on the entire insurance captive, if an insurance captive is utilized for the Facility.

(q) Independent Audit of Accounts Receivable. Upon Lender's request, but no often than once per year, and/or, upon an Event of Default, Borrowers shall submit the results of an audit of its accounts receivable and cash collections in form and substance acceptable to Lender, in Lender's sole discretion, and performed by an independent third party auditor approved by Lender, which audits will be performed at Borrowers' expense.

(r) Reports Regarding Claims. Within three (3) Business Days of being (a) presented with a claim or claims in an amount in excess of Fifty Thousand Dollars (\$50,000) against any insurance policy for the Facility related any facility under that policy or (b) presented with any claim against the Facility, a report and/or notice identifying the amount and related loss of such claim.

(s) Affiliates Facilities Reports. Should a health care facility owned by an Affiliate of any Borrower (whether or not financed by Lender or its Affiliate) be either decertified (or action taken in pursuance thereof) or is subject to a denial of new admissions, the Borrowers or the applicable Affiliate shall provide Lender with a written notice of such events.

(t) Accounts List. Within thirty (30) days after the end of each fiscal year, within five (5) Business Days of opening or closure of any account or upon Lender's request, deliver a comprehensive list of all bank accounts associated with any Borrower or the Facility and all subsidiaries thereof including, without limitation: (i) the designated number associated with each account; (ii) the name of the bank or financial institution where the account is held; and (iii) the type of account.

(u) Audited Financials. If not already required, the Lender reserves the right to require that the annual financial statements of each Borrower and the Management Company be audited and prepared by a nationally recognized accounting firm or independent certified public accountant acceptable to Lender, at Borrowers' respective cost and expense, if (i) an Event of Default has occurred or (ii) if Lender has reasonable grounds to believe that the unaudited financial statements do not accurately represent the financial condition of each Borrower, the Management Company or any Corporate Guarantor, as the case may be.

(v) Additional Information. Lender further reserves the right to require such other information of Borrowers, the Management Company, Guarantors and/or the Facility, in such form and at such other times (including monthly or more frequently) as Lender shall deem necessary, and Borrowers agree promptly to provide or to cause to be provided, such information to Lender.

(w) Statutory Rights. The provisions of this Section 4.6 shall not be in limitation of any rights which the Lender may have under any applicable law with respect to the

books and records of the Borrowers or to inspect the Facility of to discuss its affairs, finances and accounts.

(x) Borrowing Base Certificate. Borrowers shall submit a Borrowing Base Certificate: (1) in connection with each Draw updated for estimated billings and actual collections since the prior submission and (2) monthly, by the fifteenth (15th) day of each month, commencing on the month of the Operations Closing Date, regardless if there is a Draw.

#### 4.7 Government Receivables Account and Loan Account.

- (a) By no later than ten Business Days after the Closing Date, Borrowers shall establish the Government Receivables Account consistent with the definition of such term herein.
- (b) By no later than ten Business Days after the Closing Date, Borrowers shall establish the Loan Account consistent with the definition of such term herein.
- (c) By no later than ten Business Days after the Closing Date, Borrowers shall establish the Payroll Account consistent with the definition of such term herein.
- (d) By no later than ten Business Days after the Closing Date, Borrowers will enter into the ZBA Agreement pursuant to which monies on deposit in the Government Receivables Account and Payroll Account will be swept and deposited to the Loan Account.
- (e) By no later than ten Business Days after the Closing Date, Borrowers will enter into the Control Agreement with the Lender and the Facility Bank.
- (f) Borrowers will cause all Facility revenue that is not required to be deposited into the Government Receivables Account to be deposited to the Loan Account.
- (g) No Borrower shall close the Government Receivables Account, Payroll Account nor the Loan Account nor change the procedures or sweep instructions under the ZBA Agreement.
- (h) No checks, drafts or other Instruments received by Lender shall constitute final payment for the Loan to Lender unless and until such Instruments have actually been collected.
- (i) Borrowers acknowledge and agree that compliance with the terms of this section is essential, and that Lender will suffer immediate and irreparable injury and have no adequate remedy at law, if Borrowers, through acts or omissions, cause or permit Facility revenues to be deposited to other than the Government Receivables Account or Loan Account. Accordingly, in addition to all other rights and remedies of Lender hereunder, Lender shall have the right to seek specific performance of the Borrowers' obligations under this section and any other equitable relief as Lender may deem necessary or appropriate, and Borrowers waive any requirement for the posting of a bond in connection with such equitable relief.

- (j) If any Borrower breaches its obligation hereunder, Lender, as the irrevocably made, constituted and appointed true and lawful attorney for Borrowers, may upon prior notice to Borrowers, by the signature or other act of any of Lender's officers (without requiring any of them to do so), direct any account debtor to pay Facility revenues to the Loan Account or Government Receivables Account, as applicable.
- (k) Each Borrower agrees not to open any lockbox or new bank account into Facility revenues are to be delivered or deposited unless concurrently with the opening of such account, Lender, such Borrower and the bank which will maintain such account, execute a new agreement on terms substantially similar to the ZBA Agreement and Control Agreement, as applicable, with respect to such account.

4.8 **Books and Records.** Keep and maintain at all times at the Facility or the Management Company's offices, and upon Lender's request shall make available at the Facility, complete and accurate books of account and records (including copies of supporting bills and invoices) adequate to reflect correctly the results of the operation of the Facility, and copies of all written contracts,



subleases (if any), and other instruments which affect the Property, which books, records, contracts, leases (if any) and other instruments shall be subject to examination and inspection at any reasonable time by Lender (upon reasonable advance notice, which for such purposes only may be given orally, except in the case of an emergency or following an Event of Default, in which case no advance notice shall be required); provided, however, that if an Event of Default has occurred and is continuing, Borrowers shall deliver to Lender upon written demand all books, records, contracts, subleases (if any) and other instruments relating to such Facility or its operation and Borrowers authorize Lender to obtain a credit report on Borrowers at any time at Borrowers' sole cost and expense.

4.9 **Payment of Indebtedness.** Duly and punctually pay or cause to be paid all other Indebtedness now owing or hereafter incurred by Borrowers in accordance with the terms of such Indebtedness, except such Indebtedness owing to those other than Lender which is being contested in good faith and with respect to which any execution against properties of Borrowers has been effectively stayed and for which reserves and collateral for the payment and security thereof have been established as determined by Lender in its sole discretion.

4.10 **Notice of Loss.** Immediately notify the Lender of any event causing a loss or depreciation in value of either Borrower' s assets in excess of \$10,000 or any Guarantor' s assets in excess of the amount required by their Guaranty Agreement and the amount of such loss or depreciation, except Borrowers shall not be required to notify Lender of depreciation in Equipment resulting from ordinary use thereof.

4.11 **Records of Accounts.** Maintain all records, including records pertaining to the Accounts of each Borrower, at the chief executive office of each Borrower as set forth in this Agreement.

4.12 **Conduct of Business.** Conduct the operation of the Facility at all times in a manner consistent with the level of operation of the Facility as of the date hereof, including without limitation, the following:

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(a) to maintain the standard of care for the patients of the Facility at all times at a level necessary to ensure quality care for the patients of the Facility in accordance with customary and prudent industry standards;

(b) to operate the Facility in a prudent manner and in compliance with applicable laws and regulations relating thereto and cause all Permits, Reimbursement Contracts, and any other agreements necessary for the use and operation of the Facility or as may be necessary for participation in the Medicaid, Medicare or other applicable reimbursement programs to remain in effect without reduction in the number of licensed beds authorized for use in the Medicaid, Medicare or other applicable reimbursement programs;

(c) to maintain sufficient Inventory and Equipment of types and quantities at the Facility to enable Borrowers adequately to perform operations of the Facility;

(d) to keep all Improvements and Equipment located on or used or useful in connection with the Facility in good repair, working order and condition, reasonable wear and tear excepted, and from time to time make all needed and proper repairs, renewals, replacements, additions, and improvements thereto to keep the same in good operating condition;

(e) to maintain sufficient cash in the operating accounts of the Facility in order to satisfy the working capital needs of the Facility and not to comingle funds of the Facility and the Borrowers with any other funds; provided, however, that any cash or equity contributions shall not be deemed commingled funds and provided further, however, that any of such contributions that are deemed loans must be subject to a subordination agreement approved by the Lender; and

(f) to keep all required Permits current and in full force and effect.

4.13 **Minimum Financial Covenants.** Borrowers on a consolidated basis shall maintain the following:

(a) **Current Ratio.**

- (i) Borrowers shall maintain a Current Ratio (as defined below) of 1.0 to 1.0 commencing at the end of the first fiscal quarter after the Closing Date and thereafter as tested on a quarterly basis at the end of each quarter for the term of the Loan; and
- (ii) For the purposes of this Agreement, “**Current Ratio**” shall mean Current Assets divided by Current Liabilities. “**Current Assets**” shall mean, only with respect to the Facility, cash, accounts receivable aged less than 90 days (any other receivable in such calculation to be approved by Lender), inventory, marketable securities, prepaid expenses and other assets that can be converted to cash within one year, excluding, at the sole discretion of the Lender, accounts or Indebtedness due to or from Affiliates of the

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Borrowers. “**Current Liabilities**” shall mean, only with respect to the Facility, accounts payable, short term loans, expenses incurred but unpaid and other debts due within one year, excluding, at the sole discretion of the Lender, accounts or Indebtedness due to or from Affiliates of the Borrowers.

(b) **Liquidity.** Borrowers on a consolidated basis shall at all times during the term of the Loan maintain cash, or availability under a line of credit, including availability under the Loan, of no less than Two Hundred Fifty Thousand and no/ 100 Dollars (\$250,000.00).

(c) If any Borrower fails to achieve or provide evidence of achievement of the Current Ratio for the Facility, provided there is no continuing Default or Event of Default under the Loan Documents and provided, further, that there has never been a default under Section 6.1(a) of this Agreement, Borrowers may deposit with Lender, at Borrowers’ option within thirty (30) days of such failure, additional cash or other liquid collateral in an amount which would have resulted in the noncomplying Current Ratio requirement having been satisfied. If after Borrowers have deposited such additional cash or liquid collateral, any Borrower again fails to achieve or provide evidence of the achievement of the Current Ratio for the Facility requirements set forth above and such failure continues for a second consecutive quarter, Borrowers may deposit with Lender, at Borrowers’ option within thirty (30) days of such failure, additional cash or other liquid collateral (with credit for amounts currently being held by Lender pursuant to the foregoing sentence), in an amount which would have resulted in the noncomplying Current Ratio requirement for such quarter having been satisfied. Borrowers shall not have the option to cure for failure to comply for any additional consecutive quarters and such an event will constitute an Event of Default under this Agreement. Any additional cash or liquid collateral deposited by Borrowers hereunder in order to achieve the required Current Ratio for the Facility and cure any existing default with respect thereto will be held by Lender in a standard custodial account and shall constitute additional collateral for the obligations related to the Loan and an “Account” as defined in this Agreement, and, upon the occurrence of a default, may be applied by Lender, in such order and manner as Lender may elect, to the reduction of the obligations related to the Loan. Borrowers shall not be entitled to any interest earned on such additional collateral. Provided that there is no outstanding Default or Event of Default, such additional collateral which has not been applied to the Loan Obligations will be released by Lender at such time as Borrowers provided Lender with evidence that the required minimum Current Ratio requirement set forth above has been achieved and maintained (without regard to any cash or liquid collateral deposited pursuant to this section) for two (2) consecutive fiscal quarters.

Notwithstanding anything herein to the contrary, any additional liquid collateral posted by Borrowers under the Senior Loan Agreement for purposes of satisfying this covenant, if the lender thereof is an Affiliate of the Lender, shall be deemed to satisfy the requirements herein.

Borrowers shall be required to supply Lender with a certificate evidencing compliance with the requirements of this Section, which certificate shall be signed by an officer

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or manager as appropriate.

#### 4.14 **Debt Service Coverage Requirements.**

(a) **Debt Service Coverage Ratio.** Borrowers on a consolidated basis shall maintain and provide evidence to Lender of the achievement of a Debt Service Coverage Ratio and Total Debt Service Coverage Ratio for the Facility of (i) not less than 1.00 to 1.00 as tested on a quarterly basis at the end of the first full fiscal quarter ending December 31, 2012 and the second fiscal quarter ending March 31, 2013, and thereafter, (ii) 1.15 to 1.00 as tested on a quarterly basis at the end of each quarter, beginning with the last day of the third fiscal quarter after the Closing Date and continuing thereafter for the term of the Loan. Borrowers may include any outstanding amounts in the Capitalized Interest Reserve Account in such calculations.

This Debt Service Coverage Ratio and Total Debt Service Coverage Ratio will be measured as follows: (A) for a trailing three month period tested at the end of the first fiscal quarter following the Closing Date, (B) for the second fiscal quarter following the Closing Date and for a trailing six month period tested at the end of such quarter, (C) for the third fiscal quarter following the Closing Date, and for a trailing nine month period tested at the end of such quarter, and (iv) thereafter, tested quarterly and for a trailing twelve month period from the end of such quarter.

(b) If any Borrower fails to achieve or provide evidence of achievement of the Debt Service Coverage Ratio or Total Debt Service Coverage Ratio for the Facility, provided there is no continuing Default or Event of Default under the Loan Documents and provided, further, that there has never been a Default under Section 6.1(a) of this Agreement, Borrowers may deposit with Lender, at Borrowers' option within thirty (30) days of such failure, additional cash or other liquid collateral in an amount which would have resulted in the noncomplying Debt Service Coverage Ratio or noncomplying Total Debt Service Coverage Ratio requirement having been satisfied. If after Borrowers have deposited such additional cash or liquid collateral, any Borrower again fails to achieve or provide evidence of the achievement of the Debt Service Coverage Ratio or Total Debt Service Coverage Ratio for the Facility requirements set forth above and such failure continues for a second consecutive quarter, Borrowers may deposit with Lender, at Borrowers' option within thirty (30) days of such failure, additional cash or other liquid collateral (with credit for amounts currently being held by Lender pursuant to the foregoing sentence), in an amount which would have resulted in the noncomplying Debt Service Coverage Ratio or Total Debt Service Coverage Ratio requirement for such quarter having been satisfied. Borrowers shall not have the option to cure for failure to comply for any additional consecutive quarters and such an event will constitute an Event of Default under this Agreement. Any additional cash or liquid collateral deposited by Borrowers hereunder in order to achieve the required Debt Service Coverage Ratio or Total Debt Service Coverage Ratio for the Facility and cure any existing default with respect thereto will be held by Lender in a standard custodial account and shall constitute additional collateral for the obligations related to the Loan and an "Account" as defined in this Agreement, and, upon the occurrence of and during the continuance of an Event of Default, may be applied by Lender, in such order and manner as Lender may elect, to the reduction of the obligations related to the Loan. Borrowers shall not be entitled to any interest earned on such additional collateral. Provided that there is no outstanding Default or Event of Default, such additional collateral

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which has not been applied to the Loan Obligations will be released by Lender at such time as Borrowers provide Lender with evidence that the required minimum Debt Service Coverage Ratio and minimum Total Debt Service Coverage Ratio requirements set forth above have been achieved and maintained (without regard to any cash or liquid collateral deposited pursuant to this section) for two (2) consecutive fiscal quarters.

Notwithstanding anything herein to the contrary, any additional liquid collateral posted by Borrowers under the Senior Loan Agreement for purposes of satisfying this covenant, if the lender thereof is an Affiliate of the Lender, shall be deemed to satisfy the requirements herein.

Borrowers shall be required to supply Lender with a certificate evidencing compliance with the requirements of this Section, which certificate shall be signed by an officer or manager as appropriate.

4.15 **Occupancy.** Starting with the quarter ending March 31, 2013, maintain or cause to be maintained, an average annual occupancy of the Facility as tested quarterly (on the basis of a fiscal year) of seventy percent (70%) or greater (based on 102 in-service beds).

4.16 **Reserved.**

4.17 **Updated Appraisals; Inspections.**

(a) **Appraisals.** For so long as the Loan remains outstanding, if any Event of Default shall occur hereunder, or if, in Lender's judgment, a material depreciation in the value of the Property shall have occurred, then in any such event, Lender, may cause the Property to be appraised by an appraiser selected by Lender, and in accordance with Lender's appraisal guidelines and procedures then in effect, and Borrowers agree to cooperate in all respects with such appraisals and furnish to the appraisers all requested information regarding the Property and the Facility. Borrowers agree to pay all reasonable costs incurred by Lender in connection with such appraisal which costs shall be secured by the Senior Mortgage and shall accrue interest at the Default Rate until paid.

(b) **Reserved.**

(c) **Access; Inspections.** Borrowers shall authorize and permit Lender and its representatives (which term shall be deemed to include its independent accountants and counsel) to have reasonable access during normal business hours, upon reasonable notice and in such manner as will not unreasonably interfere with the conduct of business of Borrowers, to the Facility as Lender may from time to time reasonably request. Upon an Event of Default under the Loan Documents, Lender shall have access to the Facility at any hour without notice. Borrowers will agree to allow Lender or Lender's representative access to conduct inspections of the Facility upon reasonable notice to Borrowers. In cases of an emergency, Lender shall have the right to access the Facility to conduct inspections without notice. In addition to and not in substitution for Lender's rights under Section 4.8 (Books and Records), Borrowers agree to provide Lender, for any such inspection purposes, any data necessary for Lender to complete its

inspection. Borrowers shall reimburse Lender for reasonable travel costs associated with one Facility visit per year.

(d) **Reports.** If any inspector's report indicates that repairs or replacements are necessary over and above such capital expenditure requirement, Lender shall require a non-interest bearing repair escrow fund to ensure completion of the repairs. The amount of any repair escrow shall be one hundred twenty five percent (125%) of the estimated cost of repairs as determined by the inspector and Lender. Lender also shall require an agreement satisfactory to Lender, which will provide for

completion of the repairs and the disbursement of the escrow funds. All fees and costs associated with any inspection, any report and any subsequent inspections (if required) shall be paid by Borrowers.

(e) **Clinical Inspection Fee for Facility.** Borrowers shall pay to Lender the reasonable fees associated with a third party clinician that is engaged by Lender to inspect the Facility for clinical issues if the Facility's plan of correction following any survey is not approved after the first revisit or where the Facility has been decertified or given a Denial of Payment.

4.18 **Comply with Covenants and Laws.** Comply, in all material respects, with all applicable covenants and restrictions of record and all laws, ordinances, rules and regulations and keep the Facility and the Property in compliance with all applicable laws, ordinances, rules and regulations, including, without limitation, the Americans with Disabilities Act and regulations promulgated thereunder, the Fair Housing Act and regulations thereunder, and laws, ordinances, rules and regulations relating to zoning, health, building codes, setback requirements, Medicaid and Medicare laws and keep the Permits for the Facility in full force and effect (and if any material noncompliance is discovered during the term of the Loan, Borrowers will promptly remedy such noncompliance).

4.19 **Reserved.**

4.20 **Certificate.** Upon Lender's written request, furnish Lender with a certificate stating that Borrowers have complied with and is in compliance with all terms, covenants and conditions of the Loan Documents to which Borrowers are a party and that there exists no Default or Event of Default or, if such is not the case, that one or more specified events have occurred, and that the representations and warranties contained herein are true and correct with the same effect as though made on the date of such certificate.

4.21 **Notice of Fees or Penalties.** Immediately notify Lender, upon Borrower's knowledge thereof, of the assessment by any state or any Medicare, Medicaid, health or licensing agency of any fines or penalties against either Borrower or the Facility.

4.22 **Notice of Representations and Warranties.** Borrowers shall immediately notify Lender in writing, in the event any representation or warranty contained in the Loan Documents becomes untrue or there shall have been any material adverse change in any such representation or warranty.

4.23 **Lease Agreement; Management Agreement.**

(a) Maintain any lease agreement, any management agreement and any other services agreement, excluding those cancelable within thirty days or less than \$10,000 per annum (including, without limitation, the Operations Seller Lease Agreement, Lease Agreement, Operations Seller Management Agreement and Management Agreement) in full force and effect and timely perform all of its obligations thereunder and not permit the termination or amendment of such lease agreement, management agreement or other services agreement (including, without limitation, the Operations Seller Lease Agreement, Lease Agreement, Operations Seller Management Agreement and Management Agreement) or enter into any replacement or additional lease agreements, management agreements or other services agreements (including, without limitation, food service management agreements) unless the prior written consent of Lender is first obtained (which consent will not be unreasonably withheld and may be presumed a response in the affirmative if not received by the Borrowers within fifteen days of Lender's receipt of the initial request for consent); provided, however, that Lender's prior consent shall not be required for termination of any such lease agreement, management agreement or other services agreement (including, without limitation, the Operations Seller Lease Agreement, Lease Agreement, Operations Seller Management Agreement and Management Agreement) in the event of emergency situations (i.e., termination of the Facility's license or decertification of the Facility from participation in Medicare and/or Medicaid) as set forth below;

(b) In the event that proceedings are instituted to terminate the Facility's license or to terminate the Facility's Medicaid or Medicare certification, upon request of Lender immediately terminate any lease agreement, any management agreement or any other services agreement (including, without limitation, the Operations Seller Lease Agreement, Lease Agreement, Operations Seller Management Agreement and Management Agreement) relating to the Facility and engage oversight management services from a replacement lessee, management company or operator, as the case may be, reasonably acceptable to the Lender;

(c) In the event that bankruptcy or insolvency proceedings are instituted by or against the Operator, Management Company or Operations Seller, Owner shall (to the extent permitted by the applicable bankruptcy court having jurisdiction over such proceedings), upon written instruction received from Lender, to terminate any applicable lease agreement, management agreement or other services agreement (including, without limitation, the Operations Seller Lease Agreement, Lease Agreement, Operations Seller Management Agreement and Management Agreement);

(d) In the event that Borrowers fail to satisfy any covenants in the Loan Documents, Lender shall have the right, but not the obligation, to terminate any lease agreement, any management agreement and any other services agreement (including, without limitation, the Operations Seller Lease Agreement, Lease Agreement, Operations Seller Management Agreement and Management Agreement) and engage oversight management services and other relevant services from a replacement lessee, management company or operator, as the case may be, reasonably acceptable to Lender;

(e) In the event that at any time during the term of the Loan, any lessee, management company or operator materially defaults under the then applicable lease agreement, management agreement or other services agreement (including, without limitation the

Operations Seller Lease Agreement, Lease Agreement, Operations Seller Management Agreement and Management Agreement) in effect (which default is not cured within the applicable cure period, if any) Borrowers shall terminate such lease agreement, management agreement or other services agreement (including, without limitation the Operations Seller Lease Agreement, Lease Agreement, Operations Seller Management Agreement and Management Agreement) and replace such lessee, management company or operator pursuant to a replacement lease agreement, management agreement or other services agreement in form and substance acceptable to Lender, within thirty (30) days of such material default; and

(f) In any instance where a replacement manager or operator is appointed by the Borrowers and/or Owner and/or Operator or Operations Seller, as applicable, or as required by the Lender, such replacement manager or operator shall be required to enter into a replacement Subordination and Assignment of Management Agreement, environmental indemnity agreement and/or Subordination and Assignment of Lease Agreement, as applicable, and any other agreement reasonably required by the Lender, in each instance in form and substance substantially similar to those same agreements executed on the Closing Date or the Operations Closing Date.

4.24 **Required Payment.** At any time upon: (i) a sale of twenty-five percent (25%) or more of the assets of either of the Borrowers (in a single transaction or a series of transactions not in the ordinary course of business), (ii) a repayment in full of the Senior Loan, or (iii) a Change in Control of any Borrower, the Loan shall be required to be prepaid in full with accrued interest plus the Exit Fee, as set forth in Section 6.3 (Default Rate) and Section 2.6 (Prepayment), at the option of Lender in its sole discretion; provided, however, that no prepayment penalty shall be required for a prepayment due to a Change in Control.

4.25 **Other Debt Agreements.** Maintain, and cause each Affiliate to maintain, compliance with the terms, covenants and conditions of the loan agreements, notes, mortgages, deeds of trust, security agreements, assignments and/or other documents and instruments evidencing or securing Indebtedness upon which such Person is obligated or which encumbers any property of such Person, including, without limitation, the Senior Loan and all other Contemporary Debt.

4.26 **Access.** Borrowers shall authorize and permit Lender and its representatives (which term shall be deemed to include its independent accountants and counsel) to have reasonable access during normal business hours, upon reasonable notice and in such manner as will not unreasonably interfere with the conduct of business of Borrowers, to the Facility as Lender may from time to time reasonably request. Upon an Event of Default under the Loan Documents, Lender shall have access to the Facility at any hour without notice.

4.27 **USA Patriot Act Verification Information.** On the Closing Date, provide evidence of its legal name, tax identification number and street address, and, if either Borrower is an individual, a driver's license and date of birth, satisfactory to and sufficient for Lender to verify the identity of such Borrower, as required under the USA Patriot Act. Each Borrower shall notify Lender, promptly, of any change to such information.

4.28 **Lien Searches.** Upon Lender's request and at Borrowers' sole cost and expense, deliver to Lender the results of complete lien and judgment searches for each Borrower or any Guarantor at the applicable county and at the Secretary of State's Office.

4.29 **License to Operate.** Maintain or cause to be maintained the required Facility licenses, Medicaid and Medicare Reimbursement Contracts and/or Permits at all times.

4.30 **Reserved.**

## ARTICLE V. NEGATIVE COVENANTS OF BORROWERS

Until the Loan Obligations have been paid in full, each Borrower jointly and severally agrees it shall not:

5.1 **Assignment of Licenses and Permits.** Assign or transfer any of its interest in any Permits or Reimbursement Contracts (including rights to payment thereunder) pertaining to the Facility, or assign, transfer, or remove or permit any other person to assign, transfer, or remove any records pertaining to the Facility including, without limitation, patient records, medical and clinical records (except for removal of such patient records as directed by the patients owning such records), without Lender's prior written consent, which consent may be granted or refused in Lender's sole discretion.

5.2 **No Liens; Exceptions.** Create, incur, assume or suffer to exist any Lien upon or with respect to the Facility or any of any Borrower's properties, rights, income or other assets relating thereto, including, without limitation, the Collateral, whether now owned or hereafter acquired, other than the following permitted Liens ("**Permitted Encumbrances**"):

(a) Liens at any time existing in favor of the Lender or its Affiliates,

(b) Liens which are listed in Exhibit G attached hereto,

(c) Inchoate Liens arising by operation of law for the purchase of labor, services, materials, equipment or supplies, provided payment shall not be delinquent and, if such Lien is a lien upon any of the Property or Improvements, such Lien must be fully disclosed to Lender and bonded off and removed from the Property and Improvements, within thirty (30) days of its creation, in a manner satisfactory to Lender,

(d) Liens incurred in the ordinary course of business in connection with workers' compensation, unemployment insurance or other forms of governmental insurance or benefits, or to secure performance of tenders, statutory obligations, leases and contracts (other than for money borrowed or for credit received with respect to property acquired) entered into in the ordinary course of business as presently conducted or to secure obligations for surety or appeal bonds, and

(e) Liens for current year's taxes, assessments or governmental charges or levies provided payment thereof shall not be delinquent.

(f) Liens in favor of Senior Lender or any Contemporary Debt.

5.3 **Indebtedness and Other Obligations.**

(a) Incur or become obligated upon any other Indebtedness, secured or unsecured, or become obligated to make any capital contribution or loan to any other entity other than the following:

- (i) Indebtedness to Lender including Contemporary Debt;
- (ii) Indebtedness to Senior Lender;
- (iii) Indebtedness to trade creditors in the ordinary course of business as reflected on the financial statements; and
- (iv) Accrued debt for current payroll taxes and similar taxes not yet due.

(b) Other than in accordance with the terms of the Subordination and Standstill Agreement, Borrowers will not permit any increase in the Senior Loan or change in the interest rate (other than changes occurring automatically under a note having a floating rate as an index), payment terms or other material terms of any of such debt and will not enter into any agreement amending the documents evidencing such debt in any of the foregoing respects.

5.4 **Merger, Consolidation, Etc.** Consummate any Change in Control, merger, consolidation or similar transaction, or sell, assign, lease or otherwise dispose of substantially all of its assets (whether now or hereafter acquired), without the prior written consent of the Lender, which consent may be granted or refused in Lender's sole discretion.

5.5 **Maintain Single-Purpose Entity Status.**

- (a) Borrowers shall not:
- (i) engage in any business or activity other than the ownership, operation and maintenance of the Property and activities incidental thereto;
  - (ii) acquire or own any material assets other than (A) the Property, Facility, Equipment, General Intangibles, Accounts and Inventory, and (B) such incidental machinery, equipment, fixtures and other personal property as may be necessary for the operation of the Property;



- (iii) fail to preserve its existence as a limited liability company, validly existing and in good standing (if applicable) under the laws of the jurisdiction of its organization or formation, or without the prior written consent of Lender, amend, modify, terminate or fail to comply with the provisions of

its articles of organization, operating agreement or similar organizational document, as same may be further amended or supplemented, if such amendment, modification, termination or failure to comply would adversely affect its ability to perform its obligations hereunder, under the Note or any other document evidencing or securing the Loan;

- (iv) incur any debt, secured or unsecured, direct or contingent (including guaranteeing any obligation), other than the Loan and trade payables incurred in the ordinary course of business, provided same are paid when due;
- (v) fail to maintain its records, books of account and bank accounts separate and apart from those of its members and affiliates, the affiliates of any of its members, and any other person; and
- (vi) fail either to hold itself out to the public as a legal person separate and distinct from any other person or to conduct its business solely in its own name in order not (A) to mislead others as to the identity with which such other party is transacting business, or (B) to suggest that it is responsible for the debts of any third party (including any of its members or affiliates, or any general partner, principal or affiliate thereof).

#### 5.6 **Dividends, Distributions and Redemptions.**

- (a) Except as otherwise consented to by Lender in writing, none of the Borrowers may declare or pay any dividends, or purchase, redeem, retire, or otherwise acquire for value, any of its membership interests or shares of capital stock, as the case may be, now or hereafter outstanding, or return any capital to its members (each a “**Distribution**”).
- (b) Notwithstanding the foregoing, the Borrowers may declare and pay Distributions quarterly provided that:
  - (1) the Borrowers have demonstrated satisfactory compliance, as determined by Lender in Lender’ s sole discretion, with all covenants of the Loan Documents,
  - (2) the Borrowers have demonstrated satisfactory compliance, as determined by Lender in Lender’ s sole discretion, with all financial covenants of the Loan Documents including that the Borrowers have maintained a Total Debt Service Coverage Ratio of 1.35 to 1.00 for two consecutive fiscal quarters immediately prior to any Distribution, provided, however, that if the Facility falls below such coverage requirements for any quarter after meeting the immediately provided for

test, all Distributions shall cease until the Facility again meets such requirements for another two consecutive quarters,

(3) there has not existed a payment Event of Default on the Loan or the Senior Loan;

(4) neither the Loan nor the Senior Loan is in Default which Default has not been cured or waived;

(5) the making of such Distribution would not cause an Event of Default on the Loan or the Senior Loan;

(6) at no time has the Lender accelerated the Loan, otherwise there shall be no Distributions.

5.7 **Change of Business.** Make any material change in the nature of its business as it is being conducted as of the date hereof.

5.8 **Changes in Accounting.** Change its methods of accounting, unless such change is permitted by GAAP, and provided such change does not have the effect of curing or preventing what would otherwise be an Event of Default or Default had such change not taken place.

5.9 **ERISA Funding and Termination.** Permit (a) the funding requirements of ERISA with respect to any employee plan to be less than the minimum required by ERISA at any time, or (b) any employee plan to be subject to involuntary termination proceedings at any time.

5.10 **Transactions with Affiliates.** Unless previously approved by the Lender, enter into any transaction with a Person which is an Affiliate of any Borrower other than in the ordinary course of its business and on fair and reasonable terms no less favorable to Borrowers, than those they could obtain in a comparable arms-length transaction with a Person not an Affiliate.

5.11 **Transfer of Ownership Interests.** Permit a change in the Persons holding the ownership interests or capital stock of any Borrower unless the written consent of the Lender is first obtained, which consent may be granted or refused in Lender' s sole discretion.

5.12 **Change of Use.** Alter or change the use of the Facility or permit to exist any management agreement for the Facility or enter into any operating lease for the Facility (other than the Lease Agreement, Operations Seller Lease Agreement, Operations Seller Management Agreement and Management Agreement), unless Borrowers first notify Lender and provide Lender a copy of the proposed lease agreement or management agreement, obtains Lender' s written consent thereto, which consent may be withheld in Lender' s sole discretion, and obtains and provides Lender with a subordination agreement in form satisfactory to Lender, as determined by Lender in its sole discretion, from such manager or lessee subordinating to all rights of Lender.

5.13 **Domicile and Place of Business.** Change its chief executive office or its principal place of business without first giving Lender at least thirty (30) days prior written notice thereof and promptly providing Lender such information and amendatory financing statements as Lender may request in connection therewith.

5.14 **Acquisitions.** Directly or indirectly, purchase, lease, manage, own, operate, or otherwise acquire any property or other assets (or any interest therein) which are not used in connection with the operation of the Facility.

5.15 **Change in Organizational Documents.** Permit any change in the articles of organization articles of incorporation, bylaws or operating agreement of any Borrower or the Management Company, as the case may be, without in each case the prior written consent of Lender, or permit the change in the manager or managing member of any Borrower or the Management Company, as the case may be, or the admission of any other manager or managing member of any Borrower or the Management Company, as the case may be.

5.16 **Facility Status.** Borrowers shall not close the Facility.

5.17 **Compliance With Anti-Terrorism Orders.** Borrowers will not permit the transfer of any interest in any Borrower to any person or entity (or any beneficial owner of such entity) who is listed on those certain lists referred to as the OFAC Lists developed in connection with the Anti-Terrorism Laws (the “OFAC Lists”). Borrowers will not knowingly enter into a lease with any party who is listed on the OFAC Lists. Borrowers shall immediately notify Lender if any Borrower has knowledge that any principal, or any member or beneficial owner of any Borrower or principal of any Borrower is listed on the OFAC Lists or is indicted on or arraigned and held over on charges involving money laundering or predicate crimes to money laundering. Borrowers shall immediately notify Lender if any Borrower knows that any tenant of the Facility is listed on the OFAC Lists, or is convicted on, pleads nolo contendere to, is indicted on, or is arraigned and held over on charges involving money laundering or predicate crimes to money laundering.

5.18 **Involvement of Key Management.** Permit Christopher F. Brogdon to cease to be actively involved on a full time basis in the senior management of Borrowers or the Management Company, as the case may be, except with consent of Lender, which consent shall be given or withheld in its sole discretion, unless replaced by a replacement executive acceptable to Lender acting in good faith within sixty (60) days of such cessation.

5.19 **Intercompany Indebtedness Prohibited.** In addition to and not in substitution for the covenants and obligations set for in Article V and the Permitted Encumbrances set forth herein, except as noted in Schedule 5.19, no Borrower shall incur or become obligated upon any other Indebtedness, secured or unsecured, or become obligated to make any capital contribution or loan to any Affiliate of any Borrower, including, but not limited to (i) advancing or loaning funds, (ii) engaging in any actions that generate any accounts receivable due from and/or (iii) distribution of any funds of any Borrower to any other affiliate businesses of Borrowers or Guarantors which are not a Borrower hereunder, except as allowable under Section 5.6. Borrowers are prohibited from commingling Facility funds with any other funds not attributable to the Borrowers and/or the Facility.

## ARTICLE VI. EVENTS OF DEFAULT AND REMEDIES

6.1 **Events of Default.** The occurrence of any one or more of the following shall constitute an “**Event of Default**” hereunder:

(a) The failure by Borrowers to pay any installment of principal, interest, or other payments required under the Note, as and when due;

(b) Either Borrower’ s violation of any covenant set forth in Section 3.39 (Post Closing Date Covenants), Section 4.24 (Required Payment), Section 4.29 (License to Operate) and Article V hereof;

(c) Either Borrower’ s or any Guarantor’ s failure to deliver or cause to be delivered the financial statements and information set forth in Section 4.6 (Financial and Other Information) within the times required, either Borrower’ s ability to maintain the financial covenants set forth in Section 4.13 (Minimum Financial Covenants) or Section 4.14 (Debt Service

Coverage Ratio Requirements) in the applicable period, or either Borrower's timely or proper performance or observance of the covenants set forth in Section 4.5 (Insurance), and such failure is not cured within thirty (30) days following Lender's written notice to Borrowers thereof;

(d) The failure of either Borrower properly and timely to perform or observe any covenant or condition set forth in this Agreement (other than those specified in this Section 6.1) or any other Loan Documents which is susceptible of being cured and is not cured within any applicable cure period as set forth herein or, if no cure period is specified therefor, is not cured within thirty (30) days of Lender's notice to Borrowers of such Default; provided, however, that if such default cannot be cured within such thirty (30) day period, such cure period shall be extended for an additional sixty (60) days, as long as Borrowers are diligently and in good faith prosecuting said cure to completion and as long as such extension is approved by Lender in its sole discretion;

(e) The filing by either Borrower or any Guarantor of a voluntary petition, or the adjudication of any of the aforesaid Persons, or the filing by any of the aforesaid Persons of any petition or answer seeking or acquiescing, in any reorganization, arrangement, composition, readjustment, liquidation, dissolution or similar relief for itself under any present or future federal, state or other statute, law or regulation relating to bankruptcy, insolvency or other relief for debtors, or if any of the aforesaid Persons should seek or consent to or acquiesce in the appointment of any trustee, receiver or liquidator for itself or of all or any substantial part of its property or of any or all of the rents, revenues, issues, earnings, profits or income thereof, or the mailing of any general assignment for the benefit of creditors or the admission in writing by any of the aforesaid Persons of its inability to pay its debts generally as they become due;

(f) The entry by a court of competent jurisdiction of an order, judgment, or decree approving a petition filed against either Borrower or any Guarantor which such petition seeks any reorganization, arrangement, composition, readjustment, liquidation, dissolution or similar relief under any present or future federal, state or other statute, law or

regulation relating to bankruptcy, insolvency, or other relief for debtors, which order, judgment or decree remains unvacated and unstayed for an aggregate of sixty (60) days (whether or not consecutive) from the date of entry thereof, or the appointment of any trustee, receiver or liquidator of any of the aforesaid Persons or of all or any substantial part of its properties or of any or all of the rents, revenues, issues, earnings, profits or income thereof which appointment shall remain unvacated and unstayed for an aggregate of sixty (60) days (whether or not consecutive);

(g) Unless otherwise permitted hereunder or under any other Loan Documents, the sale, transfer, lease, assignment, or other disposition, voluntarily or involuntarily, of the Collateral, or any part thereof, or, except for Permitted Encumbrances as described in Section 5.2 (No Liens; Exceptions) above, any further encumbrance of the Collateral, unless the prior written consent of Lender is obtained, which consent may be withheld in Lender's sole discretion;

(h) The death or incompetence of any individual Guarantor or, if such Guarantor is a joint and several guarantor with a spouse, such Guarantor and spouse, unless replaced by a replacement Guarantor acceptable to Lender acting in good faith within four (4) months of such death or any legal determination of incompetence.

(i) Any certificate, statement, representation, warranty or audit heretofore or hereafter furnished by or on behalf of either Borrower or any Guarantor pursuant to or in connection with this Agreement (including, without limitation, representations and warranties contained herein or in any Loan Documents) or as an inducement to Lender to make the Loan to Borrowers, (i) proves to have been false in any material respect at the time when the facts therein set forth were stated or certified, (ii) proves to have omitted any substantial contingent or unliquidated liability or claim against either Borrower or any Guarantor, or (iii) on the date of execution of this Agreement there shall have been any materially adverse change in any of the acts previously disclosed by

any such certificate, statement, representation, warranty or audit, which change shall not have been disclosed to Lender in writing at or prior to the time of such execution;

(j) The failure of either Borrower to correct within the time deadlines set by any applicable Medicare, Medicaid or licensing agency, any deficiency which would result in the following actions by such agency with respect to the Facility:

- (i) a termination of any Reimbursement Contract or any Permit; or
- (ii) a ban on new admissions generally or on admission of patients otherwise qualifying for Medicare or Medicaid coverage; or
- (iii) a ban on new beds, generally.

(k) Either Borrower or the Facility should be assessed fines or penalties by any state or any Medicare, Medicaid, health or licensing agency having jurisdiction over such Persons or the Facility in excess of \$10,000;

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(l) A final judgment shall be rendered by a court of law or equity against either Borrower or any Guarantor in excess of \$10,000, and the same shall remain undischarged for a period of thirty (30) days, unless such judgment is either (i) fully covered by collectible insurance and such insurer has within such period acknowledged such coverage in writing, or (ii) although not fully covered by insurance, enforcement of such judgment has been effectively stayed, such judgment is being contested or appealed by appropriate proceedings and such Borrower or Guarantor, as the case may be, has established reserves adequate for payment in the event such Person is ultimately unsuccessful in such contest or appeal and evidence thereof is provided to Lender and such evidence is satisfactory as determined by Lender in its sole discretion;

(m) The occurrence of any "Event of Default" under any of the Senior Loan Documents or any Contemporary Debt in existence on the date hereof;

(n) The occurrence of any material default that is not cured within any applicable cure period under any other deed to secure debt or related financing documents evidencing or securing debt with respect to the Facility;

(o) The occurrence of any materially adverse change in the financial condition or prospects of either Borrower or any Guarantor, or the existence of any other condition which constitutes a material impairment of any such Person's ability to operate the Facility or of such Person's ability to perform their respective obligations under the Loan Documents, which is not remedied within thirty (30) days after written notice;

(p) Borrowers shall execute (other than to Lender) any conditional bill of sale, chattel mortgage, security agreement or other security instrument covering any materials, fixtures, machinery, equipment, articles, and/or Personal Property intended to be incorporated in the Facility or the appurtenances thereto or placed in the Facility, or if a financing statement (for collateral greater than \$10,000 in value) giving notice of a security interest created under any such security instrument shall be filed, or if any of such materials, fixtures, machinery, equipment, articles, and/or Personal Property shall not be purchased so that the ownership thereof will vest unconditionally in Borrowers, free from encumbrances other than to Lender, on delivery at the Property, or if Borrowers shall not produce to Lender upon demand the contracts, bills of sale, statements, receipted vouchers or agreements, or any of them, under which Borrower claims title to any thereof; or

(q) Any survey, report or examination discloses that the Property or any portion thereof encroaches upon or projects over a street or upon or over adjoining property or violates any setback or other restriction, however created, or any

building, zoning, subdivision, land-use, health, sanitation, or environmental protection ordinance, regulation or law of any Governmental Authority having jurisdiction over the Property or any other Legal Requirements; provided, however, that if such default cannot be cured within such thirty (30) day period, such cure period shall be extended for an additional sixty (60) days, as long as Borrowers are diligently and in good faith prosecuting said cure to completion and as long as such extension is approved by Lender.

Notwithstanding anything in this Section 6.1, all requirements of notice shall be deemed eliminated if Lender is prevented from declaring an Event of Default by bankruptcy or other applicable law. The cure period, if any, shall then run from the occurrence of the event or condition of Default rather than from the date of notice.

6.2 **Remedies.** In addition to other remedies under this Agreement, upon the occurrence of any one or more of the foregoing Events of Default, the Lender may, at its option:

(a) Declare the entire unpaid principal of the Loan Obligations to be, and the same shall thereupon become, immediately due and payable, without presentment, protest or further demand or notice of any kind, all of which are hereby expressly waived; provided, however, if a Bankruptcy Default occurs, then all such amounts shall become immediately due and payable automatically without any election by the Lender; and/or

(b) Proceed to protect and enforce its rights by action at law (including, without limitation, bringing suit to reduce any claim to judgment), suit in equity and other appropriate proceedings including, without limitation, for specific performance of any covenant or condition contained in this Agreement; and/or

(c) Exercise any and all rights and remedies afforded by the laws of the United States, the states in which any of the Property or other Collateral is located or any other appropriate jurisdiction as may be available for the collection of debts and enforcement of covenants and conditions such as those contained in this Agreement and the Loan Documents; and/or

(d) Exercise the rights and remedies of setoff and/or banker' s lien against the interest of Borrowers in and to every account and other property of either Borrower which is in the possession of the Lender or any person who then owns a participating interest in the Loan, to the extent of the full amount of the Loan; and/or

(e) Appoint a management company, in Lender' s sole discretion, to assume and manage the business of the each Borrower, as such relates to the Facility secured by the Loan Documents; and/or

(f) Exercise its rights and remedies pursuant to any other Loan Documents; and/or

(g) All rights and remedies of Lender under the terms of this Agreement, the Note, any of the other Loan Documents, and any applicable statutes or rules of law shall be cumulative and may be exercised successively or concurrently; and/or

(h) reserved.

6.3 **Default Rate; Exit Fee.**

(a) In addition to and not in substitution for the penalties set forth in Section 6.3(b) and Section 6.3(c), upon the occurrence and during the continuance of any Event of Default, the Note Rate shall be increased by the Default Rate, at the option of Lender.

(b) In addition to and not in substitution for the penalties set forth in Section 6.3(a) and Section 6.3(c), if an Event of Default occurs and the Loan is declared to be immediately due and payable, there shall be added to the principal balance of the Loan then due an amount equal to the Exit Fee, as set forth in Section 2.6.

(c) In addition to and not in substitution for the penalties set forth in Section 6.3(a) and Section 6.3(b), upon the occurrence of any Event of Default, Borrowers shall be liable to the Lender for all costs paid or incurred for the acquisition, renovating, improving and/or equipping of the Facility, whether the same shall be paid or incurred pursuant to the provisions of this section or otherwise, and all payments made or liabilities incurred by the Lender hereunder or any kind whatsoever shall be secured by the Loan Documents and shall immediately become due and payable to the Lender without notice or demand and shall be paid by Borrowers to the Lender on demand, with interest thereon at the Default Rate to the date of payment..

6.4 **Standstill Remedy.** Upon the occurrence of any Event of Default, Lender shall have the right, but not the obligation, to issue to Borrowers a standstill notice (the “**Standstill Notice**”) which notice shall set forth any or all of the following provisions:

(a) Each Borrower, jointly and severally, covenants and agrees that after receipt of this Standstill Notice, without the prior written consent of Lender:

- (i) each Borrower’s business, including the Facility, will be conducted only in the ordinary course of business and in compliance with applicable laws, regulations, and contractual obligations;
- (ii) Neither Borrower will merge, amalgamate or consolidate with any corporation, or acquire all or substantially all of the business or assets of any other Person, business organization, entity or enterprise, or acquire ownership or control of any capital stock, bonds, or other securities of, or any property interest in, any business organization, entity or enterprise or acquire control of the management or policies thereof;
- (iii) Each Borrower shall not:
  - (A) enter into any transaction with or create or assume any obligation or liability to any Affiliate, agent or relative of any Borrower or such Affiliates;
  - (B) cancel or compromise any claim, except in the ordinary course of business, or waive any rights of substantial value;
  - (C) make any Tax election or settle or compromise any Tax liability;

(D) make any capital expenditures, except those made in the ordinary course of business which do not exceed \$10,000 in the aggregate;

(E) enter into or assume any contract, agreement or commitment which, by reason of its size, term or other factor, is not in the ordinary course of business;

(F) delay the payment of its accounts payable or take any actions to accelerate the payment of its accounts receivable; or

(G) take any action, or omit to take any action, which would have, or could reasonably be expected to have, a Material Adverse Effect.

(iv) Each Borrower shall use its respective commercially reasonable efforts in a manner consistent with past practice to preserve the business organization of the Facility intact and to keep available the services of the present employees and agents of the Facility and to preserve the good will of customers, suppliers, referral sources, employees, agents, third-party payors and others having business relations with the Facility;

(v) Each Borrower shall use its respective reasonable efforts to maintain the Facility in good operating condition and repair, ordinary wear and tear excepted, and will maintain existing insurance coverage on the Facility as well as other existing insurance coverage;

(vi) Each Borrower shall pay all registration, maintenance and renewal fees that are due or past due in connection with each item of Intellectual Property relating to the Facility; and

Upon receipt of the Standstill Notice, Borrowers shall comply with all of the provisions set forth herein.

## ARTICLE VII. MISCELLANEOUS

7.1 **Waiver.** No remedy conferred upon, or reserved to, the Lender in this Agreement or any of the other Loan Documents is intended to be exclusive of any other remedy or remedies, and each and every remedy shall be cumulative and shall be in addition to every other remedy given hereunder or now or hereafter existing in law or in equity. Exercise of or omission to exercise any right of the Lender shall not affect any subsequent right of Lender to exercise the same. No course of dealing between Borrowers and Lender or any delay on the Lender's part in exercising any rights shall operate as a waiver of any of the Lender's rights. No waiver of any Default under this Agreement or any of the other Loan Documents shall extend to

or shall affect any subsequent or other then existing Default or shall impair any rights, remedies or powers of Lender.

7.2 **Costs and Expenses.** Borrowers will bear all taxes, fees, charges and expenses, including, but not limited to, in connection with the Loan, the Note, the preparation and servicing of this Agreement and the other Loan Documents (including any amendments hereafter made), and in connection with any modifications thereto after the Closing Date, the recording or re-recording of any of the Loan Documents, surveillance of the Borrowers' operations and evaluation of Lender's, Borrowers', or any Guarantor's respective rights, obligations, actions or in-actions under the Loan Documents, including, any waivers or consents, all (a) out of pocket expenses of Borrowers and Lender; (b) recording fees, recording taxes, intangibles taxes, documentary taxes or similar taxes; (c) title insurance premiums, (d) costs of third party reports, including, but not limited to, environmental, engineering, appraisal, survey, title report, lien search, inspections, drawing of papers, architects, and Engineers expenses and charges; (e) attorneys' fees of the Lender's counsel; (f) fees and expenses of consultants and advisors of Lender, including financial advisors; and (g) expenses related to the employment of watchmen to protect the Property from injury in the event that after request Borrowers do not provide such protection, the amount of which taxes, fees, charges and expenses shall constitute additional Loan Obligations of Borrowers to Lender payable on demand of Lender. If, at any time, a Default occurs or Lender becomes a party to any suit or proceeding in order to protect its interests



or priority in any collateral for any of the Loan Obligations or its rights under this Agreement or any of the Loan Documents, or if Lender is made a party to any suit or proceeding by virtue of the Loan, this Agreement or any Collateral and as a result of any of the foregoing, Lender employs or engages counsel, consultants or other advisors to advise, consult or provide other representation with respect to the Loan Documents, or to collect the balance of the Loan Obligations, or to take any action in or with respect to any suit or proceeding relating to this Agreement, any of the other Loan Documents, any Collateral, Borrowers or any Guarantor or operator, or to protect, collect, or liquidate any of the security for the Loan Obligations, or attempt to enforce any security interest or lien granted to Lender by any of the Loan Documents, then in any such events, all of the reasonable attorney's fees, consultant fees, or other advisor fees arising from such services, including any fees for preparation of litigation and in any appellate or bankruptcy proceedings, and any expenses, costs and charges relating thereto shall constitute additional Loan Obligations of Borrowers to Lender payable on demand of Lender. Without limiting the foregoing, the Borrowers have undertaken the obligation for payment of, and shall pay, all recording and filing fees, revenue or documentary stamps or taxes, intangibles taxes, and other taxes, expenses and charges payable in connection with this Agreement, any of the Loan Documents, the Loan Obligations, or the filing of any financing statements or other instruments required to effectuate the purposes of this Agreement and any record searches, lien searches or other similar searches performed by Lender during the term of the Loan as determined by Lender to be necessary or appropriate, in its sole discretions, and should the Borrowers fail to do so, the Borrowers agree to reimburse Lender for the amounts paid by Lender, together with penalties or interest, if any, incurred by Lender as a result of underpayment or nonpayment. Such amounts shall constitute a portion of the Loan Obligations, shall be secured by the Security Agreement and shall bear interest at the Default Rate (as defined in the Note) from the date advanced until repaid.

7.3 **Performance of Lender.** At its option, upon Borrowers' failure to do so, the Lender may make any payment or do any act on Borrowers' behalf that Borrowers or others are required to do to remain in compliance with this Agreement or any of the other Loan Documents, and Borrowers, jointly and severally, agree to reimburse the Lender, on demand, for any payment made or expense incurred by Lender pursuant to the foregoing authorization, including, without limitation, attorneys' fees, and until so repaid any sums advanced by Lender shall constitute a portion of the Loan Obligations, shall be secured by the Security Agreement and shall bear interest at the Default Rate from the date advanced until repaid. Further, upon the occurrence and during the continuation of an Event of Default, Lender shall have the right to notify all account debtors to make payment directly to Lender until such time as (i) Lender has determined in its sole discretion, applied in good faith, that such Event of Default has been cured by Borrowers, (ii) Lender has waived such Event of Default, or (iii) all amounts due hereunder have been fully paid and discharged, whichever occurs first.

7.4 **Indemnification.** Borrowers shall, at their sole cost and expense, protect, defend, indemnify and hold harmless the Indemnified Parties from and against any and all claims, suits, liabilities (including, without limitation, strict liabilities), actions, proceedings, obligations, debts, damages, losses, costs, expenses, diminutions in value, fines, penalties, charges, fees, expenses, judgments, awards, amounts paid in settlement, punitive damages, foreseeable and unforeseeable consequential damages, of whatever kind or nature (including but not limited to reasonable attorneys' fees and other costs of defense) imposed upon or incurred by or asserted against Lender by reason of:

- (a) ownership of the Note, the Security Agreement, the Property or any interest therein or receipt of any Rents (as defined in the Senior Mortgage);
- (b) any amendment to, or restructuring of, the Loan Obligations and/or any of the Loan Documents;
- (c) any and all lawful action that may be taken by Lender in connection with the enforcement of the provisions of the Security Agreement or the Note or any of the other Loan Documents, whether or not suit is filed in connection with same, or in connection with either Borrower, any Guarantor, and/or any partner, joint venturer, member or shareholder thereof becoming a party to a voluntary or involuntary federal or state bankruptcy, insolvency or similar proceeding;

(d) any accident, injury to or death of persons or loss of or damage to property occurring in, on or about the Property, the Improvements or any part thereof or on the adjoining sidewalks, curbs, adjacent property or adjacent parking areas, streets or ways;

(e) any use, nonuse or condition in, on or about the Property, the Improvements or any part thereof or on the adjoining sidewalks, curbs, adjacent property or adjacent parking areas, streets or ways;

(f) any failure on the part of either Borrower or any Guarantor to perform or comply with any of the terms of this Agreement or any of the other Loan Documents;

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(g) any claims by any broker, person or entity claiming to have participated in arranging the making of the Loan evidenced by the Note;

(h) any failure of the Property to be in compliance with any applicable laws;

(i) any and all claims and demands whatsoever which may be asserted against Lender by reason of any alleged obligations or undertakings on its part to perform or discharge any of the terms, covenants, or agreements contained in the Lease Agreement, Operations Seller Lease Agreement or any replacement or renewal thereof or substitution therefor;

(j) performance of any labor or services or the furnishing of any materials or other property with respect to the Property, the Improvements or any part thereof;

(k) reserved;

(l) any misrepresentation made to Lender in this Agreement or in any of the other Loan Documents;

(m) any tax on the making and/or recording of the Note or any of the other Loan Documents;

(n) the violation of any requirements of ERISA;

(o) any fines or penalties assessed or any corrective costs incurred by Lender if the Facility or any part of the Property is determined to be in violation of any covenants, restrictions of record, or any applicable laws, ordinances, rules or regulations; or

(p) the enforcement by any of the Indemnified Parties of the provisions of this Section 7.4.

Any amounts payable to Lender by reason of the application of this Section 7.4 shall become immediately due and payable, and shall constitute a portion of the Loan Obligations, shall be secured by the Security Agreement and shall accrue interest at the Default Rate. The obligations and liabilities of Borrowers under this Section 7.4 shall survive any termination, satisfaction, assignment and entry of a judgment. For purposes of this Section 7.4, the term “**Indemnified Parties**” means Lender and any Person who is or will have been involved in the origination of the Loan, any Person who is or will have been involved in the servicing of the Loan, any Person who may hold or acquire or will have held a full or partial interest in the Loan (including, without limitation, any investor in any securities backed in whole or in part by the Loan) as well as the respective directors, officers, shareholder, partners, members, employees, agents, servants, representatives, contractors, subcontractors, affiliates, subsidiaries, participants, successors and assigns of any and all of the foregoing (including, without limitation, any other Person who holds or acquires or will have held a participation or

other full or partial interest in the Loan or the Property, whether during the term of the Loan or as a part of or following a judgment on the Note and including, without limitation, any successors by merger, consolidation or acquisition of all or a substantial portion of Lender's assets and business).

7.5 **Headings.** The headings of the Sections of this Agreement are for convenience of reference only, are not to be considered a part hereof, and shall not limit or otherwise affect any of the terms hereof.

7.6 **Survival of Covenants.** All covenants, agreements, representations and warranties made herein and in certificates or reports delivered pursuant hereto shall be deemed to have been material and relied on by Lender, notwithstanding any investigation made by or on behalf of Lender, and shall survive the execution and delivery to Lender of the Note and this Agreement.

7.7 **Notices, Etc.** Any notice or other communication required or permitted to be given by this Agreement or the other Loan Documents or by applicable law shall be in writing and shall be deemed received (a) on the date delivered, if sent by hand delivery (to the person or department if one is specified below) with receipt acknowledged by the recipient thereof, (b) three (3) Business Days following the date deposited in U.S. mail, certified or registered, with return receipt requested, or (c) one (1) Business Day following the date deposited with Federal Express or other national overnight carrier, and in each case addressed as follows:

If to Borrowers:

CSCC Property Holdings, LLC  
CSCC Nursing, LLC  
Two Buckhead Plaza  
3050 Peachtree Road NW, Suite 355  
Atlanta, Georgia 30305

with a copy to:

Ellen W. Smith, Esq.  
Holt Ney Zatzoff & Wasserman, LLP  
100 Galleria Parkway, Suite 1800  
Atlanta, Georgia 30339  
Fax: (770) 956-1490

If to Lender:

Eric Smith  
Contemporary Healthcare Capital, LLC  
1040 Broad Street  
Suite 103  
Shrewsbury, New Jersey 07702

with a copy to:

Law Offices of Thomas K. Slattery, P.L.L.C.  
1250 24<sup>th</sup> Street NW, Suite 300

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Washington, DC 20037

Either party may change its address to another single address by notice given as herein provided, except any change of address notice must be actually received in order to be effective.

7.8 **Benefits.** All of the terms and provisions of this Agreement shall bind and inure to the benefit of the parties hereto and their respective successors and assigns. No Person other than Borrowers or Lender shall be entitled to rely upon this Agreement or be entitled to the benefits of this Agreement.

7.9 **Participation.** Borrowers acknowledge that Lender may, at its option, sell participation interests in the Loan or to other participating banks or Lender may (but shall not be obligated to) assign its interest in the Loan to its affiliates, or to other assignees (the "**Assignee**"). Borrowers agree with each present and future participant in the Loan or Assignee of the Loan that if an Event of Default should occur, each present and future participant or Assignee shall have all of the rights and remedies of Lender with respect to any deposit due from Borrowers. The execution by a participant of a participation agreement with Lender, and the execution by Borrowers of this Agreement, regardless of the order of execution, shall evidence an agreement between Borrowers and said participant in accordance with the terms of this Section 7.9.

7.10 **Supersedes Prior Agreements; Counterparts.** This Agreement and the instruments referred to herein supersede and incorporate all representations, promises, and statements, oral or written, made by Lender in connection with the Loan. This Agreement may not be varied, altered, or amended except by a written instrument executed by an authorized officer of the Lender. This Agreement may be executed in any number of counterparts, each of which, when executed and delivered, shall be an original, but such counterparts shall together constitute one and the same instrument.

7.11 **Loan Agreement Governs.** The Loan is governed by terms and provisions set forth in this Agreement and the other Loan Documents and in the event of any irreconcilable conflict between the terms of the other Loan Documents and the terms of this Agreement, the terms of this Agreement shall control; provided, however, in the event there is any apparent conflict between any particular term or provision which appears in both this Agreement and the other Loan Documents and it is possible and reasonable for the terms of both this Agreement and the Loan Documents to be performed or complied with then notwithstanding the foregoing both the terms of this Agreement and the other Loan Documents shall be performed and complied with.

7.12 **Construction of Provisions of this Agreement.** Lender has not agreed to make any loan other than that specifically described herein. All requirements herein shall be deemed material to Lender. Except as specified herein, all conditions and requirements must be satisfied by Borrowers prior to the Closing Date. Whenever any of the Loan Documents refers to a matter being "satisfactory" to Lender, subject to Lender's "approval" or "consent," at Lender's "option," at Lender's "determination," "required" by Lender, may be "granted" or "denied" at Lender's "request," as Lender shall "deem necessary," or similar terminology, it is

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deemed that each of the aforesaid shall be in the sole discretion of the Lender (except as otherwise expressly provided), and if any term or condition requires Lender's approval, consent, or satisfaction (the "**Lender's Approval**"), the Lender's Approval shall not be implied, but shall be evidenced only by a written notice from Lender specifically addressed to the particular requirement or condition and expressing Lender's Approval. If "Borrower" or "Guarantor" consists of more than one Person, all obligations of Borrowers or Guarantors are joint and several and all references herein to "Borrower" or "Guarantor" shall apply both individually to each Person and in the alternative to all of them collectively, whether or not so stated.

7.13 **Advertising.** Borrowers acknowledge and agree that Lender is authorized to state in advertising or other press releases the fact that the type and amount of financing contemplated under the Loan Documents has been provided to Borrowers and Guarantor for the Facility by Lender. Lender agrees not to include any confidential information of the Borrowers or any Guarantor in such advertisements.

7.14 **CONTROLLING LAW.** THE PARTIES HERETO AGREE THAT THE VALIDITY, INTERPRETATION, ENFORCEMENT AND EFFECT OF THIS AGREEMENT AND THE OTHER LOAN DOCUMENTS SHALL BE GOVERNED BY, AND CONSTRUED IN ACCORDANCE WITH, THE LAWS OF THE STATE OF NEW JERSEY AND THE PARTIES HERETO SUBMIT (AND WAIVE ALL RIGHTS TO OBJECT) TO NON-EXCLUSIVE PERSONAL JURISDICTION IN THE STATE OF NEW JERSEY, FOR THE ENFORCEMENT OF ANY AND ALL OBLIGATIONS UNDER THIS AGREEMENT AND THE OTHER LOAN DOCUMENTS EXCEPT THAT IF ANY SUCH ACTION OR PROCEEDING ARISES UNDER THE CONSTITUTION, LAWS OR TREATIES OF THE UNITED STATES OF AMERICA, OR IF THERE IS A DIVERSITY OF CITIZENSHIP BETWEEN THE PARTIES THERETO, SO THAT IT IS TO BE BROUGHT IN A UNITED STATES DISTRICT COURT, IT SHALL BE BROUGHT IN THE UNITED STATES DISTRICT COURT FOR THE DISTRICT OF NEW JERSEY OVER SHREWSBURY, NEW JERSEY OR ANY SUCCESSOR FEDERAL COURT HAVING ORIGINAL JURISDICTION.

7.15 **WAIVER OF JURY TRIAL.** EACH BORROWER HEREBY WAIVES ANY RIGHT THAT IT MAY HAVE TO A TRIAL BY JURY ON ANY CLAIM, COUNTERCLAIM, SETOFF, DEMAND, ACTION OR CAUSE OF ACTION (A) ARISING OUT OF OR IN ANY WAY RELATED TO THIS AGREEMENT, THE OTHER LOAN DOCUMENTS OR THE LOAN, OR (B) IN ANY WAY CONNECTED WITH OR PERTAINING OR RELATED TO OR INCIDENTAL TO ANY DEALINGS OF LENDER AND/OR BORROWERS WITH RESPECT TO THE LOAN DOCUMENTS OR IN CONNECTION WITH THIS AGREEMENT OR THE EXERCISE OF ANY PARTY'S RIGHTS AND REMEDIES UNDER THIS AGREEMENT OR OTHERWISE, OR THE CONDUCT OR THE RELATIONSHIP OF THE PARTIES HERETO, IN ALL OF THE FOREGOING CASES WHETHER NOW EXISTING OR HEREAFTER ARISING AND WHETHER SOUNDING IN CONTRACT, TORT OR OTHERWISE. EACH BORROWER AGREES THAT LENDER MAY FILE A COPY OF THIS AGREEMENT AND WILL BE ABLE TO FILE A COPY OF ALL LOAN DOCUMENTS WITH ANY COURT AS WRITTEN EVIDENCE OF THE KNOWING, VOLUNTARY, AND BARGAINED AGREEMENT OF EACH BORROWER IRREVOCABLY TO

WAIVE ITS RIGHTS TO TRIAL BY JURY AS AN INDUCEMENT OF LENDER TO MAKE THE LOAN, AND THAT, TO THE EXTENT PERMITTED BY APPLICABLE LAW, ANY DISPUTE OR CONTROVERSY WHATSOEVER (WHETHER OR NOT MODIFIED HEREIN) BETWEEN BORROWERS AND LENDER SHALL INSTEAD BE TRIED IN A COURT OF COMPETENT JURISDICTION BY A JUDGE SITTING WITHOUT A JURY.

7.16 **Joint and Several Obligations.** All obligations of Borrowers hereunder are joint and several. All obligations of each Guarantor under the Loan Documents are joint and several. The use of the phrases "either Borrower" or "each Borrower" or "any Guarantor" in some sentences herein is for clarity only; the failure to use such phrases elsewhere shall not alter the fact that each reference to either Borrower and any Guarantor hereunder is intended to mean each party included within such defined term, both jointly and severally.

7.17 **Time is of the Essence.** Time is of the essence of the Loan Documents and of each provision hereof.

7.18 **Seniority; Subordination.** Notwithstanding anything to the contrary contained in this Agreement, the indebtedness, rights, remedies and obligations evidenced hereby are senior and/or subordinate, if at all, in the manner and to the extent

set forth in the Subordination and Standstill Agreement and each signatory hereto shall be bound by the provisions of the Subordination and Standstill Agreement.

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**IN WITNESS WHEREOF**, Borrowers and the Lender have caused this Agreement to be properly executed, by their respective duly authorized representatives, as of the date first above written.

**BORROWERS:**

**CSCC PROPERTY HOLDINGS, LLC**, a Georgia limited liability company

By: /s/ Christopher F. Brogdon

Name: Christopher F. Brogdon

Title: Manager

**CSCC NURSING, LLC**, a Georgia limited liability company

By: /s/ Christopher F. Brogdon

Name: Christopher F. Brogdon

Title: Manager

**LENDER:**

**CONTEMPORARY HEALTHCARE FUND I, L.P.**, a Delaware limited partnership

By: CHC-GP, LLC,  
a Delaware limited liability company

Its: General Partner

By: /s/ Eric Smith

Eric Smith, Member

SIGNATURE PAGE TO LOAN AGREEMENT – ADCARE - AR

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PROMISSORY NOTE

\$5,000,000

August 17, 2012

**FOR VALUE RECEIVED**, the undersigned, **CSCC PROPERTY HOLDINGS, LLC**, a Georgia limited liability company, and **CSCC NURSING, LLC**, a Georgia limited liability company (collectively, the “**Maker**”), hereby jointly and severally promise to pay to the order of **CONTEMPORARY HEALTHCARE SENIOR LIEN FUND I, L.P.**, a Delaware limited partnership (hereinafter, together with any subsequent holder of this Note, the “**Holder**”) at its main office in the Borough of Shrewsbury, New Jersey, or at such other address as the Holder may, from time to time, designate in writing, the principal sum of Five Million and No/100 Dollars (\$5,000,000.00) (the “**Loan**”), together with interest thereon, such principal and interest to be payable as follows:

A. On the date hereof, Maker shall pay to Holder a payment of interest in the amount of \$22,430.56.

B. On September 20, 2012, and on the twentieth day of each successive calendar month thereafter until July 20, 2015, Maker shall pay to Holder an installment of interest at the Note Rate on the principal amount of this Note (such payments under paragraphs A and B being hereinafter referred to as the “**Installment Payments**”) or such greater amount pursuant to the terms of this Note. The Installment Payments are set forth on an amortization schedule attached to the Loan Agreement (as defined below) as Schedule 2.4(a). Borrower acknowledges receipt and review of both Schedule 2.4(a) of the Loan Agreement and the electronic version of Schedule 2.4(a), which electronic version, among other things, sets forth the formulas and other calculations employed to create such amortization table.

D. On August 20, 2015 (the “**Maturity Date**”), if not sooner prepaid, Maker shall pay to Holder, without demand, the outstanding principal balance of this Note, together with all accrued and unpaid interest, as such Maturity Date may be extended as provided for herein.

The Installment Payments are based upon an interest rate of eight and one-half percent per annum (8.50%) (the “**Note Rate**”).

Each payment received shall be applied in the following order:

- (1) First, to accrued and unpaid interest at the Note Rate as part of the Installment Payments; and
- (3) Second, to other principal amounts outstanding, subject to payment of any prepayment premium as defined in and due pursuant to the Loan Agreement.

Reference to the Loan Agreement between Maker and Holder of even date herewith, as the same may hereafter be amended (as so amended, the “**Loan Agreement**”) is hereby made for a statement of the rights of Holder and the obligations of Maker, which Loan Agreement is incorporated herein by this reference, but neither this reference to the Loan Agreement nor any provision thereof shall affect or impair the absolute and unconditional obligation of Maker to pay the principal and interest of this Note when due. Capitalized terms used herein without definition shall have the meanings ascribed to such terms in the Loan Agreement.

Interest on the outstanding principal balance of the Loan shall be calculated on the basis of a 360-day year by multiplying the outstanding principal amount by the applicable per annum rate, multiplying the product thereof by the actual number of days elapsed

and dividing the product so obtained by 360. Interest for partial period payments will be calculated by multiplying the outstanding principal amount by the applicable per annum rate, multiplying the product thereof by the actual days elapsed, and dividing the product so obtained by 360.

The principal and interest shall be payable in lawful money of the United States which shall be legal tender for public and private debts at the time of payment. Maker may prepay the outstanding principal balance of this Note, or any part thereof, only in accordance with the terms and conditions of the Loan Agreement.

This Note is secured and guaranteed by the Loan Documents, including but not limited to the Mortgage, the Assignment of Lease and Rents, the Security Agreement and the Collateral.

The principal sum evidenced by this Note, together with accrued interest, shall become immediately due and payable at the option of the Holder upon the occurrence of any Event of Default under the terms of the Loan Agreement, which such "Events of Default" are incorporated herein by reference as if set forth in full herein.

Notwithstanding other remedies available to the Holder, if any payment due hereunder is not made on or before the tenth (10th) day after such payment became due, Maker, in addition to the amount in default, will also pay to Holder a late charge equal to five percent (5%) of the payment which is in default, but not more than the maximum amount permitted by applicable law. Notwithstanding other remedies available to the Holder, if any payment due hereunder is not made on or before the thirtieth (30th) day after such payment became due, Maker, in addition to the amount in default, will also pay to Holder a total late charge equal to five percent (5%) of the payment which is in default, but not more than the maximum amount permitted by applicable law. Thereafter, for each thirty (30) days such payment or charge is not paid, Maker agrees to pay Holder an additional late charge equal to five percent (5%) of the amount of such payment or charge which has not been paid to Holder.

Upon an Event of Default the Note Rate shall be increased by five hundred (500) basis points (such increased rate, the "**Default Rate**"), computed from the date of the notice from Holder of the Event of Default as described in the Loan Agreement, subject to Maker's cure of such Event of Default within thirty (30) days following notice from Holder of such Event of Default. If such Event of Default is not cured within such thirty (30) day period, the Note Rate shall remain at five hundred (500) basis points above the Note Rate computed from the date of the notice from Holder of such Event of Default until the Event of Default has been cured. The intent of such provision is that following an Event of Default, and regardless of any intervening Events of Default until such initial Event of Default is cured, the Note Rate shall be increased only one time and, once cured, any succeeding Event of Default shall then again be governed by the provisions of this paragraph. In the event (i) Maker cures such Event of Default to the satisfaction of Holder in its sole discretion (which, with respect to a payment Event of Default, shall mean solely repayment by the Maker of amounts then due under this Note) and (ii) Holder elects not to exercise any of its other remedies upon such Event of Default, interest on the Loan shall return to the Note Rate, all as more particularly described in the Loan Agreement.

Maker will bear all taxes, fees and expenses (including actual attorneys' fees and expenses of counsel of Holder) in connection with this Note. If, at any time, a Default occurs or Holder becomes a party to any suit or proceeding in order to protect its interests or its rights under this Note, or if Holder is made a party to any suit or proceeding by virtue of this Note and as a result of any of the foregoing, Holder employs counsel to advise or provide other representation with respect to this Note, or to take any action in or with respect to any suit or proceeding relating to this Note, then in any such events, all of the actual attorneys' fees arising from such services, including attorneys' fees for preparation of litigation and in any appellate or bankruptcy proceedings, and any expenses, costs and charges relating thereto shall constitute additional obligations of Maker to Holder payable on demand of Holder. Such amounts shall constitute a portion of the Loan Obligations, shall be secured by the Collateral and shall bear interest at the Default Rate from the date advanced until repaid.



With respect to the amounts due pursuant to this Note, the Maker waives the following:

- (1) All rights of exemption of property from levy or sale under execution or other process for the collection of debts under the Constitution or laws of the United States or any state thereof;
- (2) Demand, presentment, protest, notice of dishonor, notice of nonpayment, suit against any party, diligence in collection of this Note, and all other requirements necessary to enforce this Note except for notices expressly required by the Loan Documents; and
- (3) Any further receipt by or acknowledgment of any collateral now or hereafter deposited as security for the Loan.

In no event shall the amount of interest due or payable hereunder exceed the maximum rate of interest designated by applicable law, and in the event such payment is inadvertently paid by Maker or inadvertently received by Holder, then such excess sum shall be credited as a payment of principal, unless Maker elects to have such excess sums refunded to Maker herewith.

It is the express intent hereof that Maker not pay and Holder not receive, directly or indirectly, interest in excess of that which may be legally paid by Maker under applicable law.

Holder shall not by any act, delay, omission, or otherwise be deemed to have waived any of its rights or remedies, and no waiver of any kind shall be valid unless in writing and signed by Holder. All rights and remedies of Holder under the terms of this Note and applicable statutes or rules of law shall be cumulative, and may be exercised successively or concurrently. Maker agrees that there are no defenses, equities or setoffs with respect to the obligations set forth herein, and to the extent any such defenses, equities, or setoffs may exist, the same are hereby expressly released, forgiven, waived and forever discharged. The obligations of Maker hereunder shall be binding upon and enforceable against Maker and its successors and assigns.

Any provisions of this Note which may be unenforceable or invalid under any law shall be ineffective to the extent of such unenforceability or invalidity without affecting the enforceability or validity of any other provision hereof.

If Maker consists of more than one individual or entity, all obligations hereunder shall be joint and several.

Holder may, at its option, release any Collateral given to secure the indebtedness evidenced hereby or may release any Guarantor of the indebtedness evidenced hereby, and no such release shall impair the obligations of Maker to Holder.

**IN ANY SUIT UPON THIS NOTE THE VALIDITY, INTERPRETATION, ENFORCEMENT, AND EFFECT OF THIS NOTE SHALL BE GOVERNED BY, AND CONSTRUED IN ACCORDANCE WITH, THE LAWS OF THE STATE OF NEW JERSEY. THE HOLDER'S PRINCIPAL PLACE OF BUSINESS IS LOCATED IN THE STATE OF NEW JERSEY, AND THE MAKER AGREES THAT THIS NOTE SHALL BE HELD BY HOLDER AT SUCH PRINCIPAL PLACE OF BUSINESS, AND THE HOLDING OF THIS NOTE BY HOLDER THEREAT SHALL CONSTITUTE SUFFICIENT MINIMUM CONTACTS OF MAKER WITH THE STATE OF NEW JERSEY FOR THE PURPOSE OF CONFERRING JURISDICTION UPON THE FEDERAL AND STATE COURTS PRESIDING IN SUCH STATE AND THE COUNTY OF HOLDER'S PRINCIPAL PLACE OF BUSINESS. MAKER CONSENTS THAT ANY LEGAL ACTION OR PROCEEDING ARISING HEREUNDER MAY BE BROUGHT IN THE FEDERAL AND STATE COURTS PRESIDING IN SUCH COUNTY AND STATE AND ASSENTS AND SUBMITS TO THE PERSONAL JURISDICTION OF ANY SUCH COURT IN ANY ACTION OR PROCEEDING INVOLVING THIS NOTE. NOTHING HEREIN SHALL LIMIT THE JURISDICTION OF ANY OTHER COURT.**

TO THE EXTENT PERMITTED BY APPLICABLE LAW, MAKER HEREBY WAIVES ANY RIGHT TO TRIAL BY JURY ON ANY CLAIM, COUNTERCLAIM, SETOFF, DEMAND, ACTION, OR CAUSE OF ACTION (A) ARISING OUT OF OR IN ANY WAY PERTAINING OR RELATING TO THIS NOTE OR ANY OF THE LOAN DOCUMENTS, OR (B) IN ANY WAY CONNECTED WITH OR PERTAINING OR RELATED TO OR INCIDENTAL TO ANY DEALINGS OF THE PARTIES HERETO WITH RESPECT TO THIS NOTE OR THE LOAN DOCUMENTS, OR IN

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CONNECTION WITH THE TRANSACTIONS RELATED THERETO OR CONTEMPLATED THEREBY OR THE EXERCISE OF EITHER PARTY' S RIGHTS AND REMEDIES THEREUNDER, IN ALL OF THE FOREGOING CASES WHETHER NOW EXISTING OR HEREAFTER ARISING, AND WHETHER SOUNDING IN CONTRACT, TORT, OR OTHERWISE.

EACH MAKER AGREES THAT HOLDER MAY FILE A COPY OF THIS WAIVER WITH ANY COURT AS WRITTEN EVIDENCE OF THE KNOWING, VOLUNTARY, AND BARGAINED-FOR AGREEMENT OF MAKER IRREVOCABLY TO WAIVE ITS RIGHT TO TRIAL BY JURY, AND THAT, TO THE EXTENT PERMITTED BY APPLICABLE LAW, ANY DISPUTE OR CONTROVERSY WHATSOEVER BETWEEN MAKER AND HOLDER SHALL INSTEAD BE TRIED IN A COURT OF COMPETENT JURISDICTION BY A JUDGE SITTING WITHOUT A JURY.

\* \* \*

[SIGNATURE APPEARS ON FOLLOWING PAGE]

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IN WITNESS WHEREOF, Maker has caused this instrument to be properly executed and delivered as of the day and year first above written.

**MAKER:**

**CSCC PROPERTY HOLDINGS, LLC**, a Georgia limited liability company

By: /s/ Christopher F. Brogdon

Name: Christopher F. Brogdon

Title: Manager

**CSCC NURSING, LLC**, a Georgia limited liability company

By: /s/ Christopher F. Brogdon

Name: Christopher F. Brogdon

Title: Manager

SIGNATURE PAGE TO PROMISSORY NOTE - ADCARE - SENIOR

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REVOLVING LOAN PROMISSORY NOTE

\$600,000

August 17, 2012

**FOR VALUE RECEIVED**, the undersigned, **CSCC PROPERTY HOLDINGS, LLC**, a Georgia limited liability company, and **CSCC NURSING, LLC**, a Georgia limited liability company (collectively, the “**Maker**”), “), hereby jointly and severally promise to pay to the order of **CONTEMPORARY HEALTHCARE FUND I, L.P.**, a Delaware limited partnership (hereinafter, together with any subsequent holder of this Note, the “**Holder**”) at its main office in the Borough of Shrewsbury, New Jersey, or at such other address as the Holder may, from time to time, designate in writing, the principal sum of Six Hundred Thousand and no/100 Dollars (\$600,000) (the “**Loan**”) or, if less, the aggregate unpaid amount of all advances made under the Loan pursuant to the Loan Agreement (hereinafter defined), and, together with interest thereon as herein provided, such principal and interest to be payable as follows:

A. Beginning September 20, 2012 and on the 20<sup>th</sup> day of each subsequent month until the Maturity Date, as defined below, if not sooner prepaid, Maker shall pay to Holder without demand, payments of interest and payments of principal in excess of the Borrowing Base as defined in the Loan Agreement (the “**Installment Payment**”). The Installment Payment amount will be calculated based upon an interest rate of nine percent (9%) per annum for the term of the Loan (the “**Note Rate**”). Each monthly Installment Payment will be the sum of:

- (i) the products of the Note Rate divided by 360 multiplied by the daily outstanding principal balance of the Loan for the preceding monthly period multiplied by thirty (30) days. Interest for partial period payments will be calculated by multiplying the outstanding principal amount by the applicable per annum rate, multiplying the product thereof by the actual days elapsed, and dividing the product so obtained by 360; and
- (ii) the difference between the outstanding principal balance and the Borrowing Base; should the outstanding principal balance be less than or equal to the Borrowing Base this amount shall be zero (0).

B. On August 20, 2015 (the “**Maturity Date**”), unless such date is extended as provided for herein, if not sooner prepaid, Maker shall pay to Holder without demand, the outstanding principal balance, together with all accrued and unpaid interest, if any.

Each Installment Payment received shall be applied in the following order:

- (i) First, to accrued and unpaid interest at the Note Rate as part of the Installment Payments;
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- (ii) Second, to any additional payments related to an Installment Payment; and
  - (iii) Third, to other principal amounts outstanding, subject to payment of any Non-Use Fee, Monitoring Fee or Exit Fee due pursuant to the Loan Agreement.

Provided Maker is not in arrears in Installment Payments, Maker may pay to Holder, up to once monthly, a payment to be credited to the aggregate outstanding principal amount of the Loan (“**Principal Reduction Payment**”). For the purposes of calculating interest on the Loan, the Principal Reduction Payment will be credited to the aggregate outstanding amount of the Loan on the date of receipt by the Holder.

Reference to the Loan Agreement between Maker and Holder of even date herewith, as the same may hereafter be amended (as so amended, the “**Loan Agreement**”) is hereby made for a statement of the rights of Holder and the obligations of Maker, which Loan Agreement is incorporated herein by this reference, but neither this reference to the Loan Agreement nor any provision thereof shall affect or impair the absolute and unconditional obligation of Maker to pay the outstanding principal and interest of this Note when due. Capitalized terms used herein without definition shall have the meanings ascribed to such terms in the Loan Agreement.

The principal and interest shall be payable in lawful money of the United States which shall be legal tender for public and private debts at the time of payment. Maker may prepay the outstanding principal balance of this Note, or any part thereof, only in accordance with the terms and conditions of the Loan Agreement.

This Note is secured and guaranteed by the Loan Documents and the Collateral.

The outstanding principal sum evidenced by this Note, together with accrued interest, shall become immediately due and payable at the option of the Holder upon the occurrence of any Event of Default under the terms of the Loan Agreement, which such “Events of Default” are incorporated herein by reference as if set forth in full herein.

Notwithstanding other remedies available to the Holder, if any payment due hereunder is not made on or before the tenth (10th) day after such payment became due, Maker, in addition to the amount in default, will also pay to Holder a late charge equal to five percent (5%) of the payment which is in default, but not more than the maximum amount permitted by applicable law. Notwithstanding other remedies available to the Holder, if any payment due hereunder is not made on or before the thirtieth (30th) day after such payment became due, Maker, in addition to the amount in default, will also pay to Holder a total late charge equal to five percent (5%) of the payment which is in default, but not more than the maximum amount permitted by applicable law. Thereafter, for each thirty (30) days such payment or charge is not paid, Maker agrees to pay Holder an additional late charge equal to five percent (5%) of the amount of such payment or charge which has not been paid to Holder.

Upon an Event of Default the Note Rate shall be increased by five hundred (500) basis points (such increased rate, the “**Default Rate**”), computed from the date of the notice from Holder of the Event of Default as described in the Loan Agreement, subject to Maker’s cure of such Event of Default within thirty (30) days following notice from Holder of such Event of Default. If such Event of Default is not cured within such thirty (30) day period, the Note Rate

shall remain at five hundred (500) basis points above the Note Rate computed from the date of the notice from Holder of such Event of Default until the Event of Default has been cured. The intent of such provision is that following an Event of Default, and regardless of any intervening Events of Default until such initial Event of Default is cured, the Note Rate shall be increased only one time and, once cured, any succeeding Event of Default shall then again be governed by the provisions of this paragraph. In the event (i) Maker cures such Event of Default to the satisfaction of Holder in its sole discretion (which, with respect to a payment Event of Default, shall mean solely repayment by the Maker of amounts then due under this Note) and (ii) Holder elects not to exercise any of its other remedies during such Event of Default, interest on the Loan shall return to the Note Rate, all as more particularly described in the Loan Agreement.

Maker will bear all taxes, fees and expenses (including actual attorneys’ fees and expenses of counsel of Holder) in connection with this Note. If, at any time, a Default occurs or Holder becomes a party to any suit or proceeding in order to protect its interests or its rights under this Note, or if Holder is made a party to any suit or proceeding by virtue of this Note and as a result of any of the foregoing, Holder employs counsel to advise or provide other representation with respect to this Note, or to take any action in or with respect to any suit or proceeding relating to this Note, then in any such events, all of the actual attorneys’ fees arising from such services, including attorneys’ fees for preparation of litigation and in any appellate or bankruptcy proceedings, and any expenses, costs and charges relating thereto shall constitute additional obligations of Maker to Holder payable on demand of Holder. Such amounts

shall constitute a portion of the Loan Obligations, shall be secured by the Collateral and shall bear interest at the Default Rate from the date advanced until repaid.

With respect to the amounts due pursuant to this Note, each Maker waives the following:

1. All rights of exemption of property from levy or sale under execution or other process for the collection of debts under the Constitution or laws of the United States or any state thereof;
2. Demand, presentment, protest, notice of dishonor, notice of nonpayment, suit against any party, diligence in collection of this Note, and all other requirements necessary to enforce this Note except for notices expressly required by the Loan Documents; and
3. Any further receipt by or acknowledgment of any collateral now or hereafter deposited as security for the Loan.

In no event shall the amount of interest due or payable hereunder exceed the maximum rate of interest designated by applicable law, and in the event such payment is inadvertently paid by Maker or inadvertently received by Holder, then such excess sum shall be credited as a payment of principal, unless Maker elects to have such excess sums refunded to Maker herewith. It is the express intent hereof that Maker not pay and Holder not receive, directly or indirectly, interest in excess of that which may be legally paid by Maker under applicable law.

Holder shall not by any act, delay, omission, or otherwise be deemed to have waived any of its rights or remedies, and no waiver of any kind shall be valid unless in writing and signed by

Holder. All rights and remedies of Holder under the terms of this Note and applicable statutes or rules of law shall be cumulative, and may be exercised successively or concurrently. Each Maker agrees that there are no defenses, equities or setoffs with respect to the obligations set forth herein, and to the extent any such defenses, equities, or setoffs may exist, the same are hereby expressly released, forgiven, waived and forever discharged. The obligations of each Maker hereunder shall be binding upon and enforceable against each Maker and its successors and assigns.

Any provisions of this Note which may be unenforceable or invalid under any law shall be ineffective to the extent of such unenforceability or invalidity without affecting the enforceability or validity of any other provision hereof.

All obligations of each Maker hereunder shall be joint and several.

Holder may, at its option, release any Collateral given to secure the indebtedness evidenced hereby or may release any Guarantor of the indebtedness evidenced hereby, and no such release shall impair the obligations of any Maker to Holder.

**IN ANY SUIT UPON THIS NOTE THE VALIDITY, INTERPRETATION, ENFORCEMENT, AND EFFECT OF THIS NOTE SHALL BE GOVERNED BY, AND CONSTRUED IN ACCORDANCE WITH, THE LAWS OF THE STATE OF NEW JERSEY. THE HOLDER'S PRINCIPAL PLACE OF BUSINESS IS LOCATED IN THE STATE OF NEW JERSEY, AND THE MAKER AGREES THAT THIS NOTE SHALL BE HELD BY HOLDER AT SUCH PRINCIPAL PLACE OF BUSINESS, AND THE HOLDING OF THIS NOTE BY HOLDER THEREAT SHALL CONSTITUTE SUFFICIENT MINIMUM CONTACTS OF MAKER WITH THE STATE OF NEW JERSEY FOR THE PURPOSE OF CONFERRING JURISDICTION UPON THE FEDERAL AND STATE COURTS PRESIDING IN SUCH STATE AND THE COUNTY OF HOLDER'S PRINCIPAL PLACE OF BUSINESS. MAKER CONSENTS THAT ANY LEGAL ACTION OR PROCEEDING ARISING HEREUNDER MAY BE BROUGHT IN THE FEDERAL AND STATE COURTS PRESIDING IN SUCH COUNTY**

AND STATE AND ASSENTS AND SUBMITS TO THE PERSONAL JURISDICTION OF ANY SUCH COURT IN ANY ACTION OR PROCEEDING INVOLVING THIS NOTE. NOTHING HEREIN SHALL LIMIT THE JURISDICTION OF ANY OTHER COURT.

TO THE EXTENT PERMITTED BY APPLICABLE LAW, MAKER, AND BY ACCEPTANCE OF THIS NOTE, HOLDER, HEREBY WAIVES ANY RIGHT TO TRIAL BY JURY ON ANY CLAIM, COUNTERCLAIM, SETOFF, DEMAND, ACTION, OR CAUSE OF ACTION (A) ARISING OUT OF OR IN ANY WAY PERTAINING OR RELATING TO THIS NOTE OR ANY OF THE LOAN DOCUMENTS, OR (B) IN ANY WAY CONNECTED WITH OR PERTAINING OR RELATED TO OR INCIDENTAL TO ANY DEALINGS OF THE PARTIES HERETO WITH RESPECT TO THIS NOTE OR THE LOAN DOCUMENTS, OR IN CONNECTION WITH THE TRANSACTIONS RELATED THERETO OR CONTEMPLATED THEREBY OR THE EXERCISE OF EITHER PARTY' S RIGHTS AND REMEDIES THEREUNDER, IN ALL OF THE FOREGOING CASES WHETHER NOW EXISTING OR HEREAFTER ARISING, AND WHETHER SOUNDING IN CONTRACT, TORT, OR OTHERWISE.

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EACH MAKER AND HOLDER AGREES THAT MAKERS AND HOLDER MAY FILE A COPY OF THIS WAIVER WITH ANY COURT AS WRITTEN EVIDENCE OF THE KNOWING, VOLUNTARY, AND BARGAINED-FOR AGREEMENT OF MAKER AND HOLDER IRREVOCABLY TO WAIVE ITS RIGHT TO TRIAL BY JURY, AND THAT, TO THE EXTENT PERMITTED BY APPLICABLE LAW, ANY DISPUTE OR CONTROVERSY WHATSOEVER BETWEEN MAKER AND HOLDER SHALL INSTEAD BE TRIED IN A COURT OF COMPETENT JURISDICTION BY A JUDGE SITTING WITHOUT A JURY.

*Signatures appear on following page*

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IN WITNESS WHEREOF, each Maker has caused this instrument to be properly executed and delivered as of the day and year first above written.

**MAKER:**

**CSCC PROPERTY HOLDINGS, LLC**, a Georgia limited liability company

By: /s/ Christopher F. Brogdon

Name: Christopher F. Brogdon

Title: Manager

**CSCC NURSING, LLC**, a Georgia limited liability company

By: /s/ Christopher F. Brogdon

Name: Christopher F. Brogdon

Title: Manager

SIGNATURE PAGE TO PROMISSORY NOTE – ADCARE - AR



PREPARED BY, AND AFTER RECORDING RETURN TO:

Thomas K. Slattery, Esq.  
Law Offices of Thomas K. Slattery, P.L.L.C.  
1250 24th Street, N.W., Suite 300  
Washington, D.C. 20037

**ASSIGNMENT OF LEASES AND RENTS**

**LESSORS:** **CSCC PROPERTY HOLDINGS, LLC**, a Georgia limited liability company, having an address of Two Buckhead Plaza, 3050 Peachtree Road NW, Suite 355, Atlanta, Georgia 30305

**CSCC NURSING, LLC**, a Georgia limited liability company, having an address of Two Buckhead Plaza, 3050 Peachtree Road NW, Suite 355, Atlanta, Georgia 30305

**STATE OF OKLAHOMA**

**COUNTY OF TULSA**

**ASSIGNMENT OF LEASES AND RENTS**

This **ASSIGNMENT OF LEASE AND RENTS** (this "Assignment"), made as of August 17, 2012, by and between **CSCC PROPERTY HOLDINGS, LLC**, a Georgia limited liability company, whose address is Two Buckhead Plaza, 3050 Peachtree Road NW, Suite 355, Atlanta, Georgia 30305 and whose organization number is GA 12034119, and **CSCC NURSING, LLC**, a Georgia limited liability company, whose address is Two Buckhead Plaza, 3050 Peachtree Road NW, Suite 355, Atlanta, Georgia 30305 and whose organization number is GA 12034132 (each a "Lessor" and, collectively the "Lessors") and **CONTEMPORARY HEALTHCARE SENIOR LIEN FUND I, L.P.**, a Delaware limited partnership ("Lender").

**W I T N E S S E T H :**

FOR AND IN CONSIDERATION of the Loan, defined below, and other good and valuable consideration, in hand paid by Lender, the receipt and sufficiency of which are hereby acknowledged, Lessors do hereby (i) grant, transfer and immediately and absolutely assign to Lender, its successors and assigns, all of the right, title and interest of Lessors in and to the rents (and payments in lieu of rents), income and profits arising from the Premises (as hereinafter defined) and (ii) all of Lessors' remaining interests as "landlord" or "lessor" in and to those certain lease agreements, residency agreements, occupancy agreements, tenant contracts, rental agreements and any other agreements for the leasing, rental, use or occupancy of space by tenants, residents or patients now or hereafter existing (together with any and all extensions, renewals and modifications thereof and guarantees of the payment and/or performance of obligations of any tenant or lessee thereunder) (hereinafter collectively referred to as the "Leases" and said tenants or lessees thereunder hereinafter collectively referred to as "Tenants" or individually as "Tenant" as the context requires), now or hereafter executed by or on behalf of the Lessors (or assigned to the Lessors), as "landlord" or "lessor" therein, and others as "Tenant" or "Lessee" therein, conveying or demising all or any portion of the space in the improvements now or hereafter located on those certain tracts or parcels of land (hereinafter referred to as the "Premises") lying and being in the state of Oklahoma within the County identified on Exhibit A attached hereto, the Premises being more particularly described in Exhibit A attached hereto and by this reference incorporated herein and made a part hereof, if any, together with all proceeds from the sale or other disposition of the Leases or rents and profits therefrom



and all of Lessors' claims and rights to the payment of damages arising from any rejection by a Tenant of any lease under the Bankruptcy Code, 11 U.S.C. §101 et seq, as the same may be amended. This assignment of rents, income and profits arising from the Premises as hereinabove provided is intended by Lessors and Lender to create, and shall be construed to create, an absolute assignment to Lender, subject only to the terms and provisions hereof, and not as an assignment as security for the indebtedness and obligations hereinbelow described. This assignment is effective immediately.

This Assignment is made in connection with the following described indebtedness and

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obligations (hereinafter referred to as the "**Indebtedness**"):

(a) Any and all indebtedness and obligations evidenced by that certain Promissory Note dated August 17, 2012 (hereinafter referred to as the "**Note**"), executed by the Lessors, payable to the order of Lender at Lender's office in Shrewsbury, New Jersey, or at such other place as the holder may from time to time require, in the principal sum of \$5,000,000.00 (the "**Loan**"), with interest thereon at the rates therein specified, together with any and all renewals, modifications, consolidations, amendments and extensions of said note and the indebtedness evidenced by said Note and made pursuant to a Loan Agreement dated August 17, 2012 by and between the Lessors and the Lender (the "**Loan Agreement**");

(b) Any and all indebtedness and obligations evidenced and secured by that certain Mortgage, Assignment of Rents and Leases, Security Agreement and Fixture Filing dated August 17, 2012 (the "**Mortgage**"), executed by the Lessors in favor of Lender, to be recorded in the official records of Tulsa County, Oklahoma, together with all modifications and amendments thereto, as well as any and all advances made by Lender to protect or preserve the lien thereof on the real property encumbered thereby, or for taxes or insurance premiums as provided therein;

(c) Any and all advances made by Lender to protect or preserve the security created by this Assignment, or to protect or preserve the Premises or the lien of the Mortgage on the Premises, or for taxes or insurance premiums as provided in the Mortgage; and

(d) Any and all indebtedness and obligations of the Lessors contained herein or in any other document or instrument (other than the Note, the Loan Agreement and the Mortgage) evidencing, securing or relating to the indebtedness secured thereby (the Note, the Loan Agreement, the Mortgage and such other instruments and documents being hereinafter collectively referred to as the "**Loan Documents**").

Lessors and Lender agree that (i) an extension or extensions may be made at the time of payment of all or any part of the Indebtedness; (ii) the terms of this Assignment and any of any of the Loan Documents may be modified; (iii) additional security may be given by the Lessors; and (iv) any of the Leases may be released herefrom, all without altering or affecting the security interest created by this Assignment and without altering or releasing the obligations of the Lessors under any of the Loan Documents.

Should the Indebtedness be paid when the same shall become due and payable, then this Assignment shall be canceled and surrendered as hereinafter provided.

Lessors and Lender hereby further covenant and agree as follows, in addition to and not in substitution for or in derogation of any other covenants contained in the Mortgage or the other Loan Documents:

## **ARTICLE I.**

1.1 **Warranties of Lessors.** Each Lessor hereby warrants unto Lender that:

- (a) Lessor is the absolute owner of the entire Lessor's interest in the Leases;
- (b) Lessor has made no assignment of any of the rights of Lessor under any of the Leases, other than this Assignment;
- (c) Lessor has neither done any act nor omitted to do any act which might prevent Lender from, or limit Lender in, exercising its remedies under any of the provisions of this Assignment;
- (d) Lessor shall not accepted payment of rental under any of the Leases for more than one (1) month in advance of the due date thereof;
- (e) There is no default that is material to the operation of the Facility by any Tenant under the terms of any of the Leases;
- (f) Lessor is not prohibited under any agreement with any other person or any judgment or decree from (i) the execution and delivery of either this Assignment or any of the Leases; (ii) the performance of each and every covenant of Lessor under either this Assignment or the Leases; or (iii) the meeting of each and every condition contained in this Assignment; and
- (g) No action has been brought or, so far as is known to Lessor, is threatened, which in any way would interfere with the right of Lessor to execute this Assignment and perform all of Lessors' obligations contained in this Assignment and in the Leases.

1.2 **Covenants of Lessor.** Each Lessor hereby covenants with Lender that:

- (a) Lessor will (i) fulfill, perform and observe each and every material condition and covenant of Lessor contained in any of the Leases in accordance with the provisions thereof; (ii) at no cost or expense to Lender, enforce the performance and observance of each and every material covenant and condition of each of the Leases to be performed or observed by the Tenant thereunder; and (iii) appear in and defend or settle any action growing out of, or in any matter connected with, any of the Leases or the obligations or liabilities of Lessor as the "landlord" or "lessor" thereunder or of the Tenant or any guarantor thereunder;
- (b) Except as permitted pursuant to the terms of the Loan Agreement, Lessor shall not, without the prior written consent of Lender, (i) enter into any Lease, except a resident lease in the ordinary course of business; (ii) modify or amend any of the Leases in any material respect without the prior written consent of Lender; (iii) terminate or accept the surrender of any of the Leases unless the Tenant thereunder shall have defaulted; (iv) waive or release any Tenant from the performance or observance of any material obligation or condition of its Lease; (v) further encumber the Lease or the collateral pledged for the Loan or (vi) permit to be made any prepayment of any installment of rent or fees under the Leases for more than one (1) months in advance (except for security deposits);
- (c) Lessor shall not execute any further assignment of the income, rents, issues or profits, or any part thereof, from the Premises or any further assignment of any of the Leases.

- (d) Lessor shall furnish to Lender, within ten (10) days after a request by Lender to do so, a sworn statement setting forth the name of all lessees and tenants of the Premises, the terms of their respective leases, tenant contracts or rental

agreements, the space occupied, and the rentals payable thereunder, and stating whether to each Lessor's knowledge any defaults, offsets or defenses exist under or in connection with any of said leases, tenant contracts or rental agreements.

(e) Lessor shall take no action which shall cause or permit the estate of the Tenant under any of the Leases to merge with the interest of Lessor in the Premises or any portion thereof;

(f) ACCEPTANCE OF THIS ASSIGNMENT SHALL NOT BE CONSTRUED AS A CONSENT BY LENDER TO ANY OF THE LEASES AND, SUBJECT TO THE TERMS OF THIS PARAGRAPH, LENDER SHALL NOT BE OBLIGATED TO PERFORM OR DISCHARGE ANY OBLIGATION OF LESSOR UNDER ANY OF THE LEASES, AND LESSORS AGREE TO, AND DO HEREBY INDEMNIFY AND HOLD LENDER HARMLESS AGAINST ANY AND ALL LIABILITIES, OBLIGATIONS, CLAIMS, DAMAGES, PENALTIES, COSTS AND EXPENSES (INCLUDING WITHOUT LIMITATION, ATTORNEY'S FEES AND EXPENSES ACTUALLY INCURRED) WHICH LENDER MAY INCUR UNDER ANY OF THE LEASES OR UNDER OR BY REASON OF THIS ASSIGNMENT, AND FROM ANY AND ALL CLAIMS AND DEMANDS WHATSOEVER WHICH MAY BE ASSERTED AGAINST LENDER BY REASON OF ANY ACT OR FAILURE TO ACT BY LENDER UNDER THIS ASSIGNMENT OR ANY ALLEGED OBLIGATION OR UNDERTAKING TO BE PERFORMED OR DISCHARGED BY LENDER UNDER THIS ASSIGNMENT UNLESS ANY SUCH CLAIM OR DEMAND IS CAUSED BY THE GROSS NEGLIGENCE OR INTENTIONAL MISCONDUCT OF LENDER. THE FOREGOING INDEMNITY SHALL NOT BE APPLICABLE TO ANY SUCH CLAIM, LIABILITY, LOSS, COST, EXPENSE OR DAMAGE WHICH RESULTS FROM ANY ACTION OF LENDER WHICH OCCURS SUBSEQUENT TO THE COMPLETION OF A FORECLOSURE OR ACCEPTANCE OF A DEED IN LIEU OF FORECLOSURE WITH RESPECT TO THE PREMISES OR DURING ANY PERIOD THAT A RECEIVER HAS BEEN APPOINTED AT THE REQUEST OF LENDER;

(g) Lessor shall authorize and direct, and does hereby authorize and direct each and every present and future Tenant of the whole or any part of the Premises to pay all rental to Lender upon receipt of written demand from Lender to so pay the same (which demand shall not be made until after an Event of Default);

(h) Upon request of Lender, Lessor shall deliver Lender certified copies of all Leases then in effect; and

(i) Upon request of Lender following an Event of Default, Lessor immediately shall deliver to Lender all security deposits and other deposits (whether refundable or non-refundable) paid by Tenants under the Leases; and Lender shall hold such deposits in a custodial account controlled by Lender, subject to the terms and conditions of the Leases.

1.3 **Covenants of Lender.** By acceptance of delivery of this Assignment, Lender covenants with Lessors that:

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(a) Although this Assignment constitutes a present and current assignment of all rents, issues and profits from the Premises, so long as there shall exist no Event of Default (as hereinafter defined) on the part of Lessors, Lessors shall have a license to collect, but not more than one (1) month prior to accrual, all such rents, issues and profits from the Premises (including, but not by way of limitation, all rental payments under any of the Leases) and to retain, use and enjoy such rents, issues and profits from the Premises for each Lessor's own account, such license to expire automatically and without further notice upon the occurrence of an Event of Default; and

(b) Upon the filing by Lender in the official records of Tulsa County, Oklahoma of a full satisfaction or release of the Mortgage without the recording of another security instrument in favor of Lender affecting the Premises, this Assignment shall likewise be canceled without the necessity of any further act by Lender.

## **ARTICLE II.**

2.1 **Event of Default.** The term “Event of Default,” wherever used in this Assignment, shall mean any one or more of the following events:

- (a) The occurrence of any default or Event of Default under the provisions of any of the Loan Documents;
- (b) Failure by the Lessors to duly observe any covenant, condition or agreement of this Assignment; or
- (c) The breach of any warranty by the Lessors contained in this Assignment, or if any representation or certification made or agreed to be made herein shall prove to be false or materially misleading.

2.2 **Remedies.** Upon the occurrence and continuance of any Event of Default, in addition to any and all other rights and remedies available to Lender under any of the Loan Documents, and not in substitution for or derogation thereof, Lender shall become immediately entitled to all rents, income, profits and proceeds arising from the Premises and may, without notice to or demand on the Lessors other than as may be otherwise provided herein, (i) as a matter of strict right and without regard to the value or occupancy of the security, have a receiver appointed to enter upon and take possession of the Premises, collect the rents and profits therefrom and apply the same as the court may direct, such receiver to have all the rights and powers permitted under the laws of the State of Oklahoma, all without becoming a mortgagee-in-possession; (ii) proceed itself to enter upon, take possession of and operate the Premises, or any portion thereof, without becoming a mortgagee-in-possession; (iii) give notice to Tenants that an event of default has occurred and instruct Tenants to pay all rents, issues, income, profits and proceeds directly to Lender to be applied to the extent actually received in accordance with the terms of the Loan Documents (in which event Lessors agree such giving of notice, receipt of rents, issues, income, profits and proceeds and application thereof shall be in accordance with the terms of the Loan Documents); (iv) proceed to perform any and all obligations of Lessors under any of the Leases and exercise any and all rights of Lessors therein contained as fully as the Lessors themselves could, all without regard to the adequacy of security for the indebtedness hereby secured and with or without the bringing of any legal action or the causing of any

receiver to be appointed by any court or other judicial authority; (v) make, enforce, modify and accept the surrender of any of the Leases; (vi) evict the Tenant under any of the Leases or obtain tenants for other space within the Premises; (vii) fix or modify rent; and (viii) do all of the acts which Lender may deem necessary, desirable or proper to protect the security created by this Assignment. Lessors hereby acknowledge and agree that the intent of this Assignment is to empower Lender to undertake any, all or any combination of the actions hereinabove set forth in this Paragraph 2.2 without notice to the Lessors except as specifically provided herein or, as to the Lessors, in the Loan Documents. If an Event of Default shall have occurred and be continuing, the Lessors do hereby specifically authorize Lender, in the name of the Lessors or in the name of Lender, to sue for or otherwise collect and receive all rents, issues and profits from the Premises, including those past due and unpaid, and to apply such collected rents, issues and profits to the payment of (w) all expenses of managing the Premises, including, without limitation, the salaries, fees and wages of a managing agent and such other employees as Lender may deem necessary or desirable, (x) all expenses of operating and maintaining the Premises, including, without limitation, all taxes, charges, claims, assessments, water rents, sewer rents, and any other liens, and premiums for all insurance which the Lender may deem necessary or desirable, (y) the cost of alterations, renovations, repairs, or replacements, and all expenses incident to taking and retaining possession of the Premises, and (z) the Indebtedness secured hereby, all in such order of priority as Lender in its sole discretion may determine. Entry upon and taking possession of the Premises and the collection of the rents, issues and profits of the Premises and the application thereof, as aforesaid, shall not operate to waive any default or event of default, or prohibit the taking of any action by Lender under this Assignment, the Note, the Loan Agreement, the Mortgage, or any other Loan Documents or at law or in equity to enforce payment of the Indebtedness secured hereby or to realize on any other security. No failure on the part of Lender to exercise, and no delay in exercising, any right shall be construed or deemed to be a waiver thereof. Any entry, payment or performance by Lender pursuant to the foregoing shall be in Lender’s reasonable discretion and Lender may commence, continue and/or discontinue any or all such actions at any time at Lender’s discretion

### ARTICLE III.

3.1 **Successors and Assigns.** This Assignment shall inure to the benefit of and be binding upon the Lessors and Lender and their respective heirs, executors, legal representatives, successors and assigns. Whenever a reference is made in this Assignment to "Lessor" or "Lender," such reference shall be deemed to include a reference to the heirs, executors, legal representatives, successors and assigns of each Lessor or Lender.

3.2 **Terminology.** All personal pronouns used in this Assignment, whether used in the masculine, feminine or neuter gender, shall include all other genders, and the singular shall include the plural, and vice versa. Titles of articles are for convenience only and neither limit nor amplify the provisions of this Assignment. All representations, warranties, covenants and other provisions applying to Lessors shall also apply to each of them.

3.3 **Severability.** If any provision of this Assignment or the application thereof to any person or circumstance shall be invalid or unenforceable to any extent, the remainder of this Assignment and the application of such provisions to other persons or circumstances shall not be affected thereby and shall be enforced to the greatest extent permitted by law.

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3.4 **Applicable Law.** Lessors and Lender hereby acknowledge and agree that this Assignment and the obligations created hereunder are made and intended as a contract under the laws of the State of Oklahoma and (i) are to be governed by and interpreted in accordance with the laws of the State of Oklahoma, and (ii) are to be construed and enforced in accordance with the laws of the State of Oklahoma.

3.5 **WAIVER OF TRIAL BY JURY. LESSORS AND LENDER (BY ACCEPTANCE HEREOF), HAVING BEEN REPRESENTED BY COUNSEL, EACH KNOWINGLY AND VOLUNTARILY WAIVES ANY RIGHT TO A TRIAL BY JURY IN ANY ACTION OR PROCEEDING TO ENFORCE OR DEFEND ANY RIGHTS (A) UNDER THIS ASSIGNMENT OR ANY RELATED AGREEMENT OR UNDER ANY AMENDMENT, INSTRUMENT, DOCUMENT OR AGREEMENT DELIVERED OR WHICH MAY IN THE FUTURE BE DELIVERED IN CONNECTION WITH THIS ASSIGNMENT OR (B) ARISING FROM ANY BANKING RELATIONSHIP EXISTING IN CONNECTION WITH THIS ASSIGNMENT, AND AGREE THAT ANY SUCH ACTION OR PROCEEDING WILL BE TRIED BEFORE A COURT AND NOT BEFORE A JURY. EACH LESSOR AGREES THAT IT WILL NOT ASSERT ANY CLAIM AGAINST LENDER OR ANY OTHER PERSON INDEMNIFIED UNDER THIS ASSIGNMENT ON ANY THEORY OF LIABILITY FOR SPECIAL, INDIRECT, CONSEQUENTIAL, INCIDENTAL OR PUNITIVE DAMAGES.**

3.6 **Security Deposits.** Each Lessor acknowledges that Lender has not received for its own account any security deposited by any tenant pursuant to the terms of the Leases and that Lender assumes no responsibility or liability for any security so deposited.

3.7 **No Third-Party Beneficiaries.** This Assignment is made solely for the benefit of Lender and its assigns. No Tenant under any of the Leases nor any other person shall have standing to bring any action against Lender as the result of this Assignment, or to assume that Lender will exercise any remedies provided herein, and no person other than Lender shall under any circumstances be deemed to be a beneficiary of any provision of this Assignment.

3.8 **No Oral Modifications.** Neither this Assignment nor any provisions hereof may be changed, waived, discharged or terminated orally, but only by an instrument in writing signed by the party against whom enforcement of the change, waiver, discharge or termination is sought.

3.9 **Cumulative Remedies.** The remedies herein provided shall be in addition and not in substitution for the rights and remedies vested in Lender in or by any of the Loan Documents or in law or equity, all of which rights and remedies are specifically reserved by Lender. The remedies herein provided or otherwise available to Lender shall be cumulative and may be exercised concurrently. The failure to exercise any of the remedies herein provided shall not constitute a waiver thereof, nor shall use of any of the remedies provided herein prevent the subsequent or concurrent resort to any other remedy or remedies. It is intended that this clause shall be broadly construed so that all remedies herein provided or otherwise available to Lender shall continue to be each and all available to Lender until the Indebtedness shall be paid in full.

3.10 **Further Assurance.** At any time and from time to time, upon request by Lender, the Lessors will make, execute and deliver, or cause to be made, executed and delivered, to

Lender and, where appropriate, cause to be recorded and/or refiled at such time and in such offices and places as shall be deemed desirable by Lender, any and all such other instruments as may, in the opinion of Lender, be necessary or desirable in order to effectuate, complete or perfect, or to continue and preserve (a) the obligations of such Lessors under this Assignment or (b) the interest created by this Assignment as a first and paramount interest in and to the Leases and the rents, issues and profits from the Premises.

3.11 **Notices.** Any and all notices, elections, demands, requests and responses thereto permitted or required to be given under this Assignment shall be in writing, signed by or on behalf of the party giving the same, and shall be deemed to have been properly given or served if (i) deposited in the United States Mail, postage prepaid, certified mail, return receipt requested, or (ii) delivered personally or by nationally recognized overnight courier to the other party at the address of such other party set forth below or at such other address as such other party may designate by notice specifically designated as a notice of change of address and given in accordance herewith. The time period in which a response to any such notice, election, demand or request must be given shall commence on the earlier of (x) the date of personal or overnight courier or facsimile delivery and (y) the third calendar day following the date of deposit of same in the United States Mail, postage prepaid, certified mail, return receipt requested. Personal delivery to a party or to any officer of such party at said address shall constitute receipt. Rejection or other refusal to accept or inability to deliver because of changed address of which no notice has been received shall also constitute receipt. Any such notice, demand, or request shall be addressed as follows:

If to Lessors:

c/o CSCC Property Holdings, LLC  
Two Buckhead Plaza  
3050 Peachtree Road NW, Suite 355  
Atlanta, Georgia 30305

with a copy to:

Ellen W. Smith, Esq.  
Holt Ney Zatcoff & Wasserman, LLP  
100 Galleria Parkway, Suite 1800  
Atlanta, Georgia 30339  
Fax: (770) 956-1490

If to Lender:

Eric Smith

Contemporary Healthcare Capital, LLC  
1040 Broad Street  
Suite 103  
Shrewsbury, New Jersey 07702

with a copy to:

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Law Offices of Thomas K. Slattery, P.L.L.C.  
1250 24<sup>th</sup> Street NW, Suite 300  
Washington, DC 20037

3.12 **No Obligations Imposed Upon Lender.** Subject to Paragraph 1.2(f) hereof, nothing contained herein shall operate or be construed to obligate Lender to perform any of the terms, covenants and conditions contained in any of the Leases or otherwise to impose any obligation upon Lender with respect to any of the Leases including, but not limited to, any obligation arising out of any covenant of quiet enjoyment therein contained in the event the tenant, lessee, occupant, or other party under any of such Leases shall have been joined as a party defendant in any action to foreclose and the estate of such tenant, lessee, occupant, or other party shall have been thereby terminated. Unless and until Lender actually enters into and takes possession of the Premises, this Assignment shall not operate to place upon Lender any responsibility for the operation, control, care, management or repair of the Premises, and the execution of this Assignment by Lessors shall constitute conclusive evidence that all responsibility for the operation, control, care, management and repair of the Premises is and shall be that of such Lessors prior to such actual entry and taking possession by Lender or by a receiver on behalf of Lender. In the event of any such entry into and taking possession of the Premises by Lender or by a receiver on behalf of Lender, Lender's or any receiver's, as the case may be, responsibility for the operation, control, care, management and repair of the Premises shall be strictly governed by the terms of the Loan Documents

3.13 **Attorney Fees.** Each Lessor agrees to reimburse Lender for all costs, expenses, and attorneys' fees that Lender incurs in connection with the enforcement of any obligation contained in this Assignment or the collection of any rents assigned herein, with or without litigation, including, without limitation, any costs, expenses, and fees incurred: (a) in making demands for and collecting any rents; (b) in any action for rents against Lessor or any lessee; (c) on appeal; (d) in any petition for review; (e) in any arbitration or mediation; (f) in any action contesting or seeking to restrain, enjoin, stay, or postpone the exercise of any remedy in which Lender prevails; (g) in any bankruptcy, probate, receivership or other proceeding involving Lessor; and (h) in connection with all negotiations, documentation, and other actions relating to any work-out, compromise, settlement or satisfaction relating to this Assignment. All such costs, expenses, and fees shall be due and payable upon demand and shall bear interest from the date incurred through the date of collection at the default rate stated in the Loan Documents.

3.14 **Inconsistencies.** To the extent the terms of the Loan Agreement and the terms of this Assignment are inconsistent, the terms of the Loan Agreement shall control

[SIGNATURES APPEAR ON FOLLOWING PAGE]

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IN WITNESS WHEREOF, Lessors have executed and delivered this Assignment by its duly authorized representatives as of the date and year first above written.

**LESSORS:**

**CSCC PROPERTY HOLDINGS, LLC**, a Georgia limited liability company

By: /s/ Christopher F. Brogdon

Name: Christopher F. Brogdon

Title: Manager

STATE OF )

[SEAL] ) ss.

COUNTY OF )

This instrument was acknowledged before me on August 17, 2012, by Christopher F. Brogdon, as Manager of CSCC Property Holdings, LLC, a Georgia limited liability company.

(Seal)

/s/ [Illegible]

Notary Public

My commission expires:

Commission #:

SIGNATURE PAGE TO ASSIGNMENT OF LEASES AND RENTS – ADCARE – SENIOR - CONTINUES

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**CSCC NURSING, LLC**, a Georgia limited liability company

By: /s/ Christopher F. Brogdon

Name: Christopher F. Brogdon

Title: Manager

STATE OF )

[SEAL] ) ss.

COUNTY OF )

This instrument was acknowledged before me on August 17, 2012, by Christopher F. Brogdon, as Manager of CSCC Nursing, LLC, a Georgia limited liability company.

(Seal)

/s/ [Illegible]

Notary Public

My commission expires:

Commission #:

SIGNATURE PAGE TO ASSIGNMENT OF LEASES AND RENTS – ADCARE - SENIOR





PREPARED BY, AND AFTER RECORDING RETURN TO:

Thomas K. Slattery, Esq.  
Law Offices of Thomas K. Slattery, P.L.L.C.  
1250 24th Street, N.W., Suite 300  
Washington, D.C. 20037

**MORTGAGE, ASSIGNMENT OF RENTS AND LEASES, SECURITY AGREEMENT AND FIXTURE FILING**

**MORTGAGOR:** CSCC PROPERTY HOLDINGS, LLC, a Georgia limited liability company, having an address of Two Buckhead Plaza, 3050 Peachtree Road NW, Suite 355, Atlanta, Georgia 30305

**LENDER:** CONTEMPORARY HEALTHCARE SENIOR LIEN FUND I, L.P., a Delaware limited partnership, having an address at 1040 Broad Street, Suite 103, Shrewsbury, New Jersey 07702

**A POWER OF SALE HAS BEEN GRANTED IN THIS MORTGAGE. A POWER OF SALE MAY ALLOW THE MORTGAGEE/LENDER TO TAKE THE MORTGAGED PROPERTY AND SELL IT WITHOUT GOING TO COURT IN A FORECLOSURE ACTION UPON DEFAULT BY THE MORTGAGOR/BORROWER UNDER THIS MORTGAGE.**

**MORTGAGE, ASSIGNMENT OF RENTS AND LEASES, SECURITY AGREEMENT AND FIXTURE FILING**

**THIS MORTGAGE, ASSIGNMENT OF RENTS AND LEASES, SECURITY AGREEMENT AND FIXTURE FILING** (this "Mortgage"), made and entered into as of the 17 day of August, 2012, by CSCC PROPERTY HOLDINGS, LLC, a Georgia limited liability company, whose address is Two Buckhead Plaza, 3050 Peachtree Road NW, Suite 355, Atlanta, Georgia 30305 and whose organization number is 12034119, (the "Mortgagor") in favor of CONTEMPORARY HEALTHCARE SENIOR LIEN FUND I, L.P., a Delaware limited partnership, having an office in Shrewsbury, New Jersey, whose address is 1040 Broad Street, Suite 103, Shrewsbury, New Jersey 07702, Attention: Mr. Eric Smith (the "Lender"; said term referring always to the lawful owner and holder of the indebtedness secured hereby).

**WITNESSETH:**

For and in consideration of the Loan, described herein, and other valuable considerations, the receipt and sufficiency whereof are hereby acknowledged, and in order to secure the indebtedness and other obligations of Borrower hereinafter set forth, Mortgagor does hereby GRANT, BARGAIN, SELL, MORTGAGES AND CONVEY TO LENDER, WITH POWER OF SALE, all of the following described land and interests in land, estates, easements, rights, improvements, fixtures, appurtenances, and other property whether now owned or hereafter acquired and including replacements and additions thereto (hereinafter referred to collectively as the "Collateral"):

**THIS MORTGAGE SECURES ADVANCES TO BE USED FOR COMMERCIAL PURPOSES.**

**THIS INSTRUMENT SHALL ALSO CONSTITUTE A UNIFORM COMMERCIAL CODE FINANCING STATEMENT WHICH IS BEING FILED AS A FIXTURE FILING IN ACCORDANCE WITH THE OKLAHOMA UNIFORM COMMERCIAL CODE. THE RECORD OWNER OF THE REAL ESTATE DESCRIBED HEREIN IS THE MORTGAGOR.**

**THE COLLATERAL IS DESCRIBED IN THIS INSTRUMENT AND SOME OF THE COLLATERAL DESCRIBED HEREIN IS OR IS TO BECOME FIXTURES ON THE REAL ESTATE DESCRIBED HEREIN.**

(a) The tract(s) or parcel(s) of land located in Tulsa County, Oklahoma as are more particularly described in Exhibit A attached hereto and by this reference made a part hereof (referred to individually and collectively as (the "Property"));

(b) All Improvements and Equipment, all of which are hereby declared and shall be deemed to be fixtures and accessions to the Property and a part of the Property as between the parties hereto and all persons claiming by, through or under them, and which shall be deemed to be a portion of the security for the Loan Obligations herein described to be secured by this Mortgage;

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(c) All building materials, equipment, fixtures, fittings, and personal property of every kind or character now owned or hereafter acquired by Mortgagor for the purpose of being used or useful in connection with the Improvements, whether such materials, equipment, fixtures, fittings, and personal property are actually located on or adjacent to the Property or not, and whether in storage or otherwise, wheresoever the same may be located, including, but without limitation, all lumber and lumber products, bricks, building stones, and building blocks, sand and cement, roofing material, paint, doors, windows, hardware, nails, wires and wiring, plumbing and plumbing fixtures, heating and air conditioning equipment and appliances, electrical and gas equipment and appliances, pipes and piping, ornamental and decorative fixtures, furniture, and in general all building materials and equipment of every kind and character used or useful in connection with said Improvements;

(d) All Appurtenant Rights;

(e) All Rents;

(f) All Accounts, General Intangibles, Instruments, Inventory, Money, and (to the full extent assignable) Permits; and

(g) All Proceeds.

Mortgagor further grants to Lender a security interest in all of the Collateral constituting goods that are or are to become fixtures related to the Property.

This Mortgage, and all rights, remedies, powers, privileges, and benefits and all titles, interests, liens, and security interests created hereby or arising by virtue hereof, are given to secure payment and performance of the following indebtedness, obligations, loans, advances, and liabilities:

(a) To secure the loan (the "Loan"), including future advances, evidenced by or arising under that certain Promissory Note of even date herewith as the same may hereafter be renewed, extended, amended and modified (together with all renewals, extensions, amendments, and modifications thereof hereafter made, collectively, the "Note"), executed by Mortgagor and CSCC Nursing, LLC, a Georgia limited liability company (also collectively referred to herein as the "Borrowers"), which Note is payable to the order of Lender in the stated principal amount of up to FIVE MILLION AND NO/100 DOLLARS (\$5,000,000.00), bearing interest and being payable in installments as therein stated, which is due and payable in full on August 20, 2015;

(b) To secure all sums advanced by Lender to Borrowers or expended by Lender for Borrowers' account, including but not limited to advances for taxes and insurance, or for Borrowers' benefit pursuant to the terms of this Mortgage and the faithful performance by Mortgagor of all terms and conditions contained herein;

(c) To secure the payment of all court costs, expenses and costs of whatever kind incident to the collection of any indebtedness secured hereby and the enforcement or protection

of the lien of this conveyance and the enforcement of one or more of the Loan Documents, including reasonable attorneys' fees, whether at trial, on appeal or review or other proceedings, or in any bankruptcy case or proceedings and including issues particular to bankruptcy; and

(d) To secure all fees (including exit fees), premiums (including prepayment premiums), charges, expenses and other amounts from time to time due to Lender pursuant to the Loan Documents and all other Loan Obligations.

Should the Loan Obligations be paid according to the tenor and effect thereof when the same shall become due and payable, then this Mortgage shall be canceled and released.

AND the Mortgagor covenants with the Lender and represents and warrants unto Lender as follows:

#### **ARTICLE I DEFINITIONS**

The following terms will have the following meanings:

**"Accounts"** means any rights of Mortgagor arising from the operation of the Facility to payment for goods sold or leased or for services rendered, not evidenced by an Instrument, including, without limitation, (a) all accounts arising from the operation of the Facility, (b) all moneys and accounts held by Lender pursuant to any Debt Service Coverage Requirements of the Loan Agreement, and (c) all rights to payment from Medicare or Medicaid programs, or similar state or federal programs, boards, bureaus or agencies and rights to payment from patients, residents, private insurers, and others arising from the operation of the Facility, including rights to payment pursuant to Reimbursement Contracts. Accounts shall include the proceeds thereof (whether cash or noncash, moveable or immoveable, tangible or intangible) received from the sale, exchange, transfer, collection or other disposition or substitution thereof.

**"Applicable Environmental Law"** shall mean any applicable laws, rules or regulations pertaining to health or the environment or petroleum products or radon radiation, or oil or hazardous substances, including, without limitation, the Comprehensive Environmental Response, Compensation and Liability Act of 1980, as amended ("CERCLA"), as codified at 42 U.S.C. § 9601 *et seq.*, as amended, the Resource Conservation and Recovery Act of 1976, as amended ("RCRA") and the Federal Emergency Planning and Community Right-To-Know Act of 1986. The terms "hazardous substance" and "release" shall have the meanings specified in CERCLA, and the terms "solid waste," "disposal," "dispose," and "disposed" shall have the meanings specified in RCRA, except that if such acts are amended to broaden the meanings thereof, the broader meaning shall apply herein prospectively from and after the date of such amendments); notwithstanding the foregoing, provided, to the extent that the laws of the State where the Property is located establish a meaning for "hazardous substance" or "release" which is broader than that specified in CERCLA, as CERCLA may be amended from time to time, or a meaning for "solid waste," "disposal," and "disposed" which is broader than specified in RCRA,

as RCRA may be amended from time to time, such broader meanings under said state law shall apply in all matters relating to the laws of such State.

“**Appurtenant Rights**” means all easements, rights-of-way, strips and gores of land, vaults, streets, ways, alleys, passages, sewer rights, waters, water courses, water rights and powers, minerals, flowers, shrubs, crops, trees, timber and other emblements now or hereafter appurtenant to, or used or useful in connection with, or located on, under or above the Property, or any part or parcel thereof, and all ground leases, estates, rights, titles, interests, privileges, liberties, tenements, hereditaments and appurtenances, reversions, and remainders whatsoever, in any way belonging, relating or appertaining to the Property or any other Collateral, or any part thereof.

“**Bankruptcy Default**” means an Event of Default pursuant to Section 6.1(e) or 6.1(f) of the Loan Agreement.

“**Equipment**” means all of Mortgagor’s fixtures and equipment located on, attached to or used or useful in connection with the Property or Facility, including, but not limited to, all beds, linen, televisions, carpeting, telephones, cash registers, computers, lamps, glassware, rehabilitation equipment, and restaurant and kitchen equipment; provided, however, that with respect to any items which are leased and not owned, the Equipment shall include the leasehold interest only together with any options to purchase any of said items and any additional or greater rights with respect to such items which are hereafter acquired.

“**Facility**” means the skilled nursing facility now or hereafter located at the Property.

“**General Intangibles**” means all of Mortgagor’s general intangibles and other intangible personal property arising out of or connected with the Property or the Improvements (other than Accounts, Rents, Instruments, Inventory, Money, Permits and Reimbursement Contracts), including, without limitation, things in action, contract rights and other rights to payment of money.

“**Improvements**” means all buildings, structures and improvements of every nature whatsoever now or hereafter situated on the Property, including, but not limited to, all gas and electric fixtures, radiators, heaters, engines and machinery, boilers, ranges, elevators and motors, plumbing and heating fixtures, air conditioning equipment, carpeting and other floor coverings, water heaters, awnings and storm sashes, cleaning apparatus, signs, landscaping and parking areas, which are or shall be attached to the Property or said buildings, structures or improvements.

“**Instruments**” means all of Mortgagor’s instruments, chattel paper, documents or other writings obtained from or in connection with the operation of the Property or the construction and operation of the Facility (including, without limitation, all ledger sheets, computer records and printouts, data bases, programs, books of account, trademarks or trade names, utility contracts, maintenance and service contracts, and files relating thereto).

“**Inventory**” means all of Mortgagor’s inventory from time to time used at the Facility, including, but not limited to, food, beverages, other comestibles, soap, paper supplies, medical supplies, drugs and all other such goods, wares and merchandise held by Mortgagor for sale to or for consumption or use by guests or residents of the Property or the Facility, including all such goods that are returned to or repossessed by Mortgagor.

“**Loan Agreement**” means the certain Loan Agreement dated the same date herewith between the Borrowers and Lender.

“**Loan Documents**” means, collectively, the Loan Agreement, the Note, this Mortgage and all other Loan Documents, each as defined in the Loan Agreement, together with any and all other documents executed by Mortgagor or others, evidencing, securing, or otherwise relating to the Loan.

“**Loan Obligations**” means the aggregate of all principal and interest owing from time to time under the Note, and all expenses, fees, premiums, charges, and other amounts from time to time owing under the Note, the Loan Agreement, this Mortgage or

any other Loan Documents and all covenants, agreements and other obligations from time to time owing to, or for the benefit of, Lender pursuant to the Loan Documents.

“**Money**” means all of Mortgagor’ s monies, cash, rights to deposit or savings accounts or other items of legal tender obtained from or for use in connection with the operation of the Facility.

“**Note**” has the meaning heretofore set forth in this Mortgage.

“**Permits**” means all licenses, permits and certificates, obtained by Mortgagor from any governmental or quasi-governmental authority, or from any private person or entity, and used or useful in connection with the ownership, operation, use or occupancy of the Property or the Facility, including, without limitation, business licenses, state health department licenses, food service licenses, licenses to conduct business, certificates of need and all such other permits, licenses and rights.

“**Permitted Encumbrances**” means all matters set forth in Exhibit B attached hereto and made a part hereof, provided that to the extent any of the same are listed as subordinate, such matters are permitted only so long as they are in fact subordinate to this Mortgage.

“**Proceeds**” means all awards, payments, earnings, royalties, issues, profits, liquidated claims and proceeds (including proceeds of insurance and condemnation or any conveyance in lieu thereof), from the sale, conversion (whether voluntary or involuntary), exchange, transfer, collection, loss, damage, condemnation, disposition, substitution or replacement of any of the Collateral.

“**Reimbursement Contracts**” shall mean all of Mortgagor’ s contracts and rights pursuant to reimbursement or third party payor programs and contracts for the Facility which are

now or hereafter in effect with respect to residents qualifying for coverage under the same, including, but not limited to, Medicare, Medicaid, any successor program or other similar reimbursement program (whether operated by a governmental or quasi-governmental agency or by a private Person) and private insurance agreements.

“**Rents**” means all rent and other payments of whatever nature from time to time payable to Mortgagor pursuant to any lease of the Property or the Facility or any part thereof, including, but not limited to, leases of individual units to residents and leases of retail space or other space at the Property for businesses such as newsstands, barbershops, beauty shops, physicians’ offices, pharmacies and specialty shops.

Singular terms shall include the plural forms and vice versa, as applicable of the terms defined.

All references to other documents or instruments shall be deemed to refer to such documents or instruments as they may hereafter be extended, renewed, modified or amended, and all replacements and substitutions therefor.

All other capitalized terms not otherwise defined in this Mortgage shall have the meanings set forth in the Loan Agreement.

## ARTICLE II MORTGAGOR’ S COVENANTS, AGREEMENTS, AND REPRESENTATIONS

Section 2.1      **Performance of Loan Documents.** The Mortgagor will perform, observe and comply with the provisions hereof and of each of the other Loan Documents when due or within any applicable cure period and duly and punctually will pay to the

Lender when due or within any applicable cure period the sum of money expressed in the Note with interest thereon and all other sums required to be paid by the Mortgagor pursuant to the provisions of this Mortgage, all without any deduction or credit for taxes or other similar charges paid by the Mortgagor.

Section 2.2      **Warranty of Title.** The Mortgagor is lawfully seized of an estate in fee simple in the Property, Improvements, and Appurtenant Rights hereby mortgaged and has good and absolute title to all other Collateral in which a security interest is herein granted, and Mortgagor has good right, full power and lawful authority to sell, convey, mortgage, and grant a security interest in the same in the manner and form aforesaid subject to any limitations which may be imposed under applicable law on the granting of a security interest in or assignment of certain of the Collateral, such as Medicare and Medicaid Accounts and Permits; that, except for Permitted Encumbrances and the Liens permitted by the Loan Agreement, the same are free and clear of all liens, charges, and encumbrances whatsoever, including, as to the Equipment (subject to the terms and conditions of the leases existing as of the Closing Date for certain copy machines), conditional sales contracts, chattel mortgages, security agreements, financing statements, and anything of a similar nature, and that Mortgagor shall and will warrant and

forever defend the title thereto unto the Lender and Lender, their successors and assigns, against the lawful claims of all persons whomsoever.

Section 2.3      **Taxes, Liens and Other Charges.**

(a)                      Subject to Mortgagor' s right to duly contest the same in accordance with this Section 2.3(a), Mortgagor shall pay, on or before the due date thereof, all taxes, levies, license fees, permit fees and all other charges (in each case whether general or special, ordinary or extraordinary, or foreseen or unforeseen) of every character whatsoever (including all penalties and interest thereon) now or hereafter levied, assessed, confirmed or imposed on, or in respect of, or which may be a lien upon the Collateral, or any part thereof, or any estate, right or interest therein, or upon the rents, issues, income or profits thereof, and shall submit to Lender such evidence of the due and punctual payment of all such taxes, assessments and other fees and charges as may be required by law. Mortgagor shall have the right before they become past due to contest or object to the amount or validity of any such tax, assessment, fee or charge by appropriate legal proceedings, but this shall not be deemed or construed in any way as relieving, modifying or extending Mortgagor' s covenant to pay any such tax, assessment, fee or charge at the time and in the manner provided herein, unless Mortgagor has given prior written notice to Lender of Mortgagor' s intent to so contest or object, and unless (i) Mortgagor shall demonstrate to Lender' s reasonable satisfaction that the legal proceedings shall conclusively operate to prevent the sale of the Collateral, or any part thereof, to satisfy such tax, assessment, fee or charge prior to final determination of such proceedings; and (ii) if required by Lender, Mortgagor shall furnish a good and sufficient bond or surety as requested by and satisfactory to Lender in an amount sufficient to fully pay the contested amount, with penalties, interest and other charges if Mortgagor should be unsuccessful in such contest; and (iii) Mortgagor shall diligently pursue such contest. Mortgagor' s right to reimbursement from any amounts paid to Lender in escrow for taxes shall be subject to the terms and conditions of the Tax and Insurance Escrow and Security Agreement with Lender of even date herewith, if such agreement is in effect.

(b)                      Mortgagor shall pay, on or before the due date thereof, all taxes, assessments, charges, expenses, costs and fees which may now or hereafter be levied upon, or assessed or charged against, or incurred in connection with, the Note, this Mortgage or any other Loan Documents; provided, however, nothing herein shall be construed as requiring Mortgagor to pay any of Lender' s income or gross receipts taxes.

(c)                      Mortgagor shall pay, on or before the due date thereof, all premiums on policies of insurance covering, affecting or relating to the Collateral, as required by the Loan Agreement; all ground lease rents and other payments; and all utility charges with respect to the Collateral, or which may become a charge or lien against the Collateral, for gas, electricity, water and

sewer services and the like furnished to the Collateral, and all other public or private assessments or charges of a similar nature affecting the Collateral or any portion thereof, whether or not the nonpayment of same may result in a lien thereon. Mortgagor shall

submit to Lender such evidence of the due and punctual payment of all such premiums, rentals and other sums as Lender may reasonably require.

(d) Mortgagor shall not suffer any construction, mechanic' s, materialman' s, laborer' s, statutory or other lien (except as expressly permitted by the Loan Agreement) to be created or remain outstanding against the Collateral; provided, however, that Mortgagor may contest any such lien in good faith by appropriate legal proceedings provided the lien is bonded off and removed as an encumbrance upon the Collateral. Lender has not consented and will not consent to the performance of any work or the furnishing of any materials which might be deemed to create a lien or liens superior to the lien hereof.

(e) In the event of the passage of any state, federal, municipal or other governmental law, order, rule or regulation, subsequent to the date hereof, in any manner changing or modifying the laws now in force governing the taxation of mortgages or security agreements or debts secured thereby or the manner of collecting such taxes so as to adversely affect Lender, Mortgagor will pay any such tax on or before the due date thereof. If Mortgagor fails to make such prompt payment or if, in the opinion of Lender, any such state, federal, municipal, or other governmental law, order, rule or regulation prohibits Mortgagor from making such payment or would penalize Lender if Mortgagor makes such payment or if, in the opinion of Lender, the making of such payment might result in the imposition of interest beyond the maximum amount permitted by applicable law, then the entire balance of the Loan Obligations shall, at the option of Lender, become immediately due and payable.

(f) The Mortgagor hereby indemnifies, agrees to reimburse Lender and holds Lender harmless for, from and against any sales or use tax that may be imposed on the Lender by virtue of Lender' s Loan to Borrowers; provided, however, nothing herein shall be construed as requiring Mortgagor to pay any of Lender' s income or gross receipts taxes.

Section 2.4 **Monthly Deposits.** Mortgagor shall, as required by the Loan Documents, deposit with Lender, on the due date of each installment under the Note, an amount equal to one-twelfth (1/12) of the yearly taxes and assessments and insurance premiums with respect to the Collateral as estimated by the Lender to be sufficient to pay such charges all in accordance with the Tax and Insurance Escrow and Security Agreement with Lender of even date herewith; said deposits to be held and to be used by Lender to pay current taxes and assessments, insurance premiums and other charges on the Collateral as the same accrue and are payable. Payment from said sums for said purposes shall be made by Lender at its discretion and may be made even though such payments will benefit subsequent owners of the Collateral. Said deposits shall not be, nor be deemed to be, trust funds, but may be, to the extent permitted by applicable law, commingled with the general funds of Lender without payment of interest. If said deposits are insufficient to pay the taxes and assessments, insurance premiums and other charges in full as the same become payable, Mortgagor will deposit with Lender such additional sum or sums as may be required in order for Lender to pay such taxes and assessments, insurance premiums and other charges in full. Upon any Event of Default, Lender may, at its option, apply any money in the

fund relating from said deposits to the payment of the Loan Obligations in such manner as it may elect.

Section 2.5 **Condemnation.**

(a) If all or any part of the Collateral shall be damaged or taken through condemnation (which term when used in this Mortgage shall include any damage or taking by any governmental authority, and any transfer by private sale in lieu



thereof), either temporarily or permanently, other than a taking of a part of the Collateral which does not in Lender's reasonable opinion adversely affect access to or use of the Collateral or operation of the Facility, the entire Loan Obligations secured hereby shall at the option of the Lender become due and payable in accordance with Article IV of the Loan Agreement.

(b) Mortgagor, immediately upon obtaining knowledge of any institution, or any proposed, contemplated or threatened institution of any action or proceeding for the taking through condemnation of the Collateral or any part thereof, will notify Lender, and Lender is hereby authorized, at its option, to commence, appear in and prosecute, through counsel selected by Lender, in its own or in Mortgagor's name, any action or proceeding relating to any condemnation. Mortgagor may compromise or settle any claim for compensation so long as no Event of Default exists and any compromise or settlement results in a payment to Lender not less than the amount that would permit Mortgagor to obtain a release of the Property and Improvements pursuant to the Loan Agreement. If an Event of Default exists, Lender shall have the sole and exclusive right to compromise or settle any claim for compensation. All such compensation, awards, damages, claims, rights of action and proceeds and the right thereto are hereby assigned by Mortgagor to Lender, and Lender is authorized, at its option, to collect and receive all such compensation, awards or damages and to give proper receipts and acquittances therefor without any obligation to question the amount of any such compensation, awards or damages. After deducting from said condemnation proceeds all of its expenses incurred in the collection and administration of such sums, including reasonable attorney's fees, Lender may release any moneys so received by it for the repair or restoration of the Collateral taken, or may apply the same in such manner as the Lender shall reasonably determine to reduce the Loan Obligations in such order as Lender may elect, whether or not then due, and without affecting this Mortgage as security for any remaining Loan Obligations, and any balance of such moneys shall be paid to the Mortgagor.

Section 2.6 **Care of Collateral.**

(a) Mortgagor will keep the Improvements in good condition and repair ordinary wear and tear excepted, will not commit or suffer any waste and will not do or suffer to be done anything which would reasonably be expected to increase the risk of fire or other hazard to the Collateral or any other part thereof or which would or could result in the cancellation of any insurance policy carried with respect to the Collateral.

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(b) Except in connection with the repair or replacement of the Facility after damage thereto or destruction or condemnation thereof, Mortgagor will not remove, demolish or alter the structural character of any Improvements in any material respect without the written consent of Lender, which such consent shall not be unreasonably withheld, nor will Mortgagor make or permit use of the Collateral for any purpose other than that for which the same are now used.

(c) Mortgagor will maintain the insurance relating to Mortgagor or the Collateral as required by the Loan Agreement. If the Collateral or any part thereof is damaged by fire or any other cause, Mortgagor will give immediate written notice thereof to Lender.

(d) Lender or its representative is hereby authorized to enter upon and inspect the Collateral during normal business hours upon reasonable advance notice to Mortgagor.

(e) Mortgagor will promptly comply with all present and future laws, ordinances, rules and regulations of any governmental authority affecting the Collateral or any part thereof; provided, however, Mortgagor shall have the right to contest the application of such laws, ordinances, rules and regulations to Mortgagor provided such contest does not impair the validity of Lender's lien on the Collateral or present a risk of forfeiture of the Collateral.

(f) If all or any part of the Collateral shall be damaged by fire or other casualty, Mortgagor will promptly restore the Collateral to the equivalent of its original condition in accordance with Section 4.5 of the Loan Agreement (or, if

Mortgagor chooses not to rebuild the Facility or is unable to satisfy the conditions of Section 4.5 of the Loan Agreement, Mortgagor shall pay to Lender in full an amount sufficient to obtain a release of the Property and Improvements pursuant to the Loan Agreement); and if a part of the Collateral shall be taken or damaged through condemnation, Mortgagor will promptly restore, repair or alter the remaining portions of the Collateral in a manner satisfactory to Lender.

Section 2.7 **Further Assurances: After-Acquired Property.** At any time, and from time to time, upon request by Lender, Mortgagor will make, execute and deliver or cause to be made, executed and delivered to Lender and, where appropriate, cause to be recorded and/or filed and from time to time thereafter to be rerecorded and/or refiled at such time and in such offices and places as shall be requested by Lender such certificates, documents, statements, amendments and other instruments and/or filings (i) to perfect and protect the security interest created or purported to be created hereby; (ii) to enable the Lender to exercise and enforce its rights and remedies hereunder in respect of the Collateral; or (iii) to effect otherwise the purposes of this Mortgage, including, without limitation: (A) executing and filing such financing or continuation statements, or amendments thereto, as may be necessary or desirable or that the Lender may request in order to perfect and preserve the security interest created by this Mortgage as a first and prior security interest upon and security title in and to all of the Collateral, whether now owned or hereafter acquired by Mortgagor; provided, however, Mortgagor authorizes Lender to file any financing statements describing the Collateral in such

jurisdictions and filing offices as Lender deems appropriate without the necessity of Mortgagor's signature; (B) if certificates of title are now or hereafter issued or outstanding with respect to any of the Collateral, by immediately causing the interest of Lender to be properly noted thereon at Mortgagor's expense; and (C) furnishing to the Lender from time to time statements and schedules further identifying and describing the Collateral and such other reports in connection with the Collateral as the Lender may reasonably request, all in reasonable detail. Upon any failure by Mortgagor so to do, Lender may make, execute, record, file, re-record and/or refile any and all such financing statements, continuation statements, or amendments thereto, certificates, and documents for and in the name of Mortgagor, and Mortgagor hereby irrevocably appoints Lender the agent and attorney-in-fact of Mortgagor so to do. The lien of this Mortgage will automatically attach, without further act, to all after-acquired property attached to and/or used in the operation of the Collateral or any part thereof.

Section 2.8 **Indemnity; Expenses.** Mortgagor will pay or reimburse Lender for all reasonable attorney's fees, costs and expenses incurred by Lender in any suit, action, trial, appeal, review, bankruptcy (including issues particular to bankruptcy) or other legal proceeding or dispute of any kind in which Lender is made a party or appears as party plaintiff or defendant, affecting the Loan Obligations, this Mortgage or the interest created herein, or the Collateral, or any appeal thereof, including, but not limited to, any foreclosure action, any condemnation action involving the Collateral or any action to protect the security hereof, any bankruptcy or other insolvency proceeding commenced by or against the Mortgagor, any lessee of the Collateral (or any part thereof), or any guarantor of any of the Loan Obligations, and including, without limitation, reasonable costs of title searches, appraisals, environmental reports and expert witness fees, and any such amounts paid by Lender shall be added to the Loan Obligations and shall be secured by this Mortgage. Mortgagor will indemnify, reimburse and hold Lender harmless for, from and against all claims, actions, losses, damages, costs, expenses, including reasonable attorney's fees and court costs, and other liabilities of every description related to or resulting from any action by a third party against Lender relating to this Mortgage or any interest created herein, or the Collateral, including, but not limited to, any action or proceeding claiming loss, damage or injury to person or property, or any action or proceeding claiming a violation of any national, state or local law, rule or regulation, including those Applicable Environmental Laws, including such matters to the extent caused in whole or part by Lender's or its agent's conduct or negligence; provided Mortgagor shall not be required to indemnify Lender for matters directly and solely caused by Lender's willful misconduct or gross negligence.

Section 2.9 **Assignment of Rents.** All Rents are hereby assigned to Lender to be applied against the Loan Obligations secured by this Mortgage in such order as Lender may elect; provided, however, that a revocable license is hereby given to Mortgagor (subject to the requirement that Lender approve any lease other than leases with residents of the Improvements), unless and until the breach of any covenant or condition of this Mortgage which is not cured within any applicable cure period or the occurrence of any

Event of Default, to collect and use such Rents as they become due and payable, but not in advance thereof. This Mortgage constitutes an absolute and present assignment of the Rents, subject, however, to the conditional and revocable license given to Mortgagor to collect and use the same as provided hereinabove.

The foregoing assignment shall be fully operative without any further action on the part of either party, and specifically, Lender shall be entitled, at its option upon the breach of any covenant or condition of this Mortgage which is not cured within any applicable cure period or the occurrence of any Event of Default hereunder, to collect all such Rents whether or not Lender takes possession of the Property. Exercise by Lender of its rights under this Section, and the application of any such Rents to such Loan Obligations shall not cure or waive any Event of Default or notice of Event of Default hereunder or invalidate any act done pursuant hereto or any such notice, but shall be cumulative of all other rights and remedies. Mortgagor shall not, without the prior written consent of Lender, further assign the Rents that are assigned to Lender herein, and any such assignment without the express written consent of Lender shall be void as against Lender (except that assignment of Accounts shall be permitted to the extent provided in the Loan Agreement).

Section 2.10 **Estoppel Affidavits.** Mortgagor, upon ten (10) days prior written notice from Lender, shall furnish Lender a written statement, duly acknowledged, based upon its records, setting forth the unpaid principal of, and interest on, the Loan Obligations, stating whether or not to its knowledge any offsets or defenses exist against the Loan Obligations, or any portion thereof, and, if such offsets or defenses exist, stating in detail the specific facts relating to each such offset or defense.

Section 2.11 **Leases.** Mortgagor shall not, without the prior written consent and approval of Lender, enter into any lease or permit any tenancy (except for the Lease and those other leases permitted by the terms of the Loan Agreement, including, but not limited to, tenancy or residency agreements with patients or residents of individual units at the Facility), or enter into or permit any management agreement, of or affecting the Collateral, except as expressly permitted in the Loan Agreement.

Section 2.12 **Limit of Validity.** If from any circumstances whatsoever, fulfillment of any provision of this Mortgage, the Note or any other Loan Document, at the time performance of such provision shall be due, shall involve transcending the limit of validity presently prescribed by any applicable usury statute or any other applicable law, with regard to obligations of like character and amount, then, *ipso facto*, the obligation to be fulfilled shall be reduced to the limit of such validity, so that in no event shall any exaction be possible under this Mortgage, the Note, or any other Loan Document that is in excess of the current limit of such validity, but such obligation shall be fulfilled to the limit of such validity. The provisions of this Section shall control every other provision of this Mortgage, the Note and any other Loan Document.

Section 2.13 **Compliance with Other Deeds of Trust.** To the extent there at any time exists any other deed of trust, mortgage or security agreement encumbering all or any part of the Collateral (“Other Mortgage Debt”) (a) the same is expressly permitted so long as, but only if, it is shown as a “Permitted Encumbrance” on Exhibit B hereto or is otherwise expressly permitted by the Loan Agreement, and (b) Mortgagor will perform, observe and comply with the same and with all related documents and instruments when due or within any applicable cure period and will maintain the same free from default and not obtain additional advances or increase the

principal amount secured thereby without Lender’s prior written consent. If a default thereunder should occur or an Event of Default exists, Lender shall have the right, but not the obligation, to cure the same or to advance such additional amounts as are necessary to protect the Lender’s interest in the Collateral, including, without limitation, payment in full of all debts and other obligations if and to the extent Lender deems necessary to prevent foreclosure or sale of all or any part of the Collateral or purchase such Other Mortgage Debt. All amounts so advanced by Lender shall constitute Loan Obligations and shall bear interest at the Default Rate from the date

advanced until repaid in full, such advance and interest shall be secured by this Mortgage, and such advance and interest shall be immediately due and payable.

### ARTICLE III EVENTS OF DEFAULT; REMEDIES

Section 3.1     **Events of Default.** The terms “Event of Default” or “Events of Default,” wherever used in this Mortgage, shall mean any one or more of the following events:

- (a)             The occurrence of any Event of Default (as therein defined) under any other Loan Documents; or
- (b)             The sale, transfer, lease, assignment, or other disposition, voluntarily or involuntarily, of the Collateral, or any part thereof or any interest therein, including a sale or transfer in lieu of condemnation, or, except for Permitted Encumbrances, any further encumbrance of the Collateral, unless expressly permitted or required by the Loan Agreement or unless the prior written consent of Lender is obtained (which consent may be withheld, conditioned or granted with or without cause in Lender’s sole and unfettered discretion) or unless such disposition is of any of the Equipment or Inventory which has become worn out or obsolete provided the same is replaced with property of similar value and of a similar quality if and to the extent such worn out or obsolete Equipment is required for the continued lawful operation of the Facility.

Section 3.2     **Acceleration of Maturity.** If an Event of Default shall exist, then the entire Loan Obligations shall, at the option of Lender, immediately become due and payable without notice or demand, time being of the essence of this Mortgage, and no omission on the part of Lender to exercise such option when entitled to do so shall be construed as a waiver of such right; provided, however, if a Bankruptcy Default occurs, then all such amounts shall become immediately due and payable automatically without any election by the Lender.

Section 3.3     **Right to Enter and Take Possession.**

- (a)             If an Event of Default shall have occurred and be continuing, Mortgagor, upon demand of Lender, shall forthwith surrender to Lender the actual possession of the Collateral and, if and to the extent permitted by law, Lender itself, or by such officers or agents as it may appoint, may enter and take possession of all or any part of the Collateral without the appointment of a receiver or an application therefor, and may exclude Mortgagor and

its agents and employees wholly therefrom, and take possession of the books, papers and accounts of Mortgagor to the extent permitted by applicable law.

- (b)             If Mortgagor shall for any reason fail to surrender or deliver the Collateral or any part thereof after such demand by Lender, Lender may obtain a judgment or decree conferring upon Lender the right to immediate possession or requiring Mortgagor to deliver immediate possession of the Collateral to Lender. Mortgagor will pay to Lender, upon demand, all reasonable expenses of obtaining such judgment or decree, including compensation to Lender, its attorneys and agents, and all such expenses and compensation shall, until paid, become part of the Loan Obligations and shall be secured by this Mortgage.

- (c)             Upon every such entering upon or taking of possession, Lender may hold, store, use, operate, manage and control the Collateral and conduct the business thereof, and, from time to time (i) make all necessary and proper maintenance, repairs, renewals, replacements, additions, betterments and improvements thereto and thereon and purchase or otherwise acquire additional fixtures, personalty and other property; (ii) insure or keep the Collateral insured; (iii) manage and operate the Collateral and exercise all of the rights and powers of Mortgagor to the same extent as Mortgagor could in its own name or otherwise

act with respect to the same; and (iv) enter into any and all agreements with respect to the exercise by others of any of the powers herein granted to Lender, all as Lender from time to time may determine to be in its best interest. Lender may collect and receive all the rents, issues, profits and revenues from the Collateral, including those past due as well as those accruing thereafter, and, after deducting (A) all expenses of taking, holding, managing and operating the Collateral (including compensation for the services of all persons employed for such purposes); (B) the cost of all such maintenance, repairs, renewals, replacements, additions, betterments, improvements, purchases and acquisitions; (C) the cost of such insurance; (D) such taxes, assessments and other similar charges as Lender may at its option pay; (E) other proper charges upon the Collateral or any part thereof; and (F) the compensation, expenses and disbursements of the attorneys and agents of Lender, Lender shall apply the remainder of the monies and proceeds so received by Lender, first, to the payment of accrued interest; second, to the payment of any deposits for taxes and insurance required in this Mortgage and to other sums required to be paid hereunder; and third, to the payment of overdue installments of principal and any other unpaid Loan Obligations then due. Anything in this Section to the contrary notwithstanding, Lender shall not be obligated to discharge or perform the duties of a landlord to any tenant except to the extent Lender has agreed to assume such duties under the terms of any applicable subordination, non-disturbance and attornment agreement or, absent gross negligence or willful misconduct, incur any liability as a result of any exercise by Lender of its rights under this Mortgage, and, absent gross negligence or willful misconduct, Lender shall be liable to account only for the rents, incomes, issues and profits actually received by Lender.

(d) If an Event of Default shall exist, Lender may require that Mortgagor cause all of its Accounts and Rents to be paid to one or more deposit accounts with Lender, or at Lender's option, with another financial institution approved by Lender. To the extent allowed by applicable law, Mortgagor assigns and grants to Lender a security interest in,

pledge of and right of setoff against all moneys from time to time held in such deposit accounts. Mortgagor agrees to promptly notify all of its account debtors and tenants, including all third-party payors pursuant to any Reimbursement Contracts then in effect, to make payments to one or more such deposit accounts upon Lender's request and as designated by Lender, and Mortgagor agrees to provide any necessary endorsements to checks, drafts and other forms of payment so that such payments will be properly deposited in such accounts. Lender may require that the deposit accounts be established so as to comply with any applicable Reimbursement Contracts and other legal requirements, if any, applicable to payments of any accounts receivable. Lender may cause moneys to be withdrawn from such deposit accounts and applied to the Loan Obligations in such order as Lender may elect, whether or not then due subject to applicable law and the applicable Reimbursement Contract. Mortgagor appoints Lender as its attorney-in-fact, with full power of substitution, which appointment is coupled with an interest and is irrevocable, to provide any notice, endorse any check, draft or other payment for deposit, or take any other action which Mortgagor agrees to take in this Section. Lender shall not be liable for failure to collect any Accounts or Rents, or to enforce the contracts or leases pursuant to which such Accounts or Rents are payable, or for any action or omission on the part of Lender, its officers, agents and employees in collecting or enforcing such Accounts, Rents, contracts or leases.

Section 3.4 **Performance by Lender.** Upon the occurrence and during the continuance of an Event of Default in the payment, performance or observance of any term, covenant or condition of this Mortgage, Lender may, at its option, pay, perform or observe the same, and all reasonable payments made or reasonable costs or expenses incurred by Lender in connection therewith, with interest thereon at the Default Rate or at the maximum rate from time to time allowed by applicable law, whichever is less, shall be secured hereby and shall be, without demand, immediately repaid by Mortgagor to Lender. Lender shall be the sole judge of the necessity for any such actions and of the amounts to be paid. Lender is hereby empowered and authorized to enter and to authorize others to enter upon the Collateral or any part thereof for the purpose of performing or observing any such defaulted term, covenant or condition without thereby becoming liable to Mortgagor or any person in possession holding under Mortgagor absent gross negligence or willful misconduct. Notwithstanding anything to the contrary herein, Lender shall have no obligation, explicit or implied, to pay, perform, or observe any such term, covenant, or condition.

Section 3.5 **Receiver.** If any Event of Default shall exist, Lender, upon application to a court of competent jurisdiction, to the extent allowed by applicable law, shall be entitled as a matter of strict right, without regard to the sufficiency or value of any security for the Loan Obligations or the solvency of any party bound for its payment, to the appointment of a receiver to take possession of and to operate the Collateral and to collect and apply the rents, issues, profits and revenues thereof. The receiver shall have all of the rights and powers permitted under the laws of the state wherein the Property is situated. Mortgagor will pay unto Lender upon demand all reasonable expenses, including receiver' s fees, attorney' s fees, costs and agent' s compensation, incurred pursuant to the provisions of this Section, and upon any Mortgagor' s

failure to pay the same, any such amounts shall be added to the Loan Obligations and shall be secured by this Mortgage.

Section 3.6 **Enforcement.**

(a) If an Event of Default exists, Lender may foreclose this Mortgage by the exercise of the power of sale or by judicial foreclosure. In lieu of or in addition to foreclosure, Lender may obtain any other legal or equitable remedy. Mortgagor confers on and grants to Lender the power to sell the Property and Improvements in the manner provided in the "Oklahoma Power of Sale Mortgage Foreclosure Act." The Lender shall have the following options in foreclosing upon the Collateral:

(i) In the event of any sale under this Mortgage by virtue of the exercise of the powers herein granted, or pursuant to any order in any judicial proceedings or otherwise, the Collateral may be sold as an entirety or in separate parcels and in such manner or order as Lender in its sole discretion may elect, and if Lender so elects, Lender or Lender may sell the personal property covered by this Mortgage at one or more separate sales in any manner permitted by the applicable Uniform Commercial Code, and one or more exercises of the powers herein granted shall not extinguish or exhaust such powers, until the entire Collateral is sold or the Loan Obligations are paid in full. If the Loan Obligations are now or hereafter further secured by any chattel mortgages, pledges, contracts of guaranty, assignments of leases or other security instruments, Lender at its option may exhaust the remedies granted under any of said security instruments or this Mortgage in such order as Lender may determine consistent with applicable law. Said sale may be adjourned by the Lender, or his agent or successors, and reset at a later date consistent with applicable law without additional publication (except as may be required by applicable law); provided that an announcement to that effect be made at the scheduled place of sale at the time and on the date the sale is originally set.

(ii) To the extent permitted by applicable law, sale of a part of the Collateral shall not exhaust the power of sale until the Loan Obligations are paid and performed in full. It shall not be necessary to have present or to exhibit at any such sale any of the Collateral.

It is intended by each of the foregoing provisions of this subsection that Lender may sell not only the Property but also the other Collateral, or any part thereof, along with the Property, or any part thereof, all as a unit and as a part of the single sale, or may sell any part of the Collateral separately from the remainder of the Collateral.

(b) If an Event of Default shall exist, Lender may, in addition to and not in abrogation of the rights covered under subsection (a) of this Section, either with or without entry or taking possession as herein provided or otherwise, proceed by a suit or suits in law or in

equity or by any other appropriate proceeding or remedy (i) to enforce payment of the Loan Obligations or the performance of any term, covenant, condition or agreement of this Mortgage or any other right, (ii) to foreclose this Mortgage and to sell, as an entirety or in separate lots or parcels, the Collateral, as provided by applicable law, and (iii) to pursue any other remedy available to it, all as Lender in its sole discretion shall elect.

(c) After notification, if any, as hereafter provided in this subsection, to the extent permitted by applicable law, Lender may sell, lease, or otherwise dispose of (herein, a “disposition”), at the office of Lender, or on the Property, or elsewhere, as chosen by Lender, all or any part of the Inventory and Equipment, in their then condition or following any commercially reasonable preparation or processing, and each disposition may be as a unit or in parcels, by public or private proceedings, and by way of one or more contracts, and, at any disposition, it shall not be necessary to have present or exhibit the Inventory and Equipment, or any part thereof being sold. The disposition of any part of the Inventory and Equipment shall not exhaust Lender’s power of disposition, but dispositions may be made from time to time until the Loan Obligations are paid and performed in full. Reasonable notification of the time and place of any public disposition pursuant to this subsection, or reasonable notification of the time after which any private disposition is to be made pursuant to this subsection, shall be sent to Mortgagor and to any other person entitled to receive notice under the Uniform Commercial Code (the “Code”) of the State of Oklahoma or other applicable jurisdiction. It is agreed that notice sent or given not less than ten calendar days prior to the taking of the action to which the notice relates is reasonable notification for the purposes of this subsection.

(d) In the event a foreclosure hereunder should be commenced by Lender in accordance with the powers of sale granted in this Mortgage, Lender may at any time before the sale, orally or in writing, delay or abandon the sale, and may upon abandonment institute suit for the collection of the Loan Obligations, and/or for the foreclosure of the liens hereof. If Lender should institute a suit for the collection of the Loan Obligations, and/or for a foreclosure of the liens hereof, Lender may at any time before the entry of a final judgment in such suit dismiss such suit (either totally or as to the counts thereof for judicial foreclosure), and sell the Collateral, or any part thereof, in accordance with the provisions of this Mortgage.

Section 3.7 **Purchase by Lender.** Upon any foreclosure sale or sale of all or any portion of the Collateral under the power herein granted, Lender may bid for and purchase the Collateral and shall be entitled to apply all or any part of the Loan Obligations as a credit to the purchase price.

Section 3.8 **Application of Proceeds of Sale.** In the event of a foreclosure or other sale of all or any portion of the Collateral, the proceeds of said sale shall be applied, first, to the reasonable expenses of such sale and of all proceedings in connection therewith, including reasonable fees of the attorney (and attorney fees and expenses shall become absolutely due and payable whenever foreclosure is commenced); then to insurance premiums, liens, assessments, taxes and charges including utility charges advanced by Lender, and interest thereon; then to payment of the Note and accrued interest thereon, and all other Loan Obligations, all in such

order of priority as Lender shall determine, in its sole discretion; and finally the remainder, if any, shall be paid to Mortgagor, or to the person or entity lawfully entitled thereto.

Section 3.9 **Mortgagor as Tenant Holding Over.** In the event of any such foreclosure sale or sale under the powers herein granted, Mortgagor (if Mortgagor shall remain in possession) shall be deemed a tenant holding over and shall forthwith deliver possession to the purchaser or purchasers at such sale or be summarily dispossessed according to provisions of law applicable to tenants holding over.

Section 3.10 **Waiver of Appraisal.** Appraisal of the Property and Improvements is hereby waived, or not, at the option of Lender, which option Lender shall exercise at or prior to the time judgment is rendered in any judicial foreclosure.

Section 3.11 **Discontinuance of Proceedings.** In case Lender shall have proceeded to enforce any right, power or remedy under this Mortgage by foreclosure, entry or otherwise, and such proceedings shall have been discontinued or abandoned for any reason, then in every such case, Mortgagor and Lender shall be restored to their former positions and rights hereunder, and all rights, powers and remedies of Lender shall continue as if no such proceedings had occurred.

Section 3.12 **Remedies Cumulative.** No right, power or remedy conferred upon or reserved to Lender by this Mortgage is intended to be exclusive of any other right, power or remedy, but each and every such right, power and remedy shall be cumulative and concurrent and shall be in addition to any other right, power and remedy given hereunder or now or hereafter existing at law, in equity or by statute.

Section 3.13 **No Waiver; Waivers.**

(a) No delay or omission by Lender or by any holder of the Note to exercise any right, power or remedy accruing upon any default shall exhaust or impair any such right, power or remedy or shall be construed to be a waiver of any such default, or acquiescence therein, and every right, power and remedy given by this Mortgage to Lender may be exercised from time to time and as often as may be deemed expedient by Lender. No consent or waiver expressed or implied by Lender to or of any breach or default by Mortgagor in the performance of the obligations of Mortgagor hereunder shall be deemed or construed to be a consent or waiver to or of any other breach or default in the performance of the same or any other obligations of Mortgagor hereunder. Failure on the part of Lender to complain of any act or failure to act or failure to declare an Event of Default, irrespective of how long such failure continues, shall not constitute a waiver by Lender of its rights hereunder or impair any rights, powers or remedies of Lender hereunder.

(b) No act or omission by Lender shall release, discharge, modify, change or otherwise affect the original liability under the Note or this Mortgage or any other obligation of either Borrower or any subsequent purchaser of the Collateral or any part thereof, or any maker, cosigner, endorser, surety or guarantor, nor preclude Lender from exercising any

right, power or privilege herein granted or intended to be granted in the event of any default then existing or of any subsequent default, nor alter the lien of this Mortgage, except as expressly provided in an instrument or instruments executed by Lender. Without limiting the generality of the foregoing, Lender may: (i) grant forbearance or an extension of time for the payment of all or any portion of the Loan Obligations; (ii) take other or additional security for the payment of any of the Loan Obligations; (iii) waive or fail to exercise any right granted herein or in the Note; (iv) release any part of the Collateral from the security interest or lien of this Mortgage or otherwise change any of the terms, covenants, conditions or agreements of the Note or this Mortgage; (v) consent to the filing of any map, plat or replat affecting the Collateral; (vi) consent to the granting of any easement or other right affecting the Collateral; (vii) make or consent to any agreement subordinating the security title or lien hereof, or (viii) with the consent of Mortgagor modify, amend or increase the Note or the Loan Obligations hereby secured or take or omit to take any action whatsoever with respect to the Note, this Mortgage, the Collateral, the Loan Documents or Loan Obligations, all without releasing, discharging, modifying, changing or affecting any such liability, or precluding Lender from exercising any such right, power or privilege or affecting the lien of this Mortgage (except for any subordination of the lien expressly granted pursuant to (vii) above). In the event of the sale or transfer by operation of law or otherwise of all or any part of the Collateral, Lender, without notice, is hereby authorized and empowered to deal with any such vendee or transferee with reference to the Collateral or the Loan Obligations, or with reference to any of the terms, covenants, conditions or agreements hereof, as fully and to the same extent as it might deal with the original parties hereto and without in any way releasing or discharging any liabilities, obligations or undertakings.

(c) Mortgagor waives:



- i. Any defense based upon any legal disability or other defense of Borrower, any other guarantor, or any other person, or by reason of the cessation or limitation of the liability of Borrower from any cause other than full payment and performance of all of the Loan Obligations;
- ii. Any defense based upon the application by Borrower of the proceeds of any credit extended to Borrower by Lender for purposes other than the purposes represented by Borrower or intended or understood by Lender or Mortgagor;
- iii. Any defense based upon Lender's election of any remedy against Mortgagor or Borrower and the consequent loss by Mortgagor of the right to recover any deficiency from Borrower;
- iv. Any defense based upon any statute or rule of law that provides that the obligation of a surety must be neither larger in amount nor in any other respects more burdensome than that of a principal;

- v. The benefit of 12 Okla. Stat. § 686 and 15 Okla. Stat. §§ 334, 335, 338, 340, 341, 379, 383, and 384 and any amendments or replacements of those statutes.

Section 3.14 **Suits to Protect the Collateral.** In the event of the failure by Mortgagor to take any of actions provided for herein, Lender shall have power to institute and maintain such suits and proceedings as it may reasonably deem expedient (a) to prevent any impairment of the Collateral by any acts which may be unlawful or constitute a default under this Mortgage; (b) to preserve or protect its interest in the Collateral and in the rents, issues, profits and revenues arising therefrom; and (c) to restrain the enforcement of or compliance with any legislation or other governmental enactment, rule or order that may be unconstitutional or otherwise invalid, if the enforcement of or compliance with such enactment, rule or order would materially impair the security hereunder or be prejudicial to the interest of Lender.

Section 3.15 **Proofs of Claim.** In the case of any receivership, insolvency, bankruptcy, reorganization, arrangement, adjustment, composition or other proceedings affecting Mortgagor, its creditors or its property, Lender, to the extent permitted by law, shall be entitled to file such proofs of claim and other documents as may be necessary or advisable in order to have the claims of Lender allowed in such proceedings for the entire amount due and payable by Mortgagor under this Mortgage at the date of the institution of such proceedings and for any additional amount which may become due and payable by Mortgagor hereunder after such date.

Section 3.16 **Tradenames, etc.** During the exercise of any right in the Collateral pursuant to this Article III, absent gross negligence or willful misconduct, Lender shall not be liable to Mortgagor for any inadvertent violation or infringement upon any trade name, trademark, service mark, or logo relating to the Collateral, and Mortgagor waives any claim for any such violation or infringement that occurs prior to written notice of such infringement by Mortgagor to Lender.

#### ARTICLE IV MISCELLANEOUS

Section 4.1 **Security Agreement.** This Mortgage creates a lien on and a security interest in that part of the Collateral which constitutes personal property under any applicable Code, and shall constitute a security agreement under the applicable Code or other law applicable to the creation of liens on personal property. This Mortgage shall constitute a financing statement under the applicable Code with Mortgagor as the "debtor" and Lender as the "secured party." If an Event of Default exists, the Lender shall have all rights and remedies of a secured party under the applicable Code.

Section 4.2 **Assembly of Collateral.** Upon the occurrence and continuance of an Event of Default, the Mortgagor shall assemble, if requested by the Lender, at its expense, all of the personal property Collateral and the documents evidencing such personal property Collateral and the books and records applicable thereto and make them available to the Lender at a place to

be designated by the Lender; provided, however, Mortgagor shall have no obligation to assemble the collateral in a manner which would impair the continued operation of the Facility as an assisted living/long term care facility.

Section 4.3 **Successors and Assigns; Successor Lender.** This Mortgage shall inure to the benefit of and be binding upon Mortgagor and Lender and their respective heirs, executors, legal representatives, successors, successors-in-title, and assigns. Whenever a reference is made in this Mortgage to "Mortgagor" or "Lender," such reference shall be deemed to include a reference to the heirs, executors, legal representatives, successors, successors-in-title and assigns of Mortgagor or Lender, as the case may be, but shall not imply any permission to make or permit any transfer which is otherwise prohibited.

Section 4.4 **Terminology.** All personal pronouns used in this Mortgage, whether used in the masculine, feminine or neuter gender, shall include all other genders; the singular shall include the plural, and vice versa. Titles and Articles are for convenience only and neither limit nor amplify the provisions of this Mortgage, and all references herein to Articles, Sections or subsections shall refer to the corresponding Articles, Sections or subsections of this Mortgage unless specific reference is made to Articles, Sections or subsections of another document or instrument.

Section 4.5 **Severability; Complete Agreement.** If any provisions of this Mortgage or the application thereof to any person or circumstance shall be invalid or unenforceable to any extent, the remainder of this Mortgage and the application of such provisions to other persons or circumstances shall not be affected thereby and shall be enforced to the greatest extent permitted by law. This Mortgage, the Note and the instruments executed in connection herewith constitute the full and complete agreement of the parties and supersede all prior negotiations, correspondence, and memoranda relating to the subject matter hereof, and this Mortgage may not be amended except by a writing signed by the parties hereto.

Section 4.6 **Applicable Law.** This Mortgage shall be interpreted, construed and enforced according to the laws of the state wherein the Property is situated. If, for any reason or to any extent any word, term, provision, or clause of this Mortgage or any of the other Loan Documents, or its application to any person or situation, shall be found by a court or other adjudicating authority to be invalid or unenforceable, the remaining words, terms, provisions or clauses shall be enforced, and the affected word, term, clause or provision shall be applied, to the fullest extent permitted by law.

Section 4.7 **Limitation of Interest.** It is the intent of Mortgagor and Lender in the execution of this Mortgage and all other Loan Documents to contract in strict compliance with the usury laws governing the Loan Obligations. In furtherance thereof, Lender and Mortgagor stipulate and agree that none of the terms and provisions contained in the Loan Documents shall ever be construed to create a contract for the use, forbearance, or detention of money requiring payment of interest at a rate in excess of the maximum interest rate permitted to be charged by the laws governing the Loan Obligations. Mortgagor or any guarantor, endorser or other party

now or hereafter becoming liable for the payment of the Loan or other amounts due to Lender shall never be liable for unearned interest on the Loan or other amounts due to Lender and shall never be required to pay interest on the Loan or other amounts due to Lender at a rate in excess of the maximum interest that may be lawfully charged under the laws governing the Loan Obligations, and the provisions of this paragraph shall control over all other provisions of the Note and other Loan Documents and any other instrument executed in

connection therewith which may be in apparent conflict herewith. In the event Lender shall collect monies that are deemed to constitute interest and that would otherwise increase the effective interest rate on the Loan Obligations or other amounts due to Lender to a rate in excess of that permitted to be charged by the laws governing the Loan Obligations, all such sums deemed to constitute interest in excess of the legal rate shall be applied to the unpaid principal balance of the Loan Obligation and if in excess of such balance, shall be immediately returned to the Mortgagor upon such determination.

Section 4.8 **Notices, etc/Lender's Consent.** All notices and other communications provided for hereunder shall be in writing and be given and deemed received in accordance with the provisions of the Loan Agreement. Except where this Mortgage or the other instruments relating to the Loan Obligations expressly provides otherwise, wherever Lender's consent or approval is called for, Lender shall not unreasonably condition or withhold such approval or consent.

Section 4.9 **Assignment.** This Mortgage is assignable by Lender and any assignment hereof by Lender shall operate to vest in the assignee all rights and powers herein conferred upon and granted to Lender. This Mortgage may not be assigned by Mortgagor.

Section 4.10 **Time of the Essence.** Time is of the essence with respect to each and every covenant, agreement and obligation of Mortgagor under this Mortgage, the Note and any and all other instruments now or hereafter evidencing, securing or otherwise relating to the Loan Obligation.

Section 4.11 **Attorney Fees.** Mortgagor agrees to reimburse Lender for all costs, expenses, and attorneys' fees that Lender incurs in connection with the enforcement of any obligation contained in this Mortgage or the collection of any rents assigned herein, with or without litigation, including, without limitation, any costs, expenses, and fees incurred: (a) in making demands for and collecting any rents; (b) in any action for rents against Lessor or any lessee; (c) on appeal; (d) in any petition for review; (e) in any arbitration or mediation; (f) in any action contesting or seeking to restrain, enjoin, stay, or postpone the exercise of any remedy in which Lender prevails; (g) in any bankruptcy, probate, receivership or other proceeding involving Lessor; and (h) in connection with all negotiations, documentation, and other actions relating to any work-out, compromise, settlement or satisfaction relating to this Mortgage. All such costs, expenses, and fees shall be due and payable upon demand and shall bear interest from the date incurred through the date of collection at the default rate stated in the Loan Documents.

Section 4.12 **Waiver of Jury Trial.** **MORTGAGOR BY ITS EXECUTION HEREOF HEREBY WAIVES ANY RIGHT THAT IT MAY HAVE TO A TRIAL BY JURY ON ANY CLAIM, COUNTERCLAIM, SETOFF, DEMAND, ACTION OR CAUSE OF ACTION (A) ARISING OUT OF OR IN ANY WAY RELATED TO THIS MORTGAGE, THE LOAN DOCUMENTS OR THE LOAN, OR (B) IN ANY WAY CONNECTED WITH OR PERTAINING OR RELATED TO OR INCIDENTAL TO ANY DEALINGS OF LENDER AND/OR MORTGAGOR WITH RESPECT TO THE LOAN DOCUMENTS OR IN CONNECTION WITH THIS MORTGAGE OR THE EXERCISE OF EITHER PARTY'S RIGHTS AND REMEDIES UNDER THIS MORTGAGE OR OTHERWISE, OR THE CONDUCT OR THE RELATIONSHIP OF THE PARTIES HERETO, IN ALL OF THE FOREGOING CASES WHETHER NOW EXISTING OR HEREAFTER ARISING AND WHETHER SOUNDING IN CONTRACT, TORT OR OTHERWISE. MORTGAGOR AGREE THAT THE LENDER MAY FILE A COPY OF THIS AGREEMENT WITH ANY COURT AS WRITTEN EVIDENCE OF THE KNOWING, VOLUNTARY, AND BARGAINED AGREEMENT OF MORTGAGOR IRREVOCABLY TO WAIVE ITS RIGHTS TO TRIAL BY JURY AS AN INDUCEMENT OF LENDER TO ENTER INTO THE LOAN AGREEMENT AND OTHER LOAN DOCUMENTS AND OF LENDER TO MAKE THE LOAN EVIDENCED AND SECURED THEREBY, AND THAT, TO THE EXTENT PERMITTED BY APPLICABLE LAW, ANY DISPUTE OR CONTROVERSY WHATSOEVER BETWEEN MORTGAGOR AND LENDER SHALL INSTEAD BE TRIED IN A COURT OF COMPETENT JURISDICTION BY A JUDGE SITTING WITHOUT A JURY.**

IN WITNESS WHEREOF, Mortgagor has caused this Mortgage to be executed as of the day and year first above written.

CSCC PROPERTY HOLDINGS, LLC, a Georgia limited liability company

By: /s/ Christopher F. Brogdon  
Name: Christopher F. Brogdon  
Title: Manager

STATE OF )  
[SEAL] ) ss.  
COUNTY OF )

This instrument was acknowledged before me on August , 2012, by Christopher F. Brogdon, as Manager of CSCC Property Holdings, LLC, a Georgia limited liability company.

(Seal) /s/ [Illegible]  
Notary Public  
My commission expires:  
Commission #:

MORTGAGE SIGNATURE PAGE – ADCARE - SENIOR

Mortgage - Exhibit A

**GUARANTY OF PAYMENT AND PERFORMANCE**

**THIS GUARANTY OF PAYMENT AND PERFORMANCE** (this “**Guaranty**”) made as of August 17, 2012, by **ADCARE HEALTH SYSTEMS, INC.**, an Ohio corporation (the “**Guarantor**”) in favor of **CONTEMPORARY HEALTHCARE FUND I, L.P.**, a Delaware limited partnership (the “**Lender**”).

**RECITALS:**

Pursuant to a Loan Agreement dated the date hereof (as the same may hereafter be amended, the “**Loan Agreement**”) between **CSCC PROPERTY HOLDINGS, LLC**, a Georgia limited liability company, and **CSCC NURSING, LLC**, a Georgia limited liability company (collectively, the “**Borrowers**”) and Lender, Lender agreed to make a loan to the Borrowers in the principal amount of up to Six Hundred Thousand and No/100 Dollars (\$600,000.00) (the “**Loan**”). As one of the conditions for the Loan, Lender required that the Guarantor guarantee the Loan Obligations (as hereinafter defined), now existing or hereafter incurred, owing to the Lender pursuant to the Loan Documents (as defined in the Loan Agreement). Capitalized terms used herein and not otherwise defined shall have the meanings set forth in the Loan Agreement. Guarantor is the parent entity of the Borrowers and will receive direct and indirect benefits from the Loan, which benefits, among others, provide adequate consideration for them to enter into this Guaranty.

**AGREEMENT**

**NOW, THEREFORE**, in consideration of the foregoing Recitals, and in order to induce the Lender to continue to make the Loan, and as security for the Loan Obligations, Guarantor agrees and covenants with Lender and represents and warrants to Lender as follows:

1. **Guarantee of Loan Obligations.** The Guarantor hereby unconditionally, jointly and severally with Borrowers and any other, guarantor of the Loan guarantees to the Lender the following (collectively, the “**Loan Obligations**”) (a) the due, regular, and punctual payment of the principal (including capitalized interest that is added to principal), interest, fees, premiums, expenses, and other charges pursuant to the Note executed by the Borrowers evidencing the Loan, as the same may hereafter be extended, renewed, modified, or amended (the “**Note**”), (b) the payment of all fees, premiums, expenses, charges, and other amounts from time to time owing to Lender pursuant to the Loan Agreement and other Loan Documents, and (c) the performance of all covenants, agreements, and other obligations from time to time owing to, or for the benefit of, Lender pursuant to the Loan Documents, including, but not limited to, the indemnity obligations under the Loan Documents; (d) upon the failure of the Borrowers timely to pay or perform any of the foregoing Loan Obligations as provided in the Loan Documents, the payment of all reasonable costs and expenses incurred by Lender in paying or performing such Loan Obligations (but Lender shall not be required to pay or perform such Loan Obligations); and (e) all reasonable costs, attorneys’ fees, and expenses that may be incurred by the Lender by

reason of an Event of Default as provided in the Loan Documents, including reasonable fees and expenses in any appellate or bankruptcy proceedings.

Upon any Event of Default pursuant to any of the Loan Documents, the Guarantor unconditionally promises to pay to the Lender such amounts as are necessary to cure the Event of Default, or at the option of the Lender in the event Lender has elected to accelerate the Loan Obligations as a result thereof, the Guarantor agrees to pay the outstanding Loan Obligations in full.

This Guaranty is unconditional except as expressly set forth herein, and the Guarantor agrees that the Lender, upon the occurrence of an Event of Default pursuant to any of the Loan Documents, shall not be required to assert any claim or cause of action against the Borrowers before asserting any claim or cause of action against the Guarantor under this Guaranty. The Guarantor further agrees that the Lender shall not be required to pursue or foreclose on any Collateral that it may receive from the Borrowers, any guarantor, or others as security for any of the Loan Obligations before making a claim or asserting a cause of action against the Guarantor under this Guaranty.

The failure of the Lender to perfect its security interest in any of the Collateral as set forth in any of the Loan Documents or any other collateral now or hereafter securing all or any part of the Loan Obligations shall not release the Guarantor from its liabilities and obligations hereunder.

Notice of acceptance of this Guaranty and of any Default or Event of Default is hereby waived by the Guarantor, except to the extent notice is otherwise expressly required by the Loan Documents. Presentment, protest, demand, and notice of protest and demand, and notice of receipt of any and all Collateral, and of the exercise of possessory remedies or foreclosure on any and all Collateral received by the Lender from the Borrowers or the Guarantor are hereby waived. To the extent any Collateral from time to time consists of accounts owing to Borrowers, all settlements, compromises, compositions, accounts stated, and agreed balances in good faith between any primary or secondary obligors on any such accounts shall be binding upon the Guarantor. With respect to the amounts now or hereafter due under this Guaranty, the Guarantor waives, to the extent permitted by law, all rights of exemption of property from levy or sale under execution or other process for the collection of debts under the laws or Constitution of the United States or any state thereof.

This Guaranty shall not be affected, modified, or impaired by the voluntary or involuntary liquidation, dissolution, sale, or other disposition of all or substantially all of the assets, marshalling of assets and liabilities, receivership, insolvency, bankruptcy, assignment for the benefit of creditors, reorganization, arrangements, composition with creditors or readjustment of, or other similar proceedings affecting the Borrowers or any guarantor, or any of the assets belonging to any of them, nor shall this Guaranty be affected, modified, or impaired by the invalidity of the Note or any of the other Loan Documents.

Without notice to the Guarantor, without the consent of the Guarantor, and without affecting or limiting the Guarantor's liability hereunder, the Lender may:

- (a) grant the Borrowers extensions of time for payment of the Loan Obligations or any part hereof;
- (b) renew any of the Loan Obligations;
- (c) grant the Borrowers extensions of time for performance of agreements or other indulgences;
- (d) at any time release any or all of the Collateral, or any mortgage, deed of trust, or security interest in any Collateral, that now or hereafter secures any of the Loan Obligations;
- (e) compromise, settle, release, or terminate any or all of the obligations, covenants, or agreements of the Borrowers under the Note or other Loan Documents;
- (f) at any time release any one or more other guarantors from their guarantees of any of the Loan Obligations;

and

(g) modify or amend any obligation, covenant, or agreement of the Borrowers as set forth in the Note or any of the other Loan Documents (and such amendments shall nevertheless be binding upon the Guarantor); provided no increase in the principal amount of the Loan will be binding upon the Guarantor unless it has consented to such increase unless such increase is made pursuant to Section 2.1(b) of the Loan Agreement.

This Guaranty shall continue to be effective, or be reinstated, as the case may be, if at any time any whole or partial payment or performance of any Loan Obligations is or is sought to be rescinded or must otherwise be restored or returned by the Lender upon the insolvency, bankruptcy, dissolution, liquidation, or reorganization of the Borrowers, the Guarantor or any guarantor upon or as a result of the appointment of a receiver, intervenor, or conservator of, or trustee or similar officer for, the Borrowers, the Guarantor or any guarantor of or for any substantial part of its property, or otherwise, all as though such payments and performance had not been made and as though this Guaranty had not expired or been terminated. This Guaranty shall not be affected in any way by the transfer or other disposition of any of the Collateral described in and granted to Lender pursuant to the Loan Documents.

2. **Representations and Warranties of the Guarantor.** To induce the Lender to make the Loan to Borrowers, Guarantor represents and warrants to the Lender as follows:

(a) **Power to Incur Obligations.** Guarantor has full power and unrestricted right to enter into this Guaranty and to incur the obligations provided for herein, all of which have been duly authorized by all necessary corporate action of Guarantor.

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(b) **Existence, Power and Qualification.** Guarantor is a limited liability company duly organized, in good standing and validly existing under the laws of the state of its formation as set forth in the introductory paragraph of this Agreement, has the power to own its properties and to carry on its business as is now being conducted and to execute and deliver this Guaranty, and is duly qualified to do business and is in good standing in every jurisdiction in which the character of the properties owned by it or in which the transaction of its business makes its qualification necessary.

(c) **Conflicts.** This Guaranty does not violate, conflict with, or constitute any default under the operating agreement of Guarantor or any decree, or judgment by which Guarantor is bound or affected, and to the best of Guarantor's knowledge, does not constitute a material violation of any agreement or instrument binding upon Guarantor.

(d) **Pending Matters.** No action or investigation is pending or, to the best of Guarantor's knowledge, threatened before or by any state or federal court or administrative agency which would reasonably be expected to result in any material adverse change in the financial condition, operations, or prospects of Guarantor. Guarantor is not in violation of any agreement, the violation of which would reasonably be expected to have a materially adverse effect on Guarantor's business or assets, and Guarantor is not in violation of any order, judgment, or decree of any state or federal court or administrative agency by which Guarantor is bound or affected.

(e) **Financial Statements Accurate.** All financial statements heretofore or hereafter provided by the Guarantor are or will, at the time of the delivery thereof be, true and complete in all material respects as of their respective dates and fairly present the financial condition of Guarantor, and there are no known liabilities, direct or indirect, fixed or contingent, as of the respective dates of such statements which are not or will not, at the time of the delivery thereof, be reflected therein or in the notes thereto or in a written certificate delivered with such statements. There has been no material adverse change in the financial condition, operations, or prospects of Guarantor since the dates of such statements except as fully disclosed in writing with the delivery of such statements.

(f) **No Defaults or Restrictions.** Guarantor is not in default under any agreement or instrument that causes or would have a material adverse effect on the business, properties, and financial operations or condition of Guarantor.

(g) **Payment of Taxes and Employee Benefits.** Guarantor has filed all federal, state, and local tax returns which are required to be filed and has paid, or made adequate provision for the payment of, all taxes which have or may become due pursuant to said returns or to assessments received by Guarantor and has made all required payments to employee benefit plans.

(h) **Disclosure.** Neither this Guaranty nor any other document, financial statement, credit information, certificate, or statement required herein or otherwise furnished to Lender by Guarantor in connection with the Loan or this Guaranty contains any untrue, incorrect,

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or misleading statement of material fact. All representations and warranties made herein or any certificate or other document delivered to Lender by or on behalf of Guarantor pursuant to or in connection with this Guaranty shall be deemed to have been relied upon by Lender notwithstanding any investigation heretofore or hereafter made by Lender or on its behalf, and shall survive the delivery of this Guaranty.

(i) **ERISA.** Guarantor is in compliance with all applicable provisions of the Employee Retirement Income Security Act of 1974, as amended (“ERISA”).

3. **Affirmative Covenants of the Guarantor.** Guarantor covenants and agrees that so long as the Loan Obligations are outstanding, Guarantor shall comply with each of the following affirmative covenants:

(a) **Payment of Loan/Performance of Loan Obligations.** Duly and punctually pay or cause to be paid the principal and interest of the Note in accordance with its terms and duly and punctually pay or cause to be paid or performed all other Loan Obligations.

(b) **Payment of Taxes.** Pay and discharge all taxes, assessments, and governmental charges or levies imposed upon the Guarantor, including, without limitation, all current tax liabilities of all kinds, all required withholdings of income taxes of employees and all required old age and unemployment contributions.

(c) **Reporting Requirements.** From time to time upon request, furnish to Lender such information regarding the business affairs, finances, and conditions of the Guarantor and its properties in such detail as the Lender reasonably may request, including tax returns; without limiting the foregoing, Guarantor will furnish to Lender financial statements as and when required by the Loan Agreement. All financial statements shall be provided in the form and at the times set forth in the Loan Agreement.

(d) **Payment of Indebtedness.** Pay or cause to be paid duly and punctually all principal and interest of any material Indebtedness of the Guarantor to its creditors, and comply with and perform all conditions, terms, and obligations of the notes or other instruments evidencing such indebtedness and any mortgages, deeds of trust, security agreements, and other instruments evidencing or securing such indebtedness. Without limiting anything herein, “material” Indebtedness shall include, without limitation, any Indebtedness which is secured by or becomes subject to any Lien. Guarantor may contest any Indebtedness in good faith and shall not be in violation of this covenant during the period of any such contest provided that execution against any property of the Guarantor must have been effectively stayed and reserves adequate for payment must have been established.

(e) **Notice of Loss.** Notify Lender of any event causing a loss or reduction in value of the Guarantor’s assets which has a material adverse effect on the Guarantor’s net worth.

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(f) **Maintenance of Existence.** Maintain its corporate existence, and, in each jurisdiction in which the character of the property owned by it or in which the transaction of its business makes qualification necessary, maintain qualification and good standing.

4. **Negative Covenants of the Guarantor.** Except as permitted by the Loan Agreement, so long as any of the Loan Obligations are outstanding, Guarantor agrees that it shall not, without Lender's prior written approval:

(a) **Change in Business.** Make any material change in the nature of its business as it is being conducted as of the date hereof which would reasonably be expected to materially and adversely affect its ability to perform its obligations pursuant to this Guaranty.

(b) **Changes in Accounting.** Change its method of accounting to one inconsistent with the method heretofore used by Guarantor.

(c) **Consolidation or Transfer of Substantially all of its Assets.** Enter into any merger, consolidation, or similar transaction with any entity other than Borrowers or any other subsidiary of Borrowers which is a guarantor of the Loan, or sell, assign, lease, or otherwise dispose of (whether in one transaction or in a series of transactions) all or substantially all of its assets (whether now or hereafter acquired) other than to Borrowers or any other subsidiary of Borrowers which is a guarantor of the Loan or unless any such disposition is of property other than the Collateral and is in the ordinary course of business for a full and fair consideration and does not violate any covenant of the Loan Agreement.

(d) **ERISA Funding and Termination.** Permit the funding requirements of ERISA with respect to any employee plan of Guarantor to be less than the minimum required by ERISA at any time, or any employee plan of Guarantor to be subject to involuntary termination proceedings at any time.

(e) **Transfer of Ownership Interests.** Permit any transfer of the ownership interests or stock of Guarantor or change in management of Guarantor that would violate any covenant of the Loan Agreement.

5. **Events of Default.** Guarantor's violation of any covenant set forth in Section 4 hereof, or Guarantor's failure to properly and timely perform or observe any covenant or condition set forth in this Guaranty (other than those in Section 4) which is not cured within any applicable cure period as set forth herein or, if no cure period is specified therefor, which is not cured within thirty (30) days of Lender's notice to Guarantor of such default (provided such cure period shall be extended an additional sixty (60) days if Guarantor commences a cure within such initial thirty (30) days, provides evidence thereof to Lender and diligently pursues a cure), or the falsity in any material respect of any representation or warranty herein or in any financial statement, certificate, or other information heretofore or hereafter provided by Guarantor to Lender, shall constitute an "**Event of Default**" hereunder and under each of the Loan Documents. The foregoing provision or any other provision requiring or providing for notice or demand from Lender is deemed eliminated if Lender is prevented from giving such notice or

demand by bankruptcy or other applicable law, and the Event of Default shall occur upon the occurrence of such event or condition if not cured within any applicable period measured from the occurrence of such event or condition rather than from notice or demand.

6. **Waiver and Subordination.** Guarantor expressly waives any right to payment arising by virtue of any subrogation or indemnification upon payment by Guarantor of amounts due from Borrowers to Lender, and Guarantor expressly subordinates any other rights to payment of indebtedness owing from Borrowers to Guarantor, whether now existing or hereafter arising, to the prior right of Lender to receive or require payment in full of the Loan Obligations, until such time as the Loan Obligations are fully paid (including interest accruing on the Note after any petition under the Bankruptcy Code, which post-petition interest Guarantor agrees shall remain a

claim that is prior and superior to any claim of Guarantor notwithstanding any contrary practice, custom, or ruling in proceedings under the Bankruptcy Code generally) and such payments are final and not subject to refund or rescission under bankruptcy or other applicable law. Furthermore, so long as an Event of Default exists under the Loan Documents, Guarantor agrees not to accept any payment or satisfaction of any kind of indebtedness of Borrowers to the Guarantor or any security for such indebtedness until such time as the Loan Obligations are fully paid. If Guarantor should receive any such payment, satisfaction or security for any indebtedness of Borrowers to the Guarantor, the Guarantor agrees to deliver the same promptly to Lender in the form received, endorsed, or assigned as may be appropriate for application on account of, or as security for, the Loan Obligations and until so delivered, agrees to hold the same in trust for Lender.

7. **Successors and Assigns.** This Guaranty shall be binding upon, and inure to the benefit of, the parties hereto and their respective heirs, legal representatives, successors, and assigns.

8. **Transfer of Rights under the Guaranty and the Loan Documents.**

(a) **Transfer by Lender.** Subject to any limitations set forth in the Loan Agreement, Lender may, at any time, sell, transfer or assign any of the Loan Documents, and any or all servicing rights with respect thereto, or grant participations therein or issue securities evidencing a beneficial interest in a rated or unrated public offering or private placement (the “**Securities**”) to any affiliate of Lender or to the Small Business Administration. Lender may forward to each purchaser, transferee, assignee, servicer, participant or investor in such Securities or any credit rating agency rating such Securities (the foregoing entities hereinafter collectively referred to as the “**Investor**”) and each prospective Investor, all documents and information which Lender now has or may hereafter acquire relating to Guarantor, whether furnished by Borrowers, Guarantor or otherwise, as Lender determines necessary or desirable. Guarantor agrees, upon request of Lender, to cooperate with Lender in connection with any transfer made or any Securities created pursuant to this Section 8(a) provided there is no material financial or other burden to Guarantor of doing so and provided such cooperation does not require an amendment to this Guaranty which would in any manner increase the obligations of Guarantor hereunder. Guarantor shall also furnish and Guarantor hereby consents, subject to Lender’s obligations hereunder, to Lender furnishing to such Investors or such prospective

Investors any and all information concerning the financial condition of Guarantor as provided for in this Section 8(a) in connection with any sale, transfer or participation interest. Notwithstanding the foregoing, in the event that Lender delivers any such information to a prospective Investor, Lender will notify Guarantor to such effect.

(b) **Transfer by Guarantor.** Without the prior written consent of Lender, which may be withheld in Lender’s sole discretion, Guarantor may not, at any time, sell, transfer or assign this Guaranty or any of the other Loan Documents to which Guarantor is a party or any of the Loan Documents to which Guarantor is a party or is otherwise a guarantor, and any or all rights or obligations with respect thereto.

9. **Severability.** In the event that any provision hereof is deemed to be invalid by reason of the operation of any law or by reason of the interpretation placed thereon by any court, this Guaranty shall be construed as not containing such provision, and the invalidity of such provision shall not affect other provisions hereof which are otherwise lawful and valid and shall remain in full force and effect.

10. **Notices.** Any notice or other communication required or permitted to be given pursuant to this Guaranty or by applicable law shall be in writing and shall be deemed received (a) on the date delivered if delivered in person to the person or department specified below, (b) three (3) days after the date deposited in the U.S. Mail, certified or registered, with return receipt requested, or (c) one (1) day following the date deposited with Federal Express or other national overnight carrier, and, in each case, shall be addressed as follows: If to Borrowers:

If to Guarantor:

AdCare Health Systems, Inc.  
Two Buckhead Plaza  
3050 Peachtree Road NW, Suite 355  
Atlanta, Georgia 30305

with a copy to:

Ellen W. Smith, Esq.  
Holt Ney Zatcoff & Wasserman, LLP  
100 Galleria Parkway, Suite 1800  
Atlanta, Georgia 30339  
Fax: (770) 956-1490

If to Lender:

Eric Smith  
Contemporary Healthcare Capital, LLC  
1040 Broad Street  
Suite 103

Shrewsbury, New Jersey 07702

with a copy to:

Law Offices of Thomas K. Slattery, P.L.L.C.  
1250 24<sup>th</sup> Street NW, Suite 300  
Washington, DC 20037

Any party may change its address to another single address by notice given as herein provided, except that any change of address must be actually received in order to be effective.

11. **Waivers.** The failure by the Lender at any time or times hereafter to require strict performance by Guarantor of any of the provisions, warranties, terms, and conditions contained herein or in any other agreement, document, or instrument now or hereafter executed by Guarantor and delivered to the Lender shall not waive, affect, or diminish any right of the Lender hereafter to demand strict compliance or performance therewith and with respect to any other provisions, warranties, terms, and conditions contained in such agreements, documents, and instruments, and any waiver of any Default or Event of Default shall not waive or affect any other Default or Event of Default, whether prior or subsequent thereto and whether of the same or a different type. None of the warranties, conditions, provisions, and terms contained in this Guaranty or in any agreement, document, or instrument now or hereafter executed by Guarantor and delivered to the Lender shall be deemed to have been waived by any act or knowledge of the Lender, its agents, officers, or employees, but a waiver, in order to be effective, must be by an instrument in writing, signed by an officer of the Lender, and directed to the Guarantor specifying such waiver.

12. **Expenses.** Guarantor guarantees payment of all costs and expenses described in the Loan Agreement, and the same shall constitute additional obligations of the Guarantor payable on demand.

13. **Singular and Plural.** Singular terms shall include the plural forms, and vice versa.

14. **Entire Agreement.** This Guaranty constitutes the entire agreement of Guarantor and Lender with respect to the subject matter hereof and supersedes all prior agreements and understandings both oral and written, between the parties with respect to the subject matter hereof.

15. **Jurisdiction.** THE VALIDITY, INTERPRETATION, ENFORCEMENT, AND EFFECT OF THIS GUARANTY SHALL BE GOVERNED BY AND CONSTRUED ACCORDING TO THE LAWS OF THE STATE OF NEW JERSEY. THE LENDER' S PRINCIPAL PLACE OF BUSINESS IS LOCATED IN THE STATE OF NEW JERSEY, AND GUARANTOR AGREES THAT THIS GUARANTY SHALL BE HELD BY LENDER AT SUCH PRINCIPAL PLACE OF BUSINESS, AND THE HOLDING OF THIS GUARANTY BY LENDER THEREAT SHALL CONSTITUTE SUFFICIENT

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MINIMUM CONTACTS OF GUARANTOR WITH THE STATE OF NEW JERSEY FOR THE PURPOSE OF CONFERRING JURISDICTION UPON THE FEDERAL AND STATE COURTS PRESIDING IN SUCH STATE AND THE COUNTY OF LENDER' S RESIDENCE. THE GUARANTOR CONSENTS THAT ANY LEGAL ACTION OR PROCEEDING ARISING HEREUNDER MAY BE BROUGHT EXCLUSIVELY IN SUCH COURTS AND ASSENTS AND SUBMITS TO THE PERSONAL JURISDICTION OF ANY SUCH COURTS IN ANY SUCH ACTION OR PROCEEDING.

16. **Jury Trial Waiver.** EACH OF GUARANTOR AND LENDER BY ITS ACCEPTANCE OF THIS GUARANTY HEREBY WAIVE ANY RIGHT TO TRIAL BY JURY ON ANY CLAIM, COUNTERCLAIM, SETOFF, DEMAND, ACTION, OR CAUSE OF ACTION (A) ARISING OUT OF OR IN ANY WAY RELATED TO THIS GUARANTY OR THE LOAN, OR (B) IN ANY WAY CONNECTED WITH OR PERTAINING OR RELATED TO OR INCIDENTAL TO ANY DEALINGS OF LENDER AND/OR BORROWERS AND GUARANTOR WITH RESPECT TO THE LOAN DOCUMENTS OR IN CONNECTION WITH THIS GUARANTY OR THE EXERCISE OF ANY PARTY' S RIGHTS AND REMEDIES UNDER THIS GUARANTY OR OTHERWISE, OR THE CONDUCT OR THE RELATIONSHIP OF THE PARTIES HERETO, IN ALL OF THE FOREGOING CASES WHETHER NOW EXISTING OR HEREAFTER ARISING AND WHETHER SOUNDING IN CONTRACT, TORT, OR OTHERWISE. EACH OF GUARANTOR AND LENDER BY ITS ACCEPTANCE OF THIS GUARANTY AGREES THAT EITHER PARTY MAY FILE A COPY OF THIS GUARANTY WITH ANY COURT AS WRITTEN EVIDENCE OF THE KNOWING, VOLUNTARY, AND BARGAINED-FOR AGREEMENT OF GUARANTOR AND LENDER IRREVOCABLY TO WAIVE THEIR RIGHTS TO TRIAL BY JURY AS AN INDUCEMENT OF LENDER TO MAKE THE LOAN AND OF GUARANTOR TO EXECUTE AND DELIVER THIS GUARANTY, AND THAT, TO THE EXTENT PERMITTED BY APPLICABLE LAW, ANY DISPUTE OR CONTROVERSY WHATSOEVER BETWEEN GUARANTOR AND LENDER SHALL INSTEAD BE TRIED IN A COURT OF COMPETENT JURISDICTION BY A JUDGE SITTING WITHOUT A JURY.

[SIGNATURES BEGIN ON NEXT PAGE]

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IN WITNESS WHEREOF, the Guarantor has executed this Guaranty as of the day and year first above written.

ADCARE HEALTH SYSTEMS, INC., an Ohio corporation

By: /s/ Christopher F. Brogdon  
Name: Christopher F. Brogdon  
Title: Vice Chairman and Chief Acquisitions Officer

STATE OF )

[SEAL]

COUNTY OF )

I, [Illegible], a Notary Public in and for said County in said State, hereby certify that Chistropher F. Brogdon, whose name as the Vice Chairman and Chief Acquisitions Officer of AdCare Health Systems, Inc., a Georgia corporation, is signed to the foregoing instrument, and who is known to me, acknowledged before me on this day that being informed of the contents of said instrument, he as such officer and with full authority, executed the same voluntarily for and as the act of said corporation.

Given under my hand and official seal this 17th day of August, 2012.

/s/ [Illegible]  
NOTARY PUBLIC

[SEAL]

My Commission Expires:

SIGNATURE PAGE TO CORPORATE GUARANTY - AHS – ADCARE - AR

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**GUARANTY OF PAYMENT AND PERFORMANCE**

**THIS GUARANTY OF PAYMENT AND PERFORMANCE** (this “**Guaranty**”) made as of August 17, 2012, by **ADCARE HEALTH SYSTEMS, INC.**, an Ohio corporation (the “**Guarantor**”) in favor of **CONTEMPORARY HEALTHCARE FUND I, L.P.**, a Delaware limited partnership (the “**Lender**”).

**RECITALS:**

Pursuant to a Loan Agreement dated the date hereof (as the same may hereafter be amended, the “**Loan Agreement**”) between **CSCC PROPERTY HOLDINGS, LLC**, a Georgia limited liability company, and **CSCC NURSING, LLC**, a Georgia limited liability company (collectively, the “**Borrowers**”) and Lender, Lender agreed to make a loan to the Borrowers in the principal amount of up to Six Hundred Thousand and No/100 Dollars (\$600,000.00) (the “**Loan**”). As one of the conditions for the Loan, Lender required that the Guarantor guarantee the Loan Obligations (as hereinafter defined), now existing or hereafter incurred, owing to the Lender pursuant to the Loan Documents (as defined in the Loan Agreement). Capitalized terms used herein and not otherwise defined shall have the meanings set forth in the Loan Agreement. Guarantor is the parent entity of the Borrowers and will receive direct and indirect benefits from the Loan, which benefits, among others, provide adequate consideration for them to enter into this Guaranty.

**AGREEMENT**

**NOW, THEREFORE**, in consideration of the foregoing Recitals, and in order to induce the Lender to continue to make the Loan, and as security for the Loan Obligations, Guarantor agrees and covenants with Lender and represents and warrants to Lender as follows:

1. **Guarantee of Loan Obligations.** The Guarantor hereby unconditionally, jointly and severally with Borrowers and any other, guarantor of the Loan guarantees to the Lender the following (collectively, the “**Loan Obligations**”) (a) the due, regular, and punctual payment of the principal (including capitalized interest that is added to principal), interest, fees, premiums, expenses, and other charges pursuant to the Note executed by the Borrowers evidencing the Loan, as the same may hereafter be extended, renewed, modified, or amended (the “**Note**”), (b) the payment of all fees, premiums, expenses, charges, and other amounts from time to time owing to Lender pursuant to the Loan Agreement and other Loan Documents, and (c) the performance of all covenants, agreements, and other obligations from time to time owing to, or for the benefit of, Lender pursuant to the Loan Documents, including, but not limited to, the indemnity obligations under the Loan Documents; (d) upon the failure of the Borrowers timely to pay or perform any of the foregoing Loan Obligations as provided in the Loan Documents, the payment of all reasonable costs and expenses incurred by Lender in paying or performing such Loan Obligations (but Lender shall not be required to pay or perform such Loan Obligations); and (e) all reasonable costs, attorneys’ fees, and expenses that may be incurred by the Lender by

reason of an Event of Default as provided in the Loan Documents, including reasonable fees and expenses in any appellate or bankruptcy proceedings.

Upon any Event of Default pursuant to any of the Loan Documents, the Guarantor unconditionally promises to pay to the Lender such amounts as are necessary to cure the Event of Default, or at the option of the Lender in the event Lender has elected to accelerate the Loan Obligations as a result thereof, the Guarantor agrees to pay the outstanding Loan Obligations in full.

This Guaranty is unconditional except as expressly set forth herein, and the Guarantor agrees that the Lender, upon the occurrence of an Event of Default pursuant to any of the Loan Documents, shall not be required to assert any claim or cause of action against the Borrowers before asserting any claim or cause of action against the Guarantor under this Guaranty. The Guarantor further agrees that the Lender shall not be required to pursue or foreclose on any Collateral that it may receive from the Borrowers, any guarantor, or others as security for any of the Loan Obligations before making a claim or asserting a cause of action against the Guarantor under this Guaranty.

The failure of the Lender to perfect its security interest in any of the Collateral as set forth in any of the Loan Documents or any other collateral now or hereafter securing all or any part of the Loan Obligations shall not release the Guarantor from its liabilities and obligations hereunder.

Notice of acceptance of this Guaranty and of any Default or Event of Default is hereby waived by the Guarantor, except to the extent notice is otherwise expressly required by the Loan Documents. Presentment, protest, demand, and notice of protest and demand, and notice of receipt of any and all Collateral, and of the exercise of possessory remedies or foreclosure on any and all Collateral received by the Lender from the Borrowers or the Guarantor are hereby waived. To the extent any Collateral from time to time consists of accounts owing to Borrowers, all settlements, compromises, compositions, accounts stated, and agreed balances in good faith between any primary or secondary obligors on any such accounts shall be binding upon the Guarantor. With respect to the amounts now or hereafter due under this Guaranty, the Guarantor waives, to the extent permitted by law, all rights of exemption of property from levy or sale under execution or other process for the collection of debts under the laws or Constitution of the United States or any state thereof.

This Guaranty shall not be affected, modified, or impaired by the voluntary or involuntary liquidation, dissolution, sale, or other disposition of all or substantially all of the assets, marshalling of assets and liabilities, receivership, insolvency, bankruptcy, assignment for the benefit of creditors, reorganization, arrangements, composition with creditors or readjustment of, or other similar proceedings affecting the Borrowers or any guarantor, or any of the assets belonging to any of them, nor shall this Guaranty be affected, modified, or impaired by the invalidity of the Note or any of the other Loan Documents.

Without notice to the Guarantor, without the consent of the Guarantor, and without affecting or limiting the Guarantor's liability hereunder, the Lender may:

- (a) grant the Borrowers extensions of time for payment of the Loan Obligations or any part hereof;
- (b) renew any of the Loan Obligations;
- (c) grant the Borrowers extensions of time for performance of agreements or other indulgences;
- (d) at any time release any or all of the Collateral, or any mortgage, deed of trust, or security interest in any Collateral, that now or hereafter secures any of the Loan Obligations;
- (e) compromise, settle, release, or terminate any or all of the obligations, covenants, or agreements of the Borrowers under the Note or other Loan Documents;
- (f) at any time release any one or more other guarantors from their guarantees of any of the Loan Obligations;

and

(g) modify or amend any obligation, covenant, or agreement of the Borrowers as set forth in the Note or any of the other Loan Documents (and such amendments shall nevertheless be binding upon the Guarantor); provided no increase in the principal amount of the Loan will be binding upon the Guarantor unless it has consented to such increase unless such increase is made pursuant to Section 2.1(b) of the Loan Agreement.

This Guaranty shall continue to be effective, or be reinstated, as the case may be, if at any time any whole or partial payment or performance of any Loan Obligations is or is sought to be rescinded or must otherwise be restored or returned by the Lender upon the insolvency, bankruptcy, dissolution, liquidation, or reorganization of the Borrowers, the Guarantor or any guarantor upon or as a result of the appointment of a receiver, intervenor, or conservator of, or trustee or similar officer for, the Borrowers, the Guarantor or any guarantor of or for any substantial part of its property, or otherwise, all as though such payments and performance had not been made and as though this Guaranty had not expired or been terminated. This Guaranty shall not be affected in any way by the transfer or other disposition of any of the Collateral described in and granted to Lender pursuant to the Loan Documents.

2. **Representations and Warranties of the Guarantor.** To induce the Lender to make the Loan to Borrowers, Guarantor represents and warrants to the Lender as follows:

(a) **Power to Incur Obligations.** Guarantor has full power and unrestricted right to enter into this Guaranty and to incur the obligations provided for herein, all of which have been duly authorized by all necessary corporate action of Guarantor.

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(b) **Existence, Power and Qualification.** Guarantor is a limited liability company duly organized, in good standing and validly existing under the laws of the state of its formation as set forth in the introductory paragraph of this Agreement, has the power to own its properties and to carry on its business as is now being conducted and to execute and deliver this Guaranty, and is duly qualified to do business and is in good standing in every jurisdiction in which the character of the properties owned by it or in which the transaction of its business makes its qualification necessary.

(c) **Conflicts.** This Guaranty does not violate, conflict with, or constitute any default under the operating agreement of Guarantor or any decree, or judgment by which Guarantor is bound or affected, and to the best of Guarantor's knowledge, does not constitute a material violation of any agreement or instrument binding upon Guarantor.

(d) **Pending Matters.** No action or investigation is pending or, to the best of Guarantor's knowledge, threatened before or by any state or federal court or administrative agency which would reasonably be expected to result in any material adverse change in the financial condition, operations, or prospects of Guarantor. Guarantor is not in violation of any agreement, the violation of which would reasonably be expected to have a materially adverse effect on Guarantor's business or assets, and Guarantor is not in violation of any order, judgment, or decree of any state or federal court or administrative agency by which Guarantor is bound or affected.

(e) **Financial Statements Accurate.** All financial statements heretofore or hereafter provided by the Guarantor are or will, at the time of the delivery thereof be, true and complete in all material respects as of their respective dates and fairly present the financial condition of Guarantor, and there are no known liabilities, direct or indirect, fixed or contingent, as of the respective dates of such statements which are not or will not, at the time of the delivery thereof, be reflected therein or in the notes thereto or in a written certificate delivered with such statements. There has been no material adverse change in the financial condition, operations, or prospects of Guarantor since the dates of such statements except as fully disclosed in writing with the delivery of such statements.

(f) **No Defaults or Restrictions.** Guarantor is not in default under any agreement or instrument that causes or would have a material adverse effect on the business, properties, and financial operations or condition of Guarantor.



(g) **Payment of Taxes and Employee Benefits.** Guarantor has filed all federal, state, and local tax returns which are required to be filed and has paid, or made adequate provision for the payment of, all taxes which have or may become due pursuant to said returns or to assessments received by Guarantor and has made all required payments to employee benefit plans.

(h) **Disclosure.** Neither this Guaranty nor any other document, financial statement, credit information, certificate, or statement required herein or otherwise furnished to Lender by Guarantor in connection with the Loan or this Guaranty contains any untrue, incorrect,

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or misleading statement of material fact. All representations and warranties made herein or any certificate or other document delivered to Lender by or on behalf of Guarantor pursuant to or in connection with this Guaranty shall be deemed to have been relied upon by Lender notwithstanding any investigation heretofore or hereafter made by Lender or on its behalf, and shall survive the delivery of this Guaranty.

(i) **ERISA.** Guarantor is in compliance with all applicable provisions of the Employee Retirement Income Security Act of 1974, as amended (“ERISA”).

3. **Affirmative Covenants of the Guarantor.** Guarantor covenants and agrees that so long as the Loan Obligations are outstanding, Guarantor shall comply with each of the following affirmative covenants:

(a) **Payment of Loan/Performance of Loan Obligations.** Duly and punctually pay or cause to be paid the principal and interest of the Note in accordance with its terms and duly and punctually pay or cause to be paid or performed all other Loan Obligations.

(b) **Payment of Taxes.** Pay and discharge all taxes, assessments, and governmental charges or levies imposed upon the Guarantor, including, without limitation, all current tax liabilities of all kinds, all required withholdings of income taxes of employees and all required old age and unemployment contributions.

(c) **Reporting Requirements.** From time to time upon request, furnish to Lender such information regarding the business affairs, finances, and conditions of the Guarantor and its properties in such detail as the Lender reasonably may request, including tax returns; without limiting the foregoing, Guarantor will furnish to Lender financial statements as and when required by the Loan Agreement. All financial statements shall be provided in the form and at the times set forth in the Loan Agreement.

(d) **Payment of Indebtedness.** Pay or cause to be paid duly and punctually all principal and interest of any material Indebtedness of the Guarantor to its creditors, and comply with and perform all conditions, terms, and obligations of the notes or other instruments evidencing such indebtedness and any mortgages, deeds of trust, security agreements, and other instruments evidencing or securing such indebtedness. Without limiting anything herein, “material” Indebtedness shall include, without limitation, any Indebtedness which is secured by or becomes subject to any Lien. Guarantor may contest any Indebtedness in good faith and shall not be in violation of this covenant during the period of any such contest provided that execution against any property of the Guarantor must have been effectively stayed and reserves adequate for payment must have been established.

(e) **Notice of Loss.** Notify Lender of any event causing a loss or reduction in value of the Guarantor’s assets which has a material adverse effect on the Guarantor’s net worth.

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(f) **Maintenance of Existence.** Maintain its corporate existence, and, in each jurisdiction in which the character of the property owned by it or in which the transaction of its business makes qualification necessary, maintain qualification and good standing.

4. **Negative Covenants of the Guarantor.** Except as permitted by the Loan Agreement, so long as any of the Loan Obligations are outstanding, Guarantor agrees that it shall not, without Lender's prior written approval:

(a) **Change in Business.** Make any material change in the nature of its business as it is being conducted as of the date hereof which would reasonably be expected to materially and adversely affect its ability to perform its obligations pursuant to this Guaranty.

(b) **Changes in Accounting.** Change its method of accounting to one inconsistent with the method heretofore used by Guarantor.

(c) **Consolidation or Transfer of Substantially all of its Assets.** Enter into any merger, consolidation, or similar transaction with any entity other than Borrowers or any other subsidiary of Borrowers which is a guarantor of the Loan, or sell, assign, lease, or otherwise dispose of (whether in one transaction or in a series of transactions) all or substantially all of its assets (whether now or hereafter acquired) other than to Borrowers or any other subsidiary of Borrowers which is a guarantor of the Loan or unless any such disposition is of property other than the Collateral and is in the ordinary course of business for a full and fair consideration and does not violate any covenant of the Loan Agreement.

(d) **ERISA Funding and Termination.** Permit the funding requirements of ERISA with respect to any employee plan of Guarantor to be less than the minimum required by ERISA at any time, or any employee plan of Guarantor to be subject to involuntary termination proceedings at any time.

(e) **Transfer of Ownership Interests.** Permit any transfer of the ownership interests or stock of Guarantor or change in management of Guarantor that would violate any covenant of the Loan Agreement.

5. **Events of Default.** Guarantor's violation of any covenant set forth in Section 4 hereof, or Guarantor's failure to properly and timely perform or observe any covenant or condition set forth in this Guaranty (other than those in Section 4) which is not cured within any applicable cure period as set forth herein or, if no cure period is specified therefor, which is not cured within thirty (30) days of Lender's notice to Guarantor of such default (provided such cure period shall be extended an additional sixty (60) days if Guarantor commences a cure within such initial thirty (30) days, provides evidence thereof to Lender and diligently pursues a cure), or the falsity in any material respect of any representation or warranty herein or in any financial statement, certificate, or other information heretofore or hereafter provided by Guarantor to Lender, shall constitute an "**Event of Default**" hereunder and under each of the Loan Documents. The foregoing provision or any other provision requiring or providing for notice or demand from Lender is deemed eliminated if Lender is prevented from giving such notice or

demand by bankruptcy or other applicable law, and the Event of Default shall occur upon the occurrence of such event or condition if not cured within any applicable period measured from the occurrence of such event or condition rather than from notice or demand.

6. **Waiver and Subordination.** Guarantor expressly waives any right to payment arising by virtue of any subrogation or indemnification upon payment by Guarantor of amounts due from Borrowers to Lender, and Guarantor expressly subordinates any other rights to payment of indebtedness owing from Borrowers to Guarantor, whether now existing or hereafter arising, to the prior right of Lender to receive or require payment in full of the Loan Obligations, until such time as the Loan Obligations are fully paid (including interest accruing on the Note after any petition under the Bankruptcy Code, which post-petition interest Guarantor agrees shall remain a

claim that is prior and superior to any claim of Guarantor notwithstanding any contrary practice, custom, or ruling in proceedings under the Bankruptcy Code generally) and such payments are final and not subject to refund or rescission under bankruptcy or other applicable law. Furthermore, so long as an Event of Default exists under the Loan Documents, Guarantor agrees not to accept any payment or satisfaction of any kind of indebtedness of Borrowers to the Guarantor or any security for such indebtedness until such time as the Loan Obligations are fully paid. If Guarantor should receive any such payment, satisfaction or security for any indebtedness of Borrowers to the Guarantor, the Guarantor agrees to deliver the same promptly to Lender in the form received, endorsed, or assigned as may be appropriate for application on account of, or as security for, the Loan Obligations and until so delivered, agrees to hold the same in trust for Lender.

7. **Successors and Assigns.** This Guaranty shall be binding upon, and inure to the benefit of, the parties hereto and their respective heirs, legal representatives, successors, and assigns.

8. **Transfer of Rights under the Guaranty and the Loan Documents.**

(a) **Transfer by Lender.** Subject to any limitations set forth in the Loan Agreement, Lender may, at any time, sell, transfer or assign any of the Loan Documents, and any or all servicing rights with respect thereto, or grant participations therein or issue securities evidencing a beneficial interest in a rated or unrated public offering or private placement (the “**Securities**”) to any affiliate of Lender or to the Small Business Administration. Lender may forward to each purchaser, transferee, assignee, servicer, participant or investor in such Securities or any credit rating agency rating such Securities (the foregoing entities hereinafter collectively referred to as the “**Investor**”) and each prospective Investor, all documents and information which Lender now has or may hereafter acquire relating to Guarantor, whether furnished by Borrowers, Guarantor or otherwise, as Lender determines necessary or desirable. Guarantor agrees, upon request of Lender, to cooperate with Lender in connection with any transfer made or any Securities created pursuant to this Section 8(a) provided there is no material financial or other burden to Guarantor of doing so and provided such cooperation does not require an amendment to this Guaranty which would in any manner increase the obligations of Guarantor hereunder. Guarantor shall also furnish and Guarantor hereby consents, subject to Lender’s obligations hereunder, to Lender furnishing to such Investors or such prospective

Investors any and all information concerning the financial condition of Guarantor as provided for in this Section 8(a) in connection with any sale, transfer or participation interest. Notwithstanding the foregoing, in the event that Lender delivers any such information to a prospective Investor, Lender will notify Guarantor to such effect.

(b) **Transfer by Guarantor.** Without the prior written consent of Lender, which may be withheld in Lender’s sole discretion, Guarantor may not, at any time, sell, transfer or assign this Guaranty or any of the other Loan Documents to which Guarantor is a party or any of the Loan Documents to which Guarantor is a party or is otherwise a guarantor, and any or all rights or obligations with respect thereto.

9. **Severability.** In the event that any provision hereof is deemed to be invalid by reason of the operation of any law or by reason of the interpretation placed thereon by any court, this Guaranty shall be construed as not containing such provision, and the invalidity of such provision shall not affect other provisions hereof which are otherwise lawful and valid and shall remain in full force and effect.

10. **Notices.** Any notice or other communication required or permitted to be given pursuant to this Guaranty or by applicable law shall be in writing and shall be deemed received (a) on the date delivered if delivered in person to the person or department specified below, (b) three (3) days after the date deposited in the U.S. Mail, certified or registered, with return receipt requested, or (c) one (1) day following the date deposited with Federal Express or other national overnight carrier, and, in each case, shall be addressed as follows: If to Borrowers:

If to Guarantor:

AdCare Health Systems, Inc.  
Two Buckhead Plaza  
3050 Peachtree Road NW, Suite 355  
Atlanta, Georgia 30305

with a copy to:

Ellen W. Smith, Esq.  
Holt Ney Zatzoff & Wasserman, LLP  
100 Galleria Parkway, Suite 1800  
Atlanta, Georgia 30339  
Fax: (770) 956-1490

If to Lender:

Eric Smith  
Contemporary Healthcare Capital, LLC  
1040 Broad Street  
Suite 103

Shrewsbury, New Jersey 07702

with a copy to:

Law Offices of Thomas K. Slattery, P.L.L.C.  
1250 24<sup>th</sup> Street NW, Suite 300  
Washington, DC 20037

Any party may change its address to another single address by notice given as herein provided, except that any change of address must be actually received in order to be effective.

11. **Waivers.** The failure by the Lender at any time or times hereafter to require strict performance by Guarantor of any of the provisions, warranties, terms, and conditions contained herein or in any other agreement, document, or instrument now or hereafter executed by Guarantor and delivered to the Lender shall not waive, affect, or diminish any right of the Lender hereafter to demand strict compliance or performance therewith and with respect to any other provisions, warranties, terms, and conditions contained in such agreements, documents, and instruments, and any waiver of any Default or Event of Default shall not waive or affect any other Default or Event of Default, whether prior or subsequent thereto and whether of the same or a different type. None of the warranties, conditions, provisions, and terms contained in this Guaranty or in any agreement, document, or instrument now or hereafter executed by Guarantor and delivered to the Lender shall be deemed to have been waived by any act or knowledge of the Lender, its agents, officers, or employees, but a waiver, in order to be effective, must be by an instrument in writing, signed by an officer of the Lender, and directed to the Guarantor specifying such waiver.

12. **Expenses.** Guarantor guarantees payment of all costs and expenses described in the Loan Agreement, and the same shall constitute additional obligations of the Guarantor payable on demand.

13. **Singular and Plural.** Singular terms shall include the plural forms, and vice versa.

14. **Entire Agreement.** This Guaranty constitutes the entire agreement of Guarantor and Lender with respect to the subject matter hereof and supersedes all prior agreements and understandings both oral and written, between the parties with respect to the subject matter hereof.

15. **Jurisdiction.** THE VALIDITY, INTERPRETATION, ENFORCEMENT, AND EFFECT OF THIS GUARANTY SHALL BE GOVERNED BY AND CONSTRUED ACCORDING TO THE LAWS OF THE STATE OF NEW JERSEY. THE LENDER'S PRINCIPAL PLACE OF BUSINESS IS LOCATED IN THE STATE OF NEW JERSEY, AND GUARANTOR AGREES THAT THIS GUARANTY SHALL BE HELD BY LENDER AT SUCH PRINCIPAL PLACE OF BUSINESS, AND THE HOLDING OF THIS GUARANTY BY LENDER THEREAT SHALL CONSTITUTE SUFFICIENT

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MINIMUM CONTACTS OF GUARANTOR WITH THE STATE OF NEW JERSEY FOR THE PURPOSE OF CONFERRING JURISDICTION UPON THE FEDERAL AND STATE COURTS PRESIDING IN SUCH STATE AND THE COUNTY OF LENDER'S RESIDENCE. THE GUARANTOR CONSENTS THAT ANY LEGAL ACTION OR PROCEEDING ARISING HEREUNDER MAY BE BROUGHT EXCLUSIVELY IN SUCH COURTS AND ASSENTS AND SUBMITS TO THE PERSONAL JURISDICTION OF ANY SUCH COURTS IN ANY SUCH ACTION OR PROCEEDING.

16. **Jury Trial Waiver.** EACH OF GUARANTOR AND LENDER BY ITS ACCEPTANCE OF THIS GUARANTY HEREBY WAIVE ANY RIGHT TO TRIAL BY JURY ON ANY CLAIM, COUNTERCLAIM, SETOFF, DEMAND, ACTION, OR CAUSE OF ACTION (A) ARISING OUT OF OR IN ANY WAY RELATED TO THIS GUARANTY OR THE LOAN, OR (B) IN ANY WAY CONNECTED WITH OR PERTAINING OR RELATED TO OR INCIDENTAL TO ANY DEALINGS OF LENDER AND/OR BORROWERS AND GUARANTOR WITH RESPECT TO THE LOAN DOCUMENTS OR IN CONNECTION WITH THIS GUARANTY OR THE EXERCISE OF ANY PARTY'S RIGHTS AND REMEDIES UNDER THIS GUARANTY OR OTHERWISE, OR THE CONDUCT OR THE RELATIONSHIP OF THE PARTIES HERETO, IN ALL OF THE FOREGOING CASES WHETHER NOW EXISTING OR HEREAFTER ARISING AND WHETHER SOUNDING IN CONTRACT, TORT, OR OTHERWISE. EACH OF GUARANTOR AND LENDER BY ITS ACCEPTANCE OF THIS GUARANTY AGREES THAT EITHER PARTY MAY FILE A COPY OF THIS GUARANTY WITH ANY COURT AS WRITTEN EVIDENCE OF THE KNOWING, VOLUNTARY, AND BARGAINED-FOR AGREEMENT OF GUARANTOR AND LENDER IRREVOCABLY TO WAIVE THEIR RIGHTS TO TRIAL BY JURY AS AN INDUCEMENT OF LENDER TO MAKE THE LOAN AND OF GUARANTOR TO EXECUTE AND DELIVER THIS GUARANTY, AND THAT, TO THE EXTENT PERMITTED BY APPLICABLE LAW, ANY DISPUTE OR CONTROVERSY WHATSOEVER BETWEEN GUARANTOR AND LENDER SHALL INSTEAD BE TRIED IN A COURT OF COMPETENT JURISDICTION BY A JUDGE SITTING WITHOUT A JURY.

[SIGNATURES BEGIN ON NEXT PAGE]

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IN WITNESS WHEREOF, the Guarantor has executed this Guaranty as of the day and year first above written.

ADCARE HEALTH SYSTEMS, INC., an Ohio corporation

By: /s/ Christopher F. Brogdon  
Name: Christopher F. Brogdon  
Title: Vice Chairman and Chief Acquisitions Officer

STATE OF )

[SEAL]

COUNTY OF )

I, [Illegible], a Notary Public in and for said County in said State, hereby certify that Chistropher F. Brogdon, whose name as the Vice Chairman and Chief Acquisitions Officer of AdCare Health Systems, Inc., a Georgia corporation, is signed to the foregoing instrument, and who is known to me, acknowledged before me on this day that being informed of the contents of said instrument, he as such officer and with full authority, executed the same voluntarily for and as the act of said corporation.

Given under my hand and official seal this 17th day of August, 2012.

/s/ [Illegible]  
NOTARY PUBLIC

[SEAL]

My Commission Expires:

SIGNATURE PAGE TO CORPORATE GUARANTY - AHS – ADCARE - AR

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**GUARANTY OF PAYMENT AND PERFORMANCE**

THIS GUARANTY OF PAYMENT AND PERFORMANCE (this “**Guaranty**”) made as of August 17, 2012, by **ADCARE HEALTH SYSTEMS, INC.**, an Ohio corporation (the “**Guarantor**”) in favor of **CONTEMPORARY HEALTHCARE SENIOR LIEN FUND I, L.P.**, a Delaware limited partnership (the “**Lender**”).

**RECITALS:**

Pursuant to a Loan Agreement dated the date hereof (as the same may hereafter be amended, the “**Loan Agreement**”) between **CSCC PROPERTY HOLDINGS, LLC**, a Georgia limited liability company, and **CSCC NURSING, LLC**, a Georgia limited liability company (collectively, the “**Borrowers**”) and Lender, Lender agreed to make a loan to the Borrowers in the principal amount of Five Million and No/100 Dollars (\$5,000,000.00) (the “**Loan**”). As one of the conditions for the Loan, Lender required that the Guarantor guarantee the Loan Obligations (as hereinafter defined), now existing or hereafter incurred, owing to the Lender pursuant to the Loan Documents (as defined in the Loan Agreement). Capitalized terms used herein and not otherwise defined shall have the meanings set forth in the Loan Agreement. Guarantor is the parent entity of the Borrowers and will receive direct and indirect benefits from the Loan, which benefits, among others, provide adequate consideration for them to enter into this Guaranty.

**AGREEMENT**

**NOW, THEREFORE**, in consideration of the foregoing Recitals, and in order to induce the Lender to continue to make the Loan, and as security for the Loan Obligations, Guarantor agrees and covenants with Lender and represents and warrants to Lender as follows:

1. **Guarantee of Loan Obligations.** The Guarantor hereby unconditionally, jointly and severally with Borrowers and any other, guarantor of the Loan guarantees to the Lender the following (collectively, the “**Loan Obligations**”) (a) the due, regular, and punctual payment of the principal (including capitalized interest that is added to principal), interest, fees, premiums, expenses, and other charges pursuant to the Note executed by the Borrowers evidencing the Loan, as the same may hereafter be extended, renewed, modified, or amended (the “**Note**”), (b) the payment of all fees, premiums, expenses, charges, and other amounts from time to time owing to Lender pursuant to the Loan Agreement and other Loan Documents, and (c) the performance of all covenants, agreements, and other obligations from time to time owing to, or for the benefit of, Lender pursuant to the Loan Documents, including, but not limited to, the indemnity obligations under the Loan Documents; (d) upon the failure of the Borrowers timely to pay or perform any of the foregoing Loan Obligations as provided in the Loan Documents, the payment of all reasonable costs and expenses incurred by Lender in paying or performing such Loan Obligations (but Lender shall not be required to pay or perform such Loan Obligations); and (e) all reasonable costs, attorneys’ fees, and expenses that may be incurred by the Lender by

reason of an Event of Default as provided in the Loan Documents, including reasonable fees and expenses in any appellate or bankruptcy proceedings.

Upon any Event of Default pursuant to any of the Loan Documents, the Guarantor unconditionally promises to pay to the Lender such amounts as are necessary to cure the Event of Default, or at the option of the Lender in the event Lender has elected to accelerate the Loan Obligations as a result thereof, the Guarantor agrees to pay the outstanding Loan Obligations in full.

This Guaranty is unconditional except as expressly set forth herein, and the Guarantor agrees that the Lender, upon the occurrence of an Event of Default pursuant to any of the Loan Documents, shall not be required to assert any claim or cause of action against the Borrowers before asserting any claim or cause of action against the Guarantor under this Guaranty. The Guarantor further agrees that the Lender shall not be required to pursue or foreclose on any Collateral that it may receive from the Borrowers, any guarantor, or others as security for any of the Loan Obligations before making a claim or asserting a cause of action against the Guarantor under this Guaranty.

The failure of the Lender to perfect its security interest in any of the Collateral as set forth in any of the Loan Documents or any other collateral now or hereafter securing all or any part of the Loan Obligations shall not release the Guarantor from its liabilities and obligations hereunder.

Notice of acceptance of this Guaranty and of any Default or Event of Default is hereby waived by the Guarantor, except to the extent notice is otherwise expressly required by the Loan Documents. Presentment, protest, demand, and notice of protest and demand, and notice of receipt of any and all Collateral, and of the exercise of possessory remedies or foreclosure on any and all Collateral received by the Lender from the Borrowers or the Guarantor are hereby waived. To the extent any Collateral from time to time consists of accounts owing to Borrowers, all settlements, compromises, compositions, accounts stated, and agreed balances in good faith between any primary or secondary obligors on any such accounts shall be binding upon the Guarantor. With respect to the amounts now or hereafter due under this Guaranty, the Guarantor waives, to the extent permitted by law, all rights of exemption of property from levy or sale under execution or other process for the collection of debts under the laws or Constitution of the United States or any state thereof.

This Guaranty shall not be affected, modified, or impaired by the voluntary or involuntary liquidation, dissolution, sale, or other disposition of all or substantially all of the assets, marshalling of assets and liabilities, receivership, insolvency, bankruptcy, assignment for the benefit of creditors, reorganization, arrangements, composition with creditors or readjustment of, or other similar proceedings affecting the Borrowers or any guarantor, or any of the assets belonging to any of them, nor shall this Guaranty be affected, modified, or impaired by the invalidity of the Note or any of the other Loan Documents.

Without notice to the Guarantor, without the consent of the Guarantor, and without affecting or limiting the Guarantor's liability hereunder, the Lender may:

- (a) grant the Borrowers extensions of time for payment of the Loan Obligations or any part hereof;
- (b) renew any of the Loan Obligations;
- (c) grant the Borrowers extensions of time for performance of agreements or other indulgences;
- (d) at any time release any or all of the Collateral, or any mortgage, deed of trust, or security interest in any Collateral, that now or hereafter secures any of the Loan Obligations;
- (e) compromise, settle, release, or terminate any or all of the obligations, covenants, or agreements of the Borrowers under the Note or other Loan Documents;
- (f) at any time release any one or more other guarantors from their guarantees of any of the Loan Obligations;

and



(g) modify or amend any obligation, covenant, or agreement of the Borrowers as set forth in the Note or any of the other Loan Documents (and such amendments shall nevertheless be binding upon the Guarantor); provided no increase in the principal amount of the Loan will be binding upon the Guarantor unless it has consented to such increase unless such increase is made pursuant to Section 2.1(b) of the Loan Agreement.

This Guaranty shall continue to be effective, or be reinstated, as the case may be, if at any time any whole or partial payment or performance of any Loan Obligations is or is sought to be rescinded or must otherwise be restored or returned by the Lender upon the insolvency, bankruptcy, dissolution, liquidation, or reorganization of the Borrowers, the Guarantor or any guarantor upon or as a result of the appointment of a receiver, intervenor, or conservator of, or trustee or similar officer for, the Borrowers, the Guarantor or any guarantor of or for any substantial part of its property, or otherwise, all as though such payments and performance had not been made and as though this Guaranty had not expired or been terminated. This Guaranty shall not be affected in any way by the transfer or other disposition of any of the Collateral described in and granted to Lender pursuant to the Loan Documents.

2. **Representations and Warranties of the Guarantor.** To induce the Lender to make the Loan to Borrowers, Guarantor represents and warrants to the Lender as follows:

(a) **Power to Incur Obligations.** Guarantor has full power and unrestricted right to enter into this Guaranty and to incur the obligations provided for herein, all of which have been duly authorized by all necessary corporate action of Guarantor.

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(b) **Existence, Power and Qualification.** Guarantor is a limited liability company duly organized, in good standing and validly existing under the laws of the state of its formation as set forth in the introductory paragraph of this Agreement, has the power to own its properties and to carry on its business as is now being conducted and to execute and deliver this Guaranty, and is duly qualified to do business and is in good standing in every jurisdiction in which the character of the properties owned by it or in which the transaction of its business makes its qualification necessary.

(c) **Conflicts.** This Guaranty does not violate, conflict with, or constitute any default under the operating agreement of Guarantor or any decree, or judgment by which Guarantor is bound or affected, and to the best of Guarantor's knowledge, does not constitute a material violation of any agreement or instrument binding upon Guarantor.

(d) **Pending Matters.** No action or investigation is pending or, to the best of Guarantor's knowledge, threatened before or by any state or federal court or administrative agency which would reasonably be expected to result in any material adverse change in the financial condition, operations, or prospects of Guarantor. Guarantor is not in violation of any agreement, the violation of which would reasonably be expected to have a materially adverse effect on Guarantor's business or assets, and Guarantor is not in violation of any order, judgment, or decree of any state or federal court or administrative agency by which Guarantor is bound or affected.

(e) **Financial Statements Accurate.** All financial statements heretofore or hereafter provided by the Guarantor are or will, at the time of the delivery thereof be, true and complete in all material respects as of their respective dates and fairly present the financial condition of Guarantor, and there are no known liabilities, direct or indirect, fixed or contingent, as of the respective dates of such statements which are not or will not, at the time of the delivery thereof, be reflected therein or in the notes thereto or in a written certificate delivered with such statements. There has been no material adverse change in the financial condition, operations, or prospects of Guarantor since the dates of such statements except as fully disclosed in writing with the delivery of such statements.

(f) **No Defaults or Restrictions.** Guarantor is not in default under any agreement or instrument that causes or would have a material adverse effect on the business, properties, and financial operations or condition of Guarantor.

(g) **Payment of Taxes and Employee Benefits.** Guarantor has filed all federal, state, and local tax returns which are required to be filed and has paid, or made adequate provision for the payment of, all taxes which have or may become due pursuant to said returns or to assessments received by Guarantor and has made all required payments to employee benefit plans.

(h) **Disclosure.** Neither this Guaranty nor any other document, financial statement, credit information, certificate, or statement required herein or otherwise furnished to Lender by Guarantor in connection with the Loan or this Guaranty contains any untrue, incorrect,

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or misleading statement of material fact. All representations and warranties made herein or any certificate or other document delivered to Lender by or on behalf of Guarantor pursuant to or in connection with this Guaranty shall be deemed to have been relied upon by Lender notwithstanding any investigation heretofore or hereafter made by Lender or on its behalf, and shall survive the delivery of this Guaranty.

(i) **ERISA.** Guarantor is in compliance with all applicable provisions of the Employee Retirement Income Security Act of 1974, as amended (“ERISA”).

3. **Affirmative Covenants of the Guarantor.** Guarantor covenants and agrees that so long as the Loan Obligations are outstanding, Guarantor shall comply with each of the following affirmative covenants:

(a) **Payment of Loan/Performance of Loan Obligations.** Duly and punctually pay or cause to be paid the principal and interest of the Note in accordance with its terms and duly and punctually pay or cause to be paid or performed all other Loan Obligations.

(b) **Payment of Taxes.** Pay and discharge all taxes, assessments, and governmental charges or levies imposed upon the Guarantor, including, without limitation, all current tax liabilities of all kinds, all required withholdings of income taxes of employees and all required old age and unemployment contributions.

(c) **Reporting Requirements.** From time to time upon request, furnish to Lender such information regarding the business affairs, finances, and conditions of the Guarantor and its properties in such detail as the Lender reasonably may request, including tax returns; without limiting the foregoing, Guarantor will furnish to Lender financial statements as and when required by the Loan Agreement. All financial statements shall be provided in the form and at the times set forth in the Loan Agreement.

(d) **Payment of Indebtedness.** Pay or cause to be paid duly and punctually all principal and interest of any material Indebtedness of the Guarantor to its creditors, and comply with and perform all conditions, terms, and obligations of the notes or other instruments evidencing such indebtedness and any mortgages, deeds of trust, security agreements, and other instruments evidencing or securing such indebtedness. Without limiting anything herein, “material” Indebtedness shall include, without limitation, any Indebtedness which is secured by or becomes subject to any Lien. Guarantor may contest any Indebtedness in good faith and shall not be in violation of this covenant during the period of any such contest provided that execution against any property of the Guarantor must have been effectively stayed and reserves adequate for payment must have been established.

(e) **Notice of Loss.** Notify Lender of any event causing a loss or reduction in value of the Guarantor’s assets which has a material adverse effect on the Guarantor’s net worth.

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(f) **Maintenance of Existence.** Maintain its corporate existence, and, in each jurisdiction in which the character of the property owned by it or in which the transaction of its business makes qualification necessary, maintain qualification and good standing.

4. **Negative Covenants of the Guarantor.** Except as permitted by the Loan Agreement, so long as any of the Loan Obligations are outstanding, Guarantor agrees that it shall not, without Lender's prior written approval:

(a) **Change in Business.** Make any material change in the nature of its business as it is being conducted as of the date hereof which would reasonably be expected to materially and adversely affect its ability to perform its obligations pursuant to this Guaranty.

(b) **Changes in Accounting.** Change its method of accounting to one inconsistent with the method heretofore used by Guarantor.

(c) **Consolidation or Transfer of Substantially all of its Assets.** Enter into any merger, consolidation, or similar transaction with any entity other than Borrowers or any other subsidiary of Borrowers which is a guarantor of the Loan, or sell, assign, lease, or otherwise dispose of (whether in one transaction or in a series of transactions) all or substantially all of its assets (whether now or hereafter acquired) other than to Borrowers or any other subsidiary of Borrowers which is a guarantor of the Loan or unless any such disposition is of property other than the Collateral and is in the ordinary course of business for a full and fair consideration and does not violate any covenant of the Loan Agreement.

(d) **ERISA Funding and Termination.** Permit the funding requirements of ERISA with respect to any employee plan of Guarantor to be less than the minimum required by ERISA at any time, or any employee plan of Guarantor to be subject to involuntary termination proceedings at any time.

(e) **Transfer of Ownership Interests.** Permit any transfer of the ownership interests or stock of Guarantor or change in management of Guarantor that would violate any covenant of the Loan Agreement.

5. **Events of Default.** Guarantor's violation of any covenant set forth in Section 4 hereof, or Guarantor's failure to properly and timely perform or observe any covenant or condition set forth in this Guaranty (other than those in Section 4) which is not cured within any applicable cure period as set forth herein or, if no cure period is specified therefor, which is not cured within thirty (30) days of Lender's notice to Guarantor of such default (provided such cure period shall be extended an additional sixty (60) days if Guarantor commences a cure within such initial thirty (30) days, provides evidence thereof to Lender and diligently pursues a cure), or the falsity in any material respect of any representation or warranty herein or in any financial statement, certificate, or other information heretofore or hereafter provided by Guarantor to Lender, shall constitute an "**Event of Default**" hereunder and under each of the Loan Documents. The foregoing provision or any other provision requiring or providing for notice or demand from Lender is deemed eliminated if Lender is prevented from giving such notice or

demand by bankruptcy or other applicable law, and the Event of Default shall occur upon the occurrence of such event or condition if not cured within any applicable period measured from the occurrence of such event or condition rather than from notice or demand.

6. **Waiver and Subordination.** Guarantor expressly waives any right to payment arising by virtue of any subrogation or indemnification upon payment by Guarantor of amounts due from Borrowers to Lender, and Guarantor expressly subordinates any other rights to payment of indebtedness owing from Borrowers to Guarantor, whether now existing or hereafter arising, to the prior right of Lender to receive or require payment in full of the Loan Obligations, until such time as the Loan Obligations are fully paid (including interest accruing on the Note after any petition under the Bankruptcy Code, which post-petition interest Guarantor agrees shall remain a

claim that is prior and superior to any claim of Guarantor notwithstanding any contrary practice, custom, or ruling in proceedings under the Bankruptcy Code generally) and such payments are final and not subject to refund or rescission under bankruptcy or other applicable law. Furthermore, so long as an Event of Default exists under the Loan Documents, Guarantor agrees not to accept any payment or satisfaction of any kind of indebtedness of Borrowers to the Guarantor or any security for such indebtedness until such time as the Loan Obligations are fully paid. If Guarantor should receive any such payment, satisfaction or security for any indebtedness of Borrowers to the Guarantor, the Guarantor agrees to deliver the same promptly to Lender in the form received, endorsed, or assigned as may be appropriate for application on account of, or as security for, the Loan Obligations and until so delivered, agrees to hold the same in trust for Lender.

7. **Successors and Assigns.** This Guaranty shall be binding upon, and inure to the benefit of, the parties hereto and their respective heirs, legal representatives, successors, and assigns.

8. **Transfer of Rights under the Guaranty and the Loan Documents.**

(a) **Transfer by Lender.** Subject to any limitations set forth in the Loan Agreement, Lender may, at any time, sell, transfer or assign any of the Loan Documents, and any or all servicing rights with respect thereto, or grant participations therein or issue securities evidencing a beneficial interest in a rated or unrated public offering or private placement (the “**Securities**”) to any affiliate of Lender or to the Small Business Administration. Lender may forward to each purchaser, transferee, assignee, servicer, participant or investor in such Securities or any credit rating agency rating such Securities (the foregoing entities hereinafter collectively referred to as the “**Investor**”) and each prospective Investor, all documents and information which Lender now has or may hereafter acquire relating to Guarantor, whether furnished by Borrowers, Guarantor or otherwise, as Lender determines necessary or desirable. Guarantor agrees, upon request of Lender, to cooperate with Lender in connection with any transfer made or any Securities created pursuant to this Section 8(a) provided there is no material financial or other burden to Guarantor of doing so and provided such cooperation does not require an amendment to this Guaranty which would in any manner increase the obligations of Guarantor hereunder. Guarantor shall also furnish and Guarantor hereby consents, subject to Lender’s obligations hereunder, to Lender furnishing to such Investors or such prospective

Investors any and all information concerning the financial condition of Guarantor as provided for in this Section 8(a) in connection with any sale, transfer or participation interest. Notwithstanding the foregoing, in the event that Lender delivers any such information to a prospective Investor, Lender will notify Guarantor to such effect.

(b) **Transfer by Guarantor.** Without the prior written consent of Lender, which may be withheld in Lender’s sole discretion, Guarantor may not, at any time, sell, transfer or assign this Guaranty or any of the other Loan Documents to which Guarantor is a party or any of the Loan Documents to which Guarantor is a party or is otherwise a guarantor, and any or all rights or obligations with respect thereto.

9. **Severability.** In the event that any provision hereof is deemed to be invalid by reason of the operation of any law or by reason of the interpretation placed thereon by any court, this Guaranty shall be construed as not containing such provision, and the invalidity of such provision shall not affect other provisions hereof which are otherwise lawful and valid and shall remain in full force and effect.

10. **Notices.** Any notice or other communication required or permitted to be given pursuant to this Guaranty or by applicable law shall be in writing and shall be deemed received (a) on the date delivered if delivered in person to the person or department specified below, (b) three (3) days after the date deposited in the U.S. Mail, certified or registered, with return receipt requested, or (c) one (1) day following the date deposited with Federal Express or other national overnight carrier, and, in each case, shall be addressed as follows: If to Borrowers:

If to Guarantor:

AdCare Health Systems, Inc.  
Two Buckhead Plaza  
3050 Peachtree Road NW, Suite 355  
Atlanta, Georgia 30305

with a copy to:

Ellen W. Smith, Esq.  
Holt Ney Zatzoff & Wasserman, LLP  
100 Galleria Parkway, Suite 1800  
Atlanta, Georgia 30339  
Fax: (770) 956-1490

If to Lender:

Eric Smith  
Contemporary Healthcare Capital, LLC  
1040 Broad Street  
Suite 103

Shrewsbury, New Jersey 07702

with a copy to:

Law Offices of Thomas K. Slattery, P.L.L.C.  
1250 24<sup>th</sup> Street NW, Suite 300  
Washington, DC 20037

Any party may change its address to another single address by notice given as herein provided, except that any change of address must be actually received in order to be effective.

11. **Waivers.** The failure by the Lender at any time or times hereafter to require strict performance by Guarantor of any of the provisions, warranties, terms, and conditions contained herein or in any other agreement, document, or instrument now or hereafter executed by Guarantor and delivered to the Lender shall not waive, affect, or diminish any right of the Lender hereafter to demand strict compliance or performance therewith and with respect to any other provisions, warranties, terms, and conditions contained in such agreements, documents, and instruments, and any waiver of any Default or Event of Default shall not waive or affect any other Default or Event of Default, whether prior or subsequent thereto and whether of the same or a different type. None of the warranties, conditions, provisions, and terms contained in this Guaranty or in any agreement, document, or instrument now or hereafter executed by Guarantor and delivered to the Lender shall be deemed to have been waived by any act or knowledge of the Lender, its agents, officers, or employees, but a waiver, in order to be effective, must be by an instrument in writing, signed by an officer of the Lender, and directed to the Guarantor specifying such waiver.

12. **Expenses.** Guarantor guarantees payment of all costs and expenses described in the Loan Agreement, and the same shall constitute additional obligations of the Guarantor payable on demand.

13. **Singular and Plural.** Singular terms shall include the plural forms, and vice versa.

14. **Entire Agreement.** This Guaranty constitutes the entire agreement of Guarantor and Lender with respect to the subject matter hereof and supersedes all prior agreements and understandings both oral and written, between the parties with respect to the subject matter hereof.

15. **Jurisdiction.** THE VALIDITY, INTERPRETATION, ENFORCEMENT, AND EFFECT OF THIS GUARANTY SHALL BE GOVERNED BY AND CONSTRUED ACCORDING TO THE LAWS OF THE STATE OF NEW JERSEY. THE LENDER' S PRINCIPAL PLACE OF BUSINESS IS LOCATED IN THE STATE OF NEW JERSEY, AND GUARANTOR AGREES THAT THIS GUARANTY SHALL BE HELD BY LENDER AT SUCH PRINCIPAL PLACE OF BUSINESS, AND THE HOLDING OF THIS GUARANTY BY LENDER THEREAT SHALL CONSTITUTE SUFFICIENT

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MINIMUM CONTACTS OF GUARANTOR WITH THE STATE OF NEW JERSEY FOR THE PURPOSE OF CONFERRING JURISDICTION UPON THE FEDERAL AND STATE COURTS PRESIDING IN SUCH STATE AND THE COUNTY OF LENDER' S RESIDENCE. THE GUARANTOR CONSENTS THAT ANY LEGAL ACTION OR PROCEEDING ARISING HEREUNDER MAY BE BROUGHT EXCLUSIVELY IN SUCH COURTS AND ASSENTS AND SUBMITS TO THE PERSONAL JURISDICTION OF ANY SUCH COURTS IN ANY SUCH ACTION OR PROCEEDING.

16. **Jury Trial Waiver.** EACH OF GUARANTOR AND LENDER BY ITS ACCEPTANCE OF THIS GUARANTY HEREBY WAIVE ANY RIGHT TO TRIAL BY JURY ON ANY CLAIM, COUNTERCLAIM, SETOFF, DEMAND, ACTION, OR CAUSE OF ACTION (A) ARISING OUT OF OR IN ANY WAY RELATED TO THIS GUARANTY OR THE LOAN, OR (B) IN ANY WAY CONNECTED WITH OR PERTAINING OR RELATED TO OR INCIDENTAL TO ANY DEALINGS OF LENDER AND/OR BORROWERS AND GUARANTOR WITH RESPECT TO THE LOAN DOCUMENTS OR IN CONNECTION WITH THIS GUARANTY OR THE EXERCISE OF ANY PARTY' S RIGHTS AND REMEDIES UNDER THIS GUARANTY OR OTHERWISE, OR THE CONDUCT OR THE RELATIONSHIP OF THE PARTIES HERETO, IN ALL OF THE FOREGOING CASES WHETHER NOW EXISTING OR HEREAFTER ARISING AND WHETHER SOUNDING IN CONTRACT, TORT, OR OTHERWISE. EACH OF GUARANTOR AND LENDER BY ITS ACCEPTANCE OF THIS GUARANTY AGREES THAT EITHER PARTY MAY FILE A COPY OF THIS GUARANTY WITH ANY COURT AS WRITTEN EVIDENCE OF THE KNOWING, VOLUNTARY, AND BARGAINED-FOR AGREEMENT OF GUARANTOR AND LENDER IRREVOCABLY TO WAIVE THEIR RIGHTS TO TRIAL BY JURY AS AN INDUCEMENT OF LENDER TO MAKE THE LOAN AND OF GUARANTOR TO EXECUTE AND DELIVER THIS GUARANTY, AND THAT, TO THE EXTENT PERMITTED BY APPLICABLE LAW, ANY DISPUTE OR CONTROVERSY WHATSOEVER BETWEEN GUARANTOR AND LENDER SHALL INSTEAD BE TRIED IN A COURT OF COMPETENT JURISDICTION BY A JUDGE SITTING WITHOUT A JURY.

[SIGNATURES BEGIN ON NEXT PAGE]

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IN WITNESS WHEREOF, the Guarantor has executed this Guaranty as of the day and year first above written.

ADCARE HEALTH SYSTEMS, INC., an Ohio corporation

By: /s/ Christopher F. Brogdon  
Name: Christopher F. Brogdon  
Title: Vice Chairman and Chief Acquisitions Officer

STATE OF )

[SEAL]

COUNTY OF )

I, [Illegible], a Notary Public in and for said County in said State, hereby certify that Chistrophe F. Brogdon, whose name as the Vice Chairman and Chief Acquisitions Officer of AdCare Health Systems, Inc., a Georgia corporation, is signed to the foregoing instrument, and who is known to me, acknowledged before me on this day that being informed of the contents of said instrument, he as such officer and with full authority, executed the same voluntarily for and as the act of said corporation.

Given under my hand and official seal this 17th day of August, 2012.

/s/ [Illegible]  
NOTARY PUBLIC

[SEAL]

My Commission Expires:

SIGNATURE PAGE TO CORPORATE GUARANTY - AHS – ADCARE - SENIOR

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**GUARANTY OF PAYMENT AND PERFORMANCE**

THIS GUARANTY OF PAYMENT AND PERFORMANCE (this “**Guaranty**”) made as of August 17, 2012, by **ADCARE OKLAHOMA MANAGEMENT, LLC**, a Georgia limited liability company (the “**Guarantor**”) in favor of **CONTEMPORARY HEALTHCARE SENIOR LIEN FUND I, L.P.**, a Delaware limited partnership (the “**Lender**”).

**RECITALS:**

Pursuant to a Loan Agreement dated the date hereof (as the same may hereafter be amended, the “**Loan Agreement**”) between **CSCC PROPERTY HOLDINGS, LLC**, a Georgia limited liability company, and **CSCC NURSING, LLC**, a Georgia limited liability company (collectively, the “**Borrowers**”) and Lender, Lender agreed to make a loan to the Borrowers in the principal amount of Five Million and No/100 Dollars (\$5,000,000.00) (the “**Loan**”). As one of the conditions for the Loan, Lender required that the Guarantor guarantee the Loan Obligations (as hereinafter defined), now existing or hereafter incurred, owing to the Lender pursuant to the Loan Documents (as defined in the Loan Agreement). Capitalized terms used herein and not otherwise defined shall have the meanings set forth in the Loan Agreement. Guarantor is the manager of the facility being financed with the Loan and is an affiliated entity under common control and ownership with the Borrowers and will receive direct and indirect benefits from the Loan, which benefits, among others, provide adequate consideration for them to enter into this Guaranty.

**AGREEMENT**

**NOW, THEREFORE**, in consideration of the foregoing Recitals, and in order to induce the Lender to continue to make the Loan, and as security for the Loan Obligations, Guarantor agrees and covenants with Lender and represents and warrants to Lender as follows:

1. **Guarantee of Loan Obligations.** The Guarantor hereby unconditionally, jointly and severally with Borrowers and any other, guarantor of the Loan guarantees to the Lender the following (collectively, the “**Loan Obligations**”) (a) the due, regular, and punctual payment of the principal (including capitalized interest that is added to principal), interest, fees, premiums, expenses, and other charges pursuant to the Note executed by the Borrowers evidencing the Loan, as the same may hereafter be extended, renewed, modified, or amended (the “**Note**”), (b) the payment of all fees, premiums, expenses, charges, and other amounts from time to time owing to Lender pursuant to the Loan Agreement and other Loan Documents, and (c) the performance of all covenants, agreements, and other obligations from time to time owing to, or for the benefit of, Lender pursuant to the Loan Documents, including, but not limited to, the indemnity obligations under the Loan Documents; (d) upon the failure of the Borrowers timely to pay or perform any of the foregoing Loan Obligations as provided in the Loan Documents, the payment of all reasonable costs and expenses incurred by Lender in paying or performing such Loan Obligations (but Lender shall not be required to pay or perform such Loan Obligations);

and (e) all reasonable costs, attorneys’ fees, and expenses that may be incurred by the Lender by reason of an Event of Default as provided in the Loan Documents, including reasonable fees and expenses in any appellate or bankruptcy proceedings.

Upon any Event of Default pursuant to any of the Loan Documents, the Guarantor unconditionally promises to pay to the Lender such amounts as are necessary to cure the Event of Default, or at the option of the Lender in the event Lender has elected to accelerate the Loan Obligations as a result thereof, the Guarantor agrees to pay the outstanding Loan Obligations in full.



This Guaranty is unconditional except as expressly set forth herein, and the Guarantor agrees that the Lender, upon the occurrence of an Event of Default pursuant to any of the Loan Documents, shall not be required to assert any claim or cause of action against the Borrowers before asserting any claim or cause of action against the Guarantor under this Guaranty. The Guarantor further agrees that the Lender shall not be required to pursue or foreclose on any Collateral that it may receive from the Borrowers, any guarantor, or others as security for any of the Loan Obligations before making a claim or asserting a cause of action against the Guarantor under this Guaranty.

The failure of the Lender to perfect its security interest in any of the Collateral as set forth in any of the Loan Documents or any other collateral now or hereafter securing all or any part of the Loan Obligations shall not release the Guarantor from its liabilities and obligations hereunder.

Notice of acceptance of this Guaranty and of any Default or Event of Default is hereby waived by the Guarantor, except to the extent notice is otherwise expressly required by the Loan Documents. Presentment, protest, demand, and notice of protest and demand, and notice of receipt of any and all Collateral, and of the exercise of possessory remedies or foreclosure on any and all Collateral received by the Lender from the Borrowers or the Guarantor are hereby waived. To the extent any Collateral from time to time consists of accounts owing to Borrowers, all settlements, compromises, compositions, accounts stated, and agreed balances in good faith between any primary or secondary obligors on any such accounts shall be binding upon the Guarantor. With respect to the amounts now or hereafter due under this Guaranty, the Guarantor waives, to the extent permitted by law, all rights of exemption of property from levy or sale under execution or other process for the collection of debts under the laws or Constitution of the United States or any state thereof.

This Guaranty shall not be affected, modified, or impaired by the voluntary or involuntary liquidation, dissolution, sale, or other disposition of all or substantially all of the assets, marshalling of assets and liabilities, receivership, insolvency, bankruptcy, assignment for the benefit of creditors, reorganization, arrangements, composition with creditors or readjustment of, or other similar proceedings affecting the Borrowers or any guarantor, or any of the assets belonging to any of them, nor shall this Guaranty be affected, modified, or impaired by the invalidity of the Note or any of the other Loan Documents.

Without notice to the Guarantor, without the consent of the Guarantor, and without affecting or limiting the Guarantor's liability hereunder, the Lender may:

- (a) grant the Borrowers extensions of time for payment of the Loan Obligations or any part hereof;
- (b) renew any of the Loan Obligations;
- (c) grant the Borrowers extensions of time for performance of agreements or other indulgences;
- (d) at any time release any or all of the Collateral, or any mortgage, deed of trust, or security interest in any Collateral, that now or hereafter secures any of the Loan Obligations;
- (e) compromise, settle, release, or terminate any or all of the obligations, covenants, or agreements of the Borrowers under the Note or other Loan Documents;
- (f) at any time release any one or more other guarantors from their guarantees of any of the Loan Obligations;

and

(g) modify or amend any obligation, covenant, or agreement of the Borrowers as set forth in the Note or any of the other Loan Documents (and such amendments shall nevertheless be binding upon the Guarantor); provided no increase in the principal amount of the Loan will be binding upon the Guarantor unless it has consented to such increase unless such increase is made pursuant to Section 2.1(b) of the Loan Agreement.

This Guaranty shall continue to be effective, or be reinstated, as the case may be, if at any time any whole or partial payment or performance of any Loan Obligations is or is sought to be rescinded or must otherwise be restored or returned by the Lender upon the insolvency, bankruptcy, dissolution, liquidation, or reorganization of the Borrowers, the Guarantor or any guarantor upon or as a result of the appointment of a receiver, intervenor, or conservator of, or trustee or similar officer for, the Borrowers, the Guarantor or any guarantor of or for any substantial part of its property, or otherwise, all as though such payments and performance had not been made and as though this Guaranty had not expired or been terminated. This Guaranty shall not be affected in any way by the transfer or other disposition of any of the Collateral described in and granted to Lender pursuant to the Loan Documents.

2. **Representations and Warranties of the Guarantor.** To induce the Lender to make the Loan to Borrowers, Guarantor represents and warrants to the Lender as follows:

(a) **Power to Incur Obligations.** Guarantor has full power and unrestricted right to enter into this Guaranty and to incur the obligations provided for herein, all of which have been duly authorized by all necessary corporate action of Guarantor.

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(b) **Existence, Power and Qualification.** Guarantor is a limited liability company duly organized, in good standing and validly existing under the laws of the state of its formation as set forth in the introductory paragraph of this Agreement, has the power to own its properties and to carry on its business as is now being conducted and to execute and deliver this Guaranty, and is duly qualified to do business and is in good standing in every jurisdiction in which the character of the properties owned by it or in which the transaction of its business makes its qualification necessary.

(c) **Conflicts.** This Guaranty does not violate, conflict with, or constitute any default under the operating agreement of Guarantor or any decree, or judgment by which Guarantor is bound or affected, and to the best of Guarantor's knowledge, does not constitute a material violation of any agreement or instrument binding upon Guarantor.

(d) **Pending Matters.** No action or investigation is pending or, to the best of Guarantor's knowledge, threatened before or by any state or federal court or administrative agency which would reasonably be expected to result in any material adverse change in the financial condition, operations, or prospects of Guarantor. Guarantor is not in violation of any agreement, the violation of which would reasonably be expected to have a materially adverse effect on Guarantor's business or assets, and Guarantor is not in violation of any order, judgment, or decree of any state or federal court or administrative agency by which Guarantor is bound or affected.

(e) **Financial Statements Accurate.** All financial statements heretofore or hereafter provided by the Guarantor are or will, at the time of the delivery thereof be, true and complete in all material respects as of their respective dates and fairly present the financial condition of Guarantor, and there are no known liabilities, direct or indirect, fixed or contingent, as of the respective dates of such statements which are not or will not, at the time of the delivery thereof, be reflected therein or in the notes thereto or in a written certificate delivered with such statements. There has been no material adverse change in the financial condition, operations, or prospects of Guarantor since the dates of such statements except as fully disclosed in writing with the delivery of such statements.

(f) **No Defaults or Restrictions.** Guarantor is not in default under any agreement or instrument that causes or would have a material adverse effect on the business, properties, and financial operations or condition of Guarantor.

(g) **Payment of Taxes and Employee Benefits.** Guarantor has filed all federal, state, and local tax returns which are required to be filed and has paid, or made adequate provision for the payment of, all taxes which have or may become due pursuant to said returns or to assessments received by Guarantor and has made all required payments to employee benefit plans.

(h) **Disclosure.** Neither this Guaranty nor any other document, financial statement, credit information, certificate, or statement required herein or otherwise furnished to Lender by Guarantor in connection with the Loan or this Guaranty contains any untrue, incorrect,

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or misleading statement of material fact. All representations and warranties made herein or any certificate or other document delivered to Lender by or on behalf of Guarantor pursuant to or in connection with this Guaranty shall be deemed to have been relied upon by Lender notwithstanding any investigation heretofore or hereafter made by Lender or on its behalf, and shall survive the delivery of this Guaranty.

(i) **ERISA.** Guarantor is in compliance with all applicable provisions of the Employee Retirement Income Security Act of 1974, as amended (“ERISA”).

3. **Affirmative Covenants of the Guarantor.** Guarantor covenants and agrees that so long as the Loan Obligations are outstanding, Guarantor shall comply with each of the following affirmative covenants:

(a) **Payment of Loan/Performance of Loan Obligations.** Duly and punctually pay or cause to be paid the principal and interest of the Note in accordance with its terms and duly and punctually pay or cause to be paid or performed all other Loan Obligations.

(b) **Payment of Taxes.** Pay and discharge all taxes, assessments, and governmental charges or levies imposed upon the Guarantor, including, without limitation, all current tax liabilities of all kinds, all required withholdings of income taxes of employees and all required old age and unemployment contributions.

(c) **Reporting Requirements.** From time to time upon request, furnish to Lender such information regarding the business affairs, finances, and conditions of the Guarantor and its properties in such detail as the Lender reasonably may request, including tax returns; without limiting the foregoing, Guarantor will furnish to Lender financial statements as and when required by the Loan Agreement. All financial statements shall be provided in the form and at the times set forth in the Loan Agreement.

(d) **Payment of Indebtedness.** Pay or cause to be paid duly and punctually all principal and interest of any material Indebtedness of the Guarantor to its creditors, and comply with and perform all conditions, terms, and obligations of the notes or other instruments evidencing such indebtedness and any mortgages, deeds of trust, security agreements, and other instruments evidencing or securing such indebtedness. Without limiting anything herein, “material” Indebtedness shall include, without limitation, any Indebtedness which is secured by or becomes subject to any Lien. Guarantor may contest any Indebtedness in good faith and shall not be in violation of this covenant during the period of any such contest provided that execution against any property of the Guarantor must have been effectively stayed and reserves adequate for payment must have been established.

(e) **Notice of Loss.** Notify Lender of any event causing a loss or reduction in value of the Guarantor’s assets which has a material adverse effect on the Guarantor’s net worth.

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(f) **Maintenance of Existence.** Maintain its corporate existence, and, in each jurisdiction in which the character of the property owned by it or in which the transaction of its business makes qualification necessary, maintain qualification and good standing.

4. **Negative Covenants of the Guarantor.** Except as permitted by the Loan Agreement, so long as any of the Loan Obligations are outstanding, Guarantor agrees that it shall not, without Lender's prior written approval:

(a) **Change in Business.** Make any material change in the nature of its business as it is being conducted as of the date hereof which would reasonably be expected to materially and adversely affect its ability to perform its obligations pursuant to this Guaranty.

(b) **Changes in Accounting.** Change its method of accounting to one inconsistent with the method heretofore used by Guarantor.

(c) **Consolidation or Transfer of Substantially all of its Assets.** Enter into any merger, consolidation, or similar transaction with any entity other than Borrowers or any other subsidiary of Borrowers which is a guarantor of the Loan, or sell, assign, lease, or otherwise dispose of (whether in one transaction or in a series of transactions) all or substantially all of its assets (whether now or hereafter acquired) other than to Borrowers or any other subsidiary of Borrowers which is a guarantor of the Loan or unless any such disposition is of property other than the Collateral and is in the ordinary course of business for a full and fair consideration and does not violate any covenant of the Loan Agreement.

(d) **ERISA Funding and Termination.** Permit the funding requirements of ERISA with respect to any employee plan of Guarantor to be less than the minimum required by ERISA at any time, or any employee plan of Guarantor to be subject to involuntary termination proceedings at any time.

(e) **Transfer of Ownership Interests.** Permit any transfer of the ownership interests or stock of Guarantor or change in management of Guarantor that would violate any covenant of the Loan Agreement.

5. **Events of Default.** Guarantor's violation of any covenant set forth in Section 4 hereof, or Guarantor's failure to properly and timely perform or observe any covenant or condition set forth in this Guaranty (other than those in Section 4) which is not cured within any applicable cure period as set forth herein or, if no cure period is specified therefor, which is not cured within thirty (30) days of Lender's notice to Guarantor of such default (provided such cure period shall be extended an additional sixty (60) days if Guarantor commences a cure within such initial thirty (30) days, provides evidence thereof to Lender and diligently pursues a cure), or the falsity in any material respect of any representation or warranty herein or in any financial statement, certificate, or other information heretofore or hereafter provided by Guarantor to Lender, shall constitute an "**Event of Default**" hereunder and under each of the Loan Documents. The foregoing provision or any other provision requiring or providing for notice or demand from Lender is deemed eliminated if Lender is prevented from giving such notice or

demand by bankruptcy or other applicable law, and the Event of Default shall occur upon the occurrence of such event or condition if not cured within any applicable period measured from the occurrence of such event or condition rather than from notice or demand.

6. **Waiver and Subordination.** Guarantor expressly waives any right to payment arising by virtue of any subrogation or indemnification upon payment by Guarantor of amounts due from Borrowers to Lender, and Guarantor expressly subordinates any other rights to payment of indebtedness owing from Borrowers to Guarantor, whether now existing or hereafter arising, to the prior right of Lender to receive or require payment in full of the Loan Obligations, until such time as the Loan Obligations are fully paid (including interest accruing on the Note after any petition under the Bankruptcy Code, which post-petition interest Guarantor agrees shall remain a

claim that is prior and superior to any claim of Guarantor notwithstanding any contrary practice, custom, or ruling in proceedings under the Bankruptcy Code generally) and such payments are final and not subject to refund or rescission under bankruptcy or other applicable law. Furthermore, so long as an Event of Default exists under the Loan Documents, Guarantor agrees not to accept any payment or satisfaction of any kind of indebtedness of Borrowers to the Guarantor or any security for such indebtedness until such time as the Loan Obligations are fully paid. If Guarantor should receive any such payment, satisfaction or security for any indebtedness of Borrowers to the Guarantor, the Guarantor agrees to deliver the same promptly to Lender in the form received, endorsed, or assigned as may be appropriate for application on account of, or as security for, the Loan Obligations and until so delivered, agrees to hold the same in trust for Lender.

7. **Successors and Assigns.** This Guaranty shall be binding upon, and inure to the benefit of, the parties hereto and their respective heirs, legal representatives, successors, and assigns.

8. **Transfer of Rights under the Guaranty and the Loan Documents.**

(a) **Transfer by Lender.** Subject to any limitations set forth in the Loan Agreement, Lender may, at any time, sell, transfer or assign any of the Loan Documents, and any or all servicing rights with respect thereto, or grant participations therein or issue securities evidencing a beneficial interest in a rated or unrated public offering or private placement (the “**Securities**”) to any affiliate of Lender or to the Small Business Administration. Lender may forward to each purchaser, transferee, assignee, servicer, participant or investor in such Securities or any credit rating agency rating such Securities (the foregoing entities hereinafter collectively referred to as the “**Investor**”) and each prospective Investor, all documents and information which Lender now has or may hereafter acquire relating to Guarantor, whether furnished by Borrowers, Guarantor or otherwise, as Lender determines necessary or desirable. Guarantor agrees, upon request of Lender, to cooperate with Lender in connection with any transfer made or any Securities created pursuant to this Section 8(a) provided there is no material financial or other burden to Guarantor of doing so and provided such cooperation does not require an amendment to this Guaranty which would in any manner increase the obligations of Guarantor hereunder. Guarantor shall also furnish and Guarantor hereby consents, subject to Lender’s obligations hereunder, to Lender furnishing to such Investors or such prospective

Investors any and all information concerning the financial condition of Guarantor as provided for in this Section 8(a) in connection with any sale, transfer or participation interest. Notwithstanding the foregoing, in the event that Lender delivers any such information to a prospective Investor, Lender will notify Guarantor to such effect.

(b) **Transfer by Guarantor.** Without the prior written consent of Lender, which may be withheld in Lender’s sole discretion, Guarantor may not, at any time, sell, transfer or assign this Guaranty or any of the other Loan Documents to which Guarantor is a party or any of the Loan Documents to which Guarantor is a party or is otherwise a guarantor, and any or all rights or obligations with respect thereto.

9. **Severability.** In the event that any provision hereof is deemed to be invalid by reason of the operation of any law or by reason of the interpretation placed thereon by any court, this Guaranty shall be construed as not containing such provision, and the invalidity of such provision shall not affect other provisions hereof which are otherwise lawful and valid and shall remain in full force and effect.

10. **Notices.** Any notice or other communication required or permitted to be given pursuant to this Guaranty or by applicable law shall be in writing and shall be deemed received (a) on the date delivered if delivered in person to the person or department specified below, (b) three (3) days after the date deposited in the U.S. Mail, certified or registered, with return receipt requested, or (c) one (1) day following the date deposited with Federal Express or other national overnight carrier, and, in each case, shall be addressed as follows: If to Borrowers:

If to Guarantor:

AdCare Oklahoma Management, LLC  
Two Buckhead Plaza  
3050 Peachtree Road NW, Suite 355  
Atlanta, Georgia 30305

with a copy to:

Ellen W. Smith, Esq.  
Holt Ney Zatcoff & Wasserman, LLP  
100 Galleria Parkway, Suite 1800  
Atlanta, Georgia 30339  
Fax: (770) 956-1490

If to Lender:

Eric Smith  
Contemporary Healthcare Capital, LLC  
1040 Broad Street  
Suite 103

Shrewsbury, New Jersey 07702

with a copy to:

Law Offices of Thomas K. Slattery, P.L.L.C.  
1250 24<sup>th</sup> Street NW, Suite 300  
Washington, DC 20037

Any party may change its address to another single address by notice given as herein provided, except that any change of address must be actually received in order to be effective.

11. **Waivers.** The failure by the Lender at any time or times hereafter to require strict performance by Guarantor of any of the provisions, warranties, terms, and conditions contained herein or in any other agreement, document, or instrument now or hereafter executed by Guarantor and delivered to the Lender shall not waive, affect, or diminish any right of the Lender hereafter to demand strict compliance or performance therewith and with respect to any other provisions, warranties, terms, and conditions contained in such agreements, documents, and instruments, and any waiver of any Default or Event of Default shall not waive or affect any other Default or Event of Default, whether prior or subsequent thereto and whether of the same or a different type. None of the warranties, conditions, provisions, and terms contained in this Guaranty or in any agreement, document, or instrument now or hereafter executed by Guarantor and delivered to the Lender shall be deemed to have been waived by any act or knowledge of the Lender, its agents, officers, or employees, but a waiver, in order to be effective, must be by an instrument in writing, signed by an officer of the Lender, and directed to the Guarantor specifying such waiver.

12. **Expenses.** Guarantor guarantees payment of all costs and expenses described in the Loan Agreement, and the same shall constitute additional obligations of the Guarantor payable on demand.

13. **Singular and Plural.** Singular terms shall include the plural forms, and vice versa.

14. **Entire Agreement.** This Guaranty constitutes the entire agreement of Guarantor and Lender with respect to the subject matter hereof and supersedes all prior agreements and understandings both oral and written, between the parties with respect to the subject matter hereof.

15. **Jurisdiction.** THE VALIDITY, INTERPRETATION, ENFORCEMENT, AND EFFECT OF THIS GUARANTY SHALL BE GOVERNED BY AND CONSTRUED ACCORDING TO THE LAWS OF THE STATE OF NEW JERSEY. THE LENDER' S PRINCIPAL PLACE OF BUSINESS IS LOCATED IN THE STATE OF NEW JERSEY, AND GUARANTOR AGREES THAT THIS GUARANTY SHALL BE HELD BY LENDER AT SUCH PRINCIPAL PLACE OF BUSINESS, AND THE HOLDING OF THIS GUARANTY BY LENDER THEREAT SHALL CONSTITUTE SUFFICIENT

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MINIMUM CONTACTS OF GUARANTOR WITH THE STATE OF NEW JERSEY FOR THE PURPOSE OF CONFERRING JURISDICTION UPON THE FEDERAL AND STATE COURTS PRESIDING IN SUCH STATE AND THE COUNTY OF LENDER' S RESIDENCE. THE GUARANTOR CONSENTS THAT ANY LEGAL ACTION OR PROCEEDING ARISING HEREUNDER MAY BE BROUGHT EXCLUSIVELY IN SUCH COURTS AND ASSENTS AND SUBMITS TO THE PERSONAL JURISDICTION OF ANY SUCH COURTS IN ANY SUCH ACTION OR PROCEEDING.

16. **Jury Trial Waiver.** EACH OF GUARANTOR AND LENDER BY ITS ACCEPTANCE OF THIS GUARANTY HEREBY WAIVE ANY RIGHT TO TRIAL BY JURY ON ANY CLAIM, COUNTERCLAIM, SETOFF, DEMAND, ACTION, OR CAUSE OF ACTION (A) ARISING OUT OF OR IN ANY WAY RELATED TO THIS GUARANTY OR THE LOAN, OR (B) IN ANY WAY CONNECTED WITH OR PERTAINING OR RELATED TO OR INCIDENTAL TO ANY DEALINGS OF LENDER AND/OR BORROWERS AND GUARANTOR WITH RESPECT TO THE LOAN DOCUMENTS OR IN CONNECTION WITH THIS GUARANTY OR THE EXERCISE OF ANY PARTY' S RIGHTS AND REMEDIES UNDER THIS GUARANTY OR OTHERWISE, OR THE CONDUCT OR THE RELATIONSHIP OF THE PARTIES HERETO, IN ALL OF THE FOREGOING CASES WHETHER NOW EXISTING OR HEREAFTER ARISING AND WHETHER SOUNDING IN CONTRACT, TORT, OR OTHERWISE. EACH OF GUARANTOR AND LENDER BY ITS ACCEPTANCE OF THIS GUARANTY AGREES THAT EITHER PARTY MAY FILE A COPY OF THIS GUARANTY WITH ANY COURT AS WRITTEN EVIDENCE OF THE KNOWING, VOLUNTARY, AND BARGAINED-FOR AGREEMENT OF GUARANTOR AND LENDER IRREVOCABLY TO WAIVE THEIR RIGHTS TO TRIAL BY JURY AS AN INDUCEMENT OF LENDER TO MAKE THE LOAN AND OF GUARANTOR TO EXECUTE AND DELIVER THIS GUARANTY, AND THAT, TO THE EXTENT PERMITTED BY APPLICABLE LAW, ANY DISPUTE OR CONTROVERSY WHATSOEVER BETWEEN GUARANTOR AND LENDER SHALL INSTEAD BE TRIED IN A COURT OF COMPETENT JURISDICTION BY A JUDGE SITTING WITHOUT A JURY.

[SIGNATURES BEGIN ON NEXT PAGE]

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IN WITNESS WHEREOF, the Guarantor has executed this Guaranty as of the day and year first above written.

**ADCARE OKLAHOMA MANAGEMENT, LLC**, a Georgia limited liability company

By: /s/ Boyd P. Gentry

Name: Boyd P. Gentry

Title: Manager

**STATE OF** )

[SEAL]

**COUNTY OF** )

I, [Illegible], a Notary Public in and for said County in said State, hereby certify that Boyd P. Gentry, whose name as the Manager of AdCare Oklahoma Management, LLC, a Georgia limited liability company, is signed to the foregoing instrument, and who is known to me, acknowledged before me on this day that being informed of the contents of said instrument, he as such officer and with full authority, executed the same voluntarily for and as the act of said corporation.

Given under my hand and official seal this 17th day of August, 2012.

/s/ [Illegible]

NOTARY PUBLIC

[SEAL]

My Commission Expires:

SIGNATURE PAGE TO CORPORATE GUARANTY - MANAGER – ADCARE - SENIOR

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**SECURITY AGREEMENT**

**THIS SECURITY AGREEMENT** (this “**Agreement**”) is made August 17, 2012, by and among **CSCC PROPERTY HOLDINGS, LLC**, a Georgia limited liability company, and **CSCC NURSING, LLC**, a Georgia limited liability company (with their respective successors and assigns, being collectively referred to as “**Borrowers**”) and **CONTEMPORARY HEALTHCARE FUND I, L.P.**, a Delaware limited partnership (with its successors and assigns, “**Secured Party**”).

**RECITALS:**

**WHEREAS**, Borrowers are borrowing up to \$600,000 (the “**Loan**”) from Secured Party evidenced by a promissory note of even date herewith (as amended from time to time, the “**Note**”), a Loan Agreement by and between Borrowers and Secured Party dated of even date herewith (as amended from time to time, the “**Loan Agreement**”) and certain other agreements and instruments (collectively, with the Note, the Loan Agreement and this Agreement, the “**Loan Documents**”);

**WHEREAS**, to induce Secured Party to make the Loan to Borrowers upon the terms and conditions set forth in the Loan Agreement and other Loan Documents and as security for the payment and performance of Borrowers’ obligations to Secured Party under the Loan Agreement and the other Loan Documents, it is the intent of Borrowers to pledge and to grant to Secured Party for the benefit of Secured Party, a security interest in certain property of Borrowers and to create such a security interest as hereinafter provided;

**WHEREAS**, capitalized terms used herein but not defined herein shall have the meanings as set forth in the Loan Agreement;

**NOW, THEREFORE**, it is hereby agreed as follows:

**ARTICLE I**

**GRANT OF SECURITY INTEREST; COLLATERAL**

1.1. **Grant of Security Interest.** Borrowers hereby pledge and grant to Secured Party for the benefit of Secured Party, a lien and security interest in and to the property described in Section 1.2 below (collectively and severally, the “**Collateral**”) to secure payment and performance of the Loan Obligations of Borrowers to Secured Party.

1.2. **Collateral.** The Collateral shall consist of all of Borrowers’ tangible and intangible property and all other tangible and intangible assets of Borrowers wherever located, whether now owned or hereafter acquired, and any additions, replacements, accessions, or substitutions thereof and all cash and non-cash proceeds and products thereof as set forth on Exhibit A hereto.

**ARTICLE II**

**REPRESENTATIONS AND WARRANTIES**

2.1. **Representations and Warranties.** Each Borrower hereby represents and warrants to Secured Party that at all times from the date of this Agreement to and including the date payment and performance of the Loan Obligations has been completed in full:

(a) Each Borrower is a limited liability company, duly organized, validly existing, and possessing all powers and authority to own its property and to conduct the business in which it is engaged as well as all other rights and privileges generally

granted by the states of their organization. Borrowers have the full right and power to grant the security interest contemplated hereunder subject to any limitations which may be imposed by applicable law on the assignment of Medicare and Medicaid accounts receivable.

(b) There is no action, suit or proceeding pending or, to the best of the Borrower's knowledge, threatened against Borrowers that Borrowers would be expected to have a Material Adverse Effect on the Collateral, or Borrowers' rights and interests therein.

(c) Borrower warrants that the Collateral consisting of Contract Rights, Chattel Paper, Accounts, or General Intangibles is (i) genuine and enforceable in accordance with its terms, except as such enforcement may be limited by bankruptcy, insolvency, reorganization, receivership, moratorium, or other laws relating to the rights of creditors generally and by general principles of equity; (ii) not subject to any defense, set-off, claim or counterclaim (other than write-offs in the ordinary course of business and other than recoupment rights possessed by any Health Regulatory Authority) of a material nature against Borrowers, except as to which Borrowers have notified Secured Party prior to the execution of this Agreement; and (iii) not subject to any other circumstances that would impair the validity, enforceability, value, or amount of the Collateral except for Permitted Encumbrances which exist or may exist upon the Collateral.

### ARTICLE III COVENANTS OF BORROWERS

3.1. **Covenants of Borrowers.** So long as the Note remains unpaid, Borrowers shall:

(a) ensure that all acts that may be necessary to maintain, preserve and protect the Collateral are done;

(b) perform all of their obligations hereunder and under the other Loan Documents when due and before any such obligations are delinquent;

(c) procure, execute and deliver from time to time any endorsements, assignments, financing statements or other writings Secured Party deems necessary or appropriate to perfect, maintain and protect its interest hereunder and the priority thereof except to the extent such delivery would conflict with Borrowers' obligations to another creditor which is a party to a subordination agreement with Secured Party;

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(d) except as permitted in the Loan Documents or as otherwise approved in writing by Secured Party, not surrender, sell, encumber, assign, pledge or otherwise dispose of or transfer the Collateral and keep the Collateral free of all levies and security interests or other liens or charges other than Permitted Encumbrances;

(e) subject to Borrowers' right to contest the same in accordance with applicable law, provided such contest does not present a risk of forfeiture of any of the Collateral, pay all taxes, assessments, charges, encumbrances and liens now or hereafter imposed upon or affecting the Collateral prior to the time the same becomes delinquent;

(f) permit Secured Party and/or its authorized representatives access to the Facility on advance written notice and during normal business hours to inspect and copy Borrowers' books and records related to the Collateral provided no material disturbance or damage is caused to the operation of the Facility, as defined in the Loan Agreement.

(g) except as permitted in, or required by, the Loan Documents or as otherwise approved in writing by Secured Party, not amend, modify or supplement in any material respect any lease, contract or agreement contained in the Collateral or waive any material provision therein, without prior written consent of Secured Party;

(h) with respect to any Collateral that is instruments, chattel paper and negotiable documents, properly assign to, and, to the extent necessary to perfect Secured Party's interest therein, and deposit originals to be held by Secured Party, unless Secured Party shall hereafter otherwise direct or consent in writing or except to the extent such delivery would conflict with Borrowers' obligations to another creditor which is a party to a subordination agreement with Secured Party;

(i) with respect to any Collateral that is uncertificated securities of Borrowers that have been pledged, by the holder registered on the books of the Borrowers as the owner thereof, as further inducement of Secured Party to make the Loan, from and after the occurrence of an Event of Default and during the continuance thereof, Borrowers shall comply with instructions originated by Secured Party without further consent or action by the registered owner thereof; provided, further that, at no time during the term of this Agreement, shall Borrowers issue certificated securities of Borrowers with regard to ownership interests in either Borrower; and

(j) to permit Secured Party, at Borrowers' cost and expense, to obtain periodic lien searches, no more frequently than quarterly.

#### ARTICLE IV DEFAULT AND REMEDIES

4.1. **Events of Default.** The occurrence of any of the following events shall constitute an event of default under the terms of this Agreement (an "Event of Default"):

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(a) any representation or warranty of Borrowers contained herein or otherwise made in connection with the transactions contemplated by this Agreement shall be false or misleading in any material respect on the date as of which made;

(b) Borrowers shall fail to perform or observe any of the terms, provisions, covenants, conditions, agreements or obligations contained in this Agreement within any time periods specified in the Loan Agreement; or

(c) an "Event of Default" shall occur and be continuing under the Loan Agreement.

4.2. **Remedies.** Upon the occurrence of an Event of Default and during the continuance thereof Secured Party may and without notice to or demand on Borrowers and in addition to all rights and remedies available to Secured Party under the terms of this Agreement and the other Loan Documents do any one or more of the following:

(a) foreclose or otherwise enforce Secured Party's security interests in any manner permitted by law, or provided for in this Agreement;

(b) extend the time of payment of, compromise, or settle for cash, credit, or otherwise upon any terms, any part or all of the Collateral;

(c) take possession of, and require Borrowers to endorse in the name of Secured Party, as appropriate, any notes, checks, money orders, drafts, cash, insurance payments, and any other instruments received in payment of the Collateral, or any part thereof; collect, sue for, and give satisfactions for, monies due on account of the Collateral; and withdraw any claims, suits, or proceedings pertaining to, or arising out of Borrowers' and/or Secured Party's right to the Collateral;

(d) recover from Borrowers all costs and expenses including, without limitation, attorneys' fees, incurred or paid by Secured Party in exercising any right, power or remedy provided by this Agreement or under law;

(e) if and to extent the Collateral includes Accounts, notify the Accounts and contract parties obligated on any or all of the Collateral to make payment thereof directly to Secured Party and Secured Party may take control of all proceeds including, without limitation, all Cash collected of any such Collateral, all of which rights Secured Party may exercise at any time. The cost of such collection and enforcement, including attorneys' fees and expenses, shall be borne solely by Borrowers whether the same is incurred by Secured Party or Borrowers. If an Event of Default should occur and be continuing, Borrowers will, upon receipt of all checks, drafts, cash and other remittances in payment on the Collateral, deposit the same in a special Secured Party account maintained with a bank of Secured Party's choice, over which Secured Party also has the power of withdrawal.

4.3. **Additional Remedies.** If an Event of Default should occur at a time when Secured Party has a security interest in Borrowers' Accounts, during the continuance of any such Event of Default, no discount, credit, or allowance shall be granted by either Borrower to any Account or contract party and no return of merchandise other than in the ordinary course of the

business of Borrowers shall be accepted by Borrowers without Secured Party's consent, which consent shall be not withheld if Borrowers, pursuant to the Loan Agreement obligating Borrowers to obtain the following consent, secure the consent thereto of any lenders having a senior security interest therein. Secured Party may, after and during the continuance of such Event of Default and subject to the limitations on its rights with respect to the Accounts of Borrowers as set forth in this [Section 4.3](#), settle or adjust disputes and claims directly with Account contract parties for amounts and upon terms that Secured Party considers advisable, and in such cases Secured Party will credit the Loan Obligations with the net amounts received by Secured Party, after deducting all of the expenses incurred by Secured Party it being understood and agreed that Secured Party shall have no rights under this [Section 4.3](#) unless it has a security interest in the Accounts and, even then, any such rights shall be subject to the rights of any lenders holding a senior security interest therein. Borrowers agree to indemnify and defend Secured Party and hold it harmless with respect to any claim or proceeding arising out of any matter related to collection of Collateral.

## ARTICLE V MISCELLANEOUS

5.1. **Uniform Commercial Code Filings.** Secured Party is hereby authorized, without further action of Borrowers, and in its own name and on behalf of Borrowers, to file any and all financing statements under the Uniform Commercial Code as in effect from time-to-time in the applicable state relating to all or any part of the Collateral (the "UCC") and other documents deemed by Secured Party to be necessary to protect Secured Party's interests in the Collateral. Secured Party agrees to provide Borrowers with a copy of, and the right to review and comment, each financing or continuation statement prior to the filing thereof; provided, however, that if Borrowers fail to respond to such proposed filing within seven (7) business days of its deemed receipt, the rights of Borrowers under this [Section 5.1](#) shall expire.

5.2. **Further Assurances.** At any time and from time to time, at the expense of Borrowers, Borrowers promptly shall execute and deliver all further instruments and documents, and will take all further action, that may be necessary or desirable, or that Secured Party may request, in order to perfect and protect the pledge and grant of security interest made by this Agreement or to enable Secured Party to exercise and enforce its rights and remedies under this Agreement with respect to any Collateral.

5.3. **Cumulative Rights.** The rights, powers and remedies of Secured Party under this Agreement shall be in addition to all rights, powers and remedies available to Secured Party at law or in equity or by virtue of any of the Note, the other Loan Documents or any other agreement contemplated hereunder or thereunder, all of which rights, powers and remedies shall be cumulative and may be exercised successively or concurrently without impairing Secured Party's security interests in the Collateral. It is intended that this clause shall be broadly construed so that all remedies herein provided or otherwise available to Secured Party shall continue to be each and all available to Secured Party until the full and final satisfaction of the Loan Obligations.

5.4. **Collateral Duties.** Secured Party shall have no custodial or ministerial duties to perform with respect to Collateral pledged except as set forth herein; and by way of explanation and not by way of limitation, absent gross negligence or willful misconduct, Secured Party shall incur no liability for any of the following: (i) loss or depreciation of Collateral, (ii) failure to present any paper for payment or protest, to protest or give notice of nonpayment, or any other notice with respect to any Collateral, (iii) failure to ascertain, notify Borrowers of, or take any action in connection with any conversion, call, redemption, retirement or any other event relating to any of the Collateral, or failure to notify any party hereto that Collateral should be presented or surrendered for any such reason. Borrowers acknowledge that Secured Party is not an investment advisor or insurer with respect to the Collateral and Secured Party has no duty to advise Borrowers of any actual or anticipated changes in the value of the Collateral.

5.5. **Continuing Security Interest.** This Agreement shall create a continuing security interest in the Collateral in accordance with its terms and shall remain in full force and effect until full and final satisfaction of the Loan Obligations. This Agreement shall terminate automatically and without the need for either party to execute any further documents or take any further action and be of no further force and effect upon the full and final satisfaction of the Loan Obligations by Borrowers.

5.6. **Waiver.** Exercise or omission to exercise any right of Secured Party shall not affect any subsequent right of Secured Party to exercise the same. No course of dealing between Borrowers and Secured Party or any delay on Secured Party's part in exercising any rights shall operate as a waiver of any of Secured Party's rights. No waiver of any Event of Default under this Agreement or any of the other Loan Documents shall be valid unless in writing and signed by Secured Party nor shall any such waiver extend to or shall affect any subsequent or other existing Event of Default or shall impair any rights, remedies or powers of Secured Party in respect thereof.

5.7. **Headings.** The headings of the Sections of this Agreement are for convenience of reference only, are not to be considered a part hereof, and shall not limit or otherwise affect any of the terms hereof.

5.8. **Survival of Covenants.** All covenants, agreements, representations and warranties made herein and in certificates or reports delivered by Borrowers pursuant hereto and all other information heretofore or hereafter supplied by Borrowers to Secured Party in connection with the Loan and Borrowers, whether written or unwritten, shall be deemed to have been material and relied on by Secured Party, notwithstanding any investigation made by or on behalf of Secured Party, and shall survive the execution and delivery to Secured Party of the Note and this Agreement.

5.9. **Notices, etc.** Any notice or other communication required or permitted to be given by this Agreement or by applicable law shall be given as described in the Loan Agreement.

5.10. **Benefits.** All of the terms and provisions of this Agreement shall bind and inure to the benefit of the parties hereto and their respective successors and assigns. No Person other than Borrowers or Secured Party shall be entitled to rely upon this Agreement or be entitled to the benefits of this Agreement.

5.11. **Supersedes Prior Agreements; Counterparts.** This Agreement and the Loan Documents referred to herein supersede and incorporate all representations, promises, and statements, oral or written, made by Secured Party in connection with the Loan. This Agreement may not be varied, altered, or amended except by a written instrument executed by an authorized officer of each of Secured Party and Borrowers. This Agreement may be executed in any number of counterparts, each of which, when executed and delivered, shall be an original, but such counterparts shall together constitute one and the same instrument.

5.12. **Construction of Provisions of this Agreement.** Secured Party has not agreed to make any loan other than that specifically described herein. All requirements herein shall be deemed material to Secured Party. Except as specified herein, all conditions and requirements must be satisfied by Borrowers prior to the Closing Date. Except as specified herein, whenever this Agreement refers to a matter being “satisfactory” to Secured Party, subject to Secured Party’s “approval” or “consent,” at Secured Party’s “option,” at Secured Party’s “determination,” “required” by Secured Party, at Secured Party’s “request,” as Secured Party shall “deem necessary,” or similar terminology, it is deemed that each of the aforesaid shall be in the sole discretion of Secured Party, and if any term or condition requires Secured Party’s approval, consent, or satisfaction (the “**Secured Party’s Approval**”), Secured Party’s Approval shall not be implied, but shall be evidenced only by a written notice from Secured Party specifically addressed to the particular requirement or condition and expressing Secured Party’s Approval. Loan Agreement.

5.13. **Loan Agreement.** The parties hereby acknowledge that the security interests granted herein are subject to the terms of the Loan Agreement

5.14. **Controlling Law.** THE PARTIES HERETO AGREE THAT THE VALIDITY, INTERPRETATION, ENFORCEMENT AND EFFECT OF THIS AGREEMENT SHALL BE GOVERNED BY, AND CONSTRUED IN ACCORDANCE WITH, THE LAWS OF THE STATE OF NEW JERSEY AND THE PARTIES HERETO SUBMIT (AND WAIVE ALL RIGHTS TO OBJECT) TO NON-EXCLUSIVE PERSONAL JURISDICTION IN THE STATE OF NEW JERSEY, FOR THE ENFORCEMENT OF ANY AND ALL OBLIGATIONS UNDER THE LOAN DOCUMENTS EXCEPT THAT IF ANY SUCH ACTION OR PROCEEDING ARISES UNDER THE CONSTITUTION, LAWS OR TREATIES OF THE UNITED STATES OF AMERICA, OR IF THERE IS A DIVERSITY OF CITIZENSHIP BETWEEN THE PARTIES THERETO, SO THAT IT IS TO BE BROUGHT IN A UNITED STATES DISTRICT COURT, IT SHALL BE BROUGHT IN THE UNITED STATES DISTRICT COURT FOR THE DISTRICT OF NEW JERSEY OVER SHREWSBURY, NEW JERSEY OR ANY SUCCESSOR FEDERAL COURT HAVING ORIGINAL JURISDICTION.

5.15. **Waiver of Jury Trial.** . TO THE EXTENT PERMITTED BY APPLICABLE LAW, EACH OF BORROWERS HEREBY WAIVE ANY RIGHT IT THEY MAY HAVE TO A TRIAL BY JURY ON ANY CLAIM, COUNTERCLAIM, SETOFF, DEMAND, ACTION OR CAUSE OF ACTION (A) ARISING OUT OF OR IN ANY WAY RELATED TO THIS AGREEMENT, THE LOAN DOCUMENTS OR THE LOAN, OR (B) IN ANY WAY CONNECTED WITH OR PERTAINING OR RELATED

TO OR INCIDENTAL TO ANY DEALINGS OF SECURED PARTY AND/OR BORROWERS WITH RESPECT TO THE LOAN DOCUMENTS OR IN CONNECTION WITH THIS AGREEMENT OR THE EXERCISE OF SUCH PARTY’S RIGHTS AND REMEDIES UNDER THIS AGREEMENT OR OTHERWISE, OR THE CONDUCT OR THE RELATIONSHIP OF THE PARTIES HERETO, IN ALL OF THE FOREGOING CASES WHETHER NOW EXISTING OR HEREAFTER ARISING AND WHETHER SOUNDING IN CONTRACT, TORT OR OTHERWISE. EACH OF BORROWERS AGREE THAT THE LENDER MAY FILE A COPY OF THIS AGREEMENT WITH ANY COURT AS WRITTEN EVIDENCE OF THE KNOWING, VOLUNTARY, AND BARGAINED AGREEMENT OF BORROWERS AND SECURED PARTY IRREVOCABLY TO WAIVE ITS RIGHTS TO TRIAL BY JURY AS AN INDUCEMENT FOR SECURED PARTY TO MAKE THE LOAN AND THAT, TO THE EXTENT PERMITTED BY APPLICABLE LAW, ANY DISPUTE OR CONTROVERSY WHATSOEVER BETWEEN BORROWERS AND SECURED PARTY SHALL INSTEAD BE TRIED IN A COURT OF COMPETENT JURISDICTION BY A JUDGE SITTING WITHOUT A JURY.

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[REMAINDER OF PAGE INTENTIONALLY LEFT BLANK]

**IN WITNESS WHEREOF**, the parties have caused this Agreement to be duly executed and delivered as of the date first above written.

**BORROWERS:**

**CSCC PROPERTY HOLDINGS, LLC**, a Georgia limited liability company

By: /s/ Christopher F. Brogdon

Name: Christopher F. Brogdon

Title: Manager

**CSCC NURSING, LLC**, a Georgia limited liability company

By: /s/ Christopher F. Brogdon

Name: Christopher F. Brogdon

Title: Manager

**SECURED PARTY:**

**CONTEMPORARY HEALTHCARE FUND I, L.P.**, a Delaware limited partnership

By: CHC-GP, LLC, a Delaware limited liability company

Its: General Partner

By: /s/ Eric Smith

Eric Smith

Member

SIGNATURE PAGE TO SECURITY AGREEMENT – ADCARE - AR

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**SECURITY AGREEMENT**

**THIS SECURITY AGREEMENT** (this “**Agreement**”) is made August 17, 2012, by and among **CSCC PROPERTY HOLDINGS, LLC**, a Georgia limited liability company, and **CSCC NURSING, LLC**, a Georgia limited liability company (with their respective successors and assigns, being collectively referred to as “**Borrowers**”) and **CONTEMPORARY HEALTHCARE SENIOR LIEN FUND I, L.P.**, a Delaware limited partnership (with its successors and assigns, “**Secured Party**”).

**RECITALS:**

**WHEREAS**, Borrowers are borrowing \$5,000,000 (the “**Loan**”) from Secured Party evidenced by a promissory note of even date herewith (as amended from time to time, the “**Note**”), a Loan Agreement by and between Borrowers and Secured Party dated of even date herewith (as amended from time to time, the “**Loan Agreement**”) and certain other agreements and instruments (collectively, with the Note, the Loan Agreement and this Agreement, the “**Loan Documents**”);

**WHEREAS**, to induce Secured Party to make the Loan to Borrowers upon the terms and conditions set forth in the Loan Agreement and other Loan Documents and as security for the payment and performance of Borrowers’ obligations to Secured Party under the Loan Agreement and the other Loan Documents, it is the intent of Borrowers to pledge and to grant to Secured Party for the benefit of Secured Party, a security interest in certain property of Borrowers and to create such a security interest as hereinafter provided;

**WHEREAS**, capitalized terms used herein but not defined herein shall have the meanings as set forth in the Loan Agreement;

**NOW, THEREFORE**, it is hereby agreed as follows:

**ARTICLE I**

**GRANT OF SECURITY INTEREST; COLLATERAL**

1.1. **Grant of Security Interest.** Borrowers hereby pledge and grant to Secured Party for the benefit of Secured Party, a lien and security interest in and to the property described in Section 1.2 below (collectively and severally, the “**Collateral**”) to secure payment and performance of the Loan Obligations of Borrowers to Secured Party.

1.2. **Collateral.** The Collateral shall consist of all of Borrowers’ tangible and intangible property and all other tangible and intangible assets of Borrowers wherever located, whether now owned or hereafter acquired, and any additions, replacements, accessions, or substitutions thereof and all cash and non-cash proceeds and products thereof as set forth on Exhibit A hereto.

**ARTICLE II**

**REPRESENTATIONS AND WARRANTIES**

2.1. **Representations and Warranties.** Each Borrower hereby represents and warrants to Secured Party that at all times from the date of this Agreement to and including the date payment and performance of the Loan Obligations has been completed in full:

(a) Each Borrower is a limited liability company, duly organized, validly existing, and possessing all powers and authority to own its property and to conduct the business in which it is engaged as well as all other rights and privileges generally



granted by the states of their organization. Borrowers have the full right and power to grant the security interest contemplated hereunder subject to any limitations which may be imposed by applicable law on the assignment of Medicare and Medicaid accounts receivable.

(b) There is no action, suit or proceeding pending or, to the best of the Borrower's knowledge, threatened against Borrowers that Borrowers would be expected to have a Material Adverse Effect on the Collateral, or Borrowers' rights and interests therein.

(c) Borrower warrants that the Collateral consisting of Contract Rights, Chattel Paper, Accounts, or General Intangibles is (i) genuine and enforceable in accordance with its terms, except as such enforcement may be limited by bankruptcy, insolvency, reorganization, receivership, moratorium, or other laws relating to the rights of creditors generally and by general principles of equity; (ii) not subject to any defense, set-off, claim or counterclaim (other than write-offs in the ordinary course of business and other than recoupment rights possessed by any Health Regulatory Authority) of a material nature against Borrowers, except as to which Borrowers have notified Secured Party prior to the execution of this Agreement; and (iii) not subject to any other circumstances that would impair the validity, enforceability, value, or amount of the Collateral except for Permitted Encumbrances which exist or may exist upon the Collateral.

### ARTICLE III COVENANTS OF BORROWERS

3.1. **Covenants of Borrowers.** So long as the Note remains unpaid, Borrowers shall:

(a) ensure that all acts that may be necessary to maintain, preserve and protect the Collateral are done;

(b) perform all of their obligations hereunder and under the other Loan Documents when due and before any such obligations are delinquent;

(c) procure, execute and deliver from time to time any endorsements, assignments, financing statements or other writings Secured Party deems necessary or appropriate to perfect, maintain and protect its interest hereunder and the priority thereof except to the extent such delivery would conflict with Borrowers' obligations to another creditor which is a party to a subordination agreement with Secured Party;

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(d) except as permitted in the Loan Documents or as otherwise approved in writing by Secured Party, not surrender, sell, encumber, assign, pledge or otherwise dispose of or transfer the Collateral and keep the Collateral free of all levies and security interests or other liens or charges other than Permitted Encumbrances;

(e) subject to Borrowers' right to contest the same in accordance with applicable law, provided such contest does not present a risk of forfeiture of any of the Collateral, pay all taxes, assessments, charges, encumbrances and liens now or hereafter imposed upon or affecting the Collateral prior to the time the same becomes delinquent;

(f) permit Secured Party and/or its authorized representatives access to the Facility on advance written notice and during normal business hours to inspect and copy Borrowers' books and records related to the Collateral provided no material disturbance or damage is caused to the operation of the Facility, as defined in the Loan Agreement.

(g) except as permitted in, or required by, the Loan Documents or as otherwise approved in writing by Secured Party, not amend, modify or supplement in any material respect any lease, contract or agreement contained in the Collateral or waive any material provision therein, without prior written consent of Secured Party;

(h) with respect to any Collateral that is instruments, chattel paper and negotiable documents, properly assign to, and, to the extent necessary to perfect Secured Party's interest therein, and deposit originals to be held by Secured Party, unless Secured Party shall hereafter otherwise direct or consent in writing or except to the extent such delivery would conflict with Borrowers' obligations to another creditor which is a party to a subordination agreement with Secured Party;

(i) with respect to any Collateral that is uncertificated securities of Borrowers that have been pledged, by the holder registered on the books of the Borrowers as the owner thereof, as further inducement of Secured Party to make the Loan, from and after the occurrence of an Event of Default and during the continuance thereof, Borrowers shall comply with instructions originated by Secured Party without further consent or action by the registered owner thereof; provided, further that, at no time during the term of this Agreement, shall Borrowers issue certificated securities of Borrowers with regard to ownership interests in either Borrower; and

(j) to permit Secured Party, at Borrowers' cost and expense, to obtain periodic lien searches, no more frequently than quarterly.

#### ARTICLE IV DEFAULT AND REMEDIES

4.1. **Events of Default.** The occurrence of any of the following events shall constitute an event of default under the terms of this Agreement (an "Event of Default"):

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(a) any representation or warranty of Borrowers contained herein or otherwise made in connection with the transactions contemplated by this Agreement shall be false or misleading in any material respect on the date as of which made;

(b) Borrowers shall fail to perform or observe any of the terms, provisions, covenants, conditions, agreements or obligations contained in this Agreement within any time periods specified in the Loan Agreement; or

(c) an "Event of Default" shall occur and be continuing under the Loan Agreement.

4.2. **Remedies.** Upon the occurrence of an Event of Default and during the continuance thereof Secured Party may and without notice to or demand on Borrowers and in addition to all rights and remedies available to Secured Party under the terms of this Agreement and the other Loan Documents do any one or more of the following:

(a) foreclose or otherwise enforce Secured Party's security interests in any manner permitted by law, or provided for in this Agreement;

(b) extend the time of payment of, compromise, or settle for cash, credit, or otherwise upon any terms, any part or all of the Collateral;

(c) take possession of, and require Borrowers to endorse in the name of Secured Party, as appropriate, any notes, checks, money orders, drafts, cash, insurance payments, and any other instruments received in payment of the Collateral, or any part thereof; collect, sue for, and give satisfactions for, monies due on account of the Collateral; and withdraw any claims, suits, or proceedings pertaining to, or arising out of Borrowers' and/or Secured Party's right to the Collateral;

(d) recover from Borrowers all costs and expenses including, without limitation, attorneys' fees, incurred or paid by Secured Party in exercising any right, power or remedy provided by this Agreement or under law;

(e) if and to extent the Collateral includes Accounts and subject to the rights therein of the AR Lender holding a senior security interest therein as permitted by the terms of the Loan Agreement, notify the Accounts and contract parties obligated on any or all of the Collateral to make payment thereof directly to Secured Party and Secured Party may take control of all proceeds including, without limitation, all Cash collected of any such Collateral, all of which rights Secured Party may exercise at any time. The cost of such collection and enforcement, including attorneys' fees and expenses, shall be borne solely by Borrowers whether the same is incurred by Secured Party or Borrowers. If an Event of Default should occur and be continuing, Borrowers will, upon receipt of all checks, drafts, cash and other remittances in payment on the Collateral, deposit the same in a special Secured Party account maintained with a bank of Secured Party' s choice, over which Secured Party also has the power of withdrawal.

4.3. **Additional Remedies.** If an Event of Default should occur at a time when Secured Party has a security interest in Borrowers' Accounts, during the continuance of any such Event of Default, no discount, credit, or allowance shall be granted by either Borrower to any

Account or contract party and no return of merchandise other than in the ordinary course of the business of Borrowers shall be accepted by Borrowers without Secured Party' s consent, which consent shall be not withheld if Borrowers, pursuant to the Loan Agreement obligating Borrowers to obtain the following consent, secure the consent thereto of any lenders having a senior security interest therein. Secured Party may, after and during the continuance of such Event of Default and subject to the limitations on its rights with respect to the Accounts of Borrowers as set forth in this Section 4.3, settle or adjust disputes and claims directly with Account contract parties for amounts and upon terms that Secured Party considers advisable, and in such cases Secured Party will credit the Loan Obligations with the net amounts received by Secured Party, after deducting all of the expenses incurred by Secured Party it being understood and agreed that Secured Party shall have no rights under this Section 4.3 unless it has a security interest in the Accounts and, even then, any such rights shall be subject to the rights of any lenders holding a senior security interest therein. Borrowers agree to indemnify and defend Secured Party and hold it harmless with respect to any claim or proceeding arising out of any matter related to collection of Collateral.

## ARTICLE V MISCELLANEOUS

5.1. **Uniform Commercial Code Filings.** Secured Party is hereby authorized, without further action of Borrowers, and in its own name and on behalf of Borrowers, to file any and all financing statements under the Uniform Commercial Code as in effect from time-to-time in the applicable state relating to all or any part of the Collateral (the "UCC") and other documents deemed by Secured Party to be necessary to protect Secured Party' s interests in the Collateral. Secured Party agrees to provide Borrowers with a copy of, and the right to review and comment, each financing or continuation statement prior to the filing thereof; provided, however, that if Borrowers fail to respond to such proposed filing within seven (7) business days of its deemed receipt, the rights of Borrowers under this Section 5.1 shall expire.

5.2. **Further Assurances.** At any time and from time to time, at the expense of Borrowers, Borrowers promptly shall execute and deliver all further instruments and documents, and will take all further action, that may be necessary or desirable, or that Secured Party may request, in order to perfect and protect the pledge and grant of security interest made by this Agreement or to enable Secured Party to exercise and enforce its rights and remedies under this Agreement with respect to any Collateral.

5.3. **Cumulative Rights.** The rights, powers and remedies of Secured Party under this Agreement shall be in addition to all rights, powers and remedies available to Secured Party at law or in equity or by virtue of any of the Note, the other Loan Documents or any other agreement contemplated hereunder or thereunder, all of which rights, powers and remedies shall be cumulative and may be exercised successively or concurrently without impairing Secured Party' s security interests in the Collateral. It is intended that this

clause shall be broadly construed so that all remedies herein provided or otherwise available to Secured Party shall continue to be each and all available to Secured Party until the full and final satisfaction of the Loan Obligations.

5.4. **Collateral Duties.** Secured Party shall have no custodial or ministerial duties to perform with respect to Collateral pledged except as set forth herein; and by way of explanation and not by way of limitation, absent gross negligence or willful misconduct, Secured Party shall incur no liability for any of the following: (i) loss or depreciation of Collateral, (ii) failure to present any paper for payment or protest, to protest or give notice of nonpayment, or any other notice with respect to any Collateral, (iii) failure to ascertain, notify Borrowers of, or take any action in connection with any conversion, call, redemption, retirement or any other event relating to any of the Collateral, or failure to notify any party hereto that Collateral should be presented or surrendered for any such reason. Borrowers acknowledge that Secured Party is not an investment advisor or insurer with respect to the Collateral and Secured Party has no duty to advise Borrowers of any actual or anticipated changes in the value of the Collateral.

5.5. **Continuing Security Interest.** This Agreement shall create a continuing security interest in the Collateral in accordance with its terms and shall remain in full force and effect until full and final satisfaction of the Loan Obligations. This Agreement shall terminate automatically and without the need for either party to execute any further documents or take any further action and be of no further force and effect upon the full and final satisfaction of the Loan Obligations by Borrowers.

5.6. **Waiver.** Exercise or omission to exercise any right of Secured Party shall not affect any subsequent right of Secured Party to exercise the same. No course of dealing between Borrowers and Secured Party or any delay on Secured Party's part in exercising any rights shall operate as a waiver of any of Secured Party's rights. No waiver of any Event of Default under this Agreement or any of the other Loan Documents shall be valid unless in writing and signed by Secured Party nor shall any such waiver extend to or shall affect any subsequent or other existing Event of Default or shall impair any rights, remedies or powers of Secured Party in respect thereof.

5.7. **Headings.** The headings of the Sections of this Agreement are for convenience of reference only, are not to be considered a part hereof, and shall not limit or otherwise affect any of the terms hereof.

5.8. **Survival of Covenants.** All covenants, agreements, representations and warranties made herein and in certificates or reports delivered by Borrowers pursuant hereto and all other information heretofore or hereafter supplied by Borrowers to Secured Party in connection with the Loan and Borrowers, whether written or unwritten, shall be deemed to have been material and relied on by Secured Party, notwithstanding any investigation made by or on behalf of Secured Party, and shall survive the execution and delivery to Secured Party of the Note and this Agreement.

5.9. **Notices, etc.** Any notice or other communication required or permitted to be given by this Agreement or by applicable law shall be given as described in the Loan Agreement.

5.10. **Benefits.** All of the terms and provisions of this Agreement shall bind and inure to the benefit of the parties hereto and their respective successors and assigns. No Person other than Borrowers or Secured Party shall be entitled to rely upon this Agreement or be entitled to the benefits of this Agreement.

5.11. **Supersedes Prior Agreements; Counterparts.** This Agreement and the Loan Documents referred to herein supersede and incorporate all representations, promises, and statements, oral or written, made by Secured Party in connection with the Loan. This Agreement may not be varied, altered, or amended except by a written instrument executed by an authorized officer of each

of Secured Party and Borrowers. This Agreement may be executed in any number of counterparts, each of which, when executed and delivered, shall be an original, but such counterparts shall together constitute one and the same instrument.

5.12. **Construction of Provisions of this Agreement.** Secured Party has not agreed to make any loan other than that specifically described herein. All requirements herein shall be deemed material to Secured Party. Except as specified herein, all conditions and requirements must be satisfied by Borrowers prior to the Closing Date. Except as specified herein, whenever this Agreement refers to a matter being “satisfactory” to Secured Party, subject to Secured Party’s “approval” or “consent,” at Secured Party’s “option,” at Secured Party’s “determination,” “required” by Secured Party, at Secured Party’s “request,” as Secured Party shall “deem necessary,” or similar terminology, it is deemed that each of the aforesaid shall be in the sole discretion of Secured Party, and if any term or condition requires Secured Party’s approval, consent, or satisfaction (the “**Secured Party’s Approval**”), Secured Party’s Approval shall not be implied, but shall be evidenced only by a written notice from Secured Party specifically addressed to the particular requirement or condition and expressing Secured Party’s Approval. Loan Agreement.

5.13. **Loan Agreement.** The parties hereby acknowledge that the security interests granted herein are subject to the terms of the Loan Agreement

5.14. **Controlling Law.** THE PARTIES HERETO AGREE THAT THE VALIDITY, INTERPRETATION, ENFORCEMENT AND EFFECT OF THIS AGREEMENT SHALL BE GOVERNED BY, AND CONSTRUED IN ACCORDANCE WITH, THE LAWS OF THE STATE OF NEW JERSEY AND THE PARTIES HERETO SUBMIT (AND WAIVE ALL RIGHTS TO OBJECT) TO NON-EXCLUSIVE PERSONAL JURISDICTION IN THE STATE OF NEW JERSEY, FOR THE ENFORCEMENT OF ANY AND ALL OBLIGATIONS UNDER THE LOAN DOCUMENTS EXCEPT THAT IF ANY SUCH ACTION OR PROCEEDING ARISES UNDER THE CONSTITUTION, LAWS OR TREATIES OF THE UNITED STATES OF AMERICA, OR IF THERE IS A DIVERSITY OF CITIZENSHIP BETWEEN THE PARTIES THERETO, SO THAT IT IS TO BE BROUGHT IN A UNITED STATES DISTRICT COURT, IT SHALL BE BROUGHT IN THE UNITED STATES DISTRICT COURT FOR THE DISTRICT OF NEW JERSEY OVER SHREWSBURY, NEW JERSEY OR ANY SUCCESSOR FEDERAL COURT HAVING ORIGINAL JURISDICTION.

5.15. **Waiver of Jury Trial.** . TO THE EXTENT PERMITTED BY APPLICABLE LAW, EACH OF BORROWERS HEREBY WAIVE ANY RIGHT IT THEY MAY HAVE TO A TRIAL BY JURY ON ANY CLAIM, COUNTERCLAIM, SETOFF, DEMAND, ACTION OR CAUSE OF ACTION (A) ARISING OUT OF OR IN ANY WAY RELATED TO THIS AGREEMENT, THE LOAN DOCUMENTS OR THE LOAN, OR (B) IN ANY WAY CONNECTED WITH OR PERTAINING OR RELATED

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TO OR INCIDENTAL TO ANY DEALINGS OF SECURED PARTY AND/OR BORROWERS WITH RESPECT TO THE LOAN DOCUMENTS OR IN CONNECTION WITH THIS AGREEMENT OR THE EXERCISE OF SUCH PARTY’S RIGHTS AND REMEDIES UNDER THIS AGREEMENT OR OTHERWISE, OR THE CONDUCT OR THE RELATIONSHIP OF THE PARTIES HERETO, IN ALL OF THE FOREGOING CASES WHETHER NOW EXISTING OR HEREAFTER ARISING AND WHETHER SOUNDING IN CONTRACT, TORT OR OTHERWISE. EACH OF BORROWERS AGREE THAT THE LENDER MAY FILE A COPY OF THIS AGREEMENT WITH ANY COURT AS WRITTEN EVIDENCE OF THE KNOWING, VOLUNTARY, AND BARGAINED AGREEMENT OF BORROWERS AND SECURED PARTY IRREVOCABLY TO WAIVE ITS RIGHTS TO TRIAL BY JURY AS AN INDUCEMENT FOR SECURED PARTY TO MAKE THE LOAN AND THAT, TO THE EXTENT PERMITTED BY APPLICABLE LAW, ANY DISPUTE OR CONTROVERSY WHATSOEVER BETWEEN BORROWERS AND SECURED PARTY SHALL INSTEAD BE TRIED IN A COURT OF COMPETENT JURISDICTION BY A JUDGE SITTING WITHOUT A JURY.

**IN WITNESS WHEREOF**, the parties have caused this Agreement to be duly executed and delivered as of the date first above written.

**BORROWERS:**

**CSCC PROPERTY HOLDINGS, LLC**, a Georgia limited liability company

By: /s/ Christopher F. Brogdon

Name: Christopher F. Brogdon

Title: Manager

**CSCC NURSING, LLC**, a Georgia limited liability company

By: /s/ Christopher F. Brogdon

Name: Christopher F. Brogdon

Title: Manager

**SECURED PARTY:**

**CONTEMPORARY HEALTHCARE SENIOR LIEN FUND I, L.P.**, a Delaware limited partnership

By: CHSL-GP, LLC, a Delaware limited liability company

Its: General Partner

By: /s/ Eric Smith

Eric Smith

Member

SIGNATURE PAGE TO SECURITY AGREEMENT – ADCARE - SENIOR

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**LOAN AND SECURITY AGREEMENT**

Dated as of September 20, 2012

by and among

**ADK THOMASVILLE OPERATOR, LLC**,  
a Georgia limited liability company,  
**ADK LUMBER CITY OPERATOR, LLC**,  
a Georgia limited liability company,  
**ADK JEFFERSONVILLE OPERATOR, LLC**,  
a Georgia limited liability company,  
**ADK LAGRANGE OPERATOR, LLC**,  
a Georgia limited liability company,  
**ADK POWDER SPRINGS OPERATOR, LLC**,  
a Georgia limited liability company,  
**ADK OCEANSIDE OPERATOR, LLC**,  
a Georgia limited liability company,  
**ADK THUNDERBOLT OPERATOR, LLC**,  
a Georgia limited liability company,  
**ADK SAVANNAH BEACH OPERATOR, LLC**,  
a Georgia limited liability company,  
**ATTALLA NURSING ADK, LLC**,  
a Georgia limited liability company,  
**MOUNTAIN TRACE NURSING ADK, LLC**,  
an Ohio limited liability company,  
**MT. KENN NURSING, LLC**,  
a Georgia limited liability company,  
**ERIN NURSING, LLC**,  
a Georgia limited liability company,  
**CP NURSING, LLC**,  
a Georgia limited liability company,

**BENTON NURSING, LLC**,  
a Georgia limited liability company,  
**VALLEY RIVER NURSING, LLC**,  
a Georgia limited liability company,  
**PARK HERITAGE NURSING, LLC**,  
a Georgia limited liability company,  
**HOMESTEAD NURSING, LLC**,  
a Georgia limited liability company,  
**WOODLAND MANOR NURSING, LLC**,  
a Georgia limited liability company,  
**MOUNTAIN VIEW NURSING, LLC**,  
a Georgia limited liability company,  
**NORTHRIDGE HC&R NURSING, LLC**,  
a Georgia limited liability company,  
**LITTLE ROCK HC&R NURSING, LLC**,  
a Georgia limited liability company,  
**WOODLAND HILLS HC NURSING, LLC**,  
a Georgia limited liability company,  
**APH&R NURSING, LLC**,  
a Georgia limited liability company,  
**GLENVUE H&R NURSING, LLC**,  
a Georgia limited liability company,  
and  
**COOSA NURSING ADK, LLC**,  
a Georgia limited liability company,

as Borrowers

and

**THE PRIVATEBANK AND TRUST COMPANY**,  
an Illinois banking corporation,  
as Lender

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## **EXHIBITS**

EXHIBIT A - DIRECT AND INDIRECT OWNERSHIP OF BORROWERS

## **LOAN AND SECURITY AGREEMENT**

THIS LOAN AND SECURITY AGREEMENT dated as of September 20, 2012 (this “**Agreement**”), is executed by and among –

**ADK THOMASVILLE OPERATOR, LLC**, a Georgia limited liability company (“**Borrower 1**”),

**ADK LUMBER CITY OPERATOR, LLC**, a Georgia limited liability company (“**Borrower 2**”),

**ADK JEFFERSONVILLE OPERATOR, LLC**, a Georgia limited liability company (“**Borrower 3**”),

**ADK LAGRANGE OPERATOR, LLC**, a Georgia limited liability company (“**Borrower 4**”),

**ADK POWDER SPRINGS OPERATOR, LLC**, a Georgia limited liability company (“**Borrower 5**”),

**ADK OCEANSIDE OPERATOR, LLC**, a Georgia limited liability company (“**Borrower 6**”),

**ADK THUNDERBOLT OPERATOR, LLC**, Georgia limited liability company (“**Borrower 7**”),

**ADK SAVANNAH BEACH OPERATOR, LLC**, a Georgia limited liability company (“**Borrower 8**”),

**ATTALLA NURSING ADK, LLC**, a Georgia limited liability company (“**Borrower 9**”),

**MOUNTAIN TRACE NURSING ADK, LLC**, an Ohio limited liability company (“**Borrower 10**”),

**MT. KENN NURSING, LLC**, a Georgia limited liability company (“**Borrower 11**”),

ERIN NURSING, LLC, a Georgia limited liability company ("**Borrower 12**"),

CP NURSING, LLC, a Georgia limited liability company ("**Borrower 13**"),

BENTON NURSING, LLC, a Georgia limited liability company ("**Borrower 14**"),

VALLEY RIVER NURSING, LLC, a Georgia limited liability company ("**Borrower 15**"),

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PARK HERITAGE NURSING, LLC, a Georgia limited liability company ("**Borrower 16**"),

HOMESTEAD NURSING, LLC, a Georgia limited liability company ("**Borrower 17**"),

WOODLAND MANOR NURSING, LLC, a Georgia limited liability company ("**Borrower 18**"),

MOUNTAIN VIEW NURSING, LLC, a Georgia limited liability company ("**Borrower 19**"),

NORTHRIDGE HC&R NURSING, LLC, a Georgia limited liability company ("**Borrower 20**"),

LITTLE ROCK HC&R NURSING, LLC, a Georgia limited liability company ("**Borrower 21**"),

WOODLAND HILLS HC NURSING, LLC, a Georgia limited liability company ("**Borrower 22**"),

APH&R NURSING, LLC, a Georgia limited liability company ("**Borrower 23**"),

GLENVUE H&R NURSING, LLC, a Georgia limited liability company ("**Borrower 24**"),

and COOSA NURSING ADK, LLC, a Georgia limited liability company ("**Borrower 25**")

(collectively, "**Borrowers**"), and THE PRIVATEBANK AND TRUST COMPANY, an Illinois banking corporation ("**Lender**").

### **RECITALS**

A. Borrowers are the lessees or sublessees of the Projects (as hereinafter defined), which are improved with the "**Facilities**" (as hereinafter defined).

B. Borrowers are the operators of the Facilities and have applied to Lender for the Loan (as hereinafter defined), to provide working capital to Borrowers for the operation of the Facilities, and Lender is willing to make the Loan upon the terms and conditions hereinafter set forth.

### **AGREEMENTS**

In consideration of the mutual representations, warranties, covenants and agreements herein contained and other good and valuable consideration, the receipt and sufficiency of which is hereby acknowledged, the parties hereby agree as follows:

## ARTICLE 1

### INCORPORATION AND DEFINITIONS

1.1 **Incorporation and Definitions.** The foregoing recitals and all exhibits hereto are hereby made a part of this Agreement. The following terms shall have the following meanings in this Agreement:

**AdCare:** AdCare Health Systems, Inc., an Ohio corporation.

**Affiliate:** As to a person or entity, any other person or entity which, directly or indirectly, Controls, is Controlled by or is under common Control with such first person or entity.

**Agreement:** This Loan and Security Agreement by and among Borrowers and Lender.

**Application:** An Application for Irrevocable Standby Letter of Credit which either originally or after the joinder contained in Section 3.2(b) of this Agreement, is from Borrowers to Lender.

**Availability:** At any time, an amount equal to the lesser of (i) the Loan Amount, or (ii) the Borrowing Base Amount; and as such amount may be reduced pursuant to the provisions of Section 3.1(b) of this Agreement.

**Bank Product Agreements:** Those certain cash management service agreements entered into from time to time between Borrower and Lender or its Affiliates in connection with any of the Bank Products.

**Bank Product Obligations:** All obligations, liabilities, contingent reimbursement obligations, fees, and expenses owing by Borrower to Lender or its Affiliates pursuant to or evidenced by the Bank Product Agreements and irrespective of whether for the payment of money, whether direct or indirect, absolute or contingent, due or to become due, now existing or hereafter arising, and including all such amounts that Borrower is obligated to reimburse to Lender as a result of Lender purchasing participations or executing indemnities or reimbursement obligations with respect to the Bank Products provided to Borrower pursuant to the Bank Product Agreements.

**Bank Products:** Any service or facility extended to Borrower by Lender or its Affiliates, including, without limitation, (i) deposit accounts, (ii) cash management services, including, without limitation, controlled disbursement, lockbox, electronic funds transfers (including, without limitation, book transfers, fedwire transfers, ACH transfers), online reporting and other services relating to accounts maintained with Lender or its Affiliates, (iii) debit cards, and (iv) Hedging Agreements.

**Borrower 1:** As defined in the Preamble hereto.

**Borrower 2:** As defined in the Preamble hereto.

**Borrower 3:** As defined in the Preamble hereto.

**Borrower 4:** As defined in the Preamble hereto.

**Borrower 5:** As defined in the Preamble hereto.

**Borrower 6:** As defined in the Preamble hereto.

**Borrower 7:** As defined in the Preamble hereto.

**Borrower 8:** As defined in the Preamble hereto.

**Borrower 9:** As defined in the Preamble hereto.

**Borrower 10:** As defined in the Preamble hereto.

**Borrower 11:** As defined in the Preamble hereto.

**Borrower 12:** As defined in the Preamble hereto.

**Borrower 13:** As defined in the Preamble hereto.

**Borrower 14:** As defined in the Preamble hereto.

**Borrower 15:** As defined in the Preamble hereto.

**Borrower 16:** As defined in the Preamble hereto.

**Borrower 17:** As defined in the Preamble hereto.

**Borrower 18:** As defined in the Preamble hereto.

**Borrower 19:** As defined in the Preamble hereto.

**Borrower 20:** As defined in the Preamble hereto.

**Borrower 21:** As defined in the Preamble hereto.

**Borrower 22:** As defined in the Preamble hereto.

**Borrower 23:** As defined in the Preamble hereto.

**Borrower 24:** As defined in the Preamble hereto.

**Borrower 25:** As defined in the Preamble hereto.

**Borrowers:** Borrower 1 through Borrower 25.

**Borrowing Base Amount:** An amount equal to (i) 80% of the amount of all Eligible Accounts, minus (ii) the amounts of such reserves and allowances as Lender deems proper and necessary, including, without limitation, reserves and allowances for credit amounts in any of the Eligible Accounts categories to provide for amounts that may become due to the Medicare, Medicaid or other payor programs.

**Borrowing Base Certificate**: A certificate to be signed by Borrowers certifying to the accuracy of the Borrowing Base Amount in form and substance satisfactory to Lender.

**Capital Lease**: With respect to any party, a lease of any interest in any kind of property or asset, whether real, personal or mixed, or tangible or intangible, by such party, as lessee, that is, or should be recorded as a “capital lease” on the financial statements of such party prepared in accordance with GAAP.

**Capitalized Lease Obligations**: With respect to any party, all rental obligations of such party as lessee under a Capital Lease which are or will be required to be capitalized on the books of such party.

**Code**: The Uniform Commercial Code of the State of Illinois as from time to time in effect; provided, however, that in the event that, by reason of mandatory provisions of law, any or all of the attachment, perfection or priority of, or remedies with respect to, the security interest in any collateral is governed by the Uniform Commercial Code as in effect in a jurisdiction other than the State of Illinois, the term “Code” shall mean the Uniform Commercial Code as in effect in such other jurisdiction for purposes of the provisions of this Agreement or the other Loan Documents relating to such attachment, perfection, priority or remedies and for purposes of definitions related to such provisions.

**Collateral**: As defined in Section 8.1 hereof.

**Control**: Possession by a person or an entity, directly or indirectly, of the power to direct or cause the direction of the management and policies of an entity, whether by contract, ownership of voting securities, membership or partnership interests or otherwise.

**Debt Service**: With respect to any party, for any period, the sum of (i) Interest Charges, plus (ii) all principal payable to a lender in connection with borrowed money or the deferred purchase price of assets that are treated as interest in accordance with GAAP, plus (iii) the portion of Capitalized Lease Obligations with respect to that period that should be treated as principal in accordance with GAAP.

**Declarations**: Any documents containing covenants, conditions, restrictions, easements, operating agreements or the like, which benefit or burden the a Project, or both, whether or not recorded.

**Default**: When used in reference to this Agreement or any other document, or in reference to any provision of or obligation under this Agreement or any other document, the occurrence of an event or the existence of a condition which, with the passage of time or the

giving of notice, or both, would constitute an Event of Default under this Agreement or such other document, as the case may be.

**Default Rate**: As defined in the Note.

**Depreciation**: With respect to any party, for any period, the total amounts added to depreciation, amortization, obsolescence, valuation and other proper reserves, as reflected on such party’ s financial statements for such period and determined in accordance with GAAP.

**“Distribution”**: In the case of any entity with respect to which the term is used, any of the following: (i) any dividend or distribution of money or property to any owner of a direct or indirect interest in such entity (each a “**Principal**”) or to any Affiliate of any Principal, (ii) any loan or advance to any Principal or to any Affiliate of any Principal, (iii) any payment of principal or interest on

any indebtedness due to any Principal or to any Affiliate of any Principal, and (iv) any payment of any fees or other compensation to any Principal or to any Affiliate of any Principal.

**EBITDA**: With respect to any party, for any period, the sum for such period of the following of or payable by such party, as the case may be: (i) Net Income, plus (ii) Interest Charges, plus (iii) federal and state income taxes, plus (iv) Depreciation.

**EBITDAR**: With respect to any party, for any period, the sum for such period of the following of or payable by such party, as the case may be: (i) Net Income, plus (ii) Interest Charges, plus (iii) federal and state income taxes, plus (iv) Depreciation, plus (v) Rental Expense.

**Eligible Account and Eligible Accounts**: Each Account and all such Accounts (exclusive of sales, excise or other similar taxes) owing to a Borrower which meets each of the following requirements:

(a) It is genuine in all respects and has arisen in the ordinary course of such Borrower's business as occupancy charges and from the performance of services by such Borrower, which services have been fully performed, acknowledged and accepted by the Account Debtor, and sales of Inventory related to such occupancy charges and services;

(b) It is subject to a perfected, first priority security interest in favor of Lender and is not subject to any other assignment, claim, security interest, lien or encumbrance;

(c) It is the valid, legally enforceable and unconditional obligation of the Account Debtor with respect thereto, and is not subject to the fulfillment of any condition whatsoever or any counterclaim, credit, trade or volume discount, allowance, discount, rebate or adjustment by the Account Debtor with respect thereto, or to any claim by such Account Debtor denying liability thereunder in whole or in part and the Account Debtor has not refused to accept or has not returned or offered to return any of the Inventory or services which are the subject of such Account; provided, however, that this paragraph shall not apply with respect to the general terms and conditions of the Medicare or the Medicaid program, including the right to recoup prior overpayments from payments due

on other claims, as opposed to matters relating to the status of a particular Account due from the Medicare or the Medicaid program;

(d) The Account Debtor with respect thereto is a resident or citizen of, and is located within, the United States, or is the Medicare or the Medicaid program;

(e) It is not an Account arising from a "sale on approval", "sale or return", "consignment", "guaranteed sale" or "bill and hold", or are subject to any other repurchase or return agreement;

(f) It is not an Account with respect to which possession or control of the goods sold giving rise thereto is held, maintained or retained by such Borrower (or by any agent or custodian of such Borrower) for the account of, or subject to, further or future direction from the Account Debtor with respect thereto;

(g) It has not arisen out of contracts with the United States or any department, agency or instrumentality thereof, or any state, county, city or other governmental body, or any department, agency or instrumentality thereof, in each case unless such Borrower has assigned its right to the proceeds of the payment of such Account to Lender in a manner consistent with applicable law governing the assignment of amounts payable under such contracts;

(h) If such Borrower maintains a credit limit for an Account Debtor, the aggregate dollar amount of Accounts due from such Account Debtor, including such Account, does not exceed such credit limit;

(i) If the Account is evidenced by chattel paper or an instrument, the originals of such chattel paper or instrument shall have been endorsed or assigned and delivered to Lender or, in the case of electronic chattel paper, shall be in the control of Lender, in each case in a manner satisfactory to Lender;

(j) Such Account is not due from a so-called private pay person who is not covered by Medicare, Medicaid or commercial insurance, or from a person who has applied for Medicare or Medicaid benefits but has not yet been approved for such benefits, or has been submitted to but has not yet been approved for payment by Medicare, Medicaid or commercial insurance;

(k) Such Account is evidenced by an invoice delivered to the related Account Debtor, and is not more than 120 days past the billing date thereof in the case of Accounts due from the Medicaid program, not more than 120 days past the billing date thereof in the case of Accounts due from the Medicare program, and not more than 120 days past the billing date thereof in the case of all other Accounts;

(l) It is not an Account with respect to an Account Debtor that is located in any jurisdiction which has adopted a statute or other requirement with respect to which any person that obtains business from within such jurisdiction must file a notice of business activities report or make any other required filings in a timely manner in order to enforce its claims in such jurisdiction' s courts unless (i) such notice of business activities

report has been duly and timely filed or such Borrower is exempt from filing such report and has provided Lender with satisfactory evidence of such exemption or (ii) the failure to make such filings may be cured retroactively by such Borrower for a nominal fee;

(m) The Account Debtor with respect thereto is not such Borrower or an Affiliate of such Borrower;

(n) Such Account does not arise out of a contract or order which, by its terms, forbids or makes void or unenforceable the assignment thereof by such Borrower to Lender and is not unassignable to Lender for any other reason;

(o) There is no bankruptcy, insolvency or liquidation proceeding pending by or against the Account Debtor with respect thereto, nor has the Account Debtor suspended business, made a general assignment for the benefit of creditors or failed to pay its debts generally as they come due, or no condition or event has occurred having a material adverse effect on the Account Debtor which would require the Accounts of such Account Debtor to be deemed uncollectible in accordance with GAAP; and

(p) It does not violate the negative covenants and does satisfy the affirmative covenants of such Borrower contained in this Agreement, and it is otherwise not unacceptable to Lender for any other reason.

An Account which is at any time an Eligible Account, but which subsequently fails to meet any of the foregoing requirements, shall forthwith cease to be an Eligible Account. Further, with respect to any Account, if Lender at any time hereafter determines in its discretion that the prospect of payment or performance by the Account Debtor with respect thereto is materially impaired for any reason whatsoever, such Account shall cease to be an Eligible Account after notice of such determination is given to such Borrower.



**Employee Plan:** Any pension, stock bonus, employee stock ownership plan, retirement, profit sharing, deferred compensation, stock option, bonus or other incentive plan, whether qualified or nonqualified, or any disability, medical, dental or other health plan, life insurance or other death benefit plan, vacation benefit plan, severance plan or other employee benefit plan or arrangement, including, without limitation, those pension, profit-sharing and retirement plans of any Borrower described from time to time in its financial statements, and any pension plan, welfare plan, Defined Benefit Pension Plans (as defined in ERISA) or multi-employer plan, maintained or administered by any Borrower or to which any Borrower is a party, or under which any Borrower may have any liability, or by which any Borrower may be bound.

**Environmental Laws:** Any and all federal, state and local laws (whether under common law, statute, rule, regulation or otherwise), requirements under permits or other authorizations issued with respect thereto, and other orders, decrees, judgments, directives or other requirements of any governmental authority relating to or imposing liability or standards of conduct (including disclosure or notification) concerning protection of human health or the environment or Hazardous Substances or any activity involving Hazardous Substances, all as previously and in the future amended from time to time, as the case may be.

**ERISA:** The Employee Retirement Income Security Act of 1974, as amended.

**Event of Default:** The following: (i) when used in reference to this Agreement, one or more of the events or occurrences referred to in Section 10.1 of this Agreement; and (ii) when used in reference to any other document, a default or event of default under such document that has continued after the giving of any applicable notice and the expiration of any applicable grace or cure periods.

**Facility:** Each of the 25 Facilities which are operated by Borrowers in the Projects, described as follows:

Facility	Borrower	Facility Name	Location	Beds
1	Borrower 1	Thomasville Nursing and Rehab Center	120 Skyline Drive, Thomasville, Thomas County, Georgia	52
2	Borrower 2	Lumber City Nursing and Rehabilitation Center	93 Highway 19, Lumber City, Telfair County, Georgia	86
3	Borrower 3	Jeffersonville Nursing and Rehabilitation Center	113 Spring Valley Drive, Jeffersonville, Twiggs County, Georgia	131
4	Borrower 4	LaGrange Nursing and Rehab Center	2111 West Point Road, LaGrange, Troup County, Georgia	138
5	Borrower 5	Powder Springs Nursing and Rehab Center	3460 Powder Springs Road, Powder Springs, Cobb County, Georgia	208
6	Borrower 6	Oceanside Nursing and Rehab Center	7 Rosewood Avenue, a/k/a 77 Van Horne Street, Tybee Island, Chatham County, Georgia	85
7	Borrower 7	Tara at Thunderbolt Nursing and Rehabilitation Center	3223 Falligant Avenue, Thunderbolt, Chatham County, Georgia	134
8	Borrower 8	Savannah Beach Nursing and Rehab Center	26 Van Horne Street, a/k/a 90 Van Horne Street, Tybee Island, Chatham County, Georgia	50
9	Borrower 9	Attalla Health Care	915 Stewart Avenue SE, Attalla, Etowah County, Alabama	182
10	Borrower 10	Mountain Trace Nursing and Rehabilitation Center	417 Mountain Trace Road, Sylva, Jackson County, North Carolina	106

11	Borrower 11	Autumn Breeze Healthcare Center	1480 Sandtown Road, Marietta, Cobb County, Georgia	109
12	Borrower 12	Southland Healthcare and Rehab Center	606 Simmons Street, Dublin, Laurens County, Georgia	126
13	Borrower 13	College Park Healthcare Center	1765 Temple Avenue, College Park, Fulton County, Georgia	100
14	Borrower 14	Bentonville Manor Nursing Home	224 South Main Street, Bentonville, Benton County, Arkansas	95
15	Borrower 15	River Valley Health and Rehabilitation Center	5301 Wheeler Ave, Fort Smith, Sebastian County, Arkansas	117
16	Borrower 16	Heritage Park Nursing Center	1513 South Dixieland Road, Rogers, Benton County, Arkansas	100
17	Borrower 17	Homestead Manor Nursing Home	826 North Street, Stamps, LaFayette County, Arkansas	94
18	Borrower 18	Eaglewood Care Center	2000 Villa Road, Springfield, Clark County, Ohio	113
19	Borrower 19	Stone County Nursing and Rehabilitation Center	706 Oak Grove Street, Mountain View, Stone County, Arkansas	97
20	Borrower 20	Northridge Healthcare and Rehabilitation	2501 John Ashley Drive, North Little Rock, Pulaski County, Arkansas	140
21	Borrower 21	Little Rock Healthcare and Rehab, a/k/a West Markham Sub Acute & Rehab Center	5720 W. Markham, Little Rock, Pulaski County, Arkansas	157
22	Borrower 22	Woodland Hills HC Nursing	8701 Riley Drive, Little Rock, Pulaski County, Arkansas	140
23	Borrower 23	Abington Place Health & Rehab Center	1516 South Cumberland Street, Little Rock, Pulaski County, Arkansas	120
24	Borrower 24	Glennvue Health and Rehabilitation	721 N. Veterans Boulevard, Glennville, Tatnall County, Georgia	160

25	Borrower 25	Coosa Valley Healthcare	513 Pineview Avenue, Glencoe, Etowah County, Alabama 35905	124
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**GAAP:** Generally accepted accounting principles set forth from time to time in the opinions and pronouncements of the Accounting Principles Board and the American Institute of Certified Public Accountants and statements and pronouncements of the Financial Accounting Standards Board (or agencies with similar functions of comparable stature and authority within the U.S. accounting profession), which are applicable to the circumstances as of the date of determination, provided, however, that interim financial statements or reports shall be deemed in compliance with GAAP despite the absence of footnotes and fiscal year-end adjustments as required by GAAP.

**Gross Revenues:** All income and receipts from all sources, including, without limitations, with respect to each Facility.

**Guarantor:** AdCare.

**Guaranty:** As defined in Section 4.1 hereof.

**Hazardous Substance:** Any substance, chemical, material or waste (i) the presence of which causes a nuisance or trespass of any kind; ii) which is regulated by any federal, state or local governmental authority because of its toxic, flammable, corrosive, reactive, carcinogenic, mutagenic, infectious, radioactive, or other hazardous property or because of its effect on the environment, natural resources or human health and safety, including, but not limited to, petroleum and petroleum products, asbestos containing materials, polychlorinated biphenyls, lead and lead based paint, radon, radioactive materials, flammables and explosives; or (iii) which is designated, classified, or regulated as being a hazardous or toxic substance, material, pollutant, waste (or a similar such designation) under any federal, state or local law, regulation or ordinance, including under any Environmental Law such as the Comprehensive Environmental Response Compensation and Liability Act (42 U.S.C. §9601 et seq.), the Emergency Planning and Community Right to Know Act (42 U.S.C. §11001 et seq.), the Hazardous Substances Transportation Act (49 U.S.C. §1801 et seq.), or the Clean Air Act (42 U.S.C. §7401 et seq.).

**Hedging Agreements:** The following: (i) any ISDA Master Agreement between any Borrower and Lender or any other provider, (ii) any Schedule to Master Agreement between any Borrower and Lender or any other provider, and (iii) all other agreements entered into from time to time by any Borrower and Lender or any other provider relating to Hedging Transactions.

**Hedging Transaction:** Any transaction (including an agreement with respect thereto) now existing or hereafter entered into between any Borrower and Lender or any other provider which is a rate swap, basis swap, forward rate transaction, commodity swap, commodity option, equity or equity index swap, equity or equity index option, bond option, interest rate option, foreign exchange transaction, cap transaction, floor transaction, collar transaction, forward transaction, currency swap transaction, cross-currency rate swap transaction, currency option or

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any other similar transaction (including any option with respect to any of these transactions) or any combination thereof, whether linked to one or more interest rates, foreign currencies, commodity prices, equity prices or other financial measures.

**Interest Charges:** With respect to any party, for any period, the sum of: (i) all interest, charges and related expenses payable with respect to that period to a lender in connection with borrowed money or the deferred purchase price of assets that are treated as interest in accordance with GAAP, plus (ii) the portion of Capitalized Lease Obligations with respect to that period that should be treated as interest in accordance with GAAP, plus (iii) all charges paid or payable (without duplication) during that period with respect to any hedging agreements.

**Leases:** Leases by Owners to each of Borrower 11 through Borrower 24 of the respective Projects and subleases by Sublessor to each of Borrower 1 through Borrower 8 of the respective Projects dated as follows:

<b>Facility</b>	<b>Borrower</b>	<b>Owner/Sublessor</b>	<b>Date of Lease/Sublease</b>
1	Borrower 1	Owner, Master Lease Lessor - William Foster Sublessor - ADK Georgia, LLC	Master Lease - August 1, 2010 Sublease - August 1, 2010
2	Borrower 2	Owner, Master Lease Lessor - William Foster Sublessor - ADK Georgia, LLC	Master Lease - August 1, 2010 Sublease - August 1, 2010
3	Borrower 3	Owner, Master Lease Lessor - William Foster Sublessor - ADK Georgia, LLC	Master Lease - August 1, 2010 Sublease - August 1, 2010
4	Borrower 4	Owner, Master Lease Lessor - William Foster Sublessor - ADK Georgia, LLC	Master Lease - August 1, 2010 Sublease - August 1, 2010

5	Borrower 5	Owner, Master Lease Lessor - William Foster Sublessor - ADK Georgia, LLC	Master Lease - August 1, 2010 Sublease - August 1, 2010
6	Borrower 6	Owner, Master Lease Lessor - William Foster Sublessor - ADK Georgia, LLC	Master Lease - August 1, 2010 Sublease - September 1, 2010
7	Borrower 7	Owner, Master Lease Lessor - William Foster Sublessor - ADK Georgia, LLC	Master Lease - August 1, 2010 Sublease - September 1, 2010
8	Borrower 8	Owner, Master Lease Lessor - William Foster Sublessor - ADK Georgia, LLC	Master Lease - August 1, 2010 Sublease - September 1, 2010
9	Borrower 9	Owner, Borrower 9	None
10	Borrower 10	Owner, Borrower 10	None

11	Borrower 11	Owner, Mt. Kenn Property Holdings, LLC	May 1, 2011
12	Borrower 12	Owner, Erin Property Holdings, LLC	May 1, 2011
13	Borrower 13	Owner, CP Property Holdings, LLC	September 6, 2011
14	Borrower 14	Owner, Benton Property Holdings, LLC	August 31, 2011
15	Borrower 15	Owner, Valley River Property Holdings, LLC	August 31, 2011
16	Borrower 16	Owner, Park Heritage Property Holdings, LLC	August 31, 2011
17	Borrower 17	Owner, Homestead Property Holdings, LLC	August 31, 2011
18	Borrower 18	Owner, Woodland Manor Property Holdings, LLC	December 29, 2011
19	Borrower 19	Owner, Mount V Property Holdings, LLC	November 30, 2011
20	Borrower 20	Owner, Northridge HC&R Property Holdings, LLC	April 1, 2012
21	Borrower 21	Owner, Little Rock HC&R Property Holdings, LLC	April 1, 2012
22	Borrower 22	Owner, Woodland Hills HC Property Holdings, LLC	April 1, 2012
23	Borrower 23	Owner, APH&R Property Holdings, LLC	June 1, 2012
24	Borrower 24	Owner, Glenvue H&R Property Holdings, LLC	June 19, 2012
25	Borrower 25	Owner, Borrower 25	None

**Legal Requirements:** As to any person or party, the organizational and governing documents of such person or party, and any law, treaty, rule or regulation or determination of an arbitrator or a court or other governmental authority, in each case applicable to or binding upon such person or party or any of its property or to which such person or party or any of its property is subject.

**Lender:** The PrivateBank and Trust Company, an Illinois banking corporation.

**Letter of Credit:** An Irrevocable Standby Letter of Credit in the Letter of Credit Amount, issued by Lender in favor one or more commercial insurance companies as beneficiary, for the account of one or more of Borrowers or AdCare.

**Letter of Credit Amount:** \$100,000, it being understood that the Letter of Credit Amount is a part of the Loan Amount and not in addition to the Loan Amount.

**Letter of Credit Documents:** The following: (i) the Master Letter of Credit Agreement dated as of February 14, 2012, originally from Borrowers 14 through 19, and joined in herein by

the other Borrowers, and (ii) any Application for the issuance of a Letter of Credit from Borrowers in favor of Lender.

**Loan:** The loan to be made pursuant to this Agreement, including, without limitation, the issuance of any Letter of Credit

**Loan Amount:** \$10,600,000, which includes the \$100,000 Letter of Credit Amount.

**Loan Documents:** This Agreement, the documents specified in Article 4 hereof, the Letter of Credit Documents, and any other instruments evidencing, securing or guarantying obligations of any party under the Loan, and any Bank Product Agreements to which Lender or any of its Affiliates is a party, including, without limitation, any Hedging Agreements to which Lender is a party.

**Loan Expenses:** All interest, charges, costs and expenses incurred by Lender in connection with the Loan, including, but not limited to, (i) interest due on the Loan and any points, loan fees, service charges, commitment fees or other fees due to Lender in connection with the Loan; (ii) all title examination, survey, escrow, filing, search, recording and registration fees and charges; (iii) all fees and disbursements of architects, engineers and consultants engaged by any Borrower and Lender; (iv) all documentary stamp and other taxes and charges imposed by law on the issuance or recording of any of the Loan Documents; (v) all appraisal fees; (vi) all title, casualty, liability, payment, performance or other insurance or bond premiums; (vii) all reasonable fees and disbursements of legal counsel engaged by Lender in connection with the Loan, including, without limitation, counsel engaged in connection with the origination, negotiation, document preparation, consummation, enforcement or administration of this Agreement or any of the Loan Documents; and (viii) any amounts required to be paid by any Borrower under this Agreement or any Loan Document after the occurrence of an Event of Default under this Agreement or any of the other Loan Documents.

**Loan Opening:** The first disbursement of Loan Proceeds.

**Loan Proceeds:** All amounts advanced as part of the Loan, whether advanced directly to Borrowers or otherwise, it being understood that any amount drawn on the Letter of Credit shall constitute Loan Proceeds.

**Master Lease:** The Lease Agreement dated as of August 1, 2010, as amended by a First Amendment to Lease dated as of August 31, 2010, by and between William M. Foster, as Lessor, and Sublessor, as Lessee.

**Maturity Date:** September 20, 2015.

**Net Income:** With respect to any party, for any period, the net income (or loss) of such party for such period as determined in accordance with GAAP, excluding any gains from dispositions of assets, any extraordinary gains and any gains from discontinued operations.

**Note:** As defined in Section 4.1 hereof.

**Old Operator:** A prior operator of a Facility which is being operated by a Borrower under an Operations Transfer Agreement.

**Operations Transfer Agreement:** An agreement under which, for a temporary period, a Borrower operates its Facility under the license or billing numbers, or both, of a prior operator of such Facility.

**Owners:** In the case of each Facility, the Owner shown in the definition of the term Lease in this Section.

**Permitted Substance:** Substances used by any Borrower or any Owner in the ordinary course of its business, or by any Borrower, any Owner and their contractors and subcontractors in the course of construction on or at any Facility or any Project, including, without limitation, medical waste, and in the case of all of the foregoing, used in compliance with all Environmental Laws.

**Prohibited Transfer:** As defined in Section 7.10 hereof.

**Project:** With respect to each Facility, the land, building and other improvements on and within which such Facility is located, the ownership, leasing and subleasing of each of which is as shown in the definition of the term Leases in this Section.

**Rental Expense:** With respect to any party, for any period, the rental expense for real estate leased by such party as lessee for such period as determined in accordance with GAAP.

**Signing Entity:** Each entity (other than a Borrower itself) that appears in the signature block of any Borrower in this Agreement, if any.

**State:** In the case of each Facility, the State in which such Facility is located.

**Sublessor:** ADK Georgia, LLC, a Georgia limited liability company

1.2 **Other Terms Defined in Code.** All other capitalized words and phrases used herein and not otherwise specifically defined herein shall have the respective meanings assigned to such terms in the Code, to the extent the same are used or defined therein.

## **ARTICLE 2**

### **REPRESENTATIONS AND WARRANTIES**

2.1 **Representations and Warranties.** To induce Lender to execute and perform this Agreement, each Borrower hereby represents, covenants and warrants to Lender as follows:

(a) Each Borrower is a limited liability company duly organized, validly existing and in good standing under the laws of the State of which is stated in the Preambles to this Agreement, and if such State is not the State in which its Facility is located, such Borrower is duly registered or qualified to transact business and in good

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standing in the State in which its Facility is located. Each Borrower has full power and authority to conduct its business as presently conducted, to lease and operate its Facility, to enter into this Agreement and to perform all of its duties and obligations under this Agreement and under the Loan Documents, all of which has been duly authorized by all necessary Legal Requirements applicable to such Borrower. Each Signing Entity is duly organized, validly existing and in good standing under the laws of the State in which it is organized, has full power and authority to conduct its business as presently conducted and to execute this Agreement and the other Loan Documents to which the applicable Borrower is a party in the capacity shown in the signature block of such Borrower contained in this Agreement, and such execution has been duly authorized by all necessary Legal Requirements applicable to such Signing Entity. Neither any Borrower nor Guarantor has been convicted of a felony and there are no proceedings or investigations being conducted involving criminal activities of either any Borrower or Guarantor. The direct and indirect ownership of Borrowers is as shown in **Exhibit A** attached to this Agreement.

(b) AdCare is a corporation duly organized, validly existing and in good standing under the laws of the State of Ohio. AdCare has full power and authority to conduct its business as presently conducted and to enter into and to perform the Guaranty and the other Loan Documents to which it is a party and to perform all of its duties and obligations thereunder, all of which has been duly authorized by all necessary Legal Requirements applicable to AdCare.

(c) Each Borrower and Guarantor is able to pay its debts as such debts become due, and each has capital sufficient to carry on its respective present businesses and transactions and all businesses and transactions in which it is about to engage. Neither any Borrower nor Guarantor (i) is bankrupt or insolvent, (ii) has made an assignment for the benefit of its respective creditors, (iii) has had a trustee or receiver appointed, (iv) has had any bankruptcy, reorganization or insolvency proceedings instituted by or against it, or (v) shall be rendered insolvent by its execution, delivery or performance of the Loan Documents or by the transactions contemplated thereunder. There is no Uniform Commercial Code financing statement on file that names any Borrower or Guarantor as debtor and covers any of the collateral for the Loan, and there is no judgment or tax lien outstanding against any Borrower or Guarantor.

(d) This Agreement, the Note, the other Loan Documents and any other documents and instruments required to be executed and delivered by any Borrower or Guarantor in connection with the Loan, when executed and delivered, will constitute the duly authorized, valid and legally binding obligations of the party required to execute the same and will be enforceable strictly in accordance with their respective terms (except to the extent that enforceability may be affected or limited by applicable bankruptcy, insolvency and other similar debtor relief laws affecting the enforcement of creditors' rights generally); and no basis exists for any claim against Lender under this Agreement, under the Loan Documents or with respect to the Loan; and enforcement of this Agreement and the Loan Documents is subject to no defenses of any kind.

(e) The execution, delivery and performance of this Agreement, the Note, the other Loan Documents and any other documents or instruments to be executed and delivered by any Borrower or Guarantor pursuant to this Agreement or in connection with the Loan and the use and occupancy of any Facility will not: (i) violate any Legal Requirements applicable to any Borrower or any Signing Entity, or (ii) conflict with, be inconsistent with, or result in any breach or default of any of the terms, covenants, conditions or provisions of any indenture, mortgage, deed of trust, instrument, document, agreement or contract of any kind to which any Borrower, Guarantor or any Signing Entity is a party or by which any of them may be bound. Neither any Borrower, Guarantor nor any Signing Entity is in default (without regard to grace or cure periods) under any contract or agreement to which it is a party, the effect of which default will adversely affect the performance by any Borrower or Guarantor of its obligations pursuant to and as contemplated by the terms and provisions of this Agreement or the other Loan Documents.

(f) No condition, circumstance, event, agreement, document, instrument, restriction, litigation or proceeding, or threatened litigation or proceeding or basis therefor, exists which could (i) adversely affect the validity or priority of the liens and security interests granted Lender under the Loan Documents; (ii) materially adversely affect the ability of any Borrower or Guarantor to perform their obligations under the Loan Documents; or (iii) constitute a Default or Event of Default under this Agreement or any of the other Loan Documents.

(g) It is a condition of this Agreement and the Loan that each Facility and the use and occupancy of each Facility do not violate or conflict with any applicable law, statute, ordinance, rule, regulation or order of any kind, including, without limitation, Environmental Laws, zoning, building, land use, noise abatement, occupational health and safety or other laws, any building permit or any Declarations, and if a third-party is required under any Declarations or other documents, to consent to use or operation of such Facility, the Borrower which is the lessee thereof has obtained such approval from such party, and to the best of Borrowers' knowledge, such condition is satisfied. In addition, and without limiting the foregoing, each Borrower shall (i) ensure that no person or entity which owns a controlling interest in or otherwise controls such Borrower is or shall be listed on the Specially Designated Nationals and Blocked Person List or other similar lists maintained by the Office of Foreign Assets Control ("**OFAC**"), the Department of the Treasury or included in any Executive Orders, (ii) not use or permit the use of any Loan Proceeds to violate any of the foreign asset control regulations of OFAC or any enabling statute or Executive Order relating thereto, and (iii) comply with all applicable Bank Secrecy Act laws and regulations, as amended.

(h) Each of the following is a condition of this Agreement and the Loan: Except as disclosed in writing to Lender, including, without limitation, in any environmental site assessment delivered to Lender, the Facilities have never been used for any activities which, directly or indirectly, involve the use, generation, treatment, storage, transportation or disposal of any Hazardous Substances other than Permitted Substances, and no Hazardous Substances other than Permitted Substances exist on the Facilities or under the Facilities or in any surface waters or groundwaters on or under the

Facilities. The Facilities and their existing and prior uses have at all times complied with and will comply with all Environmental Laws, and Borrowers have not violated any Environmental Laws. To the best of Borrowers' knowledge, each of such conditions is satisfied.

(i) There are no facilities on any Facility which are subject to reporting under any State laws or Section 312 of the Federal Emergency Planning and Community Right-to-Know Act of 1986 (42 U.S.C. Section 11022), and federal regulations promulgated thereunder. Except as disclosed in writing to Lender, including, without limitation, in any environmental site assessment delivered to Lender, each Facility does not contain any underground or above ground storage tanks.

(j) All financial statements submitted by any Borrower or Guarantor to Lender in connection with the Loan are true and correct in all material respects, have been prepared in accordance with GAAP consistently applied, and fairly present the respective financial conditions and results of operations of the entities and persons which are their subjects.

(k) This Agreement and all financial statements, budgets, schedules, opinions, certificates, confirmations, applications, rent rolls, affidavits, agreements, and other materials submitted to Lender in connection with or in furtherance of this Agreement by or on behalf of any Borrower or Guarantor fully and fairly state the matters with which they purport to deal, and neither misstate any material fact nor, separately or in the aggregate, fail to state any material fact necessary to make the statements made not misleading in any material respect.

(l) All utility and municipal services required for the construction, occupancy and operation of each Facility, including, but not limited to, water supply, storm and sanitary sewage disposal systems, cable services, gas, electric and telephone facilities are available for use by and currently provide service to such Facility.

(m) Subject to the provisions of Section 7.7(b) of this Agreement, all governmental permits and licenses required by applicable law in order for (i) the applicable Owners to own and lease their Projects to Borrower 11 through Borrower 24 and to Sublessor under the Master Lease, (ii) Sublessor to sublease the applicable Projects to Borrower 1 through Borrower 8, and (iii) each Borrower to operate its Facility, have been validly issued and are in full force.

(n) Each of the following is a condition of this Agreement and the Loan: The storm and sanitary sewage disposal system, water system, drainage system and all mechanical systems of each Facility comply with all applicable laws, statutes, ordinances, rules and regulations, including, without limitation, all Environmental Laws. The applicable environmental protection agency, pollution control board and/or other governmental agencies having jurisdiction of such Facility have issued their permits for the construction, tap-on and operation of those systems. To the best of Borrowers' knowledge, each of such conditions is satisfied.



(o) It is a condition of this Agreement and the Loan that all utility, parking, access (including curb-cuts and highway access), construction, recreational and other permits and easements required for the use of each Facility have been granted and issued, and to the best of Borrowers' knowledge, such condition is satisfied.

(p) The Loan, including interest rate, fees and charges as contemplated hereby, is a "business loan" within the meaning of subparagraph (1)(c) contained in Section 205/4 of Chapter 815 of the Illinois Compiled Statutes, as amended; the Loan is an exempted transaction under the Truth In Lending Act, 12 U.S.C. §1601 et seq.; and the Loan does not, and when disbursed will not, violate the provisions of the usury laws of the State, any consumer credit laws or the usury laws of any state which may have jurisdiction over this transaction, any Borrower or any property securing the Loan.

(q) The Master Lease is in full force and effect and no Defaults or Events of Default on the part of Sublessor have occurred and are continuing thereunder. Each Lease is in full force and effect and no Defaults or Events of Default on the part of the applicable Borrower have occurred and are continuing thereunder. No Borrower other than Borrower 23 and Borrower 24 is operating its Facility under any Operations Transfer Agreement. Each Operations Transfer Agreement is in full force and effect and no Defaults or Events of Default on the part of any Borrower or any Old Operator have occurred and are continuing thereunder.

(r) All Employee Plans of each Borrower meet the minimum funding standards of Section 302 of ERISA and 412 of the Internal Revenue Code where applicable, and each such Employee Plan that is intended to be qualified within the meaning of Section 401 of the Internal Revenue Code of 1986 is qualified. No withdrawal liability has been incurred under any such Employee Plans and no "Reportable Event" or "Prohibited Transaction" (as such terms are defined in ERISA), has occurred with respect to any such Employee Plans, unless approved by the appropriate governmental agencies. Each Borrower has promptly paid and discharged all obligations and liabilities arising under ERISA of a character which if unpaid or unperformed might result in the imposition of a lien against any of its properties or assets.

(s) Each of the following is a condition of this Agreement and the Loan: There are no strikes, lockouts or other labor disputes pending or threatened against any Borrower, hours worked by and payment made to employees of any Borrower have not been in violation of the Fair Labor Standards Act or any other applicable law, and no unfair labor practice complaint is pending, or threatened, against any Borrower before any governmental authority. To the best of Borrowers' knowledge, each of such conditions is satisfied

(t) Subject to the provisions of Section 7.7(b) of this Agreement, each Facility has all necessary licenses, permits and certifications required by any applicable governmental authority to operate and maintain a skilled nursing facility therein with its current number of beds in service, and participates in the Medicare and Medicaid programs. Each Borrower has complied and will comply with all applicable requirements of the United States of America, the State of Arkansas and all applicable

local governments, and of its agencies and instrumentalities, necessary to operate and maintain its Facility as such a facility. All utilities necessary for use, operation and occupancy of each Project and each Facility are available to such Project and such Facility. All requirements for unrestricted use of each Project and each Facility as a skilled nursing facility under the rules and regulations of each department and agency of the State having jurisdiction over such Project or such Facility, have been and will continue to be fulfilled. All building, zoning, safety, health, fire, water district, sewerage and environmental protection agency and any other permits or licenses which are required by any governmental authority for use, occupancy and operation of each Project and each Facility as a skilled nursing facility have been obtained and are and will be maintained in full force and effect. Neither any Borrower, any Owner, any Facility, any Project nor Sublessor or Guarantor is subject to any corporate

integrity agreement, compliance agreement or other agreement with any governmental authority or agency governing the operation of any Project or any Facility or the operations of any Borrower, any Owner, Sublessor or Guarantor.

(u) This Agreement creates a valid security interest in favor of Lender in the Collateral and, when properly perfected by filing in the appropriate jurisdictions, or by possession or control of such Collateral by Lender or delivery of such Collateral to Lender, shall constitute a valid, perfected, first-priority security interest in such Collateral, to the extent that a valid, perfected, first-priority security interest in such Collateral may be perfected by filing or by possession or control of such Collateral.

(v) Each Borrower, each Owner and Sublessor are in compliance in all material respects with all laws, orders, regulations and ordinances of all federal, foreign, state and local governmental authorities binding upon or affecting the business, operation or assets of any Borrower, any Owner or Sublessor. Neither any Borrower nor any Owner or Sublessor: (i) has had a civil monetary penalty assessed against it under the Social Security Act (the “**SSA**”) Section 1128(a), other than nominal amounts for violations which were not of a material nature, (ii) has been excluded from participation under the Medicare program or under a State health care program as defined in the SSA Section 1128(h) (“**State Health Care Program**”), or (iii) has been convicted (as that term is defined in 42 C.F.R. Section 1001.2) of any of the following categories of offenses as described in the SSA Section 1127(a) and (b)(1), (2), (3): (A) criminal offenses relating to the delivery of an item or service under Medicare or any State Health Care Program; (B) criminal offenses under federal or state law relating to patient neglect or abuse in connection with the delivery of a health care item or service; (C) criminal offenses under federal or state law relating to fraud, theft, embezzlement, breach of fiduciary responsibility, or other financial misconduct in connection with the delivery of a health care item or service or with respect to any act or omission in a program operated by or financed in whole or in part by any federal, state or local government agency; (D) federal or state laws relating to the interference with or obstruction of any investigations into any criminal offense described in (A) through (C) above; or (E) criminal offenses under federal or state law relating to the unlawful manufacture, distribution, prescription or dispensing of a controlled substance. Without limiting the generality of the foregoing, neither any Borrower nor any Owner or Sublessor is in default in the performance, observance or fulfillment of any of the obligations, covenants or conditions contained in

any Medicare or Medicaid Provider Agreement or other agreement or instrument to which any Borrower or any Owner or Sublessor is a party, which default has resulted in, or if not remedied within any applicable grace period could result in, the revocation, termination, cancellation or suspension of the Medicare or Medicaid Certification of any Borrower or any Owner or Sublessor.

2.2 **Continuation of Representations and Warranties.** Each Borrower hereby covenants, warrants and agrees that the representations and warranties made in Section 2.1 hereof shall be and shall remain true and correct in all material respects at the time of the Loan Opening and at all times thereafter so long as any part of the Loan shall remain outstanding. Each request for disbursement of Loan Proceeds shall constitute a reaffirmation that these representations and warranties are true in all material respects as of the date of such request and will be true in all material respects on the date of the disbursement.

### **ARTICLE 3**

#### **THE LOAN**

##### **3.1 Agreement to Lend.**

(a) On the terms of and subject to the conditions of this Agreement, Lender agrees to make advances on the Loan at such times as Borrowers may from time to time request until, but not including, the Maturity Date, and in such amounts as Borrowers may

from time to time request, provided, however, that at any time, the aggregate principal balance outstanding on the Loan, plus the combined face amount of all outstanding Letters of Credit, shall not exceed the Availability. The Loan shall be a revolving loan and may be repaid and, subject to the terms and conditions hereof, borrowed again up to, but not including the Maturity Date unless the Loan is otherwise accelerated, terminated or extended as provided in this Agreement. The Loan shall be used by Borrowers as working capital for the operation of the Facilities. The Loan shall be disbursed in accordance with Article 5 of this Agreement, including, without limitation, the borrowing procedures contained in Section 5.3 of this Agreement. A portion of the Loan may be used for the issuance of the Letter of Credit in accordance with Section 3.2 of this Agreement. The Loan shall be evidenced by the Note executed by Borrowers and shall be guaranteed by Guarantor pursuant to the Guaranty.

(b) The provisions of this paragraph (b) shall apply notwithstanding any other provisions of this Agreement. AdCare or certain of its Affiliates, or both, have a liability to the State of Georgia for certain taxes in the amount of \$1,250,145 (the "**Taxes**"). The parties have determined that on the date of this Agreement there is sufficient Availability for a disbursement to be made on the Loan to pay the Taxes. On or as soon as practicable after the date of this Agreement, Lender shall make a disbursement on the Loan in the amount of the Taxes and Borrowers shall promptly use such disbursement to pay the Taxes. Borrowers shall provide Lender with copies of the checks which are issued to pay the Taxes at the time the checks are issued, and shall within 30 days after the date of this Agreement provide Lender with copies of cancelled checks evidencing the payment of the Taxes. If within 30 days after the date of this Agreement Borrowers have not provided Lender with such cancelled checks or other evidence of

the payment of the Taxes satisfactory to Lender, or any portion thereof, the Taxes or such portion thereof shall be deemed to be unpaid, and the Availability shall be deemed to be reduced by the amount of the unpaid Taxes or such portion thereof until such time as Borrowers have provided Lender with such cancelled checks or other evidence of the payment of the Taxes or such portion thereof satisfactory to Lender.

### 3.2 **Letter of Credit.**

(a) Lender previously issued the Letter of Credit in the amount of \$100,000 pursuant to the Master Letter of Credit Agreement to which Borrowers 14 through 19 were a party, and an Application. The Letter of Credit is currently outstanding in the face amount of \$100,000. Such Letter of Credit shall be deemed to be a Letter of Credit for all purposes of this Agreement.

(b) Borrowers 1 through 13 and Borrowers 20 through 25 hereby join in and agree to be jointly and severally obligated under and bound by each of the Letter of Credit Documents.

(c) Any amounts drawn on any Letter of Credit shall be evidenced by the Letter of Credit Documents and the Note and shall be deemed to be amounts disbursed and outstanding thereunder as of the date such amounts are drawn. Notwithstanding anything to the contrary contained in this Agreement or the Note, amounts drawn on the Letter of Credit shall bear interest at the rate provided in the Letter of Credit Documents, and shall be payable by Borrowers on the terms provided in the Letter of Credit Documents.

(d) The Letter of Credit Documents shall be secured by the security interests created under this Agreement, and the obligations of Borrowers under the Letter of Credit Documents shall be guaranteed pursuant to the Guaranty. For the avoidance of doubt, the security interests created in Sections 3.2(i), 3.7(f), 4.2(b), 7.8(b) and 8.1 of this Agreement shall secure the reimbursement by Borrowers of all amounts drawn on any Letter of Credit and the payment and performance of all of the obligations of Borrowers under the Letter of Credit Documents.

(e) Borrowers paid a non-refundable annual letter of credit fee to Lender in advance on the date of the issuance of the Letter of Credit. Borrowers shall pay a non-refundable annual letter of credit fee to Lender in advance on each anniversary of the date of the issuance of the Letter of Credit, in an amount equal to 2.5% of the face amount of the Letter of Credit.

(f) Borrowers hereby covenant and agree with Lender that Borrowers shall promptly pay any amount due under the Letter of Credit Documents as and when the same shall become due and payable.

(g) Each of the Letter of Credit Documents shall be subject to the provisions of Section 12.2 of this Agreement, which Section is hereby incorporated into and made of part of each of the Letter of Credit Documents.

(h) If any Letter of Credit has not been presented for a draw pursuant to its terms, such Letter of Credit shall terminate upon the earlier to occur of the stated expiry date thereof or the date such Letter of Credit is returned to the Lender for cancellation. Except as provided in paragraph (i) of this Section, in no event shall the Lender be required to release the liens and

security interests created by this Agreement and the other Loan Documents prior to the time that all Letters of Credit have so terminated.

(i) If at a time when a Letter of Credit is outstanding, the Maturity Date of the Loan and the Note occurs and is not extended, or the obligation of Lender to make additional cash disbursements on the Loan (other than by paying draws on Letters of Credit) under the Loan Agreement otherwise terminates, Borrowers shall immediately deposit into an interest-bearing cash collateral deposit account in the name of Borrowers held by Lender (the "**L/C Cash Collateral Account**"), an amount equal to the then face amount of such Letter of Credit (a "**Deposit**"). Borrowers acknowledge and agree that the L/C Cash Collateral Account and amounts on deposit therein will be subject to the security interests in the Borrowers' Deposit Accounts (as defined in the Code) and amounts on deposit therein which are created under Section 3.7(f) of this Agreement. The failure of Borrowers to make any Deposit as provided above shall constitute an Event of Default under this Agreement, and upon or at any time after the occurrence of such Event of Default, Lender may exercise any or all of its remedies under the Loan Documents and under applicable law. Provided that Borrowers have made any required Deposit as provided above, and Lender no longer has any obligation to make any additional cash disbursements on the Loan (other than by paying draws on Letters of Credit), and the Loan has otherwise been paid in full, and no Default or Event of Default under this Agreement has occurred and is continuing, Lender shall release the liens and security interests created by this Agreement and the other Loan Documents, other than the security interest in the L/C Cash Collateral Account. Provided that no Default or Event of Default under this Agreement has occurred and is continuing, Lender shall release the L/C Cash Collateral Account at such time as Lender no longer has any liability under any Letter of Credit and all obligations to Lender under this Agreement and the other Loan Documents have been fully paid and performed.

3.3 **Interest.** Interest on funds advanced hereunder shall –

- (i) From the Loan Opening until the Maturity Date, accrue at the interest rates provided for in the Note;
- (ii) Be computed upon advances of the Loan from and including the date of each advance by Lender to or for the account of Borrowers (whether to an escrow or otherwise), on the basis of a 360-day year and the actual number of days elapsed in any portion of a month in which interest is due; and
- (iii) Be paid by Borrowers to Lender together with principal payments, if any, in the manner set forth in the Note.

3.4 **Principal Payments; Maturity Date.**

- (a) Prior to the Maturity Date, principal payments, if any, shall be made as provided in the Note.

(b) In the event the outstanding principal balance of the Loan together with the combined face amount of all outstanding Letters of Credit at any time exceeds the Availability, Borrowers shall make such repayments of the Loan as shall be necessary to eliminate such excess. In the event that at any time there is no principal balance outstanding on the Loan and

the combined face amount of all outstanding Letters of Credit exceeds the Availability, then Borrowers shall immediately deposit the amount of such excess in a cash collateral account as security for the Loan in the name of one or more of Borrowers with Lender, and shall maintain such amount on deposit in such cash collateral account so long as and to the extent that the face amount of the combined face amount of all outstanding Letters of Credit exceeds the Availability.

(c) The entire principal balance of the Note and all accrued and unpaid interest thereon shall be due, if not sooner paid, on the Maturity Date.

3.5 **Loan Fee.** In consideration of Lender's agreement to make the Loan, on the date of the execution and delivery of this Agreement, Borrowers shall pay to Lender a non-refundable fee in the amount of \$79,500. Borrowers shall also pay fees to Lender in connection with the Letter of Credit as provided in Section 3.2(e) of this Agreement.

3.6 **Non-Utilization Fee.** Borrowers agree to pay to Lender a non-utilization fee in an equal to 0.50% per annum calculated on the difference between the Loan Amount and the sum of the daily average amount of principal outstanding on the Loan plus the daily average face amount of the outstanding Letter of Credit. Such non-utilization fee shall be (i) calculated on the basis of a year consisting of 360 days, (ii) paid for the actual number of days elapsed, and (iii) payable quarterly in arrears on the last day of each March, June, September and December, commencing on September 30, 2012, on the Maturity Date of the Loan, and on the date of the occurrence of any Event of Default under this Agreement. The amount of such fee payable on September 30, 2012, shall be calculated for the period commencing on the date of this Agreement and ending on September 30, 2012.

3.7 **Uniform Commercial Code Matters.**

(a) All references in this Agreement and the other Loan Documents to the Code are to the Code as from time to time in effect.

(b) Each Borrower represents and warrants to Lender as follows:

(i) The exact legal name of such Borrower is as stated in the first paragraph of this Agreement.

(ii) The nature of the Borrower entity and the State in which it is organized is as stated in the first paragraph of this Agreement. The organizational numbers of Borrowers in such State are as follows:

<b>Borrower</b>	<b>Organizational Number</b>
Borrower 1	10049720
Borrower 2	10049712
Borrower 3	10049698
Borrower 4	10049705
Borrower 5	10049694
Borrower 6	10049766

Borrower 7	10049762
Borrower 8	10049771
Borrower 9	10010525
Borrower 10	1970736
Borrower 11	10081155
Borrower 12	10081149
Borrower 13	10081152
Borrower 14	11036042
Borrower 15	11036049
Borrower 16	11036045
Borrower 17	11036039
Borrower 18	11070717
Borrower 19	11064313
Borrower 20	12008905
Borrower 21	12008900
Borrower 22	12008912
Borrower 23	12013594
Borrower 24	12030306
Borrower 25	10010522

(iii) The address of such Borrower's chief executive office is Two Buckhead Plaza, 3050 Peachtree Road NW, Suite 355, Atlanta, Georgia 30305.

(iv) Each Borrower has no place of business other than the chief executive office referred to in (iii) above, at the address for notices set forth in Section 12.10 of this Agreement, at its Facility in the State, and at 1145 Hembree Road, Roswell, Georgia 30076.

(c) Each Borrower shall not, without not less than 30 days' prior written notice to Lender, change its legal name, the nature of the Borrower entity, the State in which it is organized, its organizational number in the State in which it is organized, if any, the address of its chief executive office, or the addresses of its other places of business, from those referred to in paragraph (b) of this Section.

(d) Except as otherwise disclosed to Lender in writing, the location of each Borrower's books and records and all Collateral is at its Facility, and each Borrower shall promptly notify Lender of any change in such location. Each Borrower shall not remove or permit the Collateral to be removed from such location without the prior written consent of Lender, except for Inventory sold in the usual and ordinary course of such Borrower's business.

(e) Each Borrower acknowledges that by entering into the security agreements contained in this Agreement and the other Loan Documents, such Borrower has authorized the filing of financing statements and amendments under the Code covering the collateral described in such security agreements, without the signature of such Borrower.

(f) As additional security for the payment and performance of all of the obligations of Borrowers under this Agreement and the other Loan Documents, each Borrower hereby grants

to Lender a security interest in all Deposit Accounts (as defined in the Code) from time to time maintained by such Borrower with Lender, all cash and investments from time to time on deposit in all such Deposit Accounts, and all proceeds of all of the foregoing.

## ARTICLE 4

### LOAN DOCUMENTS

4.1 **Loan Documents**. As a condition precedent to the Loan Opening, Borrowers agree that they will deliver the following Loan Documents to Lender at or prior to the Loan Opening, all of which must be satisfactory to Lender and Lender's counsel in form, substance and execution:

(a) **Promissory Note**. A Promissory Note (the "**Note**") dated the date hereof, executed by Borrowers jointly and severally and made payable to the order of Lender, in the Loan Amount.

(b) **Financing Statements**. Uniform Commercial Code Financing Statements as required by Lender to perfect all security interests granted by this Agreement and the other Loan Documents.

(c) **Guaranty**. A Guaranty of Payment and Performance dated as of even date herewith (the "**Guaranty**"), executed by Guarantor to and for the benefit of Lender, guaranteeing to Lender the payment and performance of all obligations of Borrowers in connection with the Loan.

(d) **Borrowing Base Certificate**. A Borrowing Base Certificate in the form prepared by Lender, certified as accurate by Borrowers and acceptable to Lender.

(e) **Letter of Credit Documents**. The Letter of Credit Documents.

(f) **Other Loan Documents**. Such other documents and instruments as further security for the Loan as Lender may reasonably require.

#### 4.2 **Interest Rate Protection**.

(a) Any and all obligations, contingent or otherwise, whether now existing or hereafter arising, of each Borrower arising under or in connection with all Hedging Transactions and Hedging Agreements to which Lender is a party shall be secured by all of the collateral for the Loan.

(b) As additional security for the payment and performance of all of the obligations of Borrowers under this Agreement and the other Loan Documents, Borrowers hereby pledge and assign to Lender, and grant to Lender a first lien on and a first priority security interest in, (i) all Hedging Transactions from time to time entered into by any Borrower with Lender or any other provider, (ii) all contracts from time to time entered into by any Borrower with Lender or any other provider with respect to such Hedging Transactions, (iii) all amounts from time to time

payable to any Borrower under such Hedging Transactions and contracts, and (iv) all proceeds of all of the foregoing.

## ARTICLE 5

### LOAN DISBURSEMENTS

5.1 **Conditions to Loan Opening.** As conditions precedent to the Loan Opening, Borrowers (i) shall satisfy all applicable conditions and requirements contained in other Sections of this Agreement, and (ii) shall furnish the following to Lender at or prior to the Loan Opening, all of which must be satisfactory to Lender and Lender's counsel in form, content and execution:

(a) **Insurance Policies.** Evidence satisfactory to Lender that the insurance coverages required by Section 7.2 hereof are in force.

(b) **Utilities; Licenses; Permits.** Evidence satisfactory to Lender that –

(i) All utility and municipal services required for the occupancy and operation of each Facility are available and currently servicing such Facility;

(ii) Subject to the provisions of Section 7.7(b) of this Agreement, all permits, licenses and governmental approvals required by applicable law to occupy and operate each Project and each Facility have been issued, are in full force and all fees therefor have been fully paid;

(iii) The storm and sanitary sewage disposal system, the water system and all mechanical systems serving each Facility comply with all applicable laws, ordinances, rules and regulations, including Environmental Laws and the applicable environmental protection agency, pollution control board and/or other governmental agencies having jurisdiction of each Facility have issued their permits for the operation thereof; and

(iv) All utility, parking, access (including curb-cuts and highway access), recreational and other easements and permits required or, in Lender's judgment, necessary for the use of each Facility have been granted or issued.

(c) **Searches.** A report from the appropriate filing officers of the state and counties in which the Facilities are located, indicating that no judgments, tax or other liens, security interests, leases of personalty, financing statements or other encumbrances are of record or on file encumbering any collateral for the Loan, and that there are no judgments, tax liens, pending litigation or bankruptcy actions outstanding with respect to Borrowers and Guarantor.

(d) **Attorney's Opinion.** Opinions of counsel to Borrowers and Guarantor addressing such issues as Lender may request, subject to assumptions and qualifications satisfactory to Lender.

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(e) **Organizational Documents.** Organizational documents, any resolutions required by such documents, and good standing certificates, for Borrowers and the other parties to the Loan Documents, and for any entities executing Loan Documents on behalf of Borrowers or any other parties to the Loan Documents.

(f) **Master Lease and Leases.** Copies of the Master Lease and of the Leases and such agreements between Lender, Owners and Sublessor as Lender shall require.

(g) **Management and Consulting Agreements.** If any Borrower has entered into a management or consulting agreement with respect to its Facility, a copy of such management or consulting agreement and a subordination agreement from the manager or consultant in a form satisfactory to Lender.



(h) **Operations Transfer Agreements**. Copies of the Operations Transfer Agreements and such agreements between Lender and Old Operators as Lender shall require.

(i) **Broker**. Evidence satisfactory to Lender that all brokers' commissions or fees due with respect to the Loan or the Facilities have been paid in full in cash.

(j) **Additional Documents**. Such other papers and documents regarding Borrowers, the Projects or the Facilities as Lender may require.

5.2 **Termination of Agreement**. Borrowers agree that all conditions precedent to the Loan Opening will be complied with on or prior to the date of this Agreement. If all of the conditions precedent to the Loan Opening hereunder shall not have been performed on or before the date of this Agreement, Lender, at its option at any time thereafter and prior to the Loan Opening, may terminate this Agreement and all of its obligations hereunder by giving a written notice of termination to Borrowers. In the event of such termination, Borrowers shall pay all Loan Expenses which have accrued or been charged as of the date of such termination.

5.3 **Additional Conditions to Loan Opening and Subsequent Disbursements**. The following are additional conditions precedent to the Loan Opening and to each subsequent disbursement of Loan Proceeds:

(a) **Borrowing Procedures**. Each disbursement of Loan Proceeds may be made available to Borrowers upon any written, electronic or telecopy loan request which Lender in good faith believes to emanate from a properly authorized representative of Borrowers, whether or not that is in fact the case. Each such request shall be effective upon receipt by Lender, shall be irrevocable, and shall specify the date and amount of the borrowing. A request for a disbursement must be received by Lender no later than 11:00 a.m. Chicago, Illinois time, on the day it is to be funded. The proceeds of each disbursement shall be made available at the office of Lender by credit to the account of Borrowers or by other means requested by Borrowers and acceptable to Lender. Borrowers do hereby irrevocably confirm, ratify and approve all such advances by Lender and does hereby indemnify Lender against losses and expenses (including court costs, and reasonable fees of attorneys and paralegals) and shall hold Lender harmless with respect thereto.

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(b) **Representations and Warranties**. All representations and warranties of Borrowers contained in this Agreement, the other Loan Documents and other documents delivered to Lender shall be true and correct in all material respects.

(c) **Financial Condition**. There shall be no material adverse change in the financial condition of any Borrower or Guarantor.

(d) **Accounts Set Up with Lender**. Without limitation on the generality of paragraph (f) below, Borrowers shall have set up all of their respective operating and other accounts with Lender as required by Section 7.8 of this Agreement.

(e) **Interest Rate Protection**. If required by Lender, Borrowers shall have purchased from a qualified counterparty one or more contracts for interest rate protection for such portion or all of the Loan as Lender may require, which contracts shall be in effect for the full term of the Loan and for a rate and otherwise in form and substance satisfactory to Lender in all respects. Lender agrees that interest rate protection is not required for the Loan.

(f) **Field Audit**. In the case of the Loan Opening, Lender shall have completed a field audit as described in Section 7.17 of this Agreement and the results of such field audit shall be acceptable to Lender.

(g) **No Default or Event of Default.** No Default or Event of Default under this Agreement, any other Loan Document or any Lease shall have occurred and be continuing.

## **ARTICLE 6**

### **PAYMENT OF LOAN EXPENSES**

6.1 **Payment of Loan Expenses at Loan Opening.** At the Loan Opening, Lender may pay from Loan Proceeds all Loan Expenses, to the extent the same have not been previously paid.

## **ARTICLE 7**

### **FURTHER AGREEMENTS OF BORROWER**

7.1 **Fixtures and Personal Property; Concerning the Leases and Operations Transfer Agreements.**

(a) Except for a security interest granted to Lender, each Borrower agrees that all of the personal property, fixtures, attachments, furnishings and equipment owned by it will be kept free and clear of all chattel mortgages, vendor' s liens, and all other liens, claims, encumbrances and security interests whatsoever, and that such Borrower will be the absolute owner of said personal property, fixtures, attachments and equipment. Borrowers, on request, shall furnish

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Lender with satisfactory evidence of such ownership, and of the terms of purchase and payment therefor.

(b) Each Borrower shall at all times maintain, preserve and keep its plant, properties and equipment, including its Facility and all Collateral, in good repair, working order and condition, normal wear and tear excepted, and shall from time to time make all needful and proper repairs, renewals, replacements, and additions thereto so that at all times the efficiency thereof shall be fully preserved and maintained. Each Borrower shall permit Lender to examine and inspect such plant, properties and equipment, including its Facility and all Collateral, at all reasonable times and in such manner so as not to cause unreasonable interference with the operations in its Facility.

(c) Each Borrower shall comply with its Lease. Each Borrower shall at all times duly perform and observe all of the terms, provisions, conditions and agreements on its part to be performed and observed under its Lease, and shall not suffer or permit any Default or Event or Default on the part of such Borrower to exist thereunder. Without the prior written consent of Lender, which may be given or withheld in its sole and absolute discretion, each Borrower shall not agree or consent to, or suffer or permit, any modification, amendment or termination of its Lease. Each Borrower shall promptly furnish to Lender copies of all notices of default and other material documents and communications sent or received by such Borrower under or relating to its Lease.

(d) Each Borrower shall comply with its Operations Transfer Agreement. Each Borrower shall at all times duly perform and observe all of the terms, provisions, conditions and agreements on its part to be performed and observed under its Operations Transfer Agreement, and shall not suffer or permit any Default or Event or Default on the part of such Borrower to exist thereunder. Without the prior written consent of Lender, which may be given or withheld in its sole and absolute discretion, each Borrower shall not agree or consent to, or suffer or permit, any modification, amendment or termination of its Operations Transfer Agreement, except that a termination of any Operations Transfer Agreement after the time that neither any Borrower nor any Old Operator has any remaining unperformed obligations thereunder shall not require Lender' s prior written consent. Each Borrower shall promptly furnish to Lender copies of all notices of default and other material documents and communications sent or received by such Borrower under or relating to its Operations Transfer Agreement.

## 7.2 **Insurance Policies.**

(a) Each Borrower shall at all times maintain with insurance companies acceptable to Lender in its reasonable judgment, such insurance coverage as may be required by any law or governmental regulation or court decree or order applicable to it and such other insurance, to such extent and against such hazards and liabilities, including employers' , public and professional liability risks, as is customarily maintained by companies similarly situated, and shall have insured amounts no less than, and deductibles no higher than, are acceptable to Lender in its reasonable judgment. Each Borrower shall furnish to Lender a certificate setting forth in reasonable detail the nature and extent of all insurance maintained by such Borrower, which shall be acceptable in all respects to Lender in its reasonable judgment. Each Borrower shall cause each issuer of an insurance policy to provide Lender with an endorsement (i) showing Lender as

lender' s loss payee with respect to each policy of property or casualty insurance; and (ii) providing that 30 days' notice will be given to Lender prior to any cancellation of, material reduction or change in coverage provided by or other material modification to such policy. Each Borrower shall execute and deliver to Lender a collateral assignment, in form and substance satisfactory to Lender, of each business interruption insurance policy maintained by such Borrower.

(b) In the event any Borrower either fail to provide Lender with evidence of the insurance coverage required by this Section or at any time hereafter shall fail to obtain or maintain any of the policies of insurance required above, or to pay any premium in whole or in part relating thereto, then Lender, without waiving or releasing any obligation or default by Borrowers hereunder, may at any time (but shall be under no obligation to so act), obtain and maintain such policies of insurance and pay such premiums and take any other action with respect thereto, which Lender deems advisable. This insurance coverage (i) may, but need not, protect such Borrower' s interests in such property, including the Collateral, and (ii) may not pay any claim made by, or against, such Borrower in connection with such property, including the Collateral. Such Borrower may later cancel any such insurance purchased by Lender, but only after providing Lender with evidence that such Borrower has obtained the insurance coverage required by this Section. If Lender purchases insurance, Borrowers will be responsible for the costs of that insurance, including interest and any other charges that may be imposed with the placement of the insurance, until the effective date of the cancellation or expiration of the insurance. The costs of the insurance may be added to the principal amount of the Loan owing hereunder. The costs of the insurance may be more than the cost of the insurance Borrowers may be able to obtain on their own.

## 7.3 **Furnishing Information.**

(a) Each Borrower shall promptly supply Lender with such information concerning its assets, liabilities and affairs, and the assets, liabilities and affairs of Guarantor, as Lender may reasonably request from time to time hereafter; which shall include:

(i) Without the necessity of any request by Lender, as soon as available and in no event later than 45 days after the end of each fiscal quarter commencing with the fiscal quarter ending September 30, 2012, consolidated and consolidating financial statements of Borrowers showing the results of operations of the Facilities and consisting of a balance sheet, statement of income and expense and statement of payor mix, prepared in accordance with GAAP, and certified by an officer of Borrowers.

(ii) Without the necessity of any request by Lender, as soon as available and in no event later than 120 days after the end of each fiscal year commencing with the fiscal year ending December 31, 2012, an annual financial statement of each Borrower showing the results of operations of its Facility and consisting of a balance sheet, statement of income and expense, statement of cash flows and statement of payor mix, prepared in accordance with GAAP, certified by an officer of such Borrower.

(iii) Without the necessity of any request by Lender, as soon as available and in no event later than 120 days after the end of each fiscal year commencing with the

fiscal year ending December 31, 2012, an annual consolidated financial statement of Borrowers showing the results of operations of the Facilities and consisting of a balance sheet, statement of income and expense, statement of cash flows and statement of payor mix, prepared in accordance with GAAP, certified by an officer of Borrowers.

(iv) Without the necessity of any request by Lender, as soon as available and in no event later than 120 days after the end of each fiscal year commencing with the fiscal year ending December 31, 2012, annual consolidated financial statements of AdCare, consisting of a balance sheet, statement of income and expense and a statement of cash flows, prepared in accordance with GAAP, and certified by an officer of AdCare, and accompanied by an audit report of a firm of independent certified public accountants.

(v) Without the necessity of any request by Lender, with the annual consolidated financial statements of AdCare required to be furnished hereunder, copies of the schedules and other financial information for Borrowers which were used in the preparation of such financial statements of AdCare, and a letter from the firm of independent certified public accountants which audited such consolidated financial statements of AdCare stating that such schedules and other financial information for Borrowers were used in the preparation of such consolidated financial statements of AdCare.

(vi) Without the necessity of any request by Lender, with each quarterly financial statement of Borrowers required to be furnished hereunder, a duly completed compliance certificate, dated the date of such financial statements and certified as true and correct by appropriate officers of Borrowers and AdCare, containing a computation of each of the financial covenants set forth in Sections 7.12, 7.13, 7.14 and 7.15 hereof, and stating that Borrowers have not become aware of any Default or Event of Default under this Agreement or any of the other Loan Documents that has occurred and is continuing or, if there is any such Default or Event of Default describing it and the steps, if any, being taken to cure it.

(vi) Without the necessity of any request by Lender, within 30 days after the end of each month commencing with the month of September, 2012, a Borrowing Base Certificate dated as of the last business day of such month, certified as true and correct by an authorized representative of Borrowers and in a form acceptable to Lender in its sole and absolute discretion, provided, however, that at any time an Event of Default exists under this Agreement, Lender may require Borrowers to deliver Borrowing Base Certificates more frequently.

(vii) Within 30 days after the end of each month, an aged schedule of the Accounts of each Borrower, listing the name and amount due from each Account Debtor and showing the aggregate amounts due each Borrower from (A) 0-30 days, (B) 31-60 days, (C) 61-90 days, (D) 91-120 days, and (E) more than 120 days, and certified as accurate by each Borrower's treasurer or chief financial officer.

(b) Borrowers shall promptly notify Lender of any condition or event which constitutes a Default or Event of Default under this Agreement or any of the other Loan

(c) It is a condition of this Agreement and the Loan that each Borrower shall each maintain a standard and modern system of accounting in accordance with GAAP consistently applied.

(d) It is a condition of this Agreement and the Loan that Borrowers shall each permit Lender or any of its agents or representatives to have access to and to examine all books and records regarding the Facilities at any time or times hereafter during business hours.

(e) It is a condition of this Agreement and the Loan that Borrowers shall each permit Lender to copy and make abstracts from any and all of said books and records.

7.4 **Excess Indebtedness.** Reference is made to Section 3.4(b) of this Agreement for provisions relating to payment and cash collateralization of amounts of the principal balance of the Loan and the face amount of the outstanding Letter of Credit which at any time exceed the Availability.

7.5 **Compliance with Laws; Environmental Matters.** Each of the following is a condition of this Agreement and the Loan:

(a) Borrowers and Owners shall comply, in all respects, including the conduct of their business and operations and the use of their properties and assets, with all applicable laws, rules, regulations, decrees, orders, judgments, licenses and permits, including without limitation, Environmental Laws, Titles XVIII and XIX of the Social Security Act, Medicare Regulations, Medicaid Regulations, and all laws, rules and regulations of any governmental authorities pertaining to the licensing of professional and other health care providers.

(b) With the exception of Permitted Substances, the Facilities will not be used, for any activities which, directly or indirectly, involve the use, generation, treatment, storage, transportation or disposal of any Hazardous Substances, and no Hazardous Substances will exist on the Facilities or under the Facilities or in any surface waters or groundwaters on or under the Facilities. The Facilities and their existing and future uses will comply with all Environmental Laws, and Borrowers and Owners will not violate any Environmental Laws.

7.6 **ERISA Liabilities; Employee Plans.** It is a condition of this Agreement and the Loan that Borrowers shall (i) keep in full force and effect any and all Employee Plans which are presently in existence or may, from time to time, come into existence under ERISA, and not withdraw from any such Employee Plans, unless such withdrawal can be effected or such Employee Plans can be terminated without liability to any Borrower; (ii) make contributions to all of such Employee Plans in a timely manner and in a sufficient amount to comply with the standards of ERISA, including the minimum funding standards of ERISA; (iii) comply with all material requirements of ERISA which relate to such Employee Plans; (iv) notify Lender immediately upon receipt by any Borrower of any notice concerning the imposition of any withdrawal liability or of the institution of any proceeding or other action which may result in the

termination of any such Employee Plans or the appointment of a trustee to administer such Employee Plans; (v) promptly advise Lender of the occurrence of any "Reportable Event" or "Prohibited Transaction" (as such terms are defined in ERISA), with respect to any such Employee Plans; and (vi) amend any Employee Plan that is intended to be qualified within the meaning of Section 401 of the Internal Revenue Code of 1986 to the extent necessary to keep the Employee Plan qualified, and to cause the Employee Plan to be administered and operated in a manner that does not cause the Employee Plan to lose its qualified status.

7.7 **Licensure; Notices of Agency Actions.** The following are conditions of this Agreement and the Loan:

(a) Subject to the provisions of paragraph (b) of this Section, each Borrower shall be fully qualified by all necessary permits, licenses, certifications, accreditations and qualifications and shall be in compliance with all annual filing requirements of all regulatory authorities.

(b) No Borrower except Borrower 23 and Borrower 24 shall at any time be operating its Facility under any Operations Transfer Agreement. It is a condition of this Agreement and the Loan that within a period of 180 days after a Borrower becomes a borrower under this Agreement, such Borrower shall have obtained all licenses and billing numbers for its Facility in its own name and shall no longer be operating under any Operations Transfer Agreement. During the time that any Borrower is permitted under the terms of this Agreement to be operating its Facility under an Operations Transfer Agreement, it shall be permissible for such Borrower to be operating under the license or billing numbers, or both, of an Old Operator in accordance with the terms and conditions of such Operations Transfer Agreement.

(c) Borrowers shall within five days after receipt, furnish to Lender copies of all adverse notices from any licensing, certifying, regulatory, reimbursing or other agency which has jurisdiction over any Facility or any Project or over any license, permit or approval under which any Facility or any Project operates, and if any Borrower becomes aware that any such notice is to be forthcoming before receipt thereof, it shall promptly inform Lender thereof.

#### 7.8 **Facility Accounts and Revenues.**

(a) It is a condition of this Agreement and the Loan that Borrowers shall set up and maintain all of their respective operating accounts and other accounts related to the Facilities with Lender, shall deposit all of their respective income and receipts promptly upon receipt in such accounts, and shall maintain all of their respective cash and investments on deposit in deposit accounts with Lender.

(b) Borrowers shall deposit all Gross Revenues promptly upon receipt thereof, into a bank account or accounts maintained by Borrowers with Lender. As additional security for the payment and performance of all of the obligations of Borrowers under this Agreement and the other Loan Documents, Borrowers hereby pledge and assign to Lender, and grant to Lender a

first lien on and a first priority security interest in, the Gross Revenues, all of Borrowers' present and future Accounts (as defined in the Code), and the proceeds of all of the foregoing.

#### 7.9 **Single-Asset Entity; Indebtedness; Distributions.**

(a) Each Borrower shall not at any time own any asset or property other than its interest under its Lease, property located in and used in the operation of its Facility and property related thereto, and shall not at any time engage in any business other than the operation of its Facility. The articles of organization and operating agreement of each Borrower shall not be modified or amended, nor shall any member of any Borrower be released or discharged from its his or her obligations under the operating agreement of such Borrower.

(b) Each Borrower shall not at any time have outstanding any indebtedness or obligations, secured or unsecured, direct or indirect, absolute or contingent, including any guaranty, other than the following: (i) obligations to Lender; (ii) obligations under interest rate protection agreements to which Lender is a party; (iii) obligations, other than borrowings, incurred in the ordinary course of the ownership and operation of its Facility; (iv) obligations under its Lease; (v) in the case of Borrowers 9, 10 and 25 and Borrowers 11, 13, 17 and 19, obligations as guarantor, borrower or co-borrower under mortgage financing for the Project in which its Facility is located, provided that such financing is not secured by any assets of which are a part of the Collateral for the Loan, other than property which under applicable law is or may become a fixture and furniture, fixtures, equipment and inventory and proceeds thereof, and provided

that such financing does not contain restrictions which would be violated by such Borrower undertaking its obligations and granting security interests under this Agreement and the other Loan Documents; and (vi) obligations under any Operations Transfer Agreement under which such Borrower is permitted by the terms of this Agreement to be operating its Facility.

(c) If any Default or Event of Default shall occur and be continuing under this Agreement or any of the other Loan Documents, each Borrower shall not, directly or indirectly, make any Distribution. In addition, each Borrower shall not, directly or indirectly, at any time make any Distribution that would cause such Borrower's cash and cash equivalents remaining after such Distribution to be less than an amount equal to a reasonable working capital reserve.

#### 7.10 **Restrictions on Transfer.**

(a) Each Borrower shall not effect, suffer or permit any Prohibited Transfer. Any conveyance, sale, assignment, transfer, lien, pledge, mortgage, security interest or other encumbrance or alienation (or any agreement to do any of the foregoing) of any of the following properties or interests shall constitute a "**Prohibited Transfer**":

(i) Tangible assets, excepting only sales or other dispositions of property no longer useful in connection with the operation of a Facility, provided that prior to the sale or other disposition thereof, such property has been replaced by property of at least equal value and utility;

(ii) Any shares of capital stock of a corporate Borrower, or a corporation which is a direct or indirect owner of an ownership interest in any Borrower (other than the shares of capital stock of a corporate trustee or a corporation whose stock is publicly

traded on a national securities exchange or on the National Association of Securities Dealers' Automated Quotation System);

(iii) All or any part of the membership interests in a limited liability company Borrower, or a limited liability company which is a direct or indirect owner of an ownership interest in any Borrower;

(iv) All or any part of the general partner or the limited partner interest, as the case may be, of a partnership or limited partnership Borrower, or a partnership or limited partnership which is a direct or indirect owner of an ownership interest in any Borrower;

(v) If there shall be any change in Control (by way of transfers of stock, partnership or member interests or otherwise) in any partner, member, manager or shareholder, as applicable, which directly or indirectly Controls the day to day operations and management of any Borrower or Guarantor that is not a natural person and/or owns a Controlling interest in any Borrower or any such Guarantor; provided, however, that this subparagraph shall not apply to AdCare; or

(vi) If any Guarantor who is a natural person shall die or be declared a legal incompetent;

in each case whether any such conveyance, sale, assignment, transfer, lien, pledge, mortgage, security interest, encumbrance or alienation is effected directly, indirectly (including the nominee agreement), voluntarily or involuntarily, by operation of law or otherwise; provided, however, that the foregoing provisions of this Section shall not apply to (i) liens securing obligations to Lender, or (ii) any transfers of any shares of stock or partnership or limited liability company interests, as the case may be, by or on behalf of an owner thereof who is deceased or declared judicially incompetent, to such owner's heirs, legatees, devisees, executors, administrators, estate or personal representatives.

(b) In determining whether or not to make the Loan, Lender evaluated the background and experience of each Borrower and its members in operating property such as the Facilities, found it acceptable and relied and continues to rely upon same as the means of maintaining the value of the Facilities. Each Borrower and its members are well experienced in borrowing money and owning and operating property such as the Facilities, were ably represented by a licensed attorney at law in the negotiation and documentation of the Loan and bargained at arm's length and without duress of any kind for all of the terms and conditions of the Loan, including this provision. Each Borrower recognizes that Lender is entitled to keep its loan portfolio at current interest rates by either making new loans at such rates or collecting assumption fees and/or increasing the interest rate on a loan, the security for which is purchased by a party other than the original Borrowers. In accordance with the foregoing, each Borrower agrees that if this Section is deemed a restraint on alienation, that it is a reasonable one.

7.11 **Leasing, Operation and Management of Projects.**

(a) Each Project shall at all times be owned and leased or subleased to the applicable Borrower under the applicable Lease as described in the definition of the term Lease in Section 1.1 of this Agreement, with the result that no Borrower except Borrower 9, Borrower 10 and

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Borrower 25 shall own a Project. Each Borrower shall not agree or consent to or suffer or permit any modification, amendment or termination of its Lease, and shall not suffer or permit any Event of Default on the part of such Borrower to exist at any time under such Lease.

(b) Each Facility shall at all times be operated as a skilled nursing facility under the management of the applicable Borrower.

7.12 **Minimum Coverage of Rent and Debt Service.** It is a condition of this Agreement and the Loan that for each fiscal quarter commencing with the fiscal quarter ending December 31, 2012, the ratio of –

- (i) the amount of the combined EBITDAR for Borrowers for such quarter, to
- (ii) the sum of the combined amounts of the following for Borrowers for such quarter: (A) Rental Expense, plus (B) Debt Service,

shall be not less than 1.25 to 1.00. Notwithstanding the definition of the term Net Income in Section 1.1 of this Agreement, the Net Income for each Borrower used in calculating EBITDAR of such Borrower for the purpose of this Section for any period, shall be computed by taking into account (i) management fees equal to the greater of such Borrower's actual management fees for such period or imputed management fees equal to 5% of such Borrower's gross income for such period as determined in accordance with GAAP, and (ii) an imputed capital expenditures reserve allowance at the annual rate of \$350 per licensed bed in such Borrower's Facility.

7.13 **Minimum Fixed Charge Coverage Ratio of Borrowers.** It is a condition of this Agreement and the Loan that as of the end of each fiscal quarter commencing with the fiscal quarter ending December 31, 2012, that the ratio of –

- (i) the amount of the combined EBITDAR for Borrowers for the 12-month period ending on the last day of such quarter, to
- (ii) the sum of the combined amounts of the following for Borrowers for the 12-month period ending on the last day of such quarter: (A) Rental Expense, plus (B) Interest Charges, plus (C) Distributions, other than any amounts which were treated as an expense for accounting purposes,



shall be not less than 1.05 to 1.00. Notwithstanding the definition of the term Net Income in Section 1.1 of this Agreement, the Net Income for each Borrower used in calculating EBITDAR of such Borrower for the purpose of this Section for any period, shall be computed by taking into account an imputed capital expenditures reserve allowance at the annual rate of \$350 per licensed bed in such Borrower's Facility. For the avoidance of doubt, (i) unlike Section 7.12 hereof, the Net Income for Borrowers used in calculating EBITDAR of Borrowers for the purpose of this Section for any period shall be computed by taking into account each Borrower's actual management fees for such period only and not taking into account any imputed management fees. Notwithstanding the foregoing provisions of this Section, in the case of the fiscal quarters ending December 31, 2012, March 31, 2013, and June 30, 2013, the calculation of such ratio shall be made for the period commencing on October 1, 2012, and ending on the last

day of such quarter, instead of for the full 12-month period ending on the last day of such quarter.

7.14 **AdCare Leverage Ratio.** It is a condition of this Agreement and the Loan that for each fiscal year commencing with the fiscal year ending December 31, 2012, the ratio of –

- (i) the total amount of long term senior secured indebtedness of AdCare, including the current portion thereof, each as determined in accordance with GAAP, outstanding on the last day of such year, to
- (ii) the amount of EBITDA for AdCare for such year,

shall be not more than 11.00 to 1.00.

7.15 **AdCare Debt Service Coverage Ratio.** It is a condition of this Agreement and the Loan that for each fiscal year commencing with the fiscal year ending December 31, 2012, the ratio of –

- (i) the amount of EBITDAR for AdCare for such year, to
- (ii) the total amount Debt Service required to be paid by AdCare for such year,

shall be not less than 1.00 to 1.00. Notwithstanding the foregoing provisions of this Section, if such ratio for any fiscal year is less than 1.00 to 1.00, the condition provided for in this Section shall nevertheless be deemed to be satisfied if the amount of unencumbered, unrestricted cash shown as an asset in AdCare's audited financial statements as at the end of such fiscal year is not less than an amount equal to the sum of (i) \$2,000,000, plus (ii) the total additional amount of EBITDAR for AdCare that would have been necessary in order for such ratio to have been not less than 1.00 to 1.00 for such fiscal year and for all prior fiscal years ending after on and after December 31, 2012 (the "**Cumulative Shortfall**"); provided, however, that the foregoing provisions of this sentence shall not apply if the Cumulative Shortfall is more than \$3,000,000.

7.16 **Security Interest Matters.** This Agreement is intended to be a security agreement under the Code for the purpose of creating the security interests provided for herein. Borrowers shall execute and deliver such additional security agreements and other documents as Lender shall from time to time request in order to create and perfect such security interests. Borrowers shall keep all of the Collateral free and clear of all other liens, security interests and encumbrances.

7.17 **Field Audits.** Each Borrower shall permit Lender to inspect the Inventory, other tangible assets and/or other business operations of such Borrower, to perform appraisals of the Equipment of such Borrower, and to inspect, audit, check and make copies of, and extracts from, the books, records, computer data, computer programs, journals, orders, receipts, correspondence and other data

relating to Inventory, Accounts and any other Collateral, the results of which must be satisfactory to Lender in Lender' s sole and absolute discretion. All such inspections or audits by Lender shall be conducted at such Borrower' s sole expense.

7.18 **Collateral Records**. Each Borrower shall keep full and accurate books and records relating to the Collateral and shall mark such books and records to indicate Lender' s security interest in the Collateral, including placing a legend, in form and content acceptable to Lender, on all Chattel Paper created by such Borrower indicating that Lender has a security interest in such Chattel Paper.

7.19 **Further Assurance**. Each Borrower, on request of Lender, from time to time, shall execute and deliver such documents as may be necessary to perfect and maintain perfected as valid liens upon the Collateral the liens granted to Lender pursuant to this Agreement or any of the other Loan Documents, and to fully consummate the transactions contemplated by this Agreement.

## **ARTICLE 8**

### **SECURITY**

8.1 **Security for the Loan**. As security for the payment of all of the principal of and interest on the Loan and the Note and all other amounts coming due under this Agreement or any of the other Loan Documents, and the performance by Borrowers of all obligations under this Agreement and the other Loan Documents, each Borrower does hereby pledge, assign, transfer, deliver and grant to Lender, for its own benefit and as agent for its Affiliates, a continuing and unconditional first priority security interest in and to any and all property of such Borrower, of any kind or description, tangible or intangible, wheresoever located and whether now existing or hereafter arising or acquired, including the following (all of which property, along with the products and proceeds therefrom, are individually and collectively referred to as the "**Collateral**"), except that (i) the real property owned by Borrowers 9, 10 and 25 is excluded, and (ii) in the case of Borrowers 9, 10 and 25 and Borrowers 11, 13, 17 and 19, the security interest in furniture, fixtures, equipment, inventory and proceeds thereof may be a second priority security interest:

(a) All property of, or for the account of, such Borrower now or hereafter coming into the possession, control or custody of, or in transit to, Lender or any agent or bailee for Lender or any parent, Affiliate or subsidiary of Lender or any participant with Lender in the Loan (whether for safekeeping, deposit, collection, custody, pledge, transmission or otherwise), including all earnings, dividends, interest, or other rights in connection therewith and the products and proceeds therefrom, including the proceeds of insurance thereon; and

(b) The additional property of such Borrower, whether now existing or hereafter arising or acquired, and wherever now or hereafter located, together with all additions and accessions thereto, substitutions, betterments and replacements therefor, products and Proceeds therefrom, and all of such Borrower' s books and records and recorded data relating thereto (regardless of the medium of recording or storage), together with all of such Borrower' s right, title and interest in and to all computer software required to utilize, create, maintain and process any such records or data on electronic media, identified and set forth as follows:

(i) All Accounts and all Goods whose sale, lease or other disposition by such Borrower has given rise to Accounts and have been returned to, or repossessed or stopped in transit by, such Borrower, or rejected or refused by an Account Debtor;

- (ii) All Inventory, including raw materials, work-in-process and finished goods;
- (iii) All Goods (other than Inventory), including embedded software, Equipment, vehicles, furniture and Fixtures;
- (iv) All Software and computer programs;
- (v) All Securities, Investment Property, Financial Assets and Deposit Accounts;
- (vi) All Chattel Paper, Electronic Chattel Paper, Instruments, Documents, Letter of Credit Rights, all proceeds of letters of credit, Health-Care-Insurance Receivables, Supporting Obligations, notes secured by real estate, Commercial Tort Claims and General Intangibles, including Payment Intangibles;
- (vii) Without limitation on the generality of the foregoing, any Operations Transfer Agreement to which such Borrower is a party, all rights of such Borrower under such Operations Transfer Agreement, and all amounts from time to time payable to such Borrower under such Operations Transfer Agreement; and
- (viii) All Proceeds (whether Cash Proceeds or Noncash Proceeds) of the foregoing property, including all insurance policies and proceeds of insurance payable by reason of loss or damage to the foregoing property, including unearned premiums, and of eminent domain or condemnation awards.

Reference is made to Section 7.7(b) of this Agreement. Until such time as the billing numbers for any Facility referred to in such Section are issued to the applicable Borrower, Accounts for services rendered by such Borrower may be in the name of the applicable Old Operator, in which case such Old Operator is obligated by the provisions of the Operations Transfer Agreement to pay collections on such Accounts to such Borrower. In order to further secure the Loan, each such Borrower shall cause each such Old Operator to grant a direct security interest to Lender in such Accounts and related collateral pursuant to an agreement in a form acceptable to Lender.

8.2 **Possession and Transfer of Collateral.** Unless an Event of Default exists hereunder, Borrowers shall be entitled to possession or use of the Collateral (other than Instruments or Documents, Tangible Chattel Paper, Investment Property consisting of certificated securities and other Collateral required to be delivered to Lender pursuant to this Article 8). The cancellation or surrender of the Note, upon payment or otherwise, shall not affect the right of Lender to retain the Collateral for any other obligations secured by the Collateral. Borrowers shall not sell, assign (by operation of law or otherwise), license, lease or otherwise

dispose of, or grant any option with respect to any of the Collateral, except that Borrowers may sell Inventory in the ordinary course of business.

8.3 **Preservation of the Collateral.** Lender may, but is not required, to take such actions from time to time as Lender deems appropriate to maintain or protect the Collateral. Lender shall have exercised reasonable care in the custody and preservation of the Collateral if Lender takes such action as Borrowers shall reasonably request in writing which is not inconsistent with Lender's status as a secured party, but the failure of Lender to comply with any such request shall not be deemed a failure to exercise reasonable care; provided, however, Lender's responsibility for the safekeeping of the Collateral shall (i) be deemed reasonable if such Collateral is accorded treatment substantially equal to that which Lender accords its own property, and (ii) not extend to matters beyond the control of Lender, including acts of God, war, insurrection, riot or governmental actions. In addition, any failure of Lender to preserve or protect any rights with respect to the Collateral against prior or third parties, or to do any act with respect to preservation of the Collateral, not so requested by Borrowers, shall not be deemed a failure to exercise reasonable care in the custody or preservation of the

Collateral. Borrowers shall have the sole responsibility for taking such action as may be necessary, from time to time, to preserve all rights of Borrowers and Lender in the Collateral against prior or third parties. Without limiting the generality of the foregoing, where Collateral consists in whole or in part of securities, each Borrower represents to, and covenants with, Lender that such Borrower has made arrangements for keeping informed of changes or potential changes affecting the securities (including rights to convert or subscribe, payment of dividends, reorganization or other exchanges, tender offers and voting rights), and each Borrower agrees that Lender shall have no responsibility or liability for informing such Borrower of any such or other changes or potential changes or for taking any action or omitting to take any action with respect thereto.

8.4 **Other Actions as to Any and All Collateral.** Each Borrower further agrees to take any other action reasonably requested by Lender to ensure the attachment, perfection and first priority of, and the ability of Lender to enforce, Lender's security interest in any and all of the Collateral, including (i) causing Lender's name to be noted as secured party on any certificate of title for a titled good if such notation is a condition to attachment, perfection or priority of, or ability of Lender to enforce, Lender's security interest in such Collateral, (ii) complying with any provision of any statute, regulation or treaty of the United States as to any Collateral if compliance with such provision is a condition to attachment, perfection or priority of, or ability of Lender to enforce, Lender's security interest in such Collateral, (iii) obtaining governmental and other third party consents and approvals, including any consent of any licensor, lessor or other person obligated on Collateral, (iv) obtaining waivers from mortgagees and landlords in form and substance satisfactory to Lender, and (v) taking all actions required by the Code in effect from time to time or by other law, as applicable in any relevant Code jurisdiction, or by other law as applicable in any foreign jurisdiction. Each Borrower further agrees to indemnify and hold Lender harmless against claims of any persons not a party to this Agreement concerning disputes arising over the Collateral.

8.5 **Collateral in the Possession of a Warehouseman or Bailee.** If any of the Collateral at any time is in the possession of a warehouseman or bailee, Borrowers shall promptly notify Lender thereof, and shall promptly obtain an agreement acceptable to Lender

under which such person acknowledges the security interest of Lender and waives any liens held by such person on such property.

8.6 **Letter-of-Credit Rights.** If any Borrower, on its own behalf and not as agent for a client of such Borrower, at any time is a beneficiary under a letter of credit now or hereafter issued in favor of such Borrower, such Borrower shall promptly notify Lender thereof and, at the request and option of Lender, such Borrower shall, pursuant to an agreement in form and substance satisfactory to Lender, either (i) arrange for the issuer and any confirmer of such letter of credit to consent to an assignment to Lender of the proceeds of any drawing under the letter of credit, or (ii) arrange for Lender to become the transferee beneficiary of the letter of credit, with Lender agreeing, in each case, that the proceeds of any drawing under the letter to credit are to be applied as provided in this Agreement.

8.7 **Commercial Tort Claims.** If any Borrower shall at any time hold or acquire a Commercial Tort Claim, such Borrower shall immediately notify Lender in writing signed by such Borrower of the details thereof and grant to Lender in such writing a security interest therein and in the proceeds thereof, all upon the terms of this Agreement, in each case in form and substance satisfactory to Lender, and shall execute any amendments hereto deemed reasonably necessary by Lender to perfect its security interest in such Commercial Tort Claim.

8.8 **Electronic Chattel Paper and Transferable Records.** If any Borrower at any time holds or acquires an interest in any electronic chattel paper or any "transferable record", as that term is defined in Section 201 of the federal Electronic Signatures in Global and National Commerce Act, or in Section 16 of the Uniform Electronic Transactions Act as in effect in any relevant jurisdiction, such Borrower shall promptly notify Lender thereof and, at the request of Lender, shall take such action as Lender may reasonably request to vest in Lender control under Section 9-105 of the Code of such electronic chattel paper or control under Section 201 of the federal Electronic Signatures in Global and National Commerce Act or, as the case may be, Section 16 of the Uniform

Electronic Transactions Act, as so in effect in such jurisdiction, of such transferable record. Lender agrees with Borrowers that Lender will arrange, pursuant to procedures satisfactory to Lender and so long as such procedures will not result in Lender's loss of control, for Borrowers to make alterations to the electronic chattel paper or transferable record permitted under Section 9-105 of the Code or, as the case may be, Section 201 of the federal Electronic Signatures in Global and National Commerce Act or Section 16 of the Uniform Electronic Transactions Act for a party in control to make without loss of control.

8.9 **Directions for Payment of Accounts to Account at Lender; Court Order for Payment of Accounts to Lender.**

(a) Subject to the provisions of Section 7.7(b) of this Agreement, in the case of all Account Debtors which are State or federal government or private healthcare payment programs, including, without limitation, Medicare, Medicaid and private insurance companies, each Borrower shall at all times cause such Account Debtors to be directed to pay, and to pay, all Accounts, including, without limitation, all Health-Care-Insurance Receivables, to a deposit account in the name of such Borrower at Lender. The failure of any Borrower to give any such direction, or the withdrawal by any Borrower of any such direction, shall constitute an immediate Event of Default.

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(b) In addition to all other remedies under the this Agreement and under applicable law, upon the occurrence of any Event of Default, Lender shall be entitled to an immediate order of court for the payment of all Accounts, including, without limitation, all Health-Care-Insurance Receivables, directly to Lender by all Account Debtors.

**ARTICLE 9**

**ASSIGNMENTS, SALE AND ENCUMBRANCES**

9.1 **Lender's Right to Assign.** Lender may assign, negotiate, pledge or otherwise hypothecate this Agreement or any of its rights and security hereunder, including the Note and the other Loan Documents, to any bank, participant, financial institution, or any other person or entity, and in case of such assignment, negotiation, pledge or other hypothecation, Borrowers shall accord full recognition thereto and agrees that all rights and remedies of Lender in connection with the interest so assigned, negotiated, pledged or otherwise hypothecated shall be enforceable against Borrowers by such bank, financial institution or other person or entity, with the same force and effect and to the same extent as the same would have been enforceable by Lender but for such assignment, negotiation, pledge or other hypothecation.

9.2 **Prohibition of Assignments and Encumbrances by Borrowers.** Except as expressly permitted by this Agreement, Borrowers shall not create, effect, consent to, attempt, contract for, agree to make, suffer or permit any Prohibited Transfer.

**ARTICLE 10**

**EVENTS OF DEFAULT BY BORROWER**

10.1 **Event of Default Defined.** The occurrence of any one or more of the following shall constitute an Event of Default under this Agreement, and any Event of Default which may occur hereunder shall constitute an Event of Default under each of the other Loan Documents:

(a) Borrowers fail to (i) pay any installment of principal or interest payable pursuant to the Note on the date when due, (ii) reimburse to Lender any amount drawn on the Letter of Credit when required by the Letter of Credit Documents, or (iii) pay any other amount payable to Lender under the Note, the Letter of Credit Documents, this Agreement or any of the other Loan Documents when any such payment is due in accordance with the terms hereof or thereof;

(b) If there is any failure to perform, observe or satisfy any obligation, covenant, agreement, term, condition or provision contained in any of the following provisions of this Agreement: Section 7.7(a), 7.7(b), 7.8, 7.9, 7.10, 7.11, 7.12, 7.13, 7.14, 7.15, 7.16 or 8.9;

(c) If there is any failure to perform, observe or satisfy any obligation, covenant, agreement, term, condition or provision contained in this Agreement and not

otherwise described in this Section and such failure is not cured within 30 days after written notice to Borrowers; provided, however, that –

(i) If such failure can be cured solely by the payment of money, such failure shall not constitute an Event of Default unless it shall continue for a period of five days after written notice to Borrowers;

(ii) If such failure cannot be cured solely by the payment of money and does not pose an emergency or dangerous condition or a material threat to the security for the Loan, such failure shall not constitute an Event of Default unless it shall continue for a period of 30 days after written notice to Borrowers; and

(iii) If a failure described in (ii) above is of such a nature that it cannot reasonably be cured within such 30-day period, and if such failure is susceptible of cure, it shall not constitute an Event of Default if corrective action is instituted by Borrowers within such 30-day period and is diligently pursued and such failure is cured within 90 days after the occurrence of such failure;

(d) The existence of any inaccuracy or untruth in any material respect in any representation or warranty contained in this Agreement or any of the other Loan Documents or of any statement or certification as to facts delivered to Lender by Borrowers or Guarantor; provided, however, that –

(i) If such inaccuracy or untruth can be cured solely by the payment of money, such failure shall not constitute an Event of Default unless it shall continue for a period of 10 days after any Borrower becomes aware of inaccuracy or untruth, whether by notice from Lender or otherwise;

(ii) If such inaccuracy or untruth cannot be cured solely by the payment of money and does not pose an emergency or dangerous condition or a material threat to the security for the Loan, such failure shall not constitute an Event of Default unless it shall continue for a period of 30 days after any Borrower becomes aware of inaccuracy or untruth, whether by notice from Lender or otherwise; and

(iii) If a failure described in (ii) above is of such a nature that it cannot reasonably be cured within such 30-day period, and if such failure is susceptible of cure, it shall not constitute an Event of Default if corrective action is instituted by Borrowers within such 30-day period and is diligently pursued and such failure is cured within 120 days after any Borrower becomes aware of such inaccuracy or untruth, whether by notice from Lender or otherwise;

(e) The occurrence of a Prohibited Transfer;

(f) The existence of any collusion, fraud, dishonesty or bad faith by or with the acquiescence of any Borrower or Guarantor which in any way relates to or affects the Loan, any Project or any Facility;

(g) The occurrence of a material adverse change in the financial condition of any Borrower or Guarantor;

(h) Any Borrower or Guarantor (i) files a voluntary petition in bankruptcy or is adjudicated a bankrupt or insolvent or files any petition or answer seeking any reorganization, arrangement, composition, readjustment, liquidation, dissolution or similar relief under the present or any future federal, state, or other statute or law, or (ii) seeks or consents to or acquiesces in the appointment of any trustee, receiver or similar officer of any Borrower or Guarantor or of all or any substantial part of the property of any Borrower or Guarantor or any portion of any Project or any Facility; or all or a substantial part of the assets of any Borrower or Guarantor are attached, seized, subjected to a writ or distress warrant or are levied upon unless the same is released or vacated within 30 days;

(i) The commencement of any involuntary petition in bankruptcy against any Borrower or Guarantor or the institution against any Borrower or Guarantor of any reorganization, arrangement, composition, readjustment, dissolution, liquidation or similar proceedings under any present or future federal, state or other statute or law, or the appointment of a receiver, trustee or similar officer for all or any substantial part of the property of any Borrower or Guarantor, which shall remain undismissed or undischarged for a period of 30 days;

(j) Any of the following: (i) the entry of any judgment, decree, levy, attachment, garnishment or other process, or the filing of any lien or encumbrance, against any of the Collateral, and the same shall not have been, within 30 days from the entry or filing thereof, vacated, satisfied or appealed from and stayed pending appeal; (ii) the loss, theft, destruction, seizure or forfeiture of, or the occurrence of any material deterioration or impairment of, any of the Collateral, (iii) any material decline or depreciation in the value or market price thereof (whether actual or reasonably anticipated), which causes the Collateral, in the sole opinion of Lender acting in good faith, to become unsatisfactory as to value or character, or which causes Lender to reasonably believe that it is insecure and that the likelihood for repayment of the Loan is or will soon be impaired, time being of the essence (it being understood that the cause of such deterioration, impairment, decline or depreciation shall include, but is not limited to, the failure by the Borrowers to do any act deemed necessary by Lender to preserve and maintain the value and collectability of the Collateral);

(k) The entry against any Borrower or Guarantor of any final judgment for the payment of money in an amount in excess of \$100,000 and such judgment shall not have been, within 30 days from the entry thereof, vacated, satisfied or appealed from and stayed pending appeal;

(l) The dissolution, termination or merger of any Borrower or Guarantor which is an entity, or the occurrence of the death or declaration of legal incompetency of any Guarantor who is a natural person;

(m) The validity or enforceability of this Agreement or any of the other Loan Documents shall be contested by any Borrower, Guarantor or any other party thereto (other than Lender), or any Borrower, Guarantor or any other party thereto (other than Lender) shall deny that it has any or further liability or obligation hereunder or thereunder;

(n) The occurrence of any Default or Event of Default on the part of Sublessor under the Master Lease, any Borrower under its Lease, or on the part of any Borrower under any Operations Transfer Agreement, or on the part of any Old Operator under any Operations Transfer Agreement if such Default or Event of Default has a material adverse effect on the security for the Loan, or the termination of any Lease, Master Lease or any Operations Transfer Agreement, other than any

termination of any Operations Transfer Agreement after the time that neither any Borrower nor any Old Operator has any remaining unperformed obligations thereunder;

(o) The occurrence of an Event of Default under the Note or any of the other Loan Documents, including, without limitation, any Bank Product Agreement to which Lender or any of its Affiliates is a party, including, without limitation, any Hedging Agreement to which Lender is a party, or any Event of Default or other similar condition or event (however described) shall occur and be continuing with respect to any Bank Product Obligation, including, without limitation, any Hedging Transaction, to which Lender or any of its Affiliates is a party;

(p) The occurrence of any Event of Default under any document or agreement evidencing or securing any other obligation or indebtedness of any Borrower, Guarantor or any Owner to Lender; or

(q) The occurrence of any Event of Default under any document or agreement evidencing or securing any loan extended by any other lender and under which loan any Borrower is a borrower, co-borrower or guarantor.

## **ARTICLE 11**

### **LENDER' S REMEDIES UPON EVENT OF DEFAULT**

11.1 **Remedies Conferred upon Lender.** During the continuance of any Event of Default under this Agreement, Lender, in addition to all remedies conferred upon Lender by law and by the terms of the Note and the other Loan Documents, may pursue any one or more of the following remedies concurrently or successively, it being the intent hereof that none of such remedies shall be to the exclusion of any others:

(a) Withhold further disbursement of Loan Proceeds and terminate any of its obligations to Borrowers;

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(b) Declare the Note to be due and payable forthwith, without presentment, demand, protest or other notice of any kind, all of which Borrowers hereby expressly waive;

(c) In addition to any rights of setoff that Lender may have under applicable law, without notice of any kind to Borrowers, appropriate and apply to the payment of the Note or of any sums due under this Agreement any and all balances, deposits, credits, accounts, certificates of deposit, instruments or money of any Borrower then or thereafter in the possession of Lender;

(d) Exercise all of the rights of a secured party under the Code;

(e) Exercise collection remedies against Account Debtors directly or through the use of collection agencies and other collection specialists;

(f) Instruct Borrowers, at their own expense, to notify any parties obligated on any of the Collateral, including any Account Debtors, to make payment directly to Lender of any amounts due or to become due thereunder, or Lender may directly notify such obligors of the security interest of Lender, or of the assignment to Lender of the Collateral and direct such obligors to make payment to Lender of any amounts due or to become due with respect thereto, and thereafter, collect any such amounts due on the Collateral directly from such persons obligated thereon;



(g) Enforce collection of any of the Collateral, including any Accounts, by suit or otherwise, or make any compromise or settlement with respect to any of the Collateral, or surrender, release or exchange all or any part thereof, or compromise, extend or renew for any period (whether or not longer than the original period) any indebtedness thereunder; or

(h) Exercise or pursue any other remedy or cause of action permitted at law or in equity or under this Agreement or any other Loan Document, including, but not limited to, enforcement of all Loan Documents.

11.2 **Possession and Assembly of Collateral.** During the continuance of any Event of Default under this Agreement, Lender may, without notice, demand or legal process of any kind, take possession of any or all of the Collateral (in addition to Collateral of which Lender already has possession), wherever it may be found, and for that purpose may pursue the same wherever it may be found, and may at any time enter into any of the premises of any Borrower where any of the Collateral may be or is supposed to be, and search for, take possession of, remove, keep and store any of the Collateral until the same shall be sold or otherwise disposed of and Lender shall have the right to store and conduct a sale of the same in any of any Borrower's premises without cost to Lender. At Lender's request, Borrowers will, at Borrowers' sole expense, assemble the Collateral and make it available to Lender at a place or places to be designated by Lender which is reasonably convenient to Lender and Borrowers.

11.3. **Sale of Collateral.** During the continuance of any Event of Default under this Agreement, Lender may sell any or all of the Collateral at public or private sale, upon such terms and conditions as Lender may deem proper, and Lender may purchase any or all of the Collateral

at any such sale. Borrowers acknowledge that Lender may be unable to effect a public sale of all or any portion of the Collateral because of certain legal and/or practical restrictions and provisions which may be applicable to the Collateral and, therefore, may be compelled to resort to one or more private sales to a restricted group of offerees and purchasers. Borrowers consent to any such private sale so made even though at places and upon terms less favorable than if the Collateral were sold at public sale. Lender shall have no obligation to clean-up or otherwise prepare the Collateral for sale. Lender may apply the net proceeds, after deducting all costs, expenses, and reasonable fees of attorneys and paralegals incurred or paid at any time in the collection, protection and sale of the Collateral and the obligations secured by the Collateral, to the payment of the Note or any of the other obligations secured by the Collateral, returning the excess proceeds, if any, to Borrowers. Borrowers shall remain liable for any amount remaining unpaid after such application, with interest at the Default Rate. Any notification of intended disposition of the Collateral required by law shall be conclusively deemed reasonably and properly given if given by Lender at least 10 calendar days before the date of such disposition. Borrowers hereby confirm, approve and ratify all acts and deeds of Lender relating to the foregoing, and each part thereof, and expressly waives any and all claims of any nature, kind or description which it have or may hereafter have against Lender or its representatives, by reason of taking, selling or collecting any portion of the Collateral. Borrowers consent to releases of the Collateral at any time (including prior to default) and to sales of the Collateral in groups, parcels or portions, or as an entirety, as Lender shall deem appropriate. Borrowers expressly absolve Lender from any loss or decline in market value of any Collateral by reason of delay in the enforcement or assertion or nonenforcement of any rights or remedies under this Agreement.

11.4 **Standards for Exercising Remedies.** To the extent that applicable law imposes duties on Lender to exercise remedies in a commercially reasonable manner, Borrowers acknowledge and agree that it is not commercially unreasonable for Lender (i) to fail to incur expenses reasonably deemed significant by Lender to prepare Collateral for disposition or otherwise to complete raw material or work-in-process into finished goods or other finished products for disposition, (ii) to fail to obtain third party consents for access to Collateral to be disposed of, or to obtain or, if not required by other law, to fail to obtain governmental or third party consents for the collection or disposition of Collateral to be collected or disposed of, (iii) to fail to exercise collection remedies against Account Debtors or other persons obligated on Collateral or to remove liens or encumbrances on or any adverse claims against Collateral, (iv) to exercise collection remedies against Account Debtors and other persons obligated on Collateral directly or through the use of collection agencies and other collection specialists, (v) to advertise dispositions of Collateral through publications or media of general circulation,

whether or not the Collateral is of a specialized nature, (vi) to contact other persons, whether or not in the same business as Borrowers, for expressions of interest in acquiring all or any portion of the Collateral, (vii) to hire one or more professional auctioneers to assist in the disposition of Collateral, whether or not the collateral is of a specialized nature, (viii) to dispose of Collateral by utilizing internet sites that provide for the auction of assets of the types included in the Collateral or that have the reasonable capability of doing so, or that match buyers and sellers of assets, (ix) to dispose of assets in wholesale rather than retail markets, (x) to disclaim disposition warranties, including any warranties of title, (xi) to purchase insurance or credit enhancements to insure Lender against risks of loss, collection or disposition of Collateral or to provide to Lender a guaranteed return from the collection or disposition of Collateral, or (xii) to the extent deemed appropriate by Lender, to obtain the services of other brokers, investment bankers, consultants

and other professionals to assist Lender in the collection or disposition of any of the Collateral. Borrowers acknowledge that the purpose of this Section is to provide non-exhaustive indications of what actions or omissions by Lender would not be commercially unreasonable in Lender's exercise of remedies against the Collateral and that other actions or omissions by Lender shall not be deemed commercially unreasonable solely on account of not being indicated in this Section. Without limitation upon the foregoing, nothing contained in this Section shall be construed to grant any rights to Borrowers or to impose any duties on Lender that would not have been granted or imposed by this Agreement or by applicable law in the absence of this Section.

11.5 **Code and Offset Rights.** Lender may exercise, from time to time, any and all rights and remedies available to it under the Code or under any other applicable law in addition to, and not in lieu of, any rights and remedies expressly granted in this Agreement or in any other Loan Document, and may, without demand or notice of any kind, appropriate and apply toward the payment of such of the obligations under the Loan Documents, whether matured or unmatured, including costs of collection and reasonable fees of attorneys and paralegals, and in such order of application as Lender may, from time to time, elect, any indebtedness of Lender to Borrowers or any other person obligated for any of the obligations under the Loan Documents, however created or arising, including balances, credits, deposits, accounts or moneys of Borrowers or any such other person in the possession, control or custody of, or in transit to Lender. Borrowers, on behalf of themselves and each such other person, hereby waive the benefit of any law that would otherwise restrict or limit Lender in the exercise of its right, which is hereby acknowledged, to appropriate at any time hereafter any such indebtedness owing from Lender to any such other person.

11.6 **Additional Remedies.** Lender shall have the right and power to –

(a) Instruct Borrowers, at their own expense, to notify any parties obligated on any of the Collateral, including any Account Debtors, to make payment directly to Lender of any amounts due or to become due thereunder, or Lender may directly notify such obligors of the security interest of Lender, or of the assignment to Lender of the Collateral, and direct such obligors to make payment to Lender of any amounts due or to become due with respect thereto, and thereafter, collect any such amounts due on the Collateral directly from such persons obligated thereon;

(b) Enforce collection of any of the Collateral, including any Accounts, by suit or otherwise, or make any compromise or settlement with respect to any of the Collateral, or surrender, release or exchange all or any part thereof, or compromise, extend or renew for any period (whether or not longer than the original period) any indebtedness thereunder;

(c) Take possession or control of any proceeds and products of any of the Collateral, including the proceeds of insurance thereon;

(d) Extend, renew or modify for one or more periods (whether or not longer than the original period) the Note, any other obligations under any of the Loan

Documents, or any obligation of any nature of any other obligor with respect to the Note or any of the Obligations;

(e) Grant releases, compromises or indulgences with respect to the Note or any of the other obligations under any of the Loan Documents, or any extension or renewal of any of the Note or such other obligations, or any security therefor, or to any other obligor with respect to the Note or any of such other obligations;

(f) Transfer the whole or any part of securities which may constitute Collateral into the name of Lender or Lender's nominee without disclosing, if Lender so desires, that such securities so transferred are subject to the security interest of Lender, and any corporation, association, or any of the managers or trustees of any trust issuing any of such securities, or any transfer agent, shall not be bound to inquire, in the event that Lender or such nominee makes any further transfer of such securities, or any portion thereof, as to whether Lender or such nominee has the right to make such further transfer, and shall not be liable for transferring the same;

(g) Vote the Collateral;

(h) Make an election with respect to the Collateral under Section 1111 of Bankruptcy Code or take action under Section 364 or any other section of Bankruptcy Code; provided, however, that any such action of Lender as set forth herein shall not, in any manner whatsoever, impair or affect the liability of Borrowers hereunder, nor prejudice, waive, nor be construed to impair, affect, prejudice or waive Lender's rights and remedies at law, in equity or by statute, nor release, discharge, nor be construed to release or discharge, Borrowers, any guarantor or other person liable to Lender for the Loan or any of the other obligations under the Loan Documents; and

(i) At any time, and from time to time, accept additions to, releases, reductions, exchanges or substitution of the Collateral, without in any way altering, impairing, diminishing or affecting the provisions of this Agreement, the Loan Documents, or any of the obligations under the Loan Documents, or Lender's rights hereunder or under the Note.

Borrowers hereby ratify and confirm whatever Lender may do with respect to the Collateral and agrees that Lender shall not be liable for any error of judgment or mistakes of fact or law with respect to actions taken in connection with the Collateral.

11.7 **Right of Lender to Make Advances to Cure Event of Defaults; Obligatory Advances.** If Borrowers shall fail to perform any of their covenants or agreements herein or in any of the other Loan Documents contained, Lender may (but shall not be required to) perform any of such covenants and agreements, and any amounts expended by Lender in so doing, and any amounts expended by Lender pursuant to Sections 11.1 through 11.6 hereof and any amounts advanced by Lender pursuant to this Agreement shall be deemed advanced by Lender under an obligation to do so regardless of the identity of the person or persons to whom said funds are disbursed. Loan Proceeds advanced by Lender to protect its security for the Loan are

obligatory advances hereunder and shall constitute additional indebtedness payable on demand and evidenced and secured by the Loan Documents.

11.8 **Attorney-in-Fact.** Each Borrower hereby irrevocably makes, constitutes and appoints Lender (and any officer of Lender or any person designated by Lender for that purpose) as such Borrower's true and lawful proxy and attorney-in-fact (and agent-in-fact) in such Borrower's name, place and stead, with full power of substitution, to (i) take such actions as are expressly permitted in this Agreement, (ii) execute such financing statements and other documents and to do such other acts as Lender may require to perfect and preserve Lender's security interest in, and during the existence of an Event of Default hereunder, to enforce such interests in the

Collateral, and (iii) during the existence of an Event of Default hereunder, carry out any remedy provided for in this Agreement, including endorsing such Borrower's name to checks, drafts, instruments and other items of payment, and proceeds of the Collateral, executing change of address forms with the postmaster of the United States Post Office serving the address of such Borrower, changing the address of such Borrower to that of Lender, opening all envelopes addressed to such Borrower and applying any payments contained therein to the amounts due to Lender. Each Borrower hereby acknowledges that the constitution and appointment of such proxy and attorney-in-fact are coupled with an interest and are irrevocable. Each Borrower hereby ratifies and confirms all that such attorney-in-fact may do or cause to be done by virtue of any provision of this Agreement.

11.9 **No Marshalling**. Lender shall not be required to marshal any present or future collateral security (including this Agreement and the Collateral) for, or other assurances of payment of, the obligations of Borrowers, or any of them or to resort to such collateral security or other assurances of payment in any particular order. To the extent that it lawfully may, Borrowers hereby agree that they will not invoke any law relating to the marshalling of collateral which might cause delay in or impede the enforcement of Lender's rights under this Agreement or under any other instrument creating or evidencing any of Borrowers' obligations or under which any of such obligations is outstanding or by which any of such obligations is secured or payment thereof is otherwise assured, and, to the extent that it lawfully may, Borrowers hereby irrevocably waive the benefits of all such laws.

11.10 **Application of Proceeds**. Lender will within three business days after receipt of cash or solvent credits from collection of items of payment, proceeds of Collateral or any other source, apply the whole or any part thereof against the obligations secured hereby. Lender shall further have the exclusive right to determine how, when and what application of such payments and such credits shall be made on such obligations, and such determination shall be conclusive upon Borrowers. Any proceeds of any disposition by Lender of all or any part of the Collateral may be first applied by Lender to the payment of expenses incurred by Lender in connection with the Collateral, including attorneys' fees and legal expenses as provided for in Section 11.11 hereof.

11.11 **Attorneys' Fees**. Borrowers shall pay Lender's reasonable attorneys' fees and costs in connection with the negotiation, preparation and administration of this Agreement and shall pay Lender's reasonable attorneys' fees and costs in connection with the administration and enforcement of this Agreement and the other Loan Documents, which shall also include reasonable attorneys' fees and time charges of attorneys who may be employees of Lender or

any affiliate of Lender. Without limiting the generality of the foregoing, if at any time or times hereafter Lender employs counsel for advice or other representation with respect to any matter concerning Borrowers, this Agreement, the Projects, the Facilities or the Loan Documents or if Lender employs one or more counsel to protect, collect, lease, sell, take possession of, or liquidate any portion of any Project or any Facility, or to attempt to enforce or protect any security interest or lien or other right in any portion of any Project or any Facility or under any of the Loan Documents, or to enforce any rights of Lender or obligations of Borrowers or any other person, firm or corporation which may be obligated to Lender by virtue of this Agreement or under any of the Loan Documents or any other agreement, instrument or document, heretofore or hereafter delivered to Lender in furtherance hereof, then in any such event, all of the attorneys' fees arising from such services and actually incurred, and any expenses, costs and charges relating thereto and actually incurred, shall constitute an additional indebtedness owing by Borrowers to Lender payable on demand and evidenced and secured by the Loan Documents.

11.12 **No Waiver**. No failure by Lender to exercise, or delay by Lender in exercising, any right, power or privilege hereunder shall operate as a waiver thereof, nor shall any single or partial exercise of any right, power or privilege hereunder preclude any other or further exercise thereof, or the exercise of any other right, power or privilege. The rights and remedies provided in this Agreement and in the Loan Documents are cumulative and not exclusive of each other or of any right or remedy provided at law or in equity. No notice to or demand on Borrowers in any case, in itself, shall entitle Borrowers to any other or further notice or demand in similar or other circumstances or constitute a waiver of the rights of Lender to any other or further action in any circumstances without notice or demand.

11.13 **Default Rate.** During the continuance of any Event of Default under this Agreement or any of the other Loan Documents, interest on funds outstanding hereunder shall accrue at the Default Rate and be payable on demand. The failure of Lender to charge interest at the Default Rate shall not be evidence of the absence of an Event of Default or waiver of an Event of Default by Lender.

## **ARTICLE 12**

### **MISCELLANEOUS**

12.1 **Time is of the Essence.** Borrowers agree that time is of the essence in all of its covenants under this Agreement.

12.2 **Joint and Several Obligations; Full Collateralization.**

(a) Each Borrower shall be jointly and severally liable for all of the obligations of all Borrowers under this Agreement and the other Loan Documents, regardless of the amount of the Loan Proceeds that is actually disbursed to or for the benefit of each Borrower, or the manner in which Borrowers or Lender account for the Loan in their respective books and records. All of the collateral provided by each Borrower shall secure all of the obligations of all Borrowers under this Agreement and the other Loan Documents, regardless of the amount of the Loan Proceeds that is actually disbursed to or for the benefit of each Borrower.

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(b) Each Borrower acknowledges that Lender has advised Borrowers that Lender is unwilling to provide the Loan to Borrowers unless each Borrower agrees to the joint and several liability and full collateralization described in paragraph (a) above. Each Borrower has determined that it is in its best interest to undertake such joint and several liability and full collateralization, because of, among other things (i) the benefit to each Borrower of being able to obtain the Loan and the desirability of the terms and conditions of the Loan, (ii) the benefit and economies to be realized by Borrowers in obtaining the Loan as a single loan facility as compared to each Borrower's obtaining an individual loan facility for its Facility, and (iii) the fact that each Borrower is an Affiliate of each of the other Borrowers.

(c) The obligations of each of Borrowers under this Agreement and the other Loan Documents, including, without limitation, the joint and several liability and full collateralization as described in paragraph (a) above, shall be continuing and shall be binding upon each of them, and shall remain in full force and effect, and shall not be discharged, impaired or affected by (i) the power or authority of any other Borrower to execute, acknowledge or deliver this Agreement or any of the other Loan Documents; (ii) the existence or continuance of any obligation on the part of any other Borrower under this Agreement or any of the other Loan Documents; (iii) the validity or invalidity of the obligations of any other Borrower under this Agreement or any of the other Loan Documents; (iv) any defense, setoff or counterclaim whatsoever that any other Borrower may or might have to the performance or observance of the obligations under this Agreement or any of the other Loan Documents or to the performance or observance of any of the terms, provisions, covenants and agreements contained in this Agreement or any of the other Loan Documents, including, without limitation, any defense based on any alleged failure of Lender to comply with the implied covenant of good faith and fair dealing, or any limitation or exculpation of liability on the part of any other Borrower; (v) the existence or continuance of any other Borrower as a legal entity; (vi) the transfer by any other Borrower of all or any part of the property encumbered by the Loan Documents; (vii) any sale, pledge, assignment, surrender, indulgence, alteration, substitution, exchange, extension, renewal, release, compromise, change in, modification or other disposition of any of the obligations of any other Borrower or of any of the Loan Documents, all of which Lender is hereby expressly authorized to make from time to time without notice to Borrowers or any of them, or to anyone; (viii) the acceptance by Lender of the primary or secondary obligation of any party with respect to, or any security for, all or any part of the obligations under this Agreement or any of the other Loan Documents; or (ix) any failure, neglect or omission on the part of Lender to realize or protect any of the obligations under this Agreement or any of the other Loan Documents or any collateral or appropriation of any moneys,

credits or property of Borrowers toward the liquidation of the obligations under this Agreement or any of the other Loan Documents or by any application of any moneys received by Lender under the Loan Documents. The obligations of Borrowers and each of them under this Agreement and under the other Loan Documents, including, without limitation, the joint and several liability and full collateralization as described in paragraph (a) above, shall not be affected, discharged, impaired or varied by any act, omission or circumstance whatsoever, whether or not specifically enumerated above, except the due and punctual payment, performance and observance of all of the obligations of Borrowers under this Agreement and the other Loan Documents, and then, in each case, only to the extent thereof.

(d) Lender shall have the right to enforce this Agreement and the other Loan Documents against any Borrower with or without enforcing or attempting to enforce the same

against any other Borrower or any security for the obligation of any of them, and whether or not other proceedings or steps are pending or have been taken or have been concluded to enforce or otherwise realize upon any security for the Loan or any guaranty of the Loan. The payment of any amount or amounts by any Borrower, pursuant to its obligation under this Agreement or any of the other Loan Documents, including, without limitation, pursuant to the joint and several liability provided for herein, shall not in any way entitle such Borrower, either at law, or in equity or otherwise, to any right, title or interest in and to this Agreement, the Note, or any of the other Loan Documents, or any principal or interest payments theretofore, then or thereafter at any time made by anyone on behalf of any of Borrowers, or in and to any security therefor, or to any right of recovery against any Borrower, in each case whether by way of indemnity, reimbursement, contribution, subrogation or otherwise, and Borrowers hereby waive and relinquish any and all such right, title and interest in and to the Note, such other obligations, such principal and interest payments, and such security and any and all such rights of recovery against Borrowers. In addition, each Borrower hereby subordinates all obligations of every sort whatsoever now or hereafter coming due to such Borrower from any other Borrower, to the Loan and the Note and to all other amounts coming due to Lender under the Loan Documents.

### 12.3 **Lender's Determination of Facts; Lender Approvals and Consents.**

(a) Lender at all times shall be free to establish independently to its satisfaction and in its sole and absolute discretion the existence or nonexistence of any fact or facts, the existence or nonexistence of which is a condition of this Agreement.

(b) Wherever in this Agreement or any of the other Loan Documents provision is made for the approval or consent of Lender or counsel to Lender, or that any matter is to be to the satisfaction of or as required by Lender or counsel to Lender, or that any matter is to be as estimated or determined by Lender, or the like, unless specifically stated to the contrary, such approval, consent, satisfaction, requirement, estimate or determination or the like shall be in the sole and absolute discretion of Lender or counsel to Lender, as the case may be.

(c) Notwithstanding any other provision of this Agreement or the other Loan Documents, wherever in this Agreement or any of the other Loan Documents provision is made for the approval or consent of Lender with respect to a matter, if Lender elects to grant such approval or consent, it shall not be unreasonable for Lender to make such approval or consent subject to the condition that such matter must also be approved or consented to in writing by Guarantor, any other guarantors of the Loan, and any parties other than Borrowers that have provided collateral for the Loan.

12.4 **Prior Agreements; No Reliance; Modifications.** This Agreement and the other Loan Documents, and any other documents or instruments executed pursuant thereto or contemplated thereby, shall represent the entire, integrated agreement between the parties hereto with respect to the subject matter of this Agreement, and shall supersede all prior negotiations, representations or agreements pertaining thereto, either oral or written. Borrowers acknowledge that they executing this Agreement without relying on any statements, representations or warranties, either oral or written, that are not expressly set forth herein. This Agreement and any

provision hereof shall not be modified, amended, waived or discharged in any manner other than by a written amendment executed by all parties to this Agreement.

12.5 **Disclaimer by Lender.** Borrowers are not or shall not be an agent of Lender for any purposes, and Lender is not a venture partner with Borrowers in any manner whatsoever. Approvals granted by Lender for any matters covered under this Agreement shall be narrowly construed to cover only the parties and facts identified in any written approval or, if not in writing, such approvals shall be solely for the benefit of Borrowers.

12.6 **Loan Expenses; Indemnification.** Borrowers shall pay all Loan Expenses promptly upon demand therefor by Lender. To the fullest extent permitted by law, Borrowers hereby agree to protect, indemnify, defend and save harmless, Lender and its directors, officers, agents and employees from and against any and all liability, expense or damage of any kind or nature and from any suits, claims or demands, including legal fees and expenses on account of any matter or thing or action or failure to act by Lender, whether or not arising from a claim by a third party, and whether or not in litigation, arising out of this Agreement or in connection herewith, unless such suit, claim or damage is caused solely by any act, omission or willful malfeasance of Lender, its directors, officers, agents and authorized employees. This indemnity is not intended to excuse Lender from performing hereunder. This obligation on the part of Borrowers shall survive the closing of the Loan, the repayment thereof and any cancellation of this Agreement. Borrowers shall pay, and hold Lender harmless from, any and all claims of any brokers, finders or agents claiming a right to any fees in connection with arranging the financing contemplated hereby. Lender hereby represents and warrants that it has not employed a broker or other finder in connection with the Loan. Borrowers hereby represent and warrant that no brokerage commissions or finder's fees are to be paid in connection with the Loan.

12.7 **Captions.** The captions and headings of various Articles and Sections of this Agreement and exhibits pertaining hereto are for convenience only and are not to be considered as defining or limiting in any way the scope or intent of the provisions hereof.

12.8 **Inconsistent Terms and Partial Invalidity.** In the event of any inconsistency among the terms hereof (including incorporated terms), or between such terms and the terms of any other Loan Document, Lender may elect which terms shall govern and prevail. If any provision of this Agreement, or any section, paragraph, sentence, clause, phrase or word, or the application thereof, in any circumstances, is adjudicated by a court of competent jurisdiction to be invalid, the validity of the remainder of this Agreement shall be construed as if such invalid part were never included herein.

12.9 **Gender and Number.** Any word herein which is expressed in the masculine or neuter gender shall be deemed to include the masculine, feminine and neuter genders. Any word herein which is expressed in the singular or plural number shall be deemed, whenever appropriate in the context, to include the singular and the plural.

12.10 **Notices.** All notices and other communications provided for in this Agreement ("**Notices**") shall be in writing. The "**Notice Addresses**" of the parties for purposes of this Agreement are as follows:

Borrowers:	Name of Borrower
	Two Buckhead Plaza
	3050 Peachtree Road NW

Atlanta, Georgia 30305  
Attention: Boyd P. Gentry

With a copy to: Holt Ney Zatzoff & Wasserman, LLP  
100 Galleria Parkway, Suite 1800  
Atlanta, Georgia 30339  
Attention: Gregory P. Youra

Lender: The PrivateBank and Trust Company  
120 South LaSalle Street  
Chicago, Illinois 60603  
Attention: Amy K. Hallberg

With a copy to: Seyfarth Shaw LLP  
131 South Dearborn Street  
Suite 2400  
Chicago, Illinois 60603  
Attention: Alvin L. Kruse

or such other address as a party may designate by notice duly given in accordance with this Section to the other parties. A Notice to a party shall be effective when delivered to such party's Notice Address by any means, including, without limitation, personal delivery by the party giving the Notice, delivery by United States regular, certified or registered mail, or delivery by a commercial courier or delivery service. If the Notice Address of a party includes a facsimile number or electronic mail address, Notice given by facsimile or electronic mail shall be effective when delivered at such facsimile number or email address. If delivery of a Notice is refused, it shall be deemed to have been delivered at the time of such refusal of delivery. The party giving a Notice shall have the burden of establishing the fact and date of delivery or refusal of delivery of a Notice.

12.11 **Effect of Agreement.** The submission of this Agreement and the Loan Documents to Borrowers for examination does not constitute a commitment or an offer by Lender to make a commitment to lend money to Borrowers; this Agreement shall become effective only upon execution and delivery hereof by Lender to Borrowers.

12.12 **Construction.** Each party to this Agreement and legal counsel to each party have participated in the drafting of this Agreement, and accordingly the general rule of construction to the effect that any ambiguities in a contract are to be resolved against the party drafting the contract shall not be employed in the construction and interpretation of this Agreement.

12.13 **Governing Law.** This Agreement has been negotiated, executed and delivered at Chicago, Illinois, and shall be construed and enforced in accordance with the laws of the State of Illinois.

12.14 **Litigation Provisions.**

(a) **EACH BORROWER CONSENTS AND SUBMITS TO THE JURISDICTION OF ANY STATE OR FEDERAL COURT LOCATED IN CHICAGO, ILLINOIS, AND OF ANY STATE OR FEDERAL COURT LOCATED OR HAVING JURISDICTION IN THE COUNTY IN WHICH ITS FACILITY IS LOCATED, IN WHICH ANY LEGAL PROCEEDING MAY BE COMMENCED OR PENDING RELATING IN ANY MANNER TO THIS AGREEMENT, THE LOAN OR ANY OF THE OTHER LOAN DOCUMENTS.**



(b) EACH BORROWER AGREES THAT ANY LEGAL PROCEEDING RELATING TO THIS AGREEMENT, THE LOAN OR ANY OF THE OTHER LOAN DOCUMENTS MAY BE BROUGHT AGAINST SUCH BORROWER IN ANY STATE OR FEDERAL COURT LOCATED IN CHICAGO, ILLINOIS, OR ANY STATE OR FEDERAL COURT LOCATED OR HAVING JURISDICTION IN THE COUNTY IN WHICH ITS FACILITY IS LOCATED. EACH BORROWER WAIVES ANY OBJECTION TO VENUE IN ANY SUCH COURT AND WAIVES ANY RIGHT IT MAY HAVE TO TRANSFER OR CHANGE THE VENUE FROM ANY SUCH COURT.

(c) EACH BORROWER AGREES THAT IT WILL NOT COMMENCE ANY LEGAL PROCEEDING AGAINST LENDER RELATING IN ANY MANNER TO THIS AGREEMENT, THE LOAN OR ANY OF THE OTHER LOAN DOCUMENTS IN ANY COURT OTHER THAN A STATE OR FEDERAL COURT LOCATED IN CHICAGO, ILLINOIS, OR IF A LEGAL PROCEEDING IS COMMENCED BY LENDER AGAINST BORROWER IN A COURT IN ANOTHER LOCATION, BY WAY OF A COUNTERCLAIM IN SUCH LEGAL PROCEEDING.

(d) EACH BORROWER HEREBY WAIVES TRIAL BY JURY IN ANY LEGAL PROCEEDING RELATING TO THIS AGREEMENT, THE LOAN OR ANY OF THE OTHER LOAN DOCUMENTS.

12.15 **Counterparts; Electronic Signatures.** This Agreement may be executed in any number of counterparts and by the different parties hereto on separate counterparts and each such counterpart shall be deemed to be an original, but all such counterparts shall together constitute but one and the same Agreement. Receipt of an executed signature page to this Agreement by facsimile or other electronic transmission shall constitute effective delivery thereof. Electronic records of executed Loan Documents maintained by Lender shall be deemed to be originals thereof.

12.16 **Customer Identification-USA Patriot Act Notice; OFAC and Bank Secrecy Act.** Lender hereby notifies Borrowers that pursuant to the requirements of the USA Patriot Act (Title III of Pub. L. 107-56, signed into law October 26, 2001) (the "**Act**"), and Lender's policies and practices, Lender is required to obtain, verify and record certain information and documentation that identifies Borrowers, which information includes the name and address of Borrowers and such other information that will allow Lender to identify Borrowers in accordance with the Act. In addition, Borrowers shall (i) ensure that no person who owns a controlling interest in or otherwise controls Borrowers or any subsidiary of Borrowers is or shall

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be listed on the Specially Designated Nationals and Blocked Person List or other similar lists maintained by the Office of Foreign Assets Control ("**OFAC**"), the Department of the Treasury, or included in any Executive Orders, (ii) not use or permit the use of Loan Proceeds to violate any of the foreign asset control regulations of OFAC or any enabling statute or Executive Order relating thereto, and (iii) comply, and cause any of its subsidiaries to comply, with all applicable Bank Secrecy Act laws and regulations, as amended.

[SIGNATURE PAGE(S) AND EXHIBIT(S),  
IF ANY, FOLLOW THIS PAGE]

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IN WITNESS WHEREOF, Borrowers and Lender have caused this Agreement to be executed the day and year first above written.

ADK THOMASVILLE OPERATOR, LLC  
ADK LUMBER CITY OPERATOR, LLC

**ADK JEFFERSONVILLE OPERATOR, LLC  
ADK LAGRANGE OPERATOR, LLC  
ADK POWDER SPRINGS OPERATOR, LLC  
ADK OCEANSIDE OPERATOR, LLC  
ADK THUNDERBOLT OPERATOR, LLC  
ADK SAVANNAH BEACH OPERATOR, LLC  
ATTALLA NURSING ADK, LLC  
MOUNTAIN TRACE NURSING ADK, LLC  
MT. KENN NURSING, LLC  
ERIN NURSING, LLC  
CP NURSING, LLC  
BENTON NURSING, LLC  
VALLEY RIVER NURSING, LLC  
PARK HERITAGE NURSING, LLC  
HOMESTEAD NURSING, LLC  
WOODLAND MANOR NURSING, LLC  
MOUNTAIN VIEW NURSING, LLC  
NORTHRIDGE HC&R NURSING, LLC  
LITTLE ROCK HC&R NURSING, LLC  
WOODLAND HILLS HC NURSING, LLC  
APH&R NURSING, LLC  
GLENVUE H&R NURSING, LLC  
COOSA NURSING ADK, LLC**

By /s/ Christopher F. Brogdon  
Christopher F. Brogdon, Manager of Each Borrower

**THE PRIVATEBANK AND TRUST COMPANY**

By /s/ Amy K. Hallberg  
Amy K. Hallberg, Managing Director

- AdCare Portfolio Operator Loan Agreement -  
- Signature Page -

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14930096

10-25-12

### MODIFICATION AGREEMENT

THIS MODIFICATION AGREEMENT dated as of October 26, 2012 (this "**Agreement**"), is entered into by and among ADK THOMASVILLE OPERATOR, LLC ("**Borrower 1**"), ADK LUMBER CITY OPERATOR, LLC ("**Borrower 2**"), ADK JEFFERSONVILLE OPERATOR, LLC ("**Borrower 3**"), ADK LAGRANGE OPERATOR, LLC ("**Borrower 4**"), ADK POWDER SPRINGS OPERATOR, LLC ("**Borrower 5**"), ADK OCEANSIDE OPERATOR, LLC ("**Borrower 6**"), ADK THUNDERBOLT OPERATOR, LLC ("**Borrower 7**"), ADK SAVANNAH BEACH OPERATOR, LLC ("**Borrower 8**"), ATTALLA NURSING ADK, LLC ("**Borrower 9**"), MOUNTAIN TRACE NURSING ADK, LLC, an Ohio limited liability company ("**Borrower 10**"), MT. KENN NURSING, LLC ("**Borrower 11**"), ERIN NURSING, LLC ("**Borrower 12**"), CP NURSING, LLC ("**Borrower 13**"), BENTON NURSING, LLC ("**Borrower 14**"), VALLEY RIVER NURSING, LLC ("**Borrower 15**"), PARK HERITAGE NURSING, LLC ("**Borrower 16**"), HOMESTEAD NURSING, LLC ("**Borrower 17**"), WOODLAND MANOR NURSING, LLC ("**Borrower 18**"), MOUNTAIN VIEW NURSING, LLC ("**Borrower 19**"), NORTHRIDGE HC&R NURSING, LLC ("**Borrower 20**"), LITTLE ROCK HC&R NURSING, LLC ("**Borrower 21**"), WOODLAND HILLS HC NURSING, LLC ("**Borrower 22**"), APH&R NURSING, LLC ("**Borrower 23**"), GLENVUE H&R NURSING, LLC ("**Borrower 24**"), and COOSA NURSING ADK, LLC ("**Borrower 25**"), each a Georgia limited liability company except as hereinabove set forth (collectively, "**Borrowers**"), ADCARE HEALTH SYSTEMS, INC., an Ohio corporation (the "**Guarantor**") (the Borrowers and the Guarantor being sometimes referred to herein collectively as the "**Borrower/Guarantor Parties**"), and THE PRIVATEBANK AND TRUST COMPANY, an Illinois banking corporation ("**Lender**").

### RECITALS

A. The Borrower/Guarantor Parties and the Lender heretofore entered into the following documents (collectively, the "**Documents**"):

- (i) Loan and Security Agreement dated as of September 20, 2012 (the "**Loan Agreement**"), by and between the Borrowers and the Lender.
- (ii) Promissory Note dated September 20, 2012 (the "**Note**"), from the Borrowers to the Lender in the principal amount of \$10,600,000.
- (iii) Guaranty of Payment and Performance dated as of September 20, 2012, by the Guarantor to and for the benefit of the Lender.

B. The parties desire to make certain modifications and amendments to the Documents, as more fully provided for herein, all as modifications, amendments and continuations of, but not as novations of, the Documents.

### AGREEMENTS

In consideration of the premises and the mutual covenants and agreements contained herein, and other good and valuable consideration, the receipt and sufficiency of which are hereby acknowledged, the parties hereby agree as follows:

**Section 1. Recitals Part of Agreement; Defined Terms.**

(a) The foregoing Recitals are hereby incorporated into and made a part of this Agreement.

(b) All capitalized terms used and not otherwise defined in this Agreement shall have the meanings set forth in the Loan Agreement.

**Section 2. Change in Definition of Application.** The defined term “Application” in Section 1.1 of the Loan Agreement is hereby modified and amended in its entirety to read as follows effective as of the date of this Agreement, with the existing defined term to continue to be effective for periods prior to the date of this Agreement:

**Application:** One or more Applications for Irrevocable Standby Letters of Credit which either originally or after the joinder contained in Section 3.2(b) of this Agreement, are from Borrowers to Lender.

**Section 3. Change in Definition of Letter of Credit.** The defined term “Letter of Credit” in Section 1.1 of the Loan Agreement is hereby modified and amended in its entirety to read as follows effective as of the date of this Agreement, with the existing defined term to continue to be effective for periods prior to the date of this Agreement:

**Letter of Credit:** One or more Irrevocable Standby Letters of Credit in an aggregate amount not to exceed the Letter of Credit Amount, issued by Lender in favor of one or more commercial insurance companies as beneficiary, for the account of one or more of Borrowers or AdCare.

**Section 4. Change in Definition of Letter of Credit Amount.** The defined term “Letter of Credit Amount” in Section 1.1 of the Loan Agreement is hereby modified and amended in its entirety to read as follows effective as of the date of this Agreement, with the existing defined term to continue to be effective for periods prior to the date of this Agreement:

**Letter of Credit Amount:** \$2,500,000, it being understood that the Letter of Credit Amount is a part of the Loan Amount and not in addition to the Loan Amount.

**Section 5. Change in Definition of Letter of Credit Documents.** The defined term “Letter of Credit Documents” in Section 1.1 of the Loan Agreement is hereby modified and amended in its entirety to read as follows effective as of the date of this Agreement, with the existing defined term to continue to be effective for periods prior to the date of this Agreement:

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**Letter of Credit Documents:** The following: (i) the Master Letter of Credit Agreement dated as of February 14, 2012, originally from Borrowers 14 through 19 to Lender, and joined in herein by the other Borrowers; (ii) the Master Letter of Credit Agreement dated as of October 15, 2012 from Borrowers to Lender; (iii) any subsequent Master Letter of Credit Agreement from Borrowers to Lender; and (iv) any Application for the issuance of a Letter of Credit from Borrowers in favor of Lender.

**Section 6. Change in Definition of Loan Amount.** The defined term “Loan Amount” in Section 1.1 of the Loan Agreement is hereby modified and amended in its entirety to read as follows effective as of the date of this Agreement, with the existing defined term to continue to be effective for periods prior to the date of this Agreement:

**Loan Amount:** \$10,600,000, which includes the \$2,500,000 Letter of Credit Amount.

**Section 7. Changes in Letter of Credit Terms.**

(a) Section 3.2(a) of the Loan Agreement is hereby modified and amended in its entirety to read as follows effective as of the date of this Agreement, with the existing Section 3.2(a) of the Loan Agreement to continue to be effective for periods prior to the date of this Agreement:

(a) Lender previously issued a Letter of Credit in the amount of \$100,000 (the “**\$100,000 Letter of Credit**”) pursuant to that certain Master Letter of Credit Agreement to which Borrowers 14 through 19 were a party, and an Application. Such Letter of Credit is currently outstanding in the face amount of \$100,000. The \$100,000 Letter of Credit and any other Letters of Credit issued by Lender pursuant to the terms of this Agreement shall each be deemed to be a Letter of Credit for purposes of this Agreement.

(b) Section 3.2(e) of the Loan Agreement is hereby modified and amended in its entirety to read as follows effective as of the date of this Agreement, with the existing Section 3.2(e) of the Loan Agreement to continue to be effective for periods prior to the date of this Agreement:

(e) Borrowers paid a non-refundable annual letter of credit fee to Lender in advance of the date of issuance of the \$100,000 Letter of Credit. Borrowers shall pay a non-refundable annual letter of credit fee to Lender in advance of the date of issuance of any subsequent Letter of Credit in such amount as shall be agreed between Borrowers and the Lender at the time such Letter of Credit is issued. Borrowers shall also pay a non-refundable annual letter of credit fee to Lender in advance on each anniversary of the date of the issuance of each Letter of Credit, in an amount equal to 2.5% of the face amount of such Letter of Credit, or such

other amount as shall be agreed between Borrowers and Lender at the time such Letter of Credit is issued.

**Section 8. Attachment to Note.** The Lender may, and prior to any transfer by it of the Note shall, attach a copy of this Agreement to the original Note and place an endorsement on the original Note making reference to the fact that such attachment has been made.

**Section 9. Representations and Warranties.** The term “**Signing Entity**” as used in this Section means any entity (other than a Borrower/Guarantor Party itself) that appears in the signature block of any Borrower/Guarantor Party in this Agreement or any of the Documents, if any. In order to induce the Lender to enter into this Agreement, the Borrower/Guarantor Parties hereby represent and warrant to the Lender as follows as of the date of this Agreement and if different, as of the date of the execution and delivery of this Agreement:

(a) Each Borrower is a limited liability company duly organized, validly existing and in good standing under the laws of the State of which is stated in the Preambles to this Agreement, and if such State is not the State in which its Facility is located, such Borrower is duly registered or qualified to transact business and in good standing in the State in which its Facility is located. Each Borrower has all necessary power and authority to carry on its present business, and has full right, power and authority to enter into this Agreement and each of the Documents to which it is a party and to perform and consummate the transactions contemplated hereby and thereby.

(b) The Guarantor is a corporation duly organized, validly existing and in good standing under the laws of the State of Ohio, has all necessary power and authority to carry on its present business, and has full right, power and authority to enter into this

Agreement and each of the Documents to which it is a party and to perform and consummate the transactions contemplated hereby and thereby.

(c) Each Signing Entity is duly organized, validly existing and in good standing under the laws of the State in which it is organized, has all necessary power and authority to carry on its present business, and has full right, power and authority to execute this Agreement and the Documents in the capacity shown in each signature block contained in this Agreement and the Documents in which its name appears, and such execution has been duly authorized by all necessary legal action applicable to such Signing Entity.

(d) This Agreement and each of the Documents has been duly authorized, executed and delivered by such of the Borrower/Guarantor Parties as are parties thereto, and this Agreement and each of the Documents constitutes a valid and legally binding obligation enforceable against such of the Borrower/Guarantor Parties as are parties thereto. The execution and delivery of this Agreement and the Documents and compliance with the provisions thereof under the circumstances contemplated therein do not and will not conflict with or constitute a breach or violation of or default under the organizational documents of any Borrower/Guarantor Party or any Signing Entity, or any agreement or other instrument to which any of the Borrower/Guarantor Parties or any Signing Entity is a party, or by which any of them is bound, or to which any of their respective properties are subject, or any existing law, administrative regulation, court order or consent decree to which any of them is subject.

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(e) The Borrower/Guarantor Parties are in full compliance with all of the terms and conditions of the Documents to which they are a party, and no Default or Event of Default has occurred and is continuing with respect to any of the Documents.

(f) There is no litigation or administrative proceeding pending or threatened to restrain or enjoin the transactions contemplated by this Agreement or any of the Documents, or questioning the validity thereof, or in any way contesting the existence or powers of any of the Borrower/Guarantor Parties or any Signing Entity, or in which an unfavorable decision, ruling or finding would adversely affect the transactions contemplated by this Agreement or any of the Documents, or would result in any material adverse change in the financial condition, properties, business or operations of any of the Borrower/Guarantor Parties.

(g) The statements contained in the Recitals to this Agreement are true and correct.

**Section 10. Documents to Remain in Effect; Confirmation of Obligations; References.** The Documents shall remain in full force and effect as originally executed and delivered by the parties, except as expressly modified and amended herein. In order to induce the Lender to enter into this Agreement, the Borrower/Guarantor Parties hereby (i) confirm and reaffirm all of their obligations under the Documents, as modified and amended herein; (ii) acknowledge and agree that the Lender, by entering into this Agreement, does not waive any existing or future default or event of default under any of the Documents, or any rights or remedies under any of the Documents, except as expressly provided herein; (iii) acknowledge and agree that the Lender has not heretofore waived any default or event of default under any of the Documents, or any rights or remedies under any of the Documents; and (iv) acknowledge and agree that they do not have any defense, setoff or counterclaim to the payment or performance of any of their obligations under, or to the enforcement by the Lender of, the Documents, as modified and amended herein, including, without limitation, any defense, setoff or counterclaim based on the covenant of good faith and fair dealing. All references in the Documents to any one or more of the Documents, or to the "Loan Documents," shall be deemed to refer to such Document, Documents or Loan Documents, as the case may be, as modified and amended by this Agreement. Electronic records of executed documents maintained by the Lender shall be deemed to be originals thereof.

**Section 11. Certifications, Representations and Warranties.** In order to induce the Lender to enter into this Agreement, the Borrower/Guarantor Parties hereby certify, represent and warrant to the Lender that all certifications, representations and warranties contained in the Documents and in all certificates heretofore delivered to the Lender are true and correct as of the date of this Agreement and if different, as of the date of the execution and delivery of this Agreement, and all such certifications,

representations and warranties are hereby remade and made to speak as of the date of this Agreement and if different, as of the date of the execution and delivery of this Agreement.

**Section 12. Entire Agreement; No Reliance.** This Agreement sets forth all of the covenants, promises, agreements, conditions and understandings of the parties relating to the subject matter of this Agreement, and there are no covenants, promises, agreements, conditions or understandings, either oral or written, between them relating to the subject matter of this Agreement other than as are herein set forth. The Borrower/Guarantor Parties acknowledge that

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they are executing this Agreement without relying on any statements, representations or warranties, either oral or written, that are not expressly set forth herein.

**Section 13. Successors.** This Agreement shall inure to the benefit of and shall be binding upon the parties and their respective successors, assigns and legal representatives.

**Section 14. Severability.** In the event any provision of this Agreement shall be held invalid or unenforceable by any court of competent jurisdiction, such holding shall not invalidate or render unenforceable any other provision hereof.

**Section 15. Amendments, Changes and Modifications.** This Agreement may be amended, changed, modified, altered or terminated only by a written instrument executed by all of the parties hereto.

**Section 16. Construction.**

- (a) The words “hereof,” “herein,” and “hereunder,” and other words of a similar import refer to this Agreement as a whole and not to the individual Sections in which such terms are used.
- (b) References to Sections and other subdivisions of this Agreement are to the designated Sections and other subdivisions of this Agreement as originally executed.
- (c) The headings of this Agreement are for convenience only and shall not define or limit the provisions hereof.
- (d) Where the context so requires, words used in singular shall include the plural and vice versa, and words of one gender shall include all other genders.
- (e) The Borrower/Guarantor Parties and the Lender, and their respective legal counsel, have participated in the drafting of this Agreement, and accordingly the general rule of construction to the effect that any ambiguities in a contract are to be resolved against the party drafting the contract shall not be employed in the construction and interpretation of this Agreement.

**Section 17. Counterparts; Electronic Signatures.** This Agreement may be executed in any number of counterparts and by the different parties hereto on separate counterparts and each such counterpart shall be deemed to be an original, but all such counterparts shall together constitute but one and the same document. Receipt of an executed signature page to this Agreement by facsimile or other electronic transmission shall constitute effective delivery thereof. An electronic record of this executed Agreement maintained by the Lender shall be deemed to be an original.

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**Section 18. Governing Law.** This Agreement is prepared and entered into with the intention that the law of the State of Illinois shall govern its construction and enforcement.

**[SIGNATURE PAGE(S) AND EXHIBIT(S),  
IF ANY, FOLLOW THIS PAGE]**

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**IN WITNESS WHEREOF**, the parties have executed this Agreement as of the date first above written.

**ADK THOMASVILLE OPERATOR, LLC  
ADK LUMBER CITY OPERATOR, LLC  
ADK JEFFERSONVILLE OPERATOR, LLC  
ADK LAGRANGE OPERATOR, LLC  
ADK POWDER SPRINGS OPERATOR, LLC  
ADK OCEANSIDE OPERATOR, LLC  
ADK THUNDERBOLT OPERATOR, LLC  
ADK SAVANNAH BEACH OPERATOR, LLC  
ATTALLA NURSING ADK, LLC  
MOUNTAIN TRACE NURSING ADK, LLC  
MT. KENN NURSING, LLC  
ERIN NURSING, LLC  
CP NURSING, LLC  
BENTON NURSING, LLC  
VALLEY RIVER NURSING, LLC  
PARK HERITAGE NURSING, LLC  
HOMESTEAD NURSING, LLC  
WOODLAND MANOR NURSING, LLC  
MOUNTAIN VIEW NURSING, LLC  
NORTHRIDGE HC&R NURSING, LLC  
LITTLE ROCK HC&R NURSING, LLC  
WOODLAND HILLS HC NURSING, LLC  
APH&R NURSING, LLC  
GLENVUE H&R NURSING, LLC  
COOSA NURSING ADK, LLC**

By /s/ Christopher F. Brogdon  
Christopher F. Brogdon, Manager of Each Borrower

**ADCARE HEALTH SYSTEMS, INC.**

By /s/ Christopher F. Brogdon  
Christopher F. Brogdon, Vice Chairman and Chief Acquisition  
Officer



**THE PRIVATEBANK AND TRUST COMPANY**

By /s/ Amy K. Hallberg  
Amy K. Hallberg, Managing Director

**PROMISSORY NOTE**

\$10,600,000  
Chicago, Illinois

September 20, 2012

1. **AGREEMENT TO PAY.** For value received, the following named undersigned parties (the "**Borrowers**") –

**ADK THOMASVILLE OPERATOR, LLC**, a Georgia limited liability company,

**ADK LUMBER CITY OPERATOR, LLC**, a Georgia limited liability company,

**ADK JEFFERSONVILLE OPERATOR, LLC**, a Georgia limited liability company,

**ADK LAGRANGE OPERATOR, LLC**, a Georgia limited liability company,

**ADK POWDER SPRINGS OPERATOR, LLC**, a Georgia limited liability company,

**ADK OCEANSIDE OPERATOR, LLC**, a Georgia limited liability company,

**ADK THUNDERBOLT OPERATOR, LLC**, Georgia limited liability company,

**ADK SAVANNAH BEACH OPERATOR, LLC**, a Georgia limited liability company,

**ATTALLA NURSING ADK, LLC**, a Georgia limited liability company,

**MOUNTAIN TRACE NURSING ADK, LLC**, an Ohio limited liability company,

**MT. KENN NURSING, LLC**, a Georgia limited liability company,

**ERIN NURSING, LLC**, a Georgia limited liability company),

**CP NURSING, LLC**, a Georgia limited liability company,

**BENTON NURSING, LLC**, a Georgia limited liability company,

**VALLEY RIVER NURSING, LLC**, a Georgia limited liability company,

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**PARK HERITAGE NURSING, LLC**, a Georgia limited liability company,

**HOMESTEAD NURSING, LLC**, a Georgia limited liability company,

**WOODLAND MANOR NURSING, LLC**, a Georgia limited liability company,

**MOUNTAIN VIEW NURSING, LLC**, a Georgia limited liability company,

**NORTHRIDGE HC&R NURSING, LLC**, a Georgia limited liability company,

**LITTLE ROCK HC&R NURSING, LLC**, a Georgia limited liability company,

**WOODLAND HILLS HC NURSING, LLC**, a Georgia limited liability company,

**APH&R NURSING, LLC**, a Georgia limited liability company,

**GLENVUE H&R NURSING, LLC**, a Georgia limited liability company,

and

**COOSA NURSING ADK, LLC**, a Georgia limited liability company,

hereby jointly and severally promise to pay to the order of **THE PRIVATEBANK AND TRUST COMPANY**, an Illinois banking corporation (the "**Lender**"), the principal sum of \$10,600,000 (the "**Loan**"), or so much of the Loan as may be advanced under and pursuant to that certain Loan and Security Agreement dated as of even date herewith (the "**Loan Agreement**"), executed by and among the Borrowers and the Lender, on or before September 20, 2015 (the "**Maturity Date**"), at the time and place and in the manner hereinafter provided, together with interest thereon at the rate or rates described below, and any and all other amounts which may be due and payable hereunder or under any of the "**Loan Documents**" (as defined in the Loan Agreement) from time to time. All capitalized terms used and not otherwise defined in this Note shall have the same meanings as in the Loan Agreement. Each disbursement on the Loan made by the Lender, and all payments on account of the principal and interest thereof, shall be recorded on the books and records of the Lender and the principal balance as shown on such books and records, or any copy thereof certified by an officer of the Lender, shall be rebuttably presumptive evidence of the principal amount owing hereunder.

## 2. **INTEREST RATE.**

2.1 **Interest Prior to Default.** Except as otherwise expressly provided in this Note, interest shall accrue on the principal balance of this Note through the Maturity Date at a rate of interest equal to the greater of (i) a floating per annum rate of interest equal to the "**Prime Rate**" (as defined below), plus 1.0%, or (ii) 5.0% per annum. Changes in the rate of interest to be charged hereunder based on the Prime Rate shall take effect immediately upon the occurrence of any change in the Prime Rate. For purposes of this Note, the term "**Prime Rate**" means the

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floating per annum rate of interest most recently announced by the Lender at Chicago, Illinois as its prime or base rate. A certificate made by an officer of the Lender stating the Prime Rate in effect on any given day, for the purposes hereof, shall be conclusive evidence of the Prime Rate in effect on such day. The Prime Rate is a base reference rate of interest adopted by the Lender as a general benchmark from which the Lender determines the floating interest rates chargeable on various loans to borrowers with varying degrees of creditworthiness and the Borrowers acknowledge and agree that the Lender has made no representations whatsoever that the Prime Rate is the interest rate actually offered by the Lender to borrowers of any particular creditworthiness.

2.2 **Interest After Default.** From and after the Maturity Date or upon the occurrence and during the continuance of an Event of Default, interest shall accrue on the unpaid principal balance during any such period at an annual rate (the "**Default Rate**") 5.0% greater than the interest rate which would otherwise be in effect under the terms of this Note. However, in no event shall the Default Rate exceed the maximum rate permitted by law. The interest accruing under this Section shall be immediately due and payable by the Borrowers to the holder of this Note upon demand and shall be additional indebtedness evidenced by this Note.

2.3 **Interest Calculation.** Interest on this Note shall be calculated on the basis of a 360-day year and the actual number of days elapsed in any portion of a month in which interest is due. If any payment to be made by the Borrowers hereunder shall become due on a day other than a Business Day, such payment shall be made on the next succeeding Business Day and such extension of time shall be included in computing any interest in respect of such payment.

3. **PAYMENT TERMS.**

3.1 **Payment of Principal and Interest.** Payments of principal and interest due under this Note, if not sooner declared to be due in accordance with the provisions hereof, shall be made as follows:

(a) On the first day of the month of October, 2012, and on the first day of each month thereafter through and including the month in which the Maturity Date occurs, interest accrued on this Note shall be due and payable.

(b) Principal shall be payable on this Note in accordance with the provisions of Section 3.4 of the Loan Agreement.

(c) The unpaid principal balance of this Note, if not sooner paid or declared to be due in accordance with the terms hereof, together with all accrued and unpaid interest thereon and any other amounts due and payable hereunder or under any of the Loan Documents shall be due and payable in full on the Maturity Date.

3.2 **Application of Payments.** Prior to the occurrence of an Event of Default, all payments and prepayments on account of the indebtedness evidenced by this Note shall be applied as follows: (a) first, to fees, expenses, costs and other similar amounts then due and payable to the Lender, including, without limitation any prepayment premium, exit fee or late charges due hereunder, (b) second, to accrued and unpaid interest on the principal balance of this Note, (c) third, to the payment of principal due in the month in which the payment or prepayment

is made, (d) fourth, to any escrows, impounds or other amounts which may then be due and payable under the Loan Documents, (e) fifth, to any other amounts then due the Lender hereunder or under any of the Loan Documents, and (f) last, to the unpaid principal balance of this Note in the inverse order of maturity. Any prepayment on account of the indebtedness evidenced by this Note shall not extend or postpone the due date or reduce the amount of any subsequent monthly payment of principal and interest due hereunder. After an Event of Default has occurred and is continuing, payments may be applied by the Lender to amounts owed hereunder and under the Loan Documents in such order as the Lender shall determine, in its sole discretion.

3.3 **Method of Payments.** All payments of principal and interest hereunder shall be paid by automatic debit, wire transfer, check or in coin or currency which, at the time or times of payment, is the legal tender for public and private debts in the United States of America and shall be made at such place as the Lender or the legal holder or holders of this Note may from time to time appoint in the payment invoice or otherwise in writing, and in the absence of such appointment, then at the offices of the Lender at 120 South LaSalle Street, Chicago, Illinois 60603. Payment made by check shall be deemed paid on the date the Lender receives such check; provided, however, that if such check is subsequently returned to the Lender unpaid due to insufficient funds or otherwise, the payment shall not be deemed to have been made and shall continue to bear interest until collected. Notwithstanding the foregoing, the final payment due under this Note must be made by wire transfer or other immediately available funds. With the exception of interest which under the terms of the Loan Documents is to be paid from a disbursement of proceeds of the Loan, interest, principal payments and any fees and expenses owed the Lender from time to time will be deducted by the Lender automatically on the due date from the Borrowers' account with the Lender, as designated in writing by the Borrowers. The Borrowers shall maintain sufficient funds in the

account on the dates the Lender enters debits authorized by this Note. If there are insufficient funds in the account on the date the Lender enters any debit authorized by this Note, the debit will be reversed.

3.4 **Late Charge.** If any payment of interest or principal due hereunder is not made within five days after such payment is due in accordance with the terms hereof, then, in addition to the payment of the amount so due, the Borrowers shall pay to the Lender a “late charge” of five cents for each whole dollar so overdue to defray part of the cost of collection and handling such late payment. The Borrowers agree that the damages to be sustained by the holder hereof for the detriment caused by any late payment are extremely difficult and impractical to ascertain, and that the amount of five cents for each one dollar due is a reasonable estimate of such damages, does not constitute interest, and is not a penalty.

3.5 **Principal Prepayments.** The principal of this Note may be prepaid, at any time, in whole or in part, without premium or penalty, provided that such prepayment is accompanied by a simultaneous payment of all accrued and unpaid interest on this Note through the date of prepayment.

4. **SECURITY; LOAN DOCUMENTS.** This Note is secured by the Loan Agreement and the other Loan Documents. Reference is hereby made to the Loan Agreement and the other Loan Documents (all of which are incorporated herein by reference as fully and with the same effect as if set forth herein at length) for a statement of the covenants and agreements contained therein, a statement of the rights, remedies, and security afforded thereby,

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and all matters therein contained. This Note and the Loan are also secured by all of the collateral provided to the Lender for the Owner Loan, and all of the collateral for this Note and the Loan also secure the Owner Loan.

5. **EVENTS OF DEFAULT.** The occurrence of any one or more of the following events shall constitute an “**Event of Default**” under this Note:

- (a) The failure by the Borrowers to pay (i) any installment of principal or interest payable pursuant to this Note on the date when due, or (ii) any other amount payable to the Lender under this Note, the Loan Agreement or any of the other Loan Documents on the date when any such payment is due in accordance with the terms hereof or thereof; or
- (b) The occurrence of any “Event of Default” under the Loan Agreement or any of the other Loan Documents.

For purposes of this Note, the term “**Default**” means the occurrence or existence of any event or circumstance which, with the giving of notice or passage of time, or both, would constitute an Event of Default.

6. **REMEDIES.** At the election of the holder hereof, and without notice, the principal balance remaining unpaid under this Note, and all unpaid interest accrued thereon and any other amounts due hereunder, shall be and become immediately due and payable in full upon the occurrence of any Event of Default. Failure to exercise this option shall not constitute a waiver of the right to exercise same in the event of any subsequent Event of Default. No holder hereof shall, by any act of omission or commission, be deemed to waive any of its rights, remedies or powers hereunder or otherwise unless such waiver is in writing and signed by the holder hereof, and then only to the extent specifically set forth therein. The rights, remedies and powers of the holder hereof, as provided in this Note and in all of the other Loan Documents are cumulative and concurrent, and may be pursued singly, successively or together against the Borrowers, any Guarantor hereof and any security given at any time to secure the repayment hereof, all at the sole discretion of the holder hereof. If any suit or action is instituted or attorneys are employed to collect this Note or any part hereof, the Borrowers promise and agree to pay all costs of collection, including reasonable attorneys’ fees and court costs.

7. **COVENANTS AND WAIVERS.** The Borrowers and all others who now or may at any time become liable for all or any part of the obligations evidenced hereby, expressly agree hereby to be jointly and severally bound, and jointly and severally: (i) waive and renounce any and all homestead, redemption and exemption rights and the benefit of all valuation and appraisal privileges against the indebtedness evidenced by this Note or by any extension or renewal hereof; (ii) waive presentment and demand for payment, notices of nonpayment and of dishonor, protest of dishonor, and notice of protest; (iii) waive any and all notices in connection with the delivery and acceptance hereof and all other notices in connection with the performance, default, or enforcement of the payment hereof or hereunder; (iv) waive any and all lack of diligence and delays in the enforcement of the payment hereof; (v) agree that the liability of the Borrowers and each guarantor, endorser or obligor shall be unconditional and without regard to the liability of any other person or entity for the payment hereof, and shall not in any manner be affected by any indulgence or forbearance granted or consented to by the Lender to any of them

with respect hereto; (vi) consent to any and all extensions of time, renewals, waivers, or modifications that may be granted by the Lender with respect to the payment or other provisions hereof, and to the release of any security at any time given for the payment hereof, or any part thereof, with or without substitution, and to the release of any person or entity liable for the payment hereof; and (vii) consent to the addition of any and all other makers, endorsers, guarantors, and other obligors for the payment hereof, and to the acceptance of any and all other security for the payment hereof, and agree that the addition of any such makers, endorsers, guarantors or other obligors, or security shall not affect the liability of the Borrowers, any guarantor and all others now liable for all or any part of the obligations evidenced hereby. This provision is a material inducement for the Lender making the Loan to the Borrowers.

8. **GENERAL AGREEMENTS.**

8.1 **Incorporation of Section 12.2 of Loan Agreement.** The provisions of Section 12.2 of the Loan Agreement are hereby incorporated into and made a part of this Note.

8.2 **Usury and Truth in Lending.** The Loan is a “business loan” within the meaning of subparagraph (1)(c) contained in Section 205/4 of Chapter 815 of the Illinois Compiled Statutes, as amended, and does not violate the provisions of the usury laws of the State, any consumer credit laws or the usury laws of any state which may have jurisdiction over this transaction, the Borrowers or any property securing the Loan. The Loan is an exempted transaction under the Truth In Lending Act, 15 U.S.C., §1601, et seq., as amended.

8.3 **Time.** Time is of the essence hereof.

8.4 **Governing Law.** This Note is governed and controlled as to validity, enforcement, interpretation, construction, effect and in all other respects by the statutes, laws and decisions of the State of Illinois, without regard to its conflict of laws provisions.

8.5 **Entire Agreement; Amendments.** This Note sets forth all of the covenants, promises, agreements, conditions and understandings of the parties relating to the subject matter of this Note, and there are no covenants, promises, agreements, conditions or understandings, either oral or written, between them other than as are herein set forth. Each Borrower acknowledges that it is executing this Note without relying on any statements, representations or warranties, either oral or written, that are not expressly set forth herein. This Note may not be changed or amended orally but only by an instrument in writing signed by the party against whom enforcement of the change or amendment is sought.

8.6 **No Joint Venture.** The Lender shall not be construed for any purpose to be a partner, joint venturer, agent or associate of the Borrowers or of any lessee, operator, concessionaire or licensee of the Borrowers in the conduct of their business, and by the execution of this Note, the Borrowers agree to indemnify, defend, and hold the Lender harmless from and against any and all damages,

costs, expenses and liability that may be incurred by the Lender as a result of a claim that the Lender is such partner, joint venturer, agent or associate.

8.7 **Disbursement.** This Note has been made and delivered at Chicago, Illinois and all funds disbursed to or for the benefit of the Borrowers will be disbursed in Chicago, Illinois.

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8.8 **Joint and Several Obligations; Successors and Assigns.** If this Note is executed by more than one party, the obligations and liabilities of each Borrower under this Note shall be joint and several. This Note shall be binding upon and enforceable against each Borrower and their respective successors and assigns. This Note shall inure to the benefit of and may be enforced by the Lender and its successors and assigns.

8.9 **Severable Provisions.** If any provision of this Note is deemed to be invalid by reason of the operation of law, or by reason of the interpretation placed thereon by any administrative agency or any court, the Borrowers and the Lender shall negotiate an equitable adjustment in the provisions of the same in order to effect, to the maximum extent permitted by law, the purpose of this Note, and the validity and enforceability of the remaining provisions, or portions or applications thereof, shall not be affected thereby and shall remain in full force and effect.

8.10 **Interest Limitation.** If the interest provisions herein or in any of the Loan Documents shall result, at any time during the Loan, in an effective rate of interest which, for any month, exceeds the limit of usury or other laws applicable to the Loan, all sums in excess of those lawfully collectible as interest for the period in question shall, without further agreement or notice between or by any party hereto, be applied upon principal immediately upon receipt of such monies by the Lender, with the same force and effect as though the payer has specifically designated such extra sums to be so applied to principal and the Lender had agreed to accept such extra payment(s) as a premium-free prepayment. Notwithstanding the foregoing, however, the Lender may at any time and from time to time elect by notice in writing to the Borrowers to reduce or limit the collection to such sums which, when added to the said first-stated interest, shall not result in any payments toward principal in accordance with the requirements of the preceding sentence. In no event shall any agreed to or actual exaction as consideration for this Loan transcend the limits imposed or provided by the law applicable to this transaction or the maker hereof for the use or detention of money or for forbearance in seeking its collection.

8.11 **Assignability.** The Lender may at any time assign its rights in this Note and the Loan Documents, or any part thereof and transfer its rights in any or all of the collateral, and the Lender thereafter shall be relieved from all liability with respect to such collateral. In addition, the Lender may at any time sell one or more participations in this Note. The Borrowers may not assign their interest in this Note, or any other agreement with the Lender or any portion thereof, either voluntarily or by operation of law, without the prior written consent of the Lender.

9. **NOTICES.** All notices required under this Note will be in writing and will be transmitted in the manner and to the addresses required by the Loan Agreement, or to such other addresses as the Lender and the Borrowers may specify from time to time in writing.

10. **LITIGATION PROVISIONS.**

10.1 **Consent to Jurisdiction.** EACH BORROWER CONSENTS AND SUBMITS TO THE JURISDICTION OF ANY STATE OR FEDERAL COURT LOCATED IN CHICAGO, ILLINOIS, AND OF ANY STATE OR FEDERAL COURT LOCATED OR HAVING JURISDICTION IN THE COUNTY IN WHICH ITS FACILITY IS LOCATED, IN WHICH ANY LEGAL PROCEEDING MAY BE COMMENCED OR PENDING

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RELATING IN ANY MANNER TO THIS NOTE, THE LOAN OR ANY OF THE OTHER LOAN DOCUMENTS.

10.2 **Consent to Venue.** EACH BORROWER AGREES THAT ANY LEGAL PROCEEDING RELATING TO THIS NOTE, THE LOAN OR ANY OF THE OTHER LOAN DOCUMENTS MAY BE BROUGHT AGAINST SUCH BORROWER IN ANY STATE OR FEDERAL COURT LOCATED IN CHICAGO, ILLINOIS, OR ANY STATE OR FEDERAL COURT LOCATED OR HAVING JURISDICTION IN THE COUNTY IN WHICH ITS FACILITY IS LOCATED. EACH BORROWER WAIVES ANY OBJECTION TO VENUE IN ANY SUCH COURT AND WAIVES ANY RIGHT IT MAY HAVE TO TRANSFER OR CHANGE THE VENUE FROM ANY SUCH COURT.

10.3 **No Proceedings in Other Jurisdictions.** EACH BORROWER AGREES THAT IT WILL NOT COMMENCE ANY LEGAL PROCEEDING AGAINST THE LENDER RELATING IN ANY MANNER TO THIS NOTE, THE LOAN OR ANY OF THE OTHER LOAN DOCUMENTS IN ANY COURT OTHER THAN A STATE OR FEDERAL COURT LOCATED IN CHICAGO, ILLINOIS, OR IF A LEGAL PROCEEDING IS COMMENCED BY THE LENDER AGAINST SUCH BORROWER IN A COURT IN ANOTHER LOCATION, BY WAY OF A COUNTERCLAIM IN SUCH LEGAL PROCEEDING.

10.4 **Waiver of Jury Trial.** EACH BORROWER HEREBY WAIVES TRIAL BY JURY IN ANY LEGAL PROCEEDING RELATING TO THIS NOTE, THE LOAN OR ANY OF THE OTHER LOAN DOCUMENTS.

11. **CUSTOMER IDENTIFICATION - USA PATRIOT ACT NOTICE; OFAC AND BANK SECRECY ACT.** The Lender hereby notifies the Borrowers that pursuant to the requirements of the USA Patriot Act (Title III of Pub. L. 107-56, signed into law October 26, 2001) (the "**Act**"), and the Lender's policies and practices, the Lender is required to obtain, verify and record certain information and documentation that identifies the Borrowers, which information includes the name and address of the Borrowers and such other information that will allow the Lender to identify the Borrowers in accordance with the Act. In addition, the Borrowers shall (a) ensure that no person who owns a controlling interest in or otherwise controls any Borrower or any subsidiary of any Borrower is or shall be listed on the Specially Designated Nationals and Blocked Person List or other similar lists maintained by the Office of Foreign Assets Control ("**OFAC**"), the Department of the Treasury or included in any Executive Orders, (b) not use or permit the use of the proceeds of the Loan to violate any of the foreign asset control regulations of OFAC or any enabling statute or Executive Order relating thereto, and (c) comply, and cause any of its subsidiaries to comply, with all applicable Bank Secrecy Act ("**BSA**") laws and regulations, as amended.

12. **EXPENSES AND INDEMNIFICATION.** The Borrowers shall pay all costs and expenses incurred by the Lender in connection with the preparation of this Note and the Loan Documents, including, without limitation, reasonable attorneys' fees and time charges of attorneys who may be employees of the Lender or any affiliate or parent of the Lender. The Borrowers shall pay any and all stamp and other taxes, UCC search fees, filing fees and other costs and expenses in connection with the execution and delivery of this Note and the other instruments and documents to be delivered hereunder, and agrees to save the Lender harmless

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from and against any and all liabilities with respect to or resulting from any delay in paying or omission to pay such costs and expenses. Each Borrowers hereby authorize the Lender to charge any account of such Borrower with the Lender for all sums due under this Section. The Borrowers also agree to defend (with counsel satisfactory to the Lender), protect, indemnify and hold harmless the Lender, any parent corporation, affiliated corporation or subsidiary of the Lender, and each of their respective officers, directors, employees, attorneys and agents (each an "**Indemnified Party**") from and against any and all liabilities, obligations, losses, damages, penalties, actions, judgments, suits, claims, costs, expenses and distributions of any kind or nature (including, without limitation, the disbursements and the reasonable fees of counsel for each Indemnified Party thereto, which shall also include, without limitation,



attorneys' fees and time charges of attorneys who may be employees of the Lender, any parent corporation or affiliated corporation of the Lender), which may be imposed on, incurred by, or asserted against, any Indemnified Party (whether direct, indirect or consequential and whether based on any federal, state or local laws or regulations, including, without limitation, securities, environmental laws and commercial laws and regulations, under common law or in equity, or based on contract or otherwise) in any manner relating to or arising out of this Note or any of the Loan Documents, or any act, event or transaction related or attendant thereto, the preparation, execution and delivery of this Note and the Loan Documents, the making or issuance and management of the Loan, the use or intended use of the proceeds of this Note and the enforcement of the Lender's rights and remedies under this Note, the Loan Documents any other instruments and documents delivered hereunder, or under any other agreement between the Borrowers and the Lender; provided, however, that the Borrowers shall not have any obligations hereunder to any Indemnified Party with respect to matters caused by or resulting from the willful misconduct or gross negligence of such Indemnified Party. To the extent that the undertaking to indemnify set forth in the preceding sentence may be unenforceable because it violates any law or public policy, the Borrowers shall satisfy such undertaking to the maximum extent permitted by applicable law. Any liability, obligation, loss, damage, penalty, cost or expense covered by this indemnity shall be paid to each Indemnified Party on demand, and failing prompt payment, together with interest thereon at the Default Rate from the date incurred by each Indemnified Party until paid by the Borrowers, shall be added to the obligations of the Borrowers evidenced by this Note and secured by the collateral securing this Note. The provisions of this Section shall survive the satisfaction and payment of this Note.

**[SIGNATURE PAGE(S) AND EXHIBIT(S),  
IF ANY, FOLLOW THIS PAGE]**

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**IN WITNESS WHEREOF**, the Borrowers have executed and delivered this Promissory Note as of the day and year first above written.

**ADK THOMASVILLE OPERATOR, LLC  
ADK LUMBER CITY OPERATOR, LLC  
ADK JEFFERSONVILLE OPERATOR, LLC  
ADK LAGRANGE OPERATOR, LLC  
ADK POWDER SPRINGS OPERATOR, LLC  
ADK OCEANSIDE OPERATOR, LLC  
ADK THUNDERBOLT OPERATOR, LLC  
ADK SAVANNAH BEACH OPERATOR, LLC  
ATTALLA NURSING ADK, LLC  
MOUNTAIN TRACE NURSING ADK, LLC  
MT. KENN NURSING, LLC  
ERIN NURSING, LLC  
CP NURSING, LLC  
BENTON NURSING, LLC  
VALLEY RIVER NURSING, LLC  
PARK HERITAGE NURSING, LLC  
HOMESTEAD NURSING, LLC  
WOODLAND MANOR NURSING, LLC  
MOUNTAIN VIEW NURSING, LLC  
NORTHRIDGE HC&R NURSING, LLC  
LITTLE ROCK HC&R NURSING, LLC  
WOODLAND HILLS HC NURSING, LLC**

**APH&R NURSING, LLC  
GLENVUE H&R NURSING, LLC  
COOSA NURSING ADK, LLC**

By /s/ Christopher F. Brogdon

Christopher F. Brogdon, Manager of Each Borrower

- AdCare Portfolio Operator Loan Note -  
- Signature Page -

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**GUARANTY OF PAYMENT AND PERFORMANCE**

THIS GUARANTY OF PAYMENT AND PERFORMANCE dated as of September 20, 2012 (this “**Guaranty**”), is executed by ADCARE HEALTH SYSTEMS, INC., an Ohio corporation (the “**Guarantor**”), to and for the benefit of THE PRIVATEBANK AND TRUST COMPANY, an Illinois banking corporation (the “**Lender**”).

**RECITALS**

A. The Lender has agreed to make a revolving loan in the principal amount of \$10,600,000 (the “**Loan**”) to ADK Thomasville Operator, LLC, ADK Lumber City Operator, LLC, ADK Jeffersonville Operator, LLC, ADK LaGrange Operator, LLC, ADK Powder Springs Operator, LLC, ADK Oceanside Operator, LLC, ADK Thunderbolt Operator, LLC, ADK Savannah Beach Operator, LLC, Attalla Nursing ADK, LLC, Mt. Kenn Nursing, LLC, Erin Nursing, LLC, CP Nursing, LLC, Benton Nursing, LLC, Valley River Nursing, LLC, Park Heritage Nursing, LLC, Homestead Nursing, LLC, Woodland Manor Nursing, LLC, Mountain View Nursing, LLC, Northridge HC&R Nursing, LLC, Little Rock HC&R Nursing, LLC, Woodland Hills HC Nursing, LLC, APH&R Nursing, LLC, Glenvue H&R Nursing, LLC, and Coosa Nursing ADK, LLC, each a Georgia limited liability company, and Mountain Trace Nursing ADK, LLC, an Ohio limited liability company (the “**Borrowers**”), pursuant to the terms and conditions of a Loan and Security Agreement of even date herewith (the “**Loan Agreement**”) by and among the Borrowers and the Lender. The Loan is evidenced by a Promissory Note of even date herewith (the “**Note**”) from the Borrowers to the Lender in the principal amount of \$10,600,000. All terms used and not otherwise defined herein shall have the meanings set forth in the Loan Agreement, and for the avoidance of doubt, all references in this Guaranty to the “Loan Documents” include, without limitation, any Bank Product Agreements (as defined in the Loan Agreement) to which the Lender or any of its Affiliates is a party, including, without limitation, any Hedging Agreements (as defined in the Loan Agreement) to which the Lender is a party.

B. The purpose of the Loan is to provide working capital financing for the Facilities described in the Loan Agreement. The Guarantor is the owner of 100% of the membership interests in each of the Borrowers either directly or indirectly through one or more intermediary entities, and is also deriving a benefit from the making of the Loan by the Lender.

C. As a condition precedent to the making of the Loan to the Borrowers by the Lender and in consideration therefor, the Lender has required the execution and delivery of this Guaranty by the Guarantor.

**AGREEMENTS**

For good and valuable consideration, the receipt and sufficiency of which hereby are acknowledged, the Guarantor hereby agrees as follows:

1. **Guaranty of Payment.**

(a) The Guarantor hereby unconditionally, absolutely and irrevocably guarantees the punctual payment and performance when due, whether at stated maturity or by acceleration or otherwise, of the indebtedness and other obligations of the Borrowers to the Lender evidenced by the Note and any other amounts that may become owing by the Borrowers under the Loan Documents (such indebtedness, obligations and other amounts are hereinafter referred to as the “**Payment Obligations**”), subject to the limitation set forth in paragraph (b) of this Section. If for any reason the Borrowers shall fail or be unable to pay, punctually and fully, any of their Payment Obligations, the Guarantor shall pay such obligations to the Lender in full immediately upon demand, subject to the limitation set forth in paragraph (b) of this Section.

(b) The liability of the Guarantor under paragraph (a) of this Section with respect to the amount of principal outstanding on the Note shall be limited to \$5,300,000 (the “**Principal Limit**”). There shall be no limitation on the liability of the Guarantor under paragraph (a) of this Section with respect to interest on the Note, or with respect to any other amounts (except principal of the Note) that may become owing by the Borrower under the Loan Documents. The limitation on the liability of the Guarantor provided for in this paragraph (b) does not apply to liability of the Guarantor arising under any provision of this Guaranty other than paragraph (a) of this Section. Amounts received by the Lender in partial payment of the principal of the Note, other than payments from the Guarantor, shall not reduce the obligation of the Guarantor under paragraph (a) of this Section with respect to the principal of the Note, except to the extent that such partial payments reduce the principal outstanding on the Note below the Principal Limit.

(c) In addition to the guaranties of payment provided for above in this Section, the Guarantor hereby unconditionally, absolutely and irrevocably guarantee, jointly and severally, the payment of (i) the Recourse Guaranty Obligations (as hereinafter defined), and (ii) the Full Re-Payment Obligations (as hereinafter defined), but, with respect to the Full Re-Payment Obligations, only if (A) there is fraud by any Borrower or any of their partners, shareholders, members, managers, officers or directors, as the case may be, or of the Guarantor, with respect to the Loan, (B) a Prohibited Transfer occurs and is not reversed within 14 days after the date on which it occurs, (C) any Borrower contests, delays or otherwise hinders any action taken by the Lender in connection with the appointment of a receiver for any collateral for the Loan or the foreclosure of the liens, deeds of trust, mortgages or other security interests created by any of the Loan Documents, or (D) any Borrower or Guarantor voluntarily files for bankruptcy, or is involuntarily placed into bankruptcy by an affiliate, accountant, attorney, or other representative of any Borrower or Guarantor and such involuntary bankruptcy is not dismissed within 30 days after the filing thereof. As used herein, the term “**Full Re-Payment Obligations**” shall mean the obligations of the Borrowers to pay the principal balance of and all interest due on the Note, whether at stated maturity or by acceleration or otherwise, and to pay any other amounts that may become owing under the Note or the other Loan Documents. As used herein, the term “**Recourse Guaranty Obligations**” shall mean:

(i) All “**Losses**” (as hereinafter defined) suffered or incurred by or on behalf of the Lender in enforcing the rights and remedies of the Lender under this Guaranty or under the other Loan Documents, together with all interest calculated at the Default Rate

until paid on all amounts owed by the Guarantor which accrues from and after the date the Lender’s demand for payment is delivered to the Guarantor;

(ii) All Losses suffered or incurred by the Lender as a result of any material misrepresentation in any of the Loan Documents;

(iii) All Losses suffered or incurred by the Lender as a result of waste with respect to any of the collateral for the Loan;

(iv) All Losses suffered or incurred by the Lender as a result of the removal or disposal of any property in which the Lender has a security interest in violation of the terms and conditions of the Loan Documents;

(v) All Losses suffered or incurred by the Lender as a result of any liens against any of the collateral for the Loan not expressly permitted or contested under the Loan Agreement or any of the other Loan Documents;

(vi) All Losses suffered or incurred by the Lender as a result of the application of any insurance proceeds (to the full extent of such proceeds) not permitted by the Loan Agreement any of the other Loan Documents, or the failure of any

Borrower to maintain or cause to be maintained the insurance coverages required by the Loan Agreement or any of the other Loan Documents; and

(vii) An amount equal to all revenues received by or on behalf of any Borrower from the operation or ownership of any Facility after the Lender has notified the Borrowers of a Default or Event of Default under any of the provisions of the Loan Documents, less only that portion of such revenues which are (A) actually used by the Borrowers to operate the Facilities in the ordinary course of business, or for other purposes which are approved in writing by the Lender, or (B) paid to the Lender.

The term "**Losses**" means any and all claims, suits, liabilities (including, without limitation, strict liabilities), actions, proceedings, obligations, debts, damages, losses, costs, expenses, fines, penalties, charges, fees, expenses, judgments, awards, amounts paid in settlement, and foreseeable and unforeseeable consequential damages, of whatever kind or nature (including but not limited to reasonable attorneys' fees and other costs of defense).

Under no circumstances shall the liability of the Guarantor hereunder be reduced by, from or as a result of any payment to or amount realized by the Lender from any rents, deposits, insurance proceeds, proceeds from bankruptcy sale, foreclosure or any conveyance in lieu of foreclosure or from any other profits, avails, revenues or proceeds derived from the Facilities, and only payments made to the Lender by the Guarantor out of its personal funds not derived from the Facilities after demand therefor by the Lender shall be applied against such liability.

(d) The guaranty in this Section 1 is a present and continuing guaranty of payment and not of collectability, and the Lender shall not be required to prosecute collection, enforcement or other remedies against any Borrower, the Guarantor, or any other guarantor of the Loan, or to enforce or resort to any collateral for the repayment of the Loan or other rights or remedies pertaining thereto, before calling on any Guarantor for payment. One or more

successive actions may be brought against the Guarantors or any of them, as often as the Lender deems advisable.

(e) The Payment Obligations, the Full Re-Payment Obligations, the Recourse Guaranty Obligations and the Performance Obligations (as hereinafter defined), are referred to herein as the "**Guaranteed Obligations.**"

2. **Guaranty of Performance.** In addition to the guaranty of the Payment Obligations, the Guarantor hereby unconditionally, absolutely and irrevocably guarantees, jointly and severally, (i) the full and prompt performance and observance by each Borrower of each and every other obligation, undertaking, liability, promise, warranty, covenant and agreement of each Borrower in and under the terms of the Loan Documents; and (ii) the truth of each and every representation and warranty made by each Borrower in the Loan Documents or in other certificates or documents delivered in connection with the Loan (the matters described in (i) and (ii) above being collectively referred to herein as the "**Performance Obligations**").

3. **Representations and Warranties.** The following shall constitute representations and warranties of the Guarantor and the Guarantor hereby acknowledges that the Lender intends to make the Loan in reliance thereon:

(a) The Guarantor is a corporation duly organized, validly existing and in good standing under the laws of the State of Ohio. The Guarantor has full power and authority to conduct its business as presently conducted, to execute and deliver the Loan Documents to which it is a party, and to perform all of its duties and obligations under the Loan Documents to which it is a party; and such execution and performance have been duly authorized by all necessary Legal Requirements. The articles of incorporation and bylaws of the Guarantor, each as amended to date, copies of which have been furnished to the Lender, are in effect, have not been further amended, and are the true, correct and complete documents relating to the Guarantor's creation and governance.

(b) The Guarantor is not in default and no event has occurred that with the passage of time or the giving of notice will constitute a default under any agreement to which the Guarantor is a party, the effect of which will impair performance by the Guarantor of its obligations under this Guaranty. Neither the execution and delivery of this Guaranty nor compliance with the terms and provisions hereof will violate any applicable law, rule, regulation, judgment, decree or order, or will conflict with or result in any breach of any of the terms, covenants, conditions or provisions of the articles of incorporation or bylaws of the Guarantor, any indenture, mortgage, deed of trust, instrument, document, agreement or contract of any kind that creates, represents, evidences or provides for any lien, charge or encumbrance upon any of the property or assets of the Guarantor, or any other indenture, mortgage, deed of trust, instrument, document, agreement or contract of any kind to which the Guarantor is a party or to which the Guarantor or the property of the Guarantor may be subject.

(c) There is no litigation, arbitration, governmental or administrative proceedings, actions, examinations, claims or demands pending, or to the Guarantor'

knowledge, threatened that could adversely affect performance by the Guarantor of its obligations under this Guaranty.

(d) Neither this Guaranty nor any statement or certification as to facts previously furnished or required herein to be furnished to the Lender by the Guarantor, contains any material inaccuracy or untruth in any representation, covenant or warranty or omits to state a fact material to this Guaranty.

4. **Continuing Guaranty.** The Guarantor agrees that performance by the Guarantor of the obligations under this Guaranty shall be a primary obligation, shall not be subject to any counterclaim, set-off, abatement, deferment or defense based upon any claim that the Guarantor may have against the Lender, any Borrower, any other guarantor of the Guaranteed Obligations or any other person or entity, and shall remain in full force and effect without regard to, and shall not be released, discharged or affected in any way by, any circumstance or condition (whether or not the Guarantor shall have any knowledge thereof), including without limitation –

- (a) Any lack of validity or enforceability of any of the Loan Documents;
- (b) Any termination, amendment, modification or other change in any of the Loan Documents, including, without limitation, any modification of the interest rate or rates described therein;
- (c) Any furnishing, exchange, substitution or release of any collateral securing repayment of the Loan, or any failure to perfect any lien in such collateral;
- (d) Any failure, omission or delay on the part of any Borrower, the Guarantor, any other guarantor of the Guaranteed Obligations or the Lender to conform or comply with any term of any of the Loan Documents or any failure of the Lender to give notice of any Event of Default;
- (e) Any waiver, compromise, release, settlement or extension of time of payment or performance or observance of any of the obligations or agreements contained in any of the Loan Documents;
- (f) Any action or inaction by the Lender under or in respect of any of the Loan Documents, any failure, lack of diligence, omission or delay on the part of the Lender to perfect, enforce, assert or exercise any lien, security interest, right, power or remedy conferred on it in any of the Loan Documents, or any other action or inaction on the part of the Lender;

(g) Any voluntary or involuntary bankruptcy, insolvency, reorganization, arrangement, readjustment, assignment for the benefit of creditors, composition, receivership, liquidation, marshalling of assets and liabilities or similar events or proceedings with respect to any Borrower, the Guarantor or any other guarantor of the Guaranteed Obligations, as applicable, or any of their respective property or creditors, or any action taken by any trustee or receiver or by any court in any such proceeding;

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(h) Any merger or consolidation of any Borrower into or with any entity, or any sale, lease or transfer of any of the assets of any Borrower, the Guarantor or any other guarantor of the Guaranteed Obligations to any other person or entity;

(i) Any change in the ownership of any Borrower, or any change in the relationship between any Borrower and the Guarantor or any other guarantor of the Guaranteed Obligations, or any termination of any such relationship;

(j) Any release or discharge by operation of law of any Borrower, the Guarantor or any other guarantor of the Guaranteed Obligations from any obligation or agreement contained in any of the Loan Documents; or

(k) Any other occurrence, circumstance, happening or event, whether similar or dissimilar to the foregoing and whether foreseen or unforeseen, which otherwise might constitute a legal or equitable defense or discharge of the liabilities of a guarantor or surety or which otherwise might limit recourse against any Borrower or the Guarantor to the fullest extent permitted by law.

5. **Waivers.** The Guarantor expressly and unconditionally waives (i) notice of any of the matters referred to in Section 4 above, (ii) all notices which may be required by statute, rule of law or otherwise, now or hereafter in effect, to preserve intact any rights against the Guarantor, including, without limitation, any demand, presentment and protest, proof of notice of non-payment under any of the Loan Documents and notice of any Event of Default or any failure on the part of any Borrower, the Guarantor or any other guarantor of the Guaranteed Obligations to perform or comply with any covenant, agreement, term or condition of any of the Loan Documents, (iii) any right to the enforcement, assertion or exercise against any Borrower, the Guarantor or any other guarantor of the Guaranteed Obligations of any right or remedy conferred under any of the Loan Documents, (iv) any requirement of diligence on the part of any person or entity, (v) to the fullest extent permitted by law and except as otherwise expressly provided in this Guaranty or the other Loan Documents, any claims based on allegations that the Lender has failed to act in a commercially reasonable manner or failed to exercise the Lender's obligation of good faith and fair dealing, (vi) any requirement to exhaust any remedies or to mitigate the damages resulting from any default under any of the Loan Documents, and (vii) any notice of any sale, transfer or other disposition of any right, title or interest of the Lender under any of the Loan Documents. The Guarantor agrees that the Guarantor is a guarantor and not a "surety" within the meaning of the Illinois Sureties Act, and also waives any and all rights under the Illinois Sureties Act.

6. **Subordination.** The Guarantor agrees that any and all present and future debts and obligations of any Borrower to the Guarantor hereby are subordinated to the claims of the Lender and hereby are assigned by the Guarantor to the Lender as security for the Guaranteed Obligations and the Guarantor's obligations under this Guaranty.

7. **Subrogation Waiver.** Until the Guaranteed Obligations are paid in full and all periods under applicable bankruptcy law for the contest of any payment by the Guarantor or the Borrowers as a preferential or fraudulent payment have expired, the Guarantor knowingly, and with advice of counsel, waives, relinquishes, releases and abandons all rights and claims to

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indemnification, contribution, reimbursement, subrogation and payment which the Guarantor may now or hereafter have by and from any Borrower and the successors and assigns of any Borrower, for any payments made by the Guarantor to the Lender, including, without limitation, any rights which might allow any Borrower, any Borrower's successors, a creditor of any Borrower, or a trustee in bankruptcy of any Borrower to claim in bankruptcy or any other similar proceedings that any payment made by any Borrower or any Borrower's successors and assigns to the Lender was on behalf of or for the benefit of the Guarantor and that such payment is recoverable by any Borrower, a creditor or trustee in bankruptcy of any Borrower as a preferential payment, fraudulent conveyance, payment of an insider or any other classification of payment which may otherwise be recoverable from the Lender.

8. **Reinstatement.** The obligations of the Guarantor pursuant to this Guaranty shall continue to be effective or automatically be reinstated, as the case may be, if at any time payment of any of the Guaranteed Obligations or the Guarantor's obligations under this Guaranty are rescinded or otherwise must be restored or returned by the Lender upon the insolvency, bankruptcy, dissolution, liquidation or reorganization of the Guarantor or any Borrower or otherwise, all as though such payment had not been made.

9. **Financial Statements.** The Guarantor represents and warrants to the Lender that (i) the financial statements of the Guarantor previously submitted to the Lender are true, complete and correct in all material respects, disclose all actual and contingent liabilities, and fairly present the financial condition of the Guarantor, and do not contain any untrue statement of a material fact or omit to state a fact material to the financial statements submitted or this Guaranty, and (ii) no material adverse change has occurred in the financial statements from the dates thereof until the date hereof. The Guarantor shall furnish to the Lender financial statements and other information as provided in Section 7.3 of the Loan Agreement.

10. **Transfers, Sales, Etc.** The Guarantor shall not sell, lease, transfer, convey or assign any of its or his assets, unless (i) if the Guarantor is a natural person, such sale, lease, transfer, conveyance or assignment is of a non-material asset of the Guarantor and will not have a material adverse effect on the Guarantor's financial condition, or (ii) if the Guarantor is a limited liability company, corporation, partnership or other entity, such sale, lease, transfer, conveyance or assignment will not have a material adverse effect on the business or financial condition of the Guarantor or its ability to perform its obligations hereunder.

11. **Default; Remedies.** An Event of Default shall occur hereunder if the Guarantor shall fail to pay or perform any of its covenants, agreements and obligations hereunder, or if any representation or warranty contained herein shall prove to be untrue or incorrect in any material respect. When any Event of Default hereunder has occurred and is continuing, the Lender may exercise any of the rights and remedies provided for herein or in any of the other Loan Documents, or provided to it by law, including, without limitation, the right of setoff.

12. **Enforcement Costs and Interest.** If: (i) this Guaranty, is placed in the hands of one or more attorneys for collection or is collected through any legal proceeding; (ii) one or more attorneys is retained to represent the Lender in any bankruptcy, reorganization, receivership or other proceedings affecting creditors' rights and involving a claim under this Guaranty, or (iii) one or more attorneys is retained to represent the Lender in any other proceedings

whatsoever in connection with this Guaranty, then the Guarantor shall pay to the Lender upon demand all fees, costs and expenses incurred by the Lender in connection therewith, including, without limitation, reasonable attorney's fees, court costs and filing fees, in addition to all other amounts due hereunder. Amounts due from a Guarantor under this Guaranty shall bear interest until paid at the Default Rate.

13. **Successors and Assigns; Joint and Several Liability.** This Guaranty shall inure to the benefit of the Lender and its successors and assigns. This Guaranty shall be binding on the Guarantor and the heirs, legatees, successors and assigns of the Guarantor. If this Guaranty is executed by more than one Guarantor, it shall be the joint and several undertaking of each of the undersigned. Regardless of whether this Guaranty is executed by more than one Guarantor, it is agreed that the liability of the



undersigned hereunder is several and independent of any other guarantees or other obligations at any time in effect with respect to the Guaranteed Obligations or any part thereof and that the liability of the Guarantor hereunder may be enforced regardless of the existence, validity, enforcement or non-enforcement of any such other guarantees or other obligations.

14. **No Waiver of Rights**. No delay or failure on the part of the Lender to exercise any right, power or privilege under this Guaranty or any of the other Loan Documents shall operate as a waiver thereof, and no single or partial exercise of any right, power or privilege shall preclude any other or further exercise thereof or the exercise of any other power or right, or be deemed to establish a custom or course of dealing or performance between the parties hereto. The rights and remedies herein provided are cumulative and not exclusive of any rights or remedies provided by law. No notice to or demand on the Guarantor in any case shall entitle the Guarantor to any other or further notice or demand in the same, similar or other circumstance.

15. **Prior Agreements; No Reliance; Modification**. This Guaranty shall represent the entire, integrated agreement between the parties hereto relating to the subject matter hereof, and shall supersede all prior negotiations, representations or agreements pertaining thereto, either oral or written. The Guarantor acknowledges that it is executing this Guaranty without relying on any statements, representations or warranties, either oral or written, that are not expressly set forth herein. The terms of this Guaranty may be waived, discharged, or terminated only by an instrument in writing signed by the party against which enforcement of the change, waiver, discharge or termination is sought. No amendment, modification, waiver or other change of any of the terms of this Guaranty shall be effective without the prior written consent of the Lender.

16. **Joinder**. Any action to enforce this Guaranty may be brought against the Guarantor without any joinder of any Borrower, any other Guarantor, or any other guarantor of the Guaranteed Obligations in such action.

17. **Incorporation of Recitals**. The Recitals to this Guaranty are hereby incorporated into and made a part of this Guaranty.

18. **Severability**. If any provision of this Guaranty is deemed to be invalid by reason of the operation of law, or by reason of the interpretation placed thereon by any administrative agency or any court, the Guarantor and the Lender shall negotiate an equitable adjustment in the provisions of the same in order to effect, to the maximum extent permitted by law, the purpose of

this Guaranty and the validity and enforceability of the remaining provisions, or portions or applications thereof, shall not be affected thereby and shall remain in full force and effect.

19. **Applicable Law**. This Guaranty is governed as to validity, interpretation, effect and in all other respects by laws and decisions of the State of Illinois.

20. **Captions**. The captions and headings of various Sections of this Guaranty pertaining hereto are for convenience only and are not to be considered as defining or limiting in any way the scope or intent of the provisions hereof.

21. **Execution of Counterparts; Electronic Signatures**. This Guaranty may be executed in any number of counterparts and by the different parties hereto on separate counterparts and each such counterpart shall be deemed to be an original, but all such counterparts shall together constitute but one and the same document. Receipt of an executed signature page to this Guaranty by facsimile or other electronic transmission shall constitute effective delivery thereof. An electronic record of this executed Guaranty maintained by the Lender shall be deemed to be an original.

22. **Construction.** Each party to this Guaranty and legal counsel to each party have participated in the drafting of this Guaranty, and accordingly the general rule of construction to the effect that any ambiguities in a contract are to be resolved against the party drafting the contract shall not be employed in the construction and interpretation of this Guaranty.

23. **Notice.** All notices and other communications provided for in this Guaranty ("**Notices**") shall be in writing. The "**Notice Addresses**" of the parties for purposes of this Guaranty are as follows:

Guarantor:	AdCare Health Systems, Inc. 5057 Troy Road Springfield, Ohio 45502 Attention: Boyd P. Gentry
With a copy to:	Holt Ney Zatcoff & Wasserman, LLP 100 Galleria Parkway, Suite 1800 Atlanta, Georgia 30339 Attention: Gregory P. Youra
Lender:	The PrivateBank and Trust Company 120 South LaSalle Street Chicago, Illinois 60603 Attention: Amy K. Hallberg
With a copy to:	Seyfarth Shaw LLP 131 South Dearborn Street Suite 2400 Chicago, Illinois 60603 Attention: Alvin L. Kruse

or such other address as a party may designate by notice duly given in accordance with this Section to the other parties. A Notice to a party shall be effective when delivered to such party's Notice Address by any means, including, without limitation, personal delivery by the party giving the Notice, delivery by United States regular, certified or registered mail, or delivery by a commercial courier or delivery service. If the Notice Address of a party includes a facsimile number or electronic mail address, Notice given by facsimile or electronic mail shall be effective when delivered at such facsimile number or email address. If delivery of a Notice is refused, it shall be deemed to have been delivered at the time of such refusal of delivery. The party giving a Notice shall have the burden of establishing the fact and date of delivery or refusal of delivery of a Notice.

24. **Litigation Provisions.**

**(a) THE GUARANTOR CONSENTS AND SUBMITS TO THE JURISDICTION OF ANY STATE OR FEDERAL COURT LOCATED IN CHICAGO, ILLINOIS, AND OF ANY STATE OR FEDERAL COURT LOCATED OR HAVING JURISDICTION IN THE COUNTY IN WHICH ANY FACILITY IS LOCATED, IN WHICH ANY LEGAL PROCEEDING MAY BE COMMENCED OR PENDING RELATING IN ANY MANNER TO THIS GUARANTY.**

(b) THE GUARANTOR AGREES THAT ANY LEGAL PROCEEDING RELATING TO THIS GUARANTY MAY BE BROUGHT AGAINST SUCH GUARANTOR IN ANY STATE OR FEDERAL COURT LOCATED IN CHICAGO, ILLINOIS, OR ANY STATE OR FEDERAL COURT LOCATED OR HAVING JURISDICTION IN THE COUNTY IN WHICH ANY FACILITY IS LOCATED. EACH GUARANTOR WAIVES ANY OBJECTION TO VENUE IN ANY SUCH COURT AND WAIVES ANY RIGHT THE GUARANTOR MAY HAVE TO TRANSFER OR CHANGE THE VENUE FROM ANY SUCH COURT.

(c) THE GUARANTOR AGREES THAT THE GUARANTOR WILL NOT COMMENCE ANY LEGAL PROCEEDING AGAINST THE LENDER RELATING IN ANY MANNER TO THIS GUARANTY IN ANY COURT OTHER THAN A STATE OR FEDERAL COURT LOCATED IN CHICAGO, ILLINOIS, OR IF A LEGAL PROCEEDING IS COMMENCED BY THE LENDER AGAINST THE GUARANTOR IN A COURT IN ANOTHER LOCATION, BY WAY OF A COUNTERCLAIM IN SUCH LEGAL PROCEEDING.

(d) THE GUARANTOR HEREBY WAIVES TRIAL BY JURY IN ANY LEGAL PROCEEDING RELATING TO THIS GUARANTY.

[SIGNATURE PAGE(S) AND EXHIBIT(S),  
IF ANY, FOLLOW THIS PAGE]

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IN WITNESS WHEREOF, the Guarantor has executed this Guaranty as of the date first above written.

**ADCARE HEALTH SYSTEMS, INC.**

By /s/ Christopher F. Brogdon

Christopher F. Brogdon, Vice Chairman and  
Chief Acquisition Officer

- AdCare Portfolio Operator Loan Guaranty -

- Signature Page -

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PAYOFF CONFIRMATION LETTER

September 20, 2012

ADK Georgia, LLC, as Borrower Representative  
5057 Troy Road  
Springfield, Ohio 45502  
Attention: Mr. Martin Brew

The PrivateBank and Trust Company  
120 South LaSalle Street  
Chicago, Illinois 60603  
Attention: Amy K. Hallberg

Gregory D. Hughes  
Hughes White Kralicek  
2110 Powers Ferry Rd., Suite 440  
Atlanta, Georgia 30339

Ladies and Gentlemen:

Reference is made to (i) that certain Credit Agreement dated October 29, 2010 (as at any time amended, restated, supplemented or otherwise modified, the "Credit Agreement") by and among Gemino Healthcare Finance, LLC (together with its successors and assigns, "Lender"), ADK Georgia, LLC, ADK Powder Springs Operator, LLC, ADK Lumber City Operator, LLC, ADK Jeffersonville Operator, LLC, ADK LaGrange Operator, LLC, ADK Thomasville Operator, LLC, ADK Oceanside Operator, LLC, ADK Savannah Beach Operator, LLC, ADK Thunderbolt Operator, LLC, Attalla Nursing ADK, LLC, Mountain Trace Nursing ADK, LLC, Mt. Kenn Nursing, LLC, Erin Nursing, LLC and CP Nursing, LLC (collectively, "Borrowers" and each individually, a "Borrower"); (ii) that certain Guaranty Agreement dated October 29, 2010, by AdCare Health Systems, Inc. ("AdCare Health Systems") in favor of Lender with respect to the indebtedness and obligations owing by Borrowers to Lender (as at any time amended, restated, supplemented or otherwise modified, the "AdCare Health Systems Guaranty"); (iii) that certain Guaranty Agreement dated November 29, 2011, by AdCare Operations, LLC ("Operations"; together with AdCare Health Systems, collectively, "Guarantors" and each individually, a "Guarantor") in favor of Lender with respect to the indebtedness and obligations owing by Borrowers to Lender (as at any time amended, restated, supplemented or otherwise modified, the "Operations Guaranty"; together with the AdCare Health Systems Guaranty, collectively, the "Guarantees" and each individually, a "Guaranty"); and (iv) that certain Guaranty Agreement dated April 27, 2011, by Borrowers in favor of Lender with respect to the indebtedness and obligations owing by ADK Bonterra/Parkview, LLC to Lender (as at any time amended, restated, supplemented or otherwise modified, the "Bonterra/Parkview Guaranty").

Lender has been informed that Borrowers intend to terminate the Credit Agreement on September 20, 2012 (the "Termination Date") and to satisfy in full all loans and other non-contingent obligations of Borrowers to Lender outstanding on the Termination Date (collectively, the "Absolute

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Obligations"), including, but not limited to, all principal, interest, legal fees and other charges outstanding or payable under the Credit Agreement, with funds made available to Lender from The PrivateBank and Trust Company, an Illinois banking corporation ("New Lender"), and wired on behalf of New Lender by Gregory D. Hughes, as escrow agent ("Escrow Agent"). Borrowers and Escrow

Agent have advised Lender that satisfaction of the Absolute Obligations will be effected by the wire transfer to Lender from Escrow Agent of immediately available funds in an amount sufficient to satisfy the full amount of the Absolute Obligations on the Termination Date. Capitalized terms used herein, unless otherwise defined herein, shall have the meanings ascribed to such terms in the Credit Agreement.

To the end of facilitating Escrow Agent's wire transfer of funds to satisfy the Absolute Obligations, please be advised that the total Absolute Obligations on the date hereof consist of the following:

1.	Principal Balance	\$	4,222,891.25
2.	Accrued Interest	\$	19,730.85
3.	Prepayment fees or termination charges	\$	0.00
4.	Actual legal fees and expenses through, and estimated legal fees and expenses after, the Termination Date	\$	18,176.50
5.	Other	\$	11,862.05
	<b>TOTAL ABSOLUTE OBLIGATIONS</b>	<b>\$</b>	<b>4,272,660.65</b>

The amount of the Total Absolute Obligations shown above is sometimes referred to herein as the "TAO Amount." Lender agrees that all of its Liens and security interests in the assets of Borrowers shall terminate and Borrowers shall be released (except as expressly set forth herein) if, at or before 4:00 p.m. (Atlanta, Georgia time) on the Termination Date, Lender receives (a) confirmation from the bank identified below that such bank has received a wire transfer from Escrow Agent of immediately available federal funds, for the account of Lender, in the TAO Amount, and (b) a copy of this letter, duly executed by Borrowers, Guarantors, New Lender and Escrow Agent. Lender further agrees that if the conditions precedent set forth in this paragraph are satisfied on or before the Termination Date, Lender agrees to waive the applicable termination fees that would otherwise be owing by Borrowers under Section 2.03(c) of the Credit Agreement.

Escrow Agent agrees that it has received recordable copies of the UCC financing statement amendments terminating those recorded UCC financing statements listed on Exhibit A attached hereto (the "ADK Financing Statements") to be held in escrow and to be released to New Lender only after Escrow Agent has received written instruction to do so (electronic mail shall be considered a writing for purposes of this requirement) from Jeff Joslin of Lender or Doug Nail or Jason Loring of Parker, Hudson, Rainer & Dobbs LLP, which instruction shall not be given prior to Lender's confirmation that it has received a wire from Escrow Agent in the TAO Amount. Escrow Agent

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agrees to all obligations set forth herein and acknowledges its agreement to act in accordance with the terms hereof.

No termination of Lender's Liens and security interests in Borrower's assets shall operate to terminate or impair Borrowers' indemnifications of Lender under the Credit Agreement or otherwise, which shall survive such termination.

The wire transfer of funds by Escrow Agent to Lender to satisfy the Absolute Obligations is as follows:

Citizens Bank of Pennsylvania  
Philadelphia, Pennsylvania  
For the Account of Gemino Healthcare Finance, LLC  
Account No. 6218883284  
ABA Routing No.: 036076150  
Reference: ADK Georgia, LLC

By their acceptance hereof, Borrowers acknowledges and agrees that (a) Lender reserves all of its rights with respect to each automated clearinghouse transfer (“ACH”) and each check and other instrument or payment item received by Lender from Borrowers or any of Borrowers’ account debtors prior to full payment of the Absolute Obligations as contemplated hereby (such checks, instruments or other payment items being collectively called “Checks”); (b) Lender has credited to Borrowers’ account the amount of all such ACH transfers and the face amount of all such Checks, but Lender has not yet received full and final credit or payment therefor; and (c) Borrowers shall reimburse and pay to Lender, promptly after Lender’s demand therefor made at any time within sixty (60) days after the date hereof, in immediately available funds, the amount of any ACH transfer and the full face amount of any Check that is hereafter dishonored or returned to Lender or remains unpaid for any reason plus any bank charges and all other reasonable costs incurred by Lender that arise as a result of any such dishonor or return.

**Each Borrower, on behalf of itself and on behalf of all those entities claiming by, through, or under it, together with their successors and assigns, and each Guarantor, on behalf of itself and on behalf of all those entities claiming by, through, or under it, together with their successors and assigns (collectively referred to as the “Company Releasers”), for good and valuable consideration, including, without limitation, the execution of this letter agreement by Lender and Lender’s release of its Liens and security interests as set forth herein, does hereby unconditionally remise, release, acquit and forever discharge Lender, Lender’s past and present officers, directors, shareholders, employees, agents, attorneys, parent corporations, subsidiaries, affiliates, successors and assigns, and the heirs, executors, trustees, administrators, successors, and assigns of any such persons and entities (collectively referred to as the “Lender Releasees”), of and from any and all manner of actions, causes of action, suits, claims, counterclaims, liabilities, obligations, defenses, and demands whatsoever (if any), at law or in equity, or disputed or undisputed, which any of the Company Releasers ever had, now has, or hereafter can, shall, or may claim to have against any of the Lender Releasees for or by reason of any cause, matter, or thing whatsoever, arising from the beginning of the world to the date of execution of this letter agreement.**

After receipt by Lender of a copy of this letter agreement, duly executed by each party hereto, and Lender’s confirmation that it has received a wire from Escrow Agent in the TAO

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Amount, Lender (a) agrees to provide written authorization to Escrow Agent to release the ADK Financing Statements from escrow to New Lender for filing as set forth herein, (b) agrees to execute and deliver all other terminations and satisfactions necessary or reasonably requested by Borrowers or Guarantors to release any and all Liens, security interests, assignments, pledges and other interests Lender may have in the assets of Borrowers or Guarantors, and (c) agrees to execute and deliver a Release of Guarantees with respect to the Guarantees and the Bonterra/Parkview Guaranty in the form of Exhibit B attached hereto. All costs and expenses of any releases executed or recorded in connection with this letter agreement shall be borne solely by Borrowers.

This letter agreement shall be binding upon and inure to the benefit of the parties hereto and their respective successors and assigns and may be executed in any number of counterparts, all of which, when taken together, shall be deemed one and the same agreement. Any manually executed counterpart of this letter agreement delivered by facsimile or other electronic transmission shall be deemed an original counterpart hereof.

*[Remainder of page intentionally left blank.]*

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When accepted by Borrowers, Guarantors, New Lender and Escrow Agent, the foregoing shall constitute an agreement made in, and governed by the internal laws of the Commonwealth of Pennsylvania.

Very truly yours,

**GEMINO HEALTHCARE FINANCE, LLC**  
("Lender")

By: /s/ Jeffrey M. Joslin

**Jeffrey M. Joslin**, Senior Portfolio  
Manager

The above and foregoing is acknowledged, accepted and agreed to:

**BORROWERS:**

**ADK GEORGIA, LLC**  
**ADK POWDER SPRINGS OPERATOR, LLC**  
**ADK LUMBER CITY OPERATOR, LLC**  
**ADK JEFFERSONVILLE OPERATOR, LLC**  
**ADK LAGRANGE OPERATOR, LLC**  
**ADK THOMASVILLE OPERATOR, LLC**  
**ADK OCEANSIDE OPERATOR, LLC**  
**ADK SAVANNAH BEACH OPERATOR, LLC**  
**ADK THUNDERBOLT OPERATOR, LLC**  
**ATTALLA NURSING ADK, LLC**  
**MOUNTAIN TRACE NURSING ADK, LLC**  
**MT. KENN NURSING, LLC**  
**ERIN NURSING, LLC**  
**CP NURSING, LLC**

By: /s/ Martin Brew

**Martin Brew**, Chief Financial Officer

**GUARANTORS:**

**ADCARE HEALTH SYSTEMS, INC.**

By: /s/ Martin Brew

**Martin Brew**, Chief Financial Officer

*[Continued on following page.]*

Payoff Letter

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**ADCARE OPERATIONS, LLC**

By: /s/ Martin Brew

**Martin Brew**, Chief Financial Officer

**NEW LENDER:**

**THE PRIVATE BANK AND TRUST COMPANY**

By: /s/ Amy K. Hallberg

**Amy K. Hallberg**, Managing Director

**ESCROW AGENT:**

/s/ Gregory D. Hughes

**Gregory D. Hughes**

Payoff Letter

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**RELEASE OF GUARANTEES**

By its signature below, Gemino Healthcare Finance, LLC (together with its successors and assigns, "Lender"), hereby (i) releases each of ADK Georgia, LLC, ADK Powder Springs Operator, LLC, ADK Lumber City Operator, LLC, ADK Jeffersonville Operator, LLC, ADK LaGrange Operator, LLC, ADK Thomasville Operator, LLC, ADK Oceanside Operator, LLC, ADK Savannah Beach Operator, LLC, ADK Thunderbolt Operator, LLC, Attalla Nursing ADK, LLC, Mountain Trace Nursing ADK, LLC, Mt. Kenn Nursing, LLC, Erin Nursing, LLC and CP Nursing, LLC (collectively, "Bonterra/Parkview Guarantors"), from that certain Guaranty Agreement dated April 27, 2011, by Bonterra/Parkview Guarantors in favor of Lender (as at any time amended, restated, supplemented or otherwise modified, the "Bonterra/Parkview Guaranty") with respect to the indebtedness and obligations owing by ADK Bonterra/Parkview, LLC ("Borrower"), to Lender, (ii) releases AdCare Health Systems, Inc. (collectively, "AdCare Health Systems") from that certain Guaranty Agreement dated October 29, 2010, by AdCare Health Systems in favor of Lender (as at any time amended, restated, supplemented or otherwise modified, the "AdCare Health Systems Guaranty") with respect to the indebtedness and obligations owing by Bonterra/Parkview Guarantors to Lender, (iii) releases AdCare Operations, LLC ("Operations"; together with Bonterra/Parkview Guarantors and AdCare Health Systems, collectively, "Guarantors") from that certain Guaranty Agreement dated November 29, 2011, by Operations in favor of Lender (as at any time amended, restated, supplemented or otherwise modified, the "Operations Guaranty"; together with the Bonterra/Parkview Guaranty and the AdCare Health Systems Guaranty, collectively, the "Guarantees" and each individually, a "Guaranty") with respect to the indebtedness and obligations owing by Bonterra/Parkview Guarantors to Lender, and (iv) acknowledges and agrees that, from and after the date hereof, Guarantors shall have no liability or obligations under their respective Guaranty; provided, however, that, nothing in this Release of Guarantees (this "Release") shall limit or otherwise affect any provision contained in any Guaranty which, by its express terms, survives the termination of the such Guaranty. Each Guarantor hereby acknowledges and affirms all such surviving obligations under its applicable Guaranty.

This Release may be executed in any number of counterparts and by different parties to this Release on separate counterparts, each of which, when so executed, shall be deemed an original, but all such counterparts shall constitute one and the same agreement. Any manually executed signature delivered by a party by facsimile or other electronic transmission shall be deemed to be an original signature hereto.

This Release is being executed in connection with that certain Payoff Confirmation Letter dated on or about the date hereof among Guarantors, Lender and the other parties thereto. Each capitalized term used herein, unless otherwise defined herein, shall have the meaning ascribed to such term in that certain Credit Agreement dated October 29, 2010, as at any time amended, restated, supplemented or otherwise modified. Except as modified hereby, the terms and provisions of the Loan Documents remain unchanged and in full force and effect. Except as expressly provided herein, this Release shall not constitute an amendment, waiver, consent or release with respect to any provision of the Loan Documents, a waiver of any Default or Unmatured Event of Default thereunder, or a waiver or release of any of Lender's rights and remedies (all of which are hereby reserved).

**To induce Lender to enter into this Release, each Guarantor hereby releases, acquits and forever discharges Lender, and all officers, directors, agents, employees, successors and assigns of Lender, from any and all liabilities, claims, demands, actions or causes of action of any kind or nature (should any exist or arise), whether absolute or contingent, disputed or**

**undisputed, at law or in equity, or known or unknown, that either Guarantor now has or ever had against Lender arising under or in connection with either Guaranty or otherwise. Each Guarantor represents and warrants to Lender that such Guarantor has not transferred or assigned to any person or entity any claim that such Guarantor ever had or claimed to have against Lender.**

[Remainder of page intentionally left blank; signatures begin on following page.]

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IN WITNESS WHEREOF, Lender has caused this Release to be duly executed and delivered by its duly authorized officer, and Guarantors and Borrower have executed and delivered this Release, each on September , 2012.

LENDER:

**GEMINO HEALTHCARE FINANCE, LLC**

By: /s/ Jeffrey M. Joslin

**Jeffrey M. Joslin**, Senior Portfolio Manager

[Signatures continued on following page.]

Release of Guarantees

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Acknowledged and agreed to:

GUARANTORS:

**ADK GEORGIA, LLC**

**ADK POWDER SPRINGS OPERATOR, LLC**

**ADK LUMBER CITY OPERATOR, LLC**

**ADK JEFFERSONVILLE OPERATOR, LLC**

**ADK LAGRANGE OPERATOR, LLC**

**ADK THOMASVILLE OPERATOR, LLC**

**ADK OCEANSIDE OPERATOR, LLC**

**ADK SAVANNAH BEACH OPERATOR, LLC**

**ADK THUNDERBOLT OPERATOR, LLC**

**ATTALLA NURSING ADK, LLC**

**MOUNTAIN TRACE NURSING ADK, LLC**

**MT. KENN NURSING, LLC**

**ERIN NURSING, LLC**

**CP NURSING, LLC**

By: /s/ Martin Brew

**Martin Brew**, Chief Financial Officer

**ADCARE HEALTH SYSTEMS, INC.**

By: /s/ Martin Brew

**Martin Brew**, Chief Financial Officer

**ADCARE OPERATIONS, LLC**

By: /s/ Martin Brew

**Martin Brew**, Chief Financial Officer

**BORROWER:**

**ADK BONTERRA/PARKVIEW, LLC**

By: /s/ Martin Brew

**Martin Brew**, Chief Financial Officer

Release of Guarantees

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**SECOND AMENDMENT TO CREDIT AGREEMENT**

THIS SECOND AMENDMENT TO CREDIT AGREEMENT (this "Amendment") is made and entered into this 20th day of September, 2012, by and between **ADK BONTERRA/PARKVIEW, LLC**, a Georgia limited liability company (hereinafter referred to as "Borrower"), with its chief executive office at Two Buckhead Plaza, 3050 Peachtree Road NW, Suite 355, Atlanta, Georgia 30305, and **GEMINO HEALTHCARE FINANCE, LLC**, a Delaware limited liability company (hereinafter referred to as "Lender") with an office at One International Plaza, Suite 220, Philadelphia, Pennsylvania 19113.

**Recitals:**

Lender and Borrower are parties to a certain Credit Agreement dated April 27, 2011 (as at any time amended, restated, modified or supplemented, the "Credit Agreement") pursuant to which Lender has made certain revolving credit loans to Borrower.

The parties desire to amend the Credit Agreement as hereinafter set forth.

NOW, THEREFORE, for TEN DOLLARS (\$10.00) in hand paid and other good and valuable consideration, the receipt and sufficiency of which are hereby severally acknowledged, the parties hereto, intending to be legally bound hereby, agree as follows:

1. **Definitions.** All capitalized terms used in this Amendment, unless otherwise defined herein, shall have the meanings ascribed to such terms in the Credit Agreement.

2. **Amendments to Credit Agreement.** The Credit Agreement is hereby amended as follows:

(a) By deleting the reference to "October 29, 2013" in Section 2.01(d) of the Credit Agreement and by substituting "January 31, 2014" in lieu thereof.

(b) By deleting Sections 6.06(a) and (b) of the Credit Agreement in their respective entireties and by substituting in lieu thereof the following:

(a) **Minimum Fixed Charge Coverage Ratio.** Borrowers shall cause ADK to maintain at all times a Fixed Charge Coverage Ratio measured quarterly at the end of the fiscal quarter ending September 30, 2012, of at least 1.00 to 1.0, and at the end of each fiscal quarter thereafter, of at least 1.10:1.

(b) **Maximum Loan Turn Days.** Borrowers shall maintain at all times a Maximum Loan Turn Days, measured quarterly at the end of the fiscal quarter ending June 30, 2011 and each fiscal quarter thereafter, of not greater than 40 days.

(c) By deleting the last sentence of Section 7.08 of the Credit Agreement in its entirety and by substituting in lieu thereof the following:

In addition, unless consented to by Lender, or if a replacement acceptable to Lender is employed within ninety (90) days of any terminations, Boyd Gentry and Martin Brew shall continue as senior management of ADK actively involved in the day-to-day management of ADK and Christopher Brogdon and AdCare Management shall continue as senior management of Borrowers actively involved in the day-to-day management of such Borrowers.

(d) By deleting Sections 8.01(x), (y) and (z) of the Credit Agreement and by substituting in lieu thereof the following:

(x) Transition Services Agreement. the Transition Services Agreement is terminated prior to completion of the transition of operations with respect to the Healthcare Facilities and unconditional written approval of the CHOW; or

(y) Bonterra/Parkview Lease Default. Any Bonterra/Parkview Lease Default shall occur.

(e) By deleting Section 9.27 of the Credit Agreement in its entirety.

(f) By deleting the address for notices set forth on the first signature page to the Credit Agreement and by substituting in lieu thereof the following:

Address for notices to Borrowers:

Two Buckhead Plaza  
3050 Peachtree Road NW  
Suite 355  
Atlanta, GA 30305  
Attn: Mr. Martin Brew  
Fax: (404) 795-0604

(g) By adding the following definition of “Medicaid Pending” to Annex I to the Credit Agreement in appropriate alphabetical order:

“Medicaid Pending” means an amount that will be billed to Medicaid for services rendered to patients that are expected to qualify for such state Medicaid program, but which patients are at the time in question in the process of completing the necessary paperwork and have not yet been officially accepted by such state as eligible Medicaid patients.

(h) By deleting the definitions of “Affiliated Credit Agreement” and “Non-Bonterra/Parkview Borrowers” set forth in Annex I to the Credit Agreement.

(i) By deleting the definitions of “Applicable LIBOR Floor”, “Applicable Margin”, “EBITDA”, “Fixed Charge Coverage Ratio”, “Guarantors” and “Maximum Loan Turn Days” set forth in Annex I to the Credit Agreement and by substituting in lieu thereof the following, respectively:

“Applicable LIBOR Floor” means a percentage equal to two and one-half percent (2.5%).

“Applicable Margin” means a percentage equal to four and three-quarters percent (4.75%).

“EBITDA” means the sum of net income plus interest expense, plus taxes, plus depreciation and amortization (but excluding non-cash stock compensation expense, acquisition loss or gain and derivative loss or gain, if any).

“Fixed Charge Coverage Ratio” means the ratio of (a) EBITDA, to (b) the sum of (i) interest expense paid, plus (ii) the current portion of any long-term Indebtedness excluding

(A) payments with respect to that certain Promissory Note made by ADK and ADK Georgia, LLC, a Georgia limited liability company, on July 31, 2010 in the principal amount of \$500,000 in favor of Triad Health Management of Georgia II, LLC, a Georgia limited liability company, to the extent such payments are not made, and (B) payments with respect to certain temporary bridge financing from time to time obtained by ADK or certain of its Subsidiaries, but only to the extent and only for so as Lender agrees in its sole discretion that such payments may be excluded from the calculation of the Fixed Charge Coverage Ratio pursuant to this clause (B), plus (iii) the current portion of obligations under capitalized leases, plus (iv) cash taxes paid, plus (v) cash Distributions, plus (vi) any unfinanced capital expenditures other than unfinanced capital expenditures made during 2012, all as determined for ADK on a consolidated basis, in accordance with GAAP consistently applied, on a rolling four quarter basis; provided, however, that such calculation as of the fiscal quarter ending September 30, 2012 shall be for the three (3) most recent fiscal quarterly periods ending on such date on a cumulative, annualized basis.

“Guarantors” means ADK and each other Person who guarantees payment or performance of any Obligations.

“Maximum Loan Turn Days” means, as of any date of determination, (i) the result of (a) the average daily outstanding balance of the Revolving Loans during the immediately preceding three (3) months, divided by (b) the average monthly Collections in the Commercial Lockbox and Government Lockbox for the immediately preceding three (3) months, multiplied by (ii) 30.

(j) By deleting clause (h) of the definition of “Eligible Accounts” set forth in Annex I to the Credit Agreement and by substituting in lieu thereof the following:

(h) which is not outstanding more than one hundred eighty (180) days past the Billing Date; provided, however that in no event may the Account be outstanding more than one hundred eighty (180) days past the date the corresponding services and/or goods were provided;

(k) By deleting clauses (l), (m) and (n) of the definition of “Eligible Accounts” set forth in Annex I to the Credit Agreement and by substituting in lieu thereof the following, respectively:

(l) which has a Billing Date on or after November 1, 2011;

(m) to the extent such Account is Medicaid Pending, it is not outstanding more than ninety (90) days past the date the corresponding services and/or goods were provided; and

(n) which complies with such other criteria and requirements as may be specified from time to time by Lender in its reasonable discretion.

**3. Ratification and Reaffirmation.** Borrower hereby ratifies and reaffirms the Obligations, each of the Loan Documents and all of Borrower’s covenants, duties, indebtedness and liabilities under the Loan Documents.

**4. Acknowledgments and Stipulations.** Borrower acknowledges and stipulates that the Credit Agreement and the other Loan Documents executed by Borrower are legal, valid and binding obligations of Borrower that are enforceable against Borrower in accordance with the terms thereof; all of the Obligations are

owing and payable without defense, offset or counterclaim (and to the extent there exists any such defense, offset or counterclaim on the date hereof, the same is hereby waived by Borrower); the security interests and liens granted by Borrower in favor of Lender are duly

perfected, first priority security interests and liens; and the unpaid principal amount of the Loans on and as of September 20, 2012, totaled \$4,222,891.25.

5. **Representations and Warranties.** Borrower represents and warrants to Lender, to induce Lender to enter into this Amendment, that no Event of Default or Unmatured Event of Default exists on the date hereof; the execution, delivery and performance of this Amendment have been duly authorized by all requisite company action on the part of Borrower and this Amendment has been duly executed and delivered by Borrower; and all of the representations and warranties made by Borrower in the Credit Agreement are true and correct on and as of the date hereof.

6. **Reference to Credit Agreement.** Upon the effectiveness of this Amendment, each reference in the Credit Agreement to “this Agreement,” “hereunder,” or words of like import shall mean and be a reference to the Credit Agreement, as amended by this Amendment.

7. **Breach of Amendment.** This Amendment shall be part of the Credit Agreement and a breach of any representation, warranty or covenant herein shall constitute an Event of Default.

8. **Conditions Precedent.** The effectiveness of the amendments contained in Section 2 hereof are subject to the satisfaction of each of the following conditions precedent, in form and substance satisfactory to Lender, unless satisfaction thereof is specifically waived in writing by Lender:

- (a) Lender shall have received a counterpart of this Amendment duly executed by Borrower; and
- (b) Lender shall have received a Consent and Reaffirmation to this Amendment duly executed by ADK.

9. **Amendment Fee; Expenses of Lender.** In consideration of Lender’s willingness to enter into this Amendment, Borrower agrees to pay (i) to Lender, a nonrefundable amendment fee in the amount of \$57,500 (the “Amendment Fee”), in immediately available funds on the date hereof, which shall be fully earned on such date and non-refundable when paid, and Borrower irrevocably authorizes Lender to make a Revolving Loan to Borrower in the amount of such Amendment Fee and to disburse the proceeds of such Revolving Loan in payment of such Amendment Fee, and (ii) **on demand**, all costs and expenses incurred by Lender in connection with the preparation, negotiation and execution of this Amendment and any other Loan Documents executed pursuant hereto and any and all amendments, modifications, and supplements thereto, including, without limitation, the costs and fees of Lender’s legal counsel and any taxes or expenses associated with or incurred in connection with any instrument or agreement referred to herein or contemplated hereby.

10. **Governing Law.** This Amendment shall be governed by and construed in accordance with the internal laws of the Commonwealth of Pennsylvania.

11. **Successors and Assigns.** This Amendment shall be binding upon and inure to the benefit of the parties hereto and their respective successors and assigns.

12. **No Novation, etc.** Except as otherwise expressly provided in this Amendment, nothing herein shall be deemed to amend or modify any provision of the Credit Agreement or any of the other Loan Documents, each of which shall remain in full force and effect. This Amendment is not intended to be, nor

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shall it be construed to create, a novation or accord and satisfaction, and the Credit Agreement as herein modified shall continue in full force and effect.

13. **Counterparts; Electronic Signatures.** This Amendment may be executed in any number of counterparts and by different parties to this Amendment on separate counterparts, each of which, when so executed, shall be deemed an original, but all such counterparts shall constitute one and the same agreement. Any manually executed signature page to this Amendment delivered by a party by facsimile or other electronic transmission shall be deemed to be an original signature hereto.

14. **Further Assurances.** Borrower agrees to take such further actions as Lender shall reasonably request from time to time in connection herewith to evidence or give effect to the amendments set forth herein or any of the transactions contemplated hereby.

15. **Section Titles.** Section titles and references used in this Amendment shall be without substantive meaning or content of any kind whatsoever and are not a part of the agreements among the parties hereto.

16. **Release of Claims.** To induce Lender to enter into this Amendment, Borrower hereby releases, acquits and forever discharges Lender, and all officers, directors, agents, employees, successors and assigns of Lender, from any and all liabilities, claims, demands, actions or causes of action of any kind or nature (if there be any), whether absolute or contingent, disputed or undisputed, at law or in equity, or known or unknown, that Borrower now has or ever had against Lender arising under or in connection with any of the Loan Documents or otherwise. Borrower represents and warrants to Lender that Borrower has not transferred or assigned to any Person any claim that Borrower ever had or claimed to have against Lender.

17. **Waiver of Jury Trial.** To the fullest extent permitted by applicable law, the parties hereto each hereby waives the right to trial by jury in any action, suit, counterclaim or proceeding arising out of or related to this Amendment.

[Remainder of page intentionally left blank; signatures begin on following page.]

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IN WITNESS WHEREOF, the parties hereto have caused this Amendment to be duly executed and delivered by their respective duly authorized officers on the date first written above.

**BORROWER:**

**ADK BONTERRA/PARKVIEW, LLC**

By: /s/ Martin Brew

**Martin Brew**, Chief Financial Officer

[Signatures continued on following page.]

Second Amendment to Credit Agreement

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**LENDER:**

**GEMINO HEALTHCARE FINANCE, LLC**

By: /s/ Jeffrey M. Joslin

**Jeffrey M. Joslin**, Senior Portfolio Manager



**CONSENT AND REAFFIRMATION**

Each of the undersigned guarantors of the Obligations of Borrower at any time owing to Lender hereby (i) acknowledges receipt of a copy of the foregoing Second Amendment to Credit Agreement; (ii) consents to Borrower's execution and delivery thereof and of the other documents, instruments or agreements Borrower agrees to execute and deliver pursuant thereto; (iii) agrees to be bound thereby; and (iv) affirms that nothing contained therein shall modify in any respect whatsoever its guaranty of the Obligations and reaffirms that such guaranty is and shall remain in full force and effect.

IN WITNESS WHEREOF, each of the undersigned has executed this Consent and Reaffirmation as of the date of such Second Amendment to Credit Agreement.

**ADCARE HEALTH SYSTEMS, INC.**

By: /s/ Martin Brew

**Martin Brew**, Chief Financial Officer

TEMPORARY EXTENSION AGREEMENT

Date: August 29, 2012

Loan No.: 400211400

THIS EXTENSION OF THE PROMISSORY NOTE is made and entered into this 29<sup>th</sup> day of August, 2012, by and between APH & R PROPERTY HOLDINGS, LLC. (hereinafter referred to as "Borrower") and METRO CITY BANK, (hereinafter referred to as "Lender").

WITNESSETH:

WHEREAS, Borrower did execute that certain Note dated April 30, 2012, in favor of Lender in the original principal amount of THREE MILLION FOUR HUNDRED TWENTY FIVE THOUSAND AND 0/100 Dollars (\$3,425,000.00). The Note being secured by a certain Deed to Secure Debt of even date therewith; and

WHEREAS, Borrower and Lender desire to modify the Note as hereinafter set forth.

NOW, THEREFORE, for good and valuable consideration, the receipt and sufficiency of which are hereby acknowledged, the parties hereto agree as follows:

- 1. The borrower and the lender have agreed to extend the term of the Note from September 1, 2012, the original maturity date, to December 1, 2012, the extended maturity date.
- 2. Monthly payments as set forth in the Note shall be extended and continue on the 1<sup>st</sup> day of each month until the maturity date, at which time all outstanding principal and interest shall be due and payable.
- 3. All other terms and conditions of the Note shall remain in full force and effect, except as otherwise expressly modified herein.
- 4. This extension of the term on the Note shall bind and inure to the benefit of the parties hereto and their respective heirs, successors, representatives and assigns.

IN WITNESS WHEREOF, the parties hereto have hereunto set their hands and seals as of the day and year first above written.

**BORROWER:**

APH & R PROPERTY HOLDINGS, LLC

**LENDER:**

METRO CITY BANK

By: /s/ Chris F. Brogdon  
Chris F. Brogdon, Manager

By: /s/ Alison Kim  
Alison Kim, Lending Officer

**CERTIFICATIONS**

I, Boyd P. Gentry, certify that:

1. I have reviewed this quarterly report on Form 10-Q of AdCare Health Systems, Inc.;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15 d-15(f)) for the registrant and have:
  - a. Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
  - b. Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, 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;
  - c. Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
  - d. Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
  - a. All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
  - b. Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: November 13, 2012

By /s/Boyd P. Gentry  
Chief Executive Officer

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**CERTIFICATIONS**

I, Martin D. Brew, certify that:

1. I have reviewed this quarterly report on Form 10-Q of AdCare Health Systems, Inc.;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15 d-15(f)) for the registrant and have:
  - a. Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
  - b. Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, 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;
  - c. Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
  - d. Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
  - a. All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
  - b. Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: November 13, 2012

By /s/Martin D. Brew  
Chief Financial Officer

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CERTIFICATION PURSUANT TO  
18 U.S.C. SECTION 1350,  
AS ADDED BY  
SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002

In connection with the Quarterly Report of AdCare Health Systems, Inc. (the "Company") on Form 10-Q for the period ended September 30, 2012, as filed with the Securities and Exchange Commission (the "Report"), I, Boyd P. Gentry, Chief Executive Officer of the Company, certify, pursuant to 18 U.S.C. § 1350, as added by § 906 of the Sarbanes-Oxley Act of 2002, that:

1. The Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934; and
2. To my knowledge, the information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company as of and for the period covered by the Report.

Date: November 13, 2012

By: /s/Boyd P. Gentry

Chief Executive Officer

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CERTIFICATION PURSUANT TO  
18 U.S.C. SECTION 1350,  
AS ADDED BY  
SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002

In connection with the Quarterly Report of AdCare Health Systems, Inc. (the "Company") on Form 10-Q for the period ended September 30, 2012, as filed with the Securities and Exchange Commission (the "Report"), I, Martin D. Brew, Chief Financial Officer of the Company, certify, pursuant to 18 U.S.C. § 1350, as added by § 906 of the Sarbanes-Oxley Act of 2002, that:

1. The Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934; and
2. To my knowledge, the information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company as of and for the period covered by the Report.

Date: November 13, 2012

By: /s/Martin D. Brew  
Chief Financial Officer

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SEGMENTS (Details) (USD \$) In Thousands, unless otherwise specified	3 Months Ended		9 Months Ended	
	Sep. 30, 2012	Sep. 30, 2011	Sep. 30, 2012 item	Sep. 30, 2011 Dec. 31, 2011
<b>SEGMENTS</b>				
<u>Number of reportable segments</u>			3	
<b>SEGMENTS</b>				
<u>Net revenues</u>	\$ 61,770	\$ 40,522	\$ 166,947	\$ 105,908
<u>Cost of services</u>	49,164	32,637	131,514	84,916
<u>General and administrative</u>	4,328	3,267	13,188	9,358
<u>Facility rent expense</u>	2,080	1,937	6,196	5,787
<u>Depreciation and amortization</u>	2,112	836	5,370	2,188
<u>Salary retirement and continuation costs</u>	38		38	622
<u>Income from Operations</u>	4,048	1,845	10,641	3,037
<u>Total assets</u>	236,891	158,286	236,891	158,286 159,081
SNF				
<b>SEGMENTS</b>				
<u>Net revenues</u>	57,978	37,729	155,753	97,382
<u>Cost of services</u>	49,812	32,887	132,582	85,495
<u>Facility rent expense</u>	2,039	1,906	6,065	5,711
<u>Depreciation and amortization</u>	1,590	631	4,075	1,595
<u>Income from Operations</u>	4,537	2,305	13,031	4,581
<u>Total assets</u>	169,546	105,620	169,546	105,620
ALF				
<b>SEGMENTS</b>				
<u>Net revenues</u>	3,364	2,463	10,038	7,214
<u>Cost of services</u>	2,441	1,885	7,362	5,740
<u>Depreciation and amortization</u>	224	158	654	470
<u>Income from Operations</u>	699	420	2,022	1,004
<u>Total assets</u>	29,181	21,490	29,181	21,490
Corporate & Other				
<b>SEGMENTS</b>				
<u>Net revenues</u>	3,505	2,349	9,487	7,646
<u>Cost of services</u>	(12)	(116)	(99)	15
<u>General and administrative</u>	4,328	3,267	13,188	9,358
<u>Facility rent expense</u>	41	31	131	76
<u>Depreciation and amortization</u>	298	47	641	123
<u>Salary retirement and continuation costs</u>	38		38	622
<u>Income from Operations</u>	(1,188)	(880)	(4,412)	(2,548)
<u>Total assets</u>	38,164	31,176	38,164	31,176
Eliminations				
<b>SEGMENTS</b>				
<u>Net revenues</u>	(3,077)	(2,109)	(8,331)	(6,334)
<u>Cost of services</u>	\$ (3,077)	\$ (2,109)	\$ (8,331)	\$ (6,334)

**FAIR VALUE  
MEASUREMENTS (Details)  
(USD \$)**

**3 Months Ended      9 Months Ended  
Sep. 30,    Sep. 30,      Sep. 30,    Sep. 30,  
2012      2011      2012      2011**

**Reconciliation of the beginning and ending balances for assets and liabilities measured at fair value on a recurring basis using significant unobservable inputs**

<u>Total loss</u>	\$	\$	\$	\$
	2,105,000	(4,745,000)	1,342,000	(807,000)

Convertible debt issued in 2010

**Reconciliation of the beginning and ending balances for assets and liabilities measured at fair value on a recurring basis using significant unobservable inputs**

<u>Conversion price of convertible notes into common stock (in dollars per share)</u>	\$ 3.73		\$ 3.73
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Recurring basis | Level 3:

**FAIR VALUE MEASUREMENTS**

<u>Derivative Liability</u>	3,200,000		3,200,000
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**Reconciliation of the beginning and ending balances for assets and liabilities measured at fair value on a recurring basis using significant unobservable inputs**

<u>Beginning Balance</u>			1,900,000
<u>Total loss</u>			(1,300,000)
<u>Ending Balance</u>	3,200,000		3,200,000

Recurring basis | Total

**FAIR VALUE MEASUREMENTS**

<u>Derivative Liability</u>	\$		\$
	3,200,000		3,200,000

	1 Months Ended			0 Months Ended			3 Months Ended			1 Months Ended			9 Months Ended			1 Months Ended			3 Months Ended			
	Mar. 29, 2012	Apr. 02, 2012	Apr. 30, 2012	Mar. 31, 2012	Apr. 30, 2012	Jul. 02, 2012	Sep. 30, 2012	Jul. 02, 2012	Sep. 30, 2012	Sep. 30, 2012	Aug. 31, 2012	Jun. 02, 2012	Aug. 31, 2012	Mar. 31, 2012	Sep. 30, 2012	Feb. 29, 2012	Feb. 29, 2012	Sep. 30, 2012	Jul. 31, 2012	Jun. 30, 2012	Sep. 30, 2012	
	Cantone Management LLC Warrant	Strome Alpha Offshore Ltd. Warrant	Promissory note Asset Management LLC	Promissory note Asset Management LLC	Promissory note Strome Alpha Offshore Ltd.	Subordinated convertible debt	Subordinated convertible debt	Subordinated convertible debt Warrant	Placement Agent Subordinated convertible debt	Placement Agent Subordinated convertible debt Maximum	Vendor Warrant	Options	Options Members of management	Options Members of management	Options Members of management	Options vest in 2013 Christopher Brogdon, the Company's Vice Chairman	Options vest in 2014 Christopher Brogdon, the Company's Vice Chairman	Restricted Stock	Restricted Stock Subordinated convertible debt	Restricted Stock Placement Agent Subordinated convertible debt	Restricted Stock Directors item	
<b>STOCK BASED COMPENSATION (Details)</b>																						
<b>COMPENSATION (USD \$)</b>																						
<b>In Millions, except Share data, unless otherwise specified</b>																						
<b>SHARE-BASED COMPENSATION</b>																						
Granted (in shares)													248,850	461,160		52,500	105,000					
Exercise price (in dollars per share)													\$ 3.93	\$ 3.93		\$ 6.67	\$ 7.62					
Estimated fair value (in dollars per share)													\$ 1.55	\$ 1.34		\$ 1.19	\$ 1.03					
Vesting period															3 years							
Maximum number of shares of the company's stock that may be issued before amendment to the Plan												1,000,000										
Maximum number of shares of the company's stock that may be issued												2,000,000									283,500	
Debt issued			\$ 1.5	\$ 3.5	\$ 5.0	\$ 7.5																
Fixed interest rate (as a percent)							8.00%															
Number of shares that can be purchased upon exercise of warrant	315,000	328,125						105,000			15,750											
Exercise price (in dollars per share)	\$ 3.81	\$ 3.81						\$ 3.81			\$ 4.37											
Estimated fair value (in dollars per share)	\$ 0.64	\$ 0.64						\$ 0.49			\$ 0.89											
Amortization of deferred loan origination fees included in interest expense										(0.1)												
Deferred loan costs									0.2													
Period of restriction on restricted stock																			1 year		3 years	
Number of directors																				9		
Period of recognition of compensation expense																					3 years	
Compensation expense																						0.2
Unrecognized compensation expense																						\$ 0.7
<b>Shares</b>																						
Stock Dividend (in shares)																						
Granted (in shares)																						16,000
Vested (in shares)																						320,000 (336,000)
Weighted Avg. Grant Date Fair Value																						\$ 3.38
Stock Dividend (in dollars per share)																						\$ 3.38
Granted (in dollars per share)																						3.50
Vested (in dollars per share)																						\$ 3.36

**VARIABLE INTEREST  
ENTITIES (Tables)**

**9 Months Ended  
Sep. 30, 2012**

**VARIABLE INTEREST  
ENTITIES**

Summary of assets and liabilities of  
the variable interest entities  
included in the consolidated  
balance sheets

Riverchase Village Facility - Assets and Liabilities:

<u>(Amounts in 000s)</u>	<u>September 30, 2012</u>	<u>December 31, 2011</u>
Cash	\$ 10	\$ 16
Accounts receivable	7	10
Restricted investments	326	451
Property and equipment, net	5,993	5,999
Other assets	411	432
<b>Total assets</b>	<b>\$ 6,747</b>	<b>\$ 6,908</b>
Accounts payable	\$ 1,112	\$ 740
Accrued expenses	130	174
Current portion of notes payable	99	99
Notes payable, net of current portion	6,010	6,077
Noncontrolling interest	(604)	(182)
<b>Total liabilities</b>	<b>\$ 6,747</b>	<b>\$ 6,908</b>

Oklahoma Facilities - Assets and Liabilities:

<u>(Amounts in 000s)</u>	<u>September 30, 2012</u>	<u>December 31, 2011</u>
Cash	\$ 191	\$ 181
Accounts receivable	1,219	800
Property and equipment, net	10,916	11,111
Other assets	586	642
<b>Total assets</b>	<b>\$ 12,912</b>	<b>\$ 12,734</b>
Accounts payable	\$ 1,672	\$ 458
Accrued expenses	428	357
Current portion of notes payable	2,998	189
Notes payable, net of current portion	9,441	12,389
Noncontrolling interest	(1,627)	(659)
<b>Total liabilities</b>	<b>\$ 12,912</b>	<b>\$ 12,734</b>

## SEGMENTS (Tables)

9 Months Ended  
Sep. 30, 2012

## SEGMENTS

Schedule of segment  
information

(Amounts in 000s)	SNF	ALF	Corporate & Other	Eliminations	Total
<b>Three months ended September 30, 2012</b>					
Net revenues	\$ 57,978	\$ 3,364	\$ 3,505	\$ (3,077)	\$ 61,770
Cost of services	49,812	2,441	(12)	(3,077)	49,164
General and administrative	—	—	4,328	—	4,328
Facility rent expense	2,039	—	41	—	2,080
Depreciation and amortization	1,590	224	298	—	2,112
Salary retirement and continuation costs	—	—	38	—	38
Operating income/(loss)	<u>\$ 4,537</u>	<u>\$ 699</u>	<u>\$ (1,188)</u>	<u>\$ —</u>	<u>\$ 4,048</u>
<b>Three months ended September 30, 2011</b>					
Net revenues	\$ 37,729	\$ 2,463	\$ 2,349	\$ (2,019)	\$ 40,522
Cost of services	32,887	1,885	(116)	(2,019)	32,637
General and administrative	—	—	3,267	—	3,267
Facility rent expense	1,906	—	31	—	1,937
Depreciation and amortization	631	158	47	—	836
Operating income/(loss)	<u>\$ 2,305</u>	<u>\$ 420</u>	<u>\$ (880)</u>	<u>\$ —</u>	<u>\$ 1,845</u>
<b>Nine months ended September 30, 2012</b>					
Net revenues	\$ 155,753	\$ 10,038	\$ 9,487	\$ (8,331)	\$ 166,947
Cost of services	132,582	7,362	(99)	(8,331)	131,514
General and administrative	—	—	13,188	—	13,188
Facility rent expense	6,065	—	131	—	6,196
Depreciation and amortization	4,075	654	641	—	5,370
Salary retirement and continuation costs	—	—	38	—	38
Operating income/(loss)	<u>\$ 13,031</u>	<u>\$ 2,022</u>	<u>\$ (4,412)</u>	<u>\$ —</u>	<u>\$ 10,641</u>
Total assets	<u>\$ 169,546</u>	<u>\$ 29,181</u>	<u>\$ 38,164</u>	<u>\$ —</u>	<u>\$ 236,891</u>
<b>Nine months ended September 30, 2011</b>					
Net revenues	\$ 97,382	\$ 7,214	\$ 7,646	\$ (6,334)	\$ 105,908
Cost of services	85,495	5,740	15	(6,334)	84,916
General and administrative	—	—	9,358	—	9,358
Facility rent expense	5,711	—	76	—	5,787
Depreciation and amortization	1,595	470	123	—	2,188
Salary retirement and continuation costs	—	—	622	—	622
Operating income/(loss)	<u>\$ 4,581</u>	<u>\$ 1,004</u>	<u>\$ (2,548)</u>	<u>\$ —</u>	<u>\$ 3,037</u>
Total assets	<u>\$ 105,620</u>	<u>\$ 21,490</u>	<u>\$ 31,176</u>	<u>\$ —</u>	<u>\$ 158,286</u>

RELATED PARTY TRANSACTIONS (Details) (USD \$)	9 Months Ended			1 Months Ended		Sep. 30, 2012 Christopher Brogdon, the Company's Chairman Purchase Agreement WP Oklahoma Nursing, LLC Minimum			
	Sep. 30, 2012	Dec. 31, 2011	Sep. 30, 2012 Riverchase item	May 31, 2012 GL Nursing, LLC	Jan. 17, 2012 Gyman Properties, LLC Purchase Agreement item		Jun. 30, 2012 Related party members of the seller Purchase Agreement Hembree Road Property PA item	Jun. 04, 2012 Related party members of the seller Purchase Agreement Hembree Road Property PA	May 09, 2012 Christopher Brogdon, the Company's Vice Chairman Minimum
<a href="#">Related party transaction</a>									
<a href="#">Capacity of skilled nursing facility (in numbers of bed)</a>				141					
<a href="#">Aggregate purchase price for acquiring the businesses</a>	\$ 60,132,000				\$ 6,500,000	\$ 1,100,000			
<a href="#">Number of non-officer employee's that are members of the seller</a>					1				
<a href="#">Amount deposited into escrow to be held as earnest money</a>	812,000	3,172,000		300,000					
<a href="#">Percentage of common stock beneficially owned by Christopher Brogdon</a>							10.00%		
<a href="#">Deposit receivable</a>				300,000					
<a href="#">Percentage of the issued and outstanding membership interests expected to be purchased</a>								100.00%	
<a href="#">Purchase price of the issued and outstanding membership interests expected to be purchased</a>								100,000	
<a href="#">Management contract period</a>			5 years						
<a href="#">Capacity of assisted living facility (in numbers of bed)</a>			105						
<a href="#">Receivable related to agreement</a>									\$ 100,000

**ACCRUED EXPENSES****(Details) (USD \$)****In Thousands, unless  
otherwise specified****Sep. 30, 2012 Dec. 31, 2011****ACCRUED EXPENSES**

<u>Accrued payroll related</u>	\$ 6,358	\$ 5,040
<u>Accrued employee benefits</u>	1,766	2,023
<u>Real estate and other taxes</u>	1,650	982
<u>Other accrued expenses</u>	2,841	1,813
<u>Accrued expenses</u>	\$ 12,615	\$ 9,858

**LIQUIDITY AND  
PROFITABILITY (Details)  
(USD \$)**

<b>3 Months Ended</b>		<b>9 Months Ended</b>	
<b>Sep. 30,</b>	<b>Sep. 30,</b>	<b>Sep. 30,</b>	<b>Sep. 30,</b>
<b>2012</b>	<b>2011</b>	<b>2012</b>	<b>2011</b>

**LIQUIDITY AND PROFITABILITY**

<u>Operating income</u>	\$ 4,048,000	\$ 1,845,000	\$ 10,641,000	\$ 3,037,000
<u>Negative working capital related to short term debt under a VIE</u>	3,000,000		3,000,000	
<u>Net loss</u>	(1,702,000)	3,528,000	(1,230,000)	(1,634,000)
<u>Negative working capital</u>	\$ 2,300,000		\$ 2,300,000	



**VARIABLE INTEREST  
ENTITIES (Details) (USD \$)  
In Thousands, unless  
otherwise specified**

**Sep. 30, 2012 Dec. 31, 2011**

**VARIABLE INTEREST ENTITIES**

<u>Accounts receivable</u>	\$ 30,397	\$ 18,759
<u>Property and equipment, net</u>	166,708	105,143
<u>Other assets</u>	169	122
<u>Accounts payable</u>	20,324	12,075
<u>Accrued expenses</u>	12,615	9,858
<u>Noncontrolling interest</u>	(2,231)	(841)

Riverchase Village Facility

**VARIABLE INTEREST ENTITIES**

<u>Cash</u>	10	16
<u>Accounts receivable</u>	7	10
<u>Restricted investments</u>	326	451
<u>Property and equipment, net</u>	5,993	5,999
<u>Other assets</u>	411	432
<u>Total assets</u>	6,747	6,908
<u>Accounts payable</u>	1,112	740
<u>Accrued expenses</u>	130	174
<u>Current portion of notes payable</u>	99	99
<u>Notes payable, net of current portion</u>	6,010	6,077
<u>Noncontrolling interest</u>	(604)	(182)
<u>Total liabilities</u>	6,747	6,908

Oklahoma Facilities

**VARIABLE INTEREST ENTITIES**

<u>Cash</u>	191	181
<u>Accounts receivable</u>	1,219	800
<u>Property and equipment, net</u>	10,916	11,111
<u>Other assets</u>	586	642
<u>Total assets</u>	12,912	12,734
<u>Accounts payable</u>	1,672	458
<u>Accrued expenses</u>	428	357
<u>Current portion of notes payable</u>	2,998	189
<u>Notes payable, net of current portion</u>	9,441	12,389
<u>Noncontrolling interest</u>	(1,627)	(659)
<u>Total liabilities</u>	\$ 12,912	\$ 12,734

**DISCONTINUED  
OPERATIONS**

**9 Months Ended  
Sep. 30, 2012**

**DISCONTINUED  
OPERATIONS**

**DISCONTINUED  
OPERATIONS**

**NOTE 3. DISCONTINUED OPERATIONS**

As part of the Company's strategy to focus on the growth of its skilled nursing segment, the Company decided in the fourth quarter of 2011 to exit the home health segment of the business. This segment represents less than 2% of total revenues for the Company over the past year. During the quarter ended September 30, 2012, the Company sold all the equipment of the home health segment for approximately \$50,000 and discontinued providing services resulting in an immaterial gain on sale.



**NOTES PAYABLE AND  
OTHER DEBT (Tables)**

**9 Months Ended  
Sep. 30, 2012**

**NOTES PAYABLE AND  
OTHER DEBT**

Schedule of notes payable and  
other debt

(Amounts in 000s)	September 30,	December 31,
	2012	2011
Revolving credit facilities and lines of credit	\$ 10,439	\$ 8,651
Senior debt HUD	15,734	15,738
Senior debt USDA	38,158	38,717
Senior debt SBA	6,247	5,087
Senior debt bonds, net of discount	15,889	6,176
Senior debt other mortgage indebtedness	63,610	23,823
Other debt	7,243	4,197
Convertible debt issued in 2010, net of discount	10,737	10,105
Convertible debt issued in 2011	4,509	4,509
Convertible debt issued in 2012	7,500	—
<b>Total</b>	<b>180,066</b>	<b>117,003</b>
Less current portion of notes payable and other debt	11,991	4,567
Less current portion of revolving credit facility and lines of credit	1,363	7,343
Notes payable and other debt, net of current portion	<u>\$ 166,712</u>	<u>\$ 105,093</u>

Summary of the scheduled  
maturities of indebtedness

(Amounts in 000s)	
2013	\$ 13,354
2014	26,323
2015	24,531
2016	15,193
2017	26,316
Thereafter	75,693
	<u>181,410</u>
Less: unamortized discounts	(1,344)
	<u>\$ 180,066</u>

**ACCRUED EXPENSES**  
**(Tables)**

**9 Months Ended**  
**Sep. 30, 2012**

**ACCRUED EXPENSES**  
**Schedule of accrued expenses**

	September 30,	December 31,
<b>(Amounts in 000s)</b>	<b>2012</b>	<b>2011</b>
Accrued payroll related	\$ 6,358	\$ 5,040
Accrued employee benefits	1,766	2,023
Real estate and other taxes	1,650	982
Other accrued expenses	2,841	1,813
	<u>\$ 12,615</u>	<u>\$ 9,858</u>

ACQUISITIONS (Details) (USD \$)	9 Months Ended		1 Months Ended						
	Sep. 30, 2012 item	Sep. 30, 2011	Jan. 02, 2012 Eaglewood Care Center and Eaglewood Village	Apr. 30, 2012 Little Rock, Northridge and Woodland Hills item	Apr. 02, 2012 Little Rock, Northridge and Woodland Hills	Jun. 02, 2012 Abington Acquisition	Jul. 02, 2012 Glenvue Nursing Home	Jul. 03, 2012 Quail Creek Health and Rehab	Aug. 17, 2012 Companion Specialized Care Center
<b>ACQUISITIONS</b>									
<a href="#">Number of skilled nursing facilities acquired</a>	8			3					
<a href="#">Number of assisted living facilities acquired</a>	1								
<a href="#">Acquisition costs</a>	\$ 1,200,000								
<b>Consideration transferred:</b>									
<a href="#">Net proceeds from loans</a>	38,805,000								
<a href="#">Seller notes</a>	5,000,000								
<a href="#">Common stock issued</a>	750,000								
<a href="#">Cash</a>	15,577,000								
<a href="#">Total consideration transferred</a>	60,132,000		12,400,000		27,200,000	3,600,000	8,200,000	5,800,000	5,800,000
<b>Assets acquired:</b>									
<a href="#">Land</a>	3,567,000								
<a href="#">Buildings</a>	39,945,000								
<a href="#">Equipment and furnishings</a>	3,906,000								
<a href="#">Intangible assets - bed licenses</a>	15,905,000								
<a href="#">Total assets acquired</a>	63,323,000								
<b>Liabilities assumed:</b>									
<a href="#">Assumed indebtedness</a>	(2,800,000)								
<a href="#">Real estate taxes and other</a>	(391,000)								
<a href="#">Total identifiable net assets</a>	60,132,000								
<b>Actual and pro forma financial information</b>									
<a href="#">Combined revenue for all acquisitions</a>	21,500,000								
<a href="#">Income from operations</a>	2,100,000								
<b>Unaudited Pro forma Financial Information</b>									
<a href="#">Pro forma revenue</a>	182,647,000	181,437,000							
<a href="#">Pro forma operating expenses</a>	171,591,000	171,859,000							
<a href="#">Pro forma income from operations</a>	\$ 11,056,000	\$ 9,578,000							

## ACQUISITIONS (Tables)

9 Months Ended  
Sep. 30, 2012

### ACQUISITIONS

#### Schedule of total purchase price

(Amounts in 000s)

Consideration transferred:	
Net proceeds from loans	\$ 38,805
Seller notes	5,000
Cash (including prepaid deposits)	15,577
Common stock issued	750
Total consideration transferred	<u>\$ 60,132</u>
Assets acquired:	
Land	\$ 3,567
Buildings	39,945
Equipment and furnishings	3,906
Intangible assets — bed licenses	<u>15,905</u>
Total assets acquired	63,323
Liabilities assumed:	
Assumed indebtedness	(2,800)
Real estate taxes and other	<u>(391)</u>
Total identifiable net assets	<u>\$ 60,132</u>

#### Schedule of pro forma results of consolidated operations

(Amounts in 000s)	Nine Months Ended September 30,	
	2012	2011
Pro forma revenue	\$ 182,647	\$ 181,437
Pro forma operating expenses	\$ 171,591	\$ 171,859
Pro forma income from operations	\$ 11,056	\$ 9,578

**STOCKHOLDERS'  
EQUITY (Tables)**

**9 Months Ended  
Sep. 30, 2012**

**STOCKHOLDERS'  
EQUITY**

[Schedule of authorized shares  
of common stock reserved for  
possible future issuance](#)

<b>(Amounts in 000s)</b>	<b>Shares</b>
Exercise and future grants of stock options under plans	1,274
Exercise of outstanding stock warrants—employee	563
Exercise of outstanding stock warrants—non-employee	3,154
Convertible debt shares issuable (including additional 20% required under agreements)	7,124
Total authorized shares reserved	<u>12,115</u>



**LIQUIDITY AND  
PROFITABILITY**

**9 Months Ended  
Sep. 30, 2012**

**LIQUIDITY AND  
PROFITABILITY**

**LIQUIDITY AND  
PROFITABILITY**

**NOTE 2. LIQUIDITY AND PROFITABILITY**

The Company had operating income of approximately \$4.0 million and \$10.6 million for the three and nine months ended September 30, 2012, respectively, compared to operating income of approximately \$1.8 million and \$3.0 million for the three and nine months ended September 30, 2011, respectively. The Company had a net loss of approximately \$1.7 million and \$1.2 million for the three and nine months ended September 30, 2012, respectively, and net income of \$3.5 million and a net loss of \$1.6 million for the three and nine months ended September 30, 2011, respectively. The Company had negative working capital of approximately \$2.3 million at September 30, 2012. Approximately \$3.0 million of the negative working capital ratio is related to short term debt under a VIE which the Company does not guarantee. (See Note 12). The Company's ability to sustain profitable operations is dependent on continued growth in revenue and controlling costs.

Management's plans for increasing liquidity and profitability in future years include the following:

- increasing facility occupancy and improving the quality mix by increasing Medicare patients and further optimizing our newly acquired facilities;
- acquiring additional long term care facilities with existing cash flowing operations to expand our operations; and
- refinancing debt where possible on longer terms to obtain more favorable terms.

Management believes that the foregoing actions, if taken by the Company, should provide the opportunity for the Company to improve liquidity and profitability; however, there is no assurance that such actions will occur or, if they do occur, that they will result in improved liquidity or profitability. The consolidated financial statements do not include any adjustments that might result from the outcome of this uncertainty.

**STOCK BASED  
COMPENSATION (Tables)**

**9 Months Ended  
Sep. 30, 2012**

**STOCK BASED  
COMPENSATION**

Summary of the Company's  
restricted stock activity

	<b>Number of Shares</b>	<b>Weighted Avg. Grant Date Fair Value</b>
Nonvested at January 1, 2012	—	—
Stock Dividend	16,000	\$ 3.38
Granted	320,000	\$ 3.38
Vested	(336,000)	\$ 3.38
Forfeited	—	—
Nonvested at September 30, 2012	<u>—</u>	<u>—</u>

**PROPERTY AND  
EQUIPMENT (Details)  
(USD \$)**

**9 Months Ended  
Sep. 30, 2012 Sep. 30, 2011 Dec. 31, 2011**

**PROPERTY AND EQUIPMENT**

<u>Property and equipment, gross</u>	\$ 179,385,000	\$ 113,300,000
<u>Less: accumulated depreciation expense</u>	11,265,000	7,624,000
<u>Less: accumulated amortization expense</u>	1,412,000	533,000
<u>Property and equipment, net</u>	166,708,000	105,143,000
<u>Depreciation and Amortization</u>	4,600,000	1,500,000

Buildings and improvements

**PROPERTY AND EQUIPMENT**

<u>Property and equipment, gross</u>	151,951,000	96,065,000
--------------------------------------	-------------	------------

Buildings and improvements | Minimum

**PROPERTY AND EQUIPMENT**

<u>Estimated Useful Lives</u>	5 years
-------------------------------	---------

Buildings and improvements | Maximum

**PROPERTY AND EQUIPMENT**

<u>Estimated Useful Lives</u>	40 years
-------------------------------	----------

Equipment

**PROPERTY AND EQUIPMENT**

<u>Property and equipment, gross</u>	12,776,000	7,108,000
--------------------------------------	------------	-----------

Equipment | Minimum

**PROPERTY AND EQUIPMENT**

<u>Estimated Useful Lives</u>	2 years
-------------------------------	---------

Equipment | Maximum

**PROPERTY AND EQUIPMENT**

<u>Estimated Useful Lives</u>	10 years
-------------------------------	----------

Land

**PROPERTY AND EQUIPMENT**

<u>Property and equipment, gross</u>	11,274,000	7,636,000
--------------------------------------	------------	-----------

Computer related

**PROPERTY AND EQUIPMENT**

<u>Property and equipment, gross</u>	2,573,000	2,414,000
--------------------------------------	-----------	-----------

Computer related | Minimum

**PROPERTY AND EQUIPMENT**

<u>Estimated Useful Lives</u>	2 years
-------------------------------	---------

Computer related | Maximum

**PROPERTY AND EQUIPMENT**

<u>Estimated Useful Lives</u>	10 years
-------------------------------	----------

Construction in process

**PROPERTY AND EQUIPMENT**

<u>Property and equipment, gross</u>	\$ 811,000	\$ 77,000
--------------------------------------	------------	-----------

**CONDENSED  
CONSOLIDATED  
BALANCE SHEETS (USD  
\$)**

**Sep. 30, Dec. 31,  
2012 2011**

**In Thousands, unless  
otherwise specified**

**Current Assets:**

<u>Cash and cash equivalents</u>	\$ 9,884	\$ 7,364
<u>Restricted cash and cash equivalents</u>	2,825	1,883
<u>Accounts receivable, net of allowance of \$3,099 and \$1,346</u>	30,397	18,759
<u>Prepaid expenses and other</u>	892	663
<u>Assets of disposal group held for sale</u>		47
<u>Total current assets</u>	43,998	28,716
<u>Restricted cash and investments</u>	5,748	4,870
<u>Property and equipment, net</u>	166,708	105,143
<u>Intangible assets - bed licenses, net</u>	2,558	1,189
<u>Intangible assets - lease rights, net</u>	7,658	8,460
<u>Goodwill</u>	906	906
<u>Escrow deposits for acquisitions</u>	812	3,172
<u>Lease deposits</u>	1,704	1,685
<u>Deferred loan costs, net</u>	6,630	4,818
<u>Other assets</u>	169	122
<u>Total assets</u>	236,891	159,081

**Current Liabilities:**

<u>Current portion of notes payable and other debt</u>	11,991	4,567
<u>Revolving credit facilities and lines of credit</u>	1,363	7,343
<u>Accounts payable</u>	20,324	12,075
<u>Accrued expenses</u>	12,615	9,858
<u>Liabilities of disposal group held for sale</u>		240
<u>Total current liabilities</u>	46,293	34,083

**Notes payable and other debt, net of current portion:**

<u>Senior debt, net of discounts</u>	134,003	87,771
<u>Convertible debt, net of discounts</u>	22,746	14,614
<u>Revolving credit facilities</u>	9,076	1,308
<u>Other debt</u>	887	1,400
<u>Derivative liability</u>	3,231	1,889
<u>Other liabilities</u>	1,728	2,437
<u>Deferred tax liability</u>	99	86
<u>Total liabilities</u>	218,063	143,588

Commitments and contingencies (Note 14)

**Stockholders' equity:**

<u>Preferred stock, no par value; 1,000 shares authorized; no shares issued or outstanding</u>		
<u>Common stock and additional paid-in capital, no par value; 29,000 shares authorized; 14,657 and 12,802 shares issued and outstanding</u>	41,002	35,047

<u>Accumulated deficit</u>	(19,943)	(18,713)
<u>Total stockholders' equity</u>	21,059	16,334
<u>Noncontrolling interest in subsidiaries</u>	(2,231)	(841)
<u>Total equity</u>	18,828	15,493
<u>Total liabilities and stockholders' equity</u>	\$	\$
	236,891	159,081

STOCKHOLDERS' EQUITY (Details) (USD \$)	1 Months Ended			9 Months Ended	
	Oct. 31, 2012	May 31, 2012	Mar. 31, 2012	Sep. 30, 2012	Sep. 06, 2012
<b><u>STOCKHOLDERS' EQUITY</u></b>					
<u>Stock dividend (as a percent)</u>					5.00%
<u>Increase in number of outstanding shares of common stock as a result of the stock dividend</u>	700,000				
<u>Number of shares issued</u>		65,000	1,100,000		
<u>Offering price (in dollars per share)</u>		\$ 3.75	\$ 3.75		
<u>Offering period to purchase additional common stock</u>			45 days		
<u>Additional number of shares</u>			165,000		
<u>Net proceeds</u>				\$ 3,837,000	
<u>Underwriting discounts and other offering-related expenses</u>				\$ 600,000	
<b><u>Shares Reserved</u></b>					
<u>Exercise and future grants of stock options under plans</u>				1,274,000	
<u>Exercise of outstanding stock warrants-employee</u>				563,000	
<u>Exercise of outstanding stock warrants-non-employee</u>				3,154,000	
<u>Convertible debt shares issuable</u>				7,124,000	
<u>Total authorized shares reserved</u>				12,115,000	
<u>Additional percentage of convertible debt shares issuable under agreements</u>					20.00%

**CONDENSED  
CONSOLIDATED  
STATEMENTS OF CASH  
FLOWS (USD \$)  
In Thousands, unless  
otherwise specified**

**9 Months Ended**

**Sep. 30,  
2012      Sep. 30,  
2011**

**Cash flows from operating activities:**

<u>Net Loss</u>	\$ (2,620)	\$ (2,724)
<u>Net Loss from discontinued operations</u>	472	285
<u>Net Loss from continuing operations</u>	(2,148)	(2,439)

**Adjustments to reconcile net loss from continuing operations to net cash provided by operating activities:**

<u>Depreciation and amortization</u>	5,370	2,188
<u>Non cash settlement gain</u>	(361)	
<u>Warrants issued for services</u>	1	162
<u>Stock based compensation expense</u>	615	579
<u>Provision for leases in excess of cash</u>	419	558
<u>Amortization of deferred financing costs</u>	1,742	599
<u>Amortization of debt discounts</u>	646	663
<u>Derivative (gain) loss</u>	1,342	(807)
<u>Loss on debt extinguishment</u>		136
<u>Deferred tax expense</u>	13	163
<u>(Gain) loss on disposal of assets</u>	(2)	126
<u>Gain on acquisitions</u>		(898)
<u>Provision for bad debts</u>	2,021	593
<u>Other noncash items</u>	40	59

**Changes in certain assets and liabilities, net of acquisitions:**

<u>Accounts receivable</u>	(13,199)	(8,305)
<u>Prepaid expenses and other</u>	(229)	(159)
<u>Other assets</u>	133	(525)
<u>Accounts payable and accrued expenses</u>	9,368	8,433
<u>Net cash provided by operating activities - continuing operations</u>	5,771	1,126
<u>Net cash used in operating activities - discontinued operations</u>	(648)	(96)
<u>Net cash provided by operating activities</u>	5,123	1,030

**Cash flows from investing activities:**

<u>Change in restricted cash and investments</u>	677	546
<u>Acquisitions</u>	(13,467)	(11,050)
<u>Proceeds from sale of assets</u>	50	
<u>Purchase of property and equipment</u>	(4,191)	(2,732)
<u>Net cash used in investing activities</u>	(16,931)	(13,236)

**Cash flows from financing activities:**

<u>Proceeds from debt</u>	13,261	7,313
<u>Debt issuance costs</u>	(740)	(389)
<u>Change in line of credit</u>	1,600	5,770

<u>Exercise of warrants and options</u>	137	6,798
<u>Proceeds from stock issuances, net</u>	3,837	
<u>Repayment of notes payable</u>	(3,620)	(1,013)
<u>Net cash provided by financing activities - continuing operations</u>	14,475	18,479
<u>Net cash used in financing activities - discontinued operations</u>	(147)	(134)
<u>Net cash provided by financing activities</u>	14,328	18,345
<u>Net Change in Cash</u>	2,520	6,139
<u>Cash, Beginning</u>	7,364	3,911
<u>Cash, Ending</u>	9,884	10,050
<b><u>Cash paid during the period for:</u></b>		
<u>Interest</u>	7,633	4,246
<u>Income Taxes</u>	217	197
<b><u>Supplemental Disclosure of Non-cash Activities:</u></b>		
<u>Acquisitions in exchange for debt and equity instruments</u>	46,605	48,826
<u>Warrants issued for financing costs</u>	439	330
<u>Restricted stock issued for financing costs</u>	175	
<u>Other assets acquired in exchange for debt</u>	\$ 4,908	\$ 5,063



**SUMMARY OF  
SIGNIFICANT  
ACCOUNTING POLICIES**  
(Details) (USD \$)  
In Thousands, except Per  
Share data, unless otherwise  
specified

**3 Months Ended                      9 Months Ended**

**Sep. 30,      Sep. 30,      Sep. 30,      Sep. 30,**  
**2012            2011            2012            2011**

**Income (loss)**

<u>Income (loss) from continuing operations</u>	\$ (2,238)	\$ 2,938	\$ (2,148)	\$ (2,439)
<u>Net Loss Attributable to Noncontrolling Interests</u>	738	748	1,390	1,090
<u>Basic net income (loss)</u>	(1,702)	3,528	(1,230)	(1,634)
<u>Diluted net income (loss) from continuing operations</u>	(1,702)	3,528	(1,230)	(1,634)

**Shares**

<u>Basic net income (loss) (in shares)</u>	14,508	11,275	13,820	9,923
<u>Effect from options, warrants and non-vested shares (in shares)</u>		1,111		
<u>Effect from assumed issuance of convertible shares (in shares)</u>		938		
<u>Diluted net income (loss) (in shares)</u>	14,508	13,324	13,820	9,923

**Per Share**

<u>Basic income (loss) from continuing operations (in dollars per share)</u>	\$ (0.10)	\$ 0.33	\$ (0.05)	\$ (0.14)
<u>Diluted net income (loss) from continuing operations (in dollars per share)</u>	\$ (0.10)	\$ 0.28	\$ (0.05)	\$ (0.14)
<u>Basic loss from discontinued operations (in dollars per share)</u>	\$ (0.01)	\$ (0.01)	\$ (0.03)	\$ (0.03)
<u>Diluted loss from discontinued operations (in dollars per share)</u>	\$ (0.01)	\$ (0.01)	\$ (0.03)	\$ (0.03)

**Net Income (Loss) Attributable to AdCare:**

<u>Basic net income (loss) (in dollars per share)</u>	\$ (0.11)	\$ 0.32	\$ (0.08)	\$ (0.17)
<u>Diluted net income (loss) (in dollars per share)</u>	\$ (0.11)	\$ 0.27	\$ (0.08)	\$ (0.17)

Continuing Operations:

**Income (loss)**

<u>Basic net income (loss)</u>	(1,500)	3,686	(758)	(1,349)
<u>Diluted net income (loss) from continuing operations</u>	(1,500)	3,686	(758)	(1,349)

**Shares**

<u>Basic net income (loss) (in shares)</u>	14,508	11,275	13,820	9,923
<u>Diluted net income (loss) (in shares)</u>	14,508	13,324	13,820	9,923

Discontinued Operations:

**Income (loss)**

<u>Basic net income (loss)</u>	(202)	(158)	(472)	(285)
<u>Diluted net income (loss) from continuing operations</u>	\$ (202)	\$ (158)	\$ (472)	\$ (285)

**Shares**

<u>Basic net income (loss) (in shares)</u>	14,508	11,275	13,820	9,923
<u>Diluted net income (loss) (in shares)</u>	14,508	11,275	13,820	9,923

## SUBSEQUENT EVENTS

**9 Months Ended  
Sep. 30, 2012**

### SUBSEQUENT EVENTS

### SUBSEQUENT EVENTS

#### NOTE 16. SUBSEQUENT EVENTS

##### Self-Insurance

Effective October 1, 2012, the Company began providing self-insured medical healthcare benefits to employees. To protect itself against loss exposure with this policy, the Company has purchased individual stop-loss insurance coverage that insures individual claims that exceed \$0.2 million for each covered person per year with an aggregate annual stop-loss level of approximately \$7.5 million. In addition, the Company entered into a large deductible worker's compensation plan for the majority of its employees with a \$0.3 million deductible limit for each occurrence with an aggregate limit of approximately \$6.5 million.

##### Oklahoma (Harty) PSA Amendment

On October 8, 2012, a wholly owned subsidiary of AdCare amended the Purchase and Sale Agreement, dated May 5, 2011, and as subsequently amended and assigned pursuant to which the Company would acquire five skilled nursing facilities located in Oklahoma. The amendment extends the closing date to 60 days after AdCare receives all required licenses and permits necessary to complete the purchase but by no later than November 30, 2012. In consideration for extending the closing date, the Company agrees to pay certain real estate taxes and assessments relating to the facilities in Oklahoma for fiscal year 2011 (which the seller represents to total approximately \$0.2 million) and fiscal year 2012.

On October 12, 2012, the Company executed an Assignment of Purchase and Sale Agreement in favor of the Edwards Assignees, pursuant to which AdCare assigns all of its right to purchase the Edwards Redeemer Nursing Center located in Oklahoma under that certain Purchase and Sale Agreement, dated May 5, 2011 and as subsequently amended and assigned. The Edwards Assignees have agreed to assume all obligations of AdCare under the Purchase and Sale Agreement with respect to the Edwards Redeemer Nursing Center facility, including reimbursement for out-of-pocket costs. AdCare Holdings, the owner of all of the issued and outstanding membership interests of Edward Redeemer (a wholly owned subsidiary of the Company) also has executed a Membership Interest Power pursuant to which it assigns all such interests to Chris Brogdon, the Company's Vice Chairman.

The Company also executed an Assignment of Purchase and Sale Agreement in favor of WP Oklahoma Nursing, LLC, an entity owned and controlled by Mr. Brogdon, pursuant to which the Company assigns all of its right to purchase the Whispering Pines Nursing Center located in Oklahoma under the Purchase and Sale Agreement, dated May 5, 2011 and as subsequently amended and assigned. WP Oklahoma Nursing, LLC has agreed to assume all obligations of the Company under the Oklahoma Facilities Purchase Agreement with respect to the WP Facility.

##### Ohio ALFs Sale

On October 11, 2012, the Company and certain subsidiaries entered into an Agreement of Sale with CHP Acquisition Company, LLC ("CHP") pursuant to which the Company may sell certain land, buildings, improvements, furniture, fixtures, operating agreements and equipment comprising the following six assisted living facilities: Community's Hearth & Home located in Springfield, Ohio; Community's Hearth & Home also located in Springfield, Ohio; Hearth & Home of Van Wert located in Van Wert, Ohio;

Community's Hearth & Home located in Urbana, Ohio; Hearth & Home of Vandalia located in Vandalia, Ohio; and Lincoln Lodge Retirement Residence located in Columbus, Ohio (collectively, the "Ohio ALFs"), for an aggregate purchase price of approximately \$22.3 million, subject to the terms and conditions of the Agreement of Sale.

The purchase price consists of: (i) \$0.2 million to be deposited by CHP into escrow to be held as earnest money (the "Deposit"); (ii) CHP's satisfaction of the principal balance of United States Department of Housing and Urban Development ("HUD") loans for certain of the Ohio ALFs (the "HUD Loan Payoff"); (iii) CHP's assumption of a HUD loan secured by one of the Ohio ALFs (the "HUD Loan Assumption"); (iv) a promissory note issued by CHP to the Company in the amount of \$3.6 million (the "CHP Promissory Note"); and (v) cash consideration in an amount equal to the purchase price minus the amount of the Deposit, the HUD Loan Payoff, the HUD Loan Assumption and the CHP Promissory Note. The Company estimates that the cash consideration to be received at closing would be approximately \$6.7 million.

The closing of the Ohio ALFs Sale may take place at any such time as mutually agreed upon by the Company and CHP, but in no event later than December 31, 2012, unless such closing date has been extended by mutual agreement of the Company and CHP. The closing of the Ohio ALFs Sale is subject to customary closing conditions, indemnification provisions and termination provisions.

At September 30, 2012, the Company did not meet the criteria to classify the Ohio ALFs as held for sale or to present the related operations as discontinued operations because management, although having the authority to approve the action had not yet committed to sell the assets, there was no active plan to locate a buyer and the disposal of the Ohio ALFs probable. Therefore, the related assets and liabilities of the Ohio ALFs were classified as held and used at September 30, 2012. The major assets that will be held as part of the disposal group include the property and equipment with a carrying value of approximately \$12.0 million and the liabilities that are expected to be extinguished consisting of debt was approximately \$11.5 million at September 30, 2012. There are no indications of potential impairment of assets.

#### PrivateBank Credit Facility Amendment

On October 26, 2012, the Company and certain of its wholly owned subsidiaries, on the one hand, and PrivateBank entered into a Modification Agreement which amends that certain Loan and Security Agreement, dated as of September 20, 2012, between certain of the Company's wholly owned subsidiaries and PrivateBank. The modification agreement amends the loan agreement to: (i) allow PrivateBank to issue additional letters of credit for the account of the borrowers under the loan agreement; and (ii) change the total amount that may be issued under any letters of credit to \$2.5 million. The modification agreement did not change the maximum amount that may be borrowed under the loan agreement by the borrowers, which remains at \$10.6 million.

#### Georgetown PSA Amendment

On November 5, 2012, the Company amended its Purchase and Sale Agreement with Winyah Nursing Home, LLC relating to the acquisition of the Georgetown Healthcare & Rehabilitation Center, an 84-bed skilled nursing facility in Georgetown, South Carolina. The amendment extends the closing date to December 27, 2012 and required the Company to deliver an additional \$50,000 extension fee to the seller.

#### Preferred Stock

On November 7, 2012, the Company announced a "best efforts" public offering of 450,000 shares of its newly designated series of its preferred stock, designated as its

10.875% Series A Cumulative Redeemable Preferred Stock (“Series A Preferred Stock”). The Series A Preferred Stock is offered at \$23 per share. Subject to the closing of the offering and sale of the 450,000 shares of Series A Preferred Stock, the Company expects to receive net proceeds of approximately \$9.3 million after deducting underwriting discounts and other offering-related expenses of approximately \$1.1 million.

**SUMMARY OF  
SIGNIFICANT  
ACCOUNTING POLICIES  
(Details 2) (USD \$)**

**9 Months Ended**

	<b>Sep. 30, 2012</b>	<b>Sep. 30, 2011</b>	<b>Dec. 31, 2011</b>
<b><u>Intangible assets</u></b>			
<u>Finite-lived intangible assets, accumulated amortization</u>	\$ 3,299,000		\$ 1,618,000
<u>Finite-lived intangible assets, net carrying amount</u>	7,658,000		8,460,000
<u>Indefinite-lived intangible assets, carrying amount</u>	2,558,000		1,189,000
<u>Finite-lived and indefinite-lived intangible assets, gross carrying amount</u>	53,164,000		36,883,000
<u>Finite-lived and indefinite-lived intangible assets, net carrying amount</u>	49,865,000		35,265,000
<b><u>Estimated amortization expense</u></b>			
<u>Finite-lived intangible assets, net carrying amount</u>	7,658,000		8,460,000
Bed Licenses - Separable			
<b><u>Intangible assets</u></b>			
<u>Indefinite-lived intangible assets, carrying amount</u>	2,558,000		1,189,000
Lease Rights			
<b><u>Intangible assets</u></b>			
<u>Finite-lived intangible assets, gross carrying amount</u>	9,545,000		9,545,000
<u>Finite-lived intangible assets, accumulated amortization</u>	1,887,000		1,085,000
<u>Finite-lived intangible assets, net carrying amount</u>	7,658,000		8,460,000
<u>Amortization expense</u>	800,000	700,000	
<b><u>Estimated amortization expense</u></b>			
<u>2012 (remainder)</u>	267,000		
<u>2013</u>	1,069,000		
<u>2014</u>	1,010,000		
<u>2015</u>	885,000		
<u>2016</u>	885,000		
<u>Thereafter</u>	3,542,000		
<u>Finite-lived intangible assets, net carrying amount</u>	7,658,000		8,460,000
Bed Licenses (included in property and equipment)			
<b><u>Intangible assets</u></b>			
<u>Finite-lived intangible assets, gross carrying amount</u>	41,061,000		26,149,000
<u>Finite-lived intangible assets, accumulated amortization</u>	1,412,000		533,000
<u>Finite-lived intangible assets, net carrying amount</u>	39,649,000		25,616,000
<u>Amortization expense</u>	900,000		
<b><u>Estimated amortization expense</u></b>			
<u>2012 (remainder)</u>	358,000		
<u>2013</u>	1,433,000		
<u>2014</u>	1,433,000		
<u>2015</u>	1,433,000		
<u>2016</u>	1,433,000		
<u>Thereafter</u>	33,559,000		
<u>Finite-lived intangible assets, net carrying amount</u>	\$ 39,649,000		\$ 25,616,000

SUMMARY OF  
SIGNIFICANT  
ACCOUNTING POLICIES  
(Tables)

9 Months Ended

Sep. 30, 2012

SUMMARY OF  
SIGNIFICANT  
ACCOUNTING POLICIES

Schedule of earnings per share

(Amounts in 000s, except per share data)	Three Months Ended September 30,					
	2012			2011		
	Income (loss)	Shares (1)	Per Share	Income (loss)	Shares (1)	Per Share
<b>Continuing Operations:</b>						
Income (loss) from continuing operations	\$ (2,238)			\$ 2,938		
Net loss attributable to noncontrolling interests	738			748		
Basic income (loss) from continuing operations	\$ (1,500)	14,508	\$ (0.10)	\$ 3,686	11,275	\$ 0.33
Effect from options, warrants and non-vested shares	—	—	—	—	1,111	—
Effect from assumed issuance of convertible shares (2)	—	—	—	—	938	—
Diluted net income (loss) from continuing operations	\$ (1,500)	14,508	\$ (0.10)	\$ 3,686	13,324	\$ 0.28
<b>Discontinued Operations:</b>						
Basic loss from discontinued operations	\$ (202)	14,508	\$ (0.01)	\$ (158)	11,275	\$ (0.01)
Diluted loss from discontinued operations	\$ (202)	14,508	\$ (0.01)	\$ (158)	11,275	\$ (0.01)
<b>Net Income (Loss) Attributable to AdCare:</b>						
Basic net income (loss)	\$ (1,702)	14,508	\$ (0.11)	\$ 3,528	11,275	\$ 0.32
Diluted net income (loss)	\$ (1,702)	14,508	\$ (0.11)	\$ 3,528	13,324	\$ 0.27

  

(Amounts in 000s, except per share data)	Nine Months Ended September 30,					
	2012			2011		
	Income (loss)	Shares (1)	Per Share	Income (loss)	Shares (1)	Per Share
<b>Continuing Operations:</b>						
Loss from continuing operations	\$ (2,148)			\$ (2,439)		
Net loss attributable to noncontrolling interests	1,390			1,090		
Basic loss from continuing operations	\$ (758)	13,820	\$ (0.05)	\$ (1,349)	9,923	\$ (0.14)
Effect from options, warrants and non-vested shares	—	—	—	—	—	—
Effect from assumed issuance of convertible shares (2)	—	—	—	—	—	—
Diluted loss from continuing operations	\$ (758)	13,820	\$ (0.05)	\$ (1,349)	9,923	\$ (0.14)
<b>Discontinued Operations:</b>						
Basic loss from discontinued operations	\$ (472)	13,820	\$ (0.03)	\$ (285)	9,923	\$ (0.03)
Diluted loss from discontinued operations	\$ (472)	13,820	\$ (0.03)	\$ (285)	9,923	\$ (0.03)
<b>Net Income (Loss) Attributable to AdCare:</b>						
Basic loss	\$ (1,230)	13,820	\$ (0.08)	\$ (1,634)	9,923	\$ (0.17)
Diluted loss	\$ (1,230)	13,820	\$ (0.08)	\$ (1,634)	9,923	\$ (0.17)

(1) The weighted average shares outstanding include retroactive adjustments for the stock dividends paid on October 22, 2012 and October 1, 2011 (See Note 10).

(2) The impact of the conversion of the subordinated convertible notes issued in 2010, 2011 and 2012 were excluded in those periods where the impact would be anti-dilutive.

Schedule of intangible assets

(Amounts in 000s)	September 30, 2012			December 31, 2011		
	Gross Carrying Amount	Accumulated Amortization	Net Carrying Amount	Gross Carrying Amount	Accumulated Amortization	Net Carrying Amount
	Lease Rights	\$ 9,545	\$ 1,887	\$ 7,658	\$ 9,545	\$ 1,085
Bed Licenses (included in property and equipment)	41,061	1,412	39,649	26,149	533	25,616
Bed Licenses - Separable	2,558	—	2,558	1,189	—	1,189
Totals	\$ 53,164	\$ 3,299	\$ 49,865	\$ 36,883	\$ 1,618	\$ 35,265

Schedule of estimated  
amortization expense

(Amounts in 000s)	Lease Rights	Bed Licenses
2012 (remainder)	\$ 267	\$ 358
2013	1,069	1,433
2014	1,010	1,433
2015	885	1,433
2016	885	1,433
Thereafter	3,542	33,559
	\$ 7,658	\$ 39,649

**SUMMARY OF  
SIGNIFICANT  
ACCOUNTING POLICIES**

**9 Months Ended**

**Sep. 30, 2012**

**SUMMARY OF  
SIGNIFICANT  
ACCOUNTING POLICIES**

**SUMMARY OF  
SIGNIFICANT  
ACCOUNTING POLICIES**

**NOTE 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**

***Basis of Presentation***

The accompanying unaudited condensed consolidated financial statements have been prepared in accordance with U.S. generally accepted accounting principles for interim financial information and with the instructions to Form 10-Q and Rule 8-03 of Regulation S-X. Accordingly, they do not include all of the information or notes required for complete annual financial statements and should be read in conjunction with the AdCare Health Systems, Inc.'s audited consolidated financial statements and notes included in AdCare Health Systems, Inc.'s Annual Report on Form 10-K for the year ended December 31, 2011 (the "Annual Report"). These statements include the accounts of AdCare Health Systems, Inc. ("AdCare") and its controlled subsidiaries (collectively with AdCare, the "Company" or "we"). Controlled subsidiaries include AdCare's majority owned subsidiaries and variable interest entities ("VIE") in which AdCare has control as primary beneficiary.

All inter-company accounts and transactions were eliminated in the consolidation. In the opinion of the Company's management, all adjustments considered for a fair presentation are included and are of a normal recurring nature. The preparation of interim financial statements requires management to make estimates and assumptions that affect certain reported amounts. Operating results for the three and nine months ended September 30, 2012 are not necessarily indicative of the results that may be expected for the year ending December 31, 2012. Certain prior year amounts have been reclassified to conform to the current year presentation.

***Earnings per Share***

Basic earnings per share is computed by dividing net income or loss by the weighted-average number of common shares outstanding during the period.

Diluted earnings per share is similar to basic earnings per share except net income or loss is adjusted by the impact of the assumed issuance of common shares upon conversion or exercise of convertible or exercisable securities and the weighted-average number of common shares outstanding includes potentially dilutive securities, such as options, warrants, non-vested shares, and additional shares issuable under convertible notes outstanding during the period when such potentially dilutive securities are not anti-dilutive. Potentially dilutive securities from options, warrants and non-vested shares are calculated in accordance with the treasury stock method, which assumes that proceeds from the exercise of all options and warrants with exercise prices exceeding the average market value are used to repurchase common stock at market value. The incremental shares remaining after the proceeds are exhausted represent the potentially dilutive effect of the securities. Potentially dilutive securities from convertible debt are calculated based on the assumed issuance at the beginning of the period, as well as any adjustment to income that would result from their assumed issuance.

**Three Months Ended September 30,**

**2012**

**2011**

(Amounts in 000s, except per share data)	2012			2011		
	Income (loss)	Shares (1)	Per Share	Income (loss)	Shares (1)	Per Share
<b>Continuing Operations:</b>						
Income (loss) from continuing operations	\$ (2,238)			\$ 2,938		
Net loss attributable to noncontrolling interests	738			748		
Basic income (loss) from continuing operations	\$ (1,500)	14,508	\$ (0.10)	\$ 3,686	11,275	\$ 0.33
Effect from options, warrants and non-vested shares	—	—		—	1,111	
Effect from assumed issuance of convertible shares (2)	—	—		—	938	
Diluted net income (loss) from continuing operations	\$ (1,500)	14,508	\$ (0.10)	\$ 3,686	13,324	\$ 0.28

<b>Discontinued Operations:</b>						
Basic loss from discontinued operations	\$ (202)	14,508	\$ (0.01)	\$ (158)	11,275	\$ (0.01)
Diluted loss from discontinued operations	\$ (202)	14,508	\$ (0.01)	\$ (158)	11,275	\$ (0.01)

<b>Net Income (Loss) Attributable to AdCare:</b>						
Basic net income (loss)	\$ (1,702)	14,508	\$ (0.11)	\$ 3,528	11,275	\$ 0.32
Diluted net income (loss)	\$ (1,702)	14,508	\$ (0.11)	\$ 3,528	13,324	\$ 0.27

(Amounts in 000s, except per share data)	Nine Months Ended September 30,					
	2012			2011		
	Income (loss)	Shares (1)	Per Share	Income (loss)	Shares (1)	Per Share
<b>Continuing Operations:</b>						
Loss from continuing operations	\$ (2,148)			\$ (2,439)		
Net loss attributable to noncontrolling interests	1,390			1,090		
Basic loss from continuing operations	\$ (758)	13,820	\$ (0.05)	\$ (1,349)	9,923	\$ (0.14)
Effect from options, warrants and non-vested shares	—	—		—	—	
Effect from assumed issuance of convertible shares (2)	—	—		—	—	
Diluted loss from continuing operations	\$ (758)	13,820	\$ (0.05)	\$ (1,349)	9,923	\$ (0.14)

<b>Discontinued Operations:</b>						
Basic loss from discontinued operations	\$ (472)	13,820	\$ (0.03)	\$ (285)	9,923	\$ (0.03)
Diluted loss from discontinued operations	\$ (472)	13,820	\$ (0.03)	\$ (285)	9,923	\$ (0.03)

<b>Net Income (Loss) Attributable to AdCare:</b>						
Basic loss	\$ (1,230)	13,820	\$ (0.08)	\$ (1,634)	9,923	\$ (0.17)
Diluted loss	\$ (1,230)	13,820	\$ (0.08)	\$ (1,634)	9,923	\$ (0.17)

(1) The weighted average shares outstanding include retroactive adjustments for the stock dividends paid on October 22, 2012 and October 1, 2011 (See Note 10).



(2) The impact of the conversion of the subordinated convertible notes issued in 2010, 2011 and 2012 were excluded in those periods where the impact would be anti-dilutive.

### ***Intangible Assets and Goodwill***

There have been no required impairment adjustments to intangible assets and goodwill during the nine months ended September 30, 2012.

Intangible assets consist of the following:

<u>Amounts in (000s)</u>	<u>September 30, 2012</u>			<u>December 31, 2011</u>		
	<u>Gross</u>		<u>Net</u>	<u>Gross</u>		<u>Net</u>
	<u>Carrying</u>	<u>Accumulated</u>	<u>Carrying</u>	<u>Carrying</u>	<u>Accumulated</u>	<u>Carrying</u>
	<u>Amount</u>	<u>Amortization</u>	<u>Amount</u>	<u>Amount</u>	<u>Amortization</u>	<u>Amount</u>
Lease Rights	\$ 9,545	\$ 1,887	\$ 7,658	\$ 9,545	\$ 1,085	\$ 8,460
Bed Licenses (included in property and equipment)	41,061	1,412	39,649	26,149	533	25,616
Bed Licenses - Separable	2,558	—	2,558	1,189	—	1,189
Totals	<u>\$ 53,164</u>	<u>\$ 3,299</u>	<u>\$ 49,865</u>	<u>\$ 36,883</u>	<u>\$ 1,618</u>	<u>\$ 35,265</u>

For the nine months ended September 30, 2012, amortization expense was approximately \$0.9 million for bed licenses included in property and equipment. For the nine months ended September 30, 2012 and 2011, amortization expense was \$0.8 million and \$0.7 million, respectively, for lease rights. Estimated amortization expense for each of the following years ending December 31 is as follows:

<u>(Amounts in 000s)</u>	<u>Lease Rights</u>	<u>Bed Licenses</u>
2012 (remainder)	\$ 267	\$ 358
2013	1,069	1,433
2014	1,010	1,433
2015	885	1,433
2016	885	1,433
Thereafter	3,542	33,559
	<u>\$ 7,658</u>	<u>\$ 39,649</u>

### ***Compensated Absences***

In 2012, the Company removed the ability for employees to accumulate earned but unused vacation beyond the current calendar year. As a result, vacation time previously accumulated must be used by the employee by December 31, 2012 or it will be forfeited. Management has estimated the potential forfeitures and has adjusted the vacation accrual accordingly.

**CONDENSED  
CONSOLIDATED  
BALANCE SHEETS  
(Parenthetical) (USD \$)  
In Thousands, unless  
otherwise specified**

**Sep. 30, 2012 Dec. 31, 2011**

**CONDENSED CONSOLIDATED BALANCE SHEETS**

<u>Accounts receivable, allowance (in dollars)</u>	\$ 3,099	\$ 1,346
<u>Preferred stock, shares authorized</u>	1,000	1,000
<u>Preferred stock, shares issued</u>	0	0
<u>Preferred stock, shares outstanding</u>	0	0
<u>Common stock and additional paid-in capital, shares authorized</u>	29,000	29,000
<u>Common stock and additional paid-in capital, shares issued</u>	14,657	12,802
<u>Common stock and additional paid-in capital, shares outstanding</u>	14,657	12,802

**STOCK BASED  
COMPENSATION**

**9 Months Ended  
Sep. 30, 2012**

[STOCK BASED  
COMPENSATION](#)

[STOCK BASED  
COMPENSATION](#)

**NOTE 11. STOCK BASED COMPENSATION**

*Employee Common Stock Warrants & Options (Shares and Strike Prices Adjusted for the 2012 Stock Dividend-See Note 10)*

In February 2012, the Company granted non-qualified stock options to Christopher Brogdon, the Company's Vice Chairman, pursuant to the Company's 2011 Stock Incentive Plan (the "2011 Plan"). A total of 52,500 options were granted with an exercise price per share of \$6.67 and 105,000 options were granted with an exercise price of \$7.62. The options vest in September of 2013 and 2014, respectively. The options are exercisable until February 2022. The fair value of the options at the date of grant was estimated at \$1.19 and \$1.03 per share, respectively, and is being recognized as share-based compensation expense over the requisite service period of the awards.

In March 2012, the Company granted incentive stock options to certain members of management pursuant to the 2011 Plan. A total of 461,160 options were granted with an exercise price per share of \$3.93. The options vest ratably on the day before each of the three subsequent anniversaries. The options are exercisable until March 2017. The fair value of the options at the date of grant was estimated at \$1.34 per share and is being recognized as share-based compensation expense over the requisite service period of the awards.

On June 1, 2012, at the Annual Meeting of Shareholders of the Company, the shareholders approved an amendment to the 2011 Plan to increase the maximum number of shares of common stock that may be issued under the 2011 Plan to an aggregate of 2.0 million shares from 1.0 million. The Company's management, key employees (including the Company's principal executive officer, principal financial officer and named executive officers), directors and consultants are eligible to participate in the 2011 Plan.

In August 2012, the Company granted incentive stock options to certain members of management pursuant to the 2011 Plan. A total of 248,850 options were granted with an exercise price per share of \$3.93. The options vest ratably over three years. The options are exercisable until August 2022. The fair value of the options on the date of grant was estimated at \$1.55 per share and is being recognized as share-based compensation expense over the requisite service period of the awards.

***Nonemployee Common Stock Warrants***

On March 29, 2012, in connection with the issuance of the \$3.5 million promissory note to Cantone Asset Management LLC, the Company granted to Cantone Asset Management LLC a warrant to purchase 315,000 shares of common stock at an exercise price per share of \$3.81. The warrant is exercisable until March 2015. The fair value of the warrant at the date of grant was estimated at \$0.64 per share and is included in deferred loan costs and is being amortized as interest expense over the life of the promissory note.

On April 1, 2012, in connection with the issuance of the \$5.0 million promissory note to Strome Alpha Offshore Ltd., the Company granted to Strome Alpha Offshore Ltd. a warrant to purchase 328,125 shares of common stock at an exercise price per share of \$3.81. The warrant is exercisable until April 2015. The fair value of the warrant at

the date of grant was estimated at \$0.64 per share and is included in deferred loan costs and is being amortized as interest expense over the life of the promissory note.

On July 2, 2012 in connection with the issuance of the \$7.5 million principal amount of 8% subordinated convertible notes, the Company granted a warrant to purchase 105,000 shares of common stock at an exercise price per share of \$3.81 to the placement agent as partial consideration for its service in the offering. The warrant is exercisable until July 2015. The fair value of the warrant at the date of grant was estimated at \$0.49 per share and is included in deferred loan costs and is being amortized as interest expense over the life of the 8% subordinated convertible notes.

On August 31, 2012 the Company granted a warrant to purchase 15,750 shares of common stock at an exercise price per share of \$4.37 to a vendor. The warrant is exercisable until August 2015. The fair value of the warrant at date of grant was estimated at \$0.89 per share and is being recognized as non-employee share —based compensation expense over the requisite service period of the awards.

### ***Restricted Stock***

In June 2012, the Company, approved issuing, pursuant to the 2011 Plan, 283,500 shares of common stock with a three year restriction on transfer to its nine directors. The restricted stock has all the rights of a shareholder from the date of grant, including, without limitation the right to receive dividends and the right to vote. The Company determined the fair value of the restricted stock at date of grant to be equal to the grant date closing stock price of \$3.36. The related compensation expense is being recognized over the three year restricted period. The compensation expense for the three months ended September 30, 2012 was approximately \$0.2 million with unrecognized compensation expense of approximately \$0.7 million remaining at September 30, 2012.

On July 2, 2012 in connection with the issuance of the \$7.5 million principal amount of 8% subordinated convertible notes, the Company granted 52,500 shares of restricted common stock with a one year restriction on transferability to the placement agent as partial consideration for its service on the offering. The Company determined the fair value of the restricted stock at the date of grant to be equal to the grant date closing stock price of \$3.50. The related compensation expense is included in deferred loan costs and is being amortized as interest expense over the term of the 8% subordinated convertible notes. The expense for the three months ended September 30, 2012 was less than \$0.1 million with unrecognized expense of approximately \$0.2 million remaining at September 30, 2012.

The following summarizes the Company's restricted stock activity for the period ended September 30, 2012:

	Number of Shares	Weighted Avg. Grant Date Fair Value
Nonvested at January 1, 2012	—	—
Stock Dividend	16,000	\$ 3.38
Granted	320,000	\$ 3.38
Vested	(336,000)	\$ 3.38
Forfeited	—	—
Nonvested at September 30, 2012	<u>—</u>	<u>—</u>

**Document and Entity  
Information**

**9 Months Ended  
Sep. 30, 2012**

**Oct. 31, 2012**

**Document and Entity Information**

<u>Entity Registrant Name</u>	ADCARE HEALTH SYSTEMS INC	
<u>Entity Central Index Key</u>	0001004724	
<u>Document Type</u>	10-Q	
<u>Document Period End Date</u>	Sep. 30, 2012	
<u>Amendment Flag</u>	false	
<u>Current Fiscal Year End Date</u>	--12-31	
<u>Entity Current Reporting Status</u>	Yes	
<u>Entity Filer Category</u>	Smaller Reporting Company	
<u>Entity Common Stock, Shares Outstanding</u>		14,658,361
<u>Document Fiscal Year Focus</u>	2012	
<u>Document Fiscal Period Focus</u>	Q3	

**VARIABLE INTEREST  
ENTITIES**

**9 Months Ended  
Sep. 30, 2012**

**VARIABLE INTEREST  
ENTITIES**

**VARIABLE INTEREST  
ENTITIES**

**NOTE 12. VARIABLE INTEREST ENTITIES**

As further described in Note 19 to the consolidated financial statements in the Annual Report, the Company has certain variable interest entities that are required to be consolidated because AdCare has control as primary beneficiary. A “primary beneficiary” is the party in a VIE that has both of the following characteristics: (a.) The power to direct the activities of the VIE that most significantly impact the VIE’s economic performance and (b.) The obligation to absorb losses of the VIE that could potentially be significant to the VIE or the right to receive benefits from the VIE that could potentially be significant to the VIE.

In June 2012, the Company amended the Option Agreement to purchase Riverchase Village Facility to extend the option exercise period to June 22, 2013. There have been no significant changes in these relationships in 2012. The following summarizes the assets and liabilities of the variable interest entities included in the consolidated balance sheets:

Riverchase Village Facility - Assets and Liabilities:

<u>(Amounts in 000s)</u>	<u>September 30, 2012</u>	<u>December 31, 2011</u>
Cash	\$ 10	\$ 16
Accounts receivable	7	10
Restricted investments	326	451
Property and equipment, net	5,993	5,999
Other assets	411	432
<b>Total assets</b>	<b>\$ 6,747</b>	<b>\$ 6,908</b>
Accounts payable	\$ 1,112	\$ 740
Accrued expenses	130	174
Current portion of notes payable	99	99
Notes payable, net of current portion	6,010	6,077
Noncontrolling interest	(604)	(182)
<b>Total liabilities</b>	<b>\$ 6,747</b>	<b>\$ 6,908</b>

Oklahoma Facilities - Assets and Liabilities:

<u>(Amounts in 000s)</u>	<u>September 30, 2012</u>	<u>December 31, 2011</u>
Cash	\$ 191	\$ 181
Accounts receivable	1,219	800
Property and equipment, net	10,916	11,111
Other assets	586	642
<b>Total assets</b>	<b>\$ 12,912</b>	<b>\$ 12,734</b>
Accounts payable	\$ 1,672	\$ 458
Accrued expenses	428	357
Current portion of notes payable	2,998	189

Notes payable, net of current portion	9,441	12,389
Noncontrolling interest	(1,627)	(659)
Total liabilities	<u>\$ 12,912</u>	<u>\$ 12,734</u>

In March 2012, a wholly owned subsidiary of AdCare entered into a purchase agreement for a skilled nursing home facility in Tulsa, Oklahoma and agreed to provide back office services for the facility until the earlier of its acquisition by the Company or the termination of the purchase agreement. It was determined that in this arrangement, the Company had a variable interest. The current owner of the facility was obligated for the outstanding debt of the facility and the Company did not provided any guarantee of the debt. The Company can terminate the current arrangement without any requirement to provide future financial support. As such, it was determined that under this arrangement the Company was not the primary beneficiary and, consolidation was not required. The arrangement terminated on August 17, 2012 when the Company acquired effective control of Companion Specialized Care Center (See Note 9).

CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS (USD \$) In Thousands, except Per Share data, unless otherwise specified	3 Months Ended		9 Months Ended	
	Sep. 30, 2012	Sep. 30, 2011	Sep. 30, 2012	Sep. 30, 2011
<b>Revenues:</b>				
<a href="#">Patient care revenues</a>	\$ 61,342	\$ 40,192	\$ 165,793	\$ 104,596
<a href="#">Management revenues</a>	428	330	1,154	1,312
<a href="#">Total revenues</a>	61,770	40,522	166,947	105,908
<b>Expenses:</b>				
<a href="#">Cost of services (exclusive of facility rent, depreciation and amortization)</a>	49,164	32,637	131,514	84,916
<a href="#">General and administrative</a>	4,328	3,267	13,188	9,358
<a href="#">Facility rent expense</a>	2,080	1,937	6,196	5,787
<a href="#">Depreciation and amortization</a>	2,112	836	5,370	2,188
<a href="#">Salary retirement and continuation costs</a>	38		38	622
<a href="#">Total expenses</a>	57,722	38,677	156,306	102,871
<a href="#">Income from Operations</a>	4,048	1,845	10,641	3,037
<b>Other Income (Expense):</b>				
<a href="#">Interest expense, net</a>	(3,992)	(2,223)	(10,312)	(5,511)
<a href="#">Acquisition costs, net of gains</a>	(342)	(1,147)	(1,160)	(789)
<a href="#">Derivative gain (loss)</a>	(2,105)	4,745	(1,342)	807
<a href="#">Loss on extinguishment of debt</a>		(58)		(136)
<a href="#">Other income (expense)</a>	271	(20)	242	567
<a href="#">Total other income (expense), net</a>	(6,168)	1,297	(12,572)	(5,062)
<a href="#">Income (Loss) from Continuing Operations Before Income Taxes</a>	(2,120)	3,142	(1,931)	(2,025)
<a href="#">Income Tax Expense</a>	(118)	(204)	(217)	(414)
<a href="#">Income (Loss) from Continuing Operations</a>	(2,238)	2,938	(2,148)	(2,439)
<a href="#">Loss from discontinued operations</a>	(202)	(158)	(472)	(285)
<a href="#">Net Income (Loss)</a>	(2,440)	2,780	(2,620)	(2,724)
<a href="#">Net Loss Attributable to Noncontrolling Interests</a>	738	748	1,390	1,090
<a href="#">Net Income (Loss) Attributable to AdCare Health Systems</a>	\$ (1,702)	\$ 3,528	\$ (1,230)	\$ (1,634)
<b>Net Income (Loss) per Common Share - Basic:</b>				
<a href="#">Continuing Operations (in dollars per share)</a>	\$ (0.10)	\$ 0.33	\$ (0.05)	\$ (0.14)
<a href="#">Discontinued Operations (in dollars per share)</a>	\$ (0.01)	\$ (0.01)	\$ (0.03)	\$ (0.03)
<a href="#">Net Income (Loss) per Common Share - Basic (in dollars per share)</a>	\$ (0.11)	\$ 0.32	\$ (0.08)	\$ (0.17)
<b>Net Income (Loss) per Common Share - Diluted:</b>				
<a href="#">Continuing Operations (in dollars per share)</a>	\$ (0.10)	\$ 0.28	\$ (0.05)	\$ (0.14)
<a href="#">Discontinued Operations (in dollars per share)</a>	\$ (0.01)	\$ (0.01)	\$ (0.03)	\$ (0.03)



<u>Net Income (Loss) per Common Share - Diluted (in dollars per share)</u>	\$ (0.11)	\$ 0.27	\$ (0.08)	\$ (0.17)
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**RESTRICTED CASH AND  
INVESTMENTS**

**9 Months Ended  
Sep. 30, 2012**

**RESTRICTED CASH AND  
INVESTMENTS**

**RESTRICTED CASH AND  
INVESTMENTS**

**NOTE 6. RESTRICTED CASH AND INVESTMENTS**

The following table sets forth the Company's various restricted cash, escrow deposits and investments:

<b>(Amounts in 000s)</b>	<b>September 30,</b>	<b>December 31,</b>
	<b>2012</b>	<b>2011</b>
HUD escrow deposits	\$ 202	\$ 326
Funds held in trust for residents	21	45
Principal and interest escrow	247	—
Refundable escrow deposit	—	500
Collateral certificates of deposit	2,355	1,012
Total current portion	2,825	1,883
HUD reserve replacements	1,157	1,130
Reserves for capital improvements	2,292	1,767
Restricted investments for other debt obligations	2,299	1,973
Total noncurrent portion	5,748	4,870
Total restricted cash and investments	\$ 8,573	\$ 6,753

**PROPERTY AND  
EQUIPMENT**

**9 Months Ended  
Sep. 30, 2012**

PROPERTY AND  
EQUIPMENT

PROPERTY AND  
EQUIPMENT

**NOTE 5. PROPERTY AND EQUIPMENT**

<u>(Amounts in 000s)</u>	<u>Estimated Useful Lives (Years)</u>	<u>September 30, 2012</u>	<u>December 31, 2011</u>
Buildings and improvements	5-40	\$ 151,951	\$ 96,065
Equipment	2-10	12,776	7,108
Land	—	11,274	7,636
Computer related	2-10	2,573	2,414
Construction in process	—	811	77
		<u>179,385</u>	<u>113,300</u>
Less: accumulated depreciation expense		11,265	7,624
Less: accumulated amortization expense		1,412	533
Property and equipment, net		<u>\$ 166,708</u>	<u>\$ 105,143</u>

For the nine months ended September 30, 2012 and 2011, depreciation and amortization expense was approximately \$4.6 million and \$1.5 million, respectively.

**SUMMARY OF  
SIGNIFICANT  
ACCOUNTING POLICIES  
(Policies)**

**9 Months Ended**

**Sep. 30, 2012**

**SUMMARY OF  
SIGNIFICANT  
ACCOUNTING POLICIES**

**Basis of Presentation**

***Basis of Presentation***

The accompanying unaudited condensed consolidated financial statements have been prepared in accordance with U.S. generally accepted accounting principles for interim financial information and with the instructions to Form 10-Q and Rule 8-03 of Regulation S-X. Accordingly, they do not include all of the information or notes required for complete annual financial statements and should be read in conjunction with the AdCare Health Systems, Inc.'s audited consolidated financial statements and notes included in AdCare Health Systems, Inc.'s Annual Report on Form 10-K for the year ended December 31, 2011 (the "Annual Report"). These statements include the accounts of AdCare Health Systems, Inc. ("AdCare") and its controlled subsidiaries (collectively with AdCare, the "Company" or "we"). Controlled subsidiaries include AdCare's majority owned subsidiaries and variable interest entities ("VIE") in which AdCare has control as primary beneficiary.

All inter-company accounts and transactions were eliminated in the consolidation. In the opinion of the Company's management, all adjustments considered for a fair presentation are included and are of a normal recurring nature. The preparation of interim financial statements requires management to make estimates and assumptions that affect certain reported amounts. Operating results for the three and nine months ended September 30, 2012 are not necessarily indicative of the results that may be expected for the year ending December 31, 2012. Certain prior year amounts have been reclassified to conform to the current year presentation.

**Earnings per Share**

***Earnings per Share***

Basic earnings per share is computed by dividing net income or loss by the weighted-average number of common shares outstanding during the period.

Diluted earnings per share is similar to basic earnings per share except net income or loss is adjusted by the impact of the assumed issuance of common shares upon conversion or exercise of convertible or exercisable securities and the weighted-average number of common shares outstanding includes potentially dilutive securities, such as options, warrants, non-vested shares, and additional shares issuable under convertible notes outstanding during the period when such potentially dilutive securities are not anti-dilutive. Potentially dilutive securities from options, warrants and non-vested shares are calculated in accordance with the treasury stock method, which assumes that proceeds from the exercise of all options and warrants with exercise prices exceeding the average market value are used to repurchase common stock at market value. The incremental shares remaining after the proceeds are exhausted represent the potentially dilutive effect of the securities. Potentially dilutive securities from convertible debt are calculated based on the assumed issuance at the beginning of the period, as well as any adjustment to income that would result from their assumed issuance.

**Three Months Ended September 30,**

**2012**

**2011**

(Amounts in 000s, except per share data)	2012			2011		
	Income (loss)	Shares (1)	Per Share	Income (loss)	Shares (1)	Per Share
<b>Continuing Operations:</b>						
Income (loss) from continuing operations	\$ (2,238)			\$ 2,938		
Net loss attributable to noncontrolling interests	738			748		
Basic income (loss) from continuing operations	\$ (1,500)	14,508	\$ (0.10)	\$ 3,686	11,275	\$ 0.33
Effect from options, warrants and non-vested shares	—	—		—	1,111	
Effect from assumed issuance of convertible shares (2)	—	—		—	938	
Diluted net income (loss) from continuing operations	\$ (1,500)	14,508	\$ (0.10)	\$ 3,686	13,324	\$ 0.28

<b>Discontinued Operations:</b>						
Basic loss from discontinued operations	\$ (202)	14,508	\$ (0.01)	\$ (158)	11,275	\$ (0.01)
Diluted loss from discontinued operations	\$ (202)	14,508	\$ (0.01)	\$ (158)	11,275	\$ (0.01)

<b>Net Income (Loss) Attributable to AdCare:</b>						
Basic net income (loss)	\$ (1,702)	14,508	\$ (0.11)	\$ 3,528	11,275	\$ 0.32
Diluted net income (loss)	\$ (1,702)	14,508	\$ (0.11)	\$ 3,528	13,324	\$ 0.27

(Amounts in 000s, except per share data)	Nine Months Ended September 30,					
	2012			2011		
	Income (loss)	Shares (1)	Per Share	Income (loss)	Shares (1)	Per Share
<b>Continuing Operations:</b>						
Loss from continuing operations	\$ (2,148)			\$ (2,439)		
Net loss attributable to noncontrolling interests	1,390			1,090		
Basic loss from continuing operations	\$ (758)	13,820	\$ (0.05)	\$ (1,349)	9,923	\$ (0.14)
Effect from options, warrants and non-vested shares	—	—		—	—	
Effect from assumed issuance of convertible shares (2)	—	—		—	—	
Diluted loss from continuing operations	\$ (758)	13,820	\$ (0.05)	\$ (1,349)	9,923	\$ (0.14)

<b>Discontinued Operations:</b>						
Basic loss from discontinued operations	\$ (472)	13,820	\$ (0.03)	\$ (285)	9,923	\$ (0.03)
Diluted loss from discontinued operations	\$ (472)	13,820	\$ (0.03)	\$ (285)	9,923	\$ (0.03)

<b>Net Income (Loss) Attributable to AdCare:</b>						
Basic loss	\$ (1,230)	13,820	\$ (0.08)	\$ (1,634)	9,923	\$ (0.17)
Diluted loss	\$ (1,230)	13,820	\$ (0.08)	\$ (1,634)	9,923	\$ (0.17)

(1) The weighted average shares outstanding include retroactive adjustments for the stock dividends paid on October 22, 2012 and October 1, 2011 (See Note 10).

(2) The impact of the conversion of the subordinated convertible notes issued in 2010, 2011 and 2012 were excluded in those periods where the impact would be anti-dilutive.

## Intangible Assets and Goodwill

### *Intangible Assets and Goodwill*

There have been no required impairment adjustments to intangible assets and goodwill during the nine months ended September 30, 2012.

Intangible assets consist of the following:

Amounts in (000s)	September 30, 2012			December 31, 2011		
	Gross		Net	Gross		Net
	Carrying	Accumulated	Carrying	Carrying	Accumulated	Carrying
	Amount	Amortization	Amount	Amount	Amortization	Amount
Lease Rights	\$ 9,545	\$ 1,887	\$ 7,658	\$ 9,545	\$ 1,085	\$ 8,460
Bed Licenses (included in property and equipment)	41,061	1,412	39,649	26,149	533	25,616
Bed Licenses - Separable	2,558	—	2,558	1,189	—	1,189
Totals	<u>\$ 53,164</u>	<u>\$ 3,299</u>	<u>\$ 49,865</u>	<u>\$ 36,883</u>	<u>\$ 1,618</u>	<u>\$ 35,265</u>

For the nine months ended September 30, 2012, amortization expense was approximately \$0.9 million for bed licenses included in property and equipment. For the nine months ended September 30, 2012 and 2011, amortization expense was \$0.8 million and \$0.7 million, respectively, for lease rights. Estimated amortization expense for each of the following years ending December 31 is as follows:

(Amounts in 000s)	Lease Rights	Bed Licenses
2012 (remainder)	\$ 267	\$ 358
2013	1,069	1,433
2014	1,010	1,433
2015	885	1,433
2016	885	1,433
Thereafter	3,542	33,559
	<u>\$ 7,658</u>	<u>\$ 39,649</u>

## Compensated Absences

### *Compensated Absences*

In 2012, the Company removed the ability for employees to accumulate earned but unused vacation beyond the current calendar year. As a result, vacation time previously accumulated must be used by the employee by December 31, 2012 or it will be forfeited. Management has estimated the potential forfeitures and has adjusted the vacation accrual accordingly.

**FAIR VALUE  
MEASUREMENTS**

**9 Months Ended  
Sep. 30, 2012**

[FAIR VALUE  
MEASUREMENTS](#)

[FAIR VALUE  
MEASUREMENTS](#)

**NOTE 13. FAIR VALUE MEASUREMENTS**

The following are the major categories of assets and liabilities measured at fair value on a recurring basis during the nine months ended September 30, 2012, using quoted prices in active markets for identical assets (Level 1); significant other observable inputs (Level 2); and significant unobservable inputs (Level 3).

	<u>Level 1:</u>	<u>Level 2:</u>	<u>Level 3:</u>	<u>Total at September 30, 2012</u>
Derivative Liability	\$ —	\$ —	\$ 3.2 million	\$ 3.2 million

Set forth below is a reconciliation of the beginning and ending balances for the derivative liability measured at fair value on a recurring basis using significant unobservable inputs (Level 3) during the nine months ended September 30, 2012:

<u>(Amounts in 000s)</u>	<u>Derivative Liability</u>
Beginning Balance	1.9 \$ million
Total loss	1.3 million
Ending Balance	3.2 \$ million

The derivative liability is the result of the Company issuing subordinated convertible notes in 2010. The notes are convertible into shares of common stock of the Company at a current conversion price of \$3.73 (adjusted for various stock dividends) that is subject to future reductions if the Company issues equity instruments at a lower price. Because there is no minimum conversion price, an indeterminate number of shares may be issued in the future. Accordingly, the Company determined an embedded derivative existed that was required to be bifurcated from the subordinated convertible notes and accounted for separately as a derivative liability recorded at fair value. The Company estimates the fair value of the derivative liability using the Black-Scholes Merton option-pricing model with changes in fair value being reported in the condensed consolidated statement of operations. This model requires certain key inputs that are significant unobservable inputs (Level 3).

The Company currently has no plans to issue equity instruments at a price lower than the conversion price of \$3.73, the current conversion price of the subordinated convertible notes issued in 2010. The derivative liability is a non-cash item. Upon conversion to common stock, the debt and derivative liability will be extinguished, the current fair market value of the common stock will be reflected as common stock and additional paid-in capital, and there may be a resulting gain or loss on the debt extinguishment. If not converted to common stock, upon settlement at the date of maturity, the debt and derivative liability will result in a gain on debt extinguishment for the remaining fair value of the derivative.

## ACQUISITIONS

**9 Months Ended  
Sep. 30, 2012**

### ACQUISITIONS ACQUISITIONS

#### NOTE 9. ACQUISITIONS

##### *Summary of 2012 Acquisitions*

During the nine months ended September 30, 2012, the Company acquired a total of eight skilled nursing facilities and one assisted living facility described further below. The Company has incurred a total of approximately \$1.2 million of acquisition costs related to these acquisitions and has recorded the cost in the "Other Income (Expense)" section of the Condensed Consolidated Statements of Operations.

##### *Eaglewood Care Center and Eaglewood Village*

On January 1, 2012, the Company obtained effective control of the Eaglewood Care Center, a skilled nursing facility and the Eaglewood Village facility, an assisted living facility each located in Springfield, Ohio. The total purchase price was \$12.4 million after final closing adjustments.

##### *Little Rock, Northridge and Woodland Hills*

On April 1, 2012, the Company obtained effective control of the Little Rock, Northridge and Woodland Hills facilities, three skilled nursing facilities located in Little Rock, Arkansas. The total purchase price was \$27.2 million after final closing adjustments.

##### *Abington Place*

On June 1, 2012, the Company obtained effective control of Abington Place, a skilled nursing facility located in Little Rock, Arkansas. The total purchase price was \$3.6 million after final closing adjustments.

##### *Glenvue Nursing Home*

On July 2, 2012, the Company obtained effective control of Glenvue Nursing, a skilled nursing facility located in Glenville, Georgia. The total purchase price was \$8.2 million.

##### *Quail Creek Health and Rehab*

On July 3, 2012, the Company obtained effective control of Quail Creek Health and Rehab a skilled nursing facility located in Oklahoma City, Oklahoma, contingent upon final approval and transfer of the operating license to AdCare. The total purchase price was \$5.8 million

##### *Companion Specialized Care Center*

On August 17, 2012, the Company obtained effective control of Companions Specialized Care Center, a skilled nursing facility located in Tulsa, Oklahoma, contingent upon final approval and transfer of the operating license to AdCare. The total purchase price was approximately \$5.8 million.

The preliminary purchase price allocation of all 2012 acquisitions is summarized as follows:



(Amounts in 000s)

<b>Consideration transferred:</b>	
Net proceeds from loans	\$ 38,805
Seller notes	5,000
Cash (including prepaid deposits)	15,577
Common stock issued	750
Total consideration transferred	<u>\$ 60,132</u>
<b>Assets acquired:</b>	
Land	\$ 3,567
Buildings	39,945
Equipment and furnishings	3,906
Intangible assets — bed licenses	15,905
Total assets acquired	<u>63,323</u>
<b>Liabilities assumed:</b>	
Assumed indebtedness	(2,800)
Real estate taxes and other	(391)
Total identifiable net assets	<u>\$ 60,132</u>

The purchase price allocations for Glenvue Nursing, Quail Creek Health and Rehab and Companion Specialized Care Center are recorded on a preliminary basis. The fair value estimates of assets acquired and liabilities are pending completion of various elements. The Quail Creek Health and Rehab and Companion Specialized Care Center acquisitions are preliminary subject to finalization of independent valuations of fair value of the assets acquired and liabilities assumed and final review by our management. The Companion Specialized Care Center consideration transferred is also subject to evaluation of the value of the stock transferred for restriction discounts. The Glenvue Nursing purchase price allocation is subject to final review by management of the independent valuations. Accordingly, there could be adjustments to our financial statements, including changes in our depreciation and amortization expense related to the valuation of building, equipment and furnishings and intangible assets acquired and their respective useful lives among other adjustments.

#### ***Unaudited Pro forma Financial Information***

The above acquisitions have been included in the consolidated financial statements since the dates the Company gained effective control. Combined revenue for all 2012 acquisitions since gaining effective control is approximately \$ 21.5 million and resulted in income from operations of approximately \$ 2.1 million for the nine months ended September 30, 2012.

The following table represents pro forma results of consolidated operations as if all of the 2011 and 2012 acquisitions had occurred at the beginning of the earliest fiscal year being presented, after giving effect to certain adjustments.

(Amounts in 000s)	Nine Months Ended September 30,	
	2012	2011
Pro forma revenue	\$ 182,647	\$ 181,437
Pro forma operating expenses	\$ 171,591	\$ 171,859
Pro forma income from operations	\$ 11,056	\$ 9,578

The forgoing pro forma information is not indicative of what the results of operations would have been if the acquisitions had actually occurred at the beginning of the periods presented and is not intended as a projection of future results or trends.

## ACCRUED EXPENSES

9 Months Ended  
Sep. 30, 2012

### ACCRUED EXPENSES ACCRUED EXPENSES

#### NOTE 7. ACCRUED EXPENSES

Accrued expenses consist of the following:

(Amounts in 000s)	September 30, December 31,	
	2012	2011
Accrued payroll related	\$ 6,358	\$ 5,040
Accrued employee benefits	1,766	2,023
Real estate and other taxes	1,650	982
Other accrued expenses	2,841	1,813
	<u>\$ 12,615</u>	<u>\$ 9,858</u>

**NOTES PAYABLE AND  
OTHER DEBT**

**9 Months Ended  
Sep. 30, 2012**

**NOTES PAYABLE AND  
OTHER DEBT**

**NOTES PAYABLE AND  
OTHER DEBT**

**NOTE 8. NOTES PAYABLE AND OTHER DEBT**

Notes payable and other debt consist of the following:

<u>(Amounts in 000s)</u>	<u>September 30, 2012</u>	<u>December 31, 2011</u>
Revolving credit facilities and lines of credit	\$ 10,439	\$ 8,651
Senior debt HUD	15,734	15,738
Senior debt USDA	38,158	38,717
Senior debt SBA	6,247	5,087
Senior debt bonds, net of discount	15,889	6,176
Senior debt other mortgage indebtedness	63,610	23,823
Other debt	7,243	4,197
Convertible debt issued in 2010, net of discount	10,737	10,105
Convertible debt issued in 2011	4,509	4,509
Convertible debt issued in 2012	7,500	—
Total	<u>180,066</u>	<u>117,003</u>
Less current portion of notes payable and other debt	11,991	4,567
Less current portion of revolving credit facility and lines of credit	<u>1,363</u>	<u>7,343</u>
Notes payable and other debt, net of current portion	<u>\$ 166,712</u>	<u>\$ 105,093</u>

***Scheduled Maturities***

The following is a summary of the scheduled maturities of indebtedness as of September 30, 2012 for each of the next five years and thereafter:

<u>(Amounts in 000s)</u>	
2013	\$ 13,354
2014	26,323
2015	24,531
2016	15,193
2017	26,316
Thereafter	<u>75,693</u>
	181,410
Less: unamortized discounts	<u>(1,344)</u>
	<u>\$ 180,066</u>

Approximately \$23.7 million of the scheduled maturities in 2012, 2014 and 2015, relate to the subordinated convertible notes issued in 2010, 2011 and 2012. While management cannot predict with certainty, we anticipate that some holders of the subordinated convertible notes will elect to convert their subordinated convertible notes into common stock provided the common stock continues to trade above the applicable conversion price for such notes. The conversion prices are \$3.73, \$4.80 and \$3.97 for the subordinated convertible notes issued in 2010, 2011 and 2012, respectively. If all of the subordinated convertible notes had been converted to common stock at September 30, 2012, then the Company would have been required to issue approximately 6.0 million shares of common stock.

***Revolving Credit Facilities***

### *Gemino Credit Agreement*

At December 31, 2011, the outstanding balance of approximately \$7.3 million for the revolving credit agreement was classified as current as a result of the required lockbox arrangement and subjective acceleration clauses.

On September 20, 2012, AdCare terminated and paid off all amounts outstanding under that certain Credit Agreement, dated October 29, 2010, between Gemino Healthcare Finance, LLC (“Gemino”) and AdCare (the “Gemino credit facility”). The Gemino credit facility was a secured credit facility for borrowings up to \$7.5 million, which was to mature on October 29, 2013. As of September 20, 2012, the amount outstanding in principal balance was approximately \$4.2 million which was paid from funds made available to AdCare from a new credit facility entered into with the PrivateBank and Trust Company (“PrivateBank”). Interest accrued on the principal balance outstanding of the Gemino credit facility at an annual rate equal to LIBOR rate plus the applicable margin of 4.75% to 5.00%, depending on the principal amount outstanding. The Gemino credit facility contained various financial covenants and other restrictions, including a fixed charge cover ratio and maximum loan turn days, as well as borrowing base restrictions. No material early termination penalties were incurred by AdCare as a result of the termination.

### *Gemino-Bonterra Amendment*

On September 20, 2012, ADK Bonterra/Parkview, LLC, a wholly owned subsidiary of AdCare (“Bonterra”), entered into a Second Amendment to the Credit Agreement with Gemino, which amended that certain Credit Agreement, dated April 27, 2011, between Bonterra and Gemino (the “Gemino-Bonterra credit facility”). The Gemino-Bonterra credit facility is a secured credit facility for borrowings up to \$2.0 million. The amendment extends the term of the Gemino-Bonterra credit facility from October 29, 2013 to January 31, 2014 and amends certain financial covenants regarding Bonterra’s fixed charge coverage ratio, maximum loan turn days and applicable margin. Interest accrues on the principal balance outstanding at an annual rate equal to LIBOR plus the applicable margin of 4.75% to 5.00%, depending upon the principal amount outstanding. As of September 30, 2012, approximately \$1.4 million was outstanding under the Gemino-Bonterra credit facility.

### *PrivateBank Credit Facility*

On September 20, 2012, in connection with the payoff of the Gemino credit facility, AdCare entered into a Loan and Security Agreement with PrivateBank. The PrivateBank credit facility provides for a three-year \$10.6 million principal amount senior secured revolving credit facility limited to certain borrowing base restrictions and offset by a \$0.1 million letter of credit.

The PrivateBank credit facility matures on September 20, 2015. Interest accrues on the principal balance thereof at an annual rate of the greater of 1% plus the prime interest rate per annum, or 5% per annum, and payments for the interest are payable monthly, commencing on October 1, 2012. In addition, there is a non-utilization fee of 0.5% of the unused portion of the available credit. The PrivateBank credit facility may be prepaid at any time without premium or penalty, provided that such prepayment is accompanied by a simultaneous payment of all accrued but unpaid interest through the date of prepayment. The PrivateBank credit facility is secured by a first priority security interest in the real property and improvements constituting nursing facilities owned and operated by AdCare. AdCare has unconditionally guaranteed all amounts owing under the PrivateBank credit facility.

Proceeds from the PrivateBank credit facility were used to pay off all amounts outstanding under (i) a separate \$2.0 million credit facility with PrivateBank under

which certain subsidiaries of AdCare were borrowers and (ii) the Gemino credit facility.

The PrivateBank credit facility was modified in October 2012. (See Note 16.)

### ***Mortgage Notes***

#### *Hearth and Home of Vandalia*

In connection with the Company's January 2012 refinance of the assisted living facility located in Vandalia, Ohio known as Hearth and Home of Vandalia, a wholly owned subsidiary of AdCare obtained a term loan insured by U.S. Department of Housing and Urban Development ("HUD") with a financial institution for a total amount of \$3.7 million that matures in 2041. The HUD term loan requires monthly principal and interest payments with a fixed interest rate of 3.74%. Deferred financing costs incurred on the term loan amounted to approximately \$0.2 million and are being amortized to interest expense over the life of the loan. The HUD term loan has a prepayment penalty of 8% starting in 2014 declining by 1% each year through 2022.

#### *Woodland Manor*

In connection with the Company's January 2012 acquisition of the skilled nursing facility located in Springfield, Ohio, known as Woodland Manor, a wholly owned subsidiary of the Company entered into a loan agreement for \$4.8 million. The loan matures in December 2016 with a required final payment of approximately \$4.3 million and accrues interest at the LIBOR rate plus 4% with a minimum rate of 6% per annum. The loan requires monthly payments of principal and interest. Deferred financing costs incurred on the loan amounted to approximately \$0.1 million and are being amortized to interest expense over the life of the loan. The loan has a prepayment penalty of 5% through 2012 declining by 1% each year through 2015. The loan is secured by the Woodland Manor facility and guaranteed by AdCare.

#### *Little Rock, Northridge and Woodland Hills*

In connection with the Company's April 2012 acquisition of three skilled nursing facilities located in Arkansas known as Little Rock, Northridge and Woodland Hills, certain wholly owned subsidiaries of AdCare entered into a loan agreement for \$21.8 million with PrivateBank. The loan originally matured in March 2017 with a required final payment of approximately \$19.7 million and accrues interest at the LIBOR rate plus 4% with a minimum rate of 6% per annum. The loan requires monthly principal payments plus interest for total current monthly payments of approximately \$0.2 million. Deferred financing costs incurred on the loan amounted to approximately \$0.4 million and are being amortized to interest expense over the life of the loan. The loan has a prepayment penalty of 5% through 2012 declining by 1% each year through 2015. The loan is secured by the three facilities and guaranteed by AdCare. The Company has approximately \$1.8 million of restricted assets related to this loan.

On June 15, 2012, certain wholly owned subsidiaries of AdCare entered into a modification agreement with PrivateBank to modify the terms of the loan agreement. The loan modification agreement, among other things, amended the loan agreement to reflect a maturity date of March 30, 2013. The Company intends on refinancing this loan to a longer term. PrivateBank has informed us in writing that, in the event the loan was not refinanced through the U.S. Small Business Administration (the "SBA"), it would be the intent of PrivateBank to reinstate the March 30, 2017 maturity date.

#### *Abington Place*

In connection with the Company's June 2012 acquisition of the skilled nursing facility located in Little Rock, Arkansas known as Abington Place, a wholly owned subsidiary of AdCare entered into a short-term loan agreement for \$3.4 million with Metro City Bank. In August 2012, the maturity date was amended from September 2012 to January 2014. The note accrues interest at the prime rate plus 2.25% with a minimum rate of 6.25% per annum. Deferred financing costs incurred on the loan amounted to approximately \$0.1 million and are being amortized to interest expense over the life of the loan. The loan may be prepaid at any time without penalty. The loan was secured by the Abington Place facility and guaranteed by AdCare.

#### *Stone County*

In June 2012, a wholly owned subsidiary of AdCare, entered into each of: (i) a Loan Agreement with Metro City Bank ("Metro") in the amount of \$1.3 million; (ii) a Loan Agreement with Metro in the amount of \$1.8 million; and (iii) a Loan Agreement with the Economic Development Corporation of Fulton County (the "CDC"), an economic development corporation working with the SBA. The purpose of these agreements was to refinance existing debt in the original principal amount of \$3.1 million used to acquire select assets of a 97-bed skilled nursing facility located in Arkansas known as the Stone County Nursing and Rehabilitation Facility.

The funding of the Metro loans for \$1.3 million and \$1.8 million occurred on June 8, 2012. The funding of the SBA loan for \$1.3 million occurred in July 2012, and the proceeds were used to satisfy the \$1.3 million Metro loan.

The \$1.8 million Metro loan matures in June 2022 and accrues interest an annual variable rate equal to the published Wall Street Journal prime rate plus 2.25% (with a minimum rate of 6.25% per annum). Deferred financing costs incurred on this loan amounted to approximately \$0.1 million and are being amortized to interest expense over the life of the loan. The Metro loan has a prepayment penalty of 10% for any prepayment through June 2013. The penalty is reduced by 1% each year thereafter until the tenth anniversary, after which there is no prepayment penalty. The Metro loan is secured by the Stone County Nursing and Rehabilitation Facility and is guaranteed by AdCare.

The SBA loan matures in July 2032 and accrues interest at a rate of 2.42% per annum. The SBA Loan is payable in equal monthly installments of principal and interest based on a twenty (20) year amortization schedule. The SBA loan may be prepaid, subject to prepayment premiums during the first 10 years. There are also annual fees associated with the SBA loan, including an SBA guarantee fee. The SBA Loan is secured by a second in priority security deed on the Stone County Nursing and Rehabilitation Facility and guarantees from AdCare, the SBA and a wholly owned subsidiary of AdCare.

#### *Glenvue*

In July 2012, a wholly owned subsidiary of AdCare financed the skilled nursing facility located in Glennville, Georgia known as Glenvue Health & Rehabilitation by entering into a loan agreement for \$6.6 million with PrivateBank. The loan matures in July 2014 with a required final payment of approximately \$6.4 million and accrues interest at an annual rate of the greater of 6.0% per annum; or the LIBOR rate plus 4.0% per annum. The loan requires monthly principal payments and interest. Deferred financing costs incurred on the loan amounted to approximately \$0.1 million and are being amortized to interest expense over the life of the loan. The loan is secured by the Glenvue facility and guaranteed by AdCare.

#### *Companions Specialized Care*

In August 2012, a wholly owned subsidiary of AdCare financed the skilled nursing facility located in Tulsa, Oklahoma known as Companions Specialized Care Center by entering into a loan agreement for \$5.0 million with Contemporary Healthcare Capital. The loan matures in August 2015 with a required final payment of \$5.0 million and accrues interest at a fixed rate of 8.5% per annum. Deferred financing costs incurred on the loan amounted to approximately \$0.2 million and are being amortized to interest expense over the life of the loan. The loan has a prepayment penalty of 5% during the first year of the term and 1% during the second year of the term. The loan is secured by the Companions Specialized Care facility and guaranteed by AdCare.

## ***Bonds***

### *Eaglewood Village Bonds*

In April 2012, a wholly owned subsidiary of AdCare entered into a loan agreement with the City of Springfield in the State of Ohio (“City of Springfield”) pursuant to which City of Springfield lent to such subsidiary the proceeds from the sale of City of Springfield’s Series 2012 Bonds. The Series 2012 Bonds consist of \$6.6 million in Series 2012A First Mortgage Revenue Bonds and \$0.6 million in Taxable Series 2012B First Mortgage Revenue Bonds. The Series 2012 Bonds were issued pursuant to an April 2012 Indenture of Trust between the City of Springfield and the Bank of Oklahoma. The Series 2012A Bonds mature in May 2042 and accrue interest at a fixed rate of 7.65% per annum. The Series 2012B Bonds mature in May 2021 and accrue interest at a fixed rate of 8.5% per annum. Deferred financing costs incurred on the loan amounted to approximately \$0.6 million and are being amortized to interest expense over the life of the loan. The loan is secured by the Company’s assisted living facility located in Springfield, Ohio known as Eaglewood Village and guaranteed by AdCare. There is an original issue discount of approximately \$0.3 million and restricted assets of \$0.3 million related to this loan.

### *Quail Creek*

In July 2012, a wholly owned subsidiary of AdCare financed the skilled nursing facility located in Oklahoma City, Oklahoma known as Quail Creek Nursing by the assumption of existing indebtedness under that certain Loan Agreement and Indenture of First Mortgage with The Bank of New York Mellon Global Corporate Trust, as assignee of The Liberty National Bank and Trust of that certain Bond Indenture, dated September 1, 1986, as amended as of September 1, 2001. The indebtedness under the Loan Agreement and Indenture consists of a principal amount of \$2.8 million. The loan matures in August 2016 and, accrues interest at a fixed rate of 10.25% per annum. The loan is secured by the Quail Creek facility.

## ***Other Debt***

### *Eaglewood Village Promissory Note*

In January 2012, two wholly owned subsidiaries of AdCare issued a promissory seller note in the amount of \$0.5 million in connection with the January 2012 acquisition of the assisted living facility located in Springfield, Ohio. The note matures in January 2014 and requires a final payment of approximately \$0.5 million. The note bears interest at 6.5% per annum payable monthly beginning February 2012. The note requires monthly principal and interest payment. The note may be prepaid without penalty at any time.

### *Cantone Promissory Notes*

In March 2012, AdCare issued an unsecured promissory note to Cantone Asset Management LLC in the amount of \$3.5 million. In April 2012, AdCare issued another promissory note to Cantone Asset Management LLC in the amount of \$1.5 million. In July 2012, these two promissory notes were refinanced through the issuance to Cantone Asset Management LLC in July 2012 of an 8% subordinated convertible note in principal amount of \$5.0 million.

#### *Strome Note*

On April 1, 2012, AdCare issued an unsecured promissory note in the amount of \$5.0 million to Strome Alpha Offshore Ltd. The promissory note matures in November 2012, and the Company anticipates paying off the promissory note with proceeds from the preferred stock offering discussed in Note 16. Interest accrues at a fixed rate of 10% per annum. The promissory note requires interest payments of approximately \$0.1 million on July 1, 2012 and October 1, 2012. The promissory note may be prepaid at any time without penalty.

#### **Convertible Debt**

##### *Convertible Debt Issued in July 2012*

AdCare entered into a Securities Purchase Agreement, dated as of June 28, 2012, with certain accredited investors pursuant to which the Company issued and sold such investors on July 2, 2012 an aggregate of \$7.5 million in principal amount of the Company's 8.0% subordinated convertible notes. The notes bear interest at 8% per annum and such interest is payable quarterly in cash in arrears beginning on September 30, 2012. The notes mature on July 31, 2015. The notes are unsecured and subordinated in right of payment to existing and future senior indebtedness of the Company. The \$7.5 million principal amount of the notes includes a refinance of existing indebtedness of \$5.0 million of promissory notes issued to Cantone Asset Management LLC.

At any time on or after the six-month anniversary of the date of issuance of the notes, the notes are convertible at the option of the holder into shares of the Company's common stock at an initial conversion price equal to \$3.97 per share (adjusted for a 5% stock dividend paid on October 22, 2012 as further discussed in Note 10) and subject to adjustment for stock dividends, stock splits, combination of shares, recapitalization and other similar events.

If at any time on or after the six-month anniversary date, the weighted average price of the common stock for any 20 trading days within a period of 30 consecutive trading days equals or exceeds 200% of the conversion price and the average daily trading volume of the common stock during such 20 days exceeds 50,000 shares, then the Company may, subject to the satisfaction of certain other conditions, redeem the notes in cash at a redemption price equal to the sum of 100% of the principal amount being redeemed plus any accrued and unpaid interest on such principal.

In addition, the holders of a majority of the aggregate principal amount of notes then outstanding may require the Company to redeem all or any portion of the notes upon a change of control transaction, as described in the Notes, at a redemption price in cash equal to 110% of the redemption amount.



**STOCKHOLDERS'  
EQUITY**

**9 Months Ended  
Sep. 30, 2012**

**STOCKHOLDERS'  
EQUITY**

**STOCKHOLDERS' EQUITY NOTE 10. STOCKHOLDERS' EQUITY**

*Stock Dividend*

On September 6, 2012, the Company's Board of Directors declared a 5% stock dividend issued on October 22, 2012 to holders of the common stock as of October 8, 2012. As a result of the stock dividend, the number of outstanding shares of common stock increased by approximately 0.7 million shares in 2012. As the Company is in a deficit position, there is no recorded impact to the reported amounts of stockholders' equity in the accompanying condensed consolidated balance sheet. As the dividend was declared before the release of the accompanying condensed consolidated financial statements, all references to the number of common shares and per-share amounts are restated based on the increased number of shares giving retroactive effect to the stock dividend on prior period amounts.

*2012 Public Common Stock Offering*

In March 2012, the Company closed a firm commitment underwritten public offering of 1.1 million shares of common stock at an offering price to the public of \$3.75 per share. The Company also granted the underwriter in the offering an option for 45 days to purchase up to an additional 165,000 shares of common stock to cover over-allotments, if any. In connection with the underwriter's partial exercise of this option, the Company issued an additional 65,000 shares of common stock at an offering price to the public of \$3.75 per share on May 22, 2012. The Company received net proceeds of approximately \$3.8 million after deducting underwriting discounts and other offering-related expenses of approximately \$0.6 million. This transaction occurred prior to the 2012 stock dividend and the share amounts, as disclosed, have not been restated as a result.

*Shares Reserved*

At September 30, 2012, the Company had reserved approximately 12.1 million shares (after the 2012 stock dividend) of its authorized but unissued common stock for possible future issuance in connection with the following approximate number of shares (in thousands):

<b>(Amounts in 000s)</b>	<b>Shares</b>
Exercise and future grants of stock options under plans	1,274
Exercise of outstanding stock warrants—employee	563
Exercise of outstanding stock warrants—non-employee	3,154
Convertible debt shares issuable (including additional 20% required under agreements)	7,124
<b>Total authorized shares reserved</b>	<b>12,115</b>

**FAIR VALUE  
MEASUREMENTS (Tables)**

**9 Months Ended  
Sep. 30, 2012**

**FAIR VALUE MEASUREMENTS**

Schedule of assets and liabilities measured at fair value on a recurring basis

	<u>Level 1:</u>	<u>Level 2:</u>	<u>Level 3:</u>	<u>Total at September 30, 2012</u>
Derivative			3.2	
Liability	\$ —	\$ —	\$million	\$ 3.2 million

Schedule of reconciliation of the beginning and ending balances for assets and liabilities measured at fair value on a recurring basis using significant unobservable inputs

<u>(Amounts in 000s)</u>	<u>Derivative Liability</u>
Beginning Balance	\$ 1.9 million
Total loss	1.3 million
Ending Balance	<u>\$ 3.2 million</u>

SUBSEQUENT EVENTS (Details) (USD \$)	9	1 Months		0 Months Ended			0 Months Ended						
	Months Ended	Ended	Ended	Ended	Ended	Ended	Ended	Ended	Ended	Ended			
	Sep. 30, 2012 item	Dec. 31, 2011	Aug. 09, 2012 Georgetown PSA Amendment item	Sep. 30, 2012 Ohio ALFs Sale item	Apr. 30, 2012 Purchase Agreement Oklahoma (Harty) PSA Amendment item	Oct. 02, 2012 Subsequent events	Nov. 07, 2012 Subsequent events Series A Preferred Stock	Oct. 26, 2012 Subsequent events PrivateBank Credit Facility Amendment	Oct. 11, 2012 Subsequent events Sale Agreement Ohio ALFs Sale item	Oct. 08, 2012 Subsequent events Purchase Agreement Oklahoma (Harty) PSA Amendment item	Nov. 05, 2012 Subsequent events Purchase Agreement Georgetown PSA Amendment item	Nov. 07, 2012 Subsequent events Forecast Series A Preferred Stock	Oct. 11, 2012 Subsequent events Forecast Sale Agreement Ohio ALFs Sale
<a href="#">SUBSEQUENT EVENTS</a>													
<a href="#">Amount of individual claims for each covered person per year in excess of which the stop-loss insurance coverage has been purchased by the entity</a>						\$ 200,000							
<a href="#">Aggregate annual stop-loss level</a>						7,500,000							
<a href="#">Large deductible worker's compensation plan, deductible limit for each occurrence</a>						300,000							
<a href="#">Large deductible worker's compensation plan, aggregate deductible limit</a>						6,500,000							
<a href="#">Number of skilled nursing facilities acquired</a>	8				5					5			
<a href="#">Expected transaction closing period</a>					60 days					60 days			
<a href="#">Real estate taxes and assessments to be paid in consideration for extending the closing date</a>										200,000			
<a href="#">Earnest money escrow deposit</a>					200,000								
<a href="#">Number of assisted living facilities</a>									6				
<a href="#">Aggregate purchase price</a>													22,300,000
<a href="#">Earnest money to be deposited by the CHP into escrow</a>									200,000				
<a href="#">Promissory note to be issued</a>									3,600,000				
<a href="#">Cash consideration</a>													6,700,000
<a href="#">Major assets</a>				12,000,000									
<a href="#">Liabilities consisting of debt</a>				11,500,000									
<a href="#">Maximum borrowing capacity</a>								10,600,000					
<a href="#">Number of beds under skilled nursing facility acquired</a>		84									84		
<a href="#">Extension fee required to be paid in consideration for extending the closing date</a>											50,000		
<a href="#">Maximum amount of letters of credit that may be issued under the credit facility</a>								2,500,000					
<a href="#">Number of shares announced in underwritten public offering</a>	1,000,000	1,000,000					450,000						
<a href="#">Dividend rate (as a percent)</a>							10.875%						
<a href="#">Offer price of shares to be sold in underwritten public offering (in dollars per share)</a>							\$ 23						
<a href="#">Sale of preferred stock (in shares)</a>	0	0					450,000						
<a href="#">Expected net proceeds</a>												9,300,000	
<a href="#">Underwriting discounts and other offering related expenses</a>												\$ 1,100,000	

**RELATED PARTY  
TRANSACTIONS**

**9 Months Ended  
Sep. 30, 2012**

[RELATED PARTY  
TRANSACTIONS](#)

[RELATED PARTY  
TRANSACTIONS](#)

**NOTE 15. RELATED PARTY TRANSACTIONS**

On January 17, 2012, a wholly owned subsidiary of AdCare entered into a Purchase and Sale Agreement with Gyman Properties, LLC to acquire a 141-bed skilled nursing facility located in Lonoke, Arkansas, known as Golden Years Manor, for an aggregate purchase price of \$6.5 million. Pursuant to the Purchase and Sale Agreement, we deposited approximately \$0.3 million into escrow to be held as earnest money. On May 9, 2012, AdCare assigned all of its rights under the Purchase and Sale Agreement to GL Nursing, LLC, an entity affiliated with Christopher Brogdon, AdCare's Vice Chairman and a beneficial owner of more than 10% of the common stock. GL Nursing, LLC has agreed to reimburse us the \$0.3 million deposit and all of our out-of-pocket costs relating to Golden Years Manor upon the closing of the acquisition, which occurred on May 31, 2012. The Company has recorded a receivable for this amount.

On June 4, 2012, a wholly owned subsidiary of AdCare entered into a Purchase Agreement with JRT Group Properties to acquire property comprising Building 1145 of the Offices at Hembree, a condominium, located in Roswell, Georgia for an aggregate purchase price of approximately \$1.1 million. The closing of the Hembree Purchase is expected to occur before the end of 2012. One member of JRT Group Properties is a non-officer employee of AdCare and another member of JRT Group Properties is the son of Christopher Brogdon, the Company's Vice Chairman. As previously disclosed in the Annual Report, AdCare leases the Hembree property for use as administrative offices.

On July 26, 2012, Hearth & Home of Ohio, Inc. ("Hearth & Home"), a wholly owned subsidiary of AdCare, entered into an Amendment with Christopher Brogdon, the Company's Vice Chairman, which amends that certain Option Agreement, as previously amended, between Hearth & Home and Mr. Brogdon, dated June 22, 2010, to extend the last date on which the option provided for thereby may be exercised from June 22, 2012 to June 22, 2013. Pursuant to the option agreement, AdCare has an exclusive and irrevocable option, exercisable until June 22, 2013 to purchase from Mr. Brogdon 100% of the issued and outstanding membership interests of Riverchase Village ADK, LLC ("Riverchase") for a purchase price of \$0.1 million. As previously disclosed, AdCare: (i) entered into a five-year management contract with Riverchase on June 22, 2010 to manage the 105-bed assisted living facility located in Hoover, Alabama, known as Riverchase Village; and (ii) guaranteed the repayment by Riverchase of certain bonds owing to The Medical Clinic Board of the City of Hoover.

On October 12, 2012, the Company executed an Assignment of Purchase and Sale Agreement in favor of Edwards Redeemer Property Holdings, LLC ("Edwards Redeemer") and ER Nursing, LLC (both indirect, wholly owned subsidiaries of the Company and, collectively, the "Edwards Assignees") pursuant to which AdCare assigned all of its right to purchase the Edwards Redeemer Nursing Center located in Oklahoma under that certain Purchase and Sale Agreement, dated May 5, 2011 and as subsequently amended and assigned. The Edwards Assignees have agreed to assume all obligations of the Company under the Purchase and Sale Agreement with respect to the Edwards Redeemer Nursing facility, including reimbursement for out-of-pocket costs. AdCare, the owner of all of the issued and outstanding membership interests of Edward Redeemer, also has executed a Membership Interest Power

pursuant to which it assigns all such interests to Chris Brogdon, the Company's Vice Chairman.

The Company also executed an Assignment of Purchase and Sale Agreement in favor of WP Oklahoma Nursing, LLC, an entity owned and controlled by Chris Brogdon, the Company's Vice Chairman, pursuant to which the Company assigns all of its right to purchase the Whispering Pines Nursing Center located in Oklahoma under the Purchase and Sale Agreement dated May 5, 2011 and as subsequently amended and assigned. WP Oklahoma Nursing, LLC has agreed to assume all obligations of AdCare under the Purchase and Sale Agreement with respect to the Whispering Pines Nursing Center facility. Related to this agreement, the Company has recorded a receivable of less than \$0.1 million.

**PROPERTY AND  
EQUIPMENT (Tables)**

**9 Months Ended  
Sep. 30, 2012**

**PROPERTY AND  
EQUIPMENT**

Schedule of property and  
equipment

<u>(Amounts in 000s)</u>	<u>Estimated Useful Lives (Years)</u>	<u>September 30, 2012</u>	<u>December 31, 2011</u>
Buildings and improvements	5-40	\$ 151,951	\$ 96,065
Equipment	2-10	12,776	7,108
Land	—	11,274	7,636
Computer related	2-10	2,573	2,414
Construction in process	—	811	77
		<u>179,385</u>	<u>113,300</u>
Less: accumulated depreciation expense		11,265	7,624
Less: accumulated amortization expense		1,412	533
Property and equipment, net		<u>\$ 166,708</u>	<u>\$ 105,143</u>

COMMITMENTS AND CONTINGENCIES (Details) (USD \$)	3 Months Ended	9 Months Ended	1 Months Ended	0 Months Ended		9 Months Ended	1 Months Ended			0 Months Ended	1 Months Ended	3 Months Ended	9 Months Ended				
	Jun. 30, 2012	Sep. 30, 2012 item	Dec. 31, 2011	Apr. 30, 2012 Oklahoma PSA Amendment Purchase Agreement item	Apr. 17, 2012 Oklahoma PSA Amendment Purchase Agreement	Sep. 27, 2012 Sumter Valley PSA Purchase Agreement	Jun. 04, 2012 Sumter Valley PSA Purchase Agreement	Sep. 30, 2012 Sumter Valley PSA Purchase Agreement	Apr. 27, 2012 Sumter Valley PSA Purchase Agreement item	Apr. 30, 2012 Sumter Valley PSA Purchase Agreement Promissory note item	Apr. 27, 2012 Sumter Valley PSA Purchase Agreement Promissory note	Aug. 09, 2012 Georgetown PSA item	Sep. 25, 2012 L.J.L. item	Jun. 30, 2012 Hembree Road Property PA Purchase Agreement Related party members of the seller item	Jun. 04, 2012 Hembree Road Property PA Purchase Agreement Related party members of the seller	Sep. 30, 2012 Settled litigation item	Sep. 30, 2012 Settled litigation item
<b>Commitments</b>																	
Number of lawsuits asserting breach of contract																	2
Settlement obligation																\$	\$
Non cash settlement gain																	1,000,000
Amount paid in settlement																	361,000
Remaining balance payment period																	1 year
Number of lawsuits settled																	3
Capacity of skilled nursing facility (in numbers of bed)								96			84	70					
Aggregate purchase price for acquiring the businesses	60,132,000								5,500,000		4,200,000	6,300,000		1,100,000			
Number of non-officer employee's that are members of the seller													1				
Amount deposited into escrow	812,000	3,172,000							100,000			100,000					
Cash payable as purchase consideration	15,577,000								5,300,000				800,000				
Number of skilled nursing facilities acquired	8		5														
Additional amount deposited into escrow to be held as earnest money					50,000												
Expected transaction closing period			60 days														
Earnest money escrow deposit			200,000			200,000	900,000						100,000				
Debt issued as purchase consideration	5,000,000										200,000		5,500,000				
Number of subsidiaries that issued debt										1							
Fixed interest rate (as a percent)											6.00%						
Maturity period											15 years						
Number of days for written notice to move closing date					14 days												
<b>Benefit Plans</b>																	
Estimated amount of obligation recorded	\$	100,000															

**RESTRICTED CASH AND  
INVESTMENTS (Details)**

**(USD \$)**

**Sep. 30, 2012 Dec. 31, 2011**

**In Thousands, unless  
otherwise specified**

**RESTRICTED CASH AND INVESTMENTS**

<u>HUD escrow deposits</u>	\$ 202	\$ 326
<u>Funds held in trust for residents</u>	21	45
<u>Principal and interest escrow</u>	247	
<u>Refundable escrow deposit</u>		500
<u>Collateral certificates of deposit</u>	2,355	1,012
<u>Total current portion</u>	2,825	1,883
<u>HUD reserve replacements</u>	1,157	1,130
<u>Reserves for capital improvements</u>	2,292	1,767
<u>Restricted investments for other debt obligations</u>	2,299	1,973
<u>Total noncurrent portion</u>	5,748	4,870
<u>Total restricted cash and investments</u>	\$ 8,573	\$ 6,753



<b>CONDENSED CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY (USD \$)</b>	<b>Total</b>	<b>Total Stockholders' Equity</b>	<b>Common Stock and Additional Paid-in Capital</b>	<b>Accumulated Noncontrolling Deficit</b>	<b>Interests</b>
<b>In Thousands, except Share data, unless otherwise specified</b>					
<a href="#"><u>Balance at Dec. 31, 2011</u></a>	\$ 15,493	\$ 16,334	\$ 35,047	\$ (18,713)	\$ (841)
<a href="#"><u>Balance (in shares) at Dec. 31, 2011</u></a>	12,802,000		12,802,000		
<b><a href="#"><u>Increase (Decrease) in Stockholders' Equity</u></a></b>					
<a href="#"><u>Common stock dividend adjustment (in shares)</u></a>			88,000		
<a href="#"><u>Nonemployee warrants for services</u></a>	441	441	441		
<a href="#"><u>Stock based compensation expense</u></a>	615	615	615		
<a href="#"><u>Public stock offering, net</u></a>	3,837	3,837	3,837		
<a href="#"><u>Public stock offering, net (in shares)</u></a>			1,165,000		
<a href="#"><u>Exercises of options and warrants</u></a>	137	137	137		
<a href="#"><u>Exercises of options and warrants (in shares)</u></a>			95,000		
<a href="#"><u>Stock issued in acquisition</u></a>	750	750	750		
<a href="#"><u>Stock issued in acquisition (in shares)</u></a>			187,000		
<a href="#"><u>Issuance of restricted stock</u></a>	175	175	175		
<a href="#"><u>Issuance of restricted stock (in shares)</u></a>			320,000		
<a href="#"><u>Net loss</u></a>	(2,620)	(1,230)		(1,230)	(1,390)
<a href="#"><u>Balance at Sep. 30, 2012</u></a>	\$ 18,828	\$ 21,059	\$ 41,002	\$ (19,943)	\$ (2,231)
<a href="#"><u>Balance (in shares) at Sep. 30, 2012</u></a>	14,657,000		14,657,000		

## SEGMENTS

**9 Months Ended  
Sep. 30, 2012**

[SEGMENTS](#)  
[SEGMENTS](#)

### NOTE 4. SEGMENTS

The Company reports its operations in three segments: Skilled Nursing Facility (“SNF”), Assisted Living Facility (“ALF”), and Corporate & Other. The SNF and ALF segments provide services to individuals needing long-term care in a nursing home or assisted living setting, and the management of those facilities. The Corporate & Other segment engages in the management of facilities and accounting and IT services. We evaluate financial performance and allocate resources primarily based upon segment operating income (loss). Segment operating results excludes interest expense and other non-operating income and expenses. The table below sets forth our segment information for the three and nine months ended September 30, 2012 and 2011.

(Amounts in 000s)	SNF	ALF	Corporate & Other	Eliminations	Total
<b>Three months ended September 30, 2012</b>					
Net revenues	\$ 57,978	\$ 3,364	\$ 3,505	\$ (3,077)	\$ 61,770
Cost of services	49,812	2,441	(12)	(3,077)	49,164
General and administrative	—	—	4,328	—	4,328
Facility rent expense	2,039	—	41	—	2,080
Depreciation and amortization	1,590	224	298	—	2,112
Salary retirement and continuation costs	—	—	38	—	38
Operating income/(loss)	<u>\$ 4,537</u>	<u>\$ 699</u>	<u>\$ (1,188)</u>	<u>\$ —</u>	<u>\$ 4,048</u>
<b>Three months ended September 30, 2011</b>					
Net revenues	\$ 37,729	\$ 2,463	\$ 2,349	\$ (2,019)	\$ 40,522
Cost of services	32,887	1,885	(116)	(2,019)	32,637
General and administrative	—	—	3,267	—	3,267
Facility rent expense	1,906	—	31	—	1,937
Depreciation and amortization	631	158	47	—	836
Operating income/(loss)	<u>\$ 2,305</u>	<u>\$ 420</u>	<u>\$ (880)</u>	<u>\$ —</u>	<u>\$ 1,845</u>
<b>Nine months ended September 30, 2012</b>					
Net revenues	\$ 155,753	\$ 10,038	\$ 9,487	\$ (8,331)	\$ 166,947
Cost of services	132,582	7,362	(99)	(8,331)	131,514
General and administrative	—	—	13,188	—	13,188
Facility rent expense	6,065	—	131	—	6,196
Depreciation and amortization	4,075	654	641	—	5,370
Salary retirement and continuation costs	—	—	38	—	38
Operating income/(loss)	<u>\$ 13,031</u>	<u>\$ 2,022</u>	<u>\$ (4,412)</u>	<u>\$ —</u>	<u>\$ 10,641</u>
Total assets	<u>\$ 169,546</u>	<u>\$ 29,181</u>	<u>\$ 38,164</u>	<u>\$ —</u>	<u>\$ 236,891</u>

**Nine months ended  
September 30, 2011**

Net revenues	\$ 97,382	\$ 7,214	\$ 7,646	\$ (6,334)	\$ 105,908
Cost of services	85,495	5,740	15	(6,334)	84,916
General and administrative	—	—	9,358	—	9,358
Facility rent expense	5,711	—	76	—	5,787
Depreciation and amortization	1,595	470	123	—	2,188
Salary retirement and continuation costs	—	—	622	—	622
Operating income/(loss)	<u>\$ 4,581</u>	<u>\$ 1,004</u>	<u>\$ (2,548)</u>	<u>\$ —</u>	<u>\$ 3,037</u>
Total assets	<u>\$ 105,620</u>	<u>\$ 21,490</u>	<u>\$ 31,176</u>	<u>\$ —</u>	<u>\$ 158,286</u>

**RESTRICTED CASH AND  
INVESTMENTS (Tables)**

**9 Months Ended  
Sep. 30, 2012**

**RESTRICTED CASH AND  
INVESTMENTS**

Schedule of restricted cash,  
escrow deposits and  
investments

<u>(Amounts in 000s)</u>	<u>September 30,</u> <u>2012</u>	<u>December 31,</u> <u>2011</u>
HUD escrow deposits	\$ 202	\$ 326
Funds held in trust for residents	21	45
Principal and interest escrow	247	—
Refundable escrow deposit	—	500
Collateral certificates of deposit	2,355	1,012
Total current portion	<u>2,825</u>	<u>1,883</u>
HUD reserve replacements	1,157	1,130
Reserves for capital improvements	2,292	1,767
Restricted investments for other debt obligations	2,299	1,973
Total noncurrent portion	<u>5,748</u>	<u>4,870</u>
<b>Total restricted cash and investments</b>	<b><u>\$ 8,573</u></b>	<b><u>\$ 6,753</u></b>

**DISCONTINUED  
OPERATIONS (Details)**  
(Home health business, USD  
\$)

**3 Months Ended 9 Months Ended**  
**Sep. 30, 2012 Sep. 30, 2012**  
**Maximum**

**DISCONTINUED OPERATIONS**

Percentage of total revenue

2.00%

Amount received from sale

\$ 50,000

## COMMITMENTS AND CONTINGENCIES

**9 Months Ended  
Sep. 30, 2012**

### COMMITMENTS AND CONTINGENCIES

### COMMITMENTS AND CONTINGENCIES

#### NOTE 14. COMMITMENTS AND CONTINGENCIES

##### *Legal Matters*

The skilled nursing and assisted living business involves a significant risk of liability given the age and health of the Company's patients and residents and the services the Company provides. The Company and others in the industry are subject to an increasing number of claims and lawsuits, including professional liability claims, which may allege that services have resulted in personal injury, elder abuse, wrongful death or other related claims. The defense of these lawsuits may result in significant legal costs, regardless of the outcome, and can result in large settlement amounts or damage awards.

In addition to the potential lawsuits and claims described above, the Company and others in the industry are also subject to potential lawsuits under the Federal False Claims Act and comparable state laws alleging submission of fraudulent claims for services to any healthcare program (such as Medicare) or payor. A violation may provide the basis for exclusion from federally-funded healthcare programs. As of September 30, 2012, the Company does not have any material loss contingencies recorded based on management's evaluation of the probability of loss from known claims.

In 2012, the Company was named as a defendant in two related lawsuits asserting breach of contract claims arising out of consulting agreements executed in 2010 in connection with the Company's becoming the operator of certain leased facilities that were previously operated by a third-party. The same transaction was already the subject of litigation commenced by the Company in 2011 against several entities which had previously operated the leased facilities. After becoming the operator of the lease facilities, the Company incurred certain losses for pre-closing activities for which the Company was entitled to indemnification. The Company sought to enforce its rights to indemnity by filing a lawsuit against the former operators of the leased facilities for breach of contract and related tort claims, and the Company proceeded to set off its losses against payment due under the consulting agreements referenced above. The defendants filed counterclaims against the Company. In the third quarter of 2012, a settlement was reached with respect to the three lawsuits that permitted the Company to eliminate a previously accrued liability in light of the lower than expected settlement amount of approximately \$1.0 million resulting in a non-cash settlement gain of approximately \$0.4 million recognized in the third quarter. During the third quarter, approximately \$0.3 million of the settlement was paid and the majority of the remaining balance will be paid within one year.

##### *Commitments*

##### Oklahoma (Harty) PSA Amendment

On April 17, 2012, a wholly owned subsidiary of AdCare amended the Purchase and Sale Agreement with First Commercial Bank to acquire five skilled nursing facilities located in Oklahoma. The amendment requires an additional deposit of \$50,000 into escrow to be used as earnest money; amends the closing date to the date which is sixty (60) days after all required licenses are received, but in no event later than September 30, 2012; and releases \$200,000 from escrow to First Commercial Bank. Upon the closing of the purchase, the Company shall receive a \$200,000 credit

against the purchase price; however, if the transaction fails to be consummated for any reason other than (i) default by First Commercial Bank; (ii) the failure of a condition to closing to be satisfied; or (iii) an event of casualty or condemnation, First Commercial Bank shall be entitled to retain the \$200,000 disbursed from escrow. If the transaction fails to be consummated for any reason other than as described in the preceding sentence, First Commercial Bank shall return the \$200,000 to the Company upon demand. (See Note 16).

#### Sumter Valley PSA

On April 27, 2012, a wholly owned subsidiary of AdCare entered into a Purchase and Sale Agreement with 1761 Pinewood Holdings, LLC to acquire a 96-bed skilled nursing facility located in Sumter, South Carolina for an aggregate purchase price of \$5.5 million. The purchase price consists of: (i) \$5.3 million cash consideration; and (ii) a \$0.2 million promissory note to be issued by one of AdCare's subsidiaries that shall bear interest at a fixed rate of 6% based on a 15-year amortization schedule. Pursuant to the purchase and sale agreement, as amended, the Company deposited \$0.1 million into escrow and delivered approximately \$0.2 million to the seller to be held as earnest money.

On September 27, 2012, under the Third Amendment to the Purchase and Sale Agreement, the closing date was extended to December 28, 2012, although, upon 14 days written notice by the Company, the closing day may be moved to the last business day of November 2012. The Company has paid approximately \$0.9 million in earnest money that will be credited against the purchase price at closing.

#### Georgetown PSA

On August 9, 2012, a wholly owned subsidiary of AdCare entered into a Purchase and Sale Agreement with Winyah Nursing Home, Inc. to acquire certain land, buildings, improvements, furniture, fixtures and equipment comprising an 84-bed skilled nursing facility known as Georgetown Healthcare & Rehabilitation Center located in Georgetown, South Carolina for an aggregate purchase price of \$4.2 million. The Company deposited \$0.1 million into escrow which will be refunded if an inspection of the facility is deemed unsatisfactory. The closing date is expected to be on or before November 30, 2012. (See Note 16).

#### Cabot PSA

On September 25, 2012, a wholly owned subsidiary of AdCare entered into a Purchase and Sale Agreement with John B. Montgomery and Michael Morton to acquire all the issued and outstanding membership interests of LJL Properties, LLC for an aggregate purchase price of \$6.3 million consisting of: (a) approximately \$0.8 million payable in cash; and (b) the assumption of indebtedness of LJL Properties, LLC in the original principle amount of approximately \$5.5 million subject to the terms and conditions of the Purchase and Sale Agreement. LJL Properties, LLC has applied for a Permit of Approval from the Arkansas Health Services Permit Agency permitting construction of a 70-bed nursing facility identified as Lonoke County Nursing and Rehab Center in Cabot, Arkansas. LJL Properties, LLC has caused the facility to be constructed with licensure of the new facility pending. AdCare has deposited \$0.1 million into escrow as earnest money. The closing is expected to occur on December 1, 2012 and the closing may be extended until December 15, 2012 with an additional payment of earnest money.

#### Hembree Road Property PA

On June 4, 2012, the Company entered into a purchase agreement with JRT Group Properties, LLC ("JRT Group Properties") to acquire property comprising Building

1145 of the Offices at Hembree, a condominium, located in Roswell, Georgia, for an aggregate purchase price of \$1.1 million. The lender which the Company anticipates using to finance this acquisition has received a third party appraisal with respect to the property which is consistent with the purchase price. One member of JRT Group Properties is a non-officer employee of the Company and another member of JRT is the son of Christopher Brogdon, the Company's Vice Chairman and Chief Acquisition officer.

#### Benefit Plans

In the second quarter of 2012, it was determined that the Company has potential obligations related to the Company sponsored 401(k) plan. The Company has recorded an obligation based on an estimated amount of approximately \$0.1 million. The Company is pursuing remedial actions under the Voluntary Correction Programs ("VCP"). The Internal Revenue Service and the Federal Department of Labor may not accept the Company's VCP proposal. Thus the obligation may be adjusted in the future. However, management does not believe the ultimate impact of the resolution will be material to its results of operations and expects this issue to be resolved before the end of 2012.