SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-K

(Mark One)

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

For the Fiscal Year Ended December 31, 2001

OR

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

Commission file number: 1-11314

LTC PROPERTIES, INC.

(Exact name of Registrant as specified in its charter)

MARYLAND **(State or other jurisdiction of incorporation or organization)**	**71-0720518** **(I.R.S. Employer Identification No.)**

300 Esplanade Drive, Suite 1860 Oxnard, California 93030
(Address of principal executive offices)

Registrant's telephone number, including area code: (805) 981-8655

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

Title of Stock	Name of each exchange on which registered
Common stock, $.01 Par Value	New York Stock Exchange
9.50% Series A Cumulative Preferred Stock, $.01 Par Value	New York Stock Exchange
9.00% Series B Cumulative Preferred Stock, $.01 Par Value	New York Stock Exchange
7.75% Convertible Subordinated Debentures due 2002	New York Stock Exchange

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

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

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

The aggregate market value of voting stock held by non-affiliates of the Company is approximately $110,654,000 as of February 28, 2002.

18,393,322
(Number of shares of common stock outstanding as of February 28, 2002)

Part III is incorporated by reference from the Company's definitive proxy statement for the Annual Meeting of Stockholders.

STATEMENT REGARDING FORWARD LOOKING DISCLOSURE

Certain information contained in this annual report includes statements that are not purely historical and are "forward looking statements" within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended, including statements regarding our expectations, beliefs, intentions or strategies regarding the future. All statements other than historical facts contained in this annual report are forward looking statements. These forward looking statements involve a number of risks and uncertainties. All forward looking statements included in this annual report are based on information available to us on the date hereof, and we assume no obligation to update such forward looking statements. Although we believe that the assumptions and expectations reflected in such forward looking statements are reasonable, no assurance can be given that such expectations will prove to have been correct. The actual results achieved by us may differ materially from any forward looking statements due to the risks and uncertainties of such statements. Exhibit 99 to this annual report contains a more comprehensive discussion of risks and uncertainties associated with our business.

Item 1. BUSINESS

General

LTC Properties, Inc., a health care real estate investment trust (a "REIT"), was organized on May 12, 1992 in the State of Maryland and commenced operations on August 25, 1992. We invest primarily in long-term care and other health care related facilities through mortgage loans, facility lease transactions and other investments. During 1998, we began making investments in the education industry by investing in private and charter schools from pre-school through eighth grade. Our primary objectives are to sustain and enhance stockholder equity value and provide current income for distribution to stockholders through real estate investments in long-term care facilities and other health care related facilities managed by experienced operators providing quality care. To meet these objectives, we attempt to invest in properties that provide opportunity for additional value and current returns to our stockholders and diversify our investment portfolio by geographic location, operator and form of investment.

In accordance with "plain English" guidelines provided by the Securities and Exchange Commission, whenever we refer to "our company" or to "us", or use the terms "we" or "our", we are referring to LTC Properties, Inc. and its subsidiaries.

We were organized to qualify, and intend to continue to qualify, as a REIT. So long as we qualify, with limited exceptions, we may deduct distributions, both preferred dividends and common dividends, to our stockholders from our taxable income. We have made distributions, and intend to continue to make distributions to our stockholders, in order to eliminate any federal tax liability.

Owned Properties. During 2001, we acquired six skilled nursing facilities with a total of 616 beds and four assisted living facilities with a total of 186 units from CLC Healthcare, Inc. (see Item 8. FINANCIAL STATEMENTS—*Note 8. CLC Healthcare, Inc., formerly LTC Healthcare, Inc.*) for a total purchase price (based upon independent appraisals) of $45.8 million subject to mortgage debt of approximately $33.0 million and minority interest of approximately $3.5 million. Of the mortgage debt assumed, $16.4 million was payable to REMIC pools originated by us and $16.6 million was payable to an unrelated third party. Additionally we purchased from an unrelated party, two assisted living facilities with a total of 222 units for a total purchase price including closing costs of $26.1 million subject to mortgage debt assumed of $17.9 million. These two facilities were acquired through transactions that did not require cash in 2001 as more fully explained in Item 7. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS. During 2001 we invested approximately $1.7 million in the expansion and improvement of existing properties. Mortgage loans with outstanding principal balances totaling $3.2 million that were secured by two long-term care facilities with 346 beds/units were converted into owned properties. As of

December 31, 2001, our investment in owned properties consisted of 71 skilled nursing facilities with a total of 8,431 beds, 89 assisted living facilities with a total of 4,222 units and one school in 24 states, representing a gross investment of approximately $496.1 million.

During the year ended December 31, 2001, we sold three skilled nursing facilities, three assisted living facilities and three schools for a total sales price of $34.3 million. Our gross investment in the properties before impairments and accumulated depreciation was $36.4 million and the net book value, after impairments and accumulated depreciation was $29.7 million. Net proceeds from the sales were $33.4 million and costs of sale were $0.2 million. We recognized one sale under the Installment Method as required by Statement of Financial Accounting Standards No. 66 and deferred a $0.3 million gain. These sales resulted in a net gain of approximately $3.2 million.

The majority of our long-term care facilities are leased to operators pursuant to long-term operating leases that generally have an initial term of 6 to 20 years and provide for increases in the rent based upon specified rate increases, increases in revenues over defined base periods, or increases based on consumer price indices. All leases are triple net leases that require the lessee to pay all taxes, insurance, maintenance and other costs of the facilities.

Mortgage Loans. As part of our strategy of making long-term investments in properties used in the provision of long-term health care services, we provide mortgage financing on such properties based on our established investment underwriting criteria. (See "*Investment and Other Policies*" in this Section.) We also provide construction loans that by their terms convert into purchase/lease transactions or permanent financing mortgage loans upon completion of construction. At December 31, 2001, we had 44 mortgage loans secured by first mortgages on 41 skilled nursing facilities with a total of 4,524 beds and eight assisted living residences with 369 units located in 21 states. At December 31, 2001, the mortgage loans had a weighted average interest rate of 11.23%, generally have 25-year amortization schedules, have balloon payments due from 2002 to 2018 and provide for certain facility fees. The majority of the mortgage loans provide for annual increases in the interest rate based upon a specified increase of 10 to 25 basis points.

We maintain a long-term investment interest in mortgages we originate either through the direct retention of the mortgages or through the retention of REMIC Certificates originated in our securitizations. We are a REIT and, as such, make our investments with the intent to hold them for long-term purposes. However, we may securitize a portion of our mortgage loan portfolio when a securitization provides us with the best available form of capital to fund additional long-term investments. In addition, we believe that the REMIC Certificates we retain from our securitizations provide our stockholders with a more diverse real estate investment while maintaining the returns we desire.

REMIC Certificates. We complete a securitization by transferring mortgage loans to a newly created Real Estate Mortgage Investment Conduit ("REMIC") that, in turn, issues mortgage pass-through certificates aggregating approximately the same amount. A portion of the REMIC Certificates are sold to third parties and a portion of the REMIC Certificates are retained by us. The REMIC Certificates we retain are subordinated in right of payment to the REMIC Certificates sold to third parties and a portion of the REMIC Certificates we retain are interest-only certificates which have no principal amount and entitle us to receive cash flows designated as interest. During the quarter ended September 30, 2001, our company sold certain REMIC Certificates with a net book value of approximately $19.0 million. The sale resulted in net proceeds of approximately $17.9 million and a realized loss of approximately $1.1 million. At December 31, 2001, we had investments in REMIC Certificates with a carrying value of $73.2 million ($74.3 million, at amortized cost, prior to any adjustment of available-for-sale certificates to fair market value).

Investment and Other Policies

Objectives and Policies. Our investment policy is to invest primarily in income-producing long-term care facilities. Five publicly held operators of long-term care facilities and one publicly held operator of assisted living facilities have filed for reorganization under Chapter 11 of the federal bankruptcy laws in the last three years. As a result of the significant financial difficulties experienced by these and other operators, we have made few investments in the last three years.

Historically our investments have consisted of:

- mortgage loans secured by long-term care facilities;
- fee ownership of long-term care facilities which are leased to operators; or
- participation in such investments indirectly through investments in real estate partnerships or other entities that themselves make direct investments in such loans or facilities.

In evaluating potential investments, we consider such factors as:

- type of property;
- the location;
- construction quality, condition and design of the property;
- the property's current and anticipated cash flow and its adequacy to meet operational needs and lease obligations or debt service obligations;
- the quality, reputation and solvency of the property's operator;
- the payor mix of private, Medicare and Medicaid patients;
- the growth, tax and regulatory environments of the communities in which the properties are located;
- the occupancy and demand for similar facilities in the area surrounding the property; and
- the Medicaid reimbursement policies and plans of the state in which the property is located.

For investments in long-term care facilities we place emphasis on facilities that have low investment per bed/unit ratios and do not have to rely on the provision of ancillary services to cover debt service or lease obligations. In addition, with respect to skilled nursing facilities, we attempt to invest in facilities that do not have to rely on a high percentage of private-pay patients. We seek to invest in facilities that are located in suburban and rural areas of states with improving reimbursement climates. Prior to every investment, we conduct a facility site review to assess the general physical condition of the facility, the potential of additional sub-acute services and the quality of care the operator provides. In addition, we review the environmental reports, state survey and financial statements of the facility before the investment is made. We prefer to invest in a facility that has a significant market presence in its community and where state certificate of need and/or licensing procedures limit the entry of competing facilities. We believe that assisted living facilities are an important sector in the long-term care market and our investments have included direct ownership of assisted living facilities. We believe that assisted living facilities represent a lower cost long-term care alternative for senior adults than skilled nursing facilities. We invest primarily in assisted living facilities that attract the moderate-income private pay patients in smaller communities, preferably in states that have adopted Medicaid waiver programs or are in the process of adopting or reviewing their policies and reimbursement programs to provide funding for assisted living residences. We believe that locating residences in a state with a favorable regulatory and reimbursement climate should provide a stable source of residents eligible for Medicaid reimbursement to the extent private-pay residents are not available, and should provide alternative sources of income for residents when their private funds are depleted and they become Medicaid eligible.

The terms of our existing revolving credit facility limit our investments outside of health care real estate to $20.0 million. There are no other formal restrictions imposed in our investment in any single type of property or joint venture; however, difficult capital market conditions in the health care industry have limited our access to traditional forms of growth capital. As a result of the tight capital markets for the health care industry, we reduced our investment activity in 2000 and 2001 and intend to continue to limit our investment activity in 2002. At December 31, 2001, we had no outstanding commitments to provide mortgage or sale/leaseback financing.

Borrowing Policies. We may incur additional indebtedness when, in the opinion of our Board of Directors, it is advisable. We may incur such indebtedness to make investments in additional long-term care facilities or to meet the distribution requirements imposed upon REITs under the Internal Revenue Code of 1986, as amended. For other short-term purposes, we may, from time to time, negotiate lines of credit, or arrange for other short-term borrowings from banks or otherwise. We may also arrange for long-term borrowings through public offerings or from institutional investors. To the extent that we receive net cash proceeds from such borrowings, the terms of our revolving credit facility require us to reduce the outstanding commitment and repay an equal amount of the net cash proceeds received from such borrowings on amounts outstanding under the revolver.

In addition, we may incur mortgage indebtedness on real estate which we have acquired through purchase, foreclosure or otherwise. We may also obtain mortgage financing for unleveraged or underleveraged properties in which we have invested or may refinance properties acquired on a leveraged basis. There is no limitation on the number or amount of mortgages that may be placed on any one property, and we have no policy with respect to limitations on borrowing, whether secured or unsecured.

Prohibited Investments and Activities. Our policies, which are subject to change by our Board of Directors without stockholder approval, impose certain prohibitions and restrictions on various of our investment practices or activities including prohibitions against:

- acquiring any real property unless the consideration paid for such real property is based on the fair market value of the property;
- investing in any junior mortgage loan unless by appraisal or other method, the Directors determine that

  (a) the capital invested in any such loan is adequately secured on the basis of the equity of the borrower in the property underlying such investment and the ability of the borrower to repay the mortgage loan; or

  (b) such loan is a financing device we enter into to establish the priority of our capital investment over the capital invested by others investing with us in a real estate project;
- investing in commodities or commodity futures contracts (other than interest rate futures, when used solely for hedging purposes);
- investing more than 1% of our total assets in contracts for sale of real estate unless such contracts are recordable in the chain of title;
- holding equity investments in unimproved, non-income producing real property, except such properties as are currently undergoing development or are presently intended to be developed within one year, together with mortgage loans on such property (other than first mortgage development loans), aggregating to more than 10% of our assets.

Competition

In the healthcare industry, we compete for real property investments with health care providers, other health care related REITs, real estate partnerships, banks, insurance companies and other investors. Many of our competitors are significantly larger and have greater financial resources and lower cost of capital than we have available to us. Our ability to compete successfully for real property investments will be determined by numerous factors, including our ability to identify suitable acquisition targets, our ability to negotiate acceptable terms for any such acquisition and the availability and cost of capital. Difficult capital market conditions for the health care industry have limited our access to traditional forms of growth capital. As a result of the tight capital markets for the health care industry, we reduced our investment activity in 2000 and 2001 and intend to continue to limit our investment activity in 2002.

The operators of our health care properties compete on a local, regional and, in some instances, national basis with other health care operators. The ability of our operators to compete successfully for patients at our facilities depends upon several factors, including the quality of care and services provided at the facilities, the operational reputation of the providers, physician referral patterns, physical appearances of the facilities, family preferences, financial condition of the operator and other competitive systems of health care delivery within the community, population and demographics.

Difficulties Experienced by Major Operators

The regulatory and reimbursement environments in which nursing homes operate have experienced significant adverse changes in recent years. Five publicly held operators of long-term care facilities and one publicly held operator of assisted living facilities have filed for reorganization under Chapter 11 of the federal bankruptcy laws in the past three years. See Item 7. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS for a discussion of Assisted Living Concepts, Inc. ("ALC"), Regent Assisted Living, Inc. ("Regent") and Alterra Healthcare Corporation ("Alterra"). Also see "*Governmental Regulation*" below. Given the negative impact of these changes on the financial performance of operators of nursing homes and assisted living facilities, we continually evaluate our real estate and marketable debt securities investment portfolios. As a result of our analyses, we recorded a non-cash impairment charge and costs of foreclosure and lease terminations on certain properties and securities in our real estate and marketable debt securities investment portfolios totaling approximately $28.6 (of which $17.3 million relates to our direct real estate investment portfolio) and $14.8 million, (of which $13.6 million relates to our direct real estate investment portfolio) respectively in 2001 and 2000. See "Item 8. FINANCIAL STATEMENTS —*Note 5. Impairment Charge*".

CLC Healthcare, Inc., formerly LTC Healthcare, Inc.

At LTC Healthcare Inc.'s annual meeting of stockholders held February 6, 2002, the stockholders approved a change in the name of LTC Healthcare, Inc. to CLC Healthcare, Inc. ("CLC").

During 1998, we completed the spin-off of all CLC voting common stock through a taxable dividend distribution to the holders of our common stock, Cumulative Convertible Series C Preferred Stock and Convertible Subordinated Debentures. Upon completion of the distribution, CLC began operating as a separate public company. Beginning in September 1999, CLC began operating skilled nursing facilities owned or financed by us and from that date through the current date, assumed operations of additional facilities and closed certain facilities on our behalf. We previously financed or leased these facilities to operators who experienced financial difficulties to such extent that the operators were not able to comply with lease provisions or debt provisions underlying the properties. As such, CLC primarily assumed operations for these properties that were in need of assistance. As a result CLC took over operations of troubled facilities and was not able to pay, nor did we record as income, rent under its leases or interest on its line of credit with us in 2001.

Pursuant to an intercompany agreement entered into at the time CLC was formed, CLC has agreed not to engage in activities or make investments that involve real estate, unless it has first provided us with written notice of the material terms and conditions of such activities or investments, and we have determined not to pursue such activities or investments either by providing written notice to CLC rejecting the opportunity or by allowing a 10-day notice period to lapse. Pursuant to the intercompany agreement, we also agreed to notify each other of, and make available to each other, investment opportunities that either company develops or of which either company becomes aware but are unable or unwilling to pursue. The intercompany agreement has a term of 10 years but shall terminate earlier upon a change of control of our company.

As of December 31, 2001, 24 of our skilled nursing facilities, which represents approximately 9.8%, or $58.2 million (including impairments totaling $3.0 million on three facilities) of our direct real estate investment portfolio were leased to CLC. Rents under these leases totaled approximately $3.1 million, annually. These leases were cancelled and replaced with new leases in January 2002 as more fully discussed below. In addition, CLC operates one skilled nursing facility securing a mortgage loan payable to a REMIC pool originated by us.

Subsequent to December 31, 2001, we sold to an unrelated party, two properties in Illinois operated by CLC. CLC will continue to operate these facilities until the new owner obtains a license and regulatory approval. Additionally, subsequent to December 31, 2001, we agreed to sell a wholly owned subsidiary, LTC-Fort Tucum, Inc. to CLC for a $0.5 million note bearing no interest for one year and thereafter interest at 8% annually for two years. CLC has certain rights to extend the note at its maturity. LTC-Fort Tucum, now owned by CLC, has acquired two skilled nursing facilities in New Mexico, previously owned by an unrelated third party and operated by Integrated Health Services, Inc., in a deed-in-lieu of foreclosure transaction. These properties are financed with debt from a REMIC pool originated by us. CLC expects to begin operating the two facilities during the second quarter of 2002. Additionally, in January 2002, we acquired from an unrelated third party a skilled nursing facility in Texas operated by CLC through the assumption of a $1.4 million mortgage loan payable to a REMIC pool originated by us and a cash payment of $0.5 million.

As a result of the subsequent events, we lease 23 facilities to CLC under individual six-year leases that provide for total rents of $3.0; $4.0; $4.8; $5.4; $5.9 and $6.5 million respectively, in years 2002 through 2007. The leases contain two five-year renewal options with increases of 2% annually. These leases have cross default provisions and a provision for acceleration should there be a change of control, as defined in the lease, of CLC. Additionally, CLC owns and operates the two New Mexico facilities discussed above which are financed with mortgage loans payable to a REMIC pool originated by us.

On November 21, 2001, we entered into a Securities Purchase Agreement with CLC pursuant to which we purchased from CLC $8.5 million face value of 7.5% convertible subordinated debentures of Regent for $7.8 million. The purchase price represented our estimate of the fair market value of the debentures. We purchased these debentures to add them with other Regent debentures we had acquired and to use the total debentures as part of the consideration necessary to acquire two assisted living facilities from Regent. The purchase price of $7.8 million was applied to reduce the total indebtedness owed by CLC to us. See Item 7. MANAGEMENTS' DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS—*Liquidity and Capital Resources*.

On December 17, 2001, our company entered into an Assignment and Assumption Agreement ("Agreement") with Healthcare Holdings, Inc. ("Holdings"), a wholly owned subsidiary of CLC, to sell to Holdings the right to receive common stock of ALC to be distributed pursuant to the First Amended Joint Plan of Reorganization of Assisted Living Concepts, Inc. and Carriage House Assisted Living, Inc. ("Plan"). The Plan was subsequently confirmed at a hearing on December 5, 2001.

On December 31, 2001, Holdings issued a Promissory Note ("Note") in accordance with the Agreement in the face amount of $7.0 million in payment for the right to receive 1,238,076 shares of ALC common stock distributed pursuant to the Plan (approximately $5.65 per share). The price of the shares was determined by reference to Exhibit G, Volume II of II of ALC's First Amended Joint Plan of Reorganization. This Exhibit G reported that the projected stockholders' equity of ALC upon emergence from bankruptcy to be $32.8 million and to be $37.1 million on December 31, 2002. ALC issued 6.5 million shares of new common stock at emergence which results in a calculated valuation of $5.05 and $5.71 per share value as of January 1, 2002 and December 31, 2002, respectively. The Note is for a term of five years and bears interest at 5.0%, compounded annually and accruing to the principal balance plus interest at 2.0% on the original principal of $7.0 million payable in cash annually. The Note is a full recourse obligation of Holdings and is secured by all of the assets owned now or in the future by Holdings and contains a provision for acceleration should there be a change of control of Holdings or CLC.

Prior to ALC's emergence from bankruptcy, Holdings owned $5.7 million face value of ALC's 5.625% convertible subordinated debentures and 30,847 shares of ALC's common stock. As a result of the Plan, Holdings received $1.4 million of ALC's new Senior Secured Notes bearing interest at 10.0% per annum, payable semi-annually in arrears; $0.5 million of new Junior Secured Notes bearing interest payable in additional new Junior Secured Notes for three years at 8.0% per annum and thereafter payable in cash at 12.0% per annum, payable semi-annually in arrears and 214,250 shares of ALC common stock. Additionally, Holdings received 468 shares of ALC common stock in exchange for the 30,847 shares owned prior to emergence. All of these securities are additional collateral for the $7.0 million note but have not been given value on our balance sheet. At December 31, 2001, the fair market value of these additional securities was approximately $2.1 million. At December 31, 2001, we recorded the Note at a value of approximately $3.1 million which represented only the then fair market value of the 1,238,076 shares acquired by Holdings pursuant to the Agreement.

On December 20, 2001, we entered into an agreement to acquire from CLC six skilled nursing facilities and four assisted living facilities. The total purchase price was approximately $45.8 million subject to mortgage debt assumed of approximately $33.0 million and minority interest of approximately $3.5 million. Of the mortgage debt assumed, $16.4 million was payable to REMIC pools originated by us and $16.6 million of mortgage debt was payable to an unrelated third party. Our company and CLC relied on current appraisals of the properties in establishing the purchase/sale price. The $9.3 million net proceeds from this transaction were used by CLC to reduce their total indebtedness to us.

Additionally, in December 2001, we agreed to forgive approximately $4.4 million in amounts owed by CLC to our company, which we had not recognized as income. This forgiveness was granted to compensate CLC for assuming operations and absorbing losses on certain facilities that our company and CLC agreed should be, and subsequently were, closed. This and the other transactions mentioned above reduced CLC's indebtedness to us under the line of credit to $5.3 million at December 31, 2001.

Cumulatively, the above transactions reduced CLC's indebtedness to us by approximately $21.5 million and will (not including recording interest income on the $7.0 million note) increase our rental income by approximately $5.6 million and net cash flow after debt service payments by approximately $1.3 million in 2002.

All of the aforementioned transactions between our company and CLC were approved by the respective disinterested and/or independent members of the Board of Directors of each company. All interested and/or non-independent Board members abstained from any such vote.

In February 2002, the independent members of CLC's Board of Directors approved, in principle, an Administrative Services Agreement between CLC and our company. This agreement would terminate on June 30, 2007 and provide that during its term, we will provide office space and certain management and administrative services to CLC for a fee of approximately $1.0 million per year beginning as of July 1, 2002. Currently, several of our Directors and Officers also serve as Directors and/or Officers of CLC.

In April 2001, our company's Board of Directors approved an indemnification agreement covering four of our company's officers who also serve as officers of CLC and one current CLC outside director.

We have provided CLC with a $20.0 million secured line of credit that bears interest at 10% and matures April 1, 2008. As of December 31, 2001, $5.3 million was outstanding under the line of credit. This agreement also contains a provision for acceleration should there be a change of control, as defined in the agreement, of CLC. Under the terms of our Senior Secured Revolving Line of Credit, we are permitted to loan CLC up to $25.0 million. We have not increased the $20.0 million secured line of credit between the companies. Should any such amendment be proposed, it would need approval of the independent Board members of each company's board.

While we believe that CLC has significantly improved the operations of the nursing facilities it operates, we will continue to record amounts due from CLC based on our evaluation of collectibility during 2002.

Employees

We currently employ 19 people.

Governmental Regulation

General. The operators of our skilled nursing facilities derive a substantial portion of their revenue from third party payors, including the Medicare and Medicaid programs. The Medicare program was enacted in 1965 to provide a nationwide, federally funded health insurance program for the elderly and certain disabled persons. The Medicaid program is a joint federal-state cooperative arrangement established for the purpose of enabling states to furnish medical assistance on behalf of aged, blind or disabled individuals, and members of families with dependent children, whose income and resources are insufficient to meet the costs of necessary medical services. Within the Medicare and Medicaid statutory framework, there are substantial areas subject to administrative regulations and rulings, interpretation and discretion which may affect payments made to providers under these programs. The amounts of program payments received by our operators can be changed by legislative or regulatory actions and by determinations made by fiscal intermediaries and other payment agents acting on behalf of the programs.

Cost Based Reimbursement. The Medicare program historically utilized a cost-based retrospective reimbursement system for skilled nursing facilities. These facilities were reimbursed for reasonable direct and indirect allowable costs incurred in providing “routine services” (as defined by the program and subject to certain limits) as well as capital costs and ancillary costs. Pursuant to the Balanced Budget Act of 1997 (the “Balanced Budget Act”) discussed below, Medicare phased in a prospective payment system (“PPS”) for skilled nursing facilities starting with cost reporting periods beginning on or after July 1, 1998.

Balanced Budget Act—Medicare. The Balanced Budget Act made numerous changes to the Medicare and Medicaid programs that affect operators of our health care properties. With respect to the Medicare program, the law required the Secretary of the Department of Health and Human Services (“HHS”) to establish a PPS system for Medicare Part A skilled nursing facility services, under which facilities are paid a federal per diem rate for virtually all covered services. Payment is determined by resource utilization groups (“RUGs”). The PPS system was phased in over three cost reporting periods, and started with cost reporting periods beginning on or after July 1, 1998. All facilities were paid at the full federal rate beginning October 1, 2001, fiscal year 2002, Subsequent legislation (see discussion below on the Balanced Budget Refinement Act and the Benefits Improvement and Protection Act of 2000) increased the per diem rate for certain higher-acuity patients. The Balanced Budget Act also instituted a consolidated billing requirement for skilled nursing facilities, under which such facilities must submit Medicare claims to the fiscal intermediary for all the Part A and Part B services that its residents receive, except for certain specifically excluded services (although this requirement subsequently was narrowed, as discussed below). Moreover, the law established: (1) a $1,500 per beneficiary annual cap for all outpatient physical therapy services and speech language pathology services; and (2) a $1,500 per beneficiary annual cap for all outpatient occupational therapy services.

All of our operators of skilled nursing facilities that participate in the Medicare program are operating under PPS. PPS has resulted in more intense price competition and lower margins for operators. There can be no assurance that operators will be successful in reducing costs of services below the PPS reimbursement rates, or that the failure of operators to do so will not have a material adverse effect on their liquidity, financial condition and results of operations which in turn could affect adversely their ability to make rental payments or mortgage payments to us.

Balanced Budget Refinement Act—Medicare. The Balanced Budget Refinement Act, enacted in November 1999, sought to mitigate some of the reductions in reimbursement to skilled nursing facilities under the Balanced Budget Act. The law temporarily increased the PPS per diem rates by 20% for 15 patient acuity categories. The increased payments began on April 1, 2000, and will end when the Centers for Medicare &

Medicaid Services ("CMS"), formerly the Health Care Financing Administration ("HCFA"), implements a refined RUG system that better accounts for medically-complex patients. The law also provided for a four percent increase in the federal per diem payment rates for all patient acuity categories for federal fiscal years 2001 and 2002. This increase is calculated exclusive of the 20% rate increase for the 15 acuity categories subject to direct adjustments. The 20% rate increase for medical complexity will not be built into the base payment rates, however, and therefore future updates to the federal payment rates will be calculated from the initial base rate. In addition to the per diem rate increases for certain patient categories, the Balanced Budget Refinement Act temporarily suspended for years 2000 and 2001 the reimbursement caps on Part B therapy services imposed by the Balanced Budget Act. The law also excluded certain additional items and services from the Part A skilled nursing facility consolidated billing requirement.

Benefits Improvement and Protection Act—Medicare. The Medicare, Medicaid and SCHIP Benefits Improvement and Protection Act of 2000, enacted in December 2000, included provisions designed to further mitigate the effects of reimbursement cuts contained in the Balanced Budget Act. Among other things, the Benefits Improvement and Protection Act eliminated the scheduled reduction in the skilled nursing facility market basket update in fiscal year 2001. This increase will not be included when determining payment rates for the subsequent period. In fiscal years 2002 and 2003, payment updates will equal the market basket index increase minus 0.5 percentage point. Temporary increases in the federal per diem rates under the Balanced Budget Refinement Act will be in addition to these payment increases. The Benefits Improvement and Protection Act also increased payment for the nursing component of each RUG by 16.66% for services furnished after April 1, 2001 and before October 1, 2002. Moreover, the Benefits Improvement and Protection Act further refined the consolidated billing requirements. The law now limits consolidated billing requirements to items and services furnished to skilled nursing facility residents in a Medicare Part A covered stay and therapy services covered under Part B. In other words, for residents not covered under a Part A stay, facilities may choose to bill for non-therapy Part B services and supplies, or they may elect to have suppliers continue to bill Medicare directly for these services. The Benefits Improvement and Protection Act also modified the treatment of the rehabilitation patient categories to ensure that Medicare payments for skilled nursing facility residents with "ultra high" and "high" rehabilitation therapy needs are appropriate in relation to payments for residents needing "medium" or "low" levels of therapy. Effective for services furnished on or after April 1, 2002 and before implementation of the refined RUG system (discussed above), the law increased by 6.7% the federal per diem payments for 14 rehabilitation categories. The 20% additional payment under the Balanced Budget Refinement Act for the three rehabilitation categories was removed to make this provision budget neutral. The Benefits Improvement and Protection Act also permits the Secretary of HHS to establish a process for geographic reclassification of skilled nursing facilities based upon the method used for inpatient hospitals. In addition, the law extends the moratorium on the physical therapy and occupational therapy payment caps for one year, through 2002.

Balanced Budget Act—Medicaid. The Balanced Budget Act also repealed the Boren Amendment, which required state Medicaid programs to reimburse nursing facilities for the costs that are incurred by efficiently and economically operated nursing homes. Since repeal, many states have sought to lower their nursing facility payment rates, and several have succeeded. It is unclear at this time the extent to which additional state Medicaid programs will adopt changes in their Medicaid reimbursement systems, or, if adopted and implemented, what effect such initiatives would have on operators. There can be no assurance that future changes in Medicaid reimbursement rates to nursing facilities will not have an adverse effect on the operators, and thus, us. Further, the Balanced Budget Act allows states to mandate enrollment in managed care systems without seeking approval from HHS for waivers from certain Medicaid requirements as long as certain standards are met. These managed care programs have historically exempted institutional care although some states have instituted pilot programs to provide such care under managed care programs. We are not able to predict whether any states' waiver provisions will change the Medicaid reimbursement systems for long-term care facilities from cost-based or fee- for-service to managed care negotiated or capitated rates or otherwise affect the level of payments to operators. Significant limits on the scope of services reimbursed and on rates of reimbursement under the Medicaid program could have a material adverse effect on the operators' liquidity, financial condition and results of operations, which in turn could affect adversely their ability to make rental payments or mortgage payments to us.

On January 12, 2001, the Secretary of HHS issued final regulations to implement changes to the Medicaid “upper payment limit” requirements and additional restrictions were issued January 18, 2002. The purpose of the rule is to stop states from using certain accounting techniques to inappropriately obtain extra federal Medicaid matching funds that are not necessarily spent on health care services for Medicaid beneficiaries. Although the rule will be phased in over eight years to reduce the adverse impact on certain states, the rule eventually could result in decreased federal funding to state Medicaid programs, which, in turn, could prompt certain states to reduce Medicaid reimbursements to providers, including nursing facilities.

Future Legislative Changes. We expect Congress to continue to consider measures to reduce the growth in Medicare and Medicaid expenditures. Certain of the increases in Medicare reimbursement for skilled nursing facilities provided for under the Balanced Budget Refinement Act and the Benefits Improvement and Protection Act will sunset in October 2002. Unless Congress enacts additional legislation, the loss of revenues associated with this occurrence could have a material adverse effect on our operators, and on us. While we are hopeful that Congress will act in a timely fashion, no assurances can be given as to whether Congress will take action, the timing of any action, or the form of any relief enacted. In addition, in January 2002, the Medicare Payment Advisory Commission (“MedPAC”), an independent federal body established to advise Congress on issues affecting the Medicare program, met to discuss draft recommendations that will be included in MedPAC’s March 2002 report to Congress. In this meeting, MedPAC recommended that Congress provide no payment update to free-standing skilled nursing facilities, and to provide a market basket update plus a 10% increase in payments to hospital-based facilities. MedPAC did recommend, however, that the 6.7% increase in the federal per diem payments for 14 rehabilitation categories and the 20% additional payment under the Balanced Budget Refinement Act for three rehabilitation categories, be incorporated into the base rate. While the MedPAC recommendations are not binding on Congress, they may affect whether a legislation action to extend the reimbursement provisions is successful.

Both the Medicare and Medicaid programs are subject to statutory and regulatory changes, administrative rulings, interpretations of policy, intermediary determinations and governmental funding restrictions, all of which may materially increase or decrease the rate of program reimbursement to health care facilities. We cannot predict at this time whether any additional measures will be adopted or if adopted and implemented, what effect such proposals would have on operators of our health care properties. There can be no assurance that payments under state and federal governmental programs will remain at levels comparable to present levels or will be sufficient to cover the costs of patients eligible for reimbursement pursuant to the programs.

Certain states are currently evaluating various proposals to restructure health care delivery within their respective jurisdictions. It is uncertain at this time what legislation of this type will ultimately be enacted and implemented or whether other changes in the administration or interpretation of governmental health care programs will occur. We anticipate that state legislatures will continue to review and assess various health care reform proposals and alternative health care systems and payment methodologies. We are unable to predict the ultimate impact of any future state restructuring of the health care delivery system, but such changes could have a material adverse effect on the operators’ liquidity, financial condition and results of operations, which in turn could affect adversely their ability to comply with the terms of the leases or loans, including making rental payments or mortgage payments to us.

Licensure. Our health care properties are subject to extensive state and local laws and regulations relating to licensure, conduct of operations, ownership of facilities, and services provided within the facilities. The nursing facilities of our operators are subject to regulation and licensing by state and local health and social services agencies and other regulatory authorities. In order to maintain their operating licenses, health care facilities must comply with standards concerning medical care, equipment and hygiene. Although regulatory requirements vary from state to state, these requirements generally address among other things: personnel education and training; staffing levels; patient records; facility services; quality of care provided; physical residence specifications; food and housekeeping services; and residents’ rights and responsibilities. These facilities are subject to periodic survey and inspection by governmental authorities. Our facilities are also subject to various state and local building codes and other ordinances, including zoning and safety codes.

Certificate of Need. Certificate of Need ("CON") statutes and regulations control the development and expansion of health care services and facilities in certain states. The CON process is intended to promote quality health care and to avoid the unnecessary duplication of services, equipment and facilities. CON or similar laws generally require that approval be obtained from the designated state health planning agency for certain acquisitions and capital expenditures, and that such agency determine that a need exists prior to the expansion of existing facilities, construction of new facilities, addition of beds, acquisition of major items of equipment or introduction of new services. Additionally, several states have instituted moratoria on new CONs or the approval of new beds. CONs or other similar approvals may be required in connection with our future acquisitions and/or expansions. There can be no assurance that our operators or we will be able to obtain the CONs or other approvals necessary for any or all such projects.

Survey and Certification. Long-term care facilities must comply with certain requirements to participate either as a skilled nursing facility under Medicare or a nursing facility under Medicaid. Regulations promulgated pursuant to the Omnibus Budget Reconciliation Act of 1987 obligate facilities to demonstrate compliance with requirements relating to resident rights, resident assessment, quality of care, quality of life, physician services, nursing services, pharmacy services, dietary services, rehabilitation services, infection control, physical environment and administration. Regulations governing survey, certification, and enforcement procedures to be used by state and federal survey agencies to determine facilities' level of compliance with the participation requirements for Medicare and Medicaid were adopted by HCFA effective July 1, 1995. These regulations require that surveys focus on resident outcomes. They also state that all deviations from participation requirements will be considered deficiencies, but a facility may have certain minor deficiencies and be in substantial compliance with the regulations. The regulations identify various remedies that may be imposed against facilities and specify the categories of deficiencies for which they will be applied. These remedies include, but are not limited to: civil money penalties of up to $10,000 per day or "per instance"; facility closure and/or transfer of residents in emergencies; denial of payment for new or all admissions; directed plans of correction; and directed in-service training. Failure to comply with applicable requirements for participation may also result in termination of the provider's Medicare and Medicaid provider agreements. Termination of an operator's Medicare or Medicaid provider agreement could have a material adverse effect on the operator's liquidity, financial condition and results of operations, which, in turn, could affect adversely its ability to make rental payments or mortgage payments to us.

The Clinton administration implemented several initiatives designed to improve the quality of care in nursing homes and to reduce fraud in the Medicare program. These initiatives include tougher enforcement measures by state surveying authorities, empowering specialized contractors to track down Medicare scams and program waste, and the creation of a Medicare financial management team made up of 100 "fraud fighters" to be located in the offices of every Medicare contractor nationwide. More recently, in November 2001, the Bush Administration announced that CMS will begin a 5 state demonstration project to collect and publish nursing home quality information. The program eventually will be expanded nationwide.

Referral Restrictions and Fraud and Abuse. The Medicare and Medicaid anti-kickback statute, 42 U.S.C. § 1320a-7b(b), prohibits the knowing and willful solicitation or receipt of any remuneration "in return for" referring an individual, or for recommending or arranging for the purchase, lease, or ordering, of any item or service for which payment may be made under Medicare or a state health care program. In addition, the statute prohibits the offer or payment of remuneration "to induce" a person to refer an individual, or to recommend or arrange for the purchase, lease, or ordering of any item or service for which payment may be made under the Medicare or state health care programs. The statute and the so-called safe harbor regulations establish numerous exceptions by defining conduct, which are not subject to prosecution or other enforcement remedies. Violation of the anti-kickback statute could result in criminal conviction, as well as civil money penalties and exclusions.

The Ethics in Patient Referrals Act ("Stark I"), effective January 1, 1992, generally prohibits physicians from referring Medicare patients to clinical laboratories for testing if the referring physician (or a member of the physician's immediate family) has a "financial relationship," through ownership or compensation, with the laboratory. The Omnibus Budget Reconciliation Act of 1993 contains provisions commonly known as "Stark II" ("Stark II") expanding Stark I by prohibiting physicians from referring Medicare and Medicaid patients to an entity with which a physician has a "financial relationship" for the furnishing of certain items set forth in a list of "designated health services," including physical therapy, occupational therapy, home health services, and other services. Subject to certain exceptions, if such a financial relationship exists, the entity is generally prohibited from claiming payment for such services under the Medicare or Medicaid programs, and civil monetary penalties may be assessed for each prohibited claim submitted. On January 4, 2001, HCFA released the first part of the long-awaited Stark II final rule. This final rule is divided into two phases. Phase I focuses on the provisions related to prohibited referrals, the general exception to ownership and compensation arrangement prohibitions and the related definitions. Most of Phase I of the rulemaking became effective January 4, 2002, one year after the date of its publication in the *Federal Register*. Phase II of the final rule has not yet been released. Phase II will cover the remaining portions of the statute, including those pertaining to Medicaid. Phase I of the final rule eases certain of the restrictions in the proposed rule, including the criteria for qualifying as a group practice. The final rule also, among other things: conforms the supervision requirements to HCFA coverage and payment policies for the specific services; clarifies the definitions of designated health services and indirect financial relationships; and creates new exceptions for indirect compensation arrangements and compensation of faculties in academic medical centers.

Other provisions in the Social Security Act and in other federal and state laws authorize the imposition of penalties, including criminal and civil fines and exclusions from participation in Medicare and Medicaid, for false claims, improper billing and other offenses.

We are unable to predict the effect of future administrative or judicial interpretations of the laws discussed above, or whether other legislation or regulations on the federal or state level in any of these areas will be adopted, what form such legislation or regulations may take, or their impact on operators of our health care properties. We endeavor to structure our arrangements with our facilities' operators and others to comply with applicable regulatory requirements, but there can be no assurance that statutory or regulatory changes, or subsequent administrative rulings or interpretations, will not require us to modify or restructure certain arrangements, or that we will not be required to expend significant amounts to maintain compliance.

Health Information Practices. The Health Insurance Portability and Accountability Act of 1996 ("HIPAA") mandates, among other things, the adoption of standards for the exchange of electronic health information in an effort to encourage overall administrative simplification and enhance the effectiveness and efficiency of the health care industry. Among the standards that HHS will adopt pursuant to the Health Insurance Portability and Accountability Act are standards for the following:

- electronic transactions and code sets;
- unique identifiers for providers, employers, health plans and individuals;
- security and electronic signatures;
- privacy; and
- enforcement.

Although HIPAA was intended ultimately to reduce administrative expenses and burdens faced within the health care industry, we believe the law could initially bring about significant and, in some cases, costly changes. HHS has released two rules to date mandating the use of new standards with respect to certain health care transactions and health information. The first rule requires the use of uniform standards for common health care transactions, including health care claims information, plan eligibility, referral certification and authorization, claims status, plan enrollment and disenrollment, payment and remittance advice, plan premium payments and coordination of benefits.

Second, HHS has released new standards relating to the privacy of individually identifiable health information. These standards not only require our operators' compliance with rules governing the use and disclosure of protected health information, but they also require entities to impose those rules, by contract, on any business associate to whom such information is disclosed. Rules governing the security of health information have been proposed but have not yet been issued in final form.

HHS finalized the new transaction standards on August 17, 2000, and covered entities, such as our operators, will be required to comply with them by October 16, 2002. Congress passed legislation in December 2001 that delays for one year (October 16, 2003) the compliance date, but only for entities that submit a compliance plan to HHS by the original implementation deadline. The privacy standards were issued on December 28, 2000, and, after certain delays, became effective April 14, 2001, with a compliance date of April 14, 2003. The Bush Administration and Congress are taking a careful look at the existing regulations, but it is uncertain whether there will be additional changes to the privacy standards or their compliance date. With respect to the security regulation, once they are issued in final form, affected parties will have approximately two years to be fully compliant. Sanctions for failing to comply with HIPAA include criminal penalties and civil sanctions.

We believe the operators of our health care properties are aware of and should be evaluating the effect of HIPAA. We believe our operators cannot at this time estimate the cost of such compliance, nor estimate the cost of compliance with standards that have not yet been finalized. The new and proposed health information standards are likely to have a significant effect on the manner in which the operators of our health care properties handle health data and communicate with payors. However, based on our current knowledge, we cannot currently estimate the cost of compliance or if there will be a material adverse effect on our business, financial condition or results of operations as a result of our operators experiencing increased costs for compliance.

Compliance Program. On March 16, 2000, the Office of Inspector General of HHS ("OIG") issued guidance to help nursing facilities design effective voluntary compliance programs to prevent fraud, waste, and abuse in health care programs, including Medicare and Medicaid. The guidance, *Compliance Program Guidance for Nursing Facilities*, was published as a notice in the *Federal Register*.

Taxation of Our Company

General. We believe that we have been organized and have operated in such a manner as to qualify for taxation as a REIT under Sections 856 to 860 of the Internal Revenue Code of 1986, as amended, commencing with our taxable year ended December 31, 1992, and we intend to continue to operate in such a manner. No assurance can be given that we have operated or will be able to continue to operate in a manner so as to qualify or to remain so qualified. This summary is qualified in its entirety by the applicable Internal Revenue Code provisions, rules and regulations, and administrative and judicial interpretations.

If we qualify for taxation as a REIT, we will generally not be subject to federal corporate income taxes as long as we distribute all of our taxable income as dividends. This treatment substantially eliminates the "double taxation" (*i.e.*, at the corporate and stockholder levels) that generally results from investment in a corporation. However, we will continue to be subject to federal income tax under certain circumstances.

Requirements for Qualification. The Internal Revenue Code defines a REIT as a corporation, trust or association:

(1) which is managed by one or more trustees or directors;

(2) the beneficial ownership of which is evidenced by transferable shares, or by transferable certificates of beneficial interest;

(3) which would be taxable, but for Sections 856 through 860 of the Internal Revenue Code, as a domestic corporation;

(4) which is neither a financial institution; nor, an insurance company subject to certain provisions of the Internal Revenue Code;

(5) the beneficial ownership of which is held by 100 or more persons;

(6) during the last half of each taxable year not more than 50% in value of the outstanding stock of which is owned, actually or constructively, by five or fewer individuals (including specified entities); and

(7) which meets certain other tests, described below, regarding the amount of its distributions and the nature of its income and assets.

The Internal Revenue Code provides that conditions (1) to (4), inclusive, must be met during the entire taxable year and that condition (5) must be met during at least 335 days of a taxable year of 12 months, or during a proportionate part of a taxable year of less than 12 months.

Income Tests. There presently are two gross income requirements that we must satisfy to qualify as a REIT:

- First, at least 75% of our gross income (excluding gross income from "prohibited transactions," as defined below) for each taxable year must be derived directly or indirectly from investments relating to real property or mortgages on real property, including rents from real property, or from certain types of temporary investment income.

- Second, at least 95% of our gross income (excluding gross income from prohibited transactions) for each taxable year must be derived from income that qualifies under the 75% test or from dividends, interest and gain from the sale or other disposition of stock or securities.

Cancellation of indebtedness income generated by us is not taken into account in applying the 75% and 95% income tests discussed above. A "prohibited transaction" is a sale or other disposition of property (other than foreclosure property) held for sale to customers in the ordinary course of business. Any gain realized from a prohibited transaction is subject to a 100% penalty tax.

Asset Tests. We, at the close of each quarter of our taxable year, must also satisfy four tests relating to the nature of our assets.

- First, at least 75% of the value of our total assets must be represented by real estate assets (including stock or debt instruments held for not more than one year purchased with the proceeds of a stock offering or long-term (at least five years) public debt offering of our company), cash, cash items and government securities.

- Second, not more than 25% of our total assets may be represented by securities other than those in the 75% asset class.

- Third, of the investments included in the 25% asset class, the value of any one issuer's securities owned by us may not exceed 5% of the value of our total assets and we may not own more than 10% of any one issuer's outstanding voting securities.

- Fourth, the Tax Relief Extension Act of 1999 ("99 Act"), provides that, subject to certain exceptions, for taxable years commencing after December 31, 2000, we may not own more than 10% of the total value of the securities of any corporation. See the 99 Act description contained at page 17.

- Fifth, the "99 Act" also provides that not more than 20% of our value may be represented by securities of one or more taxable REIT subsidiaries.

Ownership of a Partnership Interest or Stock in a Corporation. We own interests in various partnerships. In the case of a REIT that is a partner in a partnership, Treasury regulations provide that for purposes of the REIT income and asset tests the REIT will be deemed to own its proportionate share of the assets of the partnership, and will be deemed to be entitled to the income of the partnership attributable to such share. The ownership of an interest in a partnership by a REIT may involve special tax risks, including the challenge by the Internal Revenue Service of the allocations of income and expense items of the partnership, which would affect the computation of taxable income of the REIT, and the status of the partnership as a partnership (as opposed to an association taxable as a corporation) for federal income tax purposes.

We also own interests in a number of subsidiaries which are intended to be treated as qualified real estate investment trust subsidiaries. The Internal Revenue Code provides that such subsidiaries will be ignored for federal income tax purposes and all assets, liabilities and items of income, deduction and credit of such subsidiaries will be treated as assets, liabilities and such items of our company.

If any partnership or qualified real estate investment trust subsidiary in which we own an interest were treated as a regular corporation (and not as a partnership or qualified real estate investment trust subsidiary) for federal income tax purposes, we would likely fail to satisfy the REIT asset test prohibiting a REIT from owning greater than 10% of the voting power of the stock or value of securities of any issuer, as described above, and would therefore fail to qualify as a REIT. We believe that each of the partnerships and subsidiaries in which we own an interest will be treated for tax purposes as a partnership or qualified real estate investment trust subsidiary, respectively, although no assurance can be given that the Internal Revenue Service will not successfully challenge the status of any such organization.

REMIC. A regular or residual interest in a REMIC will be treated as a real estate asset for purposes of the REIT asset tests, and income derived with respect to such interest will be treated as interest on an obligation secured by a mortgage on real property, assuming that at least 95% of the assets of the REMIC are real estate assets. If less than 95% of the assets of the REMIC are real estate assets, only a proportionate share of the assets of and income derived from the REMIC will be treated as qualifying under the REIT asset and income tests. All of our REMIC Certificates are secured by real estate assets, therefore we believe that our REMIC interests fully qualify for purposes of the REIT income and asset tests.

Annual Distribution Requirements. In order to qualify as a REIT, we are required to distribute dividends (other than capital gain dividends) to our stockholders annually in an amount at least equal to:

(1) the sum of:

(A) 90% (95% for taxable years ending prior to January 1, 2001) of our "real estate investment trust taxable income" (computed without regard to the dividends paid deduction and our net capital gain); and (B) 90% (95% for taxable years ending prior to January 1, 2001) of the net income, if any (after tax), from foreclosure property; minus

(2) the excess of certain items of non-cash income over 5% of our real estate investment trust taxable income.

These annual distributions must be paid in the taxable year to which they relate. Alternatively, they must be declared and payable to stockholders of record in either October, November, or December and paid during January of the following year. In addition, if we elect, the dividends may be declared before the due date of the tax return (including extensions) and paid on or before the first regular dividend payment date after such declaration, and we must specify the dollar amount in our tax returns.

Amounts distributed must not be preferential; that is, every stockholder of the class of stock with respect to which a distribution is made must be treated the same as every other stockholder of that class, and no class of stock may be treated otherwise than in accordance with its dividend rights as a class.

To the extent that we do not distribute all of our net long-term capital gain or distribute at least 90% (95% for taxable years ending prior to January 1, 2001), but less than 100%, of our "real estate investment trust taxable income," as adjusted, it will be subject to tax on such amounts at regular corporate tax rates. Furthermore, if we should fail to distribute during each calendar year (or, in the case of distributions with declaration and record dates in the last three months of the calendar year, by the end of the following January) at least the sum of:

(1) 85% of our real estate investment trust ordinary income for such year;

(2) 95% of our real estate investment trust capital gain income for such year; and

(3) any undistributed taxable income from prior periods;

we would be subject to a 4% excise tax on the excess of such required distributions over the amounts actually distributed. Any real estate investment trust taxable income and net capital gain on which this excise tax is imposed for any year is treated as an amount distributed during that year for purposes of calculating such tax.

Failure to Qualify. If we fail to qualify for taxation as a REIT in any taxable year, and certain relief provisions do not apply, we will be subject to tax (including any applicable alternative minimum tax) on our taxable income at regular corporate rates. Distributions to stockholders in any year in which we fail to qualify as a REIT will not be deductible by us, nor will any distributions be required to be made. Unless entitled to relief under specific statutory provisions, we will also be disqualified from taxation as a REIT for the four taxable years following the year during which qualification was lost. It is not possible to state whether in all circumstances we would be entitled to the statutory relief. Failure to qualify for even one year could substantially reduce distributions to stockholders and could result in our incurring substantial indebtedness (to the extent borrowings are feasible) or liquidating substantial investments in order to pay the resulting taxes.

99 Act. The 99 Act has made a number of substantial changes to the qualification and tax treatment of REITs. The REIT changes are generally effective for taxable years commencing after December 31, 2000. The following is a brief summary of certain of the significant REIT provisions contained in the 99 Act.

1) *Investment limitations and taxable REIT subsidiaries.* The 99 Act modifies the REIT asset test by adding a requirement that except for (I) "Safe Harbor Debt" and (II) the ownership of stock in "taxable REIT subsidiaries", a REIT can not own more than 10 % of the total value of the securities of any corporation ("10% Rule"). The 10% Rule becomes effective for taxable years commencing after December 31, 2000. "Safe Harbor debt" is non-contingent, non-convertible debt ("straight-debt") which satisfies one of the following three requirements: (a) the straight-debt is issued by an individual, or (b) all of the securities of the issuer owned by the REIT is "straight debt" or (c) the issuer is a partnership in which the REIT owns at least 20 % of its profits.

For a corporation to qualify as a taxable REIT subsidiary the following requirements must be satisfied.

(1) The REIT must own stock in the subsidiary corporation.

(2) Both the REIT and the subsidiary corporation must join in an election that the subsidiary corporation be treated as a "taxable REIT subsidiary" of the REIT.

(3) The subsidiary corporation can not directly or indirectly operate or manage a health care facility.

(4) The subsidiary corporation generally cannot provide to any person rights to any brand name under which hotels or health care facilities are operated.

A taxable REIT subsidiary can provide a limited amount of services to tenants of REIT property (even if such services were not considered customarily furnished in connection with the rental of real property) and can manage or operate properties, generally for third parties, without causing the rents received by the REIT from such parties not to be treated as rent from real properties. The rule that rents paid to a REIT do not qualify as rental from real property if the REIT owns more than 10% of the corporation paying the rent is modified by excepting rents paid by taxable REIT subsidiaries provided that 90% of the space is leased to third parties at comparable rents for comparable space.

Interest paid by a taxable REIT subsidiary to the related REIT is subject to the earnings stripping rules contained in Section 163(j) of the Code and therefore the taxable REIT subsidiary cannot deduct interest in any year that would exceed 50% of the subsidiary's adjusted gross income. If any amount of interest, rent, or other deductions of the taxable REIT subsidiary to be paid to the REIT is determined not to be at arm's length, an excise tax of 100% is imposed on the portion that is determined to be excessive. However, rent received by a REIT shall not fail to qualify as rents from real property by reason of the fact that all or any portion of such rent is redetermined for purposes of the excise tax.

The Act permits a REIT to own up to 100% of the stock of a "taxable REIT subsidiary". However, the value of all of the securities of taxable REIT subsidiaries owned by the REIT cannot exceed 20% of the value of the REIT's assets.

The 10% Rule generally will not apply to securities owned by a REIT on July 12, 1999 ("Transition Rule"). However, the Transition Rule would cease to apply to securities of a corporation if, after July 12, 1999, the REIT acquires additional securities of such corporation or if such corporation engages in a substantial new line of business, or acquires any substantial assets, other than in a reorganization or in a transaction qualifying under Section 1031 or 1033 of the Code.

2) *Ownership of health care facilities*. The 99 Act permits a REIT to own and operate a health care facility for at least two years, and treat it as permitted "foreclosure" property, if the facility is acquired by the termination or expiration of a lease of the property.

3) *REIT distribution requirements*. The 99 Act reduces the requirement that a REIT must distribute at least 95% of its income as deductible dividends to 90% of its income.

4) *Rents from personal property*. A REIT may treat rent from personal property as rent from real property so long as the rent from personal property does not exceed 15% of the total rent from both real and personal property for the taxable year. The Act provides that this determination will be made by comparing the fair market value of the personal property to the fair market value of the real and personal property.

State and local taxation. We may be subject to state or local taxation in various state or local jurisdictions, including those in which we transact business or reside. The state and local tax treatment of our company may not conform to the federal income tax consequences discussed above.

Item 2. PROPERTIES

Investment Portfolio

At December 31, 2001, our "direct real estate investment portfolio" (properties that we own or on which we hold promissory notes secured by first mortgages) consisted of investments in 112 skilled nursing facilities with 12,955 beds, 97 assisted living facilities with 4,591 units and one school in 30 states. We had approximately $496.1 million (before accumulated depreciation of $58.6 million) invested in facilities we own and lease to operators, approximately $94.9 million invested in mortgage loans (before allowance for doubtful accounts of $1.3 million), and investments in REMIC Certificates with a carrying value of approximately $73.2 million ($74.3 million at amortized cost, prior to any adjustment of available-for-sale certificates to fair market value).

Skilled nursing facilities provide restorative, rehabilitative and nursing care for people not requiring the more extensive and sophisticated treatment available at acute care hospitals. Many skilled nursing facilities provide ancillary services that include occupational, speech, physical, respiratory and IV therapies, as well as provide sub-acute care services which are paid either by the patient, the patient's family, or through federal Medicare or state Medicaid programs. Assisted living facilities serve elderly persons who require assistance with activities of daily living, but do not require the constant supervision skilled nursing facilities provide. Services are usually available 24-hours a day and include personal supervision and assistance with eating, bathing, grooming and administering medication. The facilities provide a combination of housing, supportive services, personalized assistance and health care designed to respond to individual needs.

The school in our real estate investment portfolio is a charter school. Charter schools provide an alternative to the traditional public school. Charter schools are generally autonomous entities authorized by the state or locality to conduct operations independent from the surrounding public school district. Laws vary by state, but generally charters are granted by state boards of education either directly or in conjunction with local school districts or public universities. Operators are granted charters to establish and operate schools based on the goals and objectives set forth in the charter. Upon receipt of a charter, schools receive an annuity from the state for each student enrolled.

Owned Properties. At December 31, 2001, we owned 71 skilled nursing facilities with a total of 8,431 beds, 89 assisted living facilities with a total of 4,222 units and one school in 24 states, representing a gross investment of approximately $496.1 million. The properties are leased pursuant to non-cancelable leases generally with an initial term of 6 to 20 years. The leases provide for a fixed minimum base rent during the initial and renewal periods. Most of the leases provide for annual fixed rent increases or increases based on consumer price indices over the term of the lease. In addition, certain of our leases provide for additional rent through revenue participation (as defined in the lease agreement) in incremental revenues generated by the facilities over a defined base period, effective at various times during the term of the lease. Each lease is a triple net lease which requires the lessee to pay additional charges including all taxes, insurance, assessments, maintenance and repair (capital and non-capital expenditures), and other costs necessary in the operation of the facility. Many of the leases contain renewal options and one contains a limited period option that permits the operator to purchase the facility.

The following table sets forth certain information regarding our owned properties as of December 31, 2001 (*dollar amounts in thousands*):

Location	No. of SNFs	No. of ALFs	No. of Schools	No. of Beds /Units(1)	Encumbrances(2)	Lease Term(3)	Current Investment	Current Annual Rent Payments
Alabama	8	1		912	$ 13,961	138	$ 29,288	$ 4,225
Arizona	5	3		1,282	20,600	76	48,355	4,652
California	1	4		476	17,926	127	40,057	3,211
Colorado	1	6		325	6,803	105	20,383	2,193
Florida	5	6		1,205	2,303	63	38,143	4,023
Georgia	6	1		654	8,809	19	13,605	1,166
Idaho		4		148		90	9,756	1,039
Illinois	3			308	2,508	33	8,871	998
Indiana		2		78		102	5,070	516
Iowa	7	1		645	9,084	29	16,059	882
Kansas	5	4		494	9,645	56	16,215	1,372
Nebraska		4		156		91	9,332	1,019
New Jersey		1	1	39		141	12,195	1,305
New Mexico	4	1		507	13,028	153	29,632	2,180
N. Carolina		5		210		84	13,096	1,411
Ohio		11		487	22,011	140	44,718	4,627
Oklahoma		6		221	4,595	68	12,315	1,252
Oregon	1	4		324	4,076	80	17,454	1,889
Pennsylvania		1		69	5,878	196	8,327	815
South Carolina		3		128		84	7,610	835
Tennessee	3			201		10	3,852	440
Texas	17	13		2,844	27,209	57	57,588	5,613
Virginia	3			443		16	9,244	341
Washington	2	8		497	9,790	134	24,959	2,680
TOTAL	71	89	1	12,653	$ 178,226(4)		$496,124(5)	$ 48,684

(1) Number of beds/units applies to skilled nursing facilities and assisted living residences only.

(2) In addition to these encumbrances, 12 skilled nursing facilities with 1,380 beds and 55 assisted living facilities with 2,477 units with a gross investment value of $189,417 are pledged as collateral for our Senior Secured Revolving Line of Credit.

(3) Weighted average remaining months in lease term.

(4) Consists of: i) $162,232 of non-recourse mortgages payable by our company secured by 42 skilled nursing facilities containing a total of 5,013 beds, 18 assisted living facilities with 961 units, ii) $7,265 of tax-exempt bonds secured by five assisted living facilities in Washington with 188 units, iii) $4,653 of non-recourse capital lease obligations on four assisted living facilities in Kansas with 134 units, and iv) $4,076 of multi-unit housing non-recourse tax-exempt revenue bonds on one assisted living facility in Oregon with 112 units. As of December 31, 2001 our company's gross investment in properties encumbered by mortgage loans, bonds and capital leases was $248,338.

(5) Of the total, $202,946 relates to investments in skilled nursing facilities, $283,908 relates to investments in assisted living facilities and $9,270 relates to an investment in a school.

Mortgage Loans. At December 31, 2001, we had 44 mortgage loans secured by first mortgages on 41 skilled nursing facilities with a total of 4,524 beds and eight assisted living residences with 369 units located in 21 states. At December 31, 2001, the mortgage loans had a weighted average interest rate of 11.23%, generally have 25-year amortization schedules, have balloon payments due from 2002 to 2018 and provide for certain facility fees. The majority of the mortgage loans provide for annual increases in the interest rate based upon a specified increase of 10 to 25 basis points.

The following table sets forth certain information regarding our mortgage loans as of December 31, 2001 (*dollar amounts in thousands*):

Location	No. of SNFs	No. of ALFs	No. of Beds /Units	Interest Rate %	Average Months to Maturity	Face Amount of Mortgage Loans	Current Amount of Mortgage Loans	Current Annual Debt Service(1)
Alabama	1		40	10.38	199	$ 500	$ 472	$ 60
Arizona	1		144	12.20	35	2,400	2,257	310
Arkansas	2		274	10.63–10.83	112	3,400	3,007	412
California	6		886	10.15–13.70	130	12,771	11,863	1,595
Colorado	3		263	11.75–13.42	50	6,600	6,304	834
Florida	5	1	582	10.25–13.50	68	16,690	14,185	1,387
Georgia	1		63	11.55	62	1,200	1,154	147
Illinois	1		120	9.96	76	1,950	1,879	212
Iowa	1	1	143	11.44–12.25	72	4,400	4,290	538
Missouri	1		90	9.26	198	1,500	1,390	165
Montana		1	34	11.67	142	2,346	2,311	282
Nebraska		4	163	10.53–11.44	82	10,911	10,688	1,277
Nevada	1		100	11.00	104	1,200	1,043	148
N. Carolina	1		101	12.50	3	2,100	1,973	290
Ohio	1		150	10.69	52	5,200	4,907	601
Oklahoma	1		161	11.53	115	1,300	1,170	166
S. Carolina	5		509	13.05	14	11,250	10,741	1,471
S. Dakota		1	34	11.44	88	2,346	2,316	273
Texas	5		611	10.65–13.38	129	7,095	6,677	918
Washington	4		310	11.70–12.25	106	4,500	4,203	580
Wisconsin	1		115	11.00	183	2,200	2,031	273
TOTAL	41	8	4,893			$ 101,859	$ 94,861(2)	$ 11,939

(1) Includes principal and interest payments.

(2) Of the total current principal balance, $74,025 and $20,836 relate to investments in skilled nursing facilities and assisted living facilities, respectively. All mortgage loans are pledged as collateral for our Senior Secured Revolving Line of Credit.

In general, the mortgage loans may not be prepaid except in the event of the sale of the collateral facility to a third party that is not affiliated with the borrower, although partial prepayments (including the prepayment premium) are often permitted where a mortgage loan is secured by more than one facility upon a sale of one or more, but not all, of the collateral facilities to a third party which is not an affiliate of the borrower. The terms of the mortgage loans generally impose a premium upon prepayment of the loans depending upon the period in which the prepayment occurs, whether such prepayment was permitted or required, and certain other conditions such as upon the sale of the facility under pre-existing purchase option, destruction or condemnation, or other circumstances as approved by us. On certain loans, such prepayment amount is based upon a percentage of the then outstanding balance of the loan, usually declining ratably each year. For other loans, the prepayment premium is based on a yield maintenance formula. In addition to a lien on the mortgaged property, the loans are generally secured by certain non-real estate assets of the facilities and contain certain other security provisions in the form of letters of credit, pledged collateral accounts, security deposits, cross-default and cross-collateralization features and certain guarantees.

REMIC Certificates. During the quarter ended September 30, 2001, our company sold certain REMIC Certificates with a net book value of approximately $19.0 million. The sale resulted in net proceeds of approximately $17.9 million and a realized loss of approximately $1.1 million. At December 31, 2001, we had investments in REMIC Certificates with a carrying value of $73.2 million ($74.3 million, at amortized cost, prior to any adjustment of available-for-sale certificates to fair market value).

These certificates are pledged as collateral for our Senior Secured Revolving Line of Credit. The REMIC Certificates we retain are subordinate in rank and right of payment to the REMIC Certificates sold to third-party investors and as such would bear the first risk of loss in the event of an impairment to any of the underlying mortgages. The REMIC Certificates are collateralized by four pools consisting of 115 first mortgage loans secured by 168 skilled nursing facilities with a total of 19,227 beds in 23 states. Each mortgage loan, all of which we originated, is evidenced by a promissory note and secured by a mortgage, deed of trust, or other similar instrument that creates a first mortgage lien on a fee simple estate in real property. The $334.4 million current principal amount of mortgage loans represented by the REMIC Certificates have a weighted average interest rate of approximately 11.18%, and scheduled maturities ranging from 2002 to 2028.

The following table sets forth certain information regarding the mortgage loans securing the REMIC Certificates as of December 31, 2001 (*dollar amounts in thousands*):

Location	Number of Facilities	Number of Beds	Original Principal Amount of Remaining Mortgage Loans	Current Principal Amount of Remaining Mortgage Loans(1)	Current Annual Debt Service
Alabama	9	1,189	$ 22,526	$ 21,151	$ 2,793
Arizona	5	955	26,018	24,233	2,903
California	22	2,433	46,645	34,577	5,118
Colorado	1	177	2,000	1,904	240
Connecticut	1	150	2,276	2,142	281
Florida	7	945	32,310	28,779	3,600
Georgia	12	1,318	27,272	25,640	3,387
Illinois	3	282	5,126	4,885	624
Iowa	11	810	16,731	16,273	1,922
Louisiana	1	127	1,600	1,471	204
Michigan	1	236	3,000	2,652	382
Mississippi	3	400	14,050	10,314	1,203
Missouri	6	645	10,989	10,367	1,330
Montana	6	547	15,508	14,699	1,816
Nebraska	6	573	10,014	9,382	1,228
New Mexico	8	673	20,833	19,183	2,212
N. Carolina	1	168	2,950	2,794	414
Ohio	2	150	4,100	3,381	485
Oklahoma	1	112	1,300	1,125	172
S. Dakota	1	50	585	551	67
Tennessee	6	550	16,827	15,989	2,086
Texas	51	6,448	86,241	78,575	10,263
Washington	4	289	4,583	4,328	555
TOTAL	168	19,227	$ 373,484	$ 334,395	$ 43,285

(1) Included in the balances of the mortgages underlying the REMIC Certificates are $91,824 of non-recourse mortgages payable by our subsidiaries. We originated these mortgages which were subsequently transferred to the REMIC. The properties and the mortgage debt are reflected in our balance sheet.

The mortgage loans underlying the REMIC Certificates generally have 25-year amortization schedules with final maturities due from 2002 to 2028, unless prepaid prior thereto. Contractual principal and interest distributions with respect to the $74.3 million amortized cost basis of REMIC Certificates (excluding unrealized losses on changes in estimated fair value of $1.1 million) we retained are subordinated to distributions of interest and principal with respect to the $270.6 million of REMIC Certificates held by third parties. Thus, based on the terms of the underlying mortgages and assuming no unscheduled prepayments occur nor are any maturities extended as a result of the inability of the borrow to refinance, scheduled principal distributions on the REMIC

Certificates we retained will commence in August 2003 with final distributions in April 2028. Distributions on any of the REMIC Certificates will depend, in large part, on the amount and timing of payments, collections, delinquencies and defaults with respect to the mortgage loans represented by the REMIC Certificates, including the exercise of certain purchase options under existing facility leases or the sale of the mortgaged properties. Each of the mortgage loans securing the REMIC Certificates contains similar prepayment and security provisions as our mortgage loans.

As part of the REMIC transactions discussed above, we serve as the sub-servicer and, in such capacity, are responsible for performing substantially all of the servicing duties relating to the mortgage loans represented by the REMIC Certificates. We receive monthly fees equal to a fixed percentage of the then outstanding mortgage loan balance in the REMIC, which in our opinion represent currently prevailing terms for similar transactions. In addition, we will act as the special servicer to restructure any mortgage loans in the REMIC that default.

At December 31, 2001, the REMIC Certificates we held had an effective interest rate of approximately 18.05% based on the expected future cash flows with no unscheduled prepayments.

Item 3. LEGAL PROCEEDINGS

From time to time, we are a party to various claims and lawsuits arising in the ordinary course of business, which in our opinion are not singularly or in the aggregate material to our results of operations or financial condition. The various claims and lawsuits may include matters involving general or professional liability which is the responsibility of our lessees and borrowers pursuant to insurance and indemnification provisions in the leases or loans. (See “Item 8. FINANCIAL STATEMENTS—*Note 13. Contingencies*”.)

Item 4. SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS

None.

Item 5. MARKET FOR THE COMPANY’S COMMON EQUITY AND RELATED STOCKHOLDER MATTERS

(a) Our common stock is listed on the New York Stock Exchange. Set forth below are the high and low reported sale prices for our common stock as reported on the NYSE.

	2001		2000	
	High	Low	High	Low
First Quarter	$ 4.875	$ 3.500	$ 9.375	$ 5.1875
Second Quarter	$ 5.150	$ 3.600	$ 7.750	$ 4.0000
Third Quarter	$ 5.390	$ 4.300	$ 6.375	$ 2.9375
Fourth Quarter	$ 6.740	$ 5.000	$ 4.500	$ 3.0625

(b) As of December 31, 2001 we had approximately 628 stockholders of record of our common stock.

(c) We declared total cash distributions on common stock as set forth below:

	2001	2000
First Quarter	$ .00	$ .29
Second Quarter	.00	.29
Third Quarter	.00	.29
Fourth Quarter	.00	.00
	$ 0.00	$ 0.87

In January 2002, we declared a $0.10 per common share dividend payable on March 29, 2002 to stockholders of record on March 22, 2002. We intend to distribute to our stockholders an amount at least sufficient to satisfy the distribution requirements of a REIT. Cash flows from operating activities available for distribution to stockholders will be derived primarily from interest and rental payments from our real estate investments. Provisions of our Senior Secured Revolving Line of Credit Agreement limit common and preferred cash dividends to no more than 110% of consolidated taxable income. All distributions will be made subject to approval of the Board of Directors and will depend on the earnings of our company, its financial condition and such other factors as the Board of Directors deem relevant. In order to qualify for the beneficial tax treatment accorded to REITs by Sections 856 through 860 of the Internal Revenue Code, we are required to make distributions to holders of our shares equal to at least 90% (95% for years ending prior to January 1, 2001) of our “REIT taxable income.”

Item 6. SELECTED FINANCIAL INFORMATION

The following table of selected financial information should be read in conjunction with our company’s financial statements and related notes thereto included elsewhere in this Annual Report on Form 10-K.

	2001	2002	1999	1998	1997
			(In thousands, except per share amounts)		
Operating Information:					
Revenues	$ 70,112	$ 87,130	$ 87,662	$ 89,391	$ 73,434
Expenses:					
Interest expense	21,910	27,426	21,836	22,267	23,795
Depreciation and amortization	13,866	15,259	13,483	12,561	9,132
Amortization of founders’ stock	—	—	—	—	31
Provision for loan losses	—	—	—	600	—
Minority interest	973	982	1,018	1,415	1,205
Impairment charge	28,584	14,822	14,939	—	1,866
Operating and other expenses	9,247	5,994	5,863	5,084	4,393
Total expenses	74,580	64,483	57,139	41,927	40,422
Other (loss) income	—	—	1,304	(6,797)	(48)
Gain on sale of real estate and other assets, net	1,560	8,990	—	9,926	2,799
Net (loss) income	(2,908)	31,637	31,827	50,593	35,763
Preferred dividends	(15,077)	(15,087)	(15,087)	(12,896)	(6,075)
Net (loss) income available to common stockholders	$ (17,985)	$ 16,550	$ 16,740	$ 37,697	$ 29,688
Per share Information:					
Basic net (loss) income	$ (0.75)	$ 0.63	$ 0.61	$ 1.390	$ 1.260
Diluted net (loss) income	$ (0.75)	$ 0.63	$ 0.61	$ 1.390	$ 1.250
Common Stock Distributions declared	$ 0.00	$ 0.87	$ 1.56	$ 1.535	$ 1.435
Balance Sheet Information:					
Real estate investments, net	$ 604,306	$ 622,428	$ 683,736	$ 663,996	$ 640,733
Total assets	648,568	676,585	721,811	689,814	656,664
Total debt	284,634	262,560	292,274	229,695	249,724
Total liabilities	294,785	272,546	303,300	237,900	259,378
Minority interest	13,404	9,912	9,894	10,514	11,159
Total stockholders’ equity	340,379	394,127	408,617	441,400	386,127
Other Information:					
Cash flows provided by operating activities	$ 43,852	$ 45,307	$ 60,785	$ 61,885	$ 43,230
Cash flows provided by (used in) investing activities	46,772	45,697	(48,156)	(51,529)	(150,800)
Cash flows provided by (used in) financing activities	(86,172)	(91,789)	(11,477)	(13,827)	109,396
Funds from operations	$ 25,358	$ 37,641	$ 45,162	$ 47,559	$ 38,735
Basic funds from operations per share	$ 1.06	$ 1.44	$ 1.65	$ 1.76	$ 1.65
Diluted funds from operations per share	$ 1.06	$ 1.44	$ 1.64	$ 1.71	$ 1.57

Item 7. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

Operating Results

Year ended December 31, 2001 compared to year ended December 31, 2000

Revenues for the year ended December 31, 2001 were $70.1 million compared to $87.1 million for the same period in 2000. Of the $17.0 million reduction, rental income decreased by $10.4 million. Approximately $5.9 million of the rental income decrease is related to facilities closed in 2001 and our non-accrual of rental income from facilities operated by CLC in 2001. (See Item 8. FINANCIAL STATEMENTS—*Note 8. CLC Healthcare, Inc., formerly LTC Healthcare, Inc."*) Assets sold in 2001 and 2000 represent a net decrease of $6.5 million, assets purchased in 2000 represented an increase of $1.8 million and "same store" rental income (rental income from properties owned for both twelve months ended December 31, 2001 and 2000) increased by $0.2 million.

Interest income from mortgage loans and notes receivable decreased by $2.4 million due to loan repayments in 2001 and 2000 and the non-accrual of interest income on the line of credit due from CLC.

Interest income from REMIC Certificates decreased by $1.7 million due to the sale of certain certificates in the third quarter of 2001 and due to the normal amortization of the related asset.

Interest and other income decreased by $2.4 million primarily as the result of non-accrual or accretion of interest on ALC convertible subordinated debentures (See "Item 8. FINANCIAL STATEMENTS—*Note 10. Marketable Debt Securities.*").

Interest expense is lower by $5.5 million from December 31, 2000 to December 31, 2001. Of this reduction, $1.0 million is due to our payment in January 2001 to retire all of the $11.8 million of 8.50% convertible subordinated debentures and $0.4 million is due to our payment in July 2001 to retire all of the $10.4 million of 8.25% convertible subordinated debentures. Additionally, as a result of lower balances due under our credit facility and the fact that our LIBOR based interest rate for the credit facility decreased during the year from a weighted average of 9.2150% at December 31, 2000 to 4.3225% at December 31, 2001, our company had a reduction in interest expense of $4.4 million associated with our credit facility. These reductions were partially offset by an increase in interest expense related to a full year's interest expense for non-recourse mortgages assumed for acquisitions in 2000.

Depreciation and amortization expense decreased as a result of assets sold in 2001 and 2000 (See "Item 8. FINANCIAL STATEMENTS—*Note 6. Real Estate Investments.*").

Our company performs periodic comprehensive evaluations of its investments. As a result, we determined certain investments in skilled nursing facilities and other assets had become impaired. During 2001 we recorded net impairments of $16.8 million for 14 skilled nursing facilities; $0.5 million in lease termination costs; $1.5 million on a note receivable and $9.8 million on ALC convertible subordinated debentures (See "Item 8. FINANCIAL STATEMENTS—*Note 5. Impairment Charge and Note 10. Marketable Securities.*"). The fair values were based on current appraisals or other third party opinions of value and other estimates of fair value such as estimated undiscounted future cash flows.

Operating and other expenses increased by $3.3 million primarily due to a $2.5 million reduction in director and officer loans and a $0.8 million increase in compensation expense. The $2.5 million reduction was non-cash. See "Item 8. FINANCIAL STATEMENTS—*Note 12. Stockholders' Equity.*"

During the year we sold three skilled nursing facilities, three assisted living facilities and three schools. These sales resulted in a net gain of approximately $3.2 million. Additionally, we sold certain REMIC Certificates with a net book value of approximately $19.0 million for $17.9 million which resulted in a $1.1 million loss. We also sold other miscellaneous assets during the year which resulted in an aggregate $0.5 million loss.

The year ended December 31, 2001 resulted in a net loss after preferred dividends of $18.0 million compared to a net income available to common stockholders of $16.6 for the same period in 2000. Excluding the impairment charges and gains on sales of assets from both years and the non-cash charge for director and officer loan reductions in 2001, net income available to common stockholders was $11.5 million for the year ended December 31, 2001 compared to $22.4 million for the year ended December 31, 2000. Also, comparatively, there were 26.0 million common shares outstanding at December 31, 2000 and 18.4 million outstanding at December 31, 2001.

Year ended December 31, 2000 compared to year ended December 31, 1999

Revenues for the year ended December 31, 2000 were $87.1 million compared to $87.7 million for the same period in 1999. The net decrease in revenues resulted from decreases in interest from mortgage loans and notes receivable of $4.5 million and interest income from REMIC Certificates of $0.7 million and other income of $0.2 million which was offset by increases in rental income of $4.9 million.

Rental income increased $4.9 million primarily as a result of the conversion of mortgage loans into owned properties and the acquisition of two properties. “Same store” rental income (rental income from properties owned for both twelve months ended December 31, 1999 and 2000) increased $0.3 million due to rental rate increases as provided for in the lease agreements, partially offset by reduced rental rates on properties leased to CLC. Interest income from mortgage loans and notes receivable decreased due to the conversion of mortgage loans into owned properties. Interest income from REMIC Certificates decreased due to the amortization of the related asset. Interest and other income decreased primarily as a result of certain one-time investment gains that were realized in the first half of 1999.

Interest expense increased due to higher average outstanding balances on the revolving line of credit combined with higher average interest rates and the assumption of two mortgage loans related to the acquisition of two properties.

Depreciation and amortization increased as a result of a larger average investment base in owned properties in 2000 as compared to 1999.

During 2000 and 1999, we performed a comprehensive evaluation of our real estate investment portfolio. As a result of recent adverse changes in the long-term care industry, we identified certain investments in skilled nursing facilities and certain other assets that we determined to be impaired. During 2000 and 1999, we recorded impairment charges of $14.8 million and $14.9 million, respectively. (See “Item 8. FINANCIAL STATEMENTS—*Note 5. Impairment Charge.*”)

During the year ended December 31, 2000, we sold 11 skilled nursing facilities, one assisted living facility and two schools. These sales resulted in a net gain of approximately $9.0 million.

During the year ended December 31, 1999, we repurchased an aggregate of $21.6 million face amount of our convertible subordinated debentures at a discount on the open market. A gain of $1.3 million on the repurchase is included in other non-operating income.

On January 1, 1999, in accordance with recently issued accounting standards, we reclassified our investment in REMIC Certificates from trading securities to available-for-sale and held-to-maturity securities. As a result of the change in accounting for REMIC Certificates, our company no longer recognizes the change in unrealized gains or losses in current period earnings.

Net income available to common stockholders decreased to $16.6 million for the year ended December 31, 2000 from $16.7 million for the same period in 1999. Excluding the impairment charge and gain on the sale of real estate assets recorded in 2000 and the impairment charge and the gain on the repurchase of convertible subordinated debentures recorded in 1999, net income available to common stockholders was $22.4 million for the year ended December 31, 2000 compared to $30.4 million for the year ended December 31, 1999.

Significant Accounting Policies

Impairments. Impairment losses are recorded when events or changes in circumstances indicate the asset is impaired and the estimated undiscounted cash flows to be generated by the asset are less than its carrying amount. Management assesses the impairment of properties individually and impairment losses are calculated as the excess of the carrying amount of the real estate over its fair value less cost to sell as per Financial Accounting Standard No. 121 "*Accounting for the Impairment of Long-Lived Assets and for Long-Lived Assets to be Disposed of"*. In determining fair value, we use current appraisals or other third party opinions of value and other estimates of fair value such as estimated undiscounted future cash flows.

Securitization Transactions. Our company is a REIT and, as such, makes its investments with the intent to hold them for long-term purposes. However, mortgage loans may be transferred to a Real Estate Mortgage Investment Conduit ("REMIC"), a qualifying special-purpose entity, when a securitization provides us with the best available form of capital to fund additional long-term investments. When contemplating a securitization, consideration is given to our current and expected future interest rate posture and liquidity and leverage position, as well as overall economic and financial market trends.

A securitization is completed in a two-step process. First, a wholly owned special-purpose bankruptcy remote corporation (the "REMIC Corp.") is formed and selected mortgage loans are sold to the REMIC Corp. without recourse. Second, the REMIC Corp. transfers the loans to a trust (the "REMIC Trust") in exchange for commercial mortgage pass-through certificates (the "REMIC Certificates") which represent beneficial ownership interests in the REMIC Trust assets (the underlying mortgage loans). Under this structure, the REMIC Trust is a qualifying special purpose entity from which the mortgages are isolated from the REMIC Corp. and our company. Holders of REMIC Certificates issued by the REMIC Trust have the right free of any conditional constraints to pledge or exchange those interests, and neither the REMIC Corp. or our company maintains effective control over the transferred assets (the mortgages). The REMIC Trust is administered by a third-party trustee solely for the benefit of the REMIC Certificate holders.

Under the securitization structure described above, we account for the transfer of the mortgages as a sale and any gain or loss is recorded in earnings. The gain or loss is equal to the excess or deficiency of the cash proceeds and fair market value of any subordinated certificates received when compared with the carrying value of the mortgages sold, net of any transaction costs incurred and any gains or losses associated with an underlying hedge. Subordinated certificates received by us are recorded at their fair value at the date of the transaction. We have no controlling interest in the REMIC since the majority of the beneficial ownership interests (in the form of REMIC Certificates) are sold to third-party investors. Consequently, the financial statements of the REMIC Trust are not consolidated with those of our company for financial reporting purposes.

REMIC Certificates retained by our company as consideration for the mortgages sold are accounted for at fair value. In determining fair value on the date of sale, management considers various factors including, pricing of the certificates sold relative to the certificates retained as evaluated by the underwriters, discount rates and applicable spreads at the time of issuance for similar securities (or adjustments thereto if no comparable securities are available), assumptions regarding prepayments including the weighted-average life of prepayable assets, if any, and estimates relating to potential realized credit losses.

The REMIC Certificates issued by the REMIC Trust include various levels of senior, subordinated, interest only and residual classes. The subordinated REMIC Certificates generally provide a level of credit enhancement to the senior REMIC Certificates. The senior REMIC Certificates (which historically have represented 66% of the total REMIC Certificates) are then sold to outside third-party investors through a private placement under Rule 144A of the Securities Act of 1933, as amended. The subordinated REMIC Certificates along with the cash proceeds from the sale of the senior REMIC Certificates are retained by the REMIC Corp. as consideration for the initial transfer of the mortgage loans to the REMIC Trust. Neither our company, nor the REMIC Corp. is obligated to purchase any of the REMIC Trust assets or assume any liabilities.

Description of the REMIC Certificates. REMIC Certificates represent beneficial ownership interests in the REMIC Trust and can be grouped into three categories; senior, subordinated and subordinated interest-only (“I/O”). The REMIC Certificates sold to third-party investors are the senior certificates and those retained by us are the subordinated certificates. The senior and the subordinated certificates have stated principal balances and stated interest rates (“pass-through rates”). The I/O REMIC Certificates have no stated principal but are entitled to interest distributions. Interest distributions on the I/O REMIC Certificates are typically based on the spread between the monthly interest received by the REMIC Trust on the underlying mortgage collateral and the monthly pass-through interest paid by the REMIC Trust on the outstanding pass-through rate REMIC Certificates. After payment of the pass-through interest on the outstanding REMIC Certificates and interest distributions on the I/O Certificates, the REMIC Trust distributes the balance of the payments received on the underlying mortgages as a distribution of principal. Interest and principal distributions are made in order of REMIC Certificate seniority. As such, to the extent there are defaults or unrecoverable losses on the underlying mortgages resulting in reduced cash flows, the subordinated certificates held by us would in general bear the first risk of loss. Management evaluates the realizability of expected future cash flows periodically. A permanent impairment would be recorded in current period earnings when management believes that it is likely that a portion of the underlying mortgage collateral would not be realized by the REMIC Trust.

In addition to the risk from credit losses, the I/O Certificates are also subject to prepayment risk, in that prepayments of the underlying mortgages reduce future interest payments of which a portion flows to the I/O Certificates, thus, reducing their effective yield. The Certificates’ fair values are estimated, in part, based on a spread over the applicable U.S Treasury rate, and consequently, are inversely affected by increases or decreases in such interest rates. There is no active market in these securities from which to readily determine their value. The estimated fair values of both classes of Certificates are subject to change based on the estimate of future prepayments and credit losses, as well as fluctuations in interest rates and market risk. Although we are required to report our REMIC Certificate investments available for sale at fair value, many of the factors considered in estimating their fair value are difficult to predict and are beyond the control of our company’s management, consequently, changes in the reported fair values may vary widely and may not be indicative of amounts immediately realizable if our company was forced to liquidate any of the Certificates.

On January 1, 1999, we adopted SFAS No. 134 “Accounting for Mortgage-Backed Securities Retained after the Securitization of Mortgage Loans Held for Sale by a Mortgage Banking Enterprise.” Upon adoption of SFAS No. 134, our company, based on our ability and intent to hold our investments in REMIC Certificates, transferred our I/O REMIC Certificates and certificates with an investment rating of “BB” or higher from the trading category to the available-for-sale category and our certificates with an investment rating of “B” or lower to the held-to-maturity category. The transfer was recorded at fair value on the date of the transfer.

Mortgage Loans Receivable. Historically, we have sold our mortgage loans solely in connection with our REMIC securitizations. We may, in the future sell a participation interest in certain mortgages. Since certain mortgage loans may be securitized or sold in the future, direct investments in mortgage loans are classified as held for sale and carried at the lower of cost or market. If the mortgage loans aggregate cost basis exceeds their aggregate market value, a valuation allowance is established and the resulting amount is included in the determination of net income. Changes in the valuation allowance are included in current period earnings. In determining the estimated market value for mortgage loans, our company considers estimated prices and yields, based in part on a spread over the applicable U.S. Treasury Note Rate, sought by qualified institutional buyers of the REMIC Certificates originated in our company’s securitizations.

Mortgage Servicing Rights. Our company sub-services mortgage loans that are collateral for REMIC Certificates issued in our securitization transactions for which we receive servicing fees, based on market rates for such services at the time the securitization is completed, equal to a fixed percentage of the outstanding principal on the collateral loans. A separate asset for servicing rights is not recognized since the servicing fees received only adequately compensate us for the cost of servicing the loans. The fair value of servicing rights for mortgage loans originated and retained by us are estimated based on the fees received for servicing mortgage loans that serve as collateral for REMIC Certificates. All costs to originate mortgage loans are allocated to the mortgage loans since the fair value of servicing rights only sufficiently covers the servicing costs.

Revenue Recognition. Interest income on mortgage loans and REMIC Certificates is recognized using the effective interest method. We follow a policy related to mortgage interest whereby we consider a loan to be non-performing after 60 days of non-payment of amounts due and do not recognize unpaid mortgage interest income from that loan until the amounts have been received. Base rents under operating leases are accrued as earned over the terms of the leases. The majority of our leases contain provisions for specified annual increases over the rents of the prior year and are generally computed in one of four ways depending on specific provisions of each lease: (i) a specified percentage increase over the prior year, generally 2%; (ii) the higher of (i) or a calculation based on the Consumer Price Index; (iii) as a percentage of facility net patient revenues in excess of base amounts or (iv) specific dollar increases. SEC Staff Bulletin No. 101 *Revenue Recognition in Financial Statements* (“SAB 101”) does not allow for the recognition of such revenue until all possible contingencies have been eliminated. We consider the operating history of the lessee and the general condition of the industry when evaluating whether all possible contingencies have been eliminated and have historically, and expect in the future, to not include contingent rents as income until received. Our company follows a policy related to rental income whereby our company considers a lease to be non-performing after 60 days of non-payment of amounts due and do not recognize unpaid rental income from that lease until the amounts have been received.

Federal Income Taxes. Our company qualifies as a REIT under the Internal Revenue Code of 1986, as amended and as such, no provision for Federal income taxes has been made. A REIT may deduct distributions to its stockholders from its taxable income. If at least 90% (95% for taxable years ending prior to January 1, 2001) of a REIT’s taxable income is distributed to its stockholders and it complies with other Internal Revenue Code requirements, a REIT generally is not subject to Federal income taxation.

For Federal tax purposes, depreciation is generally calculated at a rate of 3.6% based on the assets’ tax basis (which approximates cost) using the straight-line method over a period of 27.5 years. Earnings and profits, which determine the taxability of dividends to stockholders, differ from net income for financial statement purposes due to the treatment of certain interest income and expense items and depreciable lives and basis of assets under the Internal Revenue Code.

Liquidity and Capital Resources

During the year ended December 31, 2001, we had net cash provided by operating activities of $43.9 million. We invested $1.7 million for renovation of owned properties. We sold three skilled nursing facilities, three assisted living facilities and three schools for aggregated net proceeds of approximately $33.4 million including notes secured by the properties sold totaling approximately $8.5 million. These sales resulted in a net gain of approximately $3.2 million and the proceeds were used to reduce amounts due under our credit facility and to fund our tender offer completed in October 2001.

We sold certain REMIC Certificates with a net book value of approximately $19.0 million. The sale resulted in net proceeds of approximately $17.9 million and a realized loss of approximately $1.1 million. We used the proceeds from this sale to fund our tender offer completed in October 2001.

Principal payments of $9.3 million were received on mortgage loans receivable, including $8.0 million related to the early payoff of two loans. These amounts were used to reduce amounts due under our credit facility.

We made an investment of approximately $2.8 million in convertible subordinated debentures of ALC with a total face value of $10.7 million. The additional investment in the ALC debentures brought the total face value of our investment in ALC debentures to $30.5 million and cash investment including accreted interest to approximately $18.7 million. During the year we recorded an impairment charge of $9.8 million related to our investment in the ALC debentures and we recorded no interest accretion or interest income relating to these debentures in 2001. We lease 37 assisted living facilities to ALC. In October 2001, ALC filed for reorganization under Chapter 11 of the federal bankruptcy laws. The filing was pre-negotiated with sufficient debt holders to allow ALC to reorganize its debt and equity and emerge from bankruptcy as of 12:01 a.m. on January 1, 2002. The final order affirming the reorganization was made in December 2001, consequently we reflected the transactions as of December 31, 2001. We agreed to reduce total rents under the 37 leases by $0.9 million a year, beginning January 1, 2002, and received a lease rejection claim of $2.5 million for this concession. Under the provisions of ALC's Plan, we would have been entitled to receive, due to our ownership of the subordinated debentures and the lease rejection claim, $8.0 million of ALC's new Senior Secured Notes bearing interest at 10% per annum, payable semi-annually in arrears, $3.0 million of new Junior Secured Notes bearing interest payable in additional new Junior Secured Notes for three years at 8% and thereafter payable in cash at 12% per annum, payable semi-annually in arrears and 1,238,076 shares of ALC common stock. Provisions of the Revenue Code governing REITs prohibit REITs from owning debt and/or equity securities representing more than 10% of the value or voting power of any one issuer. Without qualifying as safe harbor debt, securities include the Senior Secured Notes and the Junior Secured Notes. In order to qualify as safe harbor debt and retain our REIT status, we were able to hold only such debt. For REIT income test purposes, provisions would also disqualify income from any entity in which a REIT owns 10% or more of the total combined voting power of all classes of stock or 10% or more of the total value of shares of all classes of a corporate tenant. And as a result, we could not own both ALC debt securities and ALC common stock. In December 2001, we entered into an Assignment and Assumption Agreement with Healthcare Holdings, Inc. ("Holdings"), a wholly owned subsidiary of CLC, to sell to Holdings the right to receive the common stock of ALC. On December 31, 2001, Holdings issued a Promissory Note ("Note") in accordance with the Agreement in the face amount of $7.0 million, approximately $5.65 per share. The price was determined by reference to Exhibit G. Volume II of II of ALC's First Amended Joint Plan of Reorganization. This Exhibit G reported that the projected stockholders' equity of ALC upon emergence from bankruptcy to be $32.8 million and to be $37.1 million on December 31, 2002. ALC issued 6.5 million shares of new common stock at emergence which results in a calculated valuation of $5.05 and $5.71 per share value as of January 1, 2002 and December 31, 2002, respectively. The Note is for a term of five years and bears interest at 5%, compounded annually and accruing to the principal balance plus interest at 2% on the original face of $7.0 million payable in cash annually. The Note is a full recourse obligation of Holdings and is secured by all of the assets owned now or in the future by Holdings. Holdings is also the owner of $1.4 million of ALC's new Senior Secured Notes, $0.5 million of ALC's new Junior Secured Notes and 214,718 shares of ALC's common stock. At December 31, 2001, the fair market value of these additional securities was approximately $2.1 million. All of these securities are additional collateral to the $7.0 million Note but have not been given value on our balance sheet. As a result, at December 31, 2001, we recorded this Note at a value of approximately $3.1 million which represented only the then fair market value of the 1,238,076 shares acquired by Holdings pursuant to the Agreement. At December 31, 2001, we recorded an investment in marketable debt securities of $8.8 million representing the estimated market value of our ownership of ALC's new Senior Secured Notes and new Junior Secured Notes. The estimate of fair value is based on recent quotes from a broker who trades in these securities.

During 2001 Regent announced that it had appointed financial advisors to evaluate strategic alternatives and had approached us about rent concessions on five assisted living facilities leased from us. During the third quarter of 2001, as a result of several uncured events of default, we terminated the five leases with Regent and released the facilities to another operator for comparable rents. We believed that Regent's financial problems would cause them to default under their 7.5% convertible subordinated debentures and we were aware that CLC owned $8.5 million face value of these debentures which were part of the security under the line of credit between us and CLC. In order to reduce our exposure with Regent, we entered into a Securities Purchase Agreement with CLC to purchase their Regent debentures for $7.8 million and this amount was applied to reduce the total indebtedness owed by CLC to us. Additionally we purchased Regent convertible subordinated debentures with an aggregate face value of $0.4 million from our Chairman, CEO and President, Mr. Andre C. Dimitriadis, another current officer and a former officer of our company. Mr. Dimitriadis owned $160,000 in face value and cost basis of the Regent debentures. At the request of the Audit Committee of the Board of Directors, Mr. Dimitriadis agreed to sell us his debentures for $1.00 in order to avoid any appearance of self-interest or impropriety in his recommending to the Board the purchase of these debentures. The other current officer and the former officer, neither a Board Member, received approximately $0.1 million in aggregate which represented 50% of the face value and cost basis of the debentures they owned. At this point, we owned 99% of Regent's convertible subordinated debentures. We then entered into an agreement with Regent to apply all of these debentures as part of the consideration necessary to acquire two assisted living centers from Regent. The total cost of these two facilities was approximately $26.1 million and was paid by assuming $17.9 million of non-recourse mortgage debt with a weighted average interest rate of 8.56% and tendering the debentures to Regent. We entered into a 10-year lease for these two facilities with the same operator that leased the other five facilities previously operated by Regent. The annual lease amount on these two facilities is $1.8 million in year one, increasing by $0.2 million in years two and three, by $0.1 million in years four and five and then by 2% each year thereafter. We no longer have any facilities operated by or financed with Regent nor do we own any Regent securities.

In December 2001, we entered into an agreement to acquire from CLC six skilled nursing facilities and four assisted living facilities. The total purchase price was approximately $45.8 million less non-recourse mortgage debt of approximately $33.0 million with a weighted average interest rate of 8.25% and minority interest of approximately $3.5 million. Of the mortgage debt assumed, $16.4 million was payable to REMIC pools originated by us and $16.6 million of mortgage debt was payable to an unrelated third party. Our company and CLC relied on current appraisals of the properties in establishing the purchase/sale price. The $9.3 million net proceeds from this transaction were used by CLC to reduce their total indebtedness to us. These properties will generate approximately $3.8 million in rental income before debt service costs of $3.0 million (of which $2.6 million is interest expense and $0.4 million is principal) resulting in $1.2 million in additional annual future earnings.

Additionally, in December 2001, we agreed to forgive approximately $4.4 million in amounts owed by CLC to us, which we had not recognized as income. This forgiveness was granted to compensate CLC for assuming operations and absorbing losses on certain facilities that our company and CLC agreed should be, and subsequently were, closed. This and the other transactions mentioned above reduced CLC's indebtedness to us under its line of credit to $5.3 million at December 31, 2001.

During 2001 we provided CLC with an additional $4.4 million in borrowings, net of repayments, under the $20.0 million secured line of credit that bears interest at 10% and matures April 1, 2008.

In the third quarter of 2001, we obtained an $11.5 non-recourse loan secured by first mortgages on two assisted living facilities. In addition, the loan is cross-defaulted and cross-collateralized with two skilled nursing facilities and one rehabilitation facility previously secured under a $6.5 loan by the same lender. In connection with consummation of this new loan, the $6.5 million loan was extended to June 30, 2005 and interest remained at Prime. The new loan provides for an option to draw an additional $0.5 million if certain facility lease coverages and debt service coverages are achieved. The interest rate on the new loan is 90 day LIBOR plus 400 basis points subject to an 8.0% floor. Monthly payments consist of regular interest and principal with a maturity date of June 30, 2005. We used the proceeds of this loan principally to reduce amounts due under our credit facility.

During 2001, we borrowed $50.0 million and repaid $64.0 million under our Senior Secured Revolving Line of Credit that expires on October 2, 2004 and bears interest between LIBOR plus 2.00% and LIBOR plus 3.00% depending on our leverage ratio. As of December 31, 2001 borrowings of $104.0 million bearing interest at LIBOR plus 2.25% were outstanding under this credit facility and we had reduced the commitment level from $185.0 million at inception to $120.0 million. Subsequent to December 31, 2001, we received two mortgage loan repayments totaling $3.4 million. Current provisions of the credit facility require us to apply 50% of the Net Cash Proceeds, as defined in the credit facility, to reduce outstanding commitments and as such, commitments were reduced to $118.3 million in February 2002. The credit facility provides for scheduled periodic commitment reductions specifically to $95.0 million as of October 1, 2002 and then $5.0 million at the beginning of each third month thereafter to $60.0 million due at maturity. The credit facility also requires us to pay an additional fee of 4% of the then available commitment level as of October 2, 2002. The scheduled commitment level as of October 2, 2002 is $95.0 million. In addition to the 4% fee payable on October 2, 2002, we must issue book value units to the lenders under our Secured Line of Credit that entitle them to a right to participate in any increase in our book value per common share (measured at September 30, 2004) in excess of our book value per common share at September 30, 2000, less $2.00 per share from such excess. We are required to issue 20,000 book value units for each $1.0 million of outstanding commitments at October 2, 2002. Our book value per common share at September 30, 2000 was $8.92, thus, our book value per common share at September 30, 2004 would have to be in excess of $10.92 in order for us to be obligated to pay any money to our lenders for their book value units. At December 31, 2001, our book value per common share was $9.53 and our outstanding commitments under our Secured Line of Credit were $120.0 million; however, we are required to reduce our commitments to $95.0 million on October 1, 2002. Assuming our outstanding commitments were $95.0 million on October 2, 2002, we would be required to issue to our lenders 1,900,000 book value units. We will still be obligated to pay lenders any amounts due them relating to the book value units as of September 30, 2004, even if we repay in full and terminate our secured Line of Credit after October 2, 2002. Under covenants contained in the credit agreement, we are required to maintain, among other things, at December 31, 2001: (i) a ratio of senior debt to tangible net equity of no more than 0.65 to 1.0; (ii) a ratio of funded debt to tangible net equity of no greater than 1.0 to 1.0; (iii) a minimum tangible net worth of at least $300.0 million; and (iv) a ratio of cash flow to interest expense of at least 1.5 to 1.0. Covenant (iii) decreases to a minimum of tangible net worth of at least $275.0 million when commitments drop to $100.0 million or less. We are in compliance with all covenants as of December 31, 2001.

At December 31, 2001 our weighted average interest rate under our credit facility was 4.3225%, down from 9.2150% at December 31, 2000 in step with Federal Reserve interest rate reductions.

In addition to commitment reduction obligations under our credit facility, we also have $11.1 million of mortgage loans that mature in 2002 and $2.4 million of 7.75% convertible subordinated debentures that matured and were paid in January 2002.

In January 2001 we paid $11.8 million to retire all of the 8.50% convertible subordinated debentures at maturity and in July 2001 we paid $10.4 million to retire all of the 8.25% convertible subordinated debentures at maturity. We used funds available under our credit facility and cash on hand to make these payments.

It is our intent to use all available cash to continue to meet our debt obligations as they become due and meet dividend requirements to maintain our REIT status and to continue repurchasing our shares when appropriate. During the year ended December 31, 2001, we repurchased and retired 7,588,196 shares of common stock for an aggregate purchase price of approximately $41.7 million, an average of $5.50 per share. Of the shares repurchased, 6,060,996 were purchased pursuant to a tender offer completed in October 2001 for 6,000,000 shares, plus up to 2% of outstanding shares as allowed by tender offer regulations, at $5.75 per share plus costs. The balance of 1,527,200 shares were purchased on the open market under a Board authorization to purchase up to 5,000,000 shares. Therefore, our company continues to have an open Board authorization to purchase an additional 3,472,800.

Also during 2001, we repurchased, on the open market, and retired 10,800 shares of Series A Preferred Stock and 7,000 shares of Series B Preferred Stock for a total of $0.3 million. Both the Series A Preferred Stock and Series B Preferred Stock are currently redeemable at the $25.00 liquidation value per share. We currently do not have the intention to redeem either the Series A or Series B Preferred Stock; however, we may buy, from time to time, shares of the Series A and/or B Preferred Stock in the open market.

During the same period, we declared and paid cash dividends on our Series A Preferred Stock, Series B Preferred Stock and Series C Preferred Stock totaling $7.3 million, $4.5 million, $3.3 million ($0.8 million of which was accrued at December 31, 2001 and paid in January 2002), respectively. We did not pay a dividend on the common shares in 2001 and used the funds available from operations after payment of preferred dividends to further reduce amounts outstanding under our credit facility and buy back stock. We have declared a $0.10 dividend per share on our common stock payable on March 29, 2002, however, we are giving no assurances that this amount or any amount will be a continuing common dividend in the near future.

We will continue to pursue sales of assets and alternative financings in 2002 in order to comply with our credit facility's commitment reductions and mortgage loan maturities. In the aggregate, we are required to make payments in 2002 of at least $25.4 million to reduce various obligations. Since December 31, 2001, we have made $4.1 million of these payments.

Currently our company has three contracts to sell four skilled nursing homes (one is a closed facility) and three assisted livings facilities for a total aggregate sales price of $35.1 million including assumption of approximately $4.1 million of debt. These transactions would generate approximately $27.4 in cash prior to selling costs and we would receive a note for approximately $3.6 million secured by a second mortgage on one of the assisted living facilities. While these contracts do not have contingency provisions, we can give no assurances that the transactions will be completed or what cash proceeds, if any, would be generated.

We also have a Letter of Intent to sell five skilled nursing facilities that are in a partnership in which our company is the General Partner of which our ownership is 80.38%. This agreement contains a financing contingency and we can give no assurances that the transaction will be completed; however, if completed as currently contemplated, the partnership will receive approximately $10.2 million in cash, a note for approximately $3.6 million and a reduction of approximately $10.2 million in mortgage debt due to REMIC pools originated by us.

We are in discussions with one lender to obtain financing on certain owned assisted living facilities and with another lender to possibly sell a participation in certain of our currently unsecuritized mortgages. We can give no assurances that either of these financings will be completed.

Should an insufficient amount be raised to meet our debt obligations through asset sales or financings, we would need to again suspend paying a common dividend and perhaps some of the preferred dividends in order to apply funds from operations to debt reductions.

Alterra Healthcare Corporation ("Alterra") operates 35 assisted living facilities with a total of 1,416 units owned by us representing approximately 14.3%, or $84.2 million, of our "direct real estate investment portfolio" (properties that we own or on which we hold promissory notes secured by first mortgages). Alterra has announced that it has engaged financial advisors to assist Alterra in a restructuring of its debt and equity. We cannot, at this time, predict or quantify what, if any, impact any ultimate restructuring could have on us. As of March 2002, Alterra was current on all rent due us.

We expect our future income and ability to make distributions from cash flows from operations to depend on the collection of our mortgage loans receivable, REMIC Certificates and rents. The collectibility of these loans, certificates and rents will be dependent, in large part, upon the successful operation by the operators of the skilled nursing facilities, assisted living residences and the school owned by or pledged to us. The operating results of the facilities will depend on various factors over which the operators/owners may have no control. Those factors include, without limitation, the status of the economy, changes in supply of or demand for competing long-term care facilities, ability to control rising operating costs, and the potential for significant reforms in the long-term care industry. In addition, our company's future growth in net income and cash flow may be adversely impacted by various proposals for changes in the governmental regulations and financing of the long-term care industry. Specifically, certain of the increases in Medicare reimbursement for skilled nursing facilities provided for under the Balanced Budget Refinement Act and the Benefits Improvement and Protection Act will sunset in October 2002. Unless Congress enacts additional legislation, the loss of revenues associated with this occurrence could have a material adverse effect on our operators, and on us. We cannot presently predict what impact these proposals may have, if any. We believe that an adequate provision has been made for the possibility of loans proving uncollectible but will continually evaluate the status of the operations of the skilled nursing facilities, assisted living facilities and the school. In addition, we will monitor our borrowers and the underlying collateral for mortgage loans and will make future revisions to the provision, if considered necessary.

Our company's investments, principally our investments in mortgage loans, REMIC Certificates, and owned properties, are subject to the possibility of loss of their carrying values as a result of changes in market prices, interest rates and inflationary expectations. The effects on interest rates may affect our costs of financing its operations and the fair market value of its financial assets. We generally make loans which have predetermined increases in interest rates and leases which have agreed upon annual increases. In as much as our company has funded some its investments with revolving credit facilities, we are at risk of net interest margin deterioration if medium and long-term rates were to increase between the time we originated the investment and replaced the short-term variable rate borrowings with a fixed rate financing.

The REMIC Certificates retained by us are subordinate in rank and right of payment to the certificates sold to third-party investors and as such would, in most cases, bear the first risk of loss in the event of an impairment to any of the underlying mortgages. The returns on our investment in REMIC Certificates are subject to certain uncertainties and contingencies including, without limitation, the level of prepayments, estimated future credit losses, prevailing interest rates, and the timing and magnitude of credit losses on the underlying mortgages collateralizing the securities that are a result of the general condition of the real estate market or long-term care industry. As these uncertainties and contingencies are difficult to predict and are subject to future events that may alter management's estimations and assumptions, no assurance can be given that current yields will not vary significantly in future periods. To minimize the impact of prepayments, the mortgage loans underlying the REMIC Certificates generally prohibit prepayment unless the property is sold to an unaffiliated third party (with respect to the borrower).

Certain of the REMIC Certificates retained by our company have designated certificate principal balances and a stated certificate interest "pass-through" rate. These REMIC Certificates are subject to credit risk to the extent that there are estimated or realized credit losses on the underlying mortgages, and as such their effective yield would be negatively impacted by such losses. Our company also retains the interest-only (I/O) Certificates, which provide cash flow (interest-only) payments that result from the difference between the interest collected from the underlying mortgages and interest paid on all the outstanding pass-through rate certificates. In addition to the risk from credit losses, the I/O Certificates are also subject to prepayment risk, in that prepayments of the underlying mortgages reduce future interest payments of which a portion flows to the I/O Certificates, thus, reducing their effective yield. The Certificates' fair values are estimated, in part, based on a spread over the applicable U.S Treasury rate, and consequently, are inversely affected by increases or decreases in such interest rates. There is no active market in these securities from which to readily determine their value. The estimated fair values of both classes of Certificates are subject to change based on the estimate of future prepayments and credit losses, as well as fluctuations in interest rates and market risk. Although we are required to report our REMIC Certificate investments available for sale at fair value, many of the factors considered in estimating their fair value are difficult to predict and are beyond the control of our company's management, consequently, changes in the reported fair values may vary widely and may not be indicative of amounts immediately realizable if our company was forced to liquidate any of the Certificates. See "Exhibi

We believe we have sufficient liquidity and financing capability to maintain our preferred dividend payments, pay common dividends at least sufficient to maintain our REIT status and repay borrowings at or prior to their maturity.

Funds From Operations

Industry analysts generally consider funds from operations (“FFO”) to be an alternative measure of the performance of a REIT. The National Association of Real Estate Investment Trusts (“NAREIT”) has defined FFO as net income applicable to common stockholders (computed in accordance with GAAP) excluding gains (or losses) from debt restructuring, sales of property and impairment charges, plus depreciation of real property and after adjustments for unconsolidated entities in which a REIT holds an interest. In addition, in calculating FFO we have added back the non-cash charge for the reductions of loans to officers and directors.

We believe that FFO is an important supplemental measure of operating performance. FFO should not be considered as an alternative to net income or any other GAAP measurement of performance as an indicator of operating performance or as an alternative to cash flows from operations, investing or financing activities as a measure of liquidity. We believe that FFO is helpful in evaluating a real estate investment portfolio’s overall performance considering the fact that historical cost accounting implicitly assumes that the value of real estate assets diminishes predictably over time. FFO provides an alternative measurement criteria, exclusive of certain non-cash charges included in GAAP income, by which to evaluate the performance of such investments. FFO, as used by our company may not be comparable to similarly entitled items reported by other REITs.

The following table reconciles net income available to common stockholders to FFO available to common stockholders (*in thousands, except per share amounts*):

	2001	2000	1999
Net (loss) income available to common stockholders	$ (17,985)	$ 16,550	$ 16,740
Real estate depreciation	13,866	15,259	13,483
Impairment charge	28,584	14,822	14,939
Reduction in stockholder loans	2,453	—	—
Gain on sale of real estate	(1,560)	(8,990)	—
FFO available to common stockholders	$ 25,358	$ 37,641	$ 45,162
Diluted FFO available to common stockholders	$ 25,358	$ 39,194	$ 51,582
Basic FFO per share	$ 1.06	$ 1.44	$ 1.65
Diluted FFO per share	$ 1.06	$ 1.44	$ 1.64
Shares for basic FFO per share	23,924	26,108	27,412
Shares for diluted FFO per share	23,925	27,213	31,548

Item 7a. Quantitative and Qualitative Disclosures About Market Risk

Readers are cautioned that statements contained in this section “Quantitative and Qualitative Disclosures About Market Risk” are forward looking and should be read in conjunction with the disclosure under the heading “Statement Regarding Forward Looking Disclosure” set forth above.

We are exposed to market risks associated with changes in interest rates as they relate to our mortgage loans receivable, investments in REMIC Certificates and debt. Interest rate risk is sensitive to many factors, including governmental monetary and tax policies, domestic and international economic and political considerations and other factors that are beyond our control.

We do not utilize interest rate swaps, forward or option contracts or foreign currencies or commodities, or other types of derivative financial instruments. The purpose of the following disclosure is to provide a framework to understand our sensitivity to hypothetical changes in interest rates as of December 31, 2001.

Our future earnings, cash flows and estimated fair values relating to financial instruments are dependent upon prevalent market rates of interest, such as LIBOR or term rates of U.S. Treasury Notes. Changes in interest rates generally impact the fair value, but not future earnings or cash flows, of mortgage loans receivable, our investment in REMIC Certificates and fixed rate debt. For variable rate debt, such as our revolving line of credit, changes in interest rates generally do not impact the fair value, but do affect future earnings and cash flows.

At December 31, 2001, based on the prevailing interest rates for comparable loans and estimates made by management, the fair value of our mortgage loans receivable was approximately $96.6 million. A 1% increase in such rates would decrease the estimated fair value of our mortgage loans by approximately $4.0 million while a 1% decrease in such rates would increase their estimated fair value by approximately $4.3 million. A 1% increase or decrease in applicable interest rates would not have a material impact on the fair value of our investment in REMIC Certificates or fixed rate debt.

Assuming the borrowings outstanding under our revolving line of credit at December 31, 2001 and taking into effect our commitment to have the balance down to $95.0 million as of October 1, 2002, a 1% increase in interest rates would increase annual interest expense on our revolving line of credit by approximately $1.0 million. Conversely, a 1% decrease in interest rates would decrease annual interest expense on our revolving line of credit by $1.0 million.

The estimated impact of changes in interest rates discussed above are determined by considering the impact of the hypothetical interest rates on our borrowing costs, lending rates and current U.S. Treasury rates from which our financial instruments may be priced. We do not believe that future market rate risks related to our financial instruments will be material to our financial position or results of operations. These analyses do not consider the effects of industry specific events, changes in the real estate markets, or other overall economic activities that could increase or decrease the fair value of our financial instruments. If such events or changes were to occur, we would consider taking actions to mitigate and/or reduce any negative exposure to such changes. However, due to the uncertainty of the specific actions that would be taken and their possible effects, the sensitivity analysis assumes no changes in our capital structure.

Item 8. FINANCIAL STATEMENTS

REPORT OF INDEPENDENT AUDITORS

The Board of Directors and Stockholders
LTC Properties, Inc.

We have audited the accompanying consolidated balance sheets of LTC Properties, Inc. as of December 31, 2001 and 2000 and the related consolidated statements of income and comprehensive income, stockholders' equity, and cash flows for each of the three years in the period ended December 31, 2001. Our audits also included the financial statement schedules listed in the index at Item 14(a). These financial statements and financial statement schedules are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements and financial statement schedules based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the consolidated financial position of LTC Properties, Inc. at December 31, 2001 and 2000, and the consolidated results of its operations and its cash flows for each of the three years in the period ended December 31, 2001 in conformity with accounting principles generally accepted in the United States. Also, in our opinion, the related financial statement schedules, when considered in relation to the basic financial statements taken as a whole, present fairly in all material respects the information set forth therein.

/s/ ERNST & YOUNG LLP

Los Angeles, California
January 25, 2002

LTC PROPERTIES, INC.

CONSOLIDATED BALANCE SHEETS
(In thousands, except per share amounts)

	December 31, 2001	December 31, 2000
ASSETS		
Real Estate Investments:		
Buildings and improvements, net of accumulated depreciation and amortization: 2001—$58,583; 2000—$47,181	$ 410,202	$ 397,833
Land	27,339	23,484
Mortgage loans receivable, net of allowance for doubtful accounts: 2001—$1,250; 2000—$1,250	93,611	106,149
REMIC Certificates	73,154	94,962
Real estate investments, net	604,306	622,428
Other Assets:		
Cash and cash equivalents	6,322	1,870
Debt issue costs, net	3,578	3,396
Interest receivable	3,258	4,558
Prepaid expenses and other assets	2,423	4,521
Notes receivable (includes $3,095 due from CLC Healthcare, Inc.)	14,584	7,357
Marketable debt securities	8,755	15,873
Advance on line of credit due from CLC Healthcare, Inc.	5,342	16,582
	44,262	54,157
Total assets	$ 648,568	$ 676,585
LIABILITIES AND STOCKHOLDERS' EQUITY		
Convertible subordinated debentures	$ 2,408	$ 24,642
Bank borrowings	104,000	118,000
Mortgage loans payable	162,232	103,341
Bonds payable and capital lease obligations	15,994	16,577
Accrued interest	1,210	2,260
Accrued expenses and other liabilities	7,138	6,741
Distributions payable	1,803	985
Total liabilities	294,785	272,546
Minority interest	13,404	9,912
Stockholders' Equity:		
Preferred stock $0.01 par value; 10,000 shares authorized; shares issued and outstanding: 2001—7,062; 2000—7,080	165,183	165,500
Common stock $0.01 par value; 40,000 shares authorized; shares issued and outstanding: 2001—18,393; 2000—26,031	185	260
Capital in excess of par value	254,930	296,568
Cumulative net income	218,826	221,734
Notes receivable from stockholders	(8,042)	(10,126)
Accumulated comprehensive income (loss)	2,437	(1,746)
Cumulative distributions	(293,140)	(278,063)
Total stockholders' equity	340,379	394,127
Total liabilities and stockholders' equity	$ 648,568	$ 676,585

See accompanying notes.

LTC PROPERTIES, INC.

CONSOLIDATED STATEMENTS OF INCOME AND COMPREHENSIVE INCOME
(In thousands, except per share amounts)

	Years ended December 31,		
	2001	2000	1999
Revenues:			
Rental income	$ 39,512	$ 49,958	$ 45,086
Interest income from mortgage loans and notes receivable	12,603	15,025	19,506
Interest income from REMIC Certificates	15,116	16,852	17,598
Interest and other revenue	2,881	5,295	5,472
Total revenues	70,112	87,130	87,662
Expenses:			
Interest expense	21,910	27,426	21,836
Depreciation and amortization	13,866	15,259	13,483
Minority interest	973	982	1,018
Impairment charge	28,584	14,822	14,939
Operating and other expenses	9,247	5,994	5,863
Total expenses	74,580	64,483	57,139
Operating (loss) income	(4,468)	22,647	30,523
Other income, net	—	—	1,304
Gain on sale of real estate and other assets, net	1,560	8,990	—
Net (loss) income	(2,908)	31,637	31,827
Preferred dividends	15,077	15,087	15,087
Net (loss) income available to common stockholders	$ (17,985)	$ 16,550	$ 16,740
Net (Loss) Income Per Common Share:			
Basic net (loss) income per common share	$ (0.75)	$ 0.63	$ 0.61
Diluted net (loss) income per common share	$ (0.75)	$ 0.63	$ 0.61
Comprehensive Income:			
Net (loss) income available to common stockholders	$ (17,985)	$ 16,550	$ 16,740
Unrealized gain (loss) on available-for-sale securities	2,807	(500)	(1,246)
Reclassification adjustment	1,376	—	—
Total comprehensive (loss)income	$ (13,802)	$ 16,050	$ 15,494

See accompanying notes.

LTC PROPERTIES, INC.

CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY
(in thousands, except per share amounts)

	Shares							
	Preferred Stock	Common Stock	Preferred Stock	Common Stock	Capital in Excess of Par Value	Cumulative Net Income	Notes Receivable from Stockholders	Cumulative Distribution
Balance—December 31, 1998	7,080	27,661	$ 165,500	$ 277	$ 311,113	$ 158,270	$ (11,200)	$ (182,560)
Payments on stockholder notes	—	—	—	—	—	—	942	—
Conversion of debentures	—	25	—	—	430	—	—	—
Repurchase of common stock	—	(650)	—	(7)	(7,032)	—	—	—
Conversion of partnership units	—	—	—	—	16	—	—	—
Net income	—	—	—	—	—	31,827	—	—
Preferred stock dividends	—	—	—	—	—	—	—	(15,087)
Common stock cash distributions ($1.56 per share)	—	—	—	—	—	—	—	(42,626)
Balance—December 31, 1999	7,080	27,036	165,500	270	304,527	190,097	(10,258)	(240,273)
Payments on stockholder notes	—	—	—	—	—	—	132	—
Repurchase of common stock	—	(1,005)	—	(10)	(7,959)	—	—	—
Conversion of partnership units	—	—	—	—	—	—	—	—
Net income	—	—	—	—	—	31,637	—	—
Preferred stock dividends	—	—	—	—	—	—	—	(15,087)
Common stock cash distributions ($0.87 per share)	—	—	—	—	—	—	—	(22,703)
Balance—December 31, 2000	7,080	26,031	165,500	260	296,568	221,734	(10,126)	(278,063)
Interest added to stockholder note balance	—	—	—	—	—	—	(369)	—
Reduction in stockholder note balance	—	—	—	—	—	—	2,453	—
Repurchase of stock	(18)	(7,588)	(317)	(75)	(41,661)	—	—	—
Net loss	—	—	—	—	—	(2,908)	—	—
Preferred stock dividends	—	—	—	—	—	—	—	(15,077)
Vested restricted stock	—	—	—	—	23	—	—	—
Canceled restricted stock	—	(50)	—	—	—	—	—	—
Balance—December 31, 2001	7,062	18,393	$ 165,183	$ 185	$ 254,930	$ 218,826	$ (8,042)	$ (293,140)

	Accumulated Comprehensive Income (Loss)
Balance at December 31, 1998	$ —
Unrealized loss on available-for-sale securities	(1,246)
Balance at December 31, 1999	(1,246)
Unrealized loss on available-for-sale securities	(500)
Balance at December 31, 2000	(1,746)
Reclassification adjustment	1,376
Unrealized gain on available-for-sale securities	2,807
Balance at December 31, 2001	$ 2,437

See accompanying notes.

LTC PROPERTIES, INC.

CONSOLIDATED STATEMENTS OF CASH FLOWS
(In thousands)

	Year ended December 31,		
	2001	2000	1999
OPERATING ACTIVITIES:			
Net (loss) income	$ (2,908)	$ 31,637	$ 31,827
Adjustments to reconcile net income to net cash provided by operating activities:			
Depreciation and amortization	13,866	15,259	13,483
Gain on sale of real estate and other investments, net	(1,560)	(8,990)	(1,304)
Non-cash impairment charge	28,584	14,822	14,939
Reduction in stockholder notes receivable	2,453	—	—
Other non-cash charges, net	4,639	1,700	1,627
(Increase) decrease in interest receivable	32	(632)	(296)
(Increase) in prepaid, other assets and allowance	(1,068)	(5,407)	(410)
(Decrease) in accrued interest	(1,279)	(640)	(341)
(Decrease) increase in accrued expenses and other liabilities	1,093	(2,442)	1,260
Net cash provided by operating activities	43,852	45,307	60,785
INVESTING ACTIVITIES:			
Investment in real estate mortgages	—	(964)	(8,568)
Acquisition of real estate properties and capital improvements, net	(1,689)	(4,288)	(34,655)
Proceeds from sale of real estate investments, net	43,493	51,632	—
Principal payments on mortgage loans receivable	9,291	8,789	6,729
Investment in debt securities	(2,909)	—	(13,097)
Advances to CLC Healthcare, Inc.	(5,537)	(14,753)	(13,336)
Repayment of advances to CLC Healthcare, Inc.	1,149	3,540	23,527
Other	2,974	1,741	(8,756)
Net cash provided by (used in) investing activities	46,772	45,697	(48,156)
FINANCING ACTIVITIES:			
Debt issue costs	(1,187)	(2,751)	(1,129)
Distributions paid	(14,259)	(37,790)	(57,713)
Bank borrowings	50,000	125,000	147,500
Repayment of bank borrowings	(64,000)	(167,000)	(87,500)
Mortgage loan borrowings	11,500	—	24,985
Principal payments on mortgage loans, notes payable and capital leases	(3,966)	(1,410)	(976)
Redemption of convertible subordinated debentures	(22,230)	—	(29,992)
Repurchase of common and preferred stock	(42,054)	(7,969)	(7,039)
Other	24	131	387
Net cash used in financing activities	(86,172)	(91,789)	(11,477)
Increase (decrease) in cash and cash equivalents	4,452	(785)	1,152
Cash and cash equivalents, beginning of year	1,870	2,655	1,503
Cash and cash equivalents, end of year	$ 6,322	$ 1,870	$ 2,655
Supplemental disclosure of cash flow information:			
Interest paid	$ 22,184	$ 27,012	$ 21,011
Non-cash investing and financing transactions:			
See Note 4: Supplemental Cash Flow Information			

See accompanying notes.

LTC PROPERTIES, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

1. The Company

LTC Properties, Inc. (the "Company"), a Maryland corporation, commenced operations on August 25, 1992. The Company is a real estate investment trust ("REIT") that invests primarily in long-term care facilities through mortgage loans, facility lease transactions and other investments.

2. Summary of Significant Accounting Policies

Basis of Presentation. The accompanying consolidated financial statements include the accounts of the Company, its wholly-owned subsidiaries and its controlled partnerships. All intercompany accounts and transactions have been eliminated in consolidation. Certain reclassifications have been made to the prior period financial statements to conform to the current year presentation.

Use of Estimates. Preparation of the consolidated financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the amounts reported in the consolidated financial statements and accompanying notes. Actual results could differ from those estimates.

Cash Equivalents. Cash equivalents consist of highly liquid investments with a maturity of three months or less when purchased and are stated at cost which approximates market.

Land, Buildings and Improvements. Land, buildings and improvements are recorded at cost. Depreciation is computed principally by the straight-line method for financial reporting purposes and by accelerated methods for income tax purposes. Estimated useful lives for financial reporting purposes range from 3 years on computers to 7 years for equipment to 40 years for buildings.

Impairments. Impairment losses are recorded when events or changes in circumstances indicate the asset is impaired and the estimated undiscounted cash flows to be generated by the asset are less than its carrying amount. Management assesses the impairment of properties individually and impairment losses are calculated as the excess of the carrying amount of the real estate over its fair value less cost to sell as per Financial Accounting Standard No. 121 "*Accounting for the Impairment of Long-Lived Assets and for Long-Lived Assets to be Disposed of."* In determining fair value, the Company uses current appraisals or other third party opinions of value and other estimates of fair value such as estimated undiscounted future cash flows.

Securitization Transactions. The Company is a REIT and, as such, makes its investments with the intent to hold them for long-term purposes. However, mortgage loans may be transferred to a Real Estate Mortgage Investment Conduit ("REMIC"), a qualifying special-purpose entity, when a securitization provides the Company with the best available form of capital to fund additional long-term investments. When contemplating a securitization, consideration is given to the Company's current and expected future interest rate posture and liquidity and leverage position, as well as overall economic and financial market trends.

A securitization is completed in a two-step process. First, a wholly owned special-purpose bankruptcy remote corporation (the "REMIC Corp.") is formed and selected mortgage loans are sold to the REMIC Corp. without recourse. Second, the REMIC Corp. transfers the loans to a trust (the "REMIC Trust") in exchange for commercial mortgage pass-through certificates (the "REMIC Certificates") which represent beneficial ownership interests in the REMIC Trust assets (the underlying mortgage loans). Under this structure, the REMIC Trust is a qualifying special purpose entity from which the mortgages are isolated from the REMIC Corp. and the Company. Holders of REMIC Certificates issued by the REMIC Trust have the right free of any conditional constraints to pledge or exchange those interests, and neither the REMIC Corp. or the Company maintains effective control over the transferred assets (the mortgages). The REMIC Trust is administered by a third-party trustee solely for the benefit of the REMIC Certificate holders. Under the securitization structure described above, the Company accounts for the transfer of the mortgages as a sale and any gain or loss is recorded in earnings. The gain or loss is equal to the excess or deficiency of the cash proceeds and fair market value of any subordinated certificates received when compared with the carrying value of the mortgages sold, net of any transaction costs incurred and any gains or losses associated with an underlying hedge. Subordinated certificates received by the Company are recorded at their fair value at the date of the transaction. The Company has no controlling interest in the REMIC since the majority of the beneficial ownership interests (in the form of REMIC Certificates) are sold to third-party investors. Consequently, the financial statements of the REMIC Trust are not consolidated with those of the Company for financial reporting purposes.

REMIC Certificates retained by the Company as consideration for the mortgages sold are accounted for at fair value. In determining fair value on the date of sale, management considers various factors including, pricing of the certificates sold relative to the certificates retained as evaluated by the underwriters, discount rates and applicable spreads at the time of issuance for similar securities (or adjustments thereto if no comparable securities are available), assumptions regarding prepayments including the weighted-average life of prepayable assets, if any, and estimates relating to potential realized credit losses.

The REMIC Certificates issued by the REMIC Trust include various levels of senior, subordinated, interest only and residual classes. The subordinated REMIC Certificates generally provide a level of credit enhancement to the senior REMIC Certificates. The senior REMIC Certificates (which historically have represented 66% of the total REMIC Certificates) are then sold to outside third-party investors through a private placement under Rule 144A of the Securities Act of 1933, as amended. The subordinated REMIC Certificates along with the cash proceeds from the sale of the senior REMIC Certificates are retained by the REMIC Corp. as consideration for the initial transfer of the mortgage loans to the REMIC Trust. Neither the Company nor the REMIC Corp. is obligated to purchase any of the REMIC Trust assets or assume any liabilities.

Description of the REMIC Certificates. REMIC Certificates represent beneficial ownership interests in the REMIC Trust and can be grouped into three categories; senior, subordinated and subordinated interest-only (“I/O”). The REMIC Certificates sold to third-party investors are the senior certificates and those retained by the Company are the subordinated certificates. The senior and the subordinated certificates have stated principal balances and stated interest rates (“pass-through rates”). The I/O REMIC Certificates have no stated principal but are entitled to interest distributions. Interest distributions on the I/O REMIC Certificates are typically based on the spread between the monthly interest received by the REMIC Trust on the underlying mortgage collateral and the monthly pass-through interest paid by the REMIC Trust on the outstanding pass-through rate REMIC Certificates. After payment of the pass-through interest on the outstanding REMIC Certificates and interest distributions on the I/O Certificates, the REMIC Trust distributes the balance of the payments received on the underlying mortgages as a distribution of principal. Interest and principal distributions are made in order of REMIC Certificate seniority. As such, to the extent there are defaults or unrecoverable losses on the underlying mortgages resulting in reduced cash flows, the subordinated certificates held by the Company would in general bear the first risk of loss. Management evaluates the realizability of expected future cash flows periodically. A permanent impairment would be recorded in current period earnings when management believes that it is likely that a portion of the underlying mortgage collateral would not be realized by the REMIC Trust.

On January 1, 1999, the Company adopted SFAS No. 134 *“Accounting for Mortgage-Backed Securities Retained after the Securitization of Mortgage Loans Held for Sale by a Mortgage Banking Enterprise”*. Upon adoption of SFAS No. 134, the Company, based on its ability and intent to hold its investments in REMIC Certificates, transferred its I/O REMIC Certificates and certificates with an investment rating of “BB” or higher from the trading category to the available-for-sale category and its certificates with an investment rating of "B" or lower to the held-to-maturity category. The transfer was recorded at fair value on the date of the transfer.

The I/O REMIC Certificates' fair values are estimated, in part, based on a spread over the applicable U.S. Treasury Rate, and consequently, are inversely affected by increases or decreases in such interest rates. There is no active market in these securities from which to readily determine their value. The estimated fair values of both classes of certificates are subject to change based on the estimate of the current interest rate environment, estimated spreads over the U.S. Treasury Rate at which the retained certificates might trade, expectations regarding credit losses, if any, expected weighted-average life of the underlying collateral and discount rates commensurate with the risks involved.

Mortgage Loans Receivable. Historically, the Company has sold its mortgage loans solely in connection with its REMIC securitizations. The Company may, in the future sell a participation interest in certain mortgages. Since certain mortgage loans may be securitized or sold in the future, direct investments in mortgage loans are classified as held for sale and carried at the lower of cost or market. If the mortgage loans aggregate cost basis exceeds their aggregate market value, a valuation allowance is established and the resulting amount is included in the determination of net income. Changes in the valuation allowance are included in current period earnings. In determining the estimated market value for mortgage loans, the Company considers estimated prices and yields, based in part on a spread over the applicable U.S. Treasury Note Rate, sought by qualified institutional buyers of the REMIC Certificates originated in the Company's securitizations. As of December 31, 2001 and 2000 market value exceeded the carrying cost for such loans.

Mortgage Servicing Rights. The Company sub-services mortgage loans that are collateral for REMIC Certificates issued in its securitization transactions for which it receives servicing fees, based on market rates for such services at the time the securitization is completed, equal to a fixed percentage of the outstanding principal on the collateral loans. A separate asset for servicing rights is not recognized since the servicing fees received only adequately compensate the Company for the cost of servicing the loans. The fair value of servicing rights for mortgage loans originated and retained by the Company are estimated based on the fees received for servicing mortgage loans that serve as collateral for REMIC Certificates. All costs to originate mortgage loans are allocated to the mortgage loans since the fair value of servicing rights only sufficiently covers the servicing costs.

Interest Rate Contracts. Firm commitments subject the Company to interest rate risk to the extent that debt or other fixed rate financing will be used to finance the commitments. The Company may elect to enter into interest rate contracts to hedge such financing thereby reducing its exposure to interest rate risk. Interest rate contracts are designated as hedges of assets intended for securitization when the significant characteristics and expected terms of the securitization are identified and it is probable the securitization will occur. These contracts are entered into in notional amounts that generally correspond to the principal amount of the assets to be securitized. The Company effectively locks in its net interest margin on the securitization when the interest rate contract is entered into since changes in the market value of these contracts respond inversely to changes in the market value of the hedged assets. Gains or losses on interest rate contracts designated as hedges of assets to be securitized are deferred and recognized upon the completion of the securitization. The Company may also manage interest rate risk by entering into interest rate swap agreements whereby the Company effectively fixes the interest rate on variable rate debt. The Company recognizes all derivative financial instruments such as interest rate swap contracts, in the consolidated financial statements at fair value regardless of the purpose or interest for holding the instrument. Changes in the fair value of derivative financial instruments are either recognized periodically in income or in stockholders' equity as a component of comprehensive income depending on whether the derivative financial instrument qualifies for hedge accounting, and if so, whether it qualifies as a fair value hedge or cash flow hedge. Generally, changes in fair values of derivatives accounted for as fair value hedges are recorded in income along with the portions of the changes in the fair values of the hedged items that relate to the hedged risk(s). Changes in fair values of derivatives accounted for as cash flow hedges, to the extent they are effective as hedges, are recorded in other comprehensive income. Changes in the fair values of derivatives not qualifying as hedges are reported in income.

Prior to January 1, 2001, the Company also used interest rate swap contracts for hedging purposes. For interest rate swaps, the net amounts paid or received and net amounts accrued through the end of the accounting period were included in interest expense. Unrealized gains or losses on interest rate swap contracts were not recognized in income. Gains or losses on any contracts terminated early were deferred and amortized to income over the remaining average life of the terminated contracts. The discounts or premiums on the instruments were amortized to income over the lives of the contracts using the straight-line method. Realized gains and losses were included in other assets and liabilities and recognized in income when the future transaction occurred or at the time the transaction was no longer expected to occur. As of December 31, 2001 the Company had no interest rate contracts outstanding.

Investments. Available-for-sale securities are stated at fair value, with the unrealized gains and losses, reported in other comprehensive income. Realized gains and losses and declines in value judged to be other-than-temporary on available-for-sale securities are included in net income. The cost of securities sold is based on the specific identification method. Interest and dividends on securities classified as available-for-sale are included in interest and other income.

Revenue Recognition. Interest income on mortgage loans and REMIC Certificates is recognized using the effective interest method. The Company follows a policy related to mortgage interest whereby the Company considers a loan to be non-performing after 60 days of non-payment of amounts due and does not recognize unpaid mortgage interest income from that loan until the amounts have been received. Base rents under operating leases are accrued as earned over the terms of the leases. The majority of the Company’s leases contain provisions for specified annual increases over the rents of the prior year and are generally computed in one of four ways depending on specific provisions of each lease: (i) a specified percentage increase over the prior year, generally 2%; (ii) the higher of (i) or a calculation based on the Consumer Price Index; (iii) as a percentage of facility net patient revenues in excess of base amounts or (iv) specific dollar increases. SEC Staff Bulletin No. 101 *Revenue Recognition in Financial Statements* (“SAB 101”) does not allow for the recognition of such revenue until all possible contingencies have been eliminated. The Company considers the operating history of the lessee and the general condition of the industry when evaluating whether all possible contingencies have been eliminated and have historically, and expect in the future, to not include contingent rents as income until received. The Company follows a policy related to rental income whereby the Company considers a lease to be non-performing after 60 days of non-payment of amounts due and does not recognize unpaid rental income from that lease until the amounts have been received.

Federal Income Taxes. The Company qualifies as a REIT under the Internal Revenue Code of 1986, as amended and as such, no provision for Federal income taxes has been made. A REIT may deduct distributions to its stockholders from its taxable income. If at least 90% (95% for taxable years ending prior to January 1, 2001) of a REIT’s taxable income is distributed to its stockholders and it complies with other Internal Revenue Code requirements, a REIT generally is not subject to Federal income taxation.

For Federal tax purposes, depreciation is generally calculated at a rate of 3.6% based on the assets’ tax basis (which approximates cost) using the straight-line method over a period of 27.5 years. Earnings and profits, which determine the taxability of dividends to stockholders, differ from net income for financial statement purposes due to the treatment of certain interest income and expense items and depreciable lives and basis of assets under the Internal Revenue Code. The net difference in the tax basis and the reported amounts of the Company's assets and liabilities as of December 31, 2001 is approximately $40,626,000.

Concentrations of Credit Risks. Financial instruments which potentially subject the Company to concentrations of credit risk consist primarily of cash and cash equivalents, REMIC Certificates, mortgage loans receivable, operating leases on owned properties and interest rate swaps. The Company's financial instruments, principally REMIC Certificates, mortgage loans receivable and operating leases, are subject to the possibility of loss of carrying value as a result of the failure of other parties to perform according to their contractual obligations or changes in market prices which may make the instrument less valuable. The Company obtains various collateral and other protective rights, and continually monitors these rights, in order to reduce such possibilities of loss. In addition, the Company provides reserves for potential losses based upon management's periodic review of its portfolio.

The Company's REMIC Certificates are subordinate in rank and right of payment to the certificates sold to third-party investors and as such, in most cases, would bear the first risk of loss in the event of an impairment to any of the underlying mortgages. The returns on the REMIC Certificates are subject to certain uncertainties and contingencies including, without limitation, the level of prepayment, prevailing interest rates and the timing and magnitude of credit losses on the mortgages underlying the securities that are a result of the general condition of the real estate market or long-term care industry. These uncertainties and contingencies are difficult to predict and are subject to future events that may alter management's estimations and assumptions therefore, no assurance can be given that current yields will not vary significantly in future periods. In general, the mortgage loans underlying the REMIC Certificates generally prohibit prepayment unless the property is sold to an unaffiliated third party (with respect to the borrower).

Certain of the REMIC Certificates retained by the Company have designated certificate principal balances and a stated certificate interest "pass-through" rate. These REMIC Certificates are subject to credit risk to the extent that there are estimated or realized credit losses on the underlying mortgages, and as such their effective yield would be negatively impacted by such losses. The Company also retains the I/O REMIC Certificates. In addition to the risk from credit losses, the I/O REMIC Certificates are also subject to prepayment risk, in that prepayments of the underlying mortgages reduce future interest payments of which a portion flows to the I/O REMIC Certificates, thus, reducing their effective yield.

Net Income Per Share. Basic earnings per share is calculated using the weighted-average shares of common stock outstanding during the period excluding common stock equivalents. Diluted earnings per share includes the effect of all dilutive common stock equivalents.

Stock-Based Compensation. The Company grants stock options for a fixed number of shares to employees with an exercise price equal to the fair value of the shares at the date of grant. The Company accounts for stock option grants in accordance with APB Opinion No. 25, *Accounting for Stock Issued to Employees* (APB 25) and related Interpretations because the Company believes the alternative fair value accounting provided for under FASB Statement No. 123, *Accounting for Stock-Based Compensation*, (FAS 123) requires the use of option valuation models that were not developed for use in valuing employee stock options. Under APB 25, because the exercise price of the Company's employee stock options equals the market price of the underlying stock on the date of grant, no compensation expense is recognized.

3. Major Operators

As of December 31, 2001, Sun Healthcare Group, Inc. ("Sun") operated 15 facilities (13 leases and two loans) with 1,774 beds/units representing approximately 11.6%, or $68,239,000, of the Company's "direct real estate investment portfolio" (properties that the Company owns or on which the Company holds promissory notes, secured by first mortgages). Additionally, at December 31, 2001 Sun operated eight skilled nursing facilities securing mortgage loans payable to REMIC pools originated by the Company. During 1999 Sun filed for reorganization under Chapter 11 of the Bankruptcy Code and operated its business as a debtor-in-possession subject to the jurisdiction of the Bankruptcy Court until it emerged from bankruptcy in February 2002. Concurrently, 13 leases the Company had directly with Sun were affirmed, additionally one of the leases related to a loan was affirmed and the other lease related to a loan was rejected.

Assisted Living Concepts, Inc. ("ALC") operates 37 assisted living facilities with a total of 1,434 units owned by the Company representing approximately 14.9%, or $88,105,000, of the Company's direct real estate investment portfolio. In October 2001, ALC filed for reorganization under Chapter 11 of the federal bankruptcy laws. The filing was pre-negotiated with sufficient debt holders to allow ALC to reorganize its debt and equity and emerge from bankruptcy as of 12:01 a.m. on January 1, 2002. The final order affirming the reorganization was made in December 2001, consequently the Company has reflected the transaction as of December 31, 2001. The Company agreed to reduce total rents under the 37 leases by $875,000 a year, beginning January 1, 2002, and received a lease rejection claim of $2,500,000 for this concession. Under the provisions of ALC's Plan, the Company would have been entitled to receive, due to its ownership of the subordinated debentures and the lease rejection claim, $7,986,000 of ALC's new Senior Secured Notes bearing interest at 10% per annum, payable semi-annually in arrears, $3,026,000 new Junior Secured Notes bearing interest payable in additional new Junior Secured Notes for three years at 8% and thereafter payable in cash at 12% per annum, payable semi-annually in arrears and 1,238,076 shares of ALC common stock. Provisions of the Revenue Code governing REITs prohibit REITs from owning debt and/or equity securities representing more than 10% of the value or voting power of any one issuer. Without qualifying as safe harbor debt, securities include the Senior Secured Notes and the Junior Secured Notes. In order to qualify as safe harbor debt and retain the Company's REIT status the Company was able to hold only such debt. For REIT income test purposes, provisions would also disqualify income from any entity in which a REIT owns 10% or more of the total combined voting power of all classes of stock or 10% or more of the total value of shares of all classes of a corporate tenant. And as a result, the Company could not be owners of the ALC common stock. In December 2001, the Company entered into an Assignment and Assumption Agreement with Healthcare Holdings, Inc., a wholly owned subsidiary of CLC Healthcare, Inc., to purchase the right to receive the common stock of ALC (see *Note 8. CLC Healthcare, Inc. formerly LTC Healthcare Inc.* and *Note 10. Marketable Debt Securities*). At the request of the Company's Board of Directors, the Company's Chairman, CEO and President, Mr. Andre C. Dimitriadis, became a Board Member of ALC as of January 1, 2002.

Alterra Healthcare Corporation ("Alterra") operates 35 assisted living facilities with a total of 1,416 units owned by the Company representing approximately 14.3%, or $84,194,000, of the Company's direct real estate investment portfolio. Alterra has announced that it has engaged financial advisors to assist Alterra in a restructuring of its debt and equity. The Company cannot, at this time, predict or quantify what, if any, impact any ultimate restructuring could have on the Company. As of March 2002, Alterra was current on all rents due the Company.

CLC Healthcare, Inc. (See *Note 8. CLC Healthcare, Inc. formerly LTC Healthcare, Inc.*)

Sunwest Management, Inc. ("Sunwest") operates seven assisted living facilities with a total of 693 units owned by the Company representing approximately 10.5%, or $61,862,000, of the Company's direct real estate investment portfolio.

All of these companies, except Sunwest, are publicly traded companies, and as such are subject to the filing requirements of the Securities and Exchange Commission. The Company's financial position and its ability to make distributions may be adversely affected by further financial difficulties experienced by ALC, Alterra, CLC and Sun, or financial difficulties experienced by Sunwest, or any of the Company's other major operators, including additional bankruptcies, inability to emerge from bankruptcy, insolvency or general downturn in business of any such operator, or in the event any such operator does not renew and/or extend its relationship with the Company or the Company's borrowers when it expires.

4. Supplemental Cash Flow Information

	2001	2000	1999
		(in thousands)	
Non-cash investing and financing transactions:			
Conversion of debentures into common stock	$ —	$ —	$ 435
Assumption of mortgage loans payable related to acquisitions of real estate properties	50,774	13,696	10,595
Assumption of minority interest liability related to acquisition of general partnership interest	3,518	—	—
Assumption of accrued interest related to acquisitions of real estate properties	229	—	—
Conversion of mortgage loans and secured lines of credit into owned properties	3,899	12,255	47,554
Reduction in receivables from CLC Healthcare related to the acquisition of debt securities	7,800	—	—
Exchange of third party debt securities related to the acquisitions of real estate properties	7,925	—	—
Reduction in receivables from CLC Healthcare related to the acquisitions of real estate properties	9,285	5,346	—
Increase in short term notes receivable related to the disposition of real estate properties	8,483	3,055	—

5. Impairment Charge

The Company periodically performs a comprehensive evaluation of its real estate investment portfolio. The long-term care industry has experienced significant adverse changes which have resulted in continued operating losses by certain of the Company's operators and in some instances the filing by certain operators for bankruptcy protection. As a result of the adverse changes in the long-term care industry, the Company has identified certain investments in skilled nursing facilities that it determined had been impaired. These assets were determined to be impaired primarily because the estimated undiscounted future cash flows to be received from these investments are less than the carrying values of the investments.

During 2001, the Company recorded an impairment charge of approximately $28,584,000. The impairment charge included the write-down of the carrying value to the estimated fair value, less cost to sell, of 14 owned skilled nursing facilities of $16,755,000, notes receivable of $1,500,000, debt securities of $9,829,000 (see *Note 10. Marketable Debt Securities*), and $500,000 in lease termination costs. The fair values were based on current appraisals or other third-party opinions of value and other estimates of fair value such as estimated undiscounted future cash flows.

During 2000 the Company recorded an impairment charge of approximately $14,822,000. The impairment charge included the write-down of the carrying value to the estimated fair value, less cost to sell, of six owned skilled nursing facilities of $7,529,000, mortgage loans secured by skilled nursing facilities of $5,088,000 and notes receivable of $1,259,000 and the costs of foreclosure and lease terminations of approximately $946,000. The fair values were based on current appraisals or other third-party opinions of value and other estimates of fair value such as estimated undiscounted future cash flows.

During 1999, the Company recorded an impairment charge of $14,939,000. The impairment charge included the write-down of the carrying value to the estimated fair value, less cost to sell, of seven owned skilled nursing facilities of $7,428,000, two mortgage loans secured by skilled nursing facilities of $2,806,000, notes receivable of $3,329,000 and other assets and the cost of foreclosure and lease terminations of approximately $1,376,000. The fair values were based on current appraisals or other third-party opinions of value and other estimates of fair value such as estimated undiscounted future cash flows.

6. Real Estate Investments

Mortgage Loans. During the year ended December 31, 2001, the Company received principal prepayments totaling $7,990,000 on two mortgage loans originally scheduled to mature in 2006 and 2007, and scheduled principal payments of $1,301,000. Mortgage loans and secured lines of credit with outstanding principal balances totaling $3,899,000 that were secured by four long-term care facilities were converted into owned properties.

During the year ended December 31, 2000, the Company advanced an additional $964,000 for renovation and expansion under a mortgage loan previously provided on a skilled nursing facility. The Company received prepayments totaling $7,650,000 on four mortgage loans originally scheduled to mature in 2001, 2003, 2006 and 2007, and scheduled principal payments of $1,139,000. Mortgage loans with outstanding principal balances totaling $12,255,000 that were secured by eight long-term care facilities were converted into owned properties.

At December 31, 2001, the Company had 44 mortgage loans secured by first mortgages on 41 skilled nursing facilities with a total of 4,524 beds and eight assisted living residences with 369 units located in 21 states. At December 31, 2001, the mortgage loans had interest rates ranging from 9.3% to 13.7% and maturities ranging from 2002 to 2018. In addition, the loans contain certain guarantees, provide for certain facility fees and generally have 25-year amortization schedules. The majority of the mortgage loans provide for annual increases in the interest rate based upon a specified increase of 10 to 25 basis points. At December 31, 2001 and 2000, the net present value of the future cash flows discounted at 10.5% for the mortgage loans was approximately $96,581,000 and $112,748,000, respectively. Scheduled principal payments on mortgage loans are $6,728,000, $12,099,000, $5,922,000, $3,652,000, $11,429,000 and $55,031,000 in 2002, 2003, 2004, 2005, 2006 and thereafter.

Owned Properties and Lease Commitments. During 2001, $3,899,000 of mortgage loans and secured lines of credit converted into four owned properties. The Company purchased four assisted living facilities with a total of 186 units and six skilled nursing facilities with a total of 616 beds from CLC for a gross purchase price (based on independent appraisals) of $45,860,000 that was subject to the assumption of existing non-recourse mortgage debt of $32,832,000 that bears interest at a weighted average rate of 8.25%, the assumption of $229,000 of accrued interest payable related to the mortgage debt and the assumption of $3,518,000 in minority interest liability related to the acquisition of the general partnership interest in a limited liability partnership that owns three of the properties mentioned above. The Company applied the net purchase amount of $9,285,000 to reduce the total indebtedness owed by CLC to the Company. (See *Note 8. CLC Healthcare, Inc., formerly LTC Healthcare, Inc.*)

During 2001 Regent Assisted Living, Inc. ("Regent") announced that it had appointed financial advisors to evaluate strategic alternatives and had approached the Company about rent concessions on five assisted living facilities leased from the Company. During the third quarter of 2001, as a result of several uncured events of default, the Company terminated the five leases with Regent and released the facilities to another operator for comparable rents. The Company believed that Regent's financial problems would cause them to default under their 7.5% convertible subordinated debentures and CLC owned $8,500,000 face value of these debentures which were part of the security under the line of credit between the Company and CLC. In order to reduce the Company's exposure with Regent, the Company entered into a Securities Purchase Agreement with CLC to purchase their Regent debentures for $7,800,000 and this amount was applied to reduce the total indebtedness owed by CLC to the Company. Additionally the Company purchased Regent convertible subordinated debentures with an aggregate face value of $410,000 from the Company's Chairman, CEO and President, Mr. Andre C. Dimitriadis, another current officer and a former officer of the Company. Mr. Dimitriadis owned $160,000 in face value and cost basis of the Regent debentures. At the request of the Audit Committee of the Board of Directors, Mr. Dimitriadis agreed to sell his debentures to the Company for $1.00 in order to avoid any appearance of self-interest or impropriety in his recommending to the Board the purchase of these debentures. The other current officer and the former officer, neither a Board Member, received approximately $125,000 in aggregate which represented 50% of the face value and cost basis of the debentures they owned. At this point, the Company owned 99% of Regent's convertible subordinated debentures. The Company then entered into an agreement with Regent to apply all of these debentures as part of the consideration necessary to acquire two assisted living centers with a total of 222 units from Regent. The total cost of these two facilities was approximately $26,116,000 and was paid by assuming $17,942,000 of non-recourse mortgage debt with a weighted average interest rate of 8.56% and tendering the debentures to Regent. The Company leased these two facilities to the same operator that leased the other five facilities previously operated by Regent. The Company no longer has any facilities operated by or financed with Regent nor does the Company own any Regent securities.

The Company also has a Letter of Intent to sell five skilled nursing facilities that are in a partnership in which the Company owns 80.38% and is the General Partner. This agreement contains a financing contingency and the Company can give no assurances that the transaction will be completed; however, if completed as currently contemplated, the partnership will receive approximately $10,205,000 in cash, a note for approximately $3,550,000 and a reduction of approximately $10,245,000 in mortgage debt due to REMIC pools originated by the Company.

During 2000, $12,255,000 of mortgage loans converted into owned properties. In addition, the Company acquired, from CLC, two skilled nursing facilities with a total of 393 beds for a gross purchase price (based upon independent appraisals) of $19,200,000, and invested approximately $4,288,000 in the expansion and improvement of existing properties. The skilled nursing facilities acquired during 2000 were acquired subject to the assumption of existing non-recourse mortgage debt of $13,696,000 that bears interest at a weighted average rate of 9.25%

Owned facilities are leased pursuant to non-cancelable operating leases generally with an initial term of 6 to 20 years. Many of the leases contain renewal options and one contains an option for a limited time that permits the operator to purchase the facility. The leases provide for fixed minimum base rent during the initial and renewal periods. The majority of the Company's leases contain provisions for specified annual increases over the rents of the prior year and are generally computed in one of four ways depending on specific provisions of each lease: (i) a specified percentage increase over the prior year, generally 2%; (ii) the higher of (i) or a calculation based on the Consumer Price Index; (iii) as a percentage of facility net patient revenues in excess of base amounts or (iv) specific dollar increases. Each lease is a triple net lease which requires the lessee to pay all taxes, insurance, maintenance and repairs, capital and non-capital expenditures and other costs necessary in the operations of the facilities. Contingent rent income for the years ended December 31, 2001, 2000 and 1999 was not significant in relation to contractual base rent income.

Depreciation expense on buildings and improvements, including facilities owned under capital leases, was $13,695,000, $15,145,000, and $13,237,000 for the years ended December 31, 2001, 2000 and 1999.

Future minimum base rents receivable under the remaining non-cancelable terms of operating leases are: $46,427,000, $49,044,000, $48,560,000, $47,323,000, $46,017,000 and $278,320,000 for the years ending December 31, 2002, 2003, 2004, 2005, 2006 and thereafter.

REMIC Certificates. The outstanding principal balance and the weighted-average pass through rate for the senior certificates (held by third parties) and the carrying value of the subordinated certificates (held by the Company) as of December 31, 2001 and 2000 were as follows *(dollar amounts in thousands)*:

	2001			2000		
	Senior Certificates		Subordinated Certificates	Senior Certificates		Subordinated Certificates
	Principal	Rate	Carrying Value	Principal	Rate	Carrying Value
1993—1 Pool	$ 45,227	7.7%	$ 2,156	$ 46,120	7.7%	$ 3,599
1994—1 Pool	34,499	9.9%	19,437	25,414	9.4%	38,066
1996—1 Pool	77,762	7.5%	14,126	81,534	7.5%	15,013
1998—1 Pool	113,150(1)	6.3%	37,435	115,223(1)	6.3%	38,284
			$ 73,154			$ 94,962

(1) Included in the 1998—1 Pool assets are $26,382,000 of certificates originated in the 1993—1 Pool that are excluded from the amount outstanding presented for the 1993—1 Pool.

At December 31, 2001 and 2000, the aggregate effective yield of the subordinated certificates, based on expected future cash flows with no unscheduled prepayments, was 18.05% and 17.11%, respectively. Income on the subordinated certificates was as follows for the years ended December 31, 2001, 2000 and 1999 *(dollar amounts in thousands)* :

	2001	2000	1999
1993—1 Pool	$ 929	$ 921	$ 1,504
1994—1 Pool	3,847	5,129	4,943
1996—1 Pool	3,128	3,338	3,447
1998—1 Pool	7,212	7,464	7,704
	$ 15,116	$ 16,852	$ 17,598

As sub-servicer for all of the above REMIC pools, the Company is responsible for performing substantially all of the servicing duties relating to the mortgage loans underlying the REMIC Certificates and will act as the special servicer to restructure any mortgage loans that default.

The REMIC Certificates retained by the Company, represent the non-investment grade certificates issued in the securitizations. Furthermore, because of the highly specialized nature of the underlying collateral (long-term care facilities), there is an extremely limited market for these securities. Because REMIC Certificates of this nature trade infrequently, if at all, market comparability to the certificates the Company retains is very limited.

The Company uses certain assumptions and estimates in determining the fair value allocated to the retained interest at the time of initial sale and each subsequent measurement date in accordance with SFAS No. 140. These assumptions and estimates include projections concerning the expected level and timing of future cash flows, current interest rate environment, estimated spreads over the U.S. Treasury Rate at which the retained certificates might trade, expectations regarding credit losses, if any, expected weighted-average life of the underlying collateral and discount rates commensurate with the risks involved. These assumptions are reviewed periodically by management. If these assumptions change, the related asset and income would be affected. Key economic assumptions used in measuring the retained interests at December 31, 2001 were as follows: a U.S. Treasury Rate of 5%, market spread on "B" rated certificates of 875 basis points over the applicable U.S. Treasury Rate, a weighted average discount rate on unrated and interest-only certificates of 29.1%, weighted-average life of 181 months and no expected annual credit losses. At December 31, 2001, key economic assumptions and the sensitivity of the current fair value of cash flows on the REMIC Certificates retained by the Company to immediate 10% and 20% adverse changes in those assumptions are as follows: *(dollar amounts in thousands)*

	Estimated Fair Value	Carrying Amount
Retained Interests in REMIC Securitizations:		
Available-for-sale REMIC Certificates	$ 19,814	$ 19,814
Held-to-maturity REMIC Certificates	34,325	53,340
Totals	$ 54,139	$ 73,154

	10% Adverse Change Decline in Fair Value	20% Adverse Change Decline in Fair Value
Key Assumption Sensitivity Analysis:		
Average Spread and Discount Rate Assumption		
Average Spread on "B" rated certificates—875 basis points	$ 335	$ 656
Average discount rate on Unrated and I/O certificates—29.1%	$ 2,924	5,520
Total	$ 3,259	$ 6,176
U.S. Treasury Rate Assumption (5.0%)	$ 194	$ 384
Weighted-Average Life Assumption (181 Months)	$ 583	$ 1,049
Expected Credit Loss Assumption (No Expected Losses)	$ 5,329	$ 10,658

During 2001, the Company sold certain REMIC Certificates classified as available-for-sale, with a net book value of $19,035,000 prior to a valuation reserve of $1,010,000 that was classified as available-for-sale. The sale resulted in net proceeds of $17,894,000 and a realized loss of $1,141,000.

As of December 31, 2001 and 2000, available-for-sale certificates were recorded at their fair value of approximately $19,814,000 and $42,362,000, respectively. Unrealized holding losses on available-for-sale certificates of $803,000 and $315,000 were included in comprehensive income for the years ended December 31, 2001 and 2000, respectively. At December 31, 2001 and 2000 held-to-maturity certificates had a book value of $53,340,000 and $52,600,000, respectively and a fair value of $34,325,000 and $32,241,000, respectively. As of December 31, 2001 none of the REMIC pools had experienced any realized losses nor had any of the Company's REMIC Certificate investments been determined to be permanently impaired.

7. Asset Securitizations

The Company is a REIT and, as such, makes its investments with the intent to hold them for long-term purposes. However, mortgage loans may be transferred to a REMIC (securitization) when a securitization provides the Company with the best available form of capital to fund additional long-term investments. When contemplating a securitization, consideration is given to the Company's current and expected future interest rate posture and liquidity and leverage position, as well as overall economic and financial market trends. As of December 31, 2001 the Company has completed four securitization transactions, however, no securitizations occurred during 2000 or 2001, nor is the Company under commitment to complete any securitization in the future.

From its past securitizations, the Company receives annual sub-servicing fees which range from 2.0 to 3.0 basis points of the outstanding mortgage loan balances in each of the REMIC pools. Additionally, through the REMIC Certificates retained by the Company from past securitizations, the Company receives cash flows and the rights to future cash flows resulting from cash received on the underlying mortgage loans in the REMIC pools. All of the investors in the REMIC Certificates and the REMIC Trusts themselves have no recourse to the Company's assets for failure by any obligor to the REMIC Trust assets (the mortgages) to pay when due, or comply with any provisions of the mortgage contracts. The REMIC Certificates are classified separately on the balance sheet and interest income earned shown separately on the income statement. Sub-servicing fees and related fees associated with the REMIC Certificates are included in other income.

Certain cash flows received from and paid to REMIC Trusts are as follows: *(dollar amounts in thousands)*

	Year Ended	
	2001	2000
Cash flow received on retained REMIC Certificates	$ 18,224	$ 18,940
Servicing and related fees received	$ 359	$ 336
Servicing advances made	$ 1,166	$ 2,052
Repayments of servicing advances	$ 1,532	$ 2,282

At December 31, 2001 scheduled distributions of principal on REMIC Certificates retained by the Company are: $0; $0; $7,804,000; $10,119,000; $6,609,000 and $38,894,000 for the years ending December 31, 2002, 2003, 2004, 2005, 2006 and thereafter. These amounts are based upon the scheduled remaining amortization periods of the underlying mortgages, which may be subject to change. Currently, the Company has no mortgage loans in its portfolio held for securitization. Quantitative information relating to subserviced mortgage loans including delinquencies and net credit losses is as follows: *(dollar amounts in thousands)*

	2001	2000	1999
Average balance of loans in REMIC pools	$ 340,607	$ 353,300	$ 372,292
Year-end balance of loans in REMIC pools	$ 334,394	$ 348,201	$ 361,896
Net credit losses	$ 0	$ 0	$ 0
Net credit losses to average REMIC pool loans	0%	0%	0%
Delinquencies (greater than 30 days) to year-end REMIC pool loans	0.7%	2.0%	2.2%

8. CLC Healthcare, Inc., formerly LTC Healthcare, Inc.

At LTC Healthcare Inc.'s annual meeting of stockholders held February 6, 2002, the stockholders approved a change in the name of LTC Healthcare, Inc. to CLC Healthcare, Inc. ("CLC").

During 1998, the Company completed the spin-off of all CLC voting common stock through a taxable dividend distribution to the holders of the Company's common stock, Cumulative Convertible Series C Preferred Stock and Convertible Subordinated Debentures. Upon completion of the distribution, CLC began operating as a separate public company. Beginning in September 1999, CLC began operating skilled nursing facilities owned or financed by the Company and from that date through the current date, assumed operations of additional facilities and closed certain facilities on the Company's behalf. These facilities were previously financed or leased to operators who experienced financial difficulties to such extent that the operators were not able to comply with lease provisions or debt provisions underlying the properties. As such, CLC primarily assumed operations for these properties that were in need of assistance. As a result CLC took over operations of troubled facilities and was not able to pay, nor did the Company record as income, rent under its leases or interest on its line of credit with the Company in 2001.

As of December 31, 2001, 24 of the Company's skilled nursing facilities with 2,651 beds, which represents approximately 9.8%, or $58,151,000 (including impairments totaling $2,964,000 on three facilities) of the Company's direct real estate investment portfolio were leased to CLC. Rents under these leases totaled approximately $3,148,000, annually. These leases were cancelled and replaced with new leases in January 2002 as more fully discussed below. In addition, CLC operates one skilled nursing facility securing a mortgage loan payable to a REMIC pool originated by the Company.

Subsequent to December 31, 2001, the Company sold to an unrelated party two properties in Illinois operated by CLC. CLC will continue to operate these facilities until the new owner obtains a license and regulatory approval. Additionally, subsequent to December 31, 2001, the Company agreed to sell a wholly owned subsidiary, LTC-Fort Tucum, Inc. to CLC for a $500,000 note bearing no interest for one year and thereafter interest at 8% annually for two years. CLC has certain rights to extend the note at its maturity. LTC-Fort Tucum, now owned by CLC has acquired two skilled nursing facilities in New Mexico, previously operated by Integrated Health Services, Inc., in a deed-in-lieu of foreclosure transaction. These properties are financed with debt from a REMIC pool originated by the Company. CLC expects to begin operating the two facilities during the second quarter of 2002. Additionally, in January 2002, the Company acquired a skilled nursing facility in Texas operated by CLC through the assumption of a $1,357,000 mortgage loan payable to a REMIC pool originated by the Company and a cash payment of $505,000.

As a result of the subsequent events, the Company leases 23 facilities to CLC under individual six-year leases that provide for total rents of $3,000,000; $4,000,000; $4,750,000; $5,350,000; $5,900,000 and $6,500,000 respectively, in years 2002 through 2007. The leases contain two five-year renewal options with increases of 2% annually. These leases have cross default provisions and a provision for acceleration should there be a change of control, as defined in the lease, of CLC. Additionally, CLC owns and operates the two New Mexico facilities discussed above that are financed with mortgage loans payable to a REMIC pool originated by the Company.

On November 21, 2001, the Company entered into a Securities Purchase Agreement with CLC pursuant to which the Company purchased from CLC $8,500,000 face value of 7.5% convertible subordinated debentures of Regent for $7,800,000. The purchase price represented the Company's estimate of the fair market value of the debentures. The Company purchased these debentures to add them with other Regent debentures the Company had acquired and to use the total debentures as part of the consideration necessary to acquire two assisted living centers from Regent. These acquired facilities were leased to an unrelated party at an annual lease amount in the first year of $1,800,000. The lease is for 10 years and increases by $200,000 in the second and third years, by $100,000 in years four and five and then by 2% each year thereafter. The purchase price of $7,800,000 was applied to reduce the total indebtedness owed by CLC to the Company.

On December 17, 2001, the Company entered into an Assignment and Assumption Agreement ("Agreement") with Healthcare Holdings, Inc. ("Holdings"), a wholly owned subsidiary of CLC, to sell to Holdings the right to receive common stock of ALC to be distributed pursuant to the First Amended Joint Plan of Reorganization of Assisted Living Concepts, Inc. and Carriage House Assisted Living, Inc. ("Plan"). The Plan was subsequently confirmed at a hearing on December 5, 2001.

On December 31, 2001, Holdings issued a Promissory Note ("Note") in accordance with the Agreement in the face amount of $7,000,000 in payment for the right to receive 1,238,076 shares of ALC common stock distributed pursuant to the Plan (approximately $5.65 per share). The price of the shares was determined by reference to Exhibit G, Volume II of II of ALC's First Amended Joint Plan of Reorganization. This Exhibit G reported that the projected stockholders' equity of ALC upon emergence from bankruptcy to be $32,799,000 and to be $37,117,000 on December 31, 2002. ALC issued 6,500,000 shares of new common stock at emergence which results in a calculated valuation of $5.05 and $5.71 per share value as of January 1, 2002 and December 31, 2002, respectively. The Note is for a term of five years and bears interest at 5.0%, compounded annually and accruing to the principal balance plus interest at 2.0% on the original principal of $7,000,000 payable in cash annually. The Note is a full recourse obligation of Holdings and is secured by all of the assets owned now or in the future by Holdings and contains a provision for acceleration should there be a change of control of Holdings or CLC.

Prior to ALC's emergence from bankruptcy, Holdings owned $5,715,000 face value of ALC's 5.625% convertible subordinated debentures and 30,847 shares of ALC's common stock. As a result of the Plan, Holdings received $1,382,000 of ALC's new Senior Secured Notes bearing interest at 10.0% per annum, payable semi-annually in arrears; $524,000 of new Junior Secured Notes bearing interest payable in additional new Junior Secured Notes for three years at 8.0% per annum and thereafter payable in cash at 12.0% per annum, payable semi-annually in arrears and 214,250 shares of ALC common stock. Additionally, Holdings received 468 shares of ALC common stock in exchange for the 30,847 shares owned prior to emergence. All of these securities are additional collateral for the $7,000,000 note but have not been given value on the Company's balance sheet. At December 31, 2001, the fair market value of these additional securities was approximately $2,052,000. At December 31, 2001, the Company recorded the Note at a value of approximately $3,095,000 which represented only the then fair market value of the 1,238,076 shares acquired by Holdings pursuant to the Agreement.

On December 20, 2001, the Company entered into an agreement to acquire from CLC six skilled nursing facilities and four assisted living facilities. The total purchase price was approximately $45,860,000 subject to mortgage debt assumed of approximately $33,062,000 and minority interest of approximately $3,518,000. Of the mortgage debt assumed, $16,395,000 was payable to REMIC pools originated by the Company and $16,667,000 of mortgage debt was payable to an unrelated third party. The Company and CLC relied on current appraisals of the properties in establishing the purchase/sale price. The $9,285,000 net proceeds from this transaction were used by CLC to reduce their total indebtedness to the Company. These properties will generate approximately $3,760,000 in annual rental income before debt service costs of $2,997,000 (of which $2,529,000 is interest expense and $467,000 is principal) resulting in $1,231,000 in additional future earnings.

Additionally, in December 2001, the Company agreed to forgive approximately $4,401,000 in amounts owed by CLC to the Company, which the Company had not recognized as income. This forgiveness was granted to compensate CLC for assuming operations and absorbing losses on certain facilities that the Company and CLC agreed should be, and subsequently were, closed. This and the other transactions mentioned above reduced CLC's indebtedness to the Company under the line of credit to $5,342,000 at December 31, 2001.

Cumulatively, the above transactions reduced CLC's indebtedness to the Company by approximately $21,485,000 and will (not including recording interest income on the $7,000,000 note) increase the Company's rental income by approximately $5,560,000 and net cash flow after debt service payments by approximately $1,297,000 in 2002.

All of the aforementioned transactions between the Company and CLC were approved by the respective disinterested and/or independent members of the Board of Directors of each company. All interested and/or non-independent Board members abstained from any such vote.

In February 2002, the independent members of CLC's Board of Directors approved, in principle, an Administrative Services Agreement between CLC and the Company. This agreement would terminate on June 30, 2007 and provide that during its term, the Company will provide office space and certain management and administrative services to CLC for a fee of approximately $1,000,000 per year beginning as of July 1, 2002. Currently, several of the Company's Directors and Officers also serve as Directors and/or Officers of CLC.

In April 2001, the Company's Board of Directors approved an indemnification agreement covering four of the Company's officers who also serve as officers of CLC and one current CLC outside director.

During 2001, the Company sold all 180,000 shares of CLC common stock it owned at December 31, 2000. The shares were sold to CLC for $225,000, excluding selling commissions, which was the fair market value as of the date of sale. The Company recognized a loss of $386,000 on the sale of these shares. The Company sold these shares because the recently enacted Tax Relief Extension Act of 1999 ("Act") provides that, subject to certain exceptions for taxable years commencing after December 31, 2000, a REIT may not own more than 10% of the total value of the securities of any corporation. Without qualifying as safe harbor debt, securities under the Act include the line of credit provided by the Company to CLC. In order to qualify as safe harbor debt and retain REIT status, the Company was required to hold only such debt or the shares. As of December 31, 2000 and 1999, the Company owned 180,000 and 239,000 shares, respectively, of CLC common stock. At December 31, 2000 and 1999, the Company's investment in CLC common stock was recorded at its fair value of $236,000 and $480,000, respectively, in the accompanying balance sheet. An unrealized holding loss of $185,000 and $181,000, respectively, is included in comprehensive income for the years ended December 31, 2000 and 1999.

The Company has provided CLC with a $20,000,000 secured line of credit that bears interest at 10% and matures in April 1, 2008. This agreement contains a provision for acceleration should there be a change of control of CLC. As of December 31, 2001, and 2000, $5,342,000 and $16,582,000, respectively, was outstanding under the line of credit. Under the terms of our Senior Secured Revolving Line of Credit, the Company is permitted to loan CLC up to $25,000,000. The Company and CLC have not increased the $20,000,000 secured line of credit between the companies. Should any such amendment be proposed, it would need approval of the independent Board members of each company's board. During the years ended December 31, 2001 and 2000, the Company recorded interest income of $0 and $1,713,000, respectively on the average outstanding principal balance under the line of credit.

While the Company believes that CLC has significantly improved the operations of the nursing facilities it operates, the Company will continue to record amounts due from CLC based on the Company's evaluation of collectibility during 2002.

On June 23, 2000, the Company's Board of Directors appointed CLC as the Company's exclusive sales agent for all skilled nursing facilities for a period of one year and approved a commission agreement with CLC. Pursuant to the agreements, during 2000, the Company paid CLC sales commissions of $1,600,000. During 1999, the Company had an administrative services agreement with CLC. Accordingly, CLC reimbursed the Company for administrative and management advisory services in the amount of $740,000 for the year. The administrative services agreement was suspended effective January 1, 2000. The Company received no reimbursement for administrative and management advisory services in 2000 or 2001.

Pursuant to an intercompany agreement entered into at the time CLC was formed, CLC has agreed not to engage in activities or make investments that involve real estate, unless it has first provided written notice to the Company of the material terms and conditions of such activities or investments, and the Company has determined not to pursue such activities or investments either by providing written notice to CLC rejecting the opportunity or by allowing a 10-day notice period to lapse. Pursuant to the intercompany agreement, CLC and the Company also agreed to notify each other of, and make available to each other, investment opportunities that they develop or of which they become aware but are unable or unwilling to pursue. The intercompany agreement has a term of 10 years but shall terminate earlier upon a change of control of the Company.

As of December 31, 2000, 29 skilled nursing facilities with a gross carrying value of $67,107,000 were leased to CLC. Also as of December 31, 2000, CLC had mortgage loans secured by six skilled nursing facilities with a total outstanding principal of $16,433,000 and a weighted average interest rate of 9.25% payable to REMIC pools originated by the Company. During 2000, the Company recorded rental income of approximately $6,176,000 on properties leased to CLC.

As of December 31,1999, 17 skilled nursing facilities with a gross carrying value of $36,055,000 were leased to CLC. Also, as of December 31, 1999, CLC had mortgage loans secured by eight skilled nursing facilities with total outstanding principal of $30,424,000 and a weighted average interest rate of 9.18% payable to the Company's REMIC pools. During 1999, the Company recorded rental income of approximately $779,000 on properties leased to CLC.

9. Notes Receivable

During 2001, the Company received notes receivable of $8,483,000 in conjunction with the sale of two schools and two skilled nursing facilities. The notes mature in 2002, 2003 and 2004 and have a combined weighted average interest rate of 10.2%. Subsequent to December 31, 2001, one note from a school sale in the amount of $1,585,000 was paid at maturity. Additionally the Company received a five-year, $7,000,000, face value, note from CLC in connection with the sale of the right to receive ALC stock. The Company has recorded this note at a value of $3,095,000. (See *Note 8*. *CLC Healthcare, Inc., formerly LTC Healthcare, Inc.*) Interest of 2% is due annually and interest of 5% accrues to the principal balance of the note.

During 2000, the Company received three short term notes receivable of $3,055,000 in conjunction with the sale of one skilled nursing facility, one assisted living facility and one school. Two of the notes totaling $2,955,000 were paid at maturity in 2001. The remaining note of $100,000 is interest only and matures in 2002. Additionally, the Company received a three-year, interest only, $2,000,000 note with an interest rate of 10%. This note is a deposit on a skilled nursing facility in Florida. The gross sales price of this facility is approximately $6,000,000.

10. Marketable Debt Securities

As of December 31, 2000 the Company had acquired $4,195,000 face amount of ALC 5.625% convertible subordinated debentures due May 2003 and $15,645,000 face amount of ALC 6.0% convertible subordinated debentures due November 2002 for an aggregate purchase price of $13,097,000. The amortized cost and fair value as of December 31, 2000 was $15,873,000 and $8,696,000, respectively.

During 2001, the Company purchased $3,833,000 and $6,875,000 face value of the 5.625% and 6.0% debentures, respectively, for approximately $2,784,000. During the first three quarters of 2001, the Company recorded an impairment charge of $9,829,000 related to the investment in ALC debentures and recorded no interest accretion or interest income relating to these debentures in 2001. Thus, prior to ALC's reorganization discussed below, the Company owned $30,548,000 in face amount of ALC debentures.

In October 2001, ALC filed for reorganization under Chapter 11 of the federal bankruptcy laws. (See Note 3. *Major Operators.*) The filing was pre-negotiated with sufficient debt holders to allow for ALC to reorganize its debt and equity and emerge from bankruptcy as of 12:01 a.m. on January 1, 2002. The final order affirming the reorganization was made in December 2001, consequently the Company reflected the transactions as of December 31, 2001. The Company agreed to reduce rents under leases with ALC by $875,000 a year beginning January 1, 2002, and received a lease rejection claim of $2,500,000 for this concession. Under the provisions of ALC's reorganization plan at the date of emergence from bankruptcy, the Company was entitled to receive, in addition to common stock, due to its ownership of the subordinated debentures and lease rejection claim, $7,986,000 of ALC's new Senior Secured Notes bearing interest at 10% per annum, payable semi-annually in arrears and $3,026,000 of new Junior Secured Notes bearing interest payable in additional new Junior Secured Notes for three years at 8% and thereafter payable in cash at 12% per annum, payable semi-annually in arrears.

At December 31, 2001, the Company had recorded new Senior Secured Notes at their estimated fair market value of $6,788,000 and the new Junior Secured Notes at their estimated fair market value of $1,967,000. This resulted in a credit to comprehensive income of approximately $3,610,000. The estimated fair value is based on recent quotes from a broker, who trades in these securities.

11. Debt Obligations

Bank Borrowings. On October 31, 2000, the Company entered into a new Senior Secured Revolving Line of Credit Agreement (the "Senior Secured Revolving Line of Credit") that expires on October 2, 2004. The Senior Secured Revolving Line of Credit initially provided for $185,000,000 of total commitments with periodic reductions of these commitments to fully retire the commitments as of October 2, 2004. As of December 31, 2001, commitments outstanding were $120,000,000. Specifically scheduled available commitments as of December 31, 2002 and 2003 are $95,000,000 and $75,000,000 respectively. The credit facility also requires the Company to pay an additional fee of 4% of the then outstanding available commitment level as of October 2, 2002. The scheduled commitment level as of October 2, 2002 is $95,000,000. Another provision of this agreement requires certain levels of commitment reductions as a result of asset sales, financings, equity offerings and repayment of mortgages. As a result of sales of assets during 2000, the available commitment balance at December 31, 2000 was $173,960,000.

The Senior Secured Revolving Line of Credit pricing varies between LIBOR plus 2.00% and LIBOR plus 3.00% depending on the Company's leverage ratio and at December 31, 2000 the Company's weighted average interest rate was 9.215%, reflecting a pricing of LIBOR plus 2.50%. During 2001, the Company borrowed $50,000,000 and repaid $64,000,000 under this credit facility. As of December 31, 2001 borrowings of $104,000,000 bearing interest at LIBOR plus 2.25% (4.3225% weighted average) were outstanding under this credit facility and the Company had reduced the commitment level from $185,000,000 at inception to $120,000,000.

Subsequent to December 31, 2001, the Company received two mortgage loan repayments, totaling approximately $3,387,000. Current provisions of the credit facility requires the Company to apply 50% of Net Cash Proceeds, as defined in the credit facility, to reduce outstanding commitments and as such, commitments were reduced to $118,300,000 in February 2002.

Under covenants contained in the credit agreement, the Company is required to maintain, among other things, at December 31, 2001: (i) a ratio of senior debt to tangible net equity of no more than 0.65 to 1.0; (ii) a ratio of funded debt to tangible net equity of no greater than 1.0 to 1.0; (iii) a minimum tangible net worth of at least $300,000,000; and (iv) a ratio of cash flow to interest expense of at least 1.5 to 1.0. Covenant (iii) decreases to a minimum of tangible net worth of at least $275,000,000 when commitments drop to $100,000,000 or less. The Company is in compliance with all covenants at December 31, 2001. Beginning in January 2003, the credit facility commitments reduce by $5,000,000 and then every three months by additional $5,000,000 reductions to a final balance of $60,000,000 due at maturity.

In addition to the 4% fee payable on October 2, 2002, the Company must issue book value units to the lenders under the Company's Secured Line of Credit that entitle them to a right to participate in any increase in the Company's book value per common share (measured at September 30, 2004) in excess of the Company's book value per common share at September 30, 2000, less $2.00 per share from such excess. The Company is required to issue 20,000 book value units for each $1,000,000 of outstanding commitments at October 2, 2002. The Company's book value per common share at September 30, 2000 was $8.92, thus, the book value per common share at September 30, 2004 would have to be in excess of $10.92 in order for the Company to be obligated to pay any money to the lenders for their book value units. At December 31, 2001, the Company's book value per common share was $9.53 and outstanding commitments under the Company's Secured Line of Credit were $120,000,000; however, the Company is required to reduce commitments to $95,000,000 on October 1, 2002. Assuming outstanding commitments were $95,000,000 on October 2, 2002, the Company would be required to issue to the lenders 1,900,000 book value units. The Company will still be obligated to pay the lenders any amounts due them relating to the book value units as of September 30, 2004, even if the Company repays in full and terminates the Secured Line of Credit after October 2, 2002.

Under the terms of the Senior Secured Revolving Line of Credit the Company is limited in any fiscal year from paying total common and preferred cash dividends to no more than 110% of consolidated taxable income. At inception, $183,290,000 of owned properties, $113,842,000 of mortgage loans receivable and $96,332,000 of REMIC Certificates were pledged as collateral. At December 31, 2001, $189,417,000 of owned properties and all of the Company's mortgage loans and REMIC Certificates were pledged as collateral. Additional provisions in the Senior Secured Revolving Line of Credit provide for the release of certain collateral when the commitments are reduced to $100,000,000 or less and $60,000,000 or less. The credit facility allows the Company to buy back its stock once the commitments are $135,000,000 or less.

On November 2, 1998, the Company entered into an interest rate swap agreement whereby the Company effectively fixed the interest rate on LIBOR based variable rate debt. Under this agreement, which expired in November 2000, the Company was credited interest at three month LIBOR and paid interest at a fixed rate of 4.74% on a notional amount of $50,000,000. The differential paid or received on the interest rate swap was recognized as an adjustment to interest expense. During 1999, the Company received $657,000 upon early termination of the interest rate swap that was amortized over the term of the original swap agreement.

Convertible Subordinated Debentures (dollar amounts in thousands):

Interest Rate	Maturity	Conversion Price per share	Outstanding Principal at December 31, 2001	2000
8.50%	January 2001	$ 15.50	$ —	$ 11,849
7.75%	January 2002	$ 16.50	2,408	2,408
8.25%	July 2001	$ 17.25	—	10,385
			$ 2,408	$ 24,642

On January 2, 2001 the Company borrowed $12,000,000 under the Company's credit facility to pay in full the 8.50% and on July 1, 2001 the Company borrowed $5,000,000 under the Company's credit facility and used $5,385,000 of cash on hand to pay in full the 8.25% Convertible Subordinated Debentures.

On January 2, 2002, the Company paid with cash on hand $2,408,000 to retire the 7.75% Convertible Subordinated Debentures.

Mortgage Loans Payable. During 2001, the Company acquired six skilled nursing facilities and six assisted living facilities that were subject to the assumption of existing non-recourse mortgage debt totaling $50,774,000 that bears interest at a weighted average rate of 8.36% and matures on various dates over the next 27 years.

Mortgage loans payable and weighted average interest rates were (*dollar amounts in thousands*):

Maturity	December 31, 2001	Rate	December 31, 2000	Rate
2002	$ 11,126	12.00%	$ 14,413	10.87%
2003	13,852	12.00%	16,071	11.96%
2004	5,387	11.63%	3,889	11.50%
2005	28,842	9.43%	11,172	11.64%
2006	39,014	9.25%	39,495	9.25%
Thereafter	64,011	8.22%	18,301	8.81%
	$ 162,232		$ 103,341	

As of December 31, 2001 and 2000, the aggregate carrying value of real estate properties securing the Company's mortgage loans payable was $222,619,000 and $145,644,000, respectively.

Bonds Payable and Capital Leases. At December 31, 2001 and 2000, the Company had outstanding principal of $7,265,000 and $7,550,000, respectively on multifamily tax-exempt revenue bonds that are secured by five assisted living facilities in Washington. These bonds bear interest at a variable rate that is reset weekly and matures during 2015. For the year ended December 31, 2001, the weighted average interest rate, including letter of credit fees, on the outstanding bonds was 6.0%. Additionally, at December 31, 2001 and 2000, the Company had outstanding principal of $4,076,000 and $4,127,000, respectively on a multi-unit housing tax-exempt revenue bond that bears interest at 8.75% and matures in 2025 and is secured by one assisted living facility in Oregon.

At December 31, 2001 and 2000, the Company had outstanding principal of $4,653,000 and $4,900,000, respectively, under capital lease obligations. The capital leases are secured by four assisted living residences, have a weighted average interest rate of 7.6% and mature at various dates through 2013.

As of December 31, 2001 and 2000, the aggregate gross investment in real estate properties securing the Company's bonds payable and capital leases was $25,719,000.

Scheduled Principal Payments. Total scheduled principal payments for the mortgage loans payable, bonds payable and capital lease obligations as of December 31, 2001 were $13,972,000, $16,572,000, $8,248,000, $29,433,000, $38,459,000 and $71,542,000 in 2002, 2003, 2004, 2005, 2006 and thereafter.

12. Stockholders' Equity

Issuance of Stock. The Company's Series C Preferred Stock is convertible into 2,000,000 shares of the Company's common stock, has a liquidation value of $19.25 per share and has an annual coupon of 8.5%, payable quarterly. Total shares reserved for issuance of common stock related to the conversion of Series C Preferred Stock were 2,000,000 shares at December 31, 2001, 2000 and 1999.

During 2001, the Company repurchased and retired 10,800 shares of 9.5% Series A Cumulative Preferred Stock ("Series A Preferred Stock") for $197,000 and 7,000 shares of 9.0% Series B Cumulative Preferred Stock ("Series B Preferred Stock") for $120,000. At December 31, 2001, 3,069,200 shares of Series A Cumulative Preferred Stock and 1,993,000 shares of Series B Cumulative Preferred Stock were outstanding. Dividends on the Series A Preferred Stock and Series B Preferred Stock are cumulative from the date of original issue and are payable monthly to stockholders of record on the first day of each month. Dividends on the Series A Preferred Stock and the Series B Preferred Stock accrue at 9.5% and 9.0% per annum, respectively, on the $25.00 liquidation value per share (equivalent to a fixed annual amount of $2.375 and $2.25 per share, respectively). Both the Series A Preferred Stock and Series B Preferred Stock are currently redeemable at the $25.00 liquidation value per share. We currently do not have the intention to redeem either the Series A or Series B Preferred Stock; however, the Company may buy, from time to time, shares of the Series A and/or B Preferred Stock in the open market.

The liquidation preferences of Series A Preferred Stock, Series B Preferred Stock and Series C Preferred Stock are *pari passu*. Neither the Series A Preferred Stock, Series B Preferred Stock nor Series C Preferred Stock have any voting rights.

Repurchase of Common Stock. During the year ended December 31, 2001, the Company repurchased and retired 7,588,196 shares of common stock for an aggregate purchase price of approximately $41,737,000, an average of $5.50 per share. Of the shares repurchased, 6,060,996 were purchased pursuant to a tender offer for 6,000,000 shares, plus up to 2% of outstanding shares as allowed by tender offer regulations, at $5.75 per share plus costs. The balance of 1,527,200 shares were purchased on the open market under a Board authorization to purchase up to 5,000,000 shares. Therefore, the Company continues to have an open Board authorization to purchase an additional 3,472,800 shares.

During 2000 and 1999 the Company repurchased and retired 1,005,600 and 649,800 shares of common stock, respectively, for an aggregate purchase price of $7,969,000 and $7,039,000, respectively.

Stock Based Compensation Plans. During 1998, the Company adopted and its stockholders approved the 1998 Equity Participation Plan under which 500,000 shares of common stock have been reserved for stock based compensation awards. The 1998 Equity Participation Plan and the Company's Restated 1992 Stock Option Plan under which 500,000 shares of common stock were reserved (collectively "the Plans") provide for the issuance of incentive and nonqualified stock options, restricted stock and other stock based awards to officers, employees, non-employee directors and consultants. The terms of awards granted under the Plans are set by the Company's compensation committee at its discretion; however, in the case of incentive stock options, the term may not exceed 10 years from the date of grant. Total shares available for grant under the Plans as of December 31, 2001, 2000 and 1999 were 28,776, 19,880 and 507,040, respectively. We also utilized 5,000 shares authorized under the Plans to contribute to the Company's deferred compensation plan. All options outstanding vest over five years from the original date of grant. Unexercised options expire seven years after the date of vesting.

Nonqualified stock option activity for the years ended December 31, 2001, 2000 and 1999 was as follows:

	Shares			Weighted Average Price		
	2001	2000	1999	2001	2000	1999
Outstanding, January 1	509,000	23,000	23,000	$ 5.74	$ 14.86	$ 14.86
Granted	102,000	517,500	—	$ 5.29	$ 5.41	—
Exercised	—	—	—	—	—	—
Canceled	(66,000)	(31,500)	—	$ 7.73	$ 7.04	—
Outstanding, December 31	545,000	509,000	23,000	$ 5.41	$ 5.74	$ 14.86
Exercisable, December 31	102,000	16,500	18,000	$ 5.55	$ 15.41	$ 14.26

Restricted stock activity for the years ended December 31, 2001, 2000 and 1999 was as follows:

	2001	2000	1999
Outstanding, January 1	265,560	264,400	393,000
Granted	—	23,000	448,800
Vested	(6,500)	—	(128,560)
Canceled	(49,896)	(21,840)	(448,840)
Outstanding, December 31	209,164	265,560	264,400
Compensation Expense	$ 24,000	$ —	$ —

In 2000, restricted stock awards aggregating 23,000 shares with a weighted average fair value on the dates of grant of $8.07 per share were granted to employees. These grants vest evenly over four or five years with the first vesting in January 2001.

In March 1999, all outstanding shares of restricted stock as of that date were cancelled. Subsequently, restricted stock awards aggregating 448,800 shares with a weighted average fair value on the date of grant of $11.50 per share were granted to employees and non-employee directors. Each grantee will vest shares equal to 10% of their total grant per year if the Company meets certain financial objectives and the grantee remains employed by the Company. If, in any given year, the Company does not meet the stated financial objectives then the shares scheduled to vest in that year will not vest and the vesting period will be extended by one year. There was no vesting in these restricted shares during 2001, 2000 or 1999. During 2000 and 1999, certain recipients of restricted stock awarded in those years immediately vested in a portion of such shares. Compensation expense related to the vested shares approximated compensation expense recognized in prior years on the unvested shares that were cancelled in 1999. Future compensation expense will be recognized over the service period at the market price per share on the date of vesting. None of these shares of restricted stock vested in 2000.

Dividends are payable on the restricted shares to the extent and on the same date as dividends are paid on all of the Company’s common stock.

As of December 31, 2001, 2000, and 1999, there were 545,000, 509,000, and 23,000 options outstanding, respectively, subject to the disclosure requirements of SFAS No. 123. The fair value of these options was estimated utilizing the Black-Scholes valuation model and assumptions as of each respective grant date. In determining the estimated fair values for the options granted in 2001 and 2000, the weighted average expected life assumption was five years, the weighted average volatility was 0.49 and the weighted average risk free interest rate was 4.48%. The weighted average fair value of the options granted was estimated to be $1.46. There was no material pro-forma effect on net income or earnings per share for the years ending December 31, 2001, 2000, and 1999. The weighted average exercise price of the options was $5.29, $5.38 and $15.65 and the weighted average remaining contractual life was 5.0, 4.3, and 5.9 years as of December 31, 2001, 2000, and 1999, respectively.

Notes Receivable from Stockholders. In 1997, the Board of Directors adopted a loan program designed to encourage executives, key employees, consultants and directors to acquire common stock through the exercise of options. Under the program, the Company made full recourse, secured loans to participants equal to the exercise price of vested options plus up to 50% of the taxable income resulting from the exercise of options. Such loans bear interest at the then current Applicable Federal Rate ("AFR"). In January 2000, the Board of Directors approved a new loan agreement for current executives and directors in the amounts of the then remaining principal balance of the original loans.

The current loan agreements provide that the interest rate is 6.07% (AFR for an equivalent 3 to 9 year instrument) and interest payments to be paid from dividends received on shares pledged as security for the notes during the quarter in which the interest is due. If the dividend does not fully pay the interest due or if no dividend is paid, the unpaid interest is added to the principal balance. In addition, the notes also require the borrower to reduce principal by one-half of the difference between the most recent dividend received on the pledged shares and the interest paid on the loans from that dividend. No dividend was paid on the Company's common shares in 2001 and all interest due on these loans was accrued to the principal amounts.

During 2001, the Company granted a reduction in the loans to officers and Board Members with such loans. The loans were reduced to the sum of the shares collateralizing the notes times the net book value ("NBV") of a share of common stock as of September 30, 2001. The NBV per share at that date was $8.60 and the closing price as reported by the NYSE was $5.13. This total reduction amounted to a non-cash charge of $2,453,000. The Company accounts for the shares underlying the loans that were modified under variable plan accounting as required by SFAS 123 "*Accounting for Stock Based Compensation*".

Of this reduction, $1,617,000 was for the loan to the Company's Chairman, CEO and President, Mr. Andre C. Dimitriadis. At December 31, 2001, Mr. Dimitriadis owned 1,103,619 shares of the Company's common stock including the 333,500 shares collateralizing his note and 66,299 shares held in the Company's deferred compensation plan. Since inception of the note in 1997 and as of December 31, 2001, Mr. Dimitriadis has paid in cash $856,000 in interest and $615,000 in principal reduction relating to this note. As a result of his loan reduction, Mr. Dimitriadis was excluded from participating in the bonus program in 2001. Approximately $437,000, in the aggregate, of the reduction was granted to two members of the Board of Directors who each own 46,000 shares collateralizing the loans.

Of the 102,000 stock options granted in 2001, none were granted to Mr. Dimitriadis or the two members of the Board mentioned above.

The remaining $399,000 reduction in stockholder notes was granted to three officers of the Company. The aggregate shares collateralizing these loans is 96,500.

The maturity date of these notes is December 31, 2008 and at that time the remaining principal amount is due in full. Additionally, the notes contain a provision that allows the borrower the option of fully discharging the then remaining principal balance of the loan by tendering the pledged shares as full payment upon the event of a change of control of the Company or upon the death of the borrower.

Unless the Board of Directors approves otherwise, loans must be repaid within 90 days after termination of employment for any reason, other than in connection with a change of control of the Company. In 2001, the Board of Directors approved the continuation of the December 31, 2008 maturity for one officer who resigned from the Company.

The Company continues to have three notes due from two former officers and the estate of a former Board Member. These notes were not modified in 2000 or during 2001 and the interest was paid quarterly and is current on all of these notes. These remaining original notes provide for the same calculation of the periodic principal reductions; however, interest is payable every quarter, regardless of receipt of a dividend. The original notes convert to fully amortizing loans with 16 quarterly payments beginning in 2002. The original notes bear interest rates ranging from 5.77% to 6.63%.

The Company has no other loan programs for officers and/or directors and does not provide any guarantee to any officer and/or director or third party relating to purchases and sales of the Company's common stock.

The Company no longer makes loans under this program and has not made a loan since 1998. At December 31, 2001, 2000 and 1999, loans totaling $8,042,000, $10,126,000 and $10,258,000, respectively were outstanding. At December 31, 2001, 2000 and 1999, the market value of the common stock securing these loans was approximately $4,972,000, $2,968,000 and $6,691,000, respectively.

13. Contingencies

The Company currently requires, and intends to continue to require, all borrowers of funds from the Company and lessees of any of the Company's properties to secure adequate comprehensive property and general and professional liability insurance that covers the Company, as well as the borrower and/or lessee. Recently, the cost of such insurance has increased substantially and some insurers have stopped offering such insurance for nursing homes. The unavailability and increased cost of such insurance could have a material adverse effect on the ability of the lessees and operators, including their ability to make lease or mortgage payments. In addition, certain risks may be uninsurable, not economically insurable or insurance is not available and there can be no assurance that the Company, a borrower or a lessee will have adequate funds to cover all contingencies itself. Certain losses such as losses due to floods or seismic activity if insurance is available may be insured subject to certain limitations including large deductibles or co-payments and policy limits. If an uninsured loss or a loss in excess of insured limits occurs with respect to one or more of the Company's properties, the Company could be subject to an adverse claim including claims for general or professional liability; lose the capital the it has invested in the properties, as well as the anticipated future revenue from the properties and, in the case of debt which is with recourse to the Company, the Company would remain obligated for any mortgage debt or other financial obligations related to the properties.

14. Distributions

The Company must distribute at least 90% of its taxable income in order to continue to qualify as a REIT. This distribution requirement can be satisfied by current year distributions or by distributions in the following year.

For federal tax purposes, distributions to stockholders are treated as ordinary income, capital gains, return of capital or a combination thereof. Distributions for 2000 and 1999 were cash distributions. There were no distributions for common stock in 2001.

The federal income tax classification of the per share common stock distributions are (unaudited):

	2001	2000	1999
Ordinary income	$ —	$ 0.701	$ 1.185
Non-taxable distribution	—	—	0.375
Section 1250 capital gain	—	0.146	—
Long term capital gain	—	0.023	—
Total	$ —	$ 0.870	$ 1.560

15. Net (Loss) Income Per Share

Basic and diluted net income per share were as follows *(in thousands except per share amounts)*:

	2001	2000	1999
Net (loss) income	$ (2,908)	$ 31,637	$ 31,827
Preferred dividends	(15,077)	(15,087)	(15,087)
Net (loss) income for basic net income per share	(17,985)	16,550	16,740
7.75% debentures due 2002	—	—	—
8.5% debentures due 2000	—	—	—
8.25% debentures due 1999	—	—	—
Other dilutive securities	—	—	—
Net (loss) income for diluted net income (loss) per share	$ (17,985)	$ 16,550	$ 16,740
Shares for basic net income per share	23,924	26,108	27,412
Stock options	—	—	—
7.75% debentures due 2002	—	—	—
8.5% debentures due 2000	—	—	—
8.25% debentures due 1999	—	—	—
Other dilutive securities	—	—	—
Shares for diluted net income per share	23,924	26,108	27,412
Basic net (loss) income per share	$ (0.75)	$ 0.63	$ 0.61
Diluted net (loss) income per share	$ (0.75)	$ 0.63	$ 0.61

The conversion of subordinated debentures and stock options were anti-dilutive in 2001, 2000 and 1999.

16. Quarterly Financial Information (Unaudited)

	Quarter ended			
	March 31,	June 30,	September 30,	December 31,
	(in thousands except per share amounts)			
2001				
Revenues	$ 18,278	$ 18,081	$ 17,057	$ 16,696
Net income (loss) available to common stockholders(1)	294	(15,403)	2,295	(5,171)
Basic net income (loss) per share	$ 0.01	$ (0.61)	$ 0.09	$ (0.26)
Diluted net income (loss) per share	$ 0.01	$ (0.61)	$ 0.09	$ (0.26)
Dividends per share	—	—	—	—
2000				
Revenues	$ 22,506	$ 22,717	$ 21,536	$ 20,371
Net income (loss) available to common stockholders(2)	6,903	6,081	6,518	(2,952)
Basic net income (loss) per share	0.26	0.23	0.25	(0.11)
Diluted net income (loss) per share	0.26	0.23	0.25	(0.11)
Dividends per share	0.29	0.29	0.29	0.00

(1) Includes impairment charges totaling $28,584. See *Note 5. Impairment Charge*.

(2) Includes impairment charges totaling $14,822. See *Note 5. Impairment Charge*.

Item 9. CHANGES IN AND DISAGREEMENTS WITH ACCOUNTANTS ON ACCOUNTING AND FINANCIAL DISCLOSURE

None.

Item 10. DIRECTORS AND EXECUTIVE OFFICERS OF THE COMPANY

Incorporated herein by reference from the Company’s definitive proxy statement for the Annual Meeting of Stockholders to be filed pursuant to Regulation 14A.

Item 11. EXECUTIVE COMPENSATION

Incorporated herein by reference from the Company’s definitive proxy statement for the Annual Meeting of Stockholders to be filed pursuant to Regulation 14A.

Item 12. SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT

Incorporated herein by reference from the Company’s definitive proxy statement for the Annual Meeting of Stockholders to be filed pursuant to Regulation 14A.

Item 13. CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS

Incorporated herein by reference from the Company’s definitive proxy statement for the Annual Meeting of Stockholders to be filed pursuant to Regulation 14A.

Item 14. FINANCIAL STATEMENT SCHEDULES, EXHIBITS AND REPORTS ON FORM 8-K.

(a) *Financial Statement Schedules*

The financial statement schedules listed in the accompanying index to financial statement schedules are filed as part of this annual report.

(b) *Exhibits*

The exhibits listed in the accompanying index to exhibits are filed as part of this annual report.

(c) *Reports on Form 8-K*

None.

INDEX TO FINANCIAL STATEMENT SCHEDULES
(Item 14(a))

All other schedules have been omitted since the required information is not present or not present in amounts sufficient to require submission of the schedule.

LTC PROPERTIES, INC.

SCHEDULE II
VALUATION AND QUALIFYING ACCOUNTS
(in thousands)

	Balance at Beginning of Period	Charge to Operations	Balance at End of Period
Allowance for Doubtful Accounts:			
2001	$ 1,250	$ —	$ 1,250
2000	$ 1,250	$ —	$ 1,250
1999	$ 1,250	$ —	$ 1,250

LTC PROPERTIES, INC.

SCHEDULE III

REAL ESTATE AND ACCUMULATED DEPRECIATION
(In thousands)

	Encumbrances	Initial Cost to Company Land	Building and Improvements	Costs Capitalized Subsequent to Acquisition	Gross Amount at which carried at December 31, 2001 Land	Gross Amount at which carried at December 31, 2001 Building and Improvements	Gross Amount at which carried at December 31, 2001 Total(1)	Accum. Deprec.(2)	Construction/ Renovation Date	Acquisition Date
Skilled Nursing Facilities:										
Demopolis, AL	$ 10,245(3)	$ 52	$ 2,160	$ —	$ 52	$ 2,160	$ 2,212	519	1972	Jun-95
Fort Payne, AL	— (3)	86	3,539	—	86	3,539	3,625	849	1967/1973	Jun-95
Jackson, AL	— (3)	64	2,620	—	64	2,620	2,684	629	1964	Jun-95
Madison, AL	— (3)	55	2,303	—	55	2,303	2,358	549	1964/1974	Jun-95
Phoenix, AL	— (3)	52	2,130	—	52	2,130	2,182	509	1969	Jun-95
Bradenton, FL	—	330	2,720	—	330	2,720	3,050	749	1989	Sep-93
Clearwater, FL(17)	—	454	1,208	—	454	1,208	1,662	914	1965/1993	Sep-93
Lecanto, FL	—	351	2,665	2,251	351	4,916	5,267	1,169	1988	Sep-93
Chicago Heights, IL	—	221	6,406	—	221	6,406	6,627	1,639	1988	Sep-94
Rusk, TX	—	34	2,399	36	34	2,435	2,469	747	1969	Mar-94
Chesapeake, VA	—	388	3,469	34	388	3,503	3,891	907	1977	Oct-95
Richmond, VA	—	356	3,180	114	356	3,294	3,650	839	1970/1975/ 1980	Oct-95
Tappahannock, VA(17)	—	375	1,328	—	375	1,328	1,703	863	1977/1978	Oct-95
Toppanish, WA	2,525(4)	67	2,719	—	67	2,719	2,786	648	1960/1970	Jun-95
Vancouver, WA	— (4)	74	3,017	2	74	3,019	3,093	729	1952/1994	Jun-95
Jefferson, IA	10,196(5)	86	1,883	163	86	2,046	2,132	394	1968/1972	Jan-96
Houston, TX	6,905(9)	202	4,458	456	202	4,914	5,116	979	1961	Jun-96
Houston, TX	6,561(10)	365	3,769	248	365	4,017	4,382	908	1964/1968	Jun-96
Montgomery, AL	3,716(6)	243	5,327	—	243	5,327	5,570	1,086	1967/1974	Jan-96
Carroll, IA	— (5)	47	1,033	54	47	1,087	1,134	214	1969	Jan-96
Houston, TX	— (9)	202	4,458	449	202	4,907	5,109	979	1967	Jun-96
Whiteright, TX(17)	1,082	100	1,539	3	100	1,542	1,642	642	1962/1964/ 1965	Jan-96
Granger, IA	— (5)	62	1,356	59	62	1,415	1,477	281	1979	Jan-96
Bedford, TX(17)	— (5)	154	649	404	154	1,053	1,207	715	1960	Jan-96
Midland, TX	1,972	32	2,285	—	32	2,285	2,317	498	1973	Feb-96
Gardendale, AL	—	84	6,316	—	84	6,316	6,400	1,169	1976/1984	May-96
Polk City, IA	— (5)	63	1,376	15	63	1,391	1,454	282	1976	Jan-96
Atmore, AL	— (6)	131	2,877	—	131	2,877	3,008	586	1967/1974	Jan-96
Mesa, AZ	4,341	305	6,909	1,695	305	8,604	8,909	1,449	1975/1996	Jun-96
Houston, TX(17)	— (10)	569	111	824	569	935	1,504	1,503	1967	Jun-96
Roberta, GA	—	100	2,400	208	100	2,608	2,708	472	1964	May-96
Norwalk, IA	— (5)	47	1,033	46	47	1,079	1,126	214	1975	Jan-96
Altoona, IA	— (5)	105	2,309	121	105	2,430	2,535	489	1973	Jan-96
Sacramento, CA	—	220	2,929	—	220	2,929	3,149	548	1968	Feb-97
Coffeyville, KS(17)	—	100	(100)	—	100	(100)	—	—	1962	May-97
Salina, KS(17)	—	100	1,153	445	100	1,598	1,698	282	1985	May-97
South Haven, KS(17)	—	—	—	—	—	—	—	—	1969	May-97
Portland, OR	—	100	1,925	457	100	2,382	2,482	398	1956/1974	Jun-97
Nacogdoches, TX	—	100	1,738	37	100	1,775	1,875	280	1973	Oct-97
Cushing, TX(17)	—	100	293	24	100	317	417	267	1973/1984	Oct-97
Mesa, AZ	2,879	420	4,258	37	420	4,295	4,715	529	1972	Oct-97
Wells, TX(17)	2,204(7)	100	407	7	100	414	514	246	1980	Jan-98
Corrigan, TX(17)	— (7)	100	407	7	100	414	514	246	1985	Jan-98
Groesbeck, TX	1,288	100	1,649	7	100	1,656	1,756	246	1972	Jan-98
Tampa, FL	—	100	6,402	41	100	6,443	6,543	879	1970	Jun-98
Jonesboro, GA	2,623	150	2,573	3	150	2,576	2,726	223	1970	Sep-99
Griffin, GA	4,678(11)	500	2,900	—	500	2,900	3,400	259	1969	Sep-99
Atlanta, GA	— (11)	175	1,282	3	175	1,285	1,460	15	1968	Sep-99
Des Moines, IA(17)	—	115	2,096	1,177	115	3,273	3,388	288	1972	Sep-99

SCHEDULE III

REAL ESTATE AND ACCUMULATED DEPRECIATION—(Continued)
(In thousands)

					Gross Amount at which carried at December 31, 2001					
	Encumbrances	Initial Cost to Company Land	Building and Improvements	Costs Capitalized Subsequent to Acquisition	Land	Building and Improvements	Total(1)	Accum. Deprec.(2)	Construction/ Renovation Date	Acquisition Date
Olathe, KS	$ —	$ 520	$ 1,872	$ 5	$ 520	$ 1,877	$ 2,397	159	1968	Sep-99
Venice, FL(17)	—	236	346	345	236	691	927	428	1969/1972	Sep-99
Sumner, IL	961	100	877	7	100	884	984	108	1968	Oct-99
Fort Worth, TX(17)	—	100	65	—	100	65	165	165	1974	Dec-99
Jessup, GA	6,500(14)	35	465	38	35	503	538	38	1953	Dec-99
Fort Valley, GA	— (14)	230	770	86	230	856	1,086	69	1965	Dec-99
Gardner, KS	— (14)	729	4,478	196	729	4,674	5,403	319	1961/1974	Dec-99
Canyon, TX(17)	—	196	506	211	196	717	913	112	1985/86	Jun-00
Phoenix, AZ	7,250	300	9,703	—	300	9,703	10,003	489	1985	Aug-00
Tucson, AZ	6,130	276	8,924	—	276	8,924	9,200	449	1985/92	Aug-00
Holyoke, CO	—	211	1,514	257	211	1,771	1,982	108	1963	Nov-00
Manchester, TN(17)	—	50	954	83	50	1,037	1,087	55	1957/67/78	Nov-00
Dresden, TN(17)	—	31	1,529	119	31	1,648	1,679	67	1966	Nov-00
Ripley, TN(17)	—	20	985	81	20	1,066	1,086	52	1951	Nov-00
Tucson, AZ(17)	—	277	1,240	91	277	1,331	1,608	71	1974/84	Apr-01
Hereford, TX(17)	—	106	(106)	2	106	(104)	2	2	1985	Oct-01
Sumner, IL	1,547	40	1,220	—	40	1,220	1,260	—	1968	Dec-01
Roswell, NM	3,949	568	5,232	—	568	5,232	5,800	—	1975	Dec-01
Alamogordo, NM	4,672	210	2,590	—	210	2,590	2,800	—	1985	Dec-01
Richland Hills, TX	1,694	144	1,656	—	144	1,656	1,800	—	1976	Dec-01
Clovis, NM	1,599	561	5,539	—	561	5,539	6,100	—	1970	Dec-01
Clovis, NM	2,807	598	5,902	—	598	5,902	6,500	—	1969/95	Dec-01
Skilled Nursing Facilities	98,324	13,874	178,124	10,948	13,874	189,072	202,946	32,516		
Assisted Living Residences:										
Dodge City, KS	1,369	84	1,666	—	84	1,666	1,750	301	1995	Dec-95
Great Bend, KS	1,148	80	1,570	17	80	1,587	1,667	286	1995	Dec-95
McPherson, KS	986	79	1,571	—	79	1,571	1,650	283	1994	Dec-95
Salina, KS	1,150	79	1,571	—	79	1,571	1,650	283	1994	Dec-95
Longview, TX	—	38	1,568	—	38	1,568	1,606	267	1995	Oct-95
Marshall, TX	—	38	1,568	450	38	2,018	2,056	327	1995	Oct-95
Walla Walla, WA	7,265(8)	100	1,940	—	100	1,940	2,040	308	1996	Apr-96
Greenville, TX	—	42	1,565	—	42	1,565	1,607	260	1995	Jan-96
Camas, WA	— (8)	100	2,175	—	100	2,175	2,275	332	1996	May-96
Grandview, WA	— (8)	100	1,940	—	100	1,940	2,040	311	1996	Mar-96
Vancouver, WA	— (8)	100	2,785	—	100	2,785	2,885	423	1996	Jun-96
Athens, TX	—	96	1,511	—	96	1,511	1,607	252	1995	Jan-96
Lufkin, TX	—	100	1,950	—	100	1,950	2,050	310	1996	Apr-96
Kennewick, WA	— (8)	100	1,940	—	100	1,940	2,040	316	1996	Feb-96
Gardendale, AL	—	16	1,234	—	16	1,234	1,250	228	1988	May-96
Jacksonville, TX	—	100	1,900	—	100	1,900	2,000	309	1996	Mar-96
Kelso, WA	—	100	2,500	—	100	2,500	2,600	400	1996	Nov-96
Battleground, WA	—	100	2,500	—	100	2,500	2,600	343	1996	Nov-96
Hayden, ID	—	100	2,450	243	100	2,693	2,793	363	1996	Dec-96
Klamath Falls, OR	—	100	2,300	—	100	2,300	2,400	313	1996	Dec-96
Newport, OR	—	100	2,050	—	100	2,050	2,150	281	1996	Dec-96
Tyler, TX	11,291(13)	100	1,800	—	100	1,800	1,900	249	1996	Dec-96
Wichita Falls, TX	—	100	1,850	—	100	1,850	1,950	256	1996	Dec-96
Ada, OK	—	100	1,650	—	100	1,650	1,750	230	1996	Dec-96
Nampa, ID	—	100	2,240	23	100	2,263	2,363	307	1997	Jan-97
Tulsa, OK	— (13)	200	1,650	—	200	1,650	1,850	223	1997	Feb-97

LTC PROPERTIES INC.

SCHEDULE III

REAL ESTATE AND ACCUMULATED DEPRECIATION—(Continued)
(In thousands)

	Encumbrances	Initial Cost to Company Land	Building and Improvements	Costs Capitalized Subsequent to Acquisition	Gross Amount at which carried at December 31, 2001 Land	Building and Improvements	Total(1)	Accum. Deprec.(2)	Construction/ Renovation Date	Acquisition Date
Durant, OK	$ —	$ 100	$ 1,769	$ —	$ 100	$ 1,769	$ 1,869	230	1997	Apr-97
San Antonio, TX	— (13)	100	1,900	—	100	1,900	2,000	244	1997	May-97
Troy, OH	—	100	2,435	306	100	2,741	2,841	335	1997	May-97
Waco, TX	—	100	2,235	—	100	2,235	2,335	279	1997	Jun-97
Tulsa, OK	— (13)	100	2,395	—	100	2,395	2,495	298	1997	Jun-97
San Antonio, TX	— (13)	100	2,055	—	100	2,055	2,155	258	1997	Jun-97
Norfolk, NE	—	100	2,123	—	100	2,123	2,223	262	1997	Jun-97
Wahoo, NE	—	100	2,318	—	100	2,318	2,418	278	1997	Jul-97
York, NE	—	100	2,318	—	100	2,318	2,418	278	1997	Aug-97
Hoquiam, WA	—	100	2,500	—	100	2,500	2,600	299	1997	Aug-97
Tiffin, OH	—	100	2,435	—	100	2,435	2,535	291	1997	Aug-97
Millville, NJ	—	100	2,825	—	100	2,825	2,925	335	1997	Aug-97
Fremont,OH	—	100	2,435	—	100	2,435	2,535	291	1997	Aug-97
Lake Havasu, AZ	—	100	2,420	—	100	2,420	2,520	290	1997	Aug-97
Greeley, CO	—	100	2,310	270	100	2,580	2,680	302	1997	Aug-97
Springfield, OH	—	100	2,035	270	100	2,305	2,405	267	1997	Aug-97
Watauga, TX	—	100	1,668	—	100	1,668	1,768	202	1996	Aug-97
Bullhead Ctiy, AZ	—	100	2,500	—	100	2,500	2,600	293	1997	Aug-97
Arvada, CO	6,803(12)	100	2,810	276	100	3,086	3,186	352	1997	Aug-97
Edmond, OK	— (13)	100	1,365	526	100	1,891	1,991	221	1996	Aug-97
Wetherford, OK	—	100	1,669	592	100	2,261	2,361	259	1996	Aug-97
Eugene, OR	—	100	2,600	—	100	2,600	2,700	303	1997	Sep-97
Caldwell, ID	—	100	2,200	—	100	2,200	2,300	259	1997	Sep-97
Burley, ID	—	100	2,200	—	100	2,200	2,300	259	1997	Sep-97
Wheelersburg, OH	—	100	2,435	—	100	2,435	2,535	280	1997	Sep-97
Loveland, CO	— (12)	100	2,865	270	100	3,135	3,235	350	1997	Sep-97
Wichita Falls,TX	—	100	2,750	—	100	2,750	2,850	319	1997	Sep-97
Beatrice, NE	—	100	2,173	—	100	2,173	2,273	251	1997	Oct-97
Madison, IN	—	100	2,435	—	100	2,435	2,535	279	1997	Oct-97
Newark, OH	—	100	2,435	—	100	2,435	2,535	279	1997	Oct-97
Elkhart, IN	—	100	2,435	—	100	2,435	2,535	263	1997	Dec-97
Newport Richey, FL	—	100	5,845	294	100	6,139	6,239	701	1986/1995	Jan-98
Fremont, CA	—	100	3,080	212	100	3,292	3,392	325	1998	Mar-98
RioRancho, NM	—	100	8,300	32	100	8,332	8,432	799	1998	Mar-98
Ft. Meyers, FL	—	100	2,728	9	100	2,737	2,837	275	1998	Mar-98
Tallahassee, FL	— (13)	100	3,075	—	100	3,075	3,175	300	1998	Apr-98
Niceville, FL	—	100	2,680	—	100	2,680	2,780	257	1998	Jun-98
Longmont, CO	— (12)	100	2,640	—	100	2,640	2,740	254	1998	Jun-98
Shelby, NC	—	100	2,805	2	100	2,807	2,907	269	1998	Jun-98
Spring Hill, FL	—	100	2,650	—	100	2,650	2,750	255	1998	Jun-98
Portland, OR	4,076	100	7,622	—	100	7,622	7,722	700	1986	Jun-98
Tuscon, AZ	—	100	8,700	—	100	8,700	8,800	780	1998	Jun-98
Denison, IA	—	100	2,713	—	100	2,713	2,813	254	1998	Jun-98
Roseville, CA	—	100	7,300	—	100	7,300	7,400	657	1998	Jun-98
Ft. Collins, CO	—	100	2,961	—	100	2,961	3,061	232	1998	Mar-99
Greenwood, SC	—	100	2,638	—	100	2,638	2,738	205	1998	Mar-99
Greenville, NC	—	100	2,478	1	100	2,479	2,579	188	1998	Mar-99
Sumter, SC	—	100	2,351	—	100	2,351	2,451	175	1998	Mar-99
Central, SC	—	100	2,321	—	100	2,321	2,421	165	1998	Mar-99
Rocky Mount, NC	—	100	2,494	1	100	2,495	2,595	173	1998	Mar-99
New Bern, NC	—	100	2,428	1	100	2,429	2,529	156	1998	Mar-99

LTC PROPERTIES, INC.

SCHEDULE III

REAL ESTATE AND ACCUMULATED DEPRECIATION—(Continued)
(In thousands)

					Gross Amount at which carried at December 31, 2001					
	Encumbrances	Initial Cost to Company Land	Building and Improvements	Costs Capitalized Subsequent to Acquisition	Land	Building and Improvements	Total(1)	Accum. Deprec.(2)	Construction/ Renovation Date	Acquisition Date
Goldsboro, NC	$ —	$ 100	$ 2,386	$ 1	$ 100	$ 2,387	$ 2,487	153	1998	Mar-99
Ft. Collins, CO	—	100	3,400	—	100	3,400	3,500	216	1999	Jul-99
Rocky River, OH	11,325(15)	760	6,963	—	760	6,963	7,723	504	1998	Oct-99
Erie, PA	— (15)	850	7,477	—	850	7,477	8,327	563	1998	Oct-99
Lakeland, FL	—	519	2,313	79	519	2,392	2,911	141	1968/74/96	Jul-00
Cordele, GA	—	153	1,455	80	153	1,535	1,688	87	1987/88	Jul-00
Vacaville, CA	8,683	1,662	11,634	—	1,662	11,634	13,296	—	1998	Dec-01
Bakersfield, CA	9,243	834	11,986	—	834	11,986	12,820	—	1998	Dec-01
Bexley, OH	16,563(16)	306	4,196	—	306	4,196	4,502	—	1992	Dec-01
Worthington, OH	— (16)	—	6,102	—	—	6,102	6,102	—	1993	Dec-01
Arlington, OH	— (16)	629	6,973	—	629	6,973	7,602	—	1993	Dec-01
Worthington, OH	— (16)	—	3,402	—	—	3,402	3,402	—	1995	Dec-01
Assisted Living Residences	79,902	13,365	266,588	3,955	13,365	270,543	283,908	25,251		
Schools										
Trenton, NJ	—	100	6,000	3,170	100	9,170	9,270	816	1930/1998	Dec-98
Schools	—	100	6,000	3,170	100	9,170	9,270	816		
	$ 178,226	$ 27,339	$ 450,712	$ 18,073	$27,339	$ 468,785	$496,124	$ 58,583		

(1) The aggregate cost for federal income tax purposes.

(2) Depreciation for building is calculated using a 35 year life for skilled nursing facilities and 40 year life for assisted living residences and additions to facilities. Depreciation for furniture and fixtures is calculated based on a 7-year life for all facilities.

(3) Single note backed by five facilities in Alabama.

(4) Single note backed by two facilities in Washington.

(5) Single note backed by six facilities in Iowa and one facility in Texas.

(6) Single note backed by two facilities in Alabama.

(7) Single note backed by two facilities in Texas.

(8) Single note backed by five facilities in Washington.

(9) Single note backed by two facilities in Texas.

(10) Single note backed by two facilities in Texas.

(11) Single note backed by two facilities in Georgia.

(12) Single note backed by three facilities in Colorado.

(13) Single note backed by one facility in Florida, three facilities in Oklahoma, and three facilities in Texas.

(14) Single note backed by one facility in Kansas and two facilities in Georgia.

(15) Single note backed by one facility in Ohio and one facility in Pennsylvania.

(16) Single note backed by four facilities in Ohio.

(17) Impairment charge totaling $32,510,000 was taken against 20 facilities (noted above).

LTC PROPERTIES, INC.
SCHEDULE III
REAL ESTATE AND ACCUMULATED DEPRECIATION
(In thousands)

Activity for the years ended December 31, 1999, 2000 and 2001 is as follows:

	Real Estate & Equipment	Accumulated Depreciation
Balance at December 31, 1998	$ 410,659	$ 26,972
Additions	44,362	13,237
Conversion of mortgage loans into owned properties	47,554	—
Impairment charge	(7,662)	(234)
Balance at December 31, 1999	494,913	39,975
Additions	22,495	15,145
Conversion of mortgage loans into owned properties	12,255	—
Impairment charge	(7,529)	—
Cost of real estate sold	(53,636)	(7,939)
Balance at December 31, 2000	468,498	47,181
Additions	73,107	13,695
Conversion of mortgage loans into owned properties	3,899	—
Impairment Charges	(16,755)	—
Cost of real estate sold	(32,625)	(2,293)
Balance at December 31, 2001	$ 496,124	$ 58,583

LTC PROPERTIES, INC.
SCHEDULE IV
MORTGAGE LOANS ON REAL ESTATE
(dollars in thousands)

State	Number of Facilities	Units/Beds	Interest Rate (1)	Final Maturity Date	Balloon Amount (2)	Current Monthly Debt Service	Face Amount of Mortgages	Carrying Amount of Mortgages December 31, 2001	Principal Amount of Loans Subject to Delinquent Principal or Interest
SC	5	509	13.05%	2003	$ 10,754	$ 123	$ 11,250	$ 10,741	$ —
CO	2	230	11.75%	2007	5,412	62	6,000	5,788	—
CA	1	151	10.15%	2018	—	31	3,171	2,992	—
NE	1	44	11.44%	2008	2,875	30	3,036	2,992	—
OH	1	150	10.69%	2006	4,579	50	5,200	4,907	—
FL	1	191	12.00%	2017	—	49	4,500	4,174	—
CA	1	212	10.41%	2018	—	35	3,500	3,298	—
FL	1	94	10.27%	2007	2,879	31	3,290	3,152	—
NE	1	47	11.44%	2008	3,071	32	3,243	3,196	—
Various (3)	35	3,265	9.26%–13.7%	2002–2018	38,449	552	58,669	53,621	3,945
	49	4,893			$ 68,019	$ 995	$ 101,859	$ 94,861	$ 3,945

(1.) Represents current stated interest rate. Generally, the loans have 25 year amortization with principal and interest payable at varying amounts over the life to maturity with annual interest adjustments through specified fixed rate increases effective either on the first anniversary or calendar year of the loan.

(2.) Balloon payment is due upon maturity, generally the 10th year of the loan, with various prepayment penalties (as defined in the loan agreement).

(3.) Includes 44 first-lien mortgage loans as follows:

# of Loans	Original loan amounts:
25	$247–$2,000
9	$2,001–$3,000
6	$3,001–$4,000
1	$4,001–$5,000
2	$5,001–$6,000
1	$6,001–11,250

Activity for the years ended December 31, 1999, 2000 and 2001 is as follows:

Balance at December 31, 1998	$ 180,964
New mortgage loans	6,678
Additional funding of existing loans	1,890
Conversion of notes to owned properties	(47,554)
Impairment charges	(2,806)
Collections of principal	(6,729)
Balance at December 31, 1999	132,443
Additional funding of existing loans	964
Conversion of notes to owned properties	(12,131)
Impairment charges	(5,088)
Collections of principal	(8,789)
Balance at December 31, 2000	107,399
Conversion of notes to owned properties	(3,247)
Collections of principal	(9,291)
Balance at December 31, 2001	$ 94,861

INDEX TO EXHIBITS
(Item 14(b))

Exhibit Number	Description
3.1	Amended and Restated Articles of Incorporation of LTC Properties, Inc. (incorporated by reference to Exhibit 3.1 to LTC Properties, Inc.'s Current Report on Form 8-K dated June 19, 1997)
3.2	Amended and Restated By-Laws of the Company (incorporated by reference to Exhibit 3.1 to LTC Properties, Inc.'s Form 10-Q for the quarter ended June 30, 1996)
3.3	Articles Supplementary Classifying 3,080,000 shares of 9.5% Series A Cumulative Preferred Stock of LTC Properties, Inc. (incorporated by reference to Exhibit 3.2 to LTC Properties, Inc.'s Current Report on Form 8-K dated June 19, 1997)
3.4	Articles of Amendment of LTC Properties, Inc. (incorporated by reference to Exhibit 3.3 to LTC Properties, Inc.'s Current Report on Form 8-K dated June 19, 1997)
3.5	Articles Supplementary Classifying 2,000,000 Shares of 9.0% Series B Cumulative Preferred Stock of LTC Properties, Inc. (incorporated by reference to Exhibit 2.5 to LTC Properties, Inc.'s Registration Statement on Form 8-A filed on December 15, 1997)
3.6	Certificate of Amendment to Amended and Restated Bylaws of LTC Properties, Inc. (incorporated by reference to Exhibit 3.1 to LTC Properties, Inc.'s Quarterly Report on Form 10-Q for the quarter ended September 30, 1998)
3.7	Articles Supplementary Classifying 2,000,000 Shares of 8.5% Series C Cumulative Convertible Preferred Stock of LTC Properties, Inc. (incorporated by reference to Exhibit 3.2 to LTC Properties, Inc.'s Quarterly Report on Form 10-Q for the quarter ended September 30, 1998)
3.8	Articles Supplementary Classifying 40,000 shares of Series D Junior Participating Preferred Stock of LTC Properties, Inc. (incorporated by reference to Exhibit 4.7 to LTC Properties, Inc.'s Registration Statement on Form 8-A filed on May 9, 2000)
4.1	Indenture dated September 23, 1994 between LTC Properties, Inc. and Harris Trust and Savings Bank, as trustee (incorporated by reference to Exhibit 4.2 to LTC Properties, Inc.'s Form 10-K for the year ended December 31, 1994)
4.2	Second Supplemental Indenture dated as of September 21, 1995 to Indenture dated September 23, 1994 between LTC Properties, Inc. and Harris Trust and Savings Bank, as trustee with respect to $51,500,000 in principal amount of 8.5% Convertible Subordinated Debentures due 2001 (incorporated by reference to Exhibit 10.17 to LTC Properties, Inc.'s Form 10-Q for the quarter ended September 30, 1995)
4.3	Third Supplemental Indenture dated as of September 26, 1995 to Indenture dated September 23, 1994 between LTC Properties, Inc. and Harris Trust and Savings Bank, as trustee with respect to $10,000,000 in principal amount of 8.25% Convertible Subordinated Debentures due 1999 (incorporated by reference to Exhibit 10.19 to LTC Properties, Inc.'s Form 10-Q for the quarter ended September 30, 1995)
4.4	Fourth Supplemental Indenture dated as of February 5, 1996 to Indenture dated September 23, 1994 between LTC Properties, Inc. and Harris Trust and Savings Bank, as trustee with respect to $30,000,000 in principal amount of 7.75% Convertible Subordinated Debentures due 2002 (incorporated by reference to Exhibit 4.6 to LTC Properties, Inc.'s Form 10-K for the year ended December 31, 1995)
4.5	Fifth Supplemental Indenture dated as of August 23, 1996 to Indenture dated September 23, 1994 between LTC Properties, Inc. and Harris Trust and Savings Bank, as trustee with respect to $30,000,000 in principal amount of 8.25% Convertible Subordinated Debentures due 2001 (incorporated by reference to Exhibit 4.5 to LTC Properties, Inc.'s Annual Report on Form 10-K for the year ended December 31, 1998)

Exhibit Number	Description
4.6	Sixth Supplemental Indenture dated as of December 30, 1998 to Indenture dated September 23, 1994 between LTC Properties, Inc. and Harris Trust and Savings Bank, as trustee with respect to $10,000,000 in principal amount of 8.25% Convertible Subordinated Debentures due 1999 (incorporated by reference to Exhibit 4.6 to LTC Properties, Inc.'s Annual Report on Form 10-K for the year ended December 31, 1998)
4.7	Seventh Supplemental Indenture dated as of January 14, 1999 to Indenture dated September 23, 1994 between LTC Properties, Inc. and Harris Trust and Savings Bank, as trustee with respect to $10,000,000 in principal amount of 8.25% Convertible Subordinated Debentures due 1999 (incorporated by reference to Exhibit 4.7 to LTC Properties, Inc.'s Annual Report on Form 10-K for the year ended December 31, 1998)
4.8	Rights Agreement dated as of May 2, 2000 (incorporated by reference to Exhibit 4.1 to LTC Properties, Inc.'s Registration Statement on Form 8-A filed on May 9, 2000)
10.1	Pooling and Servicing Agreement, dated as of July 20, 1993, among LTC REMIC Corporation, as depositor, Bankers Trust Company, as Master Servicer, LTC Properties, Inc., as Special Servicer and originator and Union Bank, as trustee (incorporated by reference to Exhibit 10.11 to LTC Properties, Inc.'s Form 10-K for the year ended December 31, 1994)
10.2	Pooling and Servicing Agreement, dated as of November 1, 1994, among LTC REMIC Corporation, as depositor, Bankers Trust Company, as Master Servicer, LTC Properties, Inc., as Special Servicer and originator and Marine Midland Bank, as trustee (incorporated by reference to Exhibit 10.13 to LTC Properties, Inc.'s Form 10-K dated December 31, 1994)
10.3	Amended Deferred Compensation Plan (incorporated by reference to Exhibit 10.17 to LTC Properties, Inc.'s Form 10-K for the year ended December 31, 1995)
10.4	Pooling and Servicing Agreement dated as of March 1, 1996, among LTC REMIC Corporation, as depositor, GMAC Commercial Mortgage Corporation, as Master Servicer, LTC Properties, Inc., as Special Servicer and Originator, LaSalle National Bank, as Trustee and ABN AMRO Bank, N.V., as fiscal agent (incorporated by reference to Exhibit 10.1 to LTC Properties, Inc.'s Form 10-Q for the quarter ended March 31, 1996)
10.5	Amended and Restated 1992 Stock Option Plan (incorporated by reference to Exhibit 10.22 to LTC Properties, Inc.'s Form 10-K for the year ended December 31, 1996)
10.6	Subservicing Agreement dated as July 20, 1993 by and between Bankers Trust Company, as Master Servicer and LTC Properties, Inc., as Special Servicer (incorporated by reference to Exhibit 10.25 to LTC Properties, Inc.'s Form 10-K/A for the year ended December 31, 1996)
10.7	Custodial Agreement dated as of July 20, 1993 by and among Union Bank, as Trustee, LTC REMIC Corporation, as Depositor, and Bankers Trust Company as Master Servicer and Custodian (incorporated by reference to Exhibit 10.26 to LTC Properties, Inc.'s Form 10-K/A for the year ended December 31, 1996)
10.8	Form of Certificates as Exhibit as filed herewith to the Pooling and Servicing Agreement dated as of July 20, 1993 among LTC REMIC Corporation, as Depositor, Bankers Trust Company, as Master Servicer, LTC Properties, Inc. as Special Servicer and Originator and Union Bank as Trustee (incorporated by reference to Exhibit 10.11 to LTC Properties, Inc.'s Form 10-K for the year ended December 31, 1994)
10.9	Form of Certificates, Form of Custodial Agreement and Form of Subservicing Agreement as Exhibits as filed herewith to the Pooling and Servicing Agreement dated as of November 1, 1994 among LTC REMIC Corporation, as Depositor, Bankers Trust Company, as Master Servicer, LTC Properties, Inc. as Special Servicer and Originator and Marine Midland Bank as Trustee (incorporated by reference to Exhibit 10.13 to LTC Properties, Inc.'s Form 10-K for the year ended December 31, 1994)

INDEX TO EXHIBITS—(Continued)
(Item 14(b))

Exhibit Number	Description
10.10	Form of Certificates, Form of Custodial Agreement and Form of Subservicing Agreement as Exhibits as filed herewith to the Pooling and Servicing Agreement dated as of March 1, 1996 among LTC REMIC Corporation, as Depositor, GMAC Commercial Mortgage Corporation, as Master Servicer, LTC Properties, Inc. as Special Servicer and Originator and LaSalle National Bank as Trustee and ABN AMRO Bank N.V., as Fiscal Agent (incorporated by reference to Exhibit 10.1 to LTC Properties, Inc.'s Form 10-Q for the quarter ended March 31, 1996)
10.11	Subservicing Agreement dated as of May 14, 1998, by and between GMAC Commercial Mortgage Corporation, as Master Servicer, LTC Properties, Inc. as Subservicer (incorporated by reference to Exhibit 10.3 to LTC Properties, Inc.'s Quarterly Report on Form 10-Q for the quarter ended September 30, 1998)
10.12	Pooling and Servicing Agreement dated as of April 20, 1998 among LTC REMIC IV Corporation, LaSalle National Bank and LTC Properties, Inc. (incorporated by reference to Exhibit 10.4 to LTC Properties, Inc.'s Quarterly Report on Form 10-Q for the quarter ended September 30, 1998)
10.13	Distribution Agreement, dated as of September 30, 1998, by and between LTC Properties, Inc. and LTC Healthcare, Inc. (incorporated by reference to Exhibit 10.5 to LTC Properties, Inc.'s Quarterly Report on Form 10-Q for the quarter ended September 30, 1998)
10.14	Intercompany Agreement, dated as of September 30, 1998, by and between LTC Properties, Inc. and LTC Healthcare, Inc. (incorporated by reference to Exhibit 10.7 to LTC Properties, Inc.'s Quarterly Report on Form 10-Q for the quarter ended September 30, 1998)
10.15	Tax Sharing Agreement, dated as of September 30, 1998, by and between LTC Properties, Inc. and LTC Healthcare, Inc. (incorporated by reference to Exhibit 10.8 to LTC Properties, Inc.'s Quarterly Report on Form 10-Q for the quarter ended September 30, 1998)
10.16	LTC Properties, Inc. 1998 Equity Participation Plan (incorporated by reference to Exhibit 10.28 to LTC Properties, Inc.'s Annual Report on Form 10-K for the year ended December 31, 1998)
10.17	Second Amended and Restated Employment Agreement between Andre C. Dimitriadis and LTC Properties, Inc. dated March 26, 1999 (incorporated by reference to Exhibit 10.28 to LTC Properties, Inc.'s Annual Report on Form 10-K for the year ended December 31, 1998), as amended by Amendment No. 1 thereto dated June 23, 2000
10.18	Amended and Restated Employment Agreement between James J. Pieczynski and LTC Properties, Inc. dated March 26, 1999 (incorporated by reference to Exhibit 10.28 to LTC Properties, Inc.'s Annual Report on Form 10-K for the year ended December 31, 1998), as superceded by Separation Agreement effective July 1, 2000
10.19	Amended and Restated Employment Agreement between Christopher T. Ishikawa and LTC Properties, Inc. dated March 26, 1999 (incorporated by reference to Exhibit 10.28 to LTC Properties, Inc.'s Annual Report on Form 10-K for the year ended December 31, 1998), as amended by Amendment No. 1 thereto dated June 23, 2000
10.20	Amended and Restated Employment Agreement between Julia L. Kopta and LTC Properties, Inc. dated January 1, 2000 (incorporated by reference to Exhibit 10.33 to LTC Properties, Inc.'s Annual Report on Form 10-K for the year ended December 31, 1999), as amended by Amendment No. 1 thereto dated June 23, 2000
10.21	Amended and Restated Employment Agreement between Wendy L. Simpson and LTC Properties, Inc. dated April 10, 2000, as amended by Amendment No. 1 thereto dated June 23, 2000 (incorporated by reference to Exhibit 10.22 to LTC Properties, Inc.'s Annual Report on Form 10-K for the year ended December 31, 2000)
10.22	Promissory Note dated January 1, 2000, executed by Andre C. Dimitriadis in favor of LTC Properties, Inc. (incorporated by reference to Exhibit 10.23 to LTC Properties, Inc.'s Annual Report on Form 10-K for the year ended December 31, 2000)

INDEX TO EXHIBITS—(Continued)
(Item (14(b))

Exhibit Number	Description
10.23	Promissory Note dated January 1, 2000, executed by James J. Pieczynski in favor of LTC Properties, Inc. (incorporated by reference to Exhibit 10.24 to LTC Properties, Inc.'s Annual Report on Form 10-K for the year ended December 31, 2000)
10.24	Promissory Note dated January 1, 2000, executed by Wendy L. Simpson in favor of LTC Properties, Inc. (incorporated by reference to Exhibit 10.25 to LTC Properties, Inc.'s Annual Report on Form 10-K for the year ended December 31, 2000)
10.25	Promissory Note dated January 1, 2000, executed by Christopher T. Ishikawa in favor of LTC Properties, Inc. (incorporated by reference to Exhibit 10.26 to LTC Properties, Inc.'s Annual Report on Form 10-K for the year ended December 31, 2000)
10.26	Promissory Note dated January 1, 2000, executed by Edmund C. King in favor of LTC Properties, Inc. (incorporated by reference to Exhibit 10.27 to LTC Properties, Inc.'s Annual Report on Form 10-K for the year ended December 31, 2000)
10.27	Promissory Note dated January 1, 2000, executed by Sam Yellen in favor of LTC Properties, Inc. (incorporated by reference to Exhibit 10.28 to LTC Properties, Inc.'s Annual Report on Form 10-K for the year ended December 31, 2000)
10.28	Senior Secured Revolving Credit Agreement dated October 31, 2000 (incorporated by reference to Exhibit 10.29 to LTC Properties, Inc.'s Annual Report on Form 10-K for the year ended December 31, 2000)
10.29	First Amendment to Revolving Credit Agreement dated March 23, 2001 (incorporated by reference to Exhibit 10 to LTC Properties, Inc.'s Quarterly Report on Form 10-Q for the quarter ended March 31, 2001)
10.30	Second Amendment to Revolving Credit Agreement dated May 29, 2001 (incorporated by reference to Exhibit 10.1 to LTC Properties, Inc.'s Quarterly Report on Form 10-Q for the quarter ended June 30, 2001)
10.31	Secured Term Loan with Heller Healthcare Financial, Inc. dated June 29, 2001 (incorporated by reference to Exhibit 10.2 to LTC Properties, Inc.'s Quarterly Report on Form 10-Q for the quarter ended June 30, 2001)
10.32	Second Amended and Restated Promissory Note with LTC Healthcare, Inc. dated June 8, 2001 (incorporated by reference to Exhibit 10.3 to LTC Properties, Inc.'s Quarterly Report on Form 10-Q for the quarter ended June 30, 2001)
10.33	Security Agreement with LTC Healthcare, Inc. dated June 8, 2001 (incorporated by reference to Exhibit 10.4 to LTC Properties, Inc.'s Quarterly Report on Form 10-Q for the quarter ended June 30, 2001)
10.34	Form of Individual Indemnity Agreements between LTC Properties and Andre Dimitriadis; Christopher Ishikawa; Julia Kopta; Wendy Simpson; Bary Bailey and Steven Stuart dated March 18, 2001
10.35	Employment Agreement between Alex J. Chavez and LTC Properties, Inc. dated September 4, 2001
10.36	Promissory Note between LTC Properties, Inc. and Healthcare Holdings, Inc. dated December 31, 2001
10.37	Security Agreement between LTC Properties, Inc. and Healthcare Holdings, Inc. dated December 31, 2001
21.1	List of subsidiaries
23.1	Consent of Ernst & Young LLP with respect to the financial information of the Company
99.0	Risk Factors

SIGNATURE

Pursuant to the requirements of Section 13 or 15(d) of the securities Exchange Act of 1934, Registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

Dated: March 18,2002

LTC Properties, Inc.
Registrant

By: /s/ WENDY L. SIMPSON

Wendy L. Simpson
Vice Chairman, Chief Financial Officer and Director

/s/ ANDRE C. DIMITRIADIS **Andre C. Dimitriadis**	Chairman of the Board, Chief Executive Officer and Director	March 18, 2002
/s/ WENDY L. SIMPSON **Wendy L. Simpson**	Vice Chairman, Chief Financial Officer and Director	March 18, 2002
/s/ EDMUND C. KING **Edmund C. King**	Director	March 18, 2002
/s/ TIMOTHY J. TRICHE **Timothy J. Triche**	Director	March 18, 2002
/s/ SAM YELLEN **Sam Yellen**	Director	March 18, 2002

EXHIBIT 10.34

INDEMNITY AGREEMENT

This Indemnity Agreement (this "Agreement") is made and dated as of this 18th day of March, 2001, by and between LTC PROPERTIES, INC., a Maryland corporation ("LTC Properties"), and ((INDEMNITEE)), an individual (the "Indemnitee").

R E C I T A L S

1. LTC Properties has maintained a continuing economic relationship with LTC Healthcare, Inc., a Nevada corporation (the "Corporation"), which relationship has been and continues to be valuable and in the best interests of LTC Properties and its shareholders.

2. At the request of LTC Properties, Indemnitee currently serves as a director and/or officer of Corporation and/or one or more subsidiaries of the Corporation (collectively, "Affiliates") and/or in other capacities for the Corporation and/or their Affiliates (collectively "Enterprises") and, as such, may be subject to claims, actions, suits or proceedings arising out of or as a result of such service. LTC Properties may in the future request that Indemnitee provide additional service to the Corporation and/or its Affiliates.

3. LTC Properties has recognized that (i) the indemnification provisions of applicable corporate law (the "Code"), the Corporation's and/or Affiliates' Restated and Amended Articles of Incorporation (the "Articles") and the Corporation's and/or Affiliates' Restated and Amended Bylaws (the "Bylaws"; the Code, the Articles and the Bylaws shall collectively be referred to herein as the "Indemnification Provisions") may be amended, modified, repealed or limited by judicial decision, and that (ii) the Corporation and/or Affiliates may in the future be unable to purchase and maintain an adequate policy of directors and officers liability insurance ("D&O Insurance") and/or adequate liability insurance relating to the operations of the Corporation and/or Affiliates ("Liability Insurance"). As a result, LTC Properties acknowledges that the Indemnification Provisions, D&O Insurance and Liability Insurance may not be adequate protection for Indemnitee against the risks associated with service to the Corporation or Affiliates, and Indemnitee may be unwilling to continue to serve the Corporation or Affiliates in the absence of the benefits and assurances provided to Indemnitee under this Agreement.

4. LTC Properties may in the future benefit from Indemnitee's maintaining or accepting positions with the Enterprises, including positions as a director, advisory director, officer, agent, employee or fiduciary of an Enterprise (any such position Indemnitee is requested to maintain or accept by the Corporation being referred to herein as a "Corporate Position") and, for reasons similar to those described in Clause 2 above, Indemnitee may be unwilling to serve in a Corporate Position in the absence of the benefits and assurances provided to Indemnitee under this Agreement.

NOW, THEREFORE, in consideration of the foregoing recitals, of the mutual promises herein contained and for other good and valuable consideration, the receipt and adequacy of which are hereby acknowledged, the parties hereto, intending to be legally bound, hereby agree as follows:

AGREEMENT

ARTICLE 1.
INDEMNIFICATION

Section 1.01. <u>In General</u>. In connection with any actual, pending, threatened, completed, asserted or unasserted claim, action, suit, arbitration, mediation, alternative dispute resolution mechanism, investigation, administrative hearing or any other similar proceeding, whether civil, criminal, administrative or investigative, in each case arising by reason of any Corporate Position of Indemnitee or in any way connected with or related to any Corporate Position of Indemnitee, other than one initiated by Indemnitee pursuant to Article 6 to enforce Indemnitee's rights under this Agreement (collectively, "Proceedings"), LTC Properties shall, to the fullest extent permitted by applicable law in effect on the date hereof, and to such greater extent as applicable law may hereafter from time to time permit, indemnify and hold harmless Indemnitee against any and all Expenses (as hereinafter defined), judgments, penalties, damages, claims, fines and amounts paid in settlement, actually and reasonably incurred by Indemnitee or on Indemnitee's behalf in connection with such Proceeding or any claim, issue or matter therein. Amounts with respect to which LTC Properties is required to indemnify and hold harmless Indemnitee under this Section 1.01 are referred to collectively as "Covered Amounts". LTC Properties shall advance Expenses to Indemnitee and reimburse Indemnitee for any and all Expenses incurred as provided in this Agreement and to the fullest extent permitted by applicable law in effect on the date hereof and to such greater extent as applicable law may hereafter from time to time permit.

Section 1.02. Certain Defined Terms. The following terms shall have the meanings given here:

(a) "Expenses" shall include, without limitation, all fees, costs, disbursements and expenses incurred by Indemnitee in connection with the prosecution, defense, or investigation of a Proceeding, including, without limitation, all retainers, court costs, arbitrator's costs, transcript costs, fees of experts, witness fees, travel expenses, duplicating costs, printing and binding costs, telephone charges, postage, delivery service fees and reasonable attorneys' fees.

(b) "Independent Counsel" shall mean a law firm or a member of a law firm selected by Indemnitee that is experienced in matters of corporate law in one or more relevant jurisdictions and neither presently is representing, nor in the past five (5) years has been retained to represent, (i) any Enterprise or Indemnitee in any matter material to either such party, or (ii) any other party to the Proceeding giving rise to a claim for indemnification hereunder. Notwithstanding the foregoing, the Independent Counsel shall not be any person who, under the applicable standards of professional conduct then prevailing, would have a conflict of interest in representing either LTC Properties, the Corporation or Indemnitee in an action to determine Indemnitee's rights under this Agreement.

Section 1.03. Indemnification of a Party Who is Wholly or Partly Successful. If LTC Properties is permitted by law to indemnify and hold harmless Indemnitee only with respect to claims, issues or matters successfully resolved, notwithstanding any other provision of this Agreement, to the extent that Indemnitee is, by reason of Indemnitee's Corporate Position, a party to, and is successful on the merits or otherwise in, any Proceeding, Indemnitee shall be indemnified and held harmless to the maximum extent permitted by law, against any and all Covered Amounts. If Indemnitee is not wholly successful on the merits or otherwise, as to one or more but less than all claims, issues or matters in such Proceeding, and LTC Properties is permitted by law to indemnify and hold harmless Indemnitee only with respect to claims, issues or matters successfully resolved, LTC Properties shall indemnify Indemnitee to the maximum extent permitted by law against any and all Covered Amounts in connection with each successfully resolved claim, issue or matter. For purposes of this Section 1.03, and without limitation, the termination of any claim, issue or matter in such a Proceeding by judgment, dismissal, with or without prejudice, or the settlement of such claim, issue or matter shall be deemed to be a successful result as to such claim, issue or matter.

Section 1.04. Indemnification for Expenses of a Witness. Notwithstanding any other provision of this Agreement, to the extent that Indemnitee is, by reason of any Corporate Position of Indemnitee, a witness in any Proceeding, Indemnitee shall be indemnified and held harmless against all Expenses actually and reasonably incurred by Indemnitee or on Indemnitee's behalf in connection therewith.

Section 1.05. Successors. The indemnification and advancement of Expenses provided by, or granted pursuant to, this Agreement shall be applicable to activities that occurred prior to the date hereof and shall continue as to Indemnitee irrespective of whether Indemnitee is still serving in a Corporate Position and shall inure to the benefit of the heirs, executors and administrators of Indemnitee.

Section 1.06. Change in Control.

(a) LTC Properties agrees that, if there is a Change of Control (as hereinafter defined), then with respect to all matters thereafter arising concerning the rights of Indemnitee to indemnification and Expense advances under this Agreement, LTC Properties will seek legal advice only from Independent Counsel selected by Indemnitee with respect to matters arising out of this Agreement, including but not limited to the right of Indemnitee to indemnification hereunder. Such counsel shall, among other things, render its written opinion to LTC Properties and Indemnitee as to whether and to what extent Indemnitee would be permitted to be indemnified in the event of a Change of Control under the Code or pursuant to this Agreement and as to the amount of reasonable indemnification. Such written opinion shall be binding upon LTC Properties and Indemnitee. LTC Properties shall pay the reasonable fees of such counsel. In addition, if there is a Change of Control of the type described in Section 1.06(b)(iii) of this Agreement, LTC Properties shall use its best efforts to have the obligations of LTC Properties under this Agreement expressly assumed by the surviving or succeeding entity.

(b) For the purposes of this Agreement, a "Change in Control" shall be deemed to have occurred if:

(i) Any "Person," as such term is used in Section 13(d) and 14(d) of the Securities Exchange Act of 1934, as amended (the "1934 Act") or group of Persons, other than a trustee or other fiduciary holding securities under an employee benefit plan of the Corporation or any Enterprise, becomes the "Beneficial Owner," as defined in Rule 13d-3 of the 1934 Act, directly or indirectly, of securities of LTC Properties representing fifteen percent (15%) or more of the combined voting power of LTC Properties' then outstanding voting securities ("Voting Shares");

(ii) During any period of twenty-four (24) consecutive months, not including any period prior to the execution of this Agreement, individuals who, at the beginning of such period, constitute the board of directors of LTC Properties and any new director, other than a director designated by a person who has entered into an agreement with LTC Properties to effect a transaction described in Section 1.06(b)(i) or 1.06(b)(iii) whose election was approved by a vote of at least two-thirds (2/3rds) of the shares entitled to vote, cease for any reason to constitute a majority of the board; or

(iii) The shareholders of LTC Properties (i) approve a merger or consolidation of LTC Properties with any other corporation, other than a merger or consolidation that would result in the Voting Shares outstanding immediately prior thereto continuing to represent, either by remaining outstanding or by being converted into Voting Shares of the surviving entity, at least seventy percent (70%) of the combined voting power of the Voting Shares of LTC Properties or such surviving entity outstanding immediately after such merger or consolidation, (ii) approve a plan of complete liquidation of LTC Properties, or (iii) approve an agreement for sale or disposition by LTC Properties of all or substantially all of LTC Properties' assets.

(c) In the event of a Potential Change in Control (as hereinafter defined), LTC Properties shall, upon written request by Indemnitee, create a trust (the "Trust") for the benefit of Indemnitee and from time to time upon written request of Indemnitee shall fund the Trust in an amount sufficient to satisfy any and all Expenses reasonably anticipated at the time of each such request to be incurred and/or which have been incurred in connection with investigating, preparing for and/or prosecuting and/or defending any Proceeding for which Indemnitee may be entitled to indemnification hereunder. Upon formation of the Trust, LTC Properties shall deposit into the Trust an amount equal to the amount estimated by Indemnitee in good faith to be required in order for LTC Properties to satisfy its indemnification obligations to Indemnitee hereunder for all pending or threatened matters. Thereafter, the amount or amounts to be deposited in the Trust pursuant to the foregoing funding obligations shall be determined in accordance with the provisions of the Code with regard to determination and authorization of indemnification.

(d) The terms of the Trust shall provide that upon a Change in Control (i) the Trust shall not be revoked or the principal thereof invaded without the prior written consent of Indemnitee; (ii) the trustee of the Trust (the "Trustee") shall advance, within two (2) business days of a written request by Indemnitee in accordance with the requirements of Article 4, any and all Expenses to Indemnitee, and Indemnitee hereby agrees to reimburse the Trust under the circumstances under which Indemnitee would be required to reimburse LTC Properties pursuant to Article 4 of this Agreement; (iii) the Trust shall continue to be funded by LTC Properties in accordance with the funding obligations set forth above; (iv) the Trustee shall promptly pay to Indemnitee all amounts for which Indemnitee shall be entitled to indemnification pursuant to this Agreement; (v) the Trustee shall ignore claims by LTC Properties that Indemnitee is not entitled to indemnification or which otherwise seek to prevent payment by the Trust; and (vi) all unexpended funds in the Trust shall revert to LTC Properties upon a final determination by the special counsel established in Section 1.06(a) or by a court of competent jurisdiction, by arbitration or in a final decision from which there is no further right of appeal, that Indemnitee has been fully indemnified under the terms of this Agreement. The Trustee shall be selected by Indemnitee with the consent of LTC Properties, which consent shall not be unreasonably withheld, and all reasonable expenses, fees and other disbursements of the Trustee in connection with the establishment and administration of the Trust shall be paid for by LTC Properties.

(e) Nothing in this Section 1.06 shall relieve LTC Properties of any of its obligations under this Agreement.

(f) A "Potential Change in Control" shall be deemed to have occurred if: (i) LTC Properties enters into an agreement, the consummation of which would result in the occurrence of a Change in Control; (ii) any Person as such term is used in Section 13(d) and 14(d) of the 1934 Act or group of Persons publicly announces an intention to take or to consider taking actions that, if consummated, would constitute a Change in Control; (iii) any Person, other than a trustee or other fiduciary holding securities under an employee benefit plan of LTC Properties or the Enterprise, becomes the beneficial owner, directly or indirectly, of shares of LTC Properties representing nine and one-half percent (9.5%) or more of the combined voting power of LTC Properties' then outstanding Voting Shares; or (iv) the board of directors of LTC Properties adopts a resolution to the effect that, for purposes of this Agreement, a Potential Change in Control has occurred.

ARTICLE 2.
GENERAL

Section 2.01. No Modification of Engagement Terms. Anything to the contrary appearing in this Agreement notwithstanding, this Agreement shall not, and shall not be construed to, amend or otherwise modify any term of any agreement under which Indemnitee shall serve in any position with any Enterprise. Nothing contained herein shall limit Indemnitee's right at any time and for any reason to resign from any position or terminate Indemnitee's engagement with any Enterprise.

Section 2.02. Presumption of Corporation's Request. If Indemnitee acts in the future as a director, advisory director, officer, agent, employee or fiduciary of an Enterprise, Indemnitee shall conclusively be presumed to act in such capacity upon the request of LTC Properties.

Section 2.03. Ownership of Shares. LTC Properties acknowledges that Indemnitee may be a shareholder and/or option holder of the Corporation.

ARTICLE 3.
ADVANCEMENT OF EXPENSES.

Section 3.01. In General. Notwithstanding any provision to the contrary in Article 1 hereof, LTC Properties shall advance all reasonable Expenses which were incurred by or on behalf of Indemnitee in connection with any Proceeding within ten (10) days after receipt by LTC Properties of a statement or statements from Indemnitee requesting such advance or advances, whether prior to or after final disposition of such Proceeding. Such statement or statements shall reasonably evidence the Expenses incurred by Indemnitee and shall include or be preceded or accompanied by an undertaking by or on behalf of Indemnitee to repay any and all Expenses if it shall ultimately be determined that Indemnitee is not entitled to be indemnified against such Expense. For avoidance of doubt, LTC Properties shall advance all reasonable expenses during the pendency of any disputes as to whether the Indemnitee is entitled to indemnification hereunder and the arbitrator shall order LTC Properties to do so. Any advance and undertaking to repay pursuant to this Article 3 shall be unsecured and interest free.

ARTICLE 4.
PROCEDURES FOR DETERMINATION OF ENTITLEMENT TO INDEMNIFICATION.

Section 4.01. Initial Request. To obtain indemnification under this Agreement, Indemnitee shall submit to LTC Properties a written request. If a determination with respect to Indemnitee's entitlement to indemnification hereunder must by law be made by the board of directors of LTC Properties (the "Board"), the Secretary of LTC Properties shall promptly advise the Board in writing that Indemnitee has requested indemnification and a meeting of the Board shall be scheduled no later than ten (10) days following receipt of the request for indemnification.

Section 4.02. Method of Determination. If a determination with respect to Indemnitee's entitlement to indemnification hereunder is required by law, such determination shall be made by the Board by a majority vote of a quorum consisting of directors of LTC Properties who are not and were not parties to the Proceeding in respect of

which indemnification is sought by Indemnitee ("Disinterested Directors"). In the event that a quorum of the Board consisting of Disinterested Directors is not obtainable, the determination shall be made by Independent Counsel in a written opinion to the Board, a copy of which shall be delivered to Indemnitee.

Section 4.03. Selection, Payment and Discharge of Independent Counsel. In the event that the determination of entitlement to indemnification hereunder is to be made by Independent Counsel pursuant to Section 4.02 hereof, the Independent Counsel shall be selected by Indemnitee. LTC Properties shall pay any and all reasonable fees and expenses incurred by the Independent Counsel in connection with any action undertaken pursuant to this Agreement.

Section 4.04. Cooperation. Indemnitee shall cooperate with the person or persons or entity making the determination with respect to Indemnitee's entitlement to indemnification under this Agreement including, providing to such person, persons or entity, upon reasonable advance request, any documentation or information which is not privileged or otherwise protected from disclosure and which is reasonably available to Indemnitee and reasonably necessary to such determination. Any and all Expenses incurred by Indemnitee in so cooperating with such person, persons or entity making such determination shall be borne by LTC Properties (irrespective of the determination as to Indemnitee's entitlement to indemnification) and LTC Properties hereby agrees to indemnify and hold Indemnitee harmless therefrom.

Section 4.05. Payment. If it is determined that Indemnitee is entitled to indemnification, LTC Properties shall make all payments to Indemnitee, within ten (10) days after such determination; provided, however that LTC Properties shall have no obligation to make any such payments unless Indemnitee shall have provided to LTC Properties invoices and such other evidence reasonably requested by LTC Properties supporting such payments.

ARTICLE 5.
PRESUMPTION AND EFFECT OF CERTAIN PROCEEDINGS.

Section 5.01. Burden-of Proof. In making a determination with respect to entitlement of indemnification hereunder, the person, persons or entity making such determination shall presume that Indemnitee is entitled to indemnification under this Agreement if Indemnitee has submitted a request for indemnification in accordance with Section 4.01 hereof, and LTC Properties shall have the burden of proof to overcome that presumption in connection with the making of any person, persons or entity of any determination contrary to that presumption.

Section 5.02. Effect of Other Proceedings. The termination of any Proceeding or of any claim, issue or matter therein, by judgment, order, settlement or conviction, or upon a plea of nolo contendere or its equivalent, shall not of itself adversely affect the right of Indemnitee to indemnification or create a presumption that Indemnitee does not meet the standards required for indemnification hereunder.

Section 5.03. Reliance as Safe Harbor. For purposes of any determination of good faith required under the applicable laws of any jurisdiction, Indemnitee shall be deemed to have acted in good faith if Indemnitee's action is based on (i) the records or books of account of an Enterprise, including financial statements, (ii) by information supplied to Indemnitee by an officer, director, agent, fiduciary, legal counsel or investment banker of an Enterprise (or such other professional engaged by an Enterprise whose position is such that reliance on such professional is reasonable under the circumstances) in the course of their duties, or (iii) on information or records given or reports made to an Enterprise by an independent certified public accountant or by an appraiser or other expert. The provisions of this Section 5.03 shall not be deemed to be exclusive or to limit in any way the other circumstances in which Indemnitee may be deemed to have met the applicable standard of conduct set forth in this Agreement.

Section 5.04. Actions of Others. The knowledge and/or actions, or failure to act, of any director, officer, agent or employee of any Enterprise shall not be imputed to Indemnitee for purposes of determining the right to indemnification under this Agreement.

ARTICLE 6.
REMEDIES OF INDEMNITEE

Section 6.01. Application. This Article 6 shall apply in the event of a Dispute (as hereinafter defined). For purposes of this Article 6, "Dispute" shall mean any of the following events:

(a) Any determination made pursuant to Article 4 hereof that Indemnitee is not entitled to indemnification under this Agreement;

(b) Advancement of Expenses pursuant to Article 3 hereof is not made within ten (10) days after receipt by LTC Properties of a request therefor;

(c) The determination of entitlement to indemnification has not been made within twenty (20) days after receipt by LTC Properties of the request for indemnification;

(d) Payment of indemnification is not made within ten (10) days after receipt by LTC Properties of a written request therefor;

(e) Payment of Expenses incurred pursuant to Section 4 is not made within ten (10) days after a determination has been made that Indemnitee is entitled to indemnification or such determination is deemed to be have been made pursuant to Article 4 hereof; or

(f) Any other claim arising out of or related to this Agreement.

Section 6.02. Arbitration. Each of the parties agrees to submit Dispute (including the scope of this agreement to arbitrate) to private and confidential dispute resolution proceedings as provided for in this Section 6.02.

(a) The parties shall attempt in good faith to settle the dispute between themselves without invoking the arbitration procedures provided for hereinbelow. If both parties agree, prior to proceeding to binding arbitration as provided for hereinbelow, the parties may submit the Dispute for mediation by a neutral mediator pursuant to the mediation services of JAMS/Endispute (or, if applicable, its successor) ("JAMS"). If the matter is so submitted for mediation by a neutral mediator from a JAMS panel of neutrals, such mediation shall be held in Los Angeles, California and shall be private and confidential. LTC Properties shall pay all mediator fees and all other costs of such mediation. All offers, promises, conduct and statements, whether oral or written, made in the course of the mediation by either party, their respective agents, members, managers, directors, officers, employees, experts or attorneys, the mediator or any JAMS employees will be confidential, privileged and inadmissible for any purpose, including impeachment, in any arbitration or other proceeding involving the parties, provided that otherwise admissible or discoverable evidence will not be rendered inadmissible or non-discoverable as a result of its use in any such mediation. If it appears to either party at any time that the parties were unable to resolve the Dispute themselves or through mediation (whether or not any such mediation has commenced), then either party may at any time elect to initiate arbitration as set forth below.

(b) Either party may submit the Dispute to arbitration by JAMS. Arbitration shall be initiated by either party giving notice (the "Arbitration Notice") to the other party of such party's desire to have the Dispute arbitrated in accordance with this Section 6.02. Concurrently with the issuance of such Arbitration Notice (the "Commencement Date"), the initiating party shall file a demand for arbitration with JAMS in accordance with JAMS' procedures applicable to the commencement of an arbitration by a single neutral arbitrator. Any such arbitration shall be conducted in accordance with and shall be subject to the following provisions of this Section 6.02.

(c) The arbitration will be a final and binding arbitration, without right of appeal, before a single JAMS arbitrator. Except as modified by this Section 6.02, the arbitration will be conducted in accordance with the provisions of JAMS' Comprehensive Arbitration Rules and Procedures in effect at the time of filing of the demand for arbitration. Notwithstanding the foregoing, to the extent the discovery procedures contained in this Section 6.02

are broader than the JAMS' Comprehensive Arbitration Rules and Procedures relating to discovery, the procedures contained in this Section 6.02 shall govern.

(d) The parties will cooperate with JAMS and with one another in selecting the single arbitrator, who shall be a retired judge, from JAMS' panel of neutrals and in scheduling the arbitration proceedings. If either party so requests, there shall be a tape or stenographic record of any arbitration hearings.

(e) The place of arbitration shall be in Los Angeles, California.

(f) The parties shall facilitate the arbitration by: (i) making available to each other and to the arbitrator, for inspection and copying, all documents, books, records and Persons under their control or controlling such party if determined by the arbitrator to be relevant to the Dispute; (ii) conducting arbitration hearings to the greatest extent possible on successive, contiguous business days; and (iii) observing strictly the time periods established by the arbitrator for the submission of evidence and briefs.

(g) Consistent with the nature of arbitration, each party will, upon the written request of the other party, within 30 days of receipt of the request, provide the other with copies of documents relevant to the issues raised by any claim, counterclaim or defense. Any dispute regarding discovery shall be determined by the arbitrator, which determination shall be conclusive and final. All document discovery shall be completed within such time as may be determined by the arbitrator.

(h) At the request of a party, the arbitrator shall have the discretion to order examination by deposition of witnesses to the extent the arbitrator deems such deposition relevant and appropriate. With respect to such requests, each party shall submit to the other party and to the arbitrator, within 90 days after the appointment of a neutral arbitrator pursuant to Section 6.02(d) hereinabove, a list of proposed deponents, provided, however, any party may supplement such proposed list of deponents following the receipt of requested documents from the other party and/or the taking of any deposition if such party represents in good faith that such supplemental request is based on new information obtained from the review of any such document and/or the taking of any such deposition. Depositions shall be held within 30 days of the making of a request, unless the arbitrator for good cause determines otherwise. All objections to questions posed at any deposition shall be reserved for the arbitration hearing except for objections based on privilege and proprietary or confidential information.

The arbitrator will have the right to award any damages permitted by law, except that the arbitrator will have no authority to award punitive damages except as may be specifically authorized by statute. Any monetary award may, at the discretion of the arbitrator, include pre-award interest at the rate then provided by California law. Unless otherwise specified in the arbitration award, the arbitration award will bear interest at ten percent (10%) per annum (but not in excess of the rate permitted by law) from the date of the award. Judgment may be entered on the arbitration award in any court of competent jurisdiction in accordance with the rules and procedures of such jurisdiction.

(i) The prevailing party in any such arbitration (if there is a "prevailing party" as determined by the arbitrator) shall be entitled to a payment from the other party of reasonable attorneys' fees and other reasonable arbitration expenses (including without limitation any and all expenses incurred prior to the Commencement Date).

(j) The arbitration award shall be in writing, shall be signed by the arbitrator and shall include a statement of the reasons for the disposition of each claim. Such award shall be personally served on each of the parties.

(k) The arbitration shall be private and confidential. Except as may be required by law, neither the parties nor any arbitrator shall disclose the existence, content or results of any arbitration hereunder without the prior written consent of both parties.

(l) The decision arrived at by the arbitrator shall be binding upon all the parties to the arbitration, and no appeal shall be taken therefrom.

(m) If LTC Properties fails to pay the JAMS' or arbitrator's fees when and as required by JAMS or the arbitrator, then Indemnitee may request, on ten (10) business days' written notice to LTC Properties that the matter be resolved by default against LTC Properties, unless such fees are deposited within said ten (10) day notice period, in which case the arbitrator, shall enter an award by default against LTC Properties if such fees are not deposited as required.

(n) The procedures set forth in this Section 6.02 are intended to be the exclusive method of resolving any dispute arising out of or related to this Agreement, whether by contract, tort or statute, including without limitation the applicability of this Section 6.02. The only exception to the arbitration provisions contained in this Section 6.02 shall be an action by either party seeking non-monetary and equitable relief, including injunctive relief, in a court of competent jurisdiction. The obligations to arbitrate as required by this Section 6.02 may be enforced by any court having jurisdiction, and the party seeking enforcement will be entitled to an award of its costs and expenses, including its actual attorneys fees, in doing so. Anything to the contrary appearing in this Agreement notwithstanding, for all purposes of this Agreement arbitrators appointed pursuant to this Section 6.02 shall be deemed to be the sole tribunals of competent jurisdiction with respect to any matter required to be arbitrated by the terms of this Section 6.02.

Section 6.03. De Novo Review. In the event that a determination shall have been made pursuant to Article 4 hereof that Indemnitee is not entitled to indemnification, any arbitration commenced pursuant to this Article 6 shall be conducted in all respects on a de novo basis on the merits, Indemnitee shall not be prejudiced by reason of that adverse determination and such adverse determination and the records of the prior proceedings giving rise to such adverse determination shall be inadmissible in such de novo arbitration. In any such arbitration LTC Properties shall have the burden of proving that Indemnitee is not entitled to indemnification or advancement of Expenses, as the case may be, by clear and convincing evidence.

Section 6.04. Procedures Valid. LTC Properties shall be precluded from asserting in any judicial proceeding or arbitration commenced pursuant to this Article 6 that the procedures and presumptions of Articles 4 and 5 are not valid, binding and enforceable and shall stipulate in any such court or before any such arbitrator that LTC Properties is bound by all the provisions of this Agreement.

ARTICLE 7.
NON-EXCLUSIVITY, INSURANCE, SUBROGATION.

Section 7.01. Non-exclusivity. The right of Indemnitee to be indemnified for, held harmless against and to receive advancement of Expenses and Covered Amounts as provided by this Agreement shall not be deemed exclusive of any other rights to which Indemnitee may at any time be entitled under applicable law, the Articles, Bylaws or other organizational documents of any Enterprise or any other entity, any agreement, a vote of shareholders, a resolution of directors or otherwise. No amendment, alteration or replacement of this Agreement or any provision hereof shall be effective as to Indemnitee with respect to any action taken or omitted to be taken by Indemnitee in any Corporate Position prior to such amendment, alteration or replacement.

Section 7.02. Insurance. LTC Properties may maintain an insurance policy or policies against liability arising out of this Agreement or otherwise. However, nothing contained in this Agreement shall obligate LTC Properties to maintain any D&O Insurance, Liability Insurance or any other insurance, provided, however, that if LTC Properties chooses to maintain any such insurance it shall do so with respect to Indemnitee to the same extent as it does with respect to any director of LTC Properties or any Enterprise.

Section 7.03. Subrogation. In the event of any payment under this Agreement LTC Properties shall be subrogated to the extent of such payment to all of the rights of recovery of Indemnitee, who shall execute all papers reasonably required and take all action reasonably necessary, without in any way prejudicing Indemnitee's rights and remedies, to secure such rights, including execution of such documents as are necessary to enable LTC Properties to bring suit to enforce such rights, subject to any subrogation rights of an insurer pursuant to a policy obtained under Section 7.02.

Section 7.04. No Duplicative Payment. LTC Properties shall not be liable under this Agreement to make any payment of amounts otherwise indemnifiable hereunder if and to the extent that Indemnitee has otherwise

actually received a final payment or any undertaking to make final payment under any insurance policy, contract, agreement or otherwise. Notwithstanding anything to the contrary, this Agreement shall not operate to, and shall not be interpreted to, cause LTC Properties, and Enterprises or Indemnitee to lose the benefit of, or right to receive payment under, any D&O Insurance, Liability Insurance or any other insurance policy.

ARTICLE 8.
MISCELLANEOUS PROVISIONS.

Section 8.01. Entire Agreement. This Agreement supersedes any and all Agreements, either written or oral, between the parties hereto with respect to the subject matter hereof. Any amendment or modification of this Agreement shall be effective only if it is in writing signed by the authorized representatives of both parties.

Section 8.02. Governing Law. This Agreement shall be governed by and construed in accordance with the domestic laws of the State of California without giving effect to any choice or conflict of law provisions, except to the extent that the laws of the State of Maryland require that Maryland law be applied.

Section 8.03. Binding Effect. Each reference herein to any party shall be deemed to include such party's successors and assigns, legal representatives, executors or administrators.

Section 8.04. Waiver, Etc. Any waiver on the part of any party hereto of any right or interest under this Agreement shall not constitute the waiver of any other right or interest or any subsequent waiver of such right or interest. The failure of any party at any time to require performance of any provision of this Agreement shall not affect the right of any such party to require full performance thereof at any time thereafter. Any waiver by any party of a breach of any provision of this Agreement shall not constitute a waiver of any subsequent breach thereof and shall not nullify the effectiveness of such provision. The failure by any party to give notice of a breach of any provision of this Agreement shall not constitute a waiver of such breach.

Section 8.05. Severability. The invalidity or unenforceability of any provision of this Agreement shall not affect the validity or enforceability of any other provision of this Agreement, and this Agreement shall continue in full force and effect except for any such invalid or unenforceable provision.

Section 8.06. Captions. The captions throughout this Agreement are for convenience only and are not intended to limit or be used in the interpretation of the provisions of this Agreement.

[SIGNATURE PAGE TO FOLLOW]

IN WITNESS WHEREOF, the parties hereto have executed this Agreement on the date hereinabove mentioned.

LTC PROPERTIES, INC.,
a Maryland corporation

By:______________________________________
Name: Edmund C. King
Title: Compensation Committee Chairman

INDEMNITEE

____
Name: ((INDEMNITEE))

EXHIBIT 10.35

EMPLOYMENT AGREEMENT

This Employment Agreement (the "Agreement"), effective as of September 4, 2001, is by and between LTC Properties, Inc., a corporation organized under the laws of the State of Maryland ("LTC" or the "Company"), and Alex Chavez ("Executive").

NOW THEREFORE, for good and valuable consideration, the receipt and adequacy of which are hereby acknowledged, the parties hereto agree as follows:

1. Appointment, Title and Duties. LTC hereby employs Executive to serve as its Senior Vice President and Treasurer. In such capacity, Executive shall report to the Chief Executive Officer and Chief Financial Officer of the Company, and shall have such duties, powers and responsibilities as are customarily assigned to a Senior Vice President and Treasurer of a publicly held corporation, but shall also be responsible to the Board of Directors and to any committee thereof. In addition, Executive shall have such other duties and responsibilities as the Chief Executive Officer and Chief Financial Officer may assign him, with his consent, including serving with the consent or at the request of the Chief Executive Officer as an officer or on the board of directors of affiliated corporations.

2. Term of Agreement. The term of this Agreement shall commence as of the date hereof and shall extend such that at each and every moment of time hereafter the remaining term shall be one year.

3. Acceptance of Position. Executive accepts the position of Senior Vice President and Treasurer of LTC, and agrees that during the term of this Agreement he will faithfully perform his duties and, except as expressly approved by the Board of Directors of LTC, will devote substantially all of his business time to the business and affairs of LTC (and, to the extent requested by the Chief Executive Officer or Chief Financial Officer, LTC Healthcare, Inc.), and will not engage, for his own account or for the account of any other person or entity, in a business which competes with LTC. It is acknowledged and agreed that Executive may serve as an officer and/or director of companies in which LTC owns voting or non-voting stock. In addition, it is acknowledged and agreed that Executive may, from time to time, serve as a member of the board of directors of other companies, in which event the Board of Directors of LTC must expressly approve such service pursuant to a Board resolution maintained in the Company's minute books. Any compensation or remuneration which Executive receives in consideration of his service on the board of directors of other companies shall be the sole and exclusive property of Executive, and LTC shall have no right or entitlement at any time to any such compensation or remuneration.

4. Salary and Benefits. During the term of this Agreement:

(a) LTC shall pay to Executive a base salary at an annual rate of not less than One Hundred Thirty Five Thousand Dollars ($135,000) per annum ("Base Salary"), paid in approximately equal installments at intervals based on any reasonable Company policy. LTC agrees from time to time to consider increases in such base salary in the discretion of the Board of Directors. Any increase, once granted, shall automatically amend this Agreement to provide that thereafter

Executive's base salary shall not be less than the annual amount to which such base salary has been increased.

(b) Executive shall participate in all health, retirement, Company-paid insurance, sick leave, disability, expense reimbursement and other benefit programs which LTC makes available to any of its senior executives, and shall be eligible for bonuses in the discretion of the Board of Directors.

(c) Executive shall be entitled to reasonable vacation time, not less than four (4) weeks per year, provided that not more than two (2) weeks of such vacation time may be taken consecutively without prior notice to and non-objection by the Compensation Committee of the Board of Directors or, if there is no Compensation Committee, the Board of Directors.

5. Certain Terms Defined. For purposes of this Agreement:

(a) Executive shall be deemed to be "disabled" if a physical or mental condition shall occur and persist which, in the written opinion of a licensed physician selected by the Board of Directors in good faith, has rendered Executive unable to perform the duties set forth in Section 1 hereof for a period of sixty (60) days or more and, in the written opinion of such physician, the condition will continue for an indefinite period of time, rendering Executive unable to return to his duties;

(b) A termination of Executive's employment by LTC shall be deemed for "Cause" if, and only if, it is based upon (i) conviction of a felony; (ii) material disloyalty to the Company such as embezzlement, misappropriation of corporate assets or, except as permitted pursuant to Section 3 of this Agreement, breach of Executive's agreement not to engage in business for another enterprise of the type engaged in by the Company; or (iii) the engaging in unethical or illegal behavior which is of a public nature, brings LTC into disrepute, and result in material damage to the Company. The Company shall have the right to suspend Executive with pay, for a reasonable period to investigate allegations of conduct which, if proven, would establish a right to terminate this Agreement for Cause, or to permit a felony charge to be tried. Immediately upon the conclusion of such temporary period, unless Cause to terminate this Agreement has been established, Executive shall be restored to all duties and responsibilities as if such suspension had never occurred;

(c) A resignation by Executive shall not be deemed to be voluntary and shall be deemed to be a resignation with "Good Reason" if it is based upon (i) a diminution in Executive's title, duties, or salary; (ii) a reduction in benefits which is not part of an across-the-board reduction in benefits of all senior executive personnel; (iii) a direction by the Board of Directors that Executive report to any person or group other than the Chief Executive Officer and Chief Financial Officer or the Board of Directors, or (iv) a geographic relocation of Executive's place of work a distance for more than seventy-five (75) miles from LTC's offices located at 300 Esplanade Drive, Suite 1860, Oxnard, California;

(d) "Affiliate" means with respect to any Person, a Person who, directly or indirectly, through one or more intermediaries, controls, is controlled by or is under common control, with the Person specified;

(e) "Base Salary" means, as of any date of termination of employment, the highest base salary of Executive in the then current fiscal year or in any of the last four fiscal years immediately preceding such date of termination of employment;

(f) "Beneficial Owner" shall have the meaning given to such term in Rule 13d-3 under the Exchange Act;

(g) A "Change in Control" occurs if:

(i) Any Person or related group of Persons (other than Executive and his Related Persons, the Company or a Person that directly or indirectly controls, is controlled by, or is under common control with, the Company) is or becomes the Beneficial Owner, directly or indirectly, of securities of the Company representing 30% or more of the combined voting power of the Company's then outstanding securities; or

(ii) The stockholders of the Company approve a merger or consolidation of the Company with any other corporation (or other entity), other than a merger or consolidation which would result in the voting securities of the Companyoutstanding immediately prior thereto continuing to represent (either by remaining outstanding or by being converted into voting securities of the surviving entity) more than 66-2/3% of the combined voting power of the voting securities of the Company or such surviving entity outstanding immediately after such merger or consolidation; provided, however, that a merger or consolidation effected to implement a recapitalization of the Company (or similar transaction) in which no Person acquires more than 30% of the combined voting power of the Company's then outstanding securities shall not constitute a Change in Control; or

(iii) The Stockholders of the Company approve a plan of complete liquidation of the Company or an agreement for the sale or disposition by the Company of all or substantially all of the Company's assets; or

(iv) A majority of the members of the Board of Directors of the Company cease to be Continuing Directors;

(h) "Code" means the Internal Revenue Code of 1986, as amended.

(i) "Continuing Director" means, as of any date of determination, any member of the Board of Directors who (i) was a member of such Board of Directors on the date of the Agreement or (ii) was nominated for election or elected to such Board of Directors with the approval of a majority of the Continuing Directors who were members of such Board of Directors at the time of such nomination or election.

(j) "Exchange Act" means the Exchange Act of 1934, as amended.

(k) "Person" means any individual, corporation, partnership, limited liability company, trust, association or other entity.

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(l) "Related Person" means any immediate family member (spouse, partner, parent, sibling or child whether by birth or adoption) of the Executive and any trust, estate or foundation, the beneficiary of which is the Executive and/or an immediate family member of the Executive.

6. Certain Benefits Upon Termination. Executive's employment shall be terminated upon the earlier of (i) the voluntary resignation of Executive with or without Good Reason; (ii) Executive's death or permanent disability; or (iii) upon the termination of Executive's employment by LTC for any reason at any time. In the event of such termination, the below provisions of this Section 6 shall apply.

(a) If Executive's employment by LTC terminates for any reason other than as a result of (i) a termination for Cause, or (ii) a voluntary resignation by Executive without a Good Reason, or (iii) a Change in Control of the Company, then LTC shall pay Executive a lump sum severance payment equal to one times his Base Salary; provided that if employment terminates by reason of Executive's death or disability, then such salary shall be paid only to the extent the Company has available "key man" life, disability or similar insurance relating to the death or disability of Executive;

(b) Upon a Change in Control of the Company whether or not Executive's employment is terminated thereby, in lieu of the severance payment described in Section 6(a) above, LTC shall pay Executive a lump sum severance payment in cash equal to two times his Base Salary;

(c) If Executive's employment by LTC terminates for any reason, except for LTC's termination of Executive's employment for Cause or a voluntary resignation by Executive without a Good Reason, LTC shall offer to Executive the opportunity to participate in all Company-provided medical and dental plans to the extent Executive elects and remains eligible for coverage under COBRA and for a maximum period of eighteen (18) months at Company expense; provided, however, in the event Executive's employment by LTC terminated upon a Change in Control of the Company, then Executive shall not be given the opportunity to participate in any of such medical and dental plans, except to the extent required by law;

(d) In the event that Executive's employment terminates by reason of his death, all benefits provided in this Section 6 shall be paid to his estate or as his executor shall direct, but payment may be deferred until Executive's executor or personal representatives has been appointed and qualified pursuant to the laws in effect in Executive's jurisdiction of residence at the time of his death;

(e) LTC shall make all payments pursuant to the foregoing subsections (a) through (d) within seven (7) days following the date of termination of Executive's employment or consummation of a Change in Control of the Company, as applicable;

(f) Notwithstanding the foregoing, LTC shall have no liability under this Section if Executive's employment pursuant to this Agreement is terminated by LTC for Cause or by Executive without a Good Reason; provided, however, that if Executive's employment pursuant to this Agreement is terminated by LTC for Cause or by Executive without a Good Reason at any time after a Change of Control which did not result in Executive's employment being terminated, such post-Change of Control termination by LTC for Cause or by Executive without a Good Reason shall not affect in any way Executive's entitlement to the lump sum severance payment described in Section 6(b) above or any other rights, benefits or entitlements to which Executive may be entitled as a result of such Change of Control;

7. Tax Liability Loan. Upon a Change in Control of the Company, whether or not Executive's employment is terminated as a result thereof, the Company shall offer Executive an unsecured loan in the amount necessary to fund Executive's tax liability arising from the accelerated vesting of restricted shares held by Executive, if any. Such loan shall be due, in full, in ten (10) years from the

date made and shall bear interest at the then-current Applicable Federal Rate (the minimum rat necessary to avoid "unstated interest" under Section 7872 of the Code) with interest payments to be paid to the Company annually. Such loan shall be evidenced by a promissory note signed by, and with full recourse to, Executive.

8. Indemnification. LTC shall indemnify Executive and hold him harmless from and against all claims, actions, losses, damages, expense or liabilities (including expenses of defense and settlement) ("Claim") based upon or in any way arising from or connected with his employment by LTC, to the maximum extent permitted by law. To the extent permitted by law, LTC shall advance to Executive any expenses necessary in connection with the defense of any Claim which is brought if indemnification cannot be determined to be available prior to the conclusion of, or the investigation of, such Claim. The parties hereto agree that each understands and has understood that notwithstanding the above-stated provisions, nothing herein shall require LTC to hold harmless or indemnify Executive with respect to any Claim which is brought or asserted against Executive by LTC. LTC shall investigate in good faith the availability and cost of directors' and officers' insurance and shall include Executive as an insured in any directors and officers insurance policy of such insurance it maintains.

9. Attorney Fees. In the event that any action or proceeding is brought to enforce the terms and provisions of this Agreement, the prevailing party shall be entitled to recover reasonable attorney fees.

10. Notices. All notices and other communications provided to either party hereto under this Agreement shall be in writing and delivered by certified or registered mail to such party at its/his address set forth below its/his signature hereto, or at such other address as may be designated with postage prepaid, shall be deemed given when received.

11. Construction. In constructing this Agreement, if any portion of this Agreement shall be found to be invalid or unenforceable, the remaining terms and provisions of this Agreement shall be given effect to the maximum extent permitted without considering the void, invalid or unenforceable provisions. In construing this Agreement, the singular shall include the plural, the masculine shall include the feminine and neuter genders as appropriate, and no meaning in effect shall be given to the captions of the sections in this Agreement, which are inserted for convenience of reference only.

12. Headings. The section headings hereof have been inserted for convenience of reference only and shall not be construed to affect the meaning, construction or effect of this Agreement.

13. Governing Law. The provisions of this Agreement shall be construed and interpreted in accordance with the internal laws of the State of California as at the time in effect.

14. Entire Agreement. This Agreement constitutes the entire agreement and supersedes all other prior agreements (including the Employment Agreement dated as of the date hereof) and undertakings, both written and oral, among Executive and the Company, with respect to the subject matter hereof.

IN WITNESS WHEREOF, this Agreement shall be effective as of the date specified in the first paragraph of this Agreement.

LTC PROPERTIES, INC.,
a Maryland corporation

Address: 300 Esplanade St., #1860
Oxnard, CA 93030

/s/ Andre C. Dimitriadis
Chairman and Chief Executive Officer

By: /s/ Edmund King
Compensation Committee Representative

Address: 127 Los Padres Dr.
Thousand Oaks, CA 91361

/s/ Alex Chavez

EXHIBIT 10.36

PROMISSORY NOTE

$7,000,000.00 DATE: December 31, 2001

Oxnard, California

THIS NOTE (THIS "NOTE"), IS MADE BY HEALTHCARE HOLDINGS, INC., A NEVADA CORPORATION, AS MAKER ("MAKER"), IN FAVOR OF LTC PROPERTIES, INC., A MARYLAND CORPORATION, AS PAYEE ("PAYEE") IN THE AMOUNT OF SEVEN MILLION DOLLARS ($7,000,000.00).

At Maturity Date, as hereinafter defined, for value received, Maker hereby promises to pay to the order of Payee, at Payee's principal place of business in Oxnard, California, or such other place as Payee may from time to time designate, the principal sum of Seven Million Dollars ($7,000,000.00) plus accrued interest at the rate of 5%, compounded annually, ("Compounded Interest") of One Million Nine Hundred Thirty-Three Thousand Nine Hundred Seventy Dollars and Ninety-four cents ($1,933,970.94). In addition, during the term of the Note, Maker shall pay to Payee on an annual basis accrued interest at the rate of 2% ("Annual Interest") on the principal balance of $7,000,000. Therefore, on each anniversary date of the Note, beginning December 31, 2002 and ending with the last payment of Annual Interest on December 31, 2006, Maker shall pay to Payee One Hundred Forty Thousand Dollars ($140,000). All principal and accrued Compound Interest shall be due on or before December 31, 2006 (the "Maturity Date"). Principal and interest due hereunder shall be payable in lawful money of the United States.

Subject to the limitations described herein, Maker desires to obtain this Note from Payee to enable Maker to purchase from Payee the right to receive, 1,238,076 shares of common stock of Assisted Living Concepts, Inc. to be distributed pursuant to the First Amended Joint Plan of Reorganization of Assisted Living Concepts, Inc. ("ALF") and Carriage House Assisted Living, Inc. ("Plan"), which Plan was subsequently confirmed at a hearing on December 5, 2001 as set forth in, and subject to, that certain Findings of Fact, Conclusions of Law and Order Under 11 U.S.C. Section 1129 and Rule 3020 of the Federal Rules of Bankruptcy Procedure Confirming the Plan of the Companies entered on December 5, 2001. Accordingly, this Note represents funds that have been borrowed by Maker in the aggregate principal amount of Seven Million Dollars ($7,000,000.00) to make such purchase.

1. <u>Payments on Maturity Date</u>. Assuming no acceleration by Payee and no\ prepayment in full of the Loan by Maker, on the Maturity Date, Maker shall pay to Payee the entire outstanding principal, compound interest and accrued interest owing to Payee by Maker under this Note.

2. <u>Prepayments</u>. Maker shall have the right to prepay all or any part of the principal and accrued interest balance of this Note any time without premium, penalty, or charge of any kind whatsoever; provided, however, there shall be no discount of any kind for any prepayment.

3. <u>Security Documents</u>. This Note is a full recourse obligation of the Maker and is secured by all of the assets of Maker, whether heretofore or hereafter, including, but not limited to the ALF debentures and ALF common shares currently held by Maker; and the junior and senior debentures and the common shares to be distributed by ALF as described in the Plan and a security agreement and/or other security instruments given by Maker in favor of Payee, (collectively, the "Security Documents"). Reference is made to the Security Documents for a description of the collateral provided for therein and the rights of Payee with respect to such collateral.

4. <u>Sale of Collateral</u>. Maker may at any time, upon prior notice to Payee of five (5) business days, sell for cash all or a portion of the Collateral underlying this Note. One hundred percent (100%) of the proceeds, as hereinafter defined, must be remitted to the Payee within 3 business days of receipt of such proceeds. "Proceeds" is defined as total cash received before any costs, expenses or fees associated with such sale. Such Proceeds, to the extent of the proceeds, will first be applied to reduce any accrued but unpaid Annual Interest, second to reduce any accrued but unpaid Compounded Interest and finally to reduce the principal of the Note.

5. <u>Restrictive Covenants</u>. Maker hereby covenants and agrees with Payee that, for so long as the obligations of Maker under this Note remain outstanding

under the Note, Maker will comply with all of the following:

(a) Maker will not, and will not permit any subsidiary of Maker to, create, assume, incur or suffer to exist any lien or encumbrance of any kind, upon all or any portion of the Collateral (as defined in the Security Documents).

(b) Maker will not, and will not permit any subsidiary to pay a dividend, provide any loan guaranty, lend money or borrow any additional sums beyond this Note.

(c) Maker will not, and will not permit any subsidiary to (i) lease, assign or sell all or substantially all of its property or business to any other Person (as hereinafter defined), (ii) merge or consolidate with or into any other Person, (iii) purchase or lease or otherwise acquire all or substantially all of the assets of any other Person, (iv) sell, transfer, pledge or otherwise dispose of capital stock of Maker or any of its subsidiaries, (v) liquidate, suspend or dissolve its business operations, (vi) change its name, identity or corporate, partnership or other structure, or (vii) change the current principal place of business or chief executive office, in each case without the prior written consent of Payee.

6. Acknowledgement and Restrictive Covenant of LTC Healthcare, Inc., parent of Maker ("LTI"). LTI hereby acknowledges that it has heretofore pledged as collateral all of the outstanding stock of Maker pursuant to that certain Second Amended and Restated Promissory Note and Security Agreement dated June 8, 2001, which obligation remains in effect, and hereby further covenants and agrees with Payee that, for so long as the obligations of Maker under this Note remain outstanding, LTI will not pledge the stock of Maker, or otherwise encumber the stock of Maker, in any manner for any reason.

7. Change of Control. Notwithstanding anything to the contrary contained herein, upon a Change of Control (as hereinafter defined) Payee may, in its sole discretion, declare the entire balance of principal and interest hereon immediately due and payable, together with all applicable charges and payments due hereunder, all costs of collection, including reasonable attorneys' fees and all other costs and expenses incurred, and shall have all remedies available under the Security Documents, at law or in equity. For purposes of this Note, a "Change of Control" shall mean and include (i) the sale by Maker, or LTI (each hereinafter referred to as "Party") and/or any subsidiary of either Party of all or substantially all of the assets of either Party and its subsidiaries taken as a whole, (ii) any Acquisition by any person or any persons acting together which would constitute a "group" for purposes of Section 13(d) of the Exchange Act (a "Group") of 30% or more of the total voting power of all classes of capital stock of either Party entitled to vote generally in the election of the Board of Directors of either Party, (iii) any Acquisition by any person or Group of the power to elect, appoint or cause the election or appointment of at least a majority of the members of the Board of Directors of either party, through beneficial ownership of the capital stock or otherwise, or, (iv) a majority of the members of the Boards of Directors of either Party cease to be Continuing Directors (as hereinafter defined). As used herein, "Continuing Directors" means, as of any date of determination, any member of the Board of Directors of either party, who (i) was a member of the Boards of Directors of either Party on the date of this Note, or (ii) was nominated for election or elected to such Board with the approval of a majority of the Continuing Directors who were members of such Boards at the time of such nomination or election. For the purposes of this definition, "Acquisition" of the power or properties and assets stated in the preceding sentence means the earlier of (a) the actual possession thereof and (b) the consummation of any transaction or series of related transactions which, with the passage of time, will give such Person or Persons that actual possession thereof. As used herein, "Person" shall mean an individual, corporation, trust, partnership, joint venture, unincorporated organization, government agency or any agency or political subdivision thereof, or other entity.

8. Late Payment Charge; No Waiver. MAKER ACKNOWLEDGES THAT LATE PAYMENT TO PAYEE OF ANY SUMS DUE HEREUNDER WILL CAUSE PAYEE TO INCUR COSTS NOT CONTEMPLATED HEREUNDER, THE EXACT AMOUNT OF WHICH WILL BE IMPRACTICABLE OR EXTREMELY DIFFICULT TO ASCERTAIN. SUCH COSTS INCLUDE, BUT ARE NOT LIMITED TO, PROCESSING AND ACCOUNTING CHARGES. ACCORDINGLY, IF ANY INSTALLMENT IS NOT RECEIVED BY PAYEE WHEN DUE, OR IF ANY REMAINING PRINCIPAL AND ACCRUED BUT UNPAID INTEREST OWING UNDER THIS NOTE IS NOT PAID IN FULL ON THE MATURITY DATE, MAKER

SHALL THEN PAY TO PAYEE AN ADDITIONAL SUM OF FIVE PERCENT (5%) OF THE OVERDUE AMOUNT AS A LATE CHARGE. THE PARTIES HEREBY AGREE THAT THE LATE CHARGE REPRESENTS A FAIR AND REASONABLE ESTIMATE OF THE COSTS PAYEE WILL INCUR BY REASON OF LATE PAYMENT. THIS PROVISION SHALL NOT, HOWEVER, BE CONSTRUED AS EXTENDING THE TIME FOR PAYMENT OF ANY AMOUNT HEREUNDER, AND ACCEPTANCE OF SUCH LATE CHARGE BY PAYEE SHALL IN NO EVENT CONSTITUTE A WAIVER OF MAKER'S DEFAULT

WITH RESPECT TO SUCH OVERDUE AMOUNT NOR PREVENT PAYEE FROM EXERCISING ANY OF ITS OTHER RIGHTS AND REMEDIES WITH RESPECT TO SUCH DEFAULT.

INITIAL: _________
Maker

9. Additional Obligation. Maker agrees to purchase the right to receive any future distribution of ALF common stock the Payee may be entitled to receive as a result of the final settlement of the Plan. Such additional purchase shall be for $5.6539 per share and Maker shall sign an additional note with the same terms and conditions as this Note.

10. Default. The occurrence of any of the following shall constitute an event of default ("Event of Default") under this Note:

(a) failure to make any payment of principal, interest, or any other sums due hereunder within five (5) business days of the date due;

(b) the occurrence of any breach or default of any other obligation of Maker, LTI, or any of their respective subsidiaries, monetary or otherwise, hereunder or otherwise, which breach or default (except as provided below) shall continue for more than ten (10) calendar days after Maker or LTI has received written notice thereof from Payee;

(c) notwithstanding anything to the contrary contained in this Section 10, immediately upon the breach or default of any provision of Sections 4, 5, 6 and 9 hereof; or

(d) a breach or default under the Security Documents.

11. Acceleration Rights; Remedies. Upon the occurrence of an Event of Default or Change of Control hereunder, Payee may, in its sole discretion, declare the entire balance of principal and interest hereon immediately due and payable, together with all applicable charges and payments due hereunder, costs of collection, including reasonable attorneys' fees and all other costs and expenses incurred, and shall have any and all remedies available under the Security Documents, at law or in equity.

12. Attorneys' Fees and Costs. In the event it becomes necessary for Payee to utilize legal counsel for the enforcement of this Note or any of its terms, if Payee is successful in such enforcement by legal proceedings or otherwise, Payee shall be reimbursed immediately by Maker for all reasonable attorneys' fees and other costs and expenses.

13. Waivers. Maker of this Note hereby waives diligence, demand, presentment for payment, exhibit of this Note, notice of non-payment or dishonor, protest and notice of protest, notice of demand, notice of election of any right of holder hereof, any and all exemption rights against this indebtedness, and expressly agrees that, at Payee's election, the time for performance of any obligation under this note may be extended from time to time, without notice and that no such extension, renewal, or partial release shall release Maker from its obligation of payment of this Note or any installment hereof, and consents to offset of any sums owed to Maker by the holder hereof at any time.

14. Assignment/Transfer by Payee. Payee, in Payee's sole and absolute discretion, and without notice to Maker, shall have the absolute right to sell, assign, gift, transfer, convey, encumber or otherwise dispose of all or a portion of the holder's rights in this Note or any other agreement related thereto. Maker may not assign, gift,

transfer, convey, encumber or otherwise dispose of all or a portion of its rights, nor delegate its duties or obligations under this Note or any other agreement related thereto.

15. Governing Law. This Note shall in all respects be interpreted, enforced, and governed by and under the internal law of the State of California without resort to choice of law principles.

16. Severability. Every provision hereof is intended to be several. If any provision of this Note is determined by a court of competent jurisdiction to be illegal, invalid or unenforceable, such illegality, invalidity or

unenforceability shall not affect the other provisions hereof, which shall remain binding and enforceable.

17. Compliance With Usury Laws. It is the intention of the parties hereto to conform strictly to applicable usury laws regarding the use, forbearance or detention of the indebtedness evidenced by this Note, whether such laws are not or hereafter in effect, including the laws of the Untied States of America or any other jurisdiction whose laws are applicable, and including subsequent revisions to or judicial interpretations of those laws, in each case to the extent they are applicable to this Note (the "Applicable Usury Laws"); provided, however, if such laws shall hereafter permit higher rates of interest, then the Applicable Usury Laws shall be the laws allowing the higher rate of interest. Accordingly, the following shall apply:

(a) If any acceleration of the Maturity Date of this Note or any payment by maker or any other person or entity results in the amount of interest contracted for, charged, taken, reserved, received by or paid by Maker or such other person or entity on the principal amount outstanding, from time to time, on the Note being deemed to have been in excess of the Maximum Amount (as hereinafter defined) or if any transaction contemplated hereby would otherwise be usurious under any Applicable Usury Laws, then, in that event, notwithstanding anything to the contrary in this Note, it is agreed as follows: (i) the provisions of this Section 17 shall govern and control; (ii) the aggregate of all interest under Applicable Usury Laws that is contracted for, charged, taken, reserved or received under this Note, or under any of the other aforesaid agreements or instruments or otherwise shall under no circumstances exceed the Maximum Amount, and any excess shall either be refunded to Maker or applied in reduction of principal, if permitted by California law, in the sole discretion of Payee; (iii) neither Maker nor any other person or entity shall be obligated to apply the amount of such interest to the extent it is in excess of the Maximum Amount; (iv) any interest contracted for, charge, reserved, taken or received in excess of the Maximum Amount shall be deemed an accidental or bona fide error and canceled automatically to the extent of such excess; and (v) the effective rate of interest on the Loan shall be ipso facto reduced to the Highest Lawful Rate (as hereinafter defined), and the provision of this Note shall be deemed reformed, without the necessity of the execution of any new document, so as to comply with all Applicable Usury Laws. All sums paid, or agreed to be paid, to Payee for the use, forbearance, or the detention of the indebtedness of Maker to payee evidenced by this Note shall, to the fullest extent permitted by the Applicable Usury Laws, be amortized, pro-rated, allocated and spread throughout the full term of the indebtedness evidenced by this Note so that the actual rate of interest does not exceed the Highest Lawful Rate in effect at any particular time during the full term thereof. As used herein, the term "Maximum Amount" means the maximum non-usurious amount of interest which may be lawfully contracted for, charged, reserved, taken or received by Payee in connection with the indebtedness evidenced by this Note under all applicable Usury Laws.

(b) If at any time interest on the Loan, together with any fees and additional amounts payable hereunder or under any other agreements or instruments that are deemed to constitute interest under Applicable Usury Laws (the "Additional Interest"), exceeds the Highest Lawful Rate, then the amount of interest to accrue pursuant to this Note shall be limited, notwithstanding anything to the contrary in this Note, or any other agreement or instrument, to the amount of interest that would accrue at the Highest Lawful Rate; provided, however, that to the fullest extent permitted by Applicable Usury Laws, any subsequent reductions in the interest rate shall not reduce the interest to accrue pursuant to this Note below the Highest Lawful Rate until the aggregate amount of interest actually accrued pursuant to this Note, together with all Additional Interest, equals the amount of Interest which would have accrued if the Highest Lawful Rate had at all times been in effect and such Additional Interest, if any, had been paid in full.

For purposes of this Note, the term "Highest Lawful Rate" means the maximum rate of interest and other charges (if any such maximum exists) for the forbearance of the payment of monies, if any that may be

charged, contracted for, reserved, taken or received under all Applicable Usury Laws on the principal balance of this Note from time to time outstanding.

18. Notices. Any notice or other communication required or permitted to be given under this Note shall be in writing and sent by United States mail, registered or certified mail, postage prepaid, return receipt requested, and addressed as follows:

If to Maker: Healthcare Holdings, Inc.
300 Esplanade Drive, Suite 1865
Oxnard, California 93030

Attention: Mr. Chris Ishikawa

with a copy to: Healthcare Holdings, Inc.
300 Esplanade Drive, Suite 1865
Oxnard, California 93030
Attention: Legal Department

<u>If to Parent:</u> LTC Healthcare, Inc.
300 Esplanade Drive, Suite 1865
Oxnard, California 93030
Attention: Mr. Chris Ishikawa

<u>If to Payee:</u> LTC Properties, Inc.
300 Esplanade Drive, Suite 1860
Oxnard, California 93030
Attention: Ms. Wendy Simpson

with a copy to: LTC Properties, Inc.
300 Esplanade Drive, Suite 1860
Oxnard, California 93030
Attention: Legal Department

or such other address as either party may from time to time specify in writing to the other in the manner aforesaid. If personally delivered, such notices or other communications shall be deemed delivered upon delivery. If sent by United States mail, registered or certified mail, postage prepaid, return receipt requested, such notices or other communications shall be deemed delivered upon delivery or refusal to accept delivery as indicated on the return receipt.

[SIGNATURE PAGE FOLLOWS]

IN WITNESS WHEREOF, the Maker has caused this Note to be executed as of the date first above written.

MAKER:

HEALTHCARE HOLDINGS, INC.,
a Nevada corporation

By: /s/ Andre C. Dimitriadis

Name: Andre C. Dimitriadis
Its: Chairman and Chief Executive Officer

PARENT:

LTC HEALTHCARE, INC.,
a Nevada corporation

By: /s/ Wendy Simpson

Name: Wendy Simpson
Its: Executive Vice President

EXHIBIT 10.37

SECURITY AGREEMENT

THIS SECURITY AGREEMENT ("Agreement") is made and entered into as of the 31st day of December, 2001 by Healthcare Holdings, Inc., a Nevada corporation ("Debtor"), in favor of LTC Properties, Inc., a Maryland corporation ("Secured Party"), with reference to the following facts and circumstances.

A. Secured Party has agreed to extend a Loan (the "Loan") to Debtor, which Loan is evidenced by that certain Promissory Note of even date herewith executed by Debtor in favor of Secured Party (the "Note").

B. To secure its obligations under the Loan, Debtor has agreed, among other things, to grant Secured Party a security interest in all assets of Maker, whether heretofore or hereafter acquired.

NOW, THEREFORE, IN CONSIDERATION of the foregoing and other good and valuable consideration, the receipt and sufficiency of which are hereby acknowledged, Debtor and Secured Party hereby agree as follows:

1. Grant of Security Interest. As security for Debtor's due and punctual performance of the Obligations (as hereinafter defined), Debtor hereby pledges with and delivers to Secured Party the Collateral (as hereinafter defined), and grants, assigns, transfers and conveys to Secured Party a continuing security interest in all of Debtor's right, title and interest in and to the Collateral.

2. Obligations. This Agreement, and Debtor's pledge of and grant to Secured Party of a security interest in and to the Collateral, is made to secure: (i) due and punctual performance of Debtor's obligation to make any and all payments when and as due under the Note, and any other note or instrument executed by Debtor and payable to Secured Party which recites that it is secured hereby, including any and all amendments, modifications, renewals, extensions, substitutions or replacements hereof or thereof, including any future advances which are made pursuant to the terms of the Note or any such note or instrument and the performance and discharge of each and every obligation of Debtor set forth in the Note or any such note or notes; (ii) payment of all other sums, with interest thereon, herein or in the Note, or any such note or notes, or any part thereof; (iii) due, prompt and complete observance and performance of each and every obligation, covenant and agreement of Debtor contained herein, in the Note, or in any other instrument executed by Debtor for the purpose of further securing the indebtedness evidenced by the Note, or such note or notes, or any part thereof (collectively, the "Obligations").

3. Collateral. As used herein, the term "Collateral" shall collectively and severally mean all assets of Maker, including, but not limited to the following:

(a) $5,715,000 of 5.625% convertible subordinated debentures due May 2003 issued by Assisted Living Concepts, Inc. ("ALF"); 30,847 shares of ALF common stock; junior and senior debentures, and 1,238,076 common shares to be issued by ALF pursuant to the First Amended Joint Plan of Reorganization of ALF ("Plan") filed by ALF with the United States Bankruptcy Court for the District of Delaware, Case Nos. 01-1064 and 01-10670 and which Plan was subsequently confirmed on December 5, 2001 as set forth in, and subject to, that certain Findings of Fact, Conclusions of Law and Order Under 11 U.S.C. Section 1129 and Rule 3020 confirming the Plan.

(b) Accounts. All accounts, general intangibles, chattel paper, instruments (as defined in the California Uniform Commercial Code (the "Code")), and other obligations of any kind, now owned or held or hereafter acquired by the Debtor, including, without limitation, insurance claims, insurance settlement proceeds, tax refund claims and tax refunds arising out of or in connection with the sale or lease of goods or the rendering of services, and all rights in and to all security agreements, leases, and other contracts securing or otherwise relating to any such accounts, general intangibles, chattel paper, instruments or obligations, and all books and records relating to any of the foregoing (any and all of the foregoing being the "Accounts");

(c) Instruments. All notes and other instruments and any instrument which constitutes a part of chattel paper, and other evidences of indebtedness in which the Debtor now or hereafter has any interest, to the extent of that interest;

(d) Documents. All documents (as defined in the Code) in which the Debtor now or hereafter has any interest, to the extent of that interest;

(e) Chattel Paper. All chattel paper in which the Debtor now or hereafter has any interest;

(f) General Intangibles. All General Intangibles (as hereinafter defined) in which the Debtor now or hereafter has any interest, to the extent of that interest. "General Intangibles" means any "general intangibles," as such term is defined in the Code, and shall include, without limitation, (i) all patents, patent applications, trademarks, trademark registrations, trade names and trademark applications; (ii) license agreements with any other party, whether the Debtor is a licensor or licenses under any such license agreement, and the right to prepare for sale, sell and advertise for sale all inventory now or hereafter covered by such licenses; (iii) all of the Debtor's books, records and files, including computer software and tapes and all other forms of electronic information storage; (iv) copyrights and other rights in intellectual property; (v) interests in partnerships, joint ventures and other business associations; (vi) licenses and permits; (vii) trade secrets, proprietary or confidential information, customer lists, inventions (whether or not patented or patentable), technical information, procedures, designs, knowledge, know-how, software, data bases, data, skill, expertise, experience, processes, models, drawings, materials and records, and goodwill; (viii) claims in or under insurance policies, including unearned premiums; (ix) uncertificated securities; (x) deposit accounts; (xi) rights to receive tax refunds and other payments; (xii) rights of indemnification; and (xiii) all of the Debtor's rights under any warranties or guaranties of any kind, including equipment, machinery or services;

(g) Contracts. All of the Debtor's rights under all contracts undertakings or agreements (other than rights evidenced by chattel paper, documents or instruments) in or under which the Debtor may now or hereafter have any right, title or interest, including, without limitation, with respect to an Account, any agreement relating to the terms of payment or the terms of performance thereof;

(h) Money and Other Personal Property. All money (as defined in the Code) and all other goods and personal property in which the Debtor has any interest, to the extent of that interest, whether now or hereafter owned or existing, leased, consigned by or to or acquired by the Debtor and wherever located; and

(i) Stock. All of the outstanding capital stock of Debtor and its subsidiaries now formed or to be formed.

(j) Proceeds and Products. All proceeds and products of the foregoing (including, without limitation, cash proceeds and noncash proceeds resulting from the sale or other voluntary or involuntary disposition thereof or any other realization in respect thereof) and including, but not limited to, all property of any type that is acquired with any cash proceeds, and all guarantees, insurance and rights against sureties the Debtor may have in connection therewith and all proceeds and products relating thereto or therefrom, and all the Debtor's right, title and interest in and to additions, accessions, replacements and substitutions to and for the foregoing, and all documents, ledger sheets and files of the Debtor relating thereto. The term "proceeds" as used herein shall include, without limitation, all accounts, chattel paper, deposit accounts, instruments, equipment, inventory, documents, general intangibles and other proceeds that arise from the sale, lease, transfer or other use or disposition of any kind of any of the Collateral described in the foregoing paragraphs (a) through (j), inclusive, or proceeds, and all proceeds of any type described above acquired with cash proceeds.

4. Delivery of Collateral. Concurrently with the execution and delivery of this Agreement, Debtor shall deliver to Secured Party debentures and all stock certificates representing the Collateral set forth in Section 3 above. Debtor agrees to deliver to Secured Party stock certificates representing all the outstanding shares of any subsidiaries owned by Debtor and formed hereafter.

5. Declaration of Trust. If Debtor shall become entitled to receive or shall receive any goods, instruments, documents, accounts, general intangibles or other property of any kind or nature delivered to Debtor on account of or in connection with Debtor's ownership of the Collateral, Debtor shall accept and

hold the same as Secured Party's agent, in trust for Secured Party, and shall forthwith, without notice or demand, endorse, transfer and deliver the same to Secured Party, accompanied, where necessary or appropriate, by assignments duly executed in blank, to be held by Secured Party as part of the Collateral.

6. Powers of Secured Party. Debtor appoints Secured Party its true attorney-in-fact to perform any of the following powers, which are coupled with an interest, are irrevocable until termination of this Agreement and may be exercised from time to time by Secured Party's officers, employees or agents, or any of them, whether or not an Event of Default has occurred: (i) to liquidate any certificate of deposit pledged to Secured Party hereunder prior to its maturity date and to apply the proceeds thereof to payment of the Obligations or hold such proceeds as part of the Collateral, notwithstanding the fact that such liquidation may give rise to penalties for early withdrawals of funds; (ii) to sell, exchange or otherwise dispose of any portion of the Collateral if Secured Party deems such transaction reasonably necessary to preserve the value of its security interest, and to apply the proceeds thereof to payment of the Obligations, to hold such proceeds as part of the Collateral or to use such proceeds to purchase similar items of Collateral that Secured Party, in its sole discretion, deems necessary or advisable to preserve the value of its security interest; (iii) to notify any person obligated on any security, instrument or other document subject to this Agreement of Secured Party's rights hereunder; (iv) to collect by legal proceedings or otherwise all dividends, interest, principal or other sums now or hereafter payable upon or on account of the Collateral; (v) to enter into any extension, reorganization, deposit, merger or consolidation agreement, or any other agreement relating to or affecting the Collateral or proceeds, and in connection therewith to deposit or surrender control of the Collateral, accept other property in exchange for the Collateral, and do and perform such acts and things as Secured Party may deem proper, and any money or property received in exchange for the Collateral may be applied to the Obligations or held by Secured Party under this Agreement; (vi) to make any compromise or settlement Secured Party deems necessary, desirable or proper in respect of the Collateral; (vii) to insure, process and preserve the Collateral; and (viii) to perform any obligation of Debtor under this Agreement, in Debtor's name or otherwise. To effect the purposes of this Agreement, or otherwise upon instructions of Debtor, Secured Party may cause the Collateral to be transferred to Secured Party's name or the name of Secured Party's nominee.

7. Secured Party's Care and Delivery of Collateral. Secured Party's obligation with respect to Collateral in its possession shall be strictly limited to the duty to exercise reasonable care in the custody and preservation of such Collateral, and such duty shall not include any obligation to ascertain or to initiate any action with respect to or to inform Debtor of maturity dates, conversion, call, or exchange rights, or offers to purchase the Collateral, or any similar matters, notwithstanding the Secured Party's knowledge of the same. Secured Party shall have no duty to take any steps necessary to preserve the rights of Debtor against prior parties, or to initiate any action to protect against the possibility of a decline in the market value of the Collateral. Secured Party shall not be obligated to take any action with respect to the Collateral requested by Debtor unless such request is made in writing, and Secured Party determines, in its sole discretion, that the requested actions would not unreasonably jeopardize the value of the Collateral as security for the Obligations. Secured Party may at any time deliver the Collateral, or any part thereof, to Debtor, and the receipt thereof by Debtor shall be a complete and full acquittance for the Collateral and proceeds so delivered, and Secured Party shall thereafter be discharged from any liability or responsibility therefor.

8. Representations and Warranties. Debtor represents and warrants to Secured Party as follows:

(a) Debtor is a Nevada corporation, duly incorporated, validly existing and in good standing under the laws of the State of the State of Nevada. Debtor is qualified to do business as a foreign corporation in every state in which Debtor is required to be so qualified.

(b) Debtor has all requisite capacity and power to execute, deliver and perform its obligations under this Agreement. This Agreement has been duly and validly executed and delivered by Debtor, and constitutes a valid and binding obligation of Debtor, enforceable in accordance with its terms.

(c) Debtor owns the Collateral free and clear of all liens, claims, encumbrances, security interests or equities, other than the security interest created hereby.

(d) Debtor has not sold, transferred, assigned or conveyed the Collateral, or any portion thereof, to any person other than Secured Party.

9. Covenants and Agreements of Debtor. Debtor covenants and agrees with Secured Party that from the date hereof and until payment and satisfaction in full of each and all of the Obligations, unless Secured Party shall otherwise consent in writing, Debtor will:

(a) Duly observe and perform each and every term and condition of any and all agreements, instruments and documents relating to the Collateral, and diligently protect and enforce its rights under all such agreements.

(b) Give Secured Party ten (10) days prior written notice before changing its principal residence or place of business or moving its books and records to a location other than that set forth in Section 17 hereof.

(c) Not sell, lease, assign, transfer, convey, pledge, hypothecate, mortgage or further encumber any of the Collateral, provided that Debtor may sell Inventory in the ordinary course of business.

(d) Promptly pay or otherwise cause to be discharged any lien, charge, security interest or other encumbrance that may attach to the Collateral, or any portion thereof, other than pursuant to this Agreement.

(e) Promptly notify Secured Party of any attachment or other legal process levied against any of the Collateral and any information received by Debtor relating to the Collateral, or to other persons obligated in connection therewith, and of any threatened or filed claims or proceedings, that might in any way affect or impair Secured Party's security interest in the Collateral or the rights and remedies of Secured Party with respect thereto.

(f) Defend the Collateral against all claims, liens, security interests, demands and other encumbrances of third parties at any time claiming an interest in the Collateral that is adverse to Secured Party's interest in the Collateral hereunder.

(g) Notify Secured Party in the event of any occurrence that may materially or adversely affect the security interest of Secured Party in the Collateral.

(h) At the request of Secured Party, execute and permit to be filed one or more financing statements, and amendments thereto, under the California Uniform Commercial Code and any other applicable state's Uniform Commercial Code naming Debtor as debtor and Secured Party as secured party and indicating therein the types or describing the Collateral.

(i) Not, without the prior written consent of Secured Party, execute, file or authorize or permit to be filed in any jurisdiction or with any governmental authority any financing or similar statement relating to the Collateral, or any portion thereof, in which any person other than Secured Party is named as a secured party thereunder.

(j) Reimburse Secured Party upon demand for any costs and fees, including reasonable attorneys' fees and accountants' fees and other expenses, incurred in collecting any sums payable by Debtor under any of the Obligations secured hereby, enforcing any term or provision of this Agreement or otherwise in the collection of the Collateral and the preparation and enforcement of any agreement relating thereto.

(k) Upon request of Secured Party, furnish within ten (10) days thereafter to Secured Party or to any proposed assignee of Secured Party, a written statement in form satisfactory to Secured Party, duly acknowledged, certifying the amount of the principal and interest then owing under the obligations and liabilities set forth in the Note, and stating that no claims, offsets or defenses exist with respect to the Note, this Agreement or any of the Loan Documents of any nature whatsoever.

(l) Execute and deliver to Secured Party any and all further agreements, instruments, or documents and take any and all such further action as Secured Party, in its sole discretion, may deem necessary or advisable in order to evidence, effectuate, perfect, protect, maintain, or realize upon Secured Party's security interest in the Collateral or the priority thereof.

10. Events of Default. The occurrence of any of the following shall constitute an "Event of Default" hereunder:

(a) Failure to make prompt and punctual payment or performance when due of any of the Obligations, including without limitation, any Event of Default under the Note.

(b) Any representation or warranty herein, in the Note, or in any other instrument executed by Debtor in connection with its obligations hereunder, proves materially false or misleading in any way.

(c) Breach of any covenant or promise contained herein or in any other instrument executed by Debtor in connection with its obligations hereunder.

(d) Debtor becomes insolvent, generally is not paying its debts as such debts become due, or makes an assignment for the benefit of creditors.

(e) Any case is commenced by or against Debtor, under any bankruptcy, reorganization, arrangement, readjustment of debt or moratorium law or similar statute if, with respect to a case commenced against Debtor, such case is not dismissed within sixty (60) days.

(f) Any writ of attachment, garnishment, execution or other legal process is issued against any property of Debtor, if such writ, garnishment, execution or other process is not fully vacated within sixty (60) days.

(g) Debtor seeks, consents to, acquiesces in or fails to cause to be vacated or stayed within sixty (60) days (or vacated within sixty (60) days of any such stay) the appointment of a receiver, trustee or conservator of all or any substantial portion of Debtor's property.

11. Secured Party's Remedies. If an Event of Default or Change of Control (as defined in the Note) occurs hereunder, then, Secured Party may, at its option, but is not required to, do any one or more of the following without demand or notice to Debtor:

(a) Declare all of the Obligations immediately due and payable in full, notwithstanding the terms of any other writing or evidence of debt;

(b) Transfer the Collateral into Secured Party's name or that of its nominee;

(c) From time to time, proceed with the foreclosure of Secured Party's security interest and sale of the Collateral, or any portion of it, in any manner permitted by law or provided for herein;

(d) Take possession of and retain the Collateral in satisfaction of the Obligations; or

(e) Exercise any and all remedies of a secured party under the California Uniform Commercial Code or as otherwise provided by law.

12. Application of Proceeds. After the occurrence of an Event of Default, all income and distributions with respect to the Collateral and all proceeds from any sale of the Collateral pursuant hereto shall be applied as follows:

(a) First, in such order as Secured Party shall in its sole discretion determine, (i) to the payment of all costs and expenses incurred by Secured Party in connection with any sale of the Collateral, including, without limitation, all court costs and the reasonable fees and expenses of counsel for Secured Party in connection therewith; and (ii) the payment of any and all other costs and expenses paid or incurred by Secured Party in connection with this Agreement or otherwise in connection with the Obligations or the exercise of any right or remedy hereunder;

(b) Second, to the payment of interest on the Obligations;

(c) Third, to the payment or satisfaction of the Obligations; and

(d) Fourth, any amounts remaining after the foregoing applications shall be remitted to Debtor or as a court of competent jurisdiction may otherwise direct.

13. Power of Attorney.

(a) Debtor does hereby irrevocably make, constitute and appoint Secured Party or any of its officers or designees its true and lawful attorney-in-fact with full power in the name of Secured Party or Debtor to receive, open and dispose of all mail relating to the Collateral addressed to Debtor (provided, however, that Secured Party shall provide Debtor with a copy of any mail so received), and to endorse any notes, checks, drafts, money orders or other evidence of payment relating to the Collateral that may come into the possession of Secured Party, and to do any and all other acts necessary or proper to carry out the intent of this Agreement, and Debtor hereby ratifies and confirms all that Secured Party or its substitutes shall properly do by virtue hereof;

(b) Debtor does hereby further irrevocably make, constitute and appoint Secured Party or any of its officers or designees its true and lawful attorney-in-fact in the name of Secured Party or Debtor, (i) to enforce all Debtor's rights under and pursuant to all agreements with respect to the Collateral, all for the sole benefit of Secured Party, and to enter into such other agreements as may be necessary to protect Secured Party's rights and interest in and to the Collateral; (ii) to enter into and perform such agreements as may be necessary in order to carry out the terms, covenants and conditions of this Agreement that are required to be observed or performed by Debtor; (iii) to execute such other and further pledges and assignments of the Collateral as Secured Party may reasonably require for the purpose of protecting, maintaining or enforcing the security interest granted to the Secured Party herein; and (iv) to do any and all other things necessary or proper to carry out the intention of this Agreement; and Debtor ratifies and confirms all that Secured Party as such attorney-in-fact or its substitutes shall properly do by virtue of this power of attorney; and

(c) Each of the foregoing appointments shall be deemed coupled with an interest and irrevocable.

14. Private Sale Authorized.

(a) Debtor recognizes that Secured Party may be unable to effect a public sale of all or part of the Collateral. Debtor consents to a private sale even though such sale may be at prices and upon terms less favorable than if the Collateral were sold at public sales. Debtor agrees that private sales will be deemed to have been made in a commercially reasonable manner.

(b) Debtor recognizes that a sale, public or private, of the Collateral may not be able to be effected and Secured Party or its assignee are hereby expressly authorized at their election to retain the Collateral until a sale can be effected. Until such sale, Secured Party or its assignee may elect to hold the Collateral and be treated as the owner thereof, and shall be entitled to collect all income thereon.

(c) The purchaser or purchasers at any public or private sale of the Collateral shall take the Collateral free of any right or equity of redemption in Debtor, which rights and equities Debtor hereby expressly waives.

(d) Debtor agrees that written notice mailed to Debtor ten (10) business days prior to the date of public sale of the Collateral or ten (10) business days prior to the date after which private sale or any other disposition of the Collateral will be made shall constitute reasonable notice for such sales.

15. Financing Statements and Payment Directions. To the extent permitted by law, Debtor hereby authorizes Secured Party to file any amendments to or continuations of any financing statement filed with regard to the Collateral without the signature of Debtor. Debtor further authorizes Secured Party upon an Event of Default to

notify any account custodian of the Collateral that all sums payable to Debtor relating to the Collateral shall be paid directly to Secured Party.

16. Termination. Upon satisfaction in full of all of the Obligations, and the satisfaction of all additional costs and expenses of Secured Party as provided herein, this Agreement shall terminate and Secured Party shall deliver to Debtor, at Debtor's expense, such of the Collateral as shall not have been sold or otherwise disposed of or applied pursuant to this Agreement; provided that if Secured Party is required to return any amounts received by Secured Party on account of the Obligations, the security interests provided hereunder shall reattach.

17. Notices. Any notice or other communication required or permitted to be given under this Agreement shall be in writing and sent by United States mail, registered or certified mail, postage prepaid, return receipt requested, and addressed as follows:

If to Maker:	Healthcare Holdings, Inc. 300 Esplanade Drive, Suite 1865 Oxnard, California 93030 Attention: Mr. Chris Ishikawa
with a copy to:	Healthcare Holdings, Inc. 300 Esplanade Drive, Suite 1865 Oxnard, California 93030 Attention: Legal Department
If to Parent:	LTC Healthcare, Inc. 300 Esplanade Drive, Suite 1865

Oxnard, California 93030
Attention: Mr. Chris Ishikawa

If to Payee:	LTC Properties, Inc. 300 Esplanade Drive, Suite 1860 Oxnard, California 93030 Attention: Ms. Wendy Simpson
with a copy to:	LTC Properties, Inc. 300 Esplanade Drive, Suite 1860 Oxnard, California 93030 Attention: Legal Department

or such other address as either party may from time to time specify in writing to the other in the manner aforesaid. If personally delivered, such notices or other communications shall be deemed delivered upon delivery. If sent by United States mail, registered or certified mail, postage prepaid, return receipt requested, such notices or other communications shall be deemed delivered upon delivery or refusal to accept delivery as indicated on the return receipt.

18. Survival of Representations. All covenants, agreements or representations and warranties made herein and in any documents delivered pursuant hereto shall survive the execution hereof.

19. Assignments. Whenever in this Agreement any of the parties hereto is referred to, such reference shall be deemed to include the successors and assigns of such party, and all covenants, promises and agreements by or on behalf of Debtor contained in this Agreement shall bind and inure to the benefit of the successors and assigns of Secured Party and Debtor.

20. California Law. This Agreement shall be governed by, and construed and enforced in accordance with, the laws of the State of California, without regard to conflict of laws principles.

21. No Implied Waivers by Secured Party. Neither any failure nor any delay on the part of Secured Party in exercising any right, power or privilege hereunder shall operate as a waiver thereof, nor shall a single or partial exercise thereof preclude any other or further exercise of any other right, power or privilege. The rights, remedies and benefits of Secured Party herein expressly specified are cumulative and not exclusive of any other rights, remedies or benefits that Secured Party may have at law, in equity, by statute or otherwise. Without limiting

the generality of the foregoing, Secured Party shall have all rights and remedies of a secured party under Division 9 of the California Uniform Commercial Code, as it may be amended or superseded from time to time.

22. Modifications and Waivers.

(a) No modification, amendment or waiver of any provision of this Agreement, nor consent to any departure of Debtor herefrom, shall in any event be effective unless the same shall be in writing and signed by Secured Party, and then such waiver or consent shall be effective only in the specific instance and for the purpose for which given.

(b) No notice or demand on Debtor in any case shall entitle Debtor to any other or further notice or demand in the same, similar or other circumstances.

(c) Debtor hereby waives presentment, notice of dishonor and protest of all instruments included in or evidencing the liability of Debtor in respect of the Obligations or the Collateral and any and all other notices and demands whatsoever, whether or not relating to such instruments.

(d) The Obligations shall not be affected by (i) the failure of Secured Party to assert any claim or demand or to enforce any right or remedy against Debtor; (ii) any extension or renewal thereof; (iii) any rescission, waiver, amendment or modification of any of the terms or provisions of this Agreement or of any other agreement; or (iv) the release of any collateral held by Secured Party for the Obligations or any of them.

23. Severability. In case any one or more of the provisions contained in this Agreement should be determined by a court of law to be invalid, illegal or unenforceable in any respect, the validity, legality and enforceability of the remaining provisions contained herein shall not in any way be affected or

impaired thereby.

24. Service of Process.

(a) Debtor hereby irrevocably submits itself to the jurisdiction of the state courts of the State of California and to the jurisdiction of the United States District Court for the Central District of California, for the purpose of any suit, action or other proceedings arising out of or based upon this Agreement or the subject matter hereof brought by Secured Party or its successors or assigns.

(b) Debtor hereby waives, and agrees not to assert, by way of motion, as a defense, or otherwise, in any such suit, action or proceeding, any claim that it is not subject personally to the jurisdiction of the above named courts, that its property is exempt or immune from attachment or execution, that the suit, action or proceeding is brought in an inconvenient forum, that the venue of the suit, action or proceeding is improper or that this Agreement or the subject matter hereof may not be enforced in or by such court.

(c) Debtor hereby waives any right to jury trial and any offsets or counterclaims in any such action, suit or proceeding (other than compulsory counterclaims).

(d) Debtor hereby consents to service of process by registered mail at the address to which notices are to be given. Debtor agrees that its submission to jurisdiction and its consent to service of process by mail is made for the express benefit of Secured Party.

(e) Final judgment against Debtor in any such action, suit or proceeding shall be conclusive, and may be enforced in other jurisdictions (i) by suit, action or proceeding on the judgment, a certified or true copy of which shall be conclusive evidence of the fact and of the amount of any indebtedness or liability of Debtor therein described; or (ii) in any other manner permitted by applicable law, provided, however, that Secured Party may at its option bring suit, or institute other judicial proceedings against any of Debtor's assets in any state or federal court of the United States or of any country or place where such assets may be found.

25. Indemnity and Reimbursement of Secured Party.

(a) Debtor agrees (i) to indemnify and hold harmless Secured Party, to the fullest extent permitted by law, from and against any and all claims, demands, losses, judgments and liabilities (including liabilities for penalties) arising out of, resulting from or relating to any of the Collateral, this Agreement or the administration, enforcement, exercise or defense of any right or remedy granted to Secured Party herein; and (ii) to reimburse Secured Party for all costs and expenses, including legal fees and disbursements, incurred after the date hereof and arising out of, resulting from or relating to any of the Collateral, this Agreement or the administration, enforcement, exercise or defense of any right or remedy granted to Secured Party herein. The foregoing indemnity includes any reasonable costs incurred by Secured Party in connection with any litigation relating to the Collateral whether or not Secured Party shall be a party to such litigation, including, but not limited to, the reasonable fees and disbursements of counsel to Secured Party and any out-of-pocket costs incurred by Secured Party in appearing as a witness or in otherwise complying with legal process served upon it. In no event shall Secured Party be liable to Debtor for any matter or thing in connection with this Agreement other than to account for moneys actually received by it in accordance with the terms hereof.

(b) If Debtor shall fail to do any act or thing that it has covenanted to do hereunder or under any of the Loan Documents or any representation of warranty of Debtor to Secured Party shall have been breached, Secured Party may, but shall not be obligated to, do the same or cause it to be done or remedy any such breach and there shall be added to the Obligations hereunder the cost of such expense incurred by Secured Party in so doing, and any and all amounts expended by Secured Party in taking any such action shall be repayable to it upon its demand therefor and shall bear interest at the applicable interest rate under the Note from the date such amounts are expended to the date of repayment.

26. Captions. The captions in this Agreement are inserted only as a matter of convenience and for reference and shall not be deemed to define, limit, enlarge, or describe the scope of this Agreement or the relationship of the parties, and shall not affect this Agreement or the construction of any provisions herein.

27. Pronouns. Whenever the context so requires, the masculine shall include

the feminine and the neuter, and the singular shall include the plural, and conversely.

28. Counterparts. This Agreement may be executed in two or more counterparts, each of which shall be deemed an original, but all of which shall together constitute one and the same instrument.

29. Joint and Several Obligations. Whenever Debtor comprises one or more persons or entities, the obligations and promises set forth herein shall be joint and several undertakings of each of the persons or entities executing this Agreement as Debtor, and Secured Party may proceed hereunder against any one or more of said persons or entities without waiving its right to proceed against any of the others.

[Remainder of Page Intentionally Left Blank]

IN WITNESS WHEREOF, the parties hereto have executed this Agreement as of the date first above written.

DEBTOR:

HEALTHCARE HOLDINGS, INC.,
a Nevada corporation

/s/ Andre C. Dimitriadis
By:______________________________________
Name: Andre C. Dimitriadis
Its: Chairman and Chief Executive Officer

/s/ Christopher T. Ishikawa
By:______________________________________
Name: Christopher T. Ishikawa
Its: President

SECURED PARTY:

LTC PROPERTIES, INC.,
a Maryland corporation

/s/ Wendy Simpson
By:______________________________________
Name: Wendy Simpson
Its: Vice Chairman and Chief Financial Officer

/s/ Alex Chavez
By:______________________________________
Name: Alex Chavez
Its: Sr. Vice President and Treasurer

LTC PROPERTIES, INC.

EXHIBIT 21.1

LIST OF SUBSIDIARIES

<TABLE>
<CAPTION>

Company	State of Organization	Company	State of Organization
<S>	<C>	<C>	<C>
Bakersfield-LTC, Inc.	Delaware	LTC-Fort Valley, Inc.	Delaware
BV Holding-LTC, Inc.	Delaware	LTC-Gardner, Inc.	Delaware
Coronado Corporation	Delaware	LTC-Griffin, Inc.	Nevada
Education Property Investors, Inc.	Nevada	LTC-Jessup, Inc.	Delaware
Emerald Gardens-LTC, Inc.	Delaware	LTC-Jonesboro, Inc.	Nevada
Florida-LTC, Inc.	Nevada	LTC-K1 Inc.	Delaware
Illinois-LTC, Inc.	Delaware	LTC-K2 Limited Partnership	Delaware
Kansas-LTC Corporation	Delaware	LTC-K2 LP, Inc.	Delaware
LTC Flower Square, Inc.	Arizona	LTC-K2, Inc.	Delaware
LTC GP I, Inc.	Delaware	LTC-New Mexico, Inc.	Nevada
LTC GP II, Inc.	Delaware	LTC-Ohio, Inc.	Delaware
LTC GP III, Inc.	Delaware	LTC-Richmond, Inc.	Nevada
LTC GP IV, Inc.	Delaware	LTC-Sumner, Inc.	Delaware
LTC GP V, Inc.	Delaware	LTC-Tampa, Inc.	Nevada
LTC GP VI, Inc.	Delaware	L-Tex GP, Inc.	Delaware
LTC Healthcare of Red Hills, Inc.	Delaware	L-Tex L.P. Corporation	Delaware
LTC Partners I, L.P.	Delaware	Magnolia-LTC, Inc.	Delaware
LTC Partners II, L.P.	Delaware	Missouri River Corporation	Delaware
LTC Partners III, L.P.	Delaware	North Carolina Real	
LTC Partners IV, L.P.	Delaware	Estate Investments, LLC	North Carolina
LTC Partners IX, L.P.	Delaware	Park Villa Corporation	Delaware
LTC Partners V, L.P.	Delaware	Texas-LTC Colonial Manor	
LTC Partners VI, L.P.	Delaware	Limited Partnership	Delaware
LTC Partners VII, L.P.	Delaware	Texas-LTC Limited Partnership	Texas
LTC Partners VIII, L.P.	Delaware	Texas-LTC Woodridge	
LTC REMIC Corporation	Delaware	Limited Partnership	Delaware
LTC REMIC IV Corporation	Delaware	University Park Convalescent Center, Inc.	Florida
LTC West, Inc.	Nevada	Vacaville-LTC, Inc.	Delaware
LTC-Dearfield, Inc.	Nevada	Virginia-LTC, Inc.	Nevada
LTC-DS, Inc.	Delaware	Western Healthcare Funding, Inc.	Nevada

</TABLE>

LTC PROPERTIES, INC.

EXHIBIT 23.1

CONSENT OF INDEPENDENT AUDITORS

We consent to the incorporation by reference in the Registration Statement (Form S-3 No. 333-2444) and in the Registration Statement (Form S-8 No. 33-85252) of LTC Properties, Inc. of our report dated January 25, 2002 with respect to the consolidated financial statements and schedules of LTC Properties, Inc., included in its Annual Report (Form 10-K) for the year ended December 31, 2001.

/s/ ERNST & YOUNG LLP

Los Angeles, California
March 8, 2002

LTC PROPERTIES, INC.

EXHIBIT 99

RISK FACTORS

You should carefully consider the risks described below before making an investment decision in our company. The risks and uncertainties described below are not the only ones facing our company and there may be additional risks that we do not presently know of or that we currently consider immaterial. All of these risks could adversely affect our business, financial condition, results of operations and cash flows. As a result, our ability to pay distributions on, and the market price of, our common stock may be adversely affected if any of such risks are realized.

In accordance with "plain English" guidelines provided by the Securities and Exchange Commission, whenever we refer to "our company" or to "us," or use the terms "we" or "our," we are referring to LTC Properties, Inc. and its subsidiaries.

Our Performance is Subject to Risks Associated with Health Care Real Estate Investment

There are Factors Outside of our Control that Affect the Performance and Value of our Real Estate. Real property investments in the health care industry are subject to varying degrees of risk. The economic performance and values of health care real estate can be affected by many factors including governmental regulation, economic conditions, and demand for health care services. We cannot assure that the value of any property acquired by us will appreciate or that the value of property securing any of our mortgage loans or any property acquired by us will not depreciate. Certain significant expenditures associated with an investment in real estate (such as mortgage payments, real estate taxes and maintenance costs) generally do not decline when circumstances cause a reduction in income from the property.

Income and Returns from Health Care Facilities Can be Volatile. The possibility that the health care facilities in which we invest will not generate income sufficient to meet operating expenses, will generate income and capital appreciation, if any, at rates lower than those anticipated or will yield returns lower than those available through investments in comparable real estate or other investments are additional risks of investing in health care related real estate. Income from properties and yields from investments in such properties may be affected by many factors, including changes in governmental regulation (such as zoning laws and government payment), general or local economic conditions (such as fluctuations in interest rates and employment conditions), the available local supply of and demand for improved real estate, a reduction in rental income as the result of an inability to maintain occupancy levels, natural disasters (such as earthquakes and floods) or similar factors.

Real Estate Investments are Illiquid. Real estate investments are relatively illiquid and, therefore, tend to limit our ability to vary our portfolio promptly in response to changes in economic or other conditions. All of our properties are "special purpose" properties that could not be readily converted to general residential, retail or office use. Transfers of operations of nursing homes and other health care-related facilities are subject to regulatory approvals not required for transfers of other types of commercial operations and other types of real estate. Thus, if the operation of any of our properties becomes unprofitable due to competition, age of improvements or other factors such that the borrower or lessee becomes unable to meet its obligations on the debt or lease, the liquidation value of the property may be substantially less than would be the case if the property were readily adaptable to other uses. The receipt of liquidation proceeds could be delayed by the approval process of any state agency necessary for the transfer of the property. In addition, certain significant expenditures associated with real estate investment (such as real estate taxes and maintenance costs) are generally not reduced when circumstances cause a reduction in income from the investment. If any of these events occur, our income and funds available for distribution would be adversely affected.

Some Potential Losses are not Covered by Insurance. We currently require, and we intend to continue to require, all borrowers of funds from us and lessees of any of our properties to secure adequate comprehensive property and general and professional liability insurance that covers us as well as the borrower and/or lessee. Recently, the cost of such insurance has increased substantially and some insurers have stopped offering such insurance for nursing homes. The unavailability and increased cost of such insurance could have a material adverse effect on the ability of the lessees and operators, including their ability to make lease or mortgage payments. In addition, certain risks may be uninsurable, not economically insurable or insurance is not available and there can be no assurance our Company, a borrower or a lessee will have adequate funds to cover all contingencies itself. Certain losses such as losses due to floods or seismic activity may be insured subject to certain limitations including large deductibles or co-payments and policy limits. If an uninsured loss or a loss in excess of insured limits occurs with respect to one or more of our properties, we could be subject to an adverse claim including claims for general or professional liability; lose the capital we invested in the properties, as well as the anticipated future revenue from the properties and, in the case of debt which is with recourse to us, we would remain obligated for any mortgage debt or other financial obligations related to the properties.

We Depend on Lease Income and Mortgage Payments from Real Property. Since a substantial portion of our income is derived from mortgage payments and lease income from real property, our income would be adversely affected if a significant number of our borrowers or lessees were unable to meet their obligations to us or if we were unable to lease our properties or make mortgage loans on economically favorable terms. There can be no assurance that any lessee will exercise its option to renew its lease upon the expiration of the initial term or that if such failure to renew were to occur, we could lease the property to others on favorable terms.

Our Borrowers and Lessees Face Competition in the Healthcare Industry.

The long-term care industry is highly competitive and we expect that it may become more competitive in the future. Our borrowers and lessees are competing with numerous other companies providing similar long-term care services or alternatives such as home health agencies, life care at home, community-based service programs, retirement communities and convalescent centers. There can be no assurance that our borrowers and lessees will not encounter increased competition in the future which could limit their ability to attract residents or expand their businesses and therefore affect their ability to make their debt or lease payments to us.

The Healthcare Industry is Heavily Regulated by the Government.

Our borrowers and lessees who operate health care facilities are subject to heavy regulation by federal, state and local governments. These laws and regulations are subject to frequent and substantial changes resulting from legislation, adoption of rules and regulations, and administrative and judicial interpretations of existing law. These changes may have a dramatic effect on the definition of permissible or impermissible activities, the relative costs associated with doing business and the amount of reimbursement by both government and other third-party payors. These changes may be applied retroactively. The ultimate timing or effect of these changes cannot be predicted. The failure of any borrower of funds from us or lessee of any of our properties to comply with such laws, requirements and regulations could affect its ability to operate its facility or facilities and could adversely affect such borrower's or lessee's ability to make debt or lease payments to us.

Our Borrowers and Lessees Rely on Government and Third Party Reimbursement. The ability of our borrowers and lessees to generate revenue and profit determines the underlying value of that facility to us. Revenues of our borrowers and lessees are generally derived from payments for patient care. Sources of such payments include the federal Medicare program, state Medicaid programs, private insurance carriers, health care service plans, health maintenance organizations, preferred provider arrangements, self-insured employers, as well as the patients themselves.

A significant portion of the revenue of our borrowers and lessees is derived from governmentally-funded reimbursement programs, such as Medicare and Medicaid. Because of significant health care costs paid by such government programs, both federal and state governments have adopted and continue to consider various health care reform proposals to control health care costs. In recent years, there have been fundamental changes in the Medicare program which resulted in reduced levels of payment for a substantial portion of health care services. In many instances, revenues from Medicaid programs are already insufficient to cover the actual costs incurred in providing care to those patients, and several states have reduced, or are considering reducing, nursing facility payment rates. Moreover, health care facilities have experienced increasing pressures from private payors attempting to control health care costs, and reimbursement from private payors has in many cases effectively been reduced to levels approaching those of government payors.

Governmental and public concern regarding health care costs may result in significant reductions in payment to health care facilities, and there can be no assurance that future payment rates for either governmental or private payors will be sufficient to cover cost increases in providing services to patients. Any changes in reimbursement policies which reduce reimbursement to levels that are insufficient to cover the cost of providing patient care could adversely affect revenues of our borrowers and lessees and thereby adversely affect those borrowers' and lessees' abilities to make their debt or lease payments to us. Failure of the borrowers or lessees to make their debt or lease payments would have a direct and material adverse impact on us.

Regulations Have Been Adopted to Eliminate Fraud and Abuse. There are various federal and state laws prohibiting fraud by health care providers, including criminal provisions which prohibit filing false claims or making false statements to receive payment or certification under Medicare and Medicaid, or failing to refund overpayments or improper payments. Violation of these federal provisions is a felony punishable by up to five years imprisonment and/or $25,000 fines. Civil provisions prohibit the knowing filing of a false claim or the knowing use of false statements to obtain payment. The penalties for such a violation are fines of not less than $5,500 nor more than $11,000, plus treble damages, for each claim filed.

There are also laws which govern referrals and financial relationships. The federal Anti-Kickback Law prohibits, among other things, the offer, payment, solicitation or receipt of any form of remuneration in return for, or to induce, the referral of Medicare and Medicaid patients. A wide array of relationships and arrangements, including ownership interests in a company by persons who refer or who are in a position to refer patients, as well as personal services agreements, have under certain circumstances, been alleged or been found to violate these provisions. In addition to the Anti-Kickback Statute, the federal government restricts certain financial relationships between physicians and other providers of health care services.

State and federal governments are devoting increasing attention and resources to anti-fraud initiatives against health care providers. The Health Insurance Portability and Accountability Act of 1996 ("HIPAA") and the Balanced Budget Act of 1997 expand the penalties for health care fraud, including broader provisions for the exclusion of providers from the Medicare and Medicaid programs.

Although HIPAA was intended ultimately to reduce administrative expenses and burdens faced within the health care industry, we believe the law could initially bring about significant and, in some cases, costly changes. HHS has released two rules to date mandating the use of new standards with respect to certain health care transactions and health information. The first rule requires the use of uniform standards for common health care transactions, including health care claims information, plan eligibility, referral certification and authorization, claims status, plan enrollment and disenrollment, payment and remittance advice, plan premium payments and coordination of benefits.

Second, HHS has released new standards relating to the privacy of individually identifiable health information. These standards not only require our operators' compliance with rules governing the use and disclosure of protected health information, but they also require entities to impose those rules, by contract, on any business

associate to whom such information is disclosed. Rules governing the security of health information have been proposed but not yet been issued in final form.

HHS finalized the new transaction standards on August 17, 2000, and covered entities, such as our operators, will be required to comply with them by October 16, 2002. Congress passed legislation in December 2001 that delays for one year (October 16, 2003) the compliance date, but only for entities that submit a compliance plan to HHS by the original implementation deadline. The privacy standards were issued on December 28, 2000, and, after certain delays, became effective April 14, 2001, with a compliance date of April 14, 2003. The Bush Administration and Congress are taking a careful look at the existing regulations, but it is uncertain whether there will be additional changes to the privacy standards or their compliance date. With respect to the security regulation, once they are issued in final form, affected parties will have approximately two years to be fully compliant. Sanctions for failing to comply with HIPAA include criminal and civil sanctions.

We believe the operators of our health care properties are aware of and should be evaluating the effect of HIPAA. We believe our operators cannot at this time estimate the cost of such compliance, nor estimate the cost of compliance with standards that have not yet been finalized. The new and proposed health information standards are likely to have a significant effect on the manner in which the operators of our health care properties handle health data and communicate with payors. However, based on our current knowledge, we cannot currently estimate the cost of compliance or if there will be a material adverse effect on our business, financial condition or results of operations as a result of our operators experiencing increased costs for compliance.

Based upon information we have periodically received from our operators over the terms of their respective leases and loans, we believe that the nursing facilities in which we have investments are in substantial compliance with the various regulatory requirements applicable to them, although there can be no assurance that the operators are in compliance or will remain in compliance in the future.

Congress Has Enacted Health Care Reform Measures. The health care industry is facing various challenges, including increased government and private payor pressure on health care providers to control costs. The pressure to control health care costs intensified during 1994 and 1995 as a result of the national health care reform debate and continues as Congress attempts to slow the rate of growth of federal health care expenditures as part of its effort to balance the federal budget.

The Balanced Budget Act enacted significant changes to the Medicare and Medicaid programs designed to "modernize" payment and health care delivery systems while achieving substantial budgetary savings. In seeking to limit Medicare reimbursement for long term care services; Congress established the prospective payment system for skilled nursing facility services to replace the cost-based reimbursement system. Skilled nursing facilities needed to restructure their operations to accommodate the new Medicare prospective payment system reimbursement. In part because of the uncertainty as to the effect of the prospective payment system on skilled nursing facilities, in November 1998, Standard & Poor's, an international rating agency that provides credit analysis and information through the rating of financial instruments, placed many skilled nursing facility companies on a "credit watch" because of the potential negative impact of the implementation of the prospective payment system on the financial condition of skilled nursing facilities, including the ability to make interest and principal payments on outstanding borrowings. Since that time, five publicly held operators of long-tem care facilities and one publicly held operator of assisted living facilities have filed for reorganization under Chapter 11 of the federal bankruptcy laws. As of February 28, 2002, only one long-term care operator and the assisted living operated have restructured their operations and/or debt and equity and emerged from bankruptcy. There can be no assurances given that 2002 and future years will not include additional bankruptcies of skilled nursing and assisted living operators. The growing popularity of long-term care insurance and an aging population, should add to demand for nursing home services. While the Balance Budget Refinement Act and the Benefits Improvement and Protection Act of 2000 contain provisions to mitigated to a certain extent, the effects of the Balanced Budget Act, these changes may be insufficient to address the negative impact of the prospective

payment system on some skilled nursing facilities and moreover, are scheduled to end in October 2002 and if Congress fails to act to extend these or enact comparable payment increases, skilled nursing facilities could experience significant losses in revenue.

In addition, there are numerous initiatives at the federal and state levels for comprehensive reforms affecting the payment for and availability of health care services. Congress and state legislatures can be expected to continue to review and assess alternative health care delivery systems and payment methodologies. Changes in the law, new interpretations of existing laws, or changes in payment methodology may have a dramatic effect on the definition of permissible or impermissible activities, the relative costs associated with doing business and the amount of reimbursement by the government and other third party payors.

In light of forthcoming regulations and continuing state Medicaid program reform, no assurance can be given that the implementation of such regulations and reform will not have a material adverse effect on our financial condition or results of operations.

Our Facilities are Subject to Licensing, Certification and Accreditation. In addition to the requirements to be met by skilled nursing facilities for participation in the Medicare and Medicaid programs, skilled nursing facilities are subject to regulatory and licensing requirements of federal, state and local authorities. The operator of each skilled nursing facility is licensed annually by the department of health or other applicable agency in each state. In granting and renewing licenses, regulatory agencies consider, among other things, the physical buildings and equipment, the qualifications of the administrative personnel and nursing staff, the quality of care and continuing compliance with the laws and regulations relating to the operation of the facilities. State licensing of facilities is a prerequisite to certification under the Medicare and Medicaid programs. In the ordinary course of business, the operators receive notices of deficiencies for failure to comply with various regulatory requirements and take appropriate corrective and preventive actions.

Failure to obtain licensure or loss of licensure would prevent a facility from operating. Failure to maintain certification in the Medicare and Medicaid programs would result in a loss of funding from those programs. Although accreditation is generally voluntary, loss of accreditation could result in a facility not meeting eligibility requirements to participate in various reimbursement programs. These events could adversely affect the facility operator's ability to make rent and debt payments.

In addition to licensing requirements, state and local laws may regulate expansion, including the addition of new beds or services or acquisition of medical equipment, and occasionally the contraction of health care facilities by requiring certificate of need or other similar approval programs. States vary in their utilization of these programs. In addition, health care facilities are subject to the Americans with Disabilities Act and building and safety codes which govern access, physical design requirements for facilities, and building standards.

Skilled Nursing Facilities. Skilled nursing facilities are regulated primarily through the state licensing and federal certification criteria established by federal law enacted as part of the Omnibus Budget Reconciliation Act of 1987. Regulatory authorities and licensing standards vary from state to state, and in some instances from locality to locality. These standards are constantly reviewed and revised. Agencies periodically inspect facilities, at which time deficiencies may be identified. The facilities must correct these deficiencies as a condition to continued licensing or certification and participation in government reimbursement programs, and may receive sanctions for noncompliance. Depending on the nature of such deficiencies, remedies can be routine or costly, and sanctions can be modest or severe, up to revocation of a facility's license or certification or closure of a facility. Similarly, compliance with regulations that cover a broad range of areas such as patients' rights, staff training, quality of life and quality of resident care may increase facility start-up and operating costs.

Assisted Living Facilities. Assisted living facilities are subject to certain state regulations and licensing requirements. To qualify as a state licensed facility, assisted living facilities must comply with regulations that address, among other things, staffing, physical design, required services and resident characteristics. Assisted living facilities are also subject to various local building codes and other ordinances, including fire safety codes.

These requirements vary from state to state and are monitored to varying degrees by state agencies. Failure to comply with these laws and regulations could result in the denial of reimbursement, the imposition of fines, and in extreme cases, the revocation of a facility's license or closure of a facility. Such actions may have an effect on the revenues of the borrowers and lessees of properties owned by us and therefore adversely impact our revenues.

Currently, assisted living facilities are not regulated as such by the federal government. State standards required for assisted living facility providers are less stringent than those required of other licensed health care operators. There can be no assurance that federal regulations governing the operation of assisted living facilities will not be implemented in the future or that existing state regulations will not be expanded. In addition, only certain states have adopted laws or regulations permitting individuals with higher acuity levels to remain in assisted living communities who may otherwise qualify for placement in a nursing facility. While only certain states presently provide for any Medicaid reimbursement for assisted living residences, several states are currently reviewing their policies and reimbursement programs to provide funding for assisted living residences. There can be no assurance that such states will adopt the Medicaid waiver program.

Environmental Problems Are Possible and Can Be Costly. Under various federal, state and local environmental laws, ordinances and regulations, an owner of real property or a secured lender (such as our company) may be liable for the costs of removal or remediation of hazardous or toxic substances at, under or disposed of in connection with such property, as well as other potential costs relating to hazardous or toxic substances (including government fines and damages for injuries to persons and adjacent property). Such laws often impose such liability without regard to whether the owner or secured lender knew of, or was responsible for, the presence or disposal of such substances and may be imposed on the owner or secured lender in connection with the activities of an operator of the property. The cost of any required remediation, removal, fines or personal or property damages and the owner's or secured lender's liability therefore could exceed the value of the property, and/or the assets of the owner or secured lender. In addition, the presence of such substances, or the failure to properly dispose of or remediate such substances, may adversely affect the owner's ability to sell or rent such property or to borrow using such property as collateral which, in turn, would reduce our revenues.

Although the mortgage loans that we provide and leases covering our properties require the borrower and the lessee to indemnify us for certain environmental liabilities, the scope of such obligations may be limited and we cannot assure that any such borrower or lessee would be able to fulfill its indemnification obligations.

We Rely on a Few Major Operators

As of December 31, 2001, Sun Healthcare Group, Inc. ("Sun") operated 15 facilities (13 leases and two loans) with 1,774 beds/units representing approximately 11.6%, or $68,239,000, of our "direct real estate investment portfolio" (properties that we own or on which we hold promissory notes secured by first mortgages). Additionally, at December 31, 2001, Sun operated eight skilled nursing facilities securing mortgage loans payable to REMIC pools originated by us. During 1999, Sun filed for reorganization under Chapter 11 of the Bankruptcy Code. As of December 31, 2001, Sun was operating its business as a debtor-in-possession subject to the jurisdiction of the Bankruptcy Court, however, Sun has received approval of its plan of reorganization and emerged from bankruptcy in February 2002. Concurrently, 13 leases with us were affirmed, additionally one of the leases related to a loan was affirmed and the other lease related to a loan was rejected.

Assisted Living Concepts, Inc. ("ALC") operates 37 assisted living facilities with a total of 1,434 units owned by us representing approximately 14.9%, or $88,105,000, of our direct real estate investment portfolio. In October 2001, ALC filed for reorganization under Chapter 11 of the federal bankruptcy laws. The filing was pre-negotiated with sufficient debt holders to allow ALC to reorganize its debt and equity and emerge from bankruptcy as of 12:01 a.m. on January 1, 2002. At the request of our Board of Directors, we agreed to

reduce total rents under the 37 leases by $875,000 a year, beginning January 1, 2002. The final order affirming the reorganization was made in December 2001, consequently we reflected the transactions as of December 31, 2001. Our Chairman, CEO and President, Mr. Andre C. Dimitriadis, became a Board Member of ALC as of January 1, 2002.

Alterra Healthcare Corporation ("Alterra") operates 35 assisted living facilities with a total of 1,416 units owned by us representing approximately 14.3%, or $84,194,000, of our direct real estate investment portfolio. Alterra has announced that it has engaged financial advisors to assist Alterra in a restructuring of its debt and equity. We cannot, at this time, predict or quantify what, if any, impact any ultimate restructuring could have on our company. As of March 2002, Alterra was current on all rents due us.

Sunwest Management, Inc. ("Sunwest") operates seven assisted living facilities with a total of 693 units owned by us representing approximately 10.5%, or $61,862,000, of our company's direct real estate investment portfolio.

As of December 31, 2001, 24 real estate properties with a total of 2,651 beds and a gross carrying value of $58,151,000 or 9.8% of our direct real estate investment portfolio were operated by CLC Healthcare, Inc. ("CLC"). Rents under these leases totaled approximately $3,148,000, annually. These leases were cancelled and replaced with new leases in January 2002 as described below.

Subsequent to December 31, 2001, the Company sold to an unrelated party two properties in Illinois operated by CLC. CLC will continue to operate these facilities until the new owner obtains a license and regulatory approval. Additionally, subsequent to December 31, 2001, the Company agreed to sell a wholly owned subsidiary, LTC-Fort Tucum, Inc. to CLC for a $500,000 note bearing no interest for one year and thereafter interest at 8% annually for two years. CLC has certain rights to extend the note at its maturity. LTC-Fort Tucum, now owned by CLC has acquired two skilled nursing facilities in New Mexico, previously operated by Integrated Health Services, Inc., in a deed-in-lieu of foreclosure transaction. These properties are financed with debt from a REMIC pool originated by the Company. CLC expects to begin operating the two facilities during the second quarter of 2002. Additionally, in January 2002, the Company acquired a skilled nursing facility in Texas operated by CLC through the assumption of a $1,357,000 mortgage loan payable to a REMIC pool originated by the Company and a cash payment of $505,000.

As a result of the subsequent events, the Company leases 23 facilities to CLC under individual six-year leases that provide for total rents of $3,000,000; $4,000,000; $4,750,000; $5,350,000; $5,900,000 and $6,500,000 respectively, in years 2002 through 2007. The leases contain two five-year renewal options with increases of 2% annually. These leases have cross default provisions and a provision for acceleration should there be a change of control, as defined in the lease, of CLC. Additionally, CLC owns and operates the two New Mexico facilities discussed above that are financed with mortgage loans payable to a REMIC pool originated by the Company.

All of these companies, except Sunwest, are publicly traded companies, and as such are subject to the filing requirements of the Securities and Exchange Commission. Our financial position and its ability to make distributions may be adversely affected by further financial difficulties experienced by ALC, Alterra, CLC and Sun, or financial difficulties experienced by Sunwest, or any of our other major operators, including additional bankruptcies, inability to emerge from bankruptcy, insolvency or general downturn in business of any such operator, or in the event any such operator does not renew and/or extend its relationship with us or our company's borrowers when it expires.

Third Parties That Operate Our Properties May Become Bankrupt

If third parties that operate properties we invest in become bankrupt, any investments we make in assets operating in workout modes or under Chapter 11 of the Bankruptcy Code could be subordinated or disallowed,

and we could be liable to third parties. Furthermore, if we receive any distributions relating to such investments, they could be recovered from us if the distribution is regarded as a fraudulent conveyance or preferential payment. Bankruptcy laws, including the automatic stay imposed upon the filing of a bankruptcy petition, may delay our ability to realize on collateral securing loans made by us or may adversely affect the priority of our loans through doctrines such as "equitable subordination" or may result in a restructure of the debt through principles such as the "cramdown" provisions of the bankruptcy laws.

We Invest in Mortgage Loans

Borrowers May be Unable to Make Debt Service Payments. We invest in mortgages. In general, investments in mortgages include the risks that borrowers may not be able to make debt service payments or pay principal when due, that the value of the mortgaged property may be less than the principal amount of the mortgage note secured by the property and that interest rates payable on the mortgages may be lower than our cost of funds to acquire these mortgages. In any of these events, our ability to make distributions on, and the market price of, our common stock could be adversely affected.

Our Remedies May Be Limited When Mortgage Loans Default. To the extent we invest in mortgage loans, such mortgage loans may or may not be recourse obligations of the borrower and generally will not be insured or guaranteed by governmental agencies or otherwise. In the event of a default under such obligations, we may have to foreclose on the property underlying the mortgage or protect our interest by acquiring title to a property and thereafter make substantial improvements or repairs in order to maximize the property's investment potential. Borrowers may contest enforcement of foreclosure or other remedies, seek bankruptcy protection against such enforcement and/or bring claims for lender liability in response to actions to enforce mortgage obligations. If a borrower seeks bankruptcy protection, the Bankruptcy Court may impose an automatic stay that would preclude us from enforcing foreclosure or other remedies against the borrower. Relatively high "loan to value" ratios and declines in the value of the property may prevent us from realizing an amount equal to our mortgage loan upon foreclosure.

There are Disadvantages to Investments in Commercial Mortgage Backed Securities

Investments in Commercial Mortgage Backed Securities are Subject to Real Estate Risks Relating to the Underlying Properties. We retain subordinated portions of the REMIC Certificates issued in our securitizations. These REMIC Certificates are a form of mortgage backed securities and as such, we are subject to the same risks associated with investing directly in the underlying mortgage loans. This is especially true in our case due to the nature of the collateral properties securing the underlying mortgages in our securitizations. All of these properties are special purpose facilities used for the delivery of long-term care services. Any risks associated with investing in these types of properties could impact the value of our investment in the REMIC Certificates we retain.

Investments in Commercial Mortgage-Backed Securities are Subject to Risks Associated with Prepayment of the Underlying Mortgages. As with many interest bearing mortgage-backed instruments, prepayments of the underlying mortgages may expose us to the risk that an equivalent rate of return is not available in the current market and that new investment of equivalent risk will have lower rates of return. Certain types of investments in commercial mortgage-backed securities may be interest-only securities which expose the holder to the risk that the underlying mortgages may prepay at a faster rate than anticipated at acquisition. Faster than anticipated prepayments may cause the investment in interest-only commercial mortgage-backed securities to have a lower than anticipated rate of return and could result in a loss of the initial investment under extreme prepayment scenarios.

Subordinated Securities may not be Repaid Upon Default. We invest in subordinated tranches of commercial mortgage backed securities (our retained REMIC Certificates). In general, subordinated tranches of commercial

mortgage backed securities are entitled to receive repayment of principal only after all principal payments have been made on more senior tranches and also have subordinated rights as to receipt of interest distributions. In addition, an active secondary market for such subordinated securities is not as well developed as the market for other mortgage backed securities. Accordingly, such subordinated commercial mortgage backed securities may have limited marketability and there can be no assurance that a more efficient secondary market will develop.

We may be Unable to Consummate Acquisitions, Leasings and Financings on Advantageous Terms Due in Part to Competition

Investments in health care facilities entail the risk that they will fail to perform in accordance with our expectations. Estimates of the costs of improvements necessary for us to bring an acquired property up to market standards may prove inaccurate. Further, we anticipate significant competition for attractive investment opportunities from other major health care facility investors with significant capital including other REITs, real estate partnerships, health care providers and other investors, including banks and insurance companies. We expect that future investments will be financed through a combination of borrowings and proceeds from equity or debt offerings by us, which could have an adverse effect on our cash flow. We may not be able to invest in additional facilities. Our inability to finance any future investments on favorable terms or the failure of investments to conform to our expectations or investment criteria could have a direct and adverse impact on us. Difficult capital market conditions in the health care industry have limited our access to traditional forms of growth capital. As a result of the tight capital markets in the health care industry, we reduced our investment activity in 2001 and 2000 and intend to limit our investment activity in 2002.

We are Subject to Risks and Liabilities in Connection with Properties Owned Through Limited Liability Companies and Partnerships

We have ownership interests in limited liability companies and/or partnerships. We may make additional investments through these ventures in the future. Partnership or limited liability company investments may involve risks such as the following:

- our partners or co-members might become bankrupt (in which event we and any other remaining general partners or members would generally remain liable for the liabilities of the partnership or limited liability company);

- our partners or co-members might at any time have economic or other business interests or goals which are inconsistent with our business interests or goals;

- our partners or co-members may be in a position to take action contrary to our instructions, requests, policies or objectives, including our policy with respect to maintaining our qualification as a REIT; and

- agreements governing limited liability companies and partnerships often contain restrictions on the transfer of a member's or partner's interest or "buy-sell" or other provisions which may result in a purchase or sale of the interest at a disadvantageous time or on disadvantageous terms.

We will, however, generally seek to maintain sufficient control of our partnerships and limited liability companies to permit us to achieve our business objectives. Our organizational documents do not limit the amount of available funds that we may invest in partnerships or limited liability companies. The occurrence of one or more of the events described above could have a direct and adverse impact on us.

We Could Incur More Debt

We operate with a policy of incurring debt when, in the opinion of our directors, it is advisable. Accordingly, we could become more highly leveraged. The degree of leverage could have important consequences to stockholders, including affecting our ability to obtain additional financing in the future for working capital, capital expenditures, acquisitions, development or other general corporate purposes and making us more vulnerable to a downturn in business or the economy generally.

Debt Financing, Financial Covenants, Degree of Leverage and Increases in Interest Rates Could Adversely Affect Our Economic Performance

Scheduled Debt Payments Could Adversely Affect Our Financial Condition. We are subject to risks normally associated with debt financing, including the risks that our cash flow will be insufficient to make distributions to our stockholders, that we will be unable to refinance existing indebtedness on our properties (which in all cases will not have been fully amortized at maturity) and that the terms of refinancing will not be as favorable as the terms of existing indebtedness.

As of December 31, 2001, we had total debt outstanding of approximately $284,634,000 including:

- $104,000,000 outstanding under our Senior Secured Credit Facility with a maturity date of October 2, 2004 and a current interest rate of LIBOR plus 2.25%;

- $2,408,000 aggregate principal amount of convertible subordinated debentures with a maturity in January 2002 and an interest rate of 7.75%;

- $15,994,000 aggregate principal amount of capital leases and tax exempt revenue bonds with various maturities through 2025 and a weighted average interest rate of 7.2%;

. $162,232,000 aggregate principal amount of mortgage loans with various maturities ranging from 2002 through 2028 and a weighted average interest rate of 9.4%.

If we are unable to refinance or extend principal payments due at maturity or pay them with proceeds of other capital transactions, we expect that our cash flow will not be sufficient in all years to pay distributions to our stockholders and to repay all such maturing debt. Furthermore, if prevailing interest rates or other factors at the time of refinancing (such as the reluctance of lenders to make commercial real estate loans) result in higher interest rates upon refinancing, the interest expense relating to that refinanced indebtedness would increase. This increased interest expense would adversely affect our financial condition and results of operations.

Rising Interest Rates Could Adversely Affect Our Cash Flow. As of December 31, 2001, we had $104,000,000 outstanding under a variable rate line of credit. In addition, we may incur other variable rate indebtedness in the future. Increases in interest rates on this indebtedness could increase our interest expense, which would adversely affect our financial condition and results of operations.

We Are Dependent on External Sources of Capital. In order to qualify as a REIT under the Internal Revenue Code, we are required each year to distribute to our stockholders at least 90% (95% for years ending Prior to January 1, 2001) of our REIT taxable income (determined without regard to the dividends-paid deduction and by excluding any net capital gain). Because of this distribution requirement, we may not be able to fund all future capital needs, including capital needs in connection with acquisitions, from cash retained from operations. As a result, to fund capital needs, we rely on third-party sources of capital, which we may not be able to obtain on favorable terms or at all. Our access to third-party sources of capital depends upon a number of factors, including general market conditions and the market's perception of our growth potential and our current and potential future earnings and cash distributions and the market price of the shares of our capital stock. Additional debt financing may substantially increase our leverage.

Financial Covenants Could Adversely Affect our Financial Condition. If a property is mortgaged to secure payment of indebtedness and we are unable to meet mortgage payments, the mortgagee could foreclose on the property, resulting in loss of income and asset value. The mortgages on our properties contain customary negative covenants which, among other things, limit our ability, without the prior consent of the lender, to further mortgage the property, to enter into new leases or materially modify existing leases, and to discontinue insurance coverage. In addition, our line of credit contains customary restrictions, requirements and other limitations on our ability to incur indebtedness, including maximum leverage ratios, minimum debt-service coverage ratios, cash flow coverage ratios and minimum consolidated tangible net worth. Foreclosure on mortgaged properties or an inability to refinance existing indebtedness would likely have a negative impact on our financial condition and results of operations.

We Could Default on Cross-Defaulted Debt. Our line of credit contains a cross-default provision which are triggered in the event that our other material indebtedness is in default. This cross-default provision may require us to repay or restructure the line of credit in addition to any mortgage or other debt which is in default, which could adversely affect our financial condition and results of operations.

Our Hedging Policies Involve Risks of Unanticipated Movements in Interest Rates

In connection with our line of credit, we have, in the past, employed hedging techniques designed to protect us against adverse movements in interest rates. While we may benefit from the use of these hedging mechanisms generally, unanticipated changes in interest rates, securities prices, or currency exchange rates may result in a poorer overall performance for us than if it had not entered into such hedging transactions. As of December 31, 2001, we do not have any outstanding hedging agreements.

Conflicts of Interest

Some of our Executive Officers and Board Members are also Executive Officers and Board Members of CLC Healthcare, Inc.

. Andre C. Dimitriadis, who is currently our Chairman, President and Chief Executive Officer serves in the same positions with CLC Healthcare, Inc., a Nevada corporation ("CLC"); and

. Wendy L. Simpson, who is currently our Vice Chairman and Chief Financial Officer serves as a Board Member, Executive Vice President and Chief Financial Officer with CLC; and

. Christopher T. Ishikawa, who is currently our Executive Vice President and Chief Investment Officer serves as a Board member and President and

Chief Operating Officer with CLC; and

. Julia L. Kopta, who is currently our Executive Vice President and General Counsel and Corporate Secretary serves as Executive Vice President, General Counsel and Corporate Secretary with CLC; and

CLC engages in the following activities: (1) operation of long-term care facilities; (2) development of long-term care properties, and (3) ownership of equity and debt investments in long-term care companies. Although none of the members of our management is committed to spending a particular amount of time on CLC's affairs, each of the members of management spend time on CLC's affairs. The continued involvement in CLC by some of our executive officers and directors could divert management's attention from our day-to-day operations.

Conflicts of Interest May Arise in Interpretations of Intercompany Agreements Between our Company and CLC. Because our management is largely the same as CLC's management, conflicts may arise with respect to the operation and effect of our intercompany agreements and relationships which could have an adverse effect on us if not properly resolved. More specifically, overlapping members of the board of directors and senior management of both companies may be presented with conflicts of interest with respect to matters affecting us and CLC, such as the determination of which company may take advantage of potential business opportunities, decisions concerning the business focus of each company (including decisions concerning the types of properties and geographic locations in which such companies make investments), potential competition between the business activities conducted, or sought to be conducted, by such companies (including competition for properties and tenants), possible corporate transactions (such as acquisitions), and other strategic decisions affecting the future of such companies. Conflicts also may arise with respect to the restriction on CLC's right to engage in activities or make investments that involve real estate unless we were first offered the opportunity and declined to pursue such activities or investments. We have adopted procedures to be followed by our Board of Directors and the Board of Directors of CLC to address potential conflicts. Such procedures include the requirement that the persons serving as directors of both companies abstain from voting as directors with respect to matters that present a significant conflict of interest between the companies.

If We Issue Additional Equity Securities, the Investment of Existing Stockholders Will be Diluted

We may from time to time raise additional capital from the issuance and sale of equity securities. Any such issuances may significantly dilute the interests of the existing holders of our securities, including our common stock.

Limitations in Our Charter and Bylaws Could Prevent a Change in Control

Our Charter and Bylaws contain provisions that may delay, defer or prevent a change in control or other transaction that could provide the holders of our common stock with the opportunity to realize a premium over the then-prevailing market price for our common stock. To maintain our qualification as a REIT for federal income tax purposes:

. Not more than 50% in value of our outstanding stock may be owned, actually or constructively, by five or fewer individuals (as defined in the Internal Revenue Code to include certain entities) during the last half of a taxable year after the first taxable year for which a REIT election is made.

. After the first taxable year for which a REIT election is made, our common stock must be held by a minimum of 100 persons for at least 335 days of a 12-month taxable year (or a proportionate part of a taxable year of less than 12 months).

. If we, or an owner of 10% or more of our stock, actually or constructively owns 10% or more of one of our tenants (or a tenant of any partnership in which we are a partner), the rent received by us (either directly or through any such partnership) from that tenant will not be qualifying income for purposes of the REIT gross income tests of the Internal Revenue Code.

In order to protect us against the risk of losing our REIT status for federal income tax purposes, we prohibit the ownership (actually or by virtue of application of certain constructive ownership provisions of the Internal Revenue Code) by any single person of more than 9.8% (by value or number of shares, whichever is more restrictive) of the issued and outstanding shares of our common stock and more than 9.8% (by value or number of shares, whichever is more restrictive) of the issued and outstanding shares of each class of our preferred stock by any single person so that no such person, taking into account all of our stock so owned by such person, may own in excess of 9.8% of our issued and outstanding capital stock. We refer to this limitation as the "ownership limit." We will redeem shares acquired or held in excess of the ownership limit. In addition, any acquisition of our common stock or preferred stock that would result in our disqualification as a REIT is null and void. The ownership limit may have the effect of delaying, deferring or preventing a change in control and, therefore, could adversely affect our stockholders' ability to realize a premium over the then-prevailing market price for the shares of our common stock in connection with such transaction. The Board of Directors has waived the ownership limit applicable to our common stock with respect to National Health Investors, Inc., allowing it to own greater than 9.8% of our outstanding shares of Series C Preferred Stock.

Our Charter authorizes us to issue additional shares of common stock and one or more series of preferred stock and to establish the preferences, rights and other terms of any series of preferred stock that we issue. Although our Board of Directors has no intention to do so at the present time, it could establish a series of preferred stock that could delay, defer or prevent a transaction or a change in control that might involve a premium price for our common stock or otherwise be in the best interests of our stockholders.

Our Charter, our Bylaws and Maryland law also contain other provisions that may delay, defer or prevent a transaction, including a change in control, that might involve payment of a premium price for our common stock or otherwise be in the best interests of our stockholders. Those provisions include the following:

- the provision in our Bylaws requiring a two-thirds vote of stockholders for any amendment of our Bylaws;

- the requirement in the Bylaws that the request of the holders of 25% or more of our common stock is necessary for stockholders to call a special meeting;

- the requirement of Maryland law that stockholders may only take action by written consent with the unanimous approval of all stockholders entitled to vote on the matter in question; and

- the requirement in the Bylaws of advance notice by stockholders for the nomination of directors or proposal of business to be considered at a meeting of stockholders.

These provisions may impede various actions by stockholders without approval of our Board of Directors, which in turn may delay, defer or prevent a transaction involving a change of control.

In addition, in May 2000 we adopted a Rights Plan to protect stockholders from coercive or otherwise unfair takeover tactics. In general terms, the plan works by imposing significant penalties upon any person or group of persons which acquires 15% or more of our common stock without the approval of our Board of Directors.

We Could Change Our Investment and Financing Policies without a Vote of Stockholders

Subject to our fundamental investment policy to maintain our qualification as a REIT (unless a change is approved by the Board of Directors under certain circumstances), the Board of Directors will determine our investment and financing policies, our growth strategy and our debt, capitalization, distribution and operating policies. Although the Board of Directors has no present intention to revise or amend these strategies and policies, the Board of Directors may do so at any time without a vote of stockholders. Accordingly, stockholders will have no control over changes in our strategies and policies (other than through the election of directors), and any such changes may not serve the interests of all stockholders and could adversely affect our financial condition or results of operations, including our ability to distribute cash to stockholders.

Various Market Conditions Affect the Price of Our Common Stock

As with other publicly-traded equity securities, the market price of our common stock will depend upon various market conditions, which may change from time to time. Among the market conditions that may affect the market price of our common stock are the following:

- the extent of investor interest in us;

- the general reputation of REITs and the attractiveness of their equity securities in comparison to other equity securities (including securities issued by other real estate-based companies);

- our financial performance and that of our operators;

. the contents of analyst reports regarding us and the REIT industry; and

. general stock and bond market conditions, including changes in interest rates on fixed income securities which may lead prospective purchasers of our common stock to demand a higher annual yield from future distributions. Such an increase in the required yield from distributions may adversely affect the market price of our common stock.

Other factors such as governmental regulatory action and changes in tax laws could also have a significant impact on the future market price of our common stock.

Earnings and Cash Distributions, Asset Value and Market Interest Rates Affect the Price of Our Common Stock

The market value of the equity securities of a REIT generally is based primarily upon the market's perception of the REIT's growth potential and its current and potential future earnings and cash distributions, and is based secondarily upon the real estate market value of the underlying assets. For that reason, shares of our common stock may trade at prices that are higher or lower than the net asset value per share. To the extent we retain operating cash flow for investment purposes, working capital reserves or other purposes, these retained funds, while increasing the value of our underlying assets, may not correspondingly increase the market price of our common stock. Our failure to meet the market's expectation with regard to future earnings and cash distributions likely would adversely affect the market price of our common stock. Another factor that may influence the price of our common stock will be the distribution yield on our common stock (as a percentage of the price of our common stock) relative to market interest rates. An increase in market interest rates might lead prospective purchasers of our common stock to expect a higher distribution yield, which would adversely affect the market price of our common stock. If the market price of our common stock declines significantly, we might breach covenants with respect to debt obligations, which might adversely affect our liquidity and our ability to make future acquisitions and pay distributions to our stockholders.

There are Federal Income Tax Risks Associated with a REIT

Our Failure to Qualify as a REIT Would Have Serious Adverse Consequences to Our Stockholders. We intend to operate so as to qualify as a REIT under the Internal Revenue Code. We believe that we have been organized and have operated in a manner which would allow us to qualify as a REIT under the Internal Revenue Code beginning with our taxable year ended December 31, 1992. However, it is possible that we have been organized or have operated in a manner which would not allow us to qualify as a REIT, or that our future operations could cause us to fail to qualify. Qualification as a REIT requires us to satisfy numerous requirements (some on an annual and quarterly basis) established under highly technical and complex Code provisions for which there are only limited judicial and administrative interpretations, and involves the determination of various factual matters and circumstances not entirely within our control. For example, in

order to qualify as a REIT, at least 95% of our gross income in any year must be derived from qualifying sources, and we must pay dividends to stockholders aggregating annually at least 90% (95% for taxable years ending prior to January 1, 2001) of our REIT taxable income (determined without regard to the dividends paid deduction and by excluding capital gains). Legislation, new regulations, administrative interpretations or court decisions could significantly change the tax laws with respect to qualification as a REIT or the federal income tax consequences of such qualification. However, we are not aware of any pending tax legislation that would adversely affect our ability to operate as a REIT.

If we fail to qualify as a REIT in any taxable year, we will be subject to federal income tax (including any applicable alternative minimum tax) on our taxable income at regular corporate rates. Unless we are entitled to relief under statutory provisions, we would be disqualified from treatment as a REIT for the four taxable years following the year during which we lost qualification. If we lose our REIT status, our net earnings available for investment or distribution to stockholders would be significantly reduced for each of the years involved. In addition, we would no longer be required to make distributions to stockholders.

We Pay Some Taxes. Even if we qualify as a REIT, we are subject to certain federal, state and local taxes on our income and property.

We are Dependent on our Key Personnel

We depend on the efforts of our executive officers, particularly Mr. Dimitriadis, Ms. Simpson, Mr. Ishikawa and Ms. Kopta. While we believe that we could find suitable replacements for these key personnel, the loss of their services or the limitation of their availability could have an adverse impact on our operations. Although we have entered into employment agreements with our executive officers, these employment agreements may not assure their continued service.