

CareTrust REIT, Inc.  
Form 10-Q  
August 10, 2015  
Table of Contents

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

FORM 10-Q

(Mark One)

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

For the quarterly period ended June 30, 2015

OR

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

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

Commission File Number: 001-36181

CareTrust REIT, Inc.  
(Exact name of registrant as specified in its charter)

Maryland 46-3999490  
(State or other jurisdiction of (I.R.S. Employer  
incorporation or organization) Identification No.)

905 Calle Amanecer, Suite 300, San Clemente, CA 92673  
(Address of principal executive offices) (Zip Code)  
(949) 542-3130  
(Registrant’s telephone number, including area code)

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

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

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

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

Edgar Filing: CareTrust REIT, Inc. - Form 10-Q

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

At August 7, 2015, there were 31,811,409 shares of common stock outstanding.

---

#### EXPLANATORY NOTE

This report represents the Quarterly Report on Form 10-Q for the quarterly period ended June 30, 2015 for CareTrust REIT, Inc. (“CareTrust” or the “Company”). Prior to June 1, 2014, CareTrust was a wholly owned subsidiary of The Ensign Group, Inc. (“Ensign”). On June 1, 2014, Ensign completed the separation of its healthcare business and its real estate business into two separate and independent publicly traded companies through the distribution of all of the outstanding shares of common stock of CareTrust to Ensign stockholders on a pro rata basis (the “Spin-Off”). Ensign stockholders received one share of CareTrust common stock for each share of Ensign common stock held at the close of business on May 22, 2014, the record date for the Spin-Off. The Spin-Off was effective from and after June 1, 2014, with shares of CareTrust common stock distributed by Ensign on June 2, 2014.

The Company was formed on October 29, 2013 and had minimal activity prior to the Spin-Off. The condensed consolidated and combined financial statements included in this report reflect, for all periods presented, the historical financial position, results of operations and cash flows of (i) the skilled nursing, assisted living and independent living facilities that Ensign contributed to the Company immediately prior to the Spin-Off and (ii) the operations of the three independent living facilities that the Company operated immediately following the Spin-Off. The condensed consolidated and combined financial statements included in this report also reflect the new investments that the Company has made after the Spin-Off. “Ensign Properties” is the predecessor of the Company, and its historical financial statements, for the periods prior to the Spin-Off, have been prepared on a “carve-out” basis from Ensign’s consolidated financial statements using the historical results of operations, cash flows, assets and liabilities attributable to such skilled nursing, assisted living and independent living facilities, and include allocations of income, expenses, assets and liabilities from Ensign. These allocations reflect significant assumptions. Although management of the Company believes such assumptions are reasonable, the condensed consolidated and combined financial statements do not fully reflect what the Company’s financial position, results of operations and cash flows would have been had it been a stand-alone company during the period ended June 30, 2014. As a result, historical financial information is not necessarily indicative of the Company’s future results of operations, financial position and cash flows.

Effective May 15, 2014, the Company became subject to the informational requirements of the Securities Exchange Act of 1934, as amended (the “Exchange Act”), and will file annual, quarterly and current reports, proxy statements and other information with the Securities and Exchange Commission (the “SEC”). These reports and other information filed by the Company may be read and copied at the Public Reference Room of the SEC, 100 F Street N.E., Washington, D.C. 20549. Information about the Public Reference Room may be obtained by calling the SEC at 1-800-SEC-0330. The SEC also maintains an internet site that contains reports, and other information about issuers, like the Company, which file electronically with the SEC. The address of that site is <http://www.sec.gov>. The Company makes available its reports on Form 10-K, 10-Q, and 8-K (as well as all amendments to these reports), and other information, free of charge, at the Investor Relations section of its website at [www.caretrustreit.com](http://www.caretrustreit.com). The information found on, or otherwise accessible through, the Company’s website is not incorporated by reference into, nor does it form a part of, this report or any other document that we file with the SEC.

---

Table of Contents

INDEX

PART I—FINANCIAL INFORMATION

Item 1.	<u>Financial Statements</u>	
	<u>Condensed Consolidated Balance Sheets</u>	<u>1</u>
	<u>Condensed Consolidated and Combined Statements of Operations</u>	<u>2</u>
	<u>Condensed Consolidated and Combined Statements of Comprehensive Income (Loss)</u>	<u>3</u>
	<u>Condensed Consolidated and Combined Statements of Equity</u>	<u>4</u>
	<u>Condensed Consolidated and Combined Statements of Cash Flows</u>	<u>5</u>
	<u>Notes to Condensed Consolidated and Combined Financial Statements</u>	<u>6</u>
Item 2.	<u>Management’s Discussion and Analysis of Financial Condition and Results of Operations</u>	<u>29</u>
Item 3.	<u>Quantitative and Qualitative Disclosures About Market Risk</u>	<u>36</u>
Item 4.	<u>Controls and Procedures</u>	<u>36</u>

PART II—OTHER INFORMATION

Item 1.	<u>Legal Proceedings</u>	<u>37</u>
Item 1A.	<u>Risk Factors</u>	<u>37</u>
Item 6.	<u>Exhibits</u>	<u>37</u>
	<u>Signatures</u>	<u>39</u>

---

Table of Contents

## PART I—FINANCIAL INFORMATION

## Item 1. Financial Statements.

## CARETRUST REIT, INC.

## CONDENSED CONSOLIDATED BALANCE SHEETS

(in thousands, except share and per share amounts)

(unaudited)

	June 30, 2015	December 31, 2014
Assets:		
Real estate investments, net	\$459,515	\$436,215
Other real estate investments	7,987	7,532
Cash and cash equivalents	29,904	25,320
Accounts receivable (related party receivables of \$0 at June 30, 2015 and \$2,275 at December 31, 2014)	2,036	2,291
Prepaid expenses and other assets	2,292	809
Deferred financing costs, net	9,442	10,405
Total assets	\$511,176	\$482,572
Liabilities and Equity:		
Senior unsecured notes payable	\$260,000	\$260,000
Mortgage notes payable	96,854	98,205
Secured revolving credit facility	35,000	—
Accounts payable and accrued liabilities	5,946	6,959
Dividends payable	5,090	3,946
Total liabilities	402,890	369,110
Commitments and contingencies (Note 11)		
Equity:		
Preferred stock, \$0.01 par value; 100,000,000 shares authorized, no shares issued and outstanding as of June 30, 2015 and December 31, 2014	—	—
Common stock, \$0.01 par value; 500,000,000 shares authorized, 31,306,782 and 31,251,157 shares issued and outstanding as of June 30, 2015 and December 31, 2014, respectively	313	313
Additional paid-in capital	246,701	246,041
Cumulative distributions in excess of earnings	(138,728)	(132,892)
Total equity	108,286	113,462
Total liabilities and equity	\$511,176	\$482,572
See accompanying notes to condensed consolidated and combined financial statements.		

Table of Contents

## CARETRUST REIT, INC.

## CONDENSED CONSOLIDATED AND COMBINED STATEMENTS OF OPERATIONS

(in thousands, except per share amounts)

(unaudited)

	For the Three Months Ended		For the Six Months Ended June	
	June 30,		30,	
	2015	2014	2015	2014
Revenues:				
Rental income (related party rental income of \$2,308 and \$4,667 for the three months ended June 30, 2015 and 2014, respectively and \$16,308 and \$4,667 for the six months ended June 30, 2015 and 2014, respectively – Note 6)	\$15,249	\$12,205	\$30,091	\$23,228
Tenant reimbursements (related party tenant reimbursements of \$200 and \$396 for the three months ended June 30, 2015 and 2014, respectively and \$1,406 and \$396 for the six months ended June 30, 2015 and 2014, respectively – Note 6)	1,288	1,237	2,546	2,498
Independent living facilities	607	623	1,242	1,210
Interest and other income	232	—	455	—
Total revenues	17,376	14,065	34,334	26,936
Expenses:				
Depreciation and amortization	5,679	6,070	11,278	12,269
Interest expense	5,989	6,452	11,890	9,779
Loss on extinguishment of debt	—	4,067	—	4,067
Property taxes	1,288	1,237	2,546	2,498
Independent living facilities	566	555	1,168	1,098
General and administrative	1,588	6,009	3,148	7,912
Total expenses	15,110	24,390	30,030	37,623
Income (loss) before provision for income taxes	2,266	(10,325)	4,304	(10,687)
Provision for income taxes	—	17	—	53
Net income (loss)	\$2,266	\$(10,342)	\$4,304	\$(10,740)
Earnings (loss) per common share:				
Basic	\$0.07	\$(0.47)	\$0.13	\$(0.48)
Diluted	\$0.07	\$(0.47)	\$0.13	\$(0.48)
Weighted-average number of common shares:				
Basic	31,278	22,231	31,268	22,230
Diluted	31,278	22,231	31,268	22,230
Dividends declared per common share	\$0.16	\$—	\$0.32	\$—

See accompanying notes to condensed consolidated and combined financial statements.

Table of Contents

CARETRUST REIT, INC.

CONDENSED CONSOLIDATED AND COMBINED STATEMENTS OF COMPREHENSIVE INCOME (LOSS)

(in thousands)

(unaudited)

	For the Three Months Ended		For the Six Months Ended June	
	June 30,		30,	
	2015	2014	2015	2014
Net income (loss)	\$2,266	\$(10,342	) \$4,304	\$(10,740 )
Other comprehensive income (loss):				
Unrealized (loss) gain on interest rate swap	—	(30	) —	167
Reclassification adjustment on interest rate swap	—	1,661	—	1,661
Comprehensive income (loss)	\$2,266	\$(8,711	) \$4,304	\$(8,912 )

See accompanying notes to condensed consolidated and combined financial statements.

Table of Contents

## CARETRUST REIT, INC.

## CONDENSED CONSOLIDATED AND COMBINED STATEMENTS OF EQUITY

(in thousands, except share and per share amounts)

(unaudited)

	Common Stock		Additional Paid-in Capital	Cumulative Distributions in Excess of Earnings	Invested Equity	Accumulated Other Comprehensive Loss	Total Equity
	Shares	Amount					
Balance at December 31, 2013	1,000	\$—	\$—	\$—	\$164,517	\$(1,828)	\$162,689
Net capital contribution from Ensign	—	—	—	—	4,356	—	4,356
Unrealized gain on interest rate swap	—	—	—	—	—	167	167
Reclassification adjustment on interest rate swap	—	—	—	—	—	1,661	1,661
Net capital distribution to Ensign	—	—	—	—	(10,475)	—	(10,475)
Reclassification of invested equity to common stock and additional paid-in capital in conjunction with the Spin-Off (Note 1)	22,227,358	222	146,980	—	(147,202)	—	—
Vesting of restricted common stock	48,550	1	(1)	—	—	—	—
Amortization of stock-based compensation	—	—	154	—	—	—	154
Special dividend at \$5.88 per share	8,974,249	90	98,908	(131,999)	—	—	(33,001)
Common dividend at \$0.125 per share	—	—	—	(3,946)	—	—	(3,946)
Net income (loss)	—	—	—	3,053	(11,196)	—	(8,143)
Balance at December 31, 2014	31,251,157	313	246,041	(132,892)	—	—	113,462
Vesting of restricted common stock	55,625	—	—	—	—	—	—
Amortization of stock-based compensation	—	—	660	—	—	—	660
Common dividends (\$0.32 per share)	—	—	—	(10,140)	—	—	(10,140)
Net income	—	—	—	4,304	—	—	4,304
Balance at June 30, 2015	31,306,782	\$313	\$246,701	\$(138,728)	\$—	\$—	\$108,286

See accompanying notes to condensed consolidated and combined financial statements.





Table of Contents

## CARETRUST REIT, INC.

## CONDENSED CONSOLIDATED AND COMBINED STATEMENTS OF CASH FLOWS

(in thousands)

(unaudited)

	For the Six Months Ended June	
	30,	
	2015	2014
Cash flows from operating activities:		
Net income (loss)	\$4,304	\$(10,740 )
Adjustments to reconcile net income (loss) to net cash provided by operating activities:		
Depreciation and amortization	11,278	12,269
Amortization of deferred financing costs and debt discount	1,102	517
Amortization of stock-based compensation	660	—
Noncash interest income adjustments	(455 )	—
Loss on extinguishment of debt	—	1,998
Loss on settlement of interest rate swap	—	1,661
Change in operating assets and liabilities:		
Accounts receivable	(2,020 )	(3 )
Accounts receivable due from related party	2,275	(1,848 )
Prepaid expenses and other assets	(545 )	677
Interest rate swap	—	(1,661 )
Accounts payable and accrued liabilities	(1,013 )	4,683
Net cash provided by operating activities	15,586	7,553
Cash flows from investing activities:		
Acquisition of real estate	(33,646 )	—
Improvements to real estate	(143 )	—
Purchases of equipment, furniture and fixtures	(227 )	(19,009 )
Escrow deposit for acquisition of real estate	(1,500 )	—
Net cash used in investing activities	(35,516 )	(19,009 )
Cash flows from financing activities:		
Proceeds from the issuance of senior unsecured notes payable	—	260,000
Borrowings under senior secured revolving credit facility	35,000	10,000
Proceeds from the issuance of mortgage notes payable	—	50,676
Repayments of borrowings under senior secured revolving credit facility	—	(88,701 )
Payments on the mortgage notes payable	(1,351 )	(66,856 )
Payments on senior secured term loan	—	(65,624 )
Payments of deferred financing costs	(139 )	(12,945 )
Dividends paid on common stock	(8,996 )	—
Net contribution from Ensign (Note 6)	—	4,356
Net cash provided by financing activities	24,514	90,906
Net increase in cash and cash equivalents	4,584	79,450
Cash and cash equivalents beginning of period	25,320	895
Cash and cash equivalents end of period	\$29,904	\$80,345
Supplemental disclosures of cash flow information:		
Interest paid	\$10,800	\$6,414
Income taxes paid	\$—	\$104
Supplemental schedule of noncash operating, investing and financing activities:		
Increase in dividends payable	\$1,144	\$—

Edgar Filing: CareTrust REIT, Inc. - Form 10-Q

Application of escrow deposit to acquisition of real estate	\$500	\$—
Operating assets and liabilities that were not transferred to CareTrust	\$—	\$1,042
Equipment, furniture and fixtures that were not transferred to CareTrust	\$—	\$(11,684 )
Net capital distribution to Ensign	\$—	\$10,475

See accompanying notes to condensed consolidated and combined financial statements.

5

---

Table of Contents

CARETRUST REIT, INC.

NOTES TO CONDENSED CONSOLIDATED AND COMBINED FINANCIAL STATEMENTS —

(Unaudited)

## 1. ORGANIZATION

Separation from Ensign—Prior to June 1, 2014, CareTrust REIT, Inc. (“CareTrust” or the “Company”) was a wholly owned subsidiary of The Ensign Group, Inc. (“Ensign”). On June 1, 2014, Ensign completed the separation of its healthcare business and its real estate business into two separate and independent publicly traded companies through the distribution of all of the outstanding shares of common stock of CareTrust to Ensign stockholders on a pro rata basis (the “Spin-Off”). Ensign stockholders received one share of CareTrust common stock for each share of Ensign common stock held at the close of business on May 22, 2014, the record date for the Spin-Off. The Spin-Off was effective from and after June 1, 2014, with shares of CareTrust common stock distributed by Ensign on June 2, 2014. The Company was formed on October 29, 2013 and had minimal activity prior to the Spin-Off.

Prior to the Spin-Off, the Company and Ensign entered into a Separation and Distribution Agreement, setting forth the mechanics of the Spin-Off, certain organizational matters and other ongoing obligations of the Company and Ensign. The Company and Ensign or their respective subsidiaries, as applicable, also entered into a number of other agreements to govern the relationship between Ensign and the Company after the Spin-Off, including eight long-term leases (the “Ensign Master Leases”), under which Ensign leases 94 healthcare facilities on a triple-net basis.

The Company and Ensign also entered into an Opportunities Agreement, which granted the Company the right to match any offer from a third party to finance the acquisition or development of any healthcare or senior living facility by Ensign or any of its affiliates for a period of one year following the Spin-Off. In addition, this agreement granted Ensign, subject to certain exceptions, the right to either purchase and operate, or lease and operate, the facilities included in any portfolio of five or fewer healthcare or senior living facilities presented to the Company during the first year following the Spin-Off. The Opportunities Agreement and certain other agreements with Ensign terminated as of the first anniversary of the Spin-Off.

In accordance with the Financial Accounting Standards Board (“FASB”) Accounting Standards Codification (“ASC”) 505-60, Equity—Spinoffs and Reverse Spinoffs, the accounting for the separation of the Company follows its legal form, with Ensign as the legal and accounting spinor and the Company as the legal and accounting spinnee, due to the relative significance of Ensign’s healthcare business, the relative fair values of the respective companies, the retention of all senior management (except Mr. Gregory K. Stapley) by Ensign, and other relevant indicators. The assets and liabilities contributed to the Company from Ensign, or incurred in connection with the Spin-Off in the case of certain debt, were as follows (dollars in thousands):

Real estate investments, net	\$421,846	
Cash	78,731	
Accounts receivable and prepaid assets and other current assets	1,900	
Deferred financing costs, net	11,088	
Debt	(359,512)	)
Other liabilities	(6,838)	)
Net contribution	\$147,215	

Description of Business—The Company’s primary business consists of acquiring, financing and owning real property to be leased to third-party tenants in the healthcare sector. As of June 30, 2015, the Company owned and leased to independent operators, including Ensign, 102 skilled nursing, assisted living and independent living facilities which had a total of 10,647 operational beds located in Arizona, California, Colorado, Idaho, Iowa, Minnesota, Nebraska, Nevada, Texas, Utah, Virginia and Washington. The Company also owns and operates three independent living facilities which had a total of 264 units located in Texas and Utah. As of June 30, 2015, the Company also had one

other real estate investment, consisting of an \$8.0 million preferred equity investment.

## 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

6

---

Table of Contents

CARETRUST REIT, INC.

NOTES TO CONDENSED CONSOLIDATED AND COMBINED FINANCIAL STATEMENTS —

(Unaudited)

**Basis of Presentation**—The accompanying condensed consolidated and combined financial statements of the Company reflect, for all periods presented, the historical financial position, results of operations and cash flows of (i) the skilled nursing, assisted living and independent living facilities that Ensign contributed to the Company immediately prior to the Spin-Off and (ii) the operations of the three independent living facilities that the Company operated immediately following the Spin-Off. The condensed consolidated and combined financial statements included in this report also reflect the new investments that the Company has made after the Spin-Off. For the periods prior to the Spin-Off, the Company’s financial statements have been prepared on a “carve-out” basis from Ensign’s consolidated financial statements using the historical results of operations, cash flows, assets and liabilities attributable to such skilled nursing, assisted living and independent living facilities (the “Ensign Properties”).

For the periods prior to the Spin-Off, the condensed combined statements of operations reflect allocations of general corporate expenses from Ensign including, but not limited to, executive management, finance, legal, information technology, human resources, employee benefits administration, treasury, risk management, procurement, and other shared services. See further discussion in Note 6, Related Party Transactions.

Management believes that the assumptions and estimates used in preparation of the underlying condensed consolidated and combined financial statements are reasonable. However, the condensed consolidated and combined financial statements for the period January 1, 2014 through May 31, 2014, do not necessarily reflect what the Company’s financial position, results of operations or cash flows would have been if the Company had been a stand-alone company during the period presented. The historical financial information is not necessarily indicative of the Company’s future results of operations, financial position or cash flows.

The accompanying condensed consolidated and combined financial statements of the Company were prepared in accordance with accounting principles generally accepted in the United States (“GAAP”) for interim financial information and Article 10 of Regulation S-X. Accordingly, the condensed consolidated and combined financial statements do not include all of the disclosures required by GAAP for a complete set of annual audited financial statements. The condensed consolidated and combined financial statements should be read in conjunction with the audited consolidated and combined financial statements and notes thereto included in the Company’s Annual Report on Form 10-K for the fiscal year ended December 31, 2014. In the opinion of management, all adjustments which are of a normal and recurring nature and considered necessary for a fair presentation of the results of the interim periods presented have been included. The results of operations for the interim periods are not necessarily indicative of results for the full year. All intercompany transactions and account balances within the Company have been eliminated.

**Estimates and Assumptions**—The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenue and expenses during the reporting periods. Actual results could differ from those estimates.

**Reclassifications**—Certain amounts in the Company’s condensed consolidated and combined financial statements for prior periods have been reclassified to conform to the current period presentation. These reclassifications have not changed the results of operations of prior periods.

**Real Estate Depreciation and Amortization**—Real estate costs related to the acquisition and improvement of properties are capitalized and amortized over the expected useful life of the asset on a straight-line basis. Repair and maintenance costs are charged to expense as incurred and significant replacements and betterments are capitalized. Repair and maintenance costs include all costs that do not extend the useful life of the real estate asset. The Company considers the period of future benefit of an asset to determine its appropriate useful life. Expenditures for tenant improvements are capitalized and amortized over the shorter of the tenant’s lease term or expected useful life. The Company anticipates the estimated useful lives of its assets by class to be generally as follows:

Buildings

25-40 years

Edgar Filing: CareTrust REIT, Inc. - Form 10-Q

Building improvements	10-25 years
Tenant improvements	Shorter of lease term or expected useful life
Integral equipment, furniture and fixtures	5 years

7

---

Table of Contents

CARETRUST REIT, INC.

NOTES TO CONDENSED CONSOLIDATED AND COMBINED FINANCIAL STATEMENTS —

(Unaudited)

**Real Estate Acquisition Valuation**— In accordance with ASC 805, Business Combinations, the Company records the acquisition of income-producing real estate as a business combination. If the acquisition does not meet the definition of a business, the Company records the acquisition as an asset acquisition. Under both methods, all assets acquired and liabilities assumed are measured at their acquisition date fair values. For transactions that are business combinations, acquisition costs are expensed as incurred and restructuring costs that do not meet the definition of a liability at the acquisition date are expensed in periods subsequent to the acquisition date. For transactions that are asset acquisitions, acquisition costs are capitalized as incurred.

The Company assesses the acquisition date fair values of all tangible assets, identifiable intangibles and assumed liabilities using methods similar to those used by independent appraisers, generally utilizing a discounted cash flow analysis that applies appropriate discount and/or capitalization rates and available market information. Estimates of future cash flows are based on a number of factors, including historical operating results, known and anticipated trends, and market and economic conditions. The fair value of tangible assets of an acquired property considers the value of the property as if it were vacant.

Estimates of the fair values of the tangible assets, identifiable intangibles and assumed liabilities require the Company to make significant assumptions to estimate market lease rates, property-operating expenses, carrying costs during lease-up periods, discount rates, market absorption periods, and the number of years the property will be held for investment. The use of inappropriate assumptions would result in an incorrect valuation of the Company's acquired tangible assets, identifiable intangibles and assumed liabilities, which would impact the amount of the Company's net income.

**Impairment of Long-Lived Assets**—At least annually, management evaluates the Company's real estate investments for impairment indicators, including the evaluation of our assets' useful lives. Management also assesses the carrying value of the Company's real estate investments whenever events or changes in circumstances indicate that the carrying amount of the assets may not be recoverable. The judgment regarding the existence of impairment indicators is based on factors such as, but not limited to, market conditions, operator performance and legal structure. If indicators of impairment are present, management evaluates the carrying value of the related real estate investments in relation to the future undiscounted cash flows of the underlying facilities. Provisions for impairment losses related to long-lived assets are recognized when expected future undiscounted cash flows are determined to be less than the carrying values of the assets. An adjustment is made to the net carrying value of the real estate investments for the excess of carrying value over fair value. All impairments are taken as a period cost at that time, and depreciation is adjusted going forward to reflect the new value assigned to the asset.

If the Company decides to sell real estate properties, we evaluate the recoverability of the carrying amounts of the assets. If the evaluation indicates that the carrying value is not recoverable from estimated net sales proceeds, the property is written down to estimated fair value less costs to sell.

In the event of impairment, the fair value of the real estate investment is determined by market research, which includes valuing the property in its current use as well as other alternative uses, and involves significant judgment. The Company's estimates of cash flows and fair values of the properties are based on current market conditions and consider matters such as rental rates and occupancies for comparable properties, recent sales data for comparable properties, and, where applicable, contracts or the results of negotiations with purchasers or prospective purchasers. The Company's ability to accurately estimate future cash flows and estimate and allocate fair values impacts the timing and recognition of impairments. While the Company believes its assumptions are reasonable, changes in these assumptions may have a material impact on financial results.

**Other Real Estate Investments** — Preferred equity investments are accounted for at unpaid principal balance, plus accrued return, net of reserves. The Company recognizes return income on a quarterly basis based on the outstanding investment including any accrued and unpaid return.



The Company periodically evaluates each of its other real estate investments for indicators of impairment. An investment is impaired when, based on current information and events, it is probable that we will be unable to collect all amounts due according to the existing contractual terms. A reserve is established for the excess of the carrying value of the investment over its fair value.

Cash and Cash Equivalents—Cash and cash equivalents consist of bank term deposits and money market funds with original maturities of three months or less at time of purchase and therefore approximate fair value. The fair value of these

Table of Contents

CARETRUST REIT, INC.

NOTES TO CONDENSED CONSOLIDATED AND COMBINED FINANCIAL STATEMENTS —

(Unaudited)

investments is determined based on “Level 1” inputs, which consist of unadjusted quoted prices in active markets that are accessible at the measurement date for identical, unrestricted assets. The Company places its cash and short-term investments with high credit quality financial institutions.

The Company’s cash and cash equivalents balance periodically exceeds federally insurable limits. The Company monitors the cash balances in its operating accounts and adjusts the cash balances as appropriate; however, these cash balances could be impacted if the underlying financial institutions fail or are subject to other adverse conditions in the financial markets. To date, the Company has experienced no loss or lack of access to cash in its operating accounts.

**Deferred Financing Costs**—External costs incurred from placement of our debt are capitalized and amortized on a straight-line basis over the terms of the related borrowings, which approximates the effective interest method.

Amortization of deferred financing costs is classified as interest expense in our condensed consolidated and combined statements of operations. Accumulated amortization of deferred financing costs was \$3.3 million and \$2.2 million at June 30, 2015 and December 31, 2014, respectively.

When financings are terminated, unamortized deferred financing costs, as well as charges incurred for the termination, are expensed at the time the termination is made. Gains and losses from the extinguishment of debt are presented within income from continuing operations in our condensed consolidated and combined statements of operations.

**Revenue Recognition** —The Company recognizes rental revenue, including rental abatements, lease incentives and contractual fixed increases attributable to operating leases, if any, from tenants under lease arrangements with minimum fixed and determinable increases on a straight-line basis over the non-cancellable term of the related leases when collectability is reasonably assured. Tenant recoveries related to the reimbursement of real estate taxes, insurance, repairs and maintenance, and other operating expenses are recognized as revenue in the period the expenses are incurred and presented gross if the Company is the primary obligor and, with respect to purchasing goods and services from third-party suppliers, has discretion in selecting the supplier and bears the associated credit risk. For the six months ended June 30, 2015 and 2014, such tenant reimbursement revenues consist of real estate taxes. Contingent revenue, if any, is not recognized until all possible contingencies have been eliminated.

The Company evaluates the collectability of rents and other receivables on a regular basis based on factors including, among others, payment history, the operations, the asset type and current economic conditions. If our evaluation of these factors indicates we may not recover the full value of the receivable, we provide a reserve against the portion of the receivable that we estimate may not be recovered. This analysis requires us to determine whether there are factors indicating a receivable may not be fully collectible and to estimate the amount of the receivable that may not be collected. We did not reserve any receivables as of June 30, 2015 or December 31, 2014.

**Income Taxes**—The Company’s operations prior to the Spin-Off were historically included in Ensign’s U.S. federal and state income tax returns and all income taxes for periods prior to the Spin-Off were paid by Ensign. Income tax expense and other income tax related information contained in these condensed consolidated and combined financial statements are presented on a separate tax return basis as if the Company filed its own tax returns for all periods.

Management believes that the assumptions and estimates used to determine these tax amounts are reasonable.

However, the condensed consolidated and combined financial statements herein may not necessarily reflect the Company’s income tax expense or tax payments in the future, or what its tax amounts would have been if the Company had been a stand-alone company prior to the Spin-Off.

The Company expects to elect to be taxed as a REIT under the Internal Revenue Code of 1986, as amended (the “Code”), and expects to qualify as such beginning with its taxable year ending December 31, 2014. To qualify as a REIT, the Company must meet certain organizational and operational requirements, including a requirement to distribute at least 90% of the Company’s annual REIT taxable income to its stockholders (which is computed without regard to the dividends paid deduction or net capital gain and which does not necessarily equal net income as calculated in accordance with GAAP). As a REIT, the Company generally will not be subject to federal income tax to the extent it distributes qualifying dividends to its stockholders. If the Company fails to qualify as a REIT in any

taxable year, it will be subject to federal income tax on its taxable income at regular corporate income tax rates and generally will not be permitted to qualify for treatment as a REIT for federal income tax purposes for the four taxable years following the year during which qualification is lost unless the Internal Revenue Service grants the Company relief under certain statutory provisions.

Table of Contents

CARETRUST REIT, INC.

NOTES TO CONDENSED CONSOLIDATED AND COMBINED FINANCIAL STATEMENTS —

(Unaudited)

In connection with the Company's intention to qualify as a real estate investment trust in 2014, on October 17, 2014, the Company's board of directors declared a special dividend (the "Special Dividend") of \$132.0 million, or approximately \$5.88 per common share, which represents the amount of accumulated earnings and profits, or "E&P," allocated to the Company as a result of the Spin-Off. The Special Dividend was intended to purge the Company of accumulated E&P attributable to the period prior to the Company's first taxable year as a REIT. The Special Dividend was paid on December 10, 2014, to stockholders of record on October 31, 2014, in a combination of both cash and stock. The cash portion totaled \$33.0 million and the stock portion totaled \$99.0 million. The Company issued 8,974,249 shares of common stock in connection with the stock portion of the Special Dividend.

**Derivatives and Hedging Activities**—The Company evaluates variable and fixed interest rate risk exposure on a routine basis and to the extent the Company believes that it is appropriate, it will offset most of its variable rate risk exposure by entering into interest rate swap agreements. It is the Company's policy to only utilize derivative instruments for hedging purposes (i.e., not for speculation). The Company formally designates its interest rate swap agreements as hedges and documents all relationships between hedging instruments and hedged items. The Company formally assesses effectiveness of its hedging relationships, both at the hedge inception and on an ongoing basis, then measures and records ineffectiveness. The Company would discontinue hedge accounting prospectively (i) if it is determined that the derivative is no longer effective in offsetting changes in the cash flows of a hedged item, (ii) when the derivative expires or is sold, terminated or exercised, (iii) if it is no longer probable that the forecasted transaction will occur, or (iv) if management determines that designation of the derivative as a hedge instrument is no longer appropriate.

Effective May 30, 2014, the Company de-designated its interest rate swap contract that historically qualified for cash flow hedge accounting. This was due to the termination of the interest rate swap agreement related to the early retirement of the senior credit facility in place prior to the Spin-Off. As a result, the loss previously recorded in accumulated other comprehensive loss related to the interest rate swap was recognized in interest expense in the condensed consolidated and combined statements of operations during the three month period ended June 30, 2014. There was no outstanding interest rate swap contract as of June 30, 2015.

**Stock-Based Compensation**—The Company accounts for share-based payment awards in accordance with ASC Topic 718, Compensation – Stock Compensation ("ASC 718"). ASC 718 requires that the cost resulting from all share-based payment transactions be recognized in the financial statements. ASC 718 requires all entities to apply a fair value-based measurement method in accounting for share-based payment transactions with directors, officers and employees except for equity instruments held by employee share ownership plans. Net income reflects stock-based compensation expense of \$0.3 million and \$0.7 million for the three and six months ended June 30, 2015, respectively.

**Concentration of Credit Risk**—The Company is subject to concentrations of credit risk consisting primarily of operating leases on our owned properties. See Note 12, Concentration of Risk, for a discussion of major operator concentration.

**Segment Disclosures** —The FASB accounting guidance regarding disclosures about segments of an enterprise and related information establishes standards for the manner in which public business enterprises report information about operating segments. The Company has one reportable segment consisting of investments in healthcare-related real estate assets.

**Earnings (Loss) Per Share**—The Company calculates earnings (loss) per share ("EPS") in accordance with ASC 260, Earnings Per Share. Basic EPS is computed by dividing net income applicable to common stock by the weighted-average number of common shares outstanding during the period. Diluted EPS reflects the additional dilution for all potentially-dilutive securities. Basic and diluted EPS for the three and six months ended June 30, 2014 were retroactively restated for the number of basic and diluted shares outstanding immediately following the Spin-Off. **Recently Issued Accounting Standards Update**— In May 2014, the FASB issued ASU No. 2014-09, Revenue from Contracts with Customers (Topic 606) ("ASU No. 2014-09"). ASU No. 2014-09 requires an entity to recognize the

revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods and services. ASU No. 2014-09 supersedes the revenue requirements in Revenue Recognition (Topic 605) and most industry-specific guidance throughout the Industry Topics of the Codification. ASU No. 2014-09 does not apply to lease contracts within the scope of Leases (Topic 840). In July 2015, the FASB provided for a one-year deferral of the effective date of ASU No. 2014-09. The standard will be effective for annual reporting periods, and interim periods therein, beginning after December 15, 2017. The Company is currently assessing the impact of adopting ASU No. 2014-09 but does not believe it will have a material effect on income from operations or the Company's financial position.

Table of Contents

CARETRUST REIT, INC.

NOTES TO CONDENSED CONSOLIDATED AND COMBINED FINANCIAL STATEMENTS —

(Unaudited)

In February 2015, the FASB issued ASU No. 2015-02, Consolidation (Topic 810): Amendments to the Consolidation Analysis (“ASU No. 2015-02”), which makes certain changes to both the variable interest model and the voting model, including changes to (1) the identification of variable interests (fees paid to a decision maker or service provider), (2) the variable interest entity characteristics for a limited partnership or similar entity and (3) the primary beneficiary determination. ASU No. 2015-02 is effective for fiscal years, and interim periods within these fiscal years, beginning after December 15, 2015. The Company does not expect the adoption of ASU No. 2015-02 to have a significant impact on its consolidated financial statements.

In April 2015, the FASB issued ASU No. 2015-03, Simplifying the Presentation of Debt Issuance Costs (“ASU No. 2015-03”), which requires that debt issuance costs related to a recognized debt liability be presented in the balance sheet as a direct deduction from the carrying amount of that debt liability, consistent with debt discounts. The recognition and measurement guidance for debt issuance costs is not affected. Upon adoption, we will apply the new guidance on a retrospective basis and adjust the balance sheet of each individual period presented to reflect the period-specific effects of applying the new guidance. ASU No. 2015-03 is effective for fiscal years, and interim periods within these fiscal years, beginning after December 15, 2015. The Company does not expect the adoption of ASU No. 2015-03 to have a significant impact on its consolidated financial statements.

## 3. REAL ESTATE INVESTMENTS, NET

The following tables summarize our investment in owned properties at June 30, 2015, and December 31, 2014 (dollars in thousands):

	June 30, 2015	December 31, 2014
Land	\$79,804	\$75,072
Buildings and improvements	445,391	417,414
Integral equipment, furniture and fixtures	49,003	47,134
Real estate investments	574,198	539,620
Accumulated depreciation	(114,683)	(103,405)
Real estate investments, net	\$459,515	\$436,215

As of June 30, 2015, all but 11 of the Company’s facilities were leased to subsidiaries of Ensign under the Ensign Master Leases which began on June 1, 2014. The obligations under the Ensign Master Leases are guaranteed by Ensign. A default by any subsidiary of Ensign with regard to any facility leased pursuant to an Ensign Master Lease will result in a default under all of the Ensign Master Leases. The annual revenues from the Ensign Master Leases are \$56.0 million during each of the first two years of the Ensign Master Leases. Commencing in the third year under the Ensign Master Leases, the annual revenues from the Ensign Master Leases will be escalated annually by an amount equal to the product of (1) the lesser of the percentage change in the Consumer Price Index (“CPI”) (but not less than zero) or 2.5%, and (2) the prior year’s rent. In addition to rent, the subsidiaries of Ensign that are tenants under the Ensign Master Leases are solely responsible for the costs related to the leased properties (including property taxes, insurance, and maintenance and repair costs).

Table of Contents

CARETRUST REIT, INC.

NOTES TO CONDENSED CONSOLIDATED AND COMBINED FINANCIAL STATEMENTS —

(Unaudited)

As of June 30, 2015, our total future minimum rental revenues for all of our tenants were (dollars in thousands):

Year	Amount
Remaining 2015	\$30,721
2016	61,442
2017	61,442
2018	61,442
2019	61,442
Thereafter	630,333
	\$906,822

**Recent Real Estate Acquisitions**

The following recent real estate acquisitions were accounted for as asset acquisitions:

**Bethany Rehabilitation Center**

In January 2015, the Company acquired the Bethany Rehabilitation Center, a skilled nursing facility located in Lakewood, Colorado, for \$18.1 million, which includes acquisition costs capitalized of \$0.1 million.

In connection with the acquisition, the Company entered into a triple-net master lease with Eduro Healthcare LLC. The lease carries an initial term of 15 years with two five-year renewal options and CPI-based rent escalators. The Company anticipates initial annual lease revenues of \$1.7 million.

**Mira Vista Care Center**

In April 2015, the Company acquired the Mira Vista Care Center, a skilled nursing facility located in Mount Vernon, Washington, for \$9.3 million, which includes acquisition costs capitalized of \$0.2 million.

In connection with the acquisition, the Company entered into a triple-net master lease with Five Oaks Healthcare, LLC. The lease carries an initial term of 15 years with two five-year renewal options and CPI-based rent escalators. The Company anticipates initial annual lease revenues of \$0.9 million.

**Shoreline Health & Rehabilitation Center**

In June 2015, the Company acquired the Shoreline Health & Rehabilitation Center, a skilled nursing facility located in Shoreline, Washington, for \$6.8 million, which includes acquisition costs capitalized of \$0.2 million.

In connection with the acquisition, the Company entered into a triple-net master lease with Five Oaks Healthcare, LLC. The lease carries an initial term of 15 years with two five-year renewal options and CPI-based rent escalators. The Company anticipates initial annual lease revenues of \$0.7 million.

**4. OTHER REAL ESTATE INVESTMENTS**

In December 2014, the Company completed a \$7.5 million preferred equity investment with Signature Senior Living, LLC and Milestone Retirement Communities. The preferred equity investment yields 12.0% calculated on a quarterly basis on the outstanding carrying value of the investment. The investment will be used to develop Signature Senior Living at Arvada, a planned 134-unit upscale assisted living and memory care community in Arvada, Colorado that will be constructed on a five-acre site. In connection with its investment, CareTrust obtained an option to purchase the Arvada development at a fixed-formula price upon stabilization, with an initial lease yield of at least 8.0%. The project is expected to be completed in early 2016.

During the three and six months ended June 30, 2015, the Company recognized \$0.2 million and \$0.5 million of interest income and this unpaid amount was added to the outstanding carrying value of the investment.



Table of Contents

## 5. FAIR VALUE MEASUREMENTS

Under GAAP, the Company is required to measure certain financial instruments at fair value on a recurring basis. In addition, the Company is required to measure other financial instruments and balances at fair value on a non-recurring basis (e.g., carrying value of impaired long-lived assets). Fair value is defined as the exchange price that would be received for an asset or paid to transfer a liability (an exit price) in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants on the measurement date. The GAAP fair value framework uses a three-tiered approach. Fair value measurements are classified and disclosed in one of the following three categories:

Level 1: unadjusted quoted prices in active markets that are accessible at the measurement date for identical assets or liabilities;

Level 2: quoted prices for similar instruments in active markets, quoted prices for identical or similar instruments in markets that are not active, and model-derived valuations in which significant inputs and significant value drivers are observable in active markets; and

Level 3: prices or valuation techniques where little or no market data is available that requires inputs that are both significant to the fair value measurement and unobservable.

Financial Instruments: Considerable judgment is necessary to estimate the fair value of financial instruments. The estimates of fair value presented herein are not necessarily indicative of the amounts that could be realized upon disposition of the financial instruments. A summary of the face values, carrying amounts and fair values of the Company's financial instruments as of June 30, 2015 and December 31, 2014 using Level 2 inputs, for the senior unsecured notes payable, and Level 3 inputs, for all other financial instruments, is as follows (dollars in thousands):

	June 30, 2015			December 31, 2014		
	Face Value	Carrying Amount	Fair Value	Face Value	Carrying Amount	Fair Value
Financial assets:						
Preferred equity investment	\$7,500	\$7,987	\$7,987	\$7,500	\$7,532	\$7,532
Financial liabilities:						
Senior unsecured notes payable	\$260,000	\$260,000	\$265,850	\$260,000	\$260,000	\$265,200
Mortgage notes payable	\$96,854	\$96,854	\$99,697	\$98,205	\$98,205	\$101,822

Cash and cash equivalents, accounts receivable, accounts payable and accrued liabilities and senior secured revolving credit facility: These balances approximate their fair values due to the short-term nature of these instruments.

Preferred equity investment: The fair value of the preferred equity investment is estimated using an internal valuation model that considered the expected future cash flows of the investment, the underlying collateral value and other credit enhancements.

Senior unsecured notes payable: The fair value of the senior unsecured notes payable was determined using third-party quotes derived from orderly trades.

Mortgage notes payable: The fair value of the Company's notes payable is estimated using a discounted cash flow analysis based on management's estimates of current market interest rates for instruments with similar characteristics, including remaining loan term, loan-to-value ratio, type of collateral and other credit enhancements. Additionally, when determining the fair value of liabilities in circumstances in which a quoted price in an active market for an identical liability is not available, the Company measures fair value using (i) a valuation technique that uses the quoted price of the identical liability when traded as an asset or quoted prices for similar liabilities when traded as assets or (ii) another valuation technique that is consistent with the principles of fair value measurement, such as the income approach or the market approach. The Company classifies these inputs as Level 3 inputs.

6. RELATED PARTY TRANSACTIONS

13

---

Table of Contents

CARETRUST REIT, INC.

NOTES TO CONDENSED CONSOLIDATED AND COMBINED FINANCIAL STATEMENTS —

(Unaudited)

Allocation of corporate expenses—For the three and six months ended June 30, 2014, the condensed consolidated and combined statements of operations of the Company include Ensign revenues and expenses that are specifically identifiable or otherwise attributable to the Company. The specific identification methodology was utilized for all of the items on the condensed statements of operations excluding general corporate expenses. For the periods prior to the Spin-Off, Ensign Properties' operations were fully integrated with Ensign, including executive management, finance, treasury, corporate income tax, human resources, legal services and other shared services. These costs were allocated to the Company on a systematic basis utilizing a direct usage basis when identifiable, with the remainder allocated on time study, or percentage of the total revenues. The primary allocation method was a time study based on time devoted to Ensign Properties' activities.

Allocated expenses for these general and administrative services of \$5.5 million and \$7.4 million for the three and six months ended June 30, 2014 are reflected in general and administrative expense, in addition to direct expenses which are included in total expenses. There was no allocation for the three and six months ended June 30, 2015. The Company's financial statements may not be indicative of future performance and do not necessarily reflect what the results of operations, financial position and cash flows would have been had the Company operated as an independent, publicly-traded company during the six months ended June 30, 2014.

Rental income from Ensign—The Company derives almost all of its rental income through operating lease agreements with Ensign. Ensign is a holding company with no direct operating assets, employees or revenue. All of Ensign's operations are conducted by separate independent subsidiaries, each of which has its own management, employees and assets. See Note 12, Concentration of Risk, for a discussion of major operator concentration.

Christopher R. Christensen, one of the Company's directors from June 1, 2014 through April 15, 2015, serves as the chief executive officer of Ensign as well as a member of Ensign's board of directors. As such, all rental income and tenant reimbursements earned related to the Ensign Master Leases during Mr. Christensen's tenure on our board are considered related party in nature. For the three and six months ended June 30, 2015, the Company recognized \$2.3 million and \$16.3 million in rental income, respectively, from Ensign related to the Ensign Master Leases as well as \$0.2 million and \$1.4 million of tenant reimbursements, respectively. For the three and six months ended June 30, 2014, the Company recognized \$4.7 million and \$4.7 million in rental income, respectively, as well as \$0.4 million and \$0.4 million of tenant reimbursements, respectively. As of December 31, 2014, the Company also had accounts receivable totaling \$2.3 million due from Ensign for tenant reimbursements. After April 15, 2015, the effective date of Mr. Christensen's resignation from our board of directors, rental income and tenant reimbursements related to the Ensign Master Leases, and any related accounts receivable, are not considered earned or due from a related party.

Centralized cash management system—Prior to the Spin-Off, the Company participated in Ensign's centralized cash management system. In conjunction therewith, the intercompany transactions between the Company and Ensign had been considered to be effectively settled in cash in these financial statements. The net effect of the settlement of these intercompany transactions, in addition to cash transfers to and from Ensign, are reflected in "Net contribution from Ensign" on the condensed consolidated and combined statements of cash flows. The "Net contribution from Ensign" was \$4.4 million for the six months ended June 30, 2014.

## 7. DEBT

The Company had debt outstanding of \$391.9 million as of June 30, 2015, and \$358.2 million as of December 31, 2014.

### Senior Unsecured Notes Payable

On May 30, 2014, the Company's wholly owned subsidiary, CTR Partnership, L.P. (the "Operating Partnership"), and its wholly owned subsidiary, CareTrust Capital Corp. (together with the Operating Partnership, the "Issuers"), completed a private offering of \$260.0 million aggregate principal amount of 5.875% Senior Notes due 2021 (the "Notes"). The

Edgar Filing: CareTrust REIT, Inc. - Form 10-Q

Notes were issued at par, resulting in gross proceeds of \$260.0 million and net proceeds of approximately \$253.0 million after deducting underwriting fees and other offering expenses. We transferred approximately \$220.8 million of the net proceeds of the offering of the Notes to Ensign, and used the remaining portion of the net proceeds of the offering to pay the cash portion of the Special Dividend. The Notes mature on June 1, 2021 and bear interest at a rate of 5.875% per year. Interest on the Notes is payable on June 1 and December 1 of each year, beginning on December 1, 2014.

Table of Contents

CARETRUST REIT, INC.

NOTES TO CONDENSED CONSOLIDATED AND COMBINED FINANCIAL STATEMENTS —

(Unaudited)

The Issuers may redeem the Notes any time prior to June 1, 2017 at a redemption price of 100% of the principal amount of the Notes redeemed plus accrued and unpaid interest on the Notes, if any, to, but not including, the redemption date, plus a “make whole” premium described in the indenture governing the Notes and, at any time on or after June 1, 2017, at the redemption prices set forth in the indenture. In addition, at any time on or prior to June 1, 2017, up to 35% of the aggregate principal amount of the Notes may be redeemed with the net proceeds of certain equity offerings if at least 65% of the originally issued aggregate principal amount of the Notes remains outstanding. If certain changes of control of the Company occur, holders of the Notes will have the right to require the Issuers to repurchase their Notes at 101% of the principal amount plus accrued and unpaid interest, if any, to, but not including, the repurchase date.

The obligations under the Notes are fully and unconditionally guaranteed, jointly and severally, on an unsecured basis, by the Company and certain of the Company’s wholly owned existing and, subject to certain exceptions, future material subsidiaries (other than the Issuers); provided, however, that such guarantees are subject to automatic release under certain customary circumstances, including if the subsidiary guarantor is sold or sells all or substantially all of its assets, the subsidiary guarantor is designated “unrestricted” for covenant purposes under the indenture, the subsidiary guarantor’s guarantee of other indebtedness which resulted in the creation of the guarantee of the Notes is terminated or released, or the requirements for legal defeasance or covenant defeasance or to discharge the indenture have been satisfied. See Note 13, Summarized Condensed Consolidating and Combining Information.

The indenture contains covenants limiting the ability of the Company and its restricted subsidiaries to: incur or guarantee additional indebtedness; incur or guarantee secured indebtedness; pay dividends or distributions on, or redeem or repurchase, capital stock; make certain investments or other restricted payments; sell assets; enter into transactions with affiliates; merge or consolidate or sell all or substantially all of their assets; and create restrictions on the ability of the Issuers and their restricted subsidiaries to pay dividends or other amounts to the Issuers. The indenture also requires the Company and its restricted subsidiaries to maintain a specified ratio of unencumbered assets to unsecured indebtedness. These covenants are subject to a number of important and significant limitations, qualifications and exceptions. The indenture also contains customary events of default.

As of June 30, 2015, the Company was in compliance with all applicable financial covenants under the indenture.

#### Senior Secured Revolving Credit Facility

On May 30, 2014, the Operating Partnership entered into a credit and guaranty agreement (the “Credit Agreement”), which governs our senior secured revolving credit facility (the “Credit Facility”), with several banks and other financial institutions and lenders (the “Lenders”) and Suntrust Bank, in its capacity as administrative agent for the Lenders, as an issuing bank and swingline lender. The Credit Agreement provides for a borrowing capacity of \$150.0 million and includes an accordion feature that allows the Operating Partnership to increase the borrowing availability by up to an additional \$75.0 million, subject to terms and conditions. The Credit Facility is secured by mortgages on certain of the real properties owned by the Company’s subsidiaries and the amount available to be borrowed under the Credit Agreement is based on a borrowing base calculation relating to the mortgaged properties, determined according to, among other factors, the mortgageability cash flow as such term is defined in the Credit Agreement. The Credit Facility is also secured by certain personal property of the Company’s subsidiaries that have provided mortgages, the Company’s interests in the Operating Partnership and the Company’s and its subsidiaries’ equity interests in the Company’s subsidiaries that have guaranteed the Operating Partnership’s obligations under the Credit Agreement. The Credit Agreement has a maturity date of May 30, 2018, and includes a one year extension option. As of June 30, 2015, there was \$35.0 million outstanding under the Credit Agreement.

Borrowings under the Credit Agreement bear interest on the outstanding principal amount at a rate equal to the applicable percentage plus, at the Operating Partnership’s option, either (a) LIBOR or (b) a base rate determined as the

greater of (i) the prime lending rate, (ii) the Federal Funds Rate plus 0.5%, and (iii) one-month LIBOR plus 1.0% (referred to as the “Base Rate”). The applicable percentage for borrowings will vary based on the Consolidated Leverage Ratio, as defined in the Credit Agreement, and will range from 2.0% to 2.5% per annum for LIBOR based borrowings and 1.0% to 1.5% per annum for borrowings at the Base Rate. In addition, the Operating Partnership is required to pay a commitment fee to the lenders equal to between 0.35% and 0.50% per annum based on the amount of unused borrowings under the Credit Agreement. During the three and six months ended June 30, 2015, the Company incurred \$0.2 million and \$0.4 million of commitment fees, respectively.

The obligations of the Operating Partnership under the Credit Agreement are guaranteed by the Company and certain subsidiaries of the Company.

Table of Contents

CARETRUST REIT, INC.

NOTES TO CONDENSED CONSOLIDATED AND COMBINED FINANCIAL STATEMENTS —

(Unaudited)

The Credit Agreement contains customary covenants that include restrictions or limitations on the ability to make acquisitions and other investments, make distributions, incur additional indebtedness, engage in non-healthcare related business activities, enter into transactions with affiliates and sell or otherwise transfer certain assets as well as customary events of default. The Credit Agreement also requires the Company, through the Operating Partnership, to comply with specified financial covenants, which include a maximum debt to asset value ratio, a maximum secured debt to asset value ratio, a maximum secured recourse debt to asset value ratio, a minimum fixed charge coverage ratio and a minimum tangible net worth requirement. As of June 30, 2015, the Company was in compliance with all applicable financial covenants under the Credit Agreement.

**GECC Loan**

Ten of our properties are subject to secured mortgage indebtedness to General Electric Capital Corporation (the “GECC Loan”), which we assumed in connection with the Spin-Off. The outstanding amount of this mortgage indebtedness was approximately \$96.4 million as of June 30, 2015, including an advance of approximately \$50.7 million that was made on May 30, 2014. This advance bears interest at a floating rate equal to three-month LIBOR plus 3.35%, reset monthly and subject to a LIBOR floor of 0.50%, with monthly principal and interest payments based on a 25 year amortization. The remaining indebtedness under the GECC Loan bears interest at a blended rate of 7.25% per annum until, but not including, June 29, 2016, and then converts to the floating rate described above. The GECC Loan matures on May 30, 2017, subject to two 12-month extension options, the exercise of which is conditioned, in each case, on the absence of any then-existing default and the payment of an extension fee equal to 0.25% of the then-outstanding principal balance. Provided there is no then-existing default and upon 30 days written notice, the original portion of the GECC Loan, approximately \$46.9 million as of June 30, 2015, is prepayable without penalty, in whole but not in part, after January 31, 2016. The new portion of the GECC Loan, approximately \$49.5 million as of June 30, 2015, is prepayable without penalty, in whole but not in part, after January 31, 2016.

The GECC Loan is guaranteed by the Company, contains customary affirmative and negative covenants, as well as customary events of default, and requires us to comply with specified financial maintenance covenants. As of June 30, 2015, the Company was in compliance with all applicable financial covenants under the GECC Loan.

**Promissory Notes with Johnson Land Enterprises, LLC**

On October 1, 2009, Ensign entered into four separate promissory notes with Johnson Land Enterprises, LLC, for an aggregate of \$10.0 million. On May 30, 2014, in connection with the Spin-Off, three of the promissory notes were paid in full and the remaining promissory note was assumed by the Company. The remaining promissory note bears interest at 6.0%, with principal and interest payable monthly through September 30, 2019. The promissory note is collateralized by a deed of trust on real property, an assignment of rent and a security agreement. At June 30, 2015, the outstanding principal balance on the promissory note was \$0.5 million and is included in mortgage notes payable on the condensed consolidated balance sheets.

**Interest Expense**

During the three and six months ended June 30, 2015, the Company incurred \$6.0 million and \$11.9 million of interest expense, respectively. Included in interest expense for the three and six months ended June 30, 2015 was \$0.6 million and \$1.1 million of amortization of deferred financing costs, respectively. During the three and six months ended June 30, 2014, the Company incurred \$6.5 million and \$9.8 million of interest expense, respectively. Included in interest expense for the three and six months ended June 30, 2014 was \$0.3 million and \$0.5 million of amortization of deferred financing costs, respectively, and \$20,000 and \$51,000 of amortization of debt discount, respectively. As of June 30, 2015 and December 31, 2014, the Company’s interest payable was \$1.7 million and \$1.7 million, respectively.

## 8. EQUITY

### Common Stock

Dividends on Common Stock — During the first quarter of 2015, our Board of Directors declared a quarterly cash dividend of \$0.16 per share of common stock, payable on April 15, 2015 to stockholders of record as of March 31, 2015. During the second quarter of 2015, our Board of Directors declared a quarterly cash dividend of \$0.16 per share of common stock, payable on July 15, 2015 to stockholders of record as of June 30, 2015.



Table of Contents**9. STOCK-BASED COMPENSATION**

All stock-based awards are subject to the terms of the CareTrust REIT, Inc. and CTR Partnership, L.P. Incentive Award Plan (the “Plan”). The Plan provides for the granting of stock-based compensation, including stock options, restricted stock, performance awards, restricted stock units and other incentive awards to officers, employees and directors in connection with their employment with or services provided to the Company.

**Restricted Stock Awards** — In connection with the Spin-Off, employees of Ensign who had unvested shares of restricted stock were given one share of CareTrust unvested restricted stock totaling 207,580 shares at the Spin-Off. These restricted shares are subject to a time vesting provision only and the Company does not recognize any stock compensation expense associated with these awards. During the six months ended June 30, 2015, 41,600 shares vested or were forfeited. At June 30, 2015, there were 117,430 unvested restricted stock awards outstanding.

In December 2014, the Compensation Committee of the Company’s Board of Directors granted 12,270 shares of restricted stock to members of the Board of Directors. Each share had a fair market value on the date of grant of \$12.23 per share, based on the market price of the Company’s common stock on that date, and the shares vest ratably over three years beginning on May 31, 2015. Additionally, in December 2014, the Compensation Committee granted 142,770 shares of restricted stock to officers and employees. Each share had a fair market value on the date of grant of \$12.23 per share, based on the market price of the Company’s common stock on that date, and the shares vest ratably over five years beginning on May 31, 2015.

In June 2015, in separate grants, the Compensation Committee of the Company’s Board of Directors granted 15,680 shares and 13,240 shares of restricted stock to members of the Board of Directors, with each share having a fair market value on the date of grant of \$12.76 and \$12.67 per share, respectively, based on the market price of the Company’s common stock on those dates. The shares vest over one year. Additionally, in June 2015, the Compensation Committee granted 235,880 shares of restricted stock to officers and employees. Each share had a fair market value on the date of grant of \$12.76 per share, based on the market price of the Company’s common stock on that date, and the shares vest ratably over four years beginning on June 30, 2016.

During the six months ended June 30, 2015, 32,643 shares vested and none were forfeited. The Company recognized \$0.3 million and \$0.7 million of compensation expense associated with these grants for the three and six months ended June 30, 2015, respectively. As of June 30, 2015, there was \$4.5 million of unamortized stock-based compensation expense related to these unvested awards and the weighted-average remaining vesting period of such awards was 3.7 years.

**10. EARNINGS PER COMMON SHARE**

The following table presents the calculation of basic and diluted EPS for the Company’s common stock for the three and six months ended June 30, 2015 and 2014, and reconciles the weighted-average common shares outstanding used in the calculation of basic EPS to the weighted-average common shares outstanding used in the calculation of diluted EPS for the three and six months ended June 30, 2015 and 2014 (amounts in thousands, except per share amounts):

	For the Three Months Ended June 30,		For the Six Months Ended June 30,	
	2015	2014	2015	2014
Numerator:				
Net income (loss)	\$2,266	\$(10,342 )	\$4,304	\$(10,740 )
Less: Net income allocated to participating securities	(81 )	—	(117 )	—
Numerator for basic and diluted earnings (loss) available to common stockholders	\$2,185	\$(10,342 )	\$4,187	\$(10,740 )
Denominator:				

Edgar Filing: CareTrust REIT, Inc. - Form 10-Q

Weighted-average basic and diluted common shares outstanding	31,278	22,231	31,268	22,230
Basic and diluted earnings (loss) per common share	\$0.07	\$(0.47)	) \$0.13	\$(0.48)

17

---

## Table of Contents

The Company's unvested restricted shares associated with its incentive award plan and unvested restricted shares issued to employees of Ensign at the Spin-Off have been excluded from the above calculation of earnings (loss) per share for the three and six months ended June 30, 2015 and 2014, as their inclusion would have been anti-dilutive.

### 11. COMMITMENTS AND CONTINGENCIES

**U.S. Government Settlement**—In October 2013, Ensign completed and executed a settlement agreement (the “Settlement Agreement”) with the U.S. Department of Justice (“DOJ”). This settlement agreement fully and finally resolved a DOJ investigation of Ensign related primarily to claims submitted to the Medicare program for rehabilitation services provided at skilled nursing facilities in California and certain ancillary claims. Pursuant to the Settlement Agreement, Ensign made a single lump-sum remittance to the government in the amount of \$48.0 million in October 2013. Ensign denied engaging in any illegal conduct and agreed to the settlement amount without any admission of wrongdoing in order to resolve the allegations and avoid the uncertainty and expense of protracted litigation.

In connection with the settlement and effective as of October 1, 2013, Ensign entered into a five-year corporate integrity agreement with the Office of Inspector General-HHS (the “CIA”). The CIA acknowledges the existence of Ensign's current compliance program, and requires that Ensign continue during the term of the CIA to maintain a compliance program designed to promote compliance with the statutes, regulations, and written directives of Medicare, Medicaid, and all other Federal health care programs. Ensign is also required to maintain several elements of its existing program during the term of the CIA, including maintaining a compliance officer, a compliance committee of the board of directors, and a code of conduct. The CIA requires that Ensign conduct certain additional compliance-related activities during the term of the CIA, including various training and monitoring procedures, and maintaining a disciplinary process for compliance obligations.

Participation in federal healthcare programs by Ensign is not affected by the Settlement Agreement or the CIA. In the event of an uncured material breach of the CIA, Ensign could be excluded from participation in federal healthcare programs and/or subject to prosecution. The Company is subject to certain continuing operational obligations as part of Ensign's compliance program pursuant to the CIA, but otherwise has no liability related to the DOJ investigation.

**Legal Matters**—None of the Company or any of its subsidiaries is a party to, and none of their respective properties are the subject of, any material legal proceedings.

### 12. CONCENTRATION OF RISK

**Major operator concentration** – The Company has one major tenant, Ensign, from which the Company derived the majority of its overall revenue during the three and six months ended June 30, 2015 and 2014. As of June 30, 2015, Ensign leased 94 skilled nursing, assisted living and independent living facilities which had a total of 10,121 licensed beds and are located in Arizona, California, Colorado, Idaho, Iowa, Nebraska, Nevada, Texas, Utah and Washington. The four states in which Ensign leases the highest concentration of properties were California, Texas, Utah and Arizona.

Ensign's financial statements can be found at Ensign's website <http://www.ensigngroup.net>.

### 13. SUMMARIZED CONDENSED CONSOLIDATING AND COMBINING INFORMATION

The 5.875% Senior Notes due 2021 issued by the Issuers on May 30, 2014 are jointly and severally, fully and unconditionally, guaranteed by CareTrust REIT, Inc., as the parent guarantor (the “Parent Guarantor”), and certain 100% owned subsidiaries of the Parent Guarantor other than the Issuers (collectively, the “Subsidiary Guarantors” and, together with the Parent Guarantor, the “Guarantors”), subject to automatic release under certain customary circumstances, including if the Subsidiary Guarantor is sold or sells all or substantially all of its assets, the Subsidiary Guarantor is designated “unrestricted” for covenant purposes under the indenture governing the Notes, the Subsidiary Guarantor's guarantee of other indebtedness which resulted in the creation of the guarantee of the Notes is terminated

or released, or the requirements for legal defeasance or covenant defeasance or to discharge the Indenture have been satisfied.

The following provides information regarding the entity structure of the Parent Guarantor, the Issuers and the Subsidiary Guarantors:

18

---

Table of Contents

CARETRUST REIT, INC.

NOTES TO CONDENSED CONSOLIDATED AND COMBINED FINANCIAL STATEMENTS —

(Unaudited)

CareTrust REIT, Inc. – The Parent Guarantor was formed on October 29, 2013 in anticipation of the Spin-Off and the related transactions and was a wholly owned subsidiary of Ensign prior to the effective date of the Spin-Off on June 1, 2014. The Parent Guarantor did not conduct any operations or have any business prior to the date of issuance of the Notes and the consummation of the Spin-Off related transactions.

CTR Partnership, L.P. and CareTrust Capital Corp. – The Issuers, each of which is a 100% owned subsidiary of the Parent Guarantor, were formed on May 8, 2014 and May 9, 2014, respectively, in anticipation of the Spin-Off and the related transactions. The Issuers did not conduct any operations or have any business prior to the date of issuance of the Notes and the consummation of the Spin-Off related transactions.

Subsidiary Guarantors – Each of the Subsidiary Guarantors is a 100% owned subsidiary of the Parent Guarantor. Prior to the consummation of the Spin-Off, each of the Subsidiary Guarantors was a wholly owned subsidiary of Ensign. The Ensign Properties entities consist of the Subsidiary Guarantors (other than the general partner of the Operating Partnership which was formed on May 8, 2014 in anticipation of the Spin-Off and the related transactions) and the subsidiaries of the Parent Guarantor that are not Subsidiary Guarantors or Issuers (collectively, the “Non-Guarantor Subsidiaries”).

Pursuant to Rule 3-10 of Regulation S-X, the following summarized consolidating information is provided for the Parent Guarantor, the Issuers, the Subsidiary Guarantors and the Non-Guarantor Subsidiaries with respect to the Notes. This summarized financial information has been prepared from the financial statements of the Company and Ensign Properties and the books and records maintained by the Company and Ensign Properties. As described above, the Parent Guarantor and the Issuers did not conduct any operations or have any business during the periods prior to June 1, 2014.

The summarized financial information may not necessarily be indicative of the results of operations or financial position had the Parent Guarantor, the Issuers, the Subsidiary Guarantors or the Non-Guarantor Subsidiaries all been in existence or operated as independent entities during the relevant period or had the Ensign Properties entities been operated as subsidiaries of the Parent Guarantor during such period.

Table of Contents

CARETRUST REIT, INC.

NOTES TO CONDENSED CONSOLIDATED AND COMBINED FINANCIAL STATEMENTS —

(Unaudited)

## CONDENSED CONSOLIDATING BALANCE SHEETS

JUNE 30, 2015

(in thousands, except share and per share amounts)

	Parent Guarantor	Issuers	Combined Subsidiary Guarantors	Combined Non- Guarantor Subsidiaries	Elimination	Consolidated
Assets:						
Real estate investments, net	\$—	\$59,790	\$357,318	\$42,407	\$—	\$459,515
Other real estate investments	—	—	7,987	—	—	7,987
Cash and cash equivalents	—	29,904	—	—	—	29,904
Accounts receivable	—	122	1,790	124	—	2,036
Prepaid expenses and other assets	133	2,155	4	—	—	2,292
Deferred financing costs, net	—	8,970	—	472	—	9,442
Investment in subsidiaries	113,243	350,032	—	—	(463,275 )	—
Intercompany	—	—	36,831	2,738	(39,569 )	—
Total assets	\$113,376	\$450,973	\$403,930	\$45,741	\$(502,844 )	\$511,176
Liabilities and Equity:						
Senior unsecured notes payable	\$—	\$260,000	\$—	\$—	\$—	\$260,000
Mortgage notes payable	—	—	507	96,347	—	96,854
Secured revolving credit facility	—	35,000	—	—	—	35,000
Accounts payable and accrued liabilities	—	3,161	2,219	566	—	5,946
Dividends payable	5,090	—	—	—	—	5,090
Intercompany	—	39,569	—	—	(39,569 )	—
Total liabilities	5,090	337,730	2,726	96,913	(39,569 )	402,890
Equity:						
Common stock, \$0.01 par value; 500,000,000 shares authorized, 31,306,782 shares issued and outstanding as of June 30, 2015	313	—	—	—	—	313
Additional paid-in capital	246,701	116,773	374,660	(52,899 )	(438,534 )	246,701
Cumulative distributions in excess of earnings	(138,728 )	(3,530 )	26,544	1,727	(24,741 )	(138,728 )
Total equity	108,286	113,243	401,204	(51,172 )	(463,275 )	108,286
Total liabilities and equity	\$113,376	\$450,973	\$403,930	\$45,741	\$(502,844 )	\$511,176

Table of Contents

CARETRUST REIT, INC.

NOTES TO CONDENSED CONSOLIDATED AND COMBINED FINANCIAL STATEMENTS —

(Unaudited)

## CONDENSED CONSOLIDATING BALANCE SHEETS

DECEMBER 31, 2014

(in thousands, except share and per share amounts)

	Parent Guarantor	Issuers	Combined Subsidiary Guarantors	Combined Non- Guarantor Subsidiaries	Elimination	Consolidated
<b>Assets:</b>						
Real estate investments, net	\$—	\$26,104	\$366,199	\$43,912	\$—	\$436,215
Other real estate investments	—	—	7,532	—	—	7,532
Cash and cash equivalents	—	25,320	—	—	—	25,320
Accounts receivable	—	—	2,170	121	—	2,291
Prepaid expenses and other assets	—	808	1	—	—	809
Deferred financing costs, net	—	9,808	—	597	—	10,405
Investment in subsidiaries	117,408	335,020	—	—	(452,428 )	—
Intercompany	—	—	15,262	1,323	(16,585 )	—
Total assets	\$117,408	\$397,060	\$391,164	\$45,953	\$(469,013 )	\$482,572
<b>Liabilities and Equity:</b>						
Senior unsecured notes payable	\$—	\$260,000	\$—	\$—	\$—	\$260,000
Mortgage notes payable	—	—	557	97,648	—	98,205
Accounts payable and accrued liabilities	—	3,067	3,308	584	—	6,959
Dividends payable	3,946	—	—	—	—	3,946
Intercompany	—	16,585	—	—	(16,585 )	—
Total liabilities	3,946	279,652	3,865	98,232	(16,585 )	369,110
<b>Equity:</b>						
Common stock, \$0.01 par value; 500,000,000 shares authorized, 31,251,157 shares issued and outstanding as of December 31, 2014	313	—	—	—	—	313
Additional paid-in capital	246,041	125,551	374,660	(52,899 )	(447,312 )	246,041
Cumulative distributions in excess of earnings	(132,892 )	(8,143 )	12,639	620	(5,116 )	(132,892 )
Total equity	113,462	117,408	387,299	(52,279 )	(452,428 )	113,462
Total liabilities and equity	\$117,408	\$397,060	\$391,164	\$45,953	\$(469,013 )	\$482,572

Table of Contents

CARETRUST REIT, INC.

NOTES TO CONDENSED CONSOLIDATED AND COMBINED FINANCIAL STATEMENTS —

(Unaudited)

## CONDENSED CONSOLIDATING STATEMENTS OF OPERATIONS

FOR THE THREE MONTHS ENDED JUNE 30, 2015

(in thousands)

	Parent Guarantor	Issuers	Combined Subsidiary Guarantors	Combined Non- Guarantor Subsidiaries	Elimination	Consolidated
Revenues:						
Rental income	\$—	\$1,249	\$11,275	\$2,725	\$—	\$15,249
Tenant reimbursements	—	77	1,095	116	—	1,288
Independent living facilities	—	—	607	—	—	607
Interest and other income	—	—	232	—	—	232
Total revenues	—	1,326	13,209	2,841	—	17,376
Expenses:						
Depreciation and amortization	—	413	4,519	747	—	5,679
Interest expense	—	4,573	8	1,408	—	5,989
Property taxes	—	77	1,095	116	—	1,288
Independent living facilities	—	—	566	—	—	566
General and administrative	309	1,157	95	27	—	1,588
Total expenses	309	6,220	6,283	2,298	—	15,110
Income in Subsidiary	2,575	7,469	—	—	(10,044 )	—
Net income	\$2,266	\$2,575	\$6,926	\$543	\$(10,044 )	\$2,266



Table of Contents

CARETRUST REIT, INC.

NOTES TO CONDENSED CONSOLIDATED AND COMBINED FINANCIAL STATEMENTS —

(Unaudited)

## CONDENSED CONSOLIDATING AND COMBINING STATEMENTS OF OPERATIONS

FOR THE THREE MONTHS ENDED JUNE 30, 2014

(in thousands)

	Parent Guarantor	Issuers	Combined Subsidiary Guarantors	Combined Non- Guarantor Subsidiaries	Elimination	Consolidated
Revenues:						
Rental income	\$—	\$—	\$10,252	\$1,953	\$—	\$12,205
Tenant reimbursements	—	—	1,112	125	—	1,237
Independent living facilities	—	—	623	—	—	623
Interest and other income	—	—	—	—	—	—
Total revenues	—	—	11,987	2,078	—	14,065
Expenses:						
Depreciation and amortization	—	—	5,145	925	—	6,070
Interest expense	—	1,491	3,868	1,093	—	6,452
Loss on extinguishment of debt	—	—	4,067	—	—	4,067
Property taxes	—	—	1,112	125	—	1,237
Independent living facilities	—	—	555	—	—	555
General and administrative	—	6,009	—	—	—	6,009
Total expenses	—	7,500	14,747	2,143	—	24,390
Loss in Subsidiary	(10,342 )	(2,842 )	—	—	13,184	—
Loss before provision for income taxes	(10,342 )	(10,342 )	(2,760 )	(65 )	13,184	(10,325 )
Provision for income taxes	—	—	22	(5 )	—	17
Net loss	\$(10,342 )	\$(10,342 )	\$(2,782 )	\$(60 )	\$13,184	\$(10,342 )

Table of Contents

CARETRUST REIT, INC.

NOTES TO CONDENSED CONSOLIDATED AND COMBINED FINANCIAL STATEMENTS —

(Unaudited)

## CONDENSED CONSOLIDATING STATEMENTS OF OPERATIONS

FOR THE SIX MONTHS ENDED JUNE 30, 2015

(in thousands)

	Parent Guarantor	Issuers	Combined Subsidiary Guarantors	Combined Non- Guarantor Subsidiaries	Elimination	Consolidated
Revenues:						
Rental income	\$—	\$2,091	\$22,550	\$5,450	\$—	\$30,091
Tenant reimbursements	—	129	2,185	232	—	2,546
Independent living facilities	—	—	1,242	—	—	1,242
Interest and other income	—	—	455	—	—	455
Total revenues	—	2,220	26,432	5,682	—	34,334
Expenses:						
Depreciation and amortization	—	708	9,063	1,507	—	11,278
Interest expense	—	9,065	16	2,809	—	11,890
Property taxes	—	129	2,185	232	—	2,546
Independent living facilities	—	—	1,168	—	—	1,168
General and administrative	309	2,717	95	27	—	3,148
Total expenses	309	12,619	12,527	4,575	—	30,030
Income in Subsidiary	4,613	15,012	—	—	(19,625 )	—
Net income	\$4,304	\$4,613	\$13,905	\$1,107	\$(19,625 )	\$4,304

Table of Contents

CARETRUST REIT, INC.

NOTES TO CONDENSED CONSOLIDATED AND COMBINED FINANCIAL STATEMENTS —

(Unaudited)

## CONDENSED CONSOLIDATING AND COMBINING STATEMENTS OF OPERATIONS

FOR THE SIX MONTHS ENDED JUNE 30, 2014

(in thousands)

	Parent Guarantor	Issuers	Combined Subsidiary Guarantors	Combined Non- Guarantor Subsidiaries	Elimination	Consolidated
Revenues:						
Rental income	\$—	\$—	\$19,787	\$3,441	\$—	\$23,228
Tenant reimbursements	—	—	2,245	253	—	2,498
Independent living facilities	—	—	1,210	—	—	1,210
Interest and other income	—	—	—	—	—	—
Total revenues	—	—	23,242	3,694	—	26,936
Expenses:						
Depreciation and amortization	—	—	10,416	1,853	—	12,269
Interest expense	—	1,492	6,283	2,004	—	9,779
Loss on extinguishment of debt	—	—	4,067	—	—	4,067
Property taxes	—	—	2,245	253	—	2,498
Independent living facilities	—	—	1,098	—	—	1,098
General and administrative	—	7,912	—	—	—	7,912
Total expenses	—	9,404	24,109	4,110	—	37,623
Loss in Subsidiary	(10,740 )	(1,336 )	—	—	12,076	—
Loss before provision for income taxes	(10,740 )	(10,740 )	(867 )	(416 )	12,076	(10,687 )
Provision for income taxes	—	—	53	—	—	53
Net loss	\$(10,740 )	\$(10,740 )	\$(920 )	\$(416 )	\$12,076	\$(10,740 )

Table of Contents

CARETRUST REIT, INC.

NOTES TO CONDENSED CONSOLIDATED AND COMBINED FINANCIAL STATEMENTS —

(Unaudited)

## CONDENSED CONSOLIDATING STATEMENTS OF CASH FLOWS

FOR THE SIX MONTHS ENDED JUNE 30, 2015

(in thousands)

	Parent Guarantor	Issuers	Combined Subsidiary Guarantors	Combined Non-Guarantor Subsidiaries	Elimination	Consolidated
Cash flows from operating activities:						
Net cash (used in) provided by operating activities	\$(149 )	\$(8,782 )	\$21,801	\$ 2,716	\$—	\$15,586
Cash flows from investing activities:						
Acquisition of real estate	—	(33,646 )	—	—	—	(33,646 )
Improvements to real estate	—	(20 )	(123 )	—	—	(143 )
Purchases of equipment, furniture, and fixtures	—	(167 )	(60 )	—	—	(227 )
Escrow deposit for acquisition of real estate	—	(1,500 )	—	—	—	(1,500 )
Distribution from subsidiary	8,996	—	—	—	(8,996 )	—
Intercompany financing	149	22,983	—	—	(23,132 )	—
Net cash provided by (used in) investing activities	9,145	(12,350 )	(183 )	—	(32,128 )	(35,516 )
Cash flows from financing activities:						
Borrowings under senior secured revolving credit facility	—	35,000	—	—	—	35,000
Payments on the mortgage notes payable	—	—	(50 )	(1,301 )	—	(1,351 )
Payments of deferred financing costs	—	(139 )	—	—	—	(139 )
Dividends paid on common stock	(8,996 )	—	—	—	—	(8,996 )
Distribution to Parent	—	(8,996 )	—	—	8,996	—
Intercompany financing	—	(149 )	(21,568 )	(1,415 )	23,132	—
Net cash (used in) provided by financing activities	(8,996 )	25,716	(21,618 )	(2,716 )	32,128	24,514
Net increase in cash and cash equivalents	—	4,584	—	—	—	4,584
Cash and cash equivalents beginning of period	—	25,320	—	—	—	25,320
Cash and cash equivalents end of period of period	\$—	\$29,904	\$—	\$ —	\$—	\$29,904



Table of Contents

CARETRUST REIT, INC.

NOTES TO CONDENSED CONSOLIDATED AND COMBINED FINANCIAL STATEMENTS —

(Unaudited)

## CONDENSED CONSOLIDATING AND COMBINING STATEMENTS OF CASH FLOWS

FOR THE SIX MONTHS ENDED JUNE 30, 2014

(in thousands)

	Parent Guarantor	Issuers	Combined Subsidiary Guarantors	Combined Non-Guarantor Subsidiaries	Elimination	Consolidated
Cash flows from operating activities:						
Net cash (used in) provided by operating activities	\$—	\$(1,492 )	\$15,394	\$ 1,563	\$(7,912 )	\$7,553
Cash flows from investing activities:						
Purchases of equipment, furniture, and fixtures	—	—	(14,648 )	(4,361 )	—	(19,009 )
Intercompany financing	—	(165,728 )	—	—	165,728	—
Net cash (used in) provided by investing activities	—	(165,728 )	(14,648 )	(4,361 )	165,728	(19,009 )
Cash flows from financing activities:						
Proceeds from the issuance of senior unsecured notes payable	—	260,000	—	—	—	260,000
Proceeds from the senior secured revolving credit facility	—	—	10,000	—	—	10,000
Proceeds from the issuance of mortgage notes payable	—	—	—	50,676	—	50,676
Payments on the senior secured revolving credit facility	—	—	(88,701 )	—	—	(88,701 )
Payments on the mortgage notes payable	—	—	(66,856 )	—	—	(66,856 )
Payments on the senior secured term loan	—	—	(65,624 )	—	—	(65,624 )
Payments of deferred financing costs	—	(12,435 )	—	(510 )	—	(12,945 )
Net contribution from Ensign	—	—	52,385	(48,029 )	—	4,356
Distributions to Issuers	—	—	(7,912 )	—	7,912	—
Intercompany financing	—	—	165,067	661	(165,728 )	—
Net cash provided by (used in) financing activities	—	247,565	(1,641 )	2,798	(157,816 )	90,906
Net increase (decrease) in cash and cash equivalents	—	80,345	(895 )	—	—	79,450
Cash and cash equivalents beginning of period	—	—	895	—	—	895
Cash and cash equivalents end of period of period	\$—	\$80,345	\$—	\$ —	\$—	\$80,345

14. SUBSEQUENT EVENTS

The Company evaluates subsequent events in accordance with ASC 855, Subsequent Events. The Company evaluates subsequent events up until the date the condensed consolidated and combined financial statements are issued.

27

---

Table of Contents

In July 2015, the Company acquired Bristol Court Assisted Living, a 70-unit/115-bed memory care facility located in St. Petersburg, Florida, for \$8.5 million and intends to account for this investment as an asset acquisition. Also in July 2015, the Company acquired Shamrock Nursing and Rehabilitation Center, a 105-bed skilled nursing facility located in Dublin, Georgia, for \$8.3 million and intends to account for this investment as an asset acquisition.

In July 2015, the Company paid off the \$0.5 million mortgage note payable to Johnson Land Enterprises, LLC.

In August 2015, the Company and certain of its wholly owned subsidiaries entered into a credit and guaranty agreement with KeyBank National Association, as administrative agent, an issuing bank and swingline lender, and the lenders party thereto (the “New Credit Agreement”). The New Credit Agreement provides for an unsecured asset-based revolving credit facility (the “New Credit Facility”) with commitments in an aggregate principal amount of \$300.0 million from a syndicate of banks and other financial institutions. A portion of the proceeds of the New Credit Facility were used to payoff and terminate the Company’s senior secured revolving credit facility.



Table of Contents

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

Forward-Looking Statements

Certain statements in this report may constitute forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995. Those forward-looking statements include all statements that are not historical statements of fact and those regarding our intent, belief or expectations, including, but not limited to, statements regarding: future financing plans, business strategies, growth prospects and operating and financial performance; expectations regarding the making of distributions and the payment of dividends; and compliance with and changes in governmental regulations.

Words such as “anticipate(s),” “expect(s),” “intend(s),” “plan(s),” “believe(s),” “may,” “will,” “would,” “could,” “should,” “seem,” “may be,” or similar expressions, or the negative of these terms, are intended to identify such forward-looking statements. These statements are based on management's current expectations and beliefs and are subject to a number of risks and uncertainties that could lead to actual results differing materially from those projected, forecasted or expected.

Although we believe that the assumptions underlying the forward-looking statements are reasonable, we can give no assurance that our expectations will be attained. Factors which could have a material adverse effect on our operations and future prospects or which could cause actual results to differ materially from our expectations include, but are not limited to: (i) the ability to achieve some or all of the benefits that we expect to achieve from the completed Spin-Off and our ability to successfully conduct our business following the Spin-Off; (ii) the ability and willingness of Ensign to meet and/or perform its obligations under the contractual arrangements that it entered into with us in connection with the Spin-Off, including the Ensign Master Leases (as defined below), and any of its obligations to indemnify, defend and hold us harmless from and against various claims, litigation and liabilities; (iii) the ability of our tenants to comply with laws, rules and regulations in the operation of the properties we lease to them; (iv) the ability and willingness of our tenants, including Ensign, to renew their leases with us upon their expiration, and the ability to reposition our properties on the same or better terms in the event of nonrenewal or in the event we replace an existing tenant, and obligations, including indemnification obligations, we may incur in connection with the replacement of an existing tenant; (v) the availability of and the ability to identify suitable acquisition opportunities and the ability to acquire and lease the respective properties on favorable terms; (vi) the ability to generate sufficient cash flows to service our outstanding indebtedness; (vii) access to debt and equity capital markets; (viii) fluctuating interest rates; (ix) the ability to retain our key management personnel; (x) the ability to qualify or maintain our status as a real estate investment trust (“REIT”); (xi) changes in the U.S. tax law and other state, federal or local laws, whether or not specific to REITs; (xii) other risks inherent in the real estate business, including potential liability relating to environmental matters and illiquidity of real estate investments; and (xiii) any additional factors included in this report, including in the section entitled “Risk Factors” in Item 1A of Part II of this report.

Forward-looking statements speak only as of the date of this report. Except in the normal course of our public disclosure obligations, we expressly disclaim any obligation to release publicly any updates or revisions to any forward-looking statements to reflect any change in our expectations or any change in events, conditions or circumstances on which any statement is based.

Overview

CareTrust REIT, Inc. (“CareTrust” or the “Company”) was formed on October 29, 2013, as a wholly owned subsidiary of The Ensign Group, Inc. (“Ensign”). On June 1, 2014, Ensign completed the separation of its healthcare business and its real estate business into two separate and independent publicly traded companies through the distribution of all of the outstanding shares of common stock to Ensign stockholders on a pro rata basis (the “Spin-Off”). The Spin-Off was effective from and after June 1, 2014, with shares of our common stock distributed to Ensign stockholders on June 2, 2014. CareTrust holds substantially all of the real property that was previously owned by Ensign. As of June 30, 2015, we owned and leased to independent operators, including Ensign, 102 skilled nursing, assisted living and independent living facilities which had a total of 10,647 operational beds located in Arizona, California, Colorado, Idaho, Iowa, Minnesota, Nebraska, Nevada, Texas, Utah, Virginia and Washington. We also own and operate three independent living facilities which had a total of 264 units located in Texas and Utah. As of June 30, 2015, we also had one other real estate investment, consisting of an \$8.0 million preferred equity investment.

We are a separate and independent publicly traded, self-administered, self-managed REIT primarily engaged in the ownership, acquisition and leasing of healthcare-related properties. We generate revenues primarily by leasing healthcare-related properties to healthcare operators in triple-net lease arrangements, under which the tenant is solely responsible for the costs related to the property (including property taxes, insurance, and maintenance and repair costs). We conduct and manage our business as one operating segment for internal reporting and internal decision making purposes. We expect to grow our portfolio by pursuing opportunities to acquire additional properties that will be leased to a diverse group of local, regional and

## Table of Contents

national healthcare providers, which may include Ensign, as well as senior housing operators and related businesses. We also anticipate diversifying our portfolio over time, including by acquiring properties in different geographic markets, and in different asset classes.

We expect to elect to be taxed and expect to qualify as a real estate investment trust (“REIT”) for U.S. federal income tax purposes commencing with our taxable year ended December 31, 2014. We operate through an umbrella partnership, commonly referred to as an UPREIT structure, in which substantially all of our properties and assets are held through CTR Partnership, L.P. (the “Operating Partnership”). The Operating Partnership is managed by CareTrust’s wholly owned subsidiary, CareTrust GP, LLC, which is the sole general partner of the Operating Partnership. To maintain REIT status, we must meet a number of organizational and operational requirements, including a requirement that we annually distribute to our stockholders at least 90% of our REIT taxable income, determined without regard to the dividends paid deduction and excluding any net capital gains.

### Components of our Revenues and Expenses

#### Revenues

Our earnings are primarily attributable to the rental revenue from the lease of our properties to Ensign pursuant to the Ensign Master Leases. The Ensign Master Leases consist of eight triple-net leases pursuant to which Ensign is responsible for all facility maintenance and repair, insurance required in connection with the leased properties and the business conducted on the leased properties, taxes levied on or with respect to the leased properties and all utilities and other services necessary or appropriate for the leased properties and the business conducted on the leased properties. The rent is a fixed component that was initially set near the time of the Spin-Off. The annual revenues from the Ensign Master Leases are currently \$56.0 million. Commencing June 1, 2016, the annual revenues from the Ensign Master Leases will be escalated annually by an amount equal to the product of (1) the lesser of the percentage change in the Consumer Price Index (but not less than zero) or 2.5%, and (2) the prior year’s rent.

#### General and Administrative Expenses

General and administrative costs consist of items such as compensation costs (including stock-based compensation expense), professional services, office costs and other costs associated with administrative activities. General and administrative expenses are anticipated to be approximately \$6.9 million to \$7.6 million in 2015, consisting of cash compensation, incentive-based cash compensation, professional services, administration and other costs. These amounts were determined based on the experience of management, our 13 months of operations after the Spin-Off and discussions with outside service providers, consultants and advisors. The amount of non-cash stock compensation expense to be incurred by us in 2015 relating to stock grants made in 2014 and 2015 is expected to be approximately \$1.6 million.

#### Depreciation and Amortization Expense

We incur depreciation and amortization expense for the property and equipment transferred to us from Ensign and for the real estate investments that closed after the Spin-Off. We expect such expense to be approximately \$23.0 million in 2015. This amount was determined based on annualizing the depreciation and amortization expense for the six months ended June 30, 2015 and adjusting for the real estate investments that have closed during 2015.

#### Revenues and Operating Expenses of Our Independent Living Operations

We own and operate three independent living facilities (“ILFs”). We anticipate these three ILFs will generate annual revenues of approximately \$2.5 million and incur annual operating expenses of approximately \$2.3 million in 2015. These amounts were determined based on annualizing the revenues and operating expenses of these facilities for the six months ended June 30, 2015.

#### Interest Expense

We incur interest expense from our borrowing obligations. Our debt outstanding as of June 30, 2015 was approximately \$391.9 million, and our annual interest costs are approximately \$24.4 million which includes amortization of deferred financing costs and a commitment fee on the unused portion of our senior secured revolving credit facility. Our weighted average interest rate is approximately 5.5%. See “— Liquidity and Capital Resources” below for more information.

#### Results of Operations



Table of Contents

## Basis of Presentation

Prior to the Spin-Off, the combined financial statements were prepared on a stand-alone basis and were derived from the accounting records of Ensign (which are not included in this report). These statements reflect the combined historical financial condition and results of operations of the carve-out business of the entities that own the skilled nursing facilities (“SNFs”), assisted living facilities (“ALFs”) and independent living facilities that we own, and the operations of the three ILFs that we operate, in accordance with U.S. generally accepted accounting principles (“GAAP”). Subsequent to the Spin-Off, the financial statements were prepared on a consolidated basis as the entities that own the properties are now wholly owned subsidiaries of the Company. All intercompany transactions and accounts have been eliminated.

## Operating Results

Three Months Ended June 30, 2015 Compared to Three Months Ended June 30, 2014:

	Three Months Ended June 30,		Increase (Decrease)	Percentage Difference	
	2015	2014			
	(dollars in thousands)				
Revenues:					
Rental income	\$ 15,249	\$ 12,205	\$ 3,044	25	%
Tenant reimbursements	1,288	1,237	51	4	%
Independent living facilities	607	623	(16)	(3)	)%
Interest and other income	232	—	232	*	
Expenses:					
Depreciation and amortization	5,679	6,070	(391)	(6)	)%
Interest expense	5,989	6,452	(463)	(7)	)%
Loss on extinguishment of debt	—	4,067	(4,067)	*	
Property taxes	1,288	1,237	51	4	%
Independent living facilities	566	555	11	2	%
General and administrative	1,588	6,009	(4,421)	(74)	)%
Provision for income taxes	—	17	(17)	*	

\* not meaningful

Rental income. Rental income was \$15.2 million for the three months ended June 30, 2015 compared to \$12.2 million for the three months ended June 30, 2014. The \$3.0 million increase in rental income is due to \$1.8 million in incremental new rent in place after the Spin-Off and \$1.2 million in rent due to new investments made after June 1, 2014.

Depreciation and amortization. Depreciation and amortization expense decreased \$0.4 million or 6% for the three months ended June 30, 2015 to \$5.7 million compared to \$6.1 million for the three months ended June 30, 2014. The \$0.4 million decrease in depreciation and amortization was primarily due to certain assets which were not transferred to the Company in connection with the Spin-Off, offset by new investments made after June 1, 2014.

Interest expense. Interest expense decreased \$0.5 million or 7% for the three months ended June 30, 2015 to \$6.0 million compared to \$6.5 million for the three months ended June 30, 2014. The decrease was due to a \$1.7 million loss on settlement of an interest rate swap in 2014 offset by higher net borrowings after the Spin-Off as compared to the prior year three month period.

General and administrative expense. General and administrative expense decreased \$4.4 million for the three months ended June 30, 2015 to \$1.6 million compared to \$6.0 million for the three months ended June 30, 2014. The \$4.4 million decrease is primarily related to decreases in legal and other costs related to the Spin-Off, offset by higher wages and amortization of stock-based compensation.

Six Months Ended June 30, 2015 Compared to Six Months Ended June 30, 2014:



Table of Contents

	Six Months Ended		Increase (Decrease)	Percentage Difference	
	June 30, 2015	2014			
	(dollars in thousands)				
Revenues:					
Rental income	\$30,091	\$23,228	\$6,863	30	%
Tenant reimbursements	2,546	2,498	48	2	%
Independent living facilities	1,242	1,210	32	3	%
Interest and other income	455	—	455	*	
Expenses:					
Depreciation and amortization	11,278	12,269	(991)	(8)	%)
Interest expense	11,890	9,779	2,111	22	%
Loss on extinguishment of debt	—	4,067	(4,067)	*	
Property taxes	2,546	2,498	48	2	%
Independent living facilities	1,168	1,098	70	6	%
General and administrative	3,148	7,912	(4,764)	(60)	%)
Provision for income taxes	—	53	(53)	*	

\* not meaningful

Rental income. Rental income was \$30.1 million for the six months ended June 30, 2015 compared to \$23.2 million for the six months ended June 30, 2014. The \$6.9 million increase in rental income is due to \$4.8 million in incremental new rent in place after the Spin-Off and \$2.1 million in rent due to new investments made after June 1, 2014.

Depreciation and amortization. Depreciation and amortization expense decreased \$1.0 million or 8% for the six months ended June 30, 2015 to \$11.3 million compared to \$12.3 million for the six months ended June 30, 2014. The \$1.0 million decrease in depreciation and amortization was primarily due to certain assets which were not transferred to the Company in connection with the Spin-Off, offset by new investments made after June 1, 2014.

Interest expense. Interest expense increased \$2.1 million or 22% for the six months ended June 30, 2015 to \$11.9 million compared to \$9.8 million for the six months ended June 30, 2014. The increase was due to higher net borrowings after the Spin-Off as compared to the prior year six month period offset by a \$1.7 million loss on the settlement of an interest rate swap in 2014.

General and administrative expense. General and administrative expense decreased \$4.8 million for the six months ended June 30, 2015 to \$3.1 million compared to \$7.9 million for the six months ended June 30, 2014. The \$4.8 million decrease is primarily related to decreases in legal and other costs related to the Spin-Off, offset by higher wages and amortization of stock-based compensation.

#### Liquidity and Capital Resources

We are required to distribute at least 90% of our REIT taxable income, determined without regard to the dividends paid deduction and excluding any net capital gains, to our stockholders on an annual basis in order to qualify as a REIT for federal income tax purposes. Accordingly, we intend to make, but are not contractually bound to make, regular quarterly dividends to common stockholders from cash flow from operating activities. All such dividends are at the discretion of our board of directors.

We believe that our available cash, expected operating cash flows and the availability under our Credit Facility will provide sufficient funds for our operations, anticipated scheduled debt service payments and dividend requirements for at least the next twelve months.

We intend to invest in additional healthcare properties as suitable opportunities arise and adequate sources of financing are available. We expect that future investments in properties, including any improvements or renovations of current or newly-acquired properties, will depend on and will be financed by, in whole or in part, our existing cash,

borrowings available to us under the Credit Facility, future borrowings or the proceeds from additional issuances of common stock or other

32

---



Table of Contents

securities. In addition, we may seek financing from U.S. government agencies, including through Fannie Mae and the U.S. Department of Housing and Urban Development, in appropriate circumstances in connection with acquisitions and refinancings of existing mortgage loans.

Although we are subject to restrictions on our ability to incur indebtedness, we expect that we will be able to refinance existing indebtedness or incur additional indebtedness for acquisitions or other purposes, if needed. However, there can be no assurance that we will be able to refinance our indebtedness, incur additional indebtedness or access additional sources of capital, such as by issuing common stock or other debt or equity securities, on terms that are acceptable to us or at all.

**Cash Flows**

The following table presents selected data from our condensed consolidated and combined statements of cash flows for the periods presented:

	Six Months Ended June 30,	
	2015	2014
	(dollars in thousands)	
Net cash provided by operating activities	\$15,586	\$7,553
Net cash used in investing activities	(35,516	) (19,009
Net cash provided by financing activities	24,514	90,906
Net increase in cash and cash equivalents	4,584	79,450
Cash and cash equivalents at beginning of period	25,320	895
Cash and cash equivalents at end of period	\$29,904	\$80,345

**Six Months Ended June 30, 2015 Compared to Six Months Ended June 30, 2014**

Net cash provided by operating activities for the six months ended June 30, 2015 was \$15.6 million compared to \$7.6 million for the six months ended June 30, 2014, an increase of \$8.0 million. The increase was primarily due to an increase in net income of \$15.0 million offset by a \$3.9 million change in non-cash expenses and a \$3.1 million change in operating assets and liabilities.

Net cash used in investing activities for the six months ended June 30, 2015 was \$35.5 million compared to \$19.0 million for the six months ended June 30, 2014, an increase of \$16.5 million. The increase was primarily the result of an \$33.8 million increase in acquisitions and a \$1.5 million increase in deposits, offset by a net \$18.8 million decrease in purchases of equipment, furniture and fixtures.

Net cash provided by financing activities for the six months ended June 30, 2015 was \$24.5 million compared to \$90.9 million for the six months ended June 30, 2014, a decrease of \$66.4 million. This decrease was due to lower net borrowings in 2015 of \$285.7 million, an increase in dividends paid of \$9.0 million and no net contributions from Ensign in 2015, offset by \$219.8 million in lower payments on debt and \$12.8 million in lower deferred financing fees.

**Indebtedness****Senior Unsecured Notes**

On May 30, 2014, the Operating Partnership, and its wholly owned subsidiary, CareTrust Capital Corp. (together with the Operating Partnership, the "Issuers"), completed a private offering of \$260.0 million aggregate principal amount of 5.875% Senior Notes due 2021 (the "Notes"). The Notes were issued at par, resulting in gross proceeds of \$260.0 million and net proceeds of approximately \$253.0 million after deducting underwriting fees and other offering expenses. We transferred approximately \$220.8 million of the net proceeds of the offering of the Notes to Ensign, and used the remaining net proceeds of the offering to pay the cash portion of the Special Dividend. The Notes mature on June 1, 2021 and bear interest at a rate of 5.875% per year. Interest on the Notes is payable on June 1 and December 1 of each year, beginning on December 1, 2014. The Issuers subsequently exchanged the Notes for substantially identical notes registered under the Securities Act of 1933.

The Issuers may redeem the Notes any time prior to June 1, 2017 at a redemption price of 100% of the principal amount of the Notes redeemed plus accrued and unpaid interest on the Notes, if any, to, but not including, the redemption date,

Table of Contents

plus a “make whole” premium described in the indenture governing the Notes and, at any time on or after June 1, 2017, at the redemption prices set forth in the indenture. In addition, at any time on or prior to June 1, 2017, up to 35% of the aggregate principal amount of the Notes may be redeemed with the net proceeds of certain equity offerings if at least 65% of the originally issued aggregate principal amount of the Notes remains outstanding. If certain changes of control of CareTrust occur, holders of the Notes will have the right to require the Issuers to repurchase their Notes at 101% of the principal amount plus accrued and unpaid interest, if any, to, but not including, the repurchase date.

The obligations under the Notes are fully and unconditionally guaranteed, jointly and severally, on an unsecured basis, by CareTrust and certain of CareTrust’s wholly owned existing and, subject to certain exceptions, future material subsidiaries (other than the Issuers); provided, however, that such guarantees are subject to automatic release under certain customary circumstances, including if the subsidiary guarantor is sold or sells all or substantially all of its assets, the subsidiary guarantor is designated “unrestricted” for covenant purposes under the indenture, the subsidiary guarantor’s guarantee of other indebtedness which resulted in the creation of the guarantee of the Notes is terminated or released, or the requirements for legal defeasance or covenant defeasance or to discharge the indenture have been satisfied. See Note 13, Summarized Condensed Consolidating and Combining Information.

The indenture contains covenants limiting the ability of CareTrust and its restricted subsidiaries to: incur or guarantee additional indebtedness; incur or guarantee secured indebtedness; pay dividends or distributions on, or redeem or repurchase, capital stock; make certain investments or other restricted payments; sell assets; enter into transactions with affiliates; merge or consolidate or sell all or substantially all of their assets; and create restrictions on the ability of the Issuers and their restricted subsidiaries to pay dividends or other amounts to the Issuers. The indenture also requires CareTrust and its restricted subsidiaries to maintain a specified ratio of unencumbered assets to unsecured indebtedness. These covenants are subject to a number of important and significant limitations, qualifications and exceptions. The indenture also contains customary events of default.

As of June 30, 2015, we were in compliance with all applicable financial covenants under the indenture.

Senior Secured Revolving Credit Facility

On May 30, 2014, the Operating Partnership entered into a credit and guaranty agreement (the “Credit Agreement”), which governs our Credit Facility, with several banks and other financial institutions and lenders (the “Lenders”) and Suntrust Bank, in its capacity as administrative agent for the Lenders, as an issuing bank and swingline lender. The Credit Agreement provides for a borrowing capacity of \$150.0 million and includes an accordion feature that allows the Operating Partnership to increase the borrowing availability by up to an additional \$75.0 million, subject to terms and conditions. The Credit Facility is secured by mortgages on certain of the real properties owned by the Company’s subsidiaries and the amount available to be borrowed under the Credit Agreement is based on a borrowing base calculation relating to the mortgaged properties, determined according to, among other factors, the mortgageability cash flow as such term is defined in the Credit Agreement. The Credit Facility is also secured by certain personal property of the Company’s subsidiaries that have provided mortgages, the Company’s interests in the Operating Partnership and the Company’s and its subsidiaries’ equity interests in the Company’s subsidiaries that have guaranteed the Operating Partnership’s obligations under the Credit Agreement. The Credit Agreement has a maturity date of May 30, 2018, and includes a one year extension option. As of June 30, 2015, there was \$35.0 million outstanding under the Credit Agreement.

Borrowings under the Credit Agreement bear interest on the outstanding principal amount at a rate equal to the applicable percentage plus, at the Operating Partnership’s option, either (a) LIBOR or (b) a base rate determined as the greater of (i) the prime lending rate, (ii) the Federal Funds Rate plus 0.5%, and (iii) one-month LIBOR plus 1.0% (referred to as the “Base Rate”). The applicable percentage for borrowings will vary based on the Consolidated Leverage Ratio, as defined in the Credit Agreement, and will range from 2.0% to 2.5% per annum for LIBOR based borrowings and 1.0% to 1.5% per annum for borrowings at the Base Rate. In addition, the Operating Partnership is required to pay a commitment fee to the lenders equal to between 0.35% and 0.50% per annum based on the amount of unused borrowings under the Credit Agreement. During the three and six months ended June 30, 2015, the Company incurred \$0.2 million and \$0.4 million of commitment fees, respectively.

The obligations of the Operating Partnership under the Credit Agreement are guaranteed by the Company and certain subsidiaries of the Company.

The Credit Agreement contains customary covenants that include restrictions or limitations on the ability to make acquisitions and other investments, make distributions, incur additional indebtedness, engage in non-healthcare related business activities, enter into transactions with affiliates and sell or otherwise transfer certain assets as well as customary events of

Table of Contents

default. The Credit Agreement also requires the Company, through the Operating Partnership, to comply with specified financial covenants, which include a maximum debt to asset value ratio, a maximum secured debt to asset value ratio, a maximum secured recourse debt to asset value ratio, a minimum fixed charge coverage ratio and a minimum tangible net worth requirement.

As of June 30, 2015, the Company was in compliance with all applicable financial covenants under the Credit Agreement.

**GECC Loan**

Ten of our properties are subject to secured mortgage indebtedness to General Electric Capital Corporation (the "GECC Loan"), which we assumed in connection with the Spin-Off. The outstanding amount of this mortgage indebtedness was approximately \$96.4 million as of June 30, 2015, including an advance of approximately \$50.7 million that was made on May 30, 2014. This advance bears interest at a floating rate equal to three-month LIBOR plus 3.35%, reset monthly and subject to a LIBOR floor of 0.50%, with monthly principal and interest payments based on a 25 year amortization. The remaining indebtedness under the GECC Loan bears interest at a blended rate of 7.25% per annum until, but not including, June 29, 2016, and then converts to the floating rate described above. The GECC Loan matures on May 30, 2017, subject to two 12-month extension options, the exercise of which is conditioned, in each case, on the absence of any then-existing default and the payment of an extension fee equal to 0.25% of the then-outstanding principal balance. Provided there is no then-existing default and upon 30 days written notice, the original portion of the GECC Loan, approximately \$46.9 million as of June 30, 2015, is prepayable without penalty, in whole but not in part, after January 31, 2016. The new portion of the GECC Loan, approximately \$49.5 million as of June 30, 2015, is prepayable without penalty, in whole but not in part, after January 31, 2016. The GECC Loan is guaranteed by the Company, contains customary affirmative and negative covenants, as well as customary events of default, and requires us to comply with specified financial maintenance covenants.

As of June 30, 2015, the Company was in compliance with all applicable financial covenants under the GECC Loan.

**Obligations and Commitments**

The following table summarizes our contractual obligations and commitments at June 30, 2015 (in thousands):

	Payments Due by Period				
	Total	Less than 1 Year	1 Year to Less than 3 Years	3 Years to Less than 5 Years	More than 5 years
Senior Unsecured Notes (1)	\$351,650	\$15,275	\$30,550	\$30,550	\$275,275
Credit Facility (2)	39,487	1,541	37,946	—	—
Mortgage Notes Payable (3)	107,367	8,142	99,047	178	—
Operating lease	492	101	210	181	—
Total	\$498,996	\$25,059	\$167,753	\$30,909	\$275,275

(1) Amounts include interest payments of \$91.7 million.

(2) The credit facility includes payments related to the unused revolving credit facility fee due on the amount of unused borrowings.

(3) Amounts include interest payments of \$10.5 million.

**Capital Expenditures**

We anticipate incurring average annual capital expenditures of \$400 to \$500 per unit in connection with the operations of our three ILFs. Capital expenditures for each property leased under our triple-net leases are generally the responsibility of the tenant, except that, for the Ensign Master Leases, the tenant will have an option to require us to finance certain capital expenditures up to an aggregate of 20% of our initial investment in such property.

## Table of Contents

### Critical Accounting Policies and Estimates

Our Condensed Consolidated and Combined Financial Statements included in Item 1 of this Quarterly Report on Form 10-Q have been prepared in accordance with U.S. generally accepted accounting principles (“GAAP”) for interim financial information set forth in the Accounting Standards Codification (“ASC”), as published by the Financial Accounting Standards Board (“FASB”). GAAP requires us to make estimates and assumptions regarding future events that affect the reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting periods. We base these estimates on our experience and assumptions we believe to be reasonable under the circumstances. However, if our judgment or interpretation of the facts and circumstances relating to various transactions or other matters had been different, we may have applied a different accounting treatment, resulting in a different presentation of our financial statements. We periodically reevaluate our estimates and assumptions, and in the event they prove to be different from actual results, we make adjustments in subsequent periods to reflect more current estimates and assumptions about matters that are inherently uncertain. Please refer to our Annual Report on Form 10-K for the year ended December 31, 2014, filed with the SEC on February 11, 2015, for further information regarding the critical accounting policies that affect our more significant estimates and judgments used in the preparation of our Condensed Consolidated and Combined Financial Statements included in Part I, Item 1 of this Quarterly Report on Form 10-Q.

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

Our primary market risk exposure is interest rate risk with respect to our variable rate indebtedness. Approximately \$49.5 million of the GECC Loan bears interest at a floating rate equal to three-month LIBOR plus 3.35%, reset monthly and subject to a LIBOR floor of 0.50%, with monthly principal and interest payments based on a 25 year amortization. The remaining approximately \$46.9 million of the GECC Loan bears interest at a blended rate of 7.25% per annum until, but not including, June 29, 2016, and thereafter at the floating rate described above.

Our Credit Agreement provides for revolving commitments in an aggregate principal amount of \$150.0 million from a syndicate of banks and other financial institutions. At June 30, 2015, we had \$84.2 million in borrowings available under the Credit Facility (given the borrowing base requirements of the Credit Agreement), and \$35.0 million of outstanding borrowings under the Credit Facility. The interest rates per annum applicable to loans under the Credit Facility are, at the Operating Partnership’s option, equal to either a base rate plus a margin ranging from 1.00% to 1.50% per annum or LIBOR plus a margin ranging from 2.00% to 2.50% per annum, based on the debt to asset value ratio of the Operating Partnership and its subsidiaries.

An increase in interest rates could make the financing of any acquisition by us more costly as well as increase the costs of our variable rate debt obligations. Rising interest rates could also limit our ability to refinance our debt when it matures or cause us to pay higher interest rates upon refinancing and increase interest expense on refinanced indebtedness. Assuming a 100 basis point increase in the interest rates related to our variable rate debt, and assuming no change in our outstanding debt balance as described above, interest expense would have increased \$0.4 million for the six months ended June 30, 2015.

We may, in the future, manage, or hedge, interest rate risks related to our borrowings by means of interest rate swap agreements. However, the REIT provisions of the Code substantially limit our ability to hedge our assets and liabilities. See “Risk Factors — Risks Related to Our Status as a REIT — Complying with REIT requirements may limit our ability to hedge effectively and may cause us to incur tax liabilities.” As of June 30, 2015, we had no swap agreements to hedge our interest rate risks. We also expect to manage our exposure to interest rate risk by maintaining a mix of fixed and variable rates for our indebtedness.

### Item 4. Controls and Procedures.

#### Disclosure Controls and Procedures

We maintain disclosure controls and procedures (as such term is defined in Rules 13a-15(e) and 15d-15(e) under the Exchange Act) that are designed to ensure that information required to be disclosed in our reports under the Exchange

Act is processed, recorded, summarized and reported within the time periods specified in the SEC's rules and regulations and that such information is accumulated and communicated to management, including our Chief Executive Officer and Chief Financial Officer, as appropriate, to allow for timely decisions regarding required disclosure. In designing and evaluating the disclosure

Table of Contents

controls and procedures, management recognizes that any controls and procedures, no matter how well designed and operated, can provide only reasonable assurance of achieving the desired control objectives, and management is required to apply its judgment in evaluating the cost-benefit relationship of possible controls and procedures.

As of June 30, 2015, we carried out an evaluation, under the supervision and with the participation of management, including our Chief Executive Officer and Chief Financial Officer, regarding the effectiveness of our disclosure controls and procedures. Based on the foregoing, our Chief Executive Officer and Chief Financial Officer concluded that our disclosure controls and procedures were effective as of June 30, 2015.

**Changes in Internal Control over Financial Reporting**

There has been no change in our internal control over financial reporting (as such term is defined in Rules 13a-15(f) and 15d-15(f) under the Exchange Act) that occurred during the quarter ended June 30, 2015, that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

**PART II—OTHER INFORMATION**

**Item 1. Legal Proceedings.**

None of the Company or any of its subsidiaries is a party to, and none of their respective properties are the subject of, any material legal proceedings.

**Item 1A. Risk Factors.**

We have disclosed under the heading “Risk Factors” in our Annual Report on Form 10-K for the year ended December 31, 2014 risk factors which materially affect our business, financial condition, or results of operations. There have been no material changes from the risk factors previously disclosed.

**Item 6. Exhibits.**



Table of Contents

Exhibit Number	Description of the Document
2.1	Separation and Distribution Agreement, dated as of May 23, 2014, by and between The Ensign Group, Inc. and CareTrust REIT, Inc. (Exhibit 2.1 to the Company's Current Report on Form 8-K, filed on June 5, 2014, is incorporated herein by reference).
3.1	Articles of Amendment and Restatement of CareTrust REIT, Inc. (Exhibit 3.1 to the Company's Registration Statement on Form 10, filed on May 13, 2014, is incorporated herein by reference).
3.2	Amended and Restated Bylaws of CareTrust REIT, Inc. (Exhibit 3.2 to the Company's Registration Statement on Form 10, filed on May 13, 2014, is incorporated herein by reference).
4.1	Indenture, dated as of May 30, 2014, among CTR Partnership, L.P. and CareTrust Capital Corp., as Issuers, the guarantors named therein, and Wells Fargo Bank, National Association, as Trustee (Exhibit 4.1 to the Company's Current Report on Form 8-K, filed on June 5, 2014, is incorporated herein by reference).
4.2	Form of Note (included in Exhibit 4.1 above).
4.3	Specimen Stock Certificate of CareTrust REIT, Inc. (incorporated by reference to Exhibit 4.1 to CareTrust REIT, Inc.'s Registration Statement on Form 10, filed on April 15, 2014).
31.1	Certification of Chief Executive Officer, as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
31.2	Certification of Chief Financial Officer, as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
32	Certification of Chief Executive Officer and Chief Financial Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
**101.INS	XBRL Instance Document
**101.SCH	XBRL Taxonomy Extension Schema Document
**101.CAL	XBRL Taxonomy Extension Calculation Linkbase Document
**101.DEF	XBRL Taxonomy Extension Definition Linkbase Document
**101.LAB	XBRL Taxonomy Extension Label Linkbase Document
**101.PRE	XBRL Taxonomy Extension Presentation Linkbase Document
**XBRL	(Extensible Business Reporting Language) information is furnished and not filed or a part of a registration statement or prospectus for purposes of Sections 11 or 12 of the Securities Act of 1933, is deemed not filed for purposes of Section 18 of the Securities Exchange Act of

Edgar Filing: CareTrust REIT, Inc. - Form 10-Q  
1934, and otherwise is not subject to liability under these sections

Table of Contents

SIGNATURES

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

August 10, 2015	CareTrust REIT, Inc. By: /s/ Gregory K. Stapley Gregory K. Stapley President and Chief Executive Officer (duly authorized officer)
August 10, 2015	By: /s/ William M. Wagner William M. Wagner Chief Financial Officer, Treasurer and Secretary (principal financial officer and principal accounting officer)