FISCAL YEAR ENDED: 12 / 31 / 14

ANNUAL REPORT CHECKLIST

RECEIVED
MAY 05 2015
CONTINUING CARE CONTRACTS BRANCH

PROVIDER(S): FOUNTAINS SENIOR LIVING HOLDINGS, LLC

CCRC(S): THE FOUNTAINS AT THE CARLOTTA
41-505 CARLOTTA DRIVE, PALM DESERT, CA 92211

CONTACT PERSON: Julie Noonan, CPA

TELEPHONE NO.: (520) 240-0089 **EMAIL:** jnoonan@watermarkcommunities.com

● ●

A complete annual report must consist of *3 copies* of all of the following:

☑ Annual Report Checklist.

☑ Annual Provider Fee in the amount of: $ 9,092.00

- ☐ If applicable, late fee in the amount of: $____

☑ Certification by the provider's ***Chief Executive Officer*** that:
- ☑ The reports are correct to the best of his/her knowledge.
- ☑ Each continuing care contract form in use or offered to new residents has been approved by the Department.
- ☑ The provider is maintaining the required *liquid* reserves and, when applicable, the required refund reserve.

☑ Evidence of the provider's fidelity bond, as required by H&SC section 1789.8.

☑ Provider's audited financial statements, with an accompanying certified public accountant's opinion thereon.

☑ Provider's audited reserve reports (prepared on Department forms), with an accompanying certified public accountant's opinion thereon.

☑ Provider's "Continuing Care Retirement Community Disclosure Statement" and Form 7-1 "Report on CCRC Monthly Service Fees" for ***each*** community.

☐ Provider's Refund Reserve Calculation(s) – Form 9-1 and/or Form 9-2, if applicable.

The Key Indicators Report is required to be submitted within 30 days of the due date of the submission of the annual report, but may be submitted at the same time as the annual report.

FORM 1-1
RESIDENT POPULATION

Line	Continuing Care Residents	TOTAL
[1]	Number at beginning of fiscal year	172
[2]	Number at end of fiscal year	173
[3]	Total Lines 1 and 2	345
[4]	Multiply Line 3 by ".50" and enter result on Line 5.	x .50
[5]	Mean number of continuing care residents	172.5
	All Residents	
[6]	Number at beginning of fiscal year	245
[7]	Number at end of fiscal year	245
[8]	Total Lines 6 and 7	490
[9]	Multiply Line 8 by ".50" and enter result on Line 10.	x .50
[10]	Mean number of *all* residents	245
[11]	Divide the mean number of continuing care residents (Line 5) by the mean number of *all* residents (Line 10) and enter the result (round to two decimal places).	0.70

FORM 1-2
ANNUAL PROVIDER FEE

Line			TOTAL
[1]	Total Operating Expenses (including depreciation and debt service - interest only)		$15,143,842
[a]	Depreciation	$1,289,197	
[b]	Debt Service (Interest Only)	$940,765	
[2]	Subtotal (add Line 1a and 1b)		$2,229,962
[3]	Subtract Line 2 from Line 1 and enter result.		$12,913,880
[4]	Percentage allocated to continuing care residents (Form 1-1, Line 11)		70%
[5]	Total Operating Expense for Continuing Care Residents (multiply Line 3 by Line 4)		$9,092,426
			x .001
[6]	**Total Amount Due** (multiply Line 5 by .001)		$9,092

PROVIDE| Fountains Senior Living Holdings, LLC
COMMUN| The Fountains at The Carlotta

Fountains Senior Living Holdings, LLC

RECEIVED
MAY 05 2015
CONTINUING CARE
CONTRACTS BRANCH

April 30, 2015

California Department of Social Services
Continuing Care Contracts Branch
744 P Street, MS 10-90
Sacramento, CA 95814
ATTN: Allison Nakatomi

Dear Ms. Nakatomi:

This letter will serve as certification on behalf of Fountains General Partner, LLC and Fountains Senior Living Holdings, LLC to the California Department of Social Services of the following matters regarding the enclosed annual report for 2013 that Fountains Senior Living Holdings, LLC is submitting as the holder of a certificate of authority for Fountains at The Carlotta:

1. The accompanying annual report is correct to the best of my knowledge.

2. Each continuing care contract form in use or offered to new residents at The Fountains at the Carlotta has been approved by the Department.

3. As of December 31, 2014, Fountains Senior Living Holdings, LLC did maintain the liquid reserves required by California law, which are reflected on the Fountains Senior Living Holdings, LLC consolidated audited financials for the year ended December 31, 2014.

Please feel free to contact us if you have any questions about our submissions.

Sincerely,

Michael K. Casey

Michael K. Casey
Vice President
US Senior Living Investments, LLC
(Sole member of Fountains Senior Living Holdings, LLC,
the parent of Fountains Carlotta SL, LP)

ACORD®

CERTIFICATE OF LIABILITY INSURANCE

DATE (MM/DD/YYYY): 04/21/2015

RECEIVED MAY 05 2015 CONTINUING CARE CONTRACTS BRANCH

THIS CERTIFICATE IS ISSUED AS A MATTER OF INFORMATION ONLY AND CONFERS NO RIGHTS UPON THE CERTIFICATE HOLDER. THIS CERTIFICATE DOES NOT AFFIRMATIVELY OR NEGATIVELY AMEND, EXTEND OR ALTER THE COVERAGE AFFORDED BY THE POLICIES BELOW. THIS CERTIFICATE OF INSURANCE DOES NOT CONSTITUTE A CONTRACT BETWEEN THE ISSUING INSURER(S), AUTHORIZED REPRESENTATIVE OR PRODUCER, AND THE CERTIFICATE HOLDER.

IMPORTANT: If the certificate holder is an ADDITIONAL INSURED, the policy(ies) must be endorsed. If SUBROGATION IS WAIVED, subject to the terms and conditions of the policy, certain policies may require an endorsement. A statement on this certificate does not confer rights to the certificate holder in lieu of such endorsement(s).

PRODUCER MCGRIFF, SEIBELS & WILLIAMS, INC. P.O. Box 10265 Birmingham, AL 35202	**CONTACT NAME:** **PHONE (A/C, No, Ext):** 800-476-2211 **FAX (A/C, No):** **E-MAIL ADDRESS:**

INSURER(S) AFFORDING COVERAGE	NAIC #
INSURER A : National Union Fire Ins. Co of Pittsburgh PA	
INSURER B : American Zurich Insurance Company	40142
INSURER C :	
INSURER D :	
INSURER E :	
INSURER F :	

INSURED
Fountains Senior Living Holdings LLC c/o Watermark Retirement Communities, Inc. and Watermark Services IV, LLC
2020 W. Rudasill Road
Tuscon, AZ 85704

COVERAGES **CERTIFICATE NUMBER:** Y33DVQ5A **REVISION NUMBER:**

THIS IS TO CERTIFY THAT THE POLICIES OF INSURANCE LISTED BELOW HAVE BEEN ISSUED TO THE INSURED NAMED ABOVE FOR THE POLICY PERIOD INDICATED. NOTWITHSTANDING ANY REQUIREMENT, TERM OR CONDITION OF ANY CONTRACT OR OTHER DOCUMENT WITH RESPECT TO WHICH THIS CERTIFICATE MAY BE ISSUED OR MAY PERTAIN, THE INSURANCE AFFORDED BY THE POLICIES DESCRIBED HEREIN IS SUBJECT TO ALL THE TERMS, EXCLUSIONS AND CONDITIONS OF SUCH POLICIES. LIMITS SHOWN MAY HAVE BEEN REDUCED BY PAID CLAIMS.

INSR LTR	TYPE OF INSURANCE	ADDL INSD	SUBR WVD	POLICY NUMBER	POLICY EFF (MM/DD/YYYY)	POLICY EXP (MM/DD/YYYY)	LIMITS	
	COMMERCIAL GENERAL LIABILITY CLAIMS-MADE / OCCUR GEN'L AGGREGATE LIMIT APPLIES PER: POLICY / PRO-JECT / LOC OTHER:						EACH OCCURRENCE DAMAGE TO RENTED PREMISES (Ea occurrence) MED EXP (Any one person) PERSONAL & ADV INJURY GENERAL AGGREGATE PRODUCTS - COMP/OP AGG	\$ \$ \$ \$ \$ \$ \$
	AUTOMOBILE LIABILITY ANY AUTO ALL OWNED AUTOS / SCHEDULED AUTOS HIRED AUTOS / NON-OWNED AUTOS						COMBINED SINGLE LIMIT (Ea accident) BODILY INJURY (Per person) BODILY INJURY (Per accident) PROPERTY DAMAGE (Per accident)	\$ \$ \$ \$ \$
	UMBRELLA LIAB / OCCUR EXCESS LIAB / CLAIMS-MADE DED / RETENTION \$						EACH OCCURRENCE AGGREGATE	\$ \$ \$
B	WORKERS COMPENSATION AND EMPLOYERS' LIABILITY Y/N ANY PROPRIETOR/PARTNER/EXECUTIVE OFFICER/MEMBER EXCLUDED? (Mandatory in NH) If yes, describe under DESCRIPTION OF OPERATIONS below	N/A		WC593317101	02/01/2015	09/01/2015	X PER STATUTE / OTH-ER E.L. EACH ACCIDENT E.L. DISEASE - EA EMPLOYEE E.L. DISEASE - POLICY LIMIT	 \$ 1,000,000 \$ 1,000,000 \$ 1,000,000
A	Employment Practices Liability Ins and Crime Insurance			82868617	04/01/2015	04/01/2016	EPL Limit Crime Limit	\$ 10,000,000 \$ 3,000,000 \$ \$ \$

DESCRIPTION OF OPERATIONS / LOCATIONS / VEHICLES (ACORD 101, Additional Remarks Schedule, may be attached if more space is required)

RE: Fountains Carlotta SL, LP f/k/a Sunrise IV Carlotta SL, LP d/b/a The Fountains at the Carlotta

Employment Practices: $250,000 Retention for Class Action & Third Party; $150,000 for other loss
Crime: $25,000 deductible
Workers' Compensation is Guaranteed Cost

CERTIFICATE HOLDER	CANCELLATION
Evidence of Coverage	**SHOULD ANY OF THE ABOVE DESCRIBED POLICIES BE CANCELLED BEFORE THE EXPIRATION DATE THEREOF, NOTICE WILL BE DELIVERED IN ACCORDANCE WITH THE POLICY PROVISIONS.** AUTHORIZED REPRESENTATIVE

KPMG

FOUNTAINS CARLOTTA SL, L.P.

(d/b/a The Fountains at The Carlotta)

(A Wholly Owned Subsidiary of Fountains Senior Living Holdings, LLC)

Financial Statements

December 31, 2014 and 2013

(With Independent Auditors' Report Thereon)

FOUNTAINS CARLOTTA SL, L.P.
(d/b/a The Fountains at The Carlotta)
(A Wholly Owned Subsidiary of Fountains Senior Living Holdings, LLC)

Table of Contents

	Page
Independent Auditors' Report	1
Financial Statements:	
Balance Sheets	2–3
Statements of Operations	4
Statements of Changes in Partners' Deficit	5
Statements of Cash Flows	6–7
Notes to Financial Statements	8–19

KPMG LLP
Suite 800
60 East Rio Salado Parkway
Tempe, AZ 85281-9125

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MAY 05 2015
CONTINUING CARE
CONTRACTS BRANCH

Independent Auditors' Report

The Partners
Fountains Carlotta SL, L.P.:

We have audited the accompanying financial statements of Fountains Carlotta SL, L.P. (a wholly owned subsidiary of Fountains Senior Living Holdings, LLC), which comprise the balance sheets as of December 31, 2014 and 2013, and the related statements of operations, changes in partners' deficit, and cash flows for the years then ended, and the related notes to the financial statements.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with U.S. generally accepted accounting principles; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditors' Responsibility

Our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditors' judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Fountains Carlotta SL, L.P. as of December 31, 2014 and 2013, and the results of its operations and its cash flows for the years then ended, in accordance with U.S. generally accepted accounting principles.

KPMG LLP

Phoenix, Arizona
April 30, 2015

FOUNTAINS CARLOTTA SL, L.P.
(d/b/a The Fountains at The Carlotta)
(A Wholly Owned Subsidiary of Fountains Senior Living Holdings, LLC)

Balance Sheets

December 31, 2014 and 2013

Assets		**2014**	**2013**
Current assets:			
Cash	$	475,651	793,438
Accounts receivable – less allowance for doubtful accounts of $156,000 and $668,000 at December 31, 2014 and 2013, respectively		954,836	844,855
Prepaid expenses and other current assets		237,560	257,484
Total current assets		1,668,047	1,895,777
Property and equipment:			
Land and land improvements		5,904,878	5,887,626
Buildings and improvements		16,262,626	14,239,391
Furniture, fixtures, and equipment		4,758,384	4,385,788
Construction in progress		98,643	44,601
Total property and equipment		27,024,531	24,557,406
Less accumulated depreciation and amortization		(6,568,620)	(5,279,423)
Property and equipment – net		20,455,911	19,277,983
Restricted cash		7,175	10,779
Other assets		220,516	167,608
Deferred financing costs – less accumulated amortization of $186,114 and $103,397 at December 31, 2014 and 2013, respectively		26,284	82,717
Total – pledged for parent company debt (notes 6 and 8)	$	22,377,933	21,434,864

(Continued)

FOUNTAINS CARLOTTA SL, L.P.
(d/b/a The Fountains at The Carlotta)
(A Wholly Owned Subsidiary of Fountains Senior Living Holdings, LLC)

Balance Sheets

December 31, 2014 and 2013

Liabilities and Partners' Deficit	**2014**	**2013**
Current liabilities:		
Accounts payable and accrued expenses	$ 990,817	996,719
Security and reservation deposits	135,032	93,955
Accrued interest	2,309	2,706
Refundable entrance fees	2,039,857	1,880,011
Insurance liability reserves	106,560	269,495
Derivative liability	—	31,954
Current maturities of note payable	21,134,332	1,051,291
Capital lease obligation	9,699	9,130
Total current liabilities	24,418,606	4,335,261
Long-term liabilities:		
Note payable – less current maturities	—	21,638,678
Capital lease obligation – less current maturities	26,014	35,713
Deferred revenue	66,406	55,007
Insurance liability reserves – less current portion	460,400	329,245
Refundable entrance fees – less current portion	10,709,252	9,870,058
Unearned nonrefundable entrance fees	5,531,196	4,786,672
Total long-term liabilities	16,793,268	36,715,373
Total liabilities	41,211,874	41,050,634
Commitments and contingencies (note 8)		
Partners' deficit	(18,833,941)	(19,615,770)
Total	$ 22,377,933	21,434,864

See accompanying notes to financial statements.

FOUNTAINS CARLOTTA SL, L.P.
(d/b/a The Fountains at The Carlotta)
(A Wholly Owned Subsidiary of Fountains Senior Living Holdings, LLC)

Statements of Operations

Years ended December 31, 2014 and 2013

		2014	2013
Operating revenue:			
Healthcare revenue, net of contractual allowances	$	6,506,095	6,378,005
Provision for bad debts (note 3)		(30,038)	(162,244)
Healthcare revenue, net		6,476,057	6,215,761
Resident fees		6,625,509	6,143,758
Amortization of entrance fees		1,146,283	1,159,808
Other operating income		170,113	112,379
Total operating revenue		14,417,962	13,631,706
Operating expenses:			
Wages and benefits		5,719,274	5,542,848
Depreciation		1,289,197	1,009,973
Ancillary/therapy expenses		1,833,279	1,893,555
General and administrative		302,681	517,609
Food		600,965	587,610
Supplies		169,493	203,214
Utilities		764,050	661,057
Insurance		429,269	499,159
Taxes and license fees		363,689	376,635
Repairs and maintenance		743,099	754,769
Gain on disposal of assets		(250)	—
Lease expense		37,339	44,165
Management fees		722,400	689,697
Occupancy costs		265,638	253,622
Professional services		962,954	652,995
Total operating expenses		14,203,077	13,686,908
Income (loss) from operations		214,885	(55,202)
Other (expense) income:			
Interest expense		(940,765)	(989,940)
Change in fair value of interest rate swap agreements		31,954	10,492
Interest income		36	67
Other expense		(119,859)	(7,585)
Total other expense		(1,028,634)	(986,966)
Net loss	$	(813,749)	(1,042,168)

See accompanying notes to financial statements.

FOUNTAINS CARLOTTA SL, L.P.
(d/b/a The Fountains at The Carlotta)
(A Wholly Owned Subsidiary of Fountains Senior Living Holdings, LLC)

Statements of Changes in Partners' Deficit

Years ended December 31, 2014 and 2013

Partners' deficit – December 31, 2012	$ (18,127,141)
Distributions – net	(446,461)
Net loss	(1,042,168)
Partners' deficit – December 31, 2013	(19,615,770)
Contributions – net	1,595,578
Net loss	(813,749)
Partners' deficit – December 31, 2014	$ (18,833,941)

See accompanying notes to financial statements.

FOUNTAINS CARLOTTA SL, L.P.
(d/b/a The Fountains at The Carlotta)
(A Wholly Owned Subsidiary of Fountains Senior Living Holdings, LLC)

Statements of Cash Flows

Years ended December 31, 2014 and 2013

		2014	2013
Cash flows from operating activities:			
Cash received from residents and third-party payors	$	13,041,371	13,155,896
Entrance fees received		4,326,000	4,557,511
Interest received		36	67
Cash paid to suppliers and employees		(10,365,650)	(11,946,115)
Interest paid		(928,243)	(971,741)
Net cash provided by operating activities		6,073,514	4,795,618
Cash flows used in investing activities:			
(Decrease) increase in restricted cash		3,604	(4,965)
Purchases of property and equipment		(2,461,520)	(1,220,810)
Net cash used in investing activities		(2,457,916)	(1,225,775)
Cash flows used in financing activities:			
Refunds of entrance fees		(1,319,397)	(1,720,867)
Principal payments on note payable		(540,121)	(459,459)
Principal payments on installment loan		—	(41,616)
Principal payments on capital lease obligation		(9,130)	(5,328)
(Distributions)/contributions – net		(2,064,737)	(1,251,564)
Net cash used in financing activities		(3,933,385)	(3,478,834)
Net (decrease) increase in cash		(317,787)	91,009
Cash – beginning of year		793,438	702,429
Cash – end of year	$	475,651	793,438

(Continued)

FOUNTAINS CARLOTTA SL, L.P.
(d/b/a The Fountains at The Carlotta)
(A Wholly Owned Subsidiary of Fountains Senior Living Holdings, LLC)

Statements of Cash Flows

Years ended December 31, 2014 and 2013

		2014	2013
Reconciliation of net loss to net cash provided by operating activities:			
Net loss	$	(813,749)	(1,042,168)
Adjustments to reconcile net loss to net cash provided by operating activities:			
Depreciation		1,289,197	1,009,973
Amortization of entrance fees		(1,146,283)	(1,159,808)
Entrance fees received		4,326,000	4,557,511
Amortization of financing costs		82,717	82,718
Amortization of waived interest on troubled debt restructuring		(57,400)	(55,733)
Provision for bad debts		56,047	429,717
Change in fair value of interest rate swap agreements		(31,954)	(10,492)
Operating expenses charged to intercompany		2,675,915	518,817
Changes in operating assets and liabilities:			
Accounts receivable		(340,284)	378,645
Prepaid expenses and other current assets		(66,229)	59,076
Accounts payable and accrued expenses		2,356	(106,961)
Accrued interest		(12,795)	(8,786)
Deferred revenue		11,399	55,007
Security and reservation deposits		98,577	88,102
Net cash provided by operating activities	$	6,073,514	4,795,618
Supplemental disclosure of cash flow information:			
Cash paid for interest	$	928,243	971,741
Supplemental disclosures of noncash investing and financing activities:			
Entrance fee draw downs applied to accounts receivable	$	222,756	291,998
Accrued capital expenditures		40,910	47,703
Assets acquired by capital lease		—	50,171
Reduction of notes payable charged to intercompany		958,116	286,287
Financing costs charged to intercompany		26,284	—

See accompanying notes to financial statements.

(1) Organization

Fountains Carlotta SL, L.P., d/b/a The Fountains at The Carlotta (the Partnership) (a wholly owned subsidiary of Fountains Senior Living Holdings, LLC), a Delaware limited partnership, operates a continuing care retirement community (CCRC) located in the state of California, and is owned by Fountains General Partner, LLC (GP) as general partner with a 1% interest and Fountains Pool V, LLC (Pool V), as limited partner with a 99% interest. Both the GP and Pool V are wholly owned by Fountains Senior Living Holdings, LLC (the Parent Company). The Partnership was created pursuant to a transaction in which the Parent Company acquired certain assets and assumed certain liabilities of 16 senior living facilities (the Facilities) in June 2005, including the facility known as The Fountains at The Carlotta.

The Partnership services the varying lifestyle needs of seniors and elderly residents by combining the services for independent living, assisted living, and skilled nursing facilities in a campus setting (the Facility). The Facility consists of 174 independent living apartments/casitas, 36 assisted living units, and 45 available licensed nursing beds, as well as a common area.

The Partnership's independent living resident contracts offer its CCRC residents preferential access to assisted living or the skilled nursing facility. Once a resident permanently transfers to assisted living or the skilled nursing facility, their independent living contract is terminated and the refundable portion of the entrance fee is refunded to the resident when triggered per the terms of the residency agreement. Assisted living and skilled nursing facility contracts are month to month. Preferential access is offered from the assisted living to the skilled nursing facility. A CCRC resident receives up to 10 free days in the skilled nursing facility per year until they permanently transfer. The skilled nursing facility is not considered to be a continued care unit.

Watermark Retirement Communities (Watermark) was retained to manage the Partnership effective January 1, 2012. The management agreement with Watermark has an initial term of five years, and shall automatically continue thereafter for successive one-year terms, unless terminated sooner as provided for in the agreement. The agreement provides for the management fee to be paid monthly. The fee is equal to 5% of the gross income accrued for each month. Management fees earned by Watermark totaled $722,400 and $689,697 in 2014 and 2013, respectively.

(2) Summary of Significant Accounting Policies

(a) Basis of Accounting

The Partnership's financial statements are prepared in accordance with accounting principles generally accepted in the United States of America (GAAP).

(b) Consideration of Going Concern

The accompanying financial statements have been prepared on the basis of the Partnership and the Parent Company continuing as a going concern. As described in Note 6, the note payable has been extended to December 31, 2015 and is therefore, reflected as a current liability as of December 31, 2014. However, as described in Note 10, the Parent Company executed a purchase and sale agreement in early 2015 and the note payable is anticipated to be paid in its entirety in 2015 at closing of the sale.

(c) Use of Estimates

The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. Actual results could differ from those estimates.

(d) Cash

Cash consists of demand deposit accounts at financial institutions. Throughout the year, the Partnership may have cash balances in excess of federally insured amounts on deposit with various financial institutions.

(e) Accounts Receivable

Accounts receivable are stated net of an allowance for doubtful accounts. The Partnership provides an allowance for doubtful accounts on its outstanding receivables balance, based on its collection history and an estimate of uncollectible accounts. Generally, accounts receivable are considered to be past due after 30 days. Accounts receivable are written off when deemed uncollectible on a specific-identification basis.

(f) Inventories

Inventories are valued at the lower of cost or market and are included in prepaid expenses and other current assets in the accompanying balance sheets. Inventories mainly consist of food, glassware, dishware, utensils, linens and chemicals.

(g) Property and Equipment

Property and equipment are recorded at cost. Maintenance and repairs are charged to expense as incurred. The Partnership capitalizes interest during construction to the extent such assets qualify for capitalization. Depreciation is computed using the straight-line method over the estimated useful lives of the related assets, as follows:

Land improvements	10–15 years
Buildings and improvements	5–40 years
Furniture, fixtures, and equipment	3–10 years

Depreciation expense was $1,289,197 and $1,009,973 in 2014 and 2013, respectively. Depreciation includes amortization of assets recorded under capital leases.

Property and equipment are reviewed for impairment whenever events or circumstances indicate that the carrying value may not be recoverable. Impairment is recognized when the asset's expected undiscounted cash flows are not sufficient to recover its carrying amount. The Partnership measures an impairment loss for such assets by comparing the fair value of the asset to its carrying amount. As of December 31, 2014 and 2013, management estimates that the future undiscounted cash flows for its investments in property and equipment are in excess of the carrying amount recorded in the balance sheets and no impairment adjustment is required.

Construction in progress includes project costs related to the construction of capital improvements and renovations at the Facility. These costs are allocated to the appropriate fixed asset accounts upon the completion of construction.

(h) Restricted Cash

Restricted cash reflects funds held in trust on behalf of certain healthcare residents; a corresponding liability is carried by the Partnership in refundable deposits.

The California Department of Social Services requires funds to be set aside to meet both a debt service reserve and an operating reserve which is based on the current year debt service paid and net operating expenses incurred related to continuing care residents for 75 days. The Partnership has designated $200,000 and $500,000, respectively, held in cash and the Parent Company has designated an additional $2,300,000 and $2,000,000, respectively, held in cash and cash equivalents to meet this reserve requirement as of December 31, 2014 and 2013.

(i) Deferred Financing Costs

During 2012, the Parent Company paid fees to the lender to modify the loan agreement terms as discussed in note 5. The portion of the fees allocated to the Partnership was $186,114. The allocation of fees was made in proportion to the debt allocation to the Partnership from the Parent Company. Amortization expense for the years ended December 31, 2014 and 2013 was $82,717 and $82,717, respectively, and is included in interest expense in the accompanying statements of operations.

In December 2014, the Parent Company paid fees to the lender to extend the maturity of the loan. The portion of the fee allocated to the Company was $26,284. The allocation of fees was made in proportion to the debt allocated to the Company from the Parent Company and will be amortized over the one-year extension period of the loan.

(j) Unearned and Refundable Entrance Fees

The Partnership provides housing to senior residents under an entrance fee agreement whereby 50% of the fee is refundable to the resident or the resident's estate upon termination of the contract and/or upon reoccupancy of the unit by the next resident. The Partnership estimates the portion of the nonrefundable fees expected to be refunded to residents due to early termination. Accordingly, the estimated refundable portion has been classified as refundable entrance fees with a portion recorded as a current liability for those expected to be refunded during the subsequent fiscal year.

The remainder of the entrance fee becomes nonrefundable over time and is recorded by the Partnership as a long-term liability. The nonrefundable portion of the entrance fee is amortized into income using the straight-line method over the estimated remaining life expectancy of the resident, based upon an annually adjusted actuarial projection. The Partnership records a receivable for entrance fees when a payment agreement is entered into with a resident. Such receivables, totaling $48,500 and $0 at December 31, 2014 and 2013, respectively, are included in accounts receivable on the balance sheets.

In conjunction with the acquisition of The Fountains at The Carlotta in 2005, the Partnership assumed refundable entrance fee liabilities. Due to the uncertainty of timing of settlement of the liability, the fair value could not be reasonably estimated. As a result, the Partnership has recorded the liability at its face value as refundable entrance fees in the accompanying balance sheet. At December 31, 2014 and 2013, the remaining liability totaled $2,469,575 and $2,949,668, respectively. The Partnership expects the source of repayment of refundable entrance fees to come from entrance fees received from the re-occupancy of the unit.

(k) Revenue Recognition and Deferred Revenue

Resident fee revenue, including resident community fees, is recognized when services are rendered. The Partnership invoices the residents one month in advance of the services being rendered, and therefore, cash payments received for services are recorded as liabilities until the services are rendered and the revenue is earned.

Typically, nonrefundable resident community fees approximating 30 times the daily residence fee are collected for assisted living residents upon move-in. These fees relate to apartment make-ready services performed by the Partnership. The rental agreements are cancelable by residents with 30 days' notice. Resident community fees are recognized as income upon move-in along with the related direct incremental costs incurred.

Healthcare services revenue is derived primarily from providing long-term healthcare services to residents. For residents under reimbursement arrangements with third-party payors, including Medicaid, Medicare, and private insurers, revenue is recorded based on contractually agreed-upon amounts on a per patient, daily basis. The Partnership records revenue from private-pay patients at the agreed-upon rate as services are performed.

Healthcare services rendered to Medicare beneficiaries are billed and collected based on the Prospective Payment System (PPS). Fee amounts are determined annually and are based on the care needs of the resident. As a result, PPS does not have estimated annual settlements. California Medicaid determines fee amounts annually based on information provided in submitted cost reports. The California Medicaid office performs a desk review of all submitted cost reports and they audit only selected providers. Laws and regulations governing the Medicare and Medicaid programs are complex and subject to interpretation. As a result, there is at least a reasonable possibility that estimates may change. There were no receivables or payables recorded for estimated Medicaid settlements at December 31, 2014 and 2013.

(l) Marketing and Advertising Costs

Costs for advertising and marketing are expensed at the time the advertising takes place. Total costs expensed during 2014 and 2013 were $187,244 and $189,973, respectively, and are included in professional services expense.

(m) Insurance

The Partnership is insured for professional and general liability, and automobile liability, subject to deductibles per occurrence of $100,000 and $1,000, respectively. Losses subject to these deductibles are accrued based upon the aggregate liability for reported claims and an estimated liability for claims incurred but not reported. These liabilities are not discounted. The policies, however, do not extinguish or provide legal release from the Partnership's obligation prior to payment to the harmed party. Therefore, at December 31, 2014 and 2013, the Partnership estimated the total unlimited unpaid claims and recorded insurance liability reserves of $566,960 and $598,740, respectively. These insurance liability reserves are classified as current or long-term based on the period claims are expected to be paid. The Partnership also recorded related assets of $271,555 and $304,800 as of December 31, 2014 and 2013, respectively, for the amount in excess of the Partnership's deductible thresholds that are estimated to be received from insurance carriers. These insurance receivables are recorded in prepaid and other current assets or other assets based on the period claims are expected to be paid.

The Partnership also has a guaranteed cost program for workers compensation and employee health insurance.

(n) Income Taxes

No provision has been made for federal and state income taxes, as the liability for such taxes, if any, is that of the partners and not the Partnership. The Partnership is subject to franchise taxes in the state of California where the facility is located. These taxes are expensed as incurred and are included in taxes and license fees in the accompanying statements of operations.

(o) Derivatives

The Partnership accounts for its derivative instruments in accordance with Accounting Standards Codification (ASC) 815, *Derivatives and Hedging*, which establishes accounting and reporting standards for derivative instruments, including certain derivative instruments embedded in other contracts and for hedging activities. All derivatives, whether designated in hedging relationships or not, are required to be recorded on the balance sheets at fair value. ASC 815 requires that changes in the derivative instrument's fair value be recognized currently in earnings, unless specific hedge accounting criteria are met.

Effective December 29, 2014, the Parent Company's derivative instrument had expired. The derivative had been an interest rate swap agreement that it entered into to manage its exposure to interest rate risk. The Parent Company's interest rate swap instrument was not designated as a hedge in accordance with the ASC 815, and as a result, changes in the fair value of the derivative instruments are recorded in other (expense) income. Such amounts have been allocated to the Partnership by the Parent Company as described in note 6.

(p) Fair Value Measurements

Fair value is based on the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. In order to increase consistency and comparability in fair value measurements, ASC 820, *Fair Value Measurement*, establishes a fair value hierarchy that prioritizes observable and unobservable inputs used to measure fair value into three broad levels. These levels, in order of highest priority to lowest priority, are described below:

Level 1 – Quoted prices (unadjusted) in active markets that are accessible at the measurement date for assets or liabilities

Level 2 – Observable prices that are based on inputs not quoted on active markets, but corroborated by market data

Level 3 – Unobservable inputs developed using estimates and assumptions developed by the Partnership, which reflect those that a market participant would use

As of December 31, 2014 and 2013, the carrying amounts of certain financial instruments, including cash, restricted cash, accounts receivable, accounts payable and accrued expenses were representative of their fair values because of the short-term maturity of these instruments.

(3) Healthcare Revenue Recognition

In 2014, the Partnership adopted ASU No. 2011-07, *Presentation and Disclosure of Patient Service Revenue, Provision for Bad Debts, and the Allowance for Doubtful Accounts for Certain Healthcare Entities.* Trade receivables are presented net of allowances for contractual discounts and uncompensated care. The allowance for contractual discounts is related to residents covered by Medicare, Medicaid and insurance. The allowance for uncompensated care is related to receivables recorded for self-pay residents.

The allowances for contractual discounts and uncompensated care are as follows at December 31:

		2014	2013
Allowance for contractual discounts	$	117,810	599,784
Allowance for uncompensated care		37,866	68,021
Total	$	155,676	667,805

The Company recognizes healthcare revenue in the period services are provided based on its standard rates for self-pay payors and at the contracted rates for third party payors. The Company records a provision for bad debts each month based on the age of unpaid balances and payor type. Healthcare revenue, net of contractual discounts but before provision for bad debts, by major payor class, was as follows:

		2014	2013
Medicare	$	4,972,360	4,848,016
Medicaid		837,369	878,510
Insurance		100,617	137,330
Self-pay		595,749	514,149
Total	$	6,506,095	6,378,005

In prior years, the Partnership had reflected the healthcare bad debt provision with general and administrative operating expense. The 2013 amounts have been reclassified to conform to current year presentation.

(4) Transactions with Parent Company

The Parent Company has a furniture, fixtures, and equipment (FF&E) escrow account that is used to replace fixtures, equipment, structural elements, and other components of the Facility as required in the management agreement. Under the operating agreement, all amounts in the capital expenditure reserves for the Partnership are considered to be pooled into one account at the Parent Company level, and may be used for any of the other Facilities. The reserve is funded by each of the Facilities monthly based on the number of resident units in each facility. The balance of the Parent Company's FF&E escrow account was $995,230 and $237,258 as of December 31, 2014 and 2013, respectively.

The Partnership and Parent Company do not settle intercompany balances in cash. The intercompany activity between the Parent Company and the Partnership for 2014 and 2013 has been presented as a net (distribution) contribution in the statements of changes in partners' deficit for the years ended December 31, 2014 and 2013, respectively.

(5) Concentrations of Credit Risk

The Partnership grants credit without collateral to its residents, many of whom are insured under third-party agreements. The Medicare program is a large source of healthcare revenue for the Partnership. Revenue from the Medicare program totaled approximately $5 million or 34.5% of total revenue during 2014. Revenue from the Medicare program totaled approximately $4.8 million or 35% of total revenue during 2013. The mix of receivables from residents and third-party payers at December 31, 2014 and 2013 was as follows:

	2014	2013
Medicare	59.53%	33.77%
Medicaid	6.21	32.20
Insurance	26.77	27.07
Private	7.49	6.96
Total	100.00%	100.00%

(6) Note Payable

At the time of the acquisition in 2005, the Parent Company obtained a loan from Nordbank with a commitment amount of $405,750,000 of which $330,750,000 was drawn on the date of acquisition. The loan is collateralized by the assets of each Facility and the total loan amount was allocated by the Parent Company to each Facility based upon the lender-appraised values at the date of acquisition. The loan was initially scheduled to mature on June 30, 2010; however, if the Parent Company met certain criteria at applicable milestone dates, it could be extended three times. The Parent Company exercised all three extension options and the loan is currently due December 31, 2015. As described in note 9, the loan is anticipated to be paid in full from proceeds of a 2015 scheduled sale of the Partnership and all other subsidiaries of the Parent Company. As of December 31, 2014 and 2013, the Parent Company had outstanding borrowings of $265,290,980 and $284,392,275, respectively, of which $21,074,562 and $22,572,799 was allocated to the Partnership, respectively.

The loan bears interest at the London InterBank Offered Rate (LIBOR) plus the stated spread. LIBOR was .25% as of December 31, 2014 and 2013. The spread is 3.75% effective September 28, 2012. The loan currently requires monthly payments of principal and quarterly payments of interest.

The Parent Company is subject to certain debt service and other financial covenants pursuant to its long-term debt agreement described above. The Parent Company failed to meet its liquidity and Debt Service Coverage Ratio (DSCR) requirements under the original loan agreement with Nordbank at each quarter-end in 2008 and for the quarter ended March 31, 2009. This precipitated the Second Amended and Restated Loan Agreement (the Loan Agreement) that was executed October 27, 2009 (the Closing Date). As a result of successfully amending its credit agreement, the Parent Company's loan was modified in that default interest was waived, ongoing principal amortization was postponed for 13 months, and swap arrangements were modified.

The Parent Company determined the modification to be a troubled debt restructuring in accordance with ASC 470, *Debt*, which requires that the effects of a restructuring involving only modification of terms of a payable, and not a transfer of assets or grant of equity interest, be accounted for prospectively from the time of the restructuring, and shall not change the carrying amount of the long-term debt unless the carrying amount exceeds the total future cash payments specified by the new terms.

As the total future cash payments required by the terms of the Loan Agreement exceeded the carrying value of the loan at the Closing Date, which includes principal and accrued interest less unamortized financing costs, interest expense is being accounted for prospectively using the effective interest rate, which is determined to be 3.85% annually. The default interest, which was waived as part of the 2009 loan modification, is being amortized as a credit to interest expense. The amortization during 2014 and 2013 was $57,400 and $55,733, respectively. As of December 31, 2014, the remaining unamortized default interest was $59,770.

Under the amended agreement, the Parent Company was not required to meet a DSCR threshold until the quarter ended March 31, 2012. DSCR is calculated as the ratio of earnings – before the deduction of interest, taxes, depreciation and amortization, plus the net cash received and refunded for entrance fees – to principal and interest (including interest related to interest rate swap agreements) for the period. A failure to achieve a DSCR of at least 1.00:1 will constitute an event of default. In addition, beginning June 30, 2012, and semiannually thereafter on each December 31st and June 30th, the Parent Company must deliver computations of Excess Cash Flow (ECF), noting any prior prepayments from ECF, and at Nordbank's option, prepay a portion of the loan not to exceed 50% of ECF. ECF is a measure of the cumulative increase in cash from the Closing Date through the quarter preceding the measurement date, less certain adjustments.

On September 28, 2012, the Second Amendment to the Loan Agreement was executed. This agreement extended the maturity date of the second extension option to December 31, 2014 and the maturity date of the third extension option to December 31, 2015. Additionally, the margin with respect to LIBOR was increased to 3.75% effective September 28, 2012. Under the new Loan Agreement, the maximum percentage of ECF was increased to 90% and the DSCR was increased to 1.15:1.0 as a condition for the third extension. Effective with this amendment, the second extension option was exercised.

The Parent Company determined this amendment to be a modification in accordance with ASC 470, *Debt*, which requires the calculation of a new effective interest rate. As noted above, this was determined to be 3.85%.

The DSCR was met for all quarters of 2013 and 2012. The June 30, 2013 ECF calculation resulted in a prepayment on the loan made by the Parent Company in 2013 in the amount of $1,731,821. The December 31, 2013 and June 30, 2014 ECF calculations resulted in prepayments on the loan made by the Parent Company in March and September 2014 of $6,440,175 and $4,108,706, respectively, of which $511,170 and $339,633 was allocated to the Partnership. The December 31, 2014 ECF calculation resulted in prepayment on the loan made by the Parent Company in March 2015 of $5,988,353 of which $475,308 was allocated to the Partnership.

Under the Loan Agreement, the Parent Company is subject to certain nonfinancial covenants. Management believes the Parent Company is in compliance with all debt covenants as of December 31, 2014 and 2013.

The fair value of the Parent Company's long-term debt, including amounts allocated to the Partnership, has been estimated based on current rates offered for debt with the same remaining maturities and comparable collateralizing assets. Changes in assumptions or methodologies used to make estimates may have a material effect on the estimated fair value. In accordance with ASC 820, the Partnership has applied Level 2 type inputs to determine that the estimated fair value of the Parent Company's long-term debt was $264,599,210 and $283,009,770, of which $21,019,608 and $22,463,067 was allocated to the Partnership, at December 31, 2014 and 2013, respectively.

Scheduled annual principal maturities of the note payable until maturity and the installment loan are as follows:

		Amount
Year ending December 31:		
2015	$	21,074,562
Total scheduled principal maturities		21,074,562
Unamortized waived interest		59,770
Total note payable		21,134,332
Less current maturities		(21,134,332)
Note payable – less current maturities	$	—

The Parent Company executed an interest rate swap agreement with Nordbank effective September 28, 2012. The swap agreement is designated as a hedge in accordance with ASC 815, *Derivatives and Hedging*. This interest rate swap was held to reduce to the risk of changes in LIBOR on the interest payments on the note payable. The swap agreement expired December 29, 2014.

The fair value of the interest rate swap at December 31, 2013, at the Parent Company level was a liability of $402,586. As the Company's interest rate swap agreement is not traded on a market exchange, the fair value is determined through a discounted cash flow approach using market-based interest rate yield curves and are based on Level 2 inputs in accordance with ASC 820. The fair value of the interest rate swap agreement allocated to the Partnership was $31,954 at December 31 2013 and is included in the derivative liability in the accompanying balance sheets. Changes in fair value of the interest rate swap agreement are included in other (expense) income in the accompanying statements of operations. The allocation of the derivative liability is consistent with the allocation of the loan amount to each Facility.

The Parent Company utilized this interest-rate related derivative instrument (interest rate swap agreements) to manage its exposure on its debt instruments. The Parent Company does not enter into derivative instruments for any purpose other than to mitigate the impact of changes in interest rates on its cash flows. That is, the Parent Company does not speculate using derivative instruments

ASC 820 requires that nonperformance risk be considered in measuring the fair value of assets and liabilities. For derivatives, nonperformance risk refers to the risk that one of the parties to a derivative transaction will be unable to perform under the contractual terms of that derivative, such as the risk that one party will be unable to make cash payments at periodic net settlement dates or upon termination. The Parent Company has considered the counterparty's credit risk as well as the effect of its own credit standing in determining the fair value of its interest rate swap agreements. The Parent Company minimizes the credit risk in derivative instruments by entering into transactions with high-quality counterparties.

(7) Capital Lease

The Partnership leased a vehicle under a capital lease in 2013. The following is a schedule of future minimum lease payments under this capital lease together with the present value of net minimum lease payments as of December 31, 2014:

Year ending December 31:		
2015	$	11,600
2016		11,600
2017		11,600
2018		4,833
Total minimum lease payments		39,633
Less amount representing interest		(3,920)
Present value of net minimum lease payments	$	35,713

(8) Commitments and Contingencies

The Partnership entered into an Amended and Restated Guaranty and Pledge Agreement (Guaranty) on the Closing Date, whereby, it has unconditionally guaranteed payment of the principal and interest on the Parent Company loan described in note 6 and the related performance obligations of the Parent Company's subsidiaries under the Guaranty, as defined. The occurrence and continuance of an event of default by the Parent Company under the Loan Agreement beyond the cure period constitutes an event of default under the Guaranty. As a remedy for default, the lender may take possession, sell, lease, license, or otherwise dispose of the Partnership's facility and all other assets of the Partnership.

From time to time, the Partnership is involved in claims and lawsuits incidental to the ordinary course of business. While the outcome of these claims and lawsuits cannot be predicted with certainty, management of the Partnership does not believe the ultimate resolution of these matters will have a material adverse effect on the Partnership's financial statements.

Watermark has provided the Partnership limited indemnifications against actions taken on behalf of the Partnership in Watermark's capacity as manager. The Watermark indemnity rights may not protect the Partnership against all of the risks and possible losses faced by the Partnership from Watermark's role as manager.

In December 2014, legal claims were filed against the Partnership by two former employees alleging wrongful wage and hour claims. One of the claims also alleges wrongful termination. Both cases are in the early phase of litigation. Management believes there is a reasonable possibility of an unfavorable outcome. However, due to the lack of information provided by the claimants, management has determined that an amount is not reasonably estimable. Therefore, there was no contingent loss accrual recorded as of December 31, 2014.

The Partnership acquired the Facility subject to a potential contingent liability of $3,188,295 to refund certain entrance fees collected prior to the acquisition date. Since these fees were collected by the prior owner of the Facility and did not represent a legal obligation to the Partnership unless the residents vacated their units prior to certain contractually determined dates, no liability was recorded at the time of the acquisition. As of December 31, 2014 and 2013, the remaining amount of this contingent liability was $362,453 and $475,255, respectively. As it is not probable the Partnership will have to pay this amount, no liability has been recorded as of December 31, 2014 and 2013. The Partnership did not refund any entrance fees related to the contingent liability during the years ended December 31, 2014 and 2013.

At December 31, 2014 and 2013, the Partnership had entered into $154,000 and $76,000, respectively, in firm commitments for the completion of construction projects.

(9) Employee Benefit Plan

The Parent Company offers a 401(k) retirement plan (the 401(k) Plan) under Watermark Services IV, LLC for the benefit of the employees. Employees that complete six months of service and are 21 years of age or older may participate in the 401(k) Plan. Employees may make pretax salary deferrals of 1% to 75% of their compensation, subject to annual dollar limits determined by the Internal Revenue Service. Employer matching contributions for the 401(k) Plan are on a discretionary year-end match. To receive the match, employees must be actively employed as of the last day of the year. The Partnership contributed a total of approximately $6,600 and $4,300 during the years ended December 31, 2014 and 2013, to the 401(k) Plan, respectively.

(10) Subsequent Events

In preparing the financial statements, the Partnership evaluated subsequent events occurring through April 30, 2015, the date the financial statements were available to be issued, in accordance with the Partnership procedures related to disclosure of subsequent events.

The Parent Company executed a purchase and sale agreement ("PSA") on February 18, 2015 in which the Partnership, along with all the subsidiaries of the Company, is a party to the agreement whereby each subsidiary will sell its respective property and transfer licenses to the buyer. The sale is expected to close by July 1, 2015. Proceeds from the sale are anticipated to be sufficient to repay the Nordbank loan in full at closing and no loss on the sale is anticipated.

KPMG

FOUNTAINS SENIOR LIVING HOLDINGS, LLC AND SUBSIDIARIES

Consolidated Financial Statements

December 31, 2014 and 2013

(With Independent Auditors' Report Thereon)

FOUNTAINS SENIOR LIVING HOLDINGS, LLC
AND SUBSIDIARIES

Table of Contents

	Page(s)
Independent Auditors' Report	1
Consolidated Financial Statements as of and for the years ended December 31, 2014 and 2013:	
Consolidated Balance Sheets	2–3
Consolidated Statements of Operations	4
Consolidated Statements of Changes in Member's Deficit	5
Consolidated Statements of Cash Flows	6–7
Notes to Consolidated Financial Statements	8–21

KPMG

KPMG LLP
Suite 800
60 East Rio Salado Parkway
Tempe, AZ 85281-9125

Independent Auditors' Report

The Member
Fountains Senior Living Holdings, LLC:

We have audited the accompanying consolidated financial statements of Fountains Senior Living Holdings, LLC and its subsidiaries, which comprise the consolidated balance sheets as of December 31, 2014 and 2013, and the related consolidated statements of operations, changes in member's deficit, and cash flows for the years then ended, and the related notes to the consolidated financial statements.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these consolidated financial statements in accordance with U.S. generally accepted accounting principles; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

Auditors' Responsibility

Our responsibility is to express an opinion on these consolidated financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on the auditors' judgment, including the assessment of the risks of material misstatement of the consolidated financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the consolidated financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the consolidated financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Fountains Senior Living Holdings, LLC and its subsidiaries as of December 31, 2014 and 2013, and the results of their operations and their cash flows for the years then ended, in accordance with U.S. generally accepted accounting principles.

KPMG LLP

Phoenix, Arizona
April 30, 2015

FOUNTAINS SENIOR LIVING HOLDINGS, LLC
AND SUBSIDIARIES

Consolidated Balance Sheets

December 31, 2014 and 2013

Assets		2014	2013
Current assets:			
Cash and cash equivalents	$	20,123,400	23,777,786
Accounts receivable – less allowance for doubtful accounts of $591,000 and $1,206,000 at December 31, 2014 and 2013, respectively		5,393,791	5,149,194
Prepaid expenses and other current assets		2,073,037	2,583,859
Total current assets		27,590,228	31,510,839
Property and equipment:			
Land and land improvements		70,907,658	71,163,804
Buildings and improvements		336,689,689	329,644,178
Furniture, fixtures, and equipment		44,836,440	41,209,688
Construction in progress		418,059	1,557,637
Total property and equipment		452,851,846	443,575,307
Less accumulated depreciation		(110,064,229)	(92,860,837)
Property and equipment – net		342,787,617	350,714,470
Restricted cash		1,708,031	1,504,750
Other assets		2,207,169	1,901,882
Deferred financing costs – less accumulated amortization of $2,284,700 and $1,269,000 at December 31, 2014 and 2013, respectively		330,874	1,015,410
Total	$	374,623,919	386,647,351

(Continued)

FOUNTAINS SENIOR LIVING HOLDINGS, LLC
AND SUBSIDIARIES

Consolidated Balance Sheets

December 31, 2014 and 2013

Liabilities and Member's Deficit		**2014**	**2013**
Current liabilities:			
Accounts payable and accrued expenses	$	10,278,141	12,929,647
Payable to affiliates – net		188,021	136,672
Security and reservation deposits		1,147,259	1,260,069
Accrued interest		29,073	43,304
Refundable entrance fees		11,209,577	10,306,543
Resident refund liabilities		479,880	559,205
Insurance liability reserves		890,135	2,466,448
Derivative liability		—	402,586
Current portion capital lease obligations		103,818	60,583
Current maturities of notes payable		266,087,416	13,263,688
Total current liabilities		290,413,320	41,428,745
Long-term liabilities:			
Notes payable – less current maturities		30,868	272,720,576
Capital lease obligation – less current portion		345,292	245,125
Deferred revenue		1,010,048	744,823
Insurance liability reserves – less current portion		3,905,142	3,013,297
Refundable entrance fees – less current portion		58,715,967	54,109,350
Unearned nonrefundable entrance fees		36,122,637	33,010,628
Total long-term liabilities		100,129,954	363,843,799
Total liabilities		390,543,274	405,272,544
Commitments and contingencies (notes 5, 9, and 10)			
Member's deficit		(15,919,355)	(18,625,193)
Total	$	374,623,919	386,647,351

See accompanying notes to consolidated financial statements.

FOUNTAINS SENIOR LIVING HOLDINGS, LLC
AND SUBSIDIARIES

Consolidated Statements of Operations

Years ended December 31, 2014 and 2013

		2014	2013
Operating revenue:			
Healthcare revenue, net of contractual allowances	$	36,175,268	36,708,812
Provision for bad debts (note 3)		(480,437)	(744,625)
Healthcare revenue, net		35,694,831	35,964,187
Resident fees		105,033,929	100,575,631
Amortization of entrance fees		6,266,498	6,312,218
Lease income		5,415,400	5,422,470
Other operating income		4,616,002	4,168,781
Total operating revenue		157,026,660	152,443,287
Operating expenses:			
Wages and benefits		56,681,034	56,474,879
Depreciation		17,453,889	15,615,396
Ancillary/therapy expenses		8,900,227	8,987,603
General and administrative		2,267,410	2,513,832
Food		9,399,654	9,721,498
Supplies		2,134,940	2,296,037
Utilities		7,323,747	6,854,713
Insurance		3,062,027	3,399,828
Taxes and license fees		4,642,872	4,523,831
Repairs and maintenance		5,661,780	5,228,021
Gain on disposal of assets		(1,950)	(456,898)
Loss on impairment		3,648,363	—
Lease expense		3,675,930	3,654,607
Management fees		8,234,471	7,879,101
Occupancy costs		2,458,692	2,533,124
Professional services		6,146,413	5,378,244
Total operating expenses		141,689,499	134,603,816
Income from operations		15,337,161	17,839,471
Other (expense) income:			
Interest expense		(11,695,963)	(12,376,731)
Change in fair value of interest rate swap agreements		402,586	132,190
Interest income		8,995	19,507
Other expense		(1,346,941)	(171,843)
Total other expense		(12,631,323)	(12,396,877)
Net income	$	2,705,838	5,442,594

See accompanying notes to consolidated financial statements.

FOUNTAINS SENIOR LIVING HOLDINGS, LLC
AND SUBSIDIARIES

Consolidated Statements of Changes in Member's Deficit

Years ended December 31, 2014 and 2013

Balance – December 31, 2012	$ (24,067,787)
Net income	5,442,594
Balance – December 31, 2013	(18,625,193)
Net income	2,705,838
Balance – December 31, 2014	$ (15,919,355)

See accompanying notes to consolidated financial statements.

FOUNTAINS SENIOR LIVING HOLDINGS, LLC
AND SUBSIDIARIES

Consolidated Statements of Cash Flows

Years ended December 31, 2014 and 2013

	2014	2013
Cash flows from operating activities:		
Net income	$ 2,705,838	5,442,594
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation	17,453,889	15,615,396
Amortization of entrance fees	(6,266,498)	(6,312,218)
Entrance fees received	24,071,517	23,819,889
Amortization of financing and loan modification costs	1,015,410	1,015,410
Amortization of waived interest on troubled debt restructuring	(745,159)	(723,506)
Gain on sale/disposition of fixed assets	(1,950)	(456,898)
Loss on impairment	3,648,363	—
Provision for bad debts	688,171	965,653
Change in fair value of interest rate swap agreements	(402,586)	(132,190)
Changes in operating assets and liabilities:		
Accounts receivable	(1,083,275)	564,291
Prepaid expenses and other current assets	(311,859)	729,693
Straight-line lease receivable	31,171	10,589
Accounts payable and accrued expenses	(3,075,461)	788,952
Payable to affiliates – net	51,349	136,672
Accrued interest	(140,566)	(139,421)
Deferred revenue	265,225	323,502
Security and reservation deposits	348,173	593,311
Net cash provided by operating activities	38,251,752	42,241,719
Cash flows from investing activities:		
Decrease in restricted cash	(203,281)	(185,490)
Proceeds from sale of fixed assets	767,334	1,480,476
Purchases of property and equipment	(13,627,439)	(11,688,330)
Net cash used in investing activities	(13,063,386)	(10,393,344)
Cash flows from financing activities:		
Payment of financing costs	(330,874)	—
Payment on notes payable	(19,120,821)	(9,424,586)
Payment on short-term installment loan	—	(548,141)
Payment on capital lease obligations	(84,038)	(21,508)
Payment of resident refund liabilities	(79,325)	(102,317)
Refunds of entrance fees	(9,227,694)	(10,749,932)
Net cash used in financing activities	(28,842,752)	(20,846,484)
Net (decrease) increase in cash and cash equivalents	(3,654,386)	11,001,891
Cash and cash equivalents – beginning of year	23,777,786	12,775,895
Cash and cash equivalents – end of year	$ 20,123,400	23,777,786

(Continued)

FOUNTAINS SENIOR LIVING HOLDINGS, LLC
AND SUBSIDIARIES

Consolidated Statements of Cash Flows

Years ended December 31, 2014 and 2013

		2014	2013
Supplemental disclosure of cash flow information:			
Cash paid for interest	$	11,566,278	12,224,248
Supplemental disclosures of noncash investing and financing activities:			
Accrued capital expenditures	$	679,942	720,373
Security deposits applied against entrance fees		460,983	94,200
Entrance fee draw-downs applied to accounts receivable		291,421	358,860
Assets acquired by capital lease		227,440	327,216

See accompanying notes to consolidated financial statements.

(1) Organization

Fountains Senior Living Holdings, LLC (the Company) fka as Sunrise IV Senior Living Holdings, LLC, a Delaware limited liability company, was formed on June 30, 2005, to acquire 16 senior living facilities (the acquisition). The Company began operations on July 1, 2005 to provide for the varying lifestyle needs of seniors and elderly residents by combining the services for independent living, assisted living, Alzheimer's and related dementia care, and skilled nursing facilities in a campus setting. Several of the Company's Facilities are considered continuing care retirement communities.

The Company owns the following 13 single-purpose limited liability companies and 3 single-purpose limited partnerships (collectively, the Operator Entities), which operate 16 senior living facilities (the Facilities) as follows:

Operator entity	Facility	Location
Fountains La Cholla SL, LLC	Fountains at La Cholla	Tucson, Arizona
Fountains Canterbury SL, LLC	Fountains at Canterbury	Oklahoma, Oklahoma
Fountains Albemarle SL, LLC	Fountains at Albemarle	Tarboro, North Carolina
Fountains Crystal Lake SL, LLC	Fountains at Crystal Lake	Crystal Lake, Illinois
Fountains La Jolla SL, L.P.	Fountains at La Jolla	San Diego, California
Fountains Bellevue SL, LLC	Fountains at Bellevue	Bellevue, Washington
Fountains Sea Bluffs SL, L.P.	Fountains at Sea Bluffs	Dana Point, California
Fountains Franklin SL, LLC	Fountains at Franklin	Southfield, Michigan
Fountains Millbrook SL, LLC	Fountains at Millbrook	Millbrook, New York
Fountains Lake Pointe Woods SL, LLC	Fountains at Lake Pointe Woods	Sarasota, Florida
Fountains Boca Ciega SL, LLC	Fountains at Boca Ciega Bay	St. Petersburg, Florida
Fountains Carlotta SL, L.P.	Fountains at Carlotta	Palm Desert, California
Fountains Bronson Place SL, LLC	Fountains at Bronson Place	Kalamazoo, Michigan
Fountains Washington House SL, LLC	Fountains at The Washington House	Alexandria, Virginia
Fountains Greenbriar SL, LLC	Fountains at Greenbriar	Independence, Missouri
Fountains RiverVue SL, LLC	Fountains at RiverVue	Tuckahoe, New York

During various dates in 2010, Watermark Retirement Communities, Inc. (Watermark) was retained to manage the Facilities with the exception of Fountains at Carlotta, which transitioned January 1, 2012. The agreements have an initial term of five years from the final closing date as defined in the master management agreement, and shall thereafter automatically continue for successive one-year terms, unless sooner terminated as provided for in the agreements. The agreements provide for management fees to be paid monthly. The fee is equal to 5% of the gross income accrued for each month. Total management fees incurred under these agreements in 2014 and 2013 were $7,583,675 and $7,430,070, respectively.

These management agreements also entitle Watermark to be compensated for early termination in an amount equal to the management fee earned in the preceding 12 months for the discontinued operations if termination is effective during the second or third year of the initial term. If the effective termination is in the fourth year, the fee is 50% of the management fees earned in the preceding 12 months. There were no early termination fees incurred in 2014 and 2013.

In addition to the individual facility management agreements, the Company entered into a master portfolio management agreement with Watermark. This agreement entitles the manager to receive an incentive management fee as additional compensation equal to 10% of the amount by which current cash flow for a current measurement period exceeds base cash flow for a base measurement period as defined in the agreement. The total incentive management fee incurred was $578,642 and $375,141 in 2014 and 2013, respectively.

The Company leases property to Fountains Operating Company of (NY), Inc. (FOC). FOC is the licensed operator for the Fountains at Millbrook and Fountains at RiverVue senior living facilities, which are also managed by Watermark. The lease income for 2014 and 2013 was $3,591,708 and $3,487,092, respectively. The Company had a payable to FOC of $326,266 and $123,233 as of December 31, 2014 and 2013, respectively.

(2) Summary of Significant Accounting Policies

(a) *Basis of Accounting*

The Company's consolidated financial statements are prepared in accordance with accounting principles generally accepted in the United States of America (GAAP). The accompanying consolidated financial statements include the consolidated accounts of Fountains and the Operator Entities after elimination of intercompany accounts and transactions.

(b) *Consideration of Going Concern*

The accompanying consolidated financial statements have been prepared on the basis of the Company continuing as a going concern. As described in Note 5, the note payable has been extended to December 31, 2015 and is therefore, reflected as a current liability as of December 31, 2014. However, as described in Note 12, the Company executed a purchase and sale agreement in early 2015 and the note payable is anticipated to be paid in full in 2015 at closing of the sale.

(c) *Use of Estimates*

The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the amounts reported in the consolidated financial statements and accompanying notes. Actual results could differ from those estimates.

(d) *Cash and Cash Equivalents*

Cash and cash equivalents include all highly liquid investments with an original maturity of three months or less. Throughout the year, the Company may have cash balances in excess of federally insured amounts on deposit with various financial institutions.

(e) Accounts Receivable

Accounts receivable are stated net of an allowance for doubtful accounts. The Company provides an allowance for doubtful accounts on its outstanding receivables balance based on its collection history and an estimate of uncollectible accounts. Generally, accounts receivable are considered to be past due after 30 days. Accounts receivable are written off when deemed uncollectible on a specific-identification basis.

(f) Inventories

Inventories are valued at the lower of cost or market and are included in prepaid expenses and other current assets in the accompanying consolidated balance sheets. Inventories mainly consist of food, glassware, dishware, utensils, linens and chemicals.

(g) Property and Equipment

Property and equipment are recorded at cost. Maintenance and repairs are charged to expense as incurred. The Company capitalizes interest during construction to the extent such assets qualify for capitalization. Depreciation is computed using the straight-line method over the estimated useful lives of the related assets as follows:

Land improvements	10–15 years
Buildings and improvements	5–40 years
Furniture, fixtures, and equipment	3–10 years

Depreciation expense was $17,453,889 and $15,615,396 in 2014 and 2013, respectively. Depreciation includes amortization of assets recorded under capital leases.

The Company evaluates long-lived assets for impairment at the individual facility level, which is the lowest level at which individual cash flows can be identified. Impairment losses are recorded on long-lived assets used in operations when events and circumstances indicate that the assets might be impaired and the undiscounted cash flows estimated to be generated by those assets are less than the carrying amounts of the assets. When events such as these occur, the impaired assets are adjusted to their estimated fair value and an impairment loss is recorded separately as a component of income from operations under loss on impairment of assets. In 2014, the Company recorded a loss on impairment of assets in the accompanying consolidated statements of operations of $3,648,363 related to the facility Fountains at Canterbury. Management determined the fair value of the assets through the use of a discounted cash flow model and with reference to market conditions and prices achieved in the sale of comparable assets. The determination of fair value is based on significant unobservable inputs and, as such, is classified as a Level 3 fair value measurement in accordance with the hierarchy established in ASC 820, *Fair Value Measurements and Disclosures*. As of December 31, 2013, management believes that the future estimated undiscounted cash flows for its investments in property and equipment are in excess of the carrying amount recorded in the consolidated balance sheet, and no impairment adjustment is required.

Construction in progress includes project costs related to the construction of capital improvements and renovations at the Facilities. These costs are allocated to the appropriate fixed asset accounts upon the completion of the construction.

(h) Restricted Cash

Restricted cash includes a cash escrow reserve for working capital, which is required by the State of Florida for Fountains at Lake Pointe Woods. This restricted cash amount, which is held by state authorities, totaled $696,800 as of December 31, 2014 and 2013. The reserve requirement under state statutes is calculated by applying a mandated percentage to the Facility's net operating expenses, plus a debt service reserve, as defined.

Restricted cash also includes a furniture, fixtures and equipment (FF&E) escrow account to be used to replace fixtures, equipment, structural elements and other components of the Facilities as required in the management agreements. The balance of the FF&E escrow account was $995,230 and $237,258 as of December 31, 2014 and 2013, respectively, and is included in restricted cash in the accompanying consolidated balance sheets.

The California Department of Social Services, related to Fountains Carlotta SL, LLC, requires funds to be set aside to meet both a debt service reserve and an operating reserve that is based on the current year debt service paid and net operating expenses incurred related to continuing care residents for 75 days. The Company designated $2,500,000 held in cash and cash equivalents to meet this reserve requirement as of December 31, 2014 and 2013.

(i) Deferred Financing Costs

During 2012, the Company paid fees totaling $2,024,947 to the lender to modify the loan agreement terms as discussed in note 5. In addition to the fee paid in 2012, $259,726 was paid to reimburse for legal and other closing costs related to the loan amendment. Amortization expense for the years ended December 31, 2014 and 2013 was $1,015,410 and $1,015,410, respectively, and is included in interest expense in the accompanying consolidated statements of operations.

In December 2014, the Company paid $330,874 in fees to the lender to extend the maturity of the loan which will be amortized over the remaining one-year term of the loan.

(j) Unearned and Refundable Entrance Fees

The Company provides housing to senior residents under an entrance fee agreement at certain facilities whereby an agreed upon percentage of the fee is refundable to the resident or the resident's estate upon termination of the contract and/or upon reoccupancy of the unit by the next resident. The contracts vary and can range from 0% to 90% refundable. The Company estimates the portion of the nonrefundable fees expected to be refunded to residents due to early termination. Accordingly, the estimated refundable portion has been classified as refundable entrance fees with a portion recorded as a current liability for those expected to be refunded during the subsequent fiscal year.

The remainder of the entrance fee becomes nonrefundable over time and is recorded by the Company as a long term liability. The nonrefundable portion of the entrance fee is amortized into income using

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the straight line method over the estimated remaining life expectancy of the resident, based upon an annually adjusted actuarial projection. The Company records a receivable for entrance fees when a payment agreement is entered into with a resident. Such receivables, totaling $140,914 and $0 at December 31, 2014 and 2013, respectively, are included in accounts receivable on the consolidated balance sheets.

In conjunction with the acquisition in 2005, the Company assumed refundable entrance fee liabilities at certain Facilities. Due to the uncertainty of timing of settlement of the liability, the fair value could not be reasonably estimated. As a result, the Company has recorded the liability at its face value as refundable entrance fees in the accompanying consolidated balance sheets. At December 31, 2014 and 2013, the remaining liability totaled $9,370,789 and $12,143,483, respectively. The Company expects the source of repayment of refundable entrance fees to come from entrance fees received from the reoccupancy of the unit.

(k) Future Service Obligation

The Company owns a Facility where life care contracts were previously offered and is, therefore, obligated to provide services and the use of facilities to the residents of this community over their remaining lives based on the terms of the life care contract agreements (Care Agreements). The facility is the Fountains at The Washington House. When the present value of estimated costs to be incurred under the Care Agreements exceeds the present value of the estimated related revenues, such excess is accrued. The obligation is discounted at 6% for 2013 based on a rate that reasonably reflects the Company's risk premium as determined by management. For 2014, Management reviewed facts and circumstances as of yearend compared to those used in the 2013 valuation and concluded that circumstances have not significantly changed. Therefore, Management has determined that there is no future service obligation as of December 31, 2014 and 2013.

(l) Revenue Recognition and Deferred Revenue

Resident fee revenue, including resident community fees, is recognized when services are rendered. The Company invoices the residents one month in advance of the services being rendered, and therefore, cash payments received for services are recorded as liabilities until the services are rendered and the revenue is earned.

Typically, nonrefundable resident community fees approximating 30 to 60 times the daily residence fee are collected in rental communities upon move-in. These fees relate to apartment make-ready services performed by the Company. The rental agreements are cancelable by residents with 30 days' notice. Resident community fees are recognized as income upon move-in along with the related direct incremental costs incurred.

Healthcare services revenue is derived primarily from providing long-term healthcare services to residents. For residents under reimbursement arrangements with third-party payors, including Medicaid, Medicare, and private insurers, revenue is recorded based on contractually agreed-upon amounts on a per-patient, daily basis. The Company records revenue from private pay patients at the agreed upon rate as services are performed.

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Healthcare services rendered to Medicare beneficiaries are billed and collected based on a Prospective Payment System (PPS). Fee amounts are determined annually and are based on the care needs of the resident. As a result, PPS does not have estimated annual settlements. Medicaid payment methodologies vary by state. Most state Medicaid programs will perform desk reviews of all submitted cost reports and audit only selected providers. Laws and regulations governing the Medicaid programs are complex and subject to interpretation. As a result, there is at least a reasonable possibility that recorded estimates may change. There were no receivables or payables recorded for estimated Medicaid settlements at December 31, 2014 and 2013.

Lease income is recognized on a straight-line basis over the terms of the respective leases.

(m) Marketing and Advertising Costs

Costs for advertising and marketing are expensed at the time the advertising takes place. Total costs expensed during 2014 and 2013 were $1,845,870 and $1,696,314, respectively, and are included in professional services expense.

(n) Insurance

The Company is insured for professional and general liability, and automobile liability, subject to deductibles per occurrence of $100,000 and $1,000, respectively. Losses subject to these deductibles are accrued based upon the aggregate liability for reported claims and an estimated liability for claims incurred but not reported. These liabilities are not discounted. The policies, however, do not extinguish or provide legal release from the Company's obligation prior to payment to the harmed party. Therefore, at December 31, 2014 and 2013, the Company estimated the total unlimited unpaid claims and recorded insurance liability reserves of $4,795,277 and $5,479,745, respectively. These insurance liability reserves are classified as current or long-term based on the period claims are expected to be paid. The Company also recorded related assets of $2,303,347 and $2,789,570 as of December 31, 2014 and 2013, respectively, for the amount in excess of the Company's deductible thresholds that are estimated to be received from insurance carriers. These insurance receivables are recorded in prepaid and other current assets or other assets based on the period claims are expected to be paid.

The Company also has a guaranteed cost program for workers compensation and employee health insurance.

(o) Income Taxes

The Company is treated as a partnership for income tax purposes. Accordingly, no provision has been made for federal and state income taxes, as the liability for such taxes, if any, is that of the member and not the Company. The Company is subject to franchise taxes in the state of California, where certain of the Facilities are located. These taxes are expensed as incurred and are included in taxes and license fees in the accompanying consolidated statements of operations.

(p) Derivatives

The Company accounts for its derivative instruments in accordance with Accounting Standards Codification (ASC) 815, *Derivatives and Hedging*, which establishes accounting and reporting standards for derivative instruments, including certain derivative instruments embedded in other contracts and for hedging activities. All derivatives, whether designated in hedging relationships or not, are required to be recorded on the consolidated balance sheets at fair value. ASC 815 requires that changes in the derivative instrument's fair value be recognized currently in earnings, unless specific hedge accounting criteria are met.

Effective December 29, 2014, the Company's derivative instrument had expired. The derivative had been an interest rate swap agreement that it entered into to manage its exposure to interest rate risk. This derivative instrument was not designated as a hedge in accordance with ASC 815, and as a result, changes in the fair value of the derivative instruments are recorded in other (expense) income.

(q) Fair Value Measurements

Fair value is based on the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. In order to increase consistency and comparability in fair value measurements, ASC 820, *Fair Value Measurement*, establishes a fair value hierarchy that prioritizes observable and unobservable inputs used to measure fair value into three broad levels. These levels, in order of highest priority to lowest priority, are described below:

Level 1 – Quoted prices (unadjusted) in active markets that are accessible at the measurement date for assets or liabilities

Level 2 – Observable prices that are based on inputs not quoted on active markets, but corroborated by market data

Level 3 – Unobservable inputs developed using estimates and assumptions developed by the Company, which reflect those that a market participant would use

As of December 31, 2014 and 2013, the carrying amounts of certain financial instruments, including cash and cash equivalents, restricted cash, accounts receivable, accounts payable and accrued expenses, which meet the definition of a financial instrument, and other liabilities were representative of their fair values because of the short-term maturity of these instruments.

(3) Healthcare Revenue Recognition

In 2014, the Company adopted ASU No. 2011-07, *Presentation and Disclosure of Patient Service Revenue, Provision for Bad Debts, and the Allowance for Doubtful Accounts for Certain Healthcare Entities.* Trade receivables are presented net of allowances for contractual discounts and uncompensated care. The allowance for contractual discounts is related to residents covered by Medicare, Medicaid and insurance. The allowance for uncompensated care is related to receivables recorded for self-pay residents.

The allowances for contractual discounts and uncompensated care are as follows at December 31:

		2014	2013
Allowance for contractual discounts	$	415,413	872,548
Allowance for uncompensated care		175,476	333,819
Total	$	590,889	1,206,367

The Company recognizes healthcare revenue in the period services are provided based on its standard rates for self-pay payors and at the contracted rates for third party payors. The Company records a provision for bad debts each month based on the age of unpaid balances and payor type. Healthcare revenue, net of contractual discounts but before provision for bad debts, by major payor class, was as follows:

		2014	2013
Medicare	$	21,794,994	22,935,507
Medicaid		3,953,578	3,916,126
Insurance		3,683,433	2,906,360
Self-pay		6,743,263	6,950,819
Total	$	36,175,268	36,708,812

In prior years, the Company had reflected the healthcare bad debt provision with general and administrative operating expense. The 2013 amounts have been reclassified to conform to current year presentation.

(4) Concentrations of Credit Risk

The Company grants credit without collateral to its residents for amounts due under resident agreements, many of whom are insured under third-party agreements. The Medicare program is a large source of healthcare revenue for the Company. Revenue from the Medicare program totaled approximately $21.8 million and $22.9 million or 13.9% and 14.9% of total revenue during 2014 and 2013, respectively. The mix of receivables from residents and third-party payers as of December 31, 2014 and 2013 was as follows:

	2014	2013
Medicare	43.58%	39.63%
Medicaid	7.83	14.18
Insurance	29.33	27.71
Private	19.26	18.48
Total	100.00%	100.00%

(5) Notes Payable

At the time of the acquisition in 2005, the Company obtained a loan from Nordbank with a commitment amount of $405,750,000, of which $330,750,000 was drawn on the date of acquisition. The loan is collateralized by the assets of each facility. The loan was initially scheduled to mature on June 30, 2010; however, if the Company met certain criteria at applicable milestone dates, it could be extended three times. The Parent Company exercised all three extension options and the loan is currently due December 31, 2015. As described in note 12, the loan is anticipated to be paid in full from proceeds of a 2015 scheduled sale of the Company. At December 31, 2014 and 2013, the Company had outstanding borrowings of $265,290,980 and $284,392,275, respectively.

The loan bears interest at the London InterBank Offered Rate (LIBOR) plus the stated spread. LIBOR was .25% as of December 31, 2014 and 2013. The spread is 3.75% effective September 28, 2012. The loan currently requires monthly payments of principal and quarterly payments of interest.

The Company failed to meet its liquidity and Debt Service Coverage Ratio (DSCR) requirements under the original loan agreement with Nordbank at each quarter end in 2008 and for the quarter ended March 31, 2009. This precipitated the Second Amended and Restated Loan Agreement (the Loan Agreement) that was executed on October 27, 2009 (the Closing Date). The modification resulted in the waiver of default interest, the waiver of principal amortization due July 1, 2009, the postponement of ongoing principal amortization for 13 months, modification of the covenant requirements, and the modification of the swap arrangements.

The Company determined the modification to be a troubled debt restructuring in accordance with ASC 470, *Debt*, that required the effects of a restructuring involving only modification of terms of a payable, and not a transfer of assets or grant of equity interest, be accounted for prospectively from the time of the restructuring, and shall not change the carrying amount of the long-term debt unless the carrying amount exceeds the total future cash payments specified by the new terms.

As the total future cash payments required by the terms of the Loan Agreement exceeded the carrying value of the loan at the Closing Date, which includes principal and accrued interest less unamortized financing costs, interest expense is being accounted for prospectively using the effective interest rate, which is determined to be 3.85% annually. The default interest, which was waived as part of the 2009 loan modification, is being amortized as a credit to interest expense. The amortization during 2014 and 2013 was $745,159 and $723,506, respectively. As of December 31, 2014, the remaining unamortized default interest was $775,916.

Under the Loan Agreement, the Company was not required to meet a DSCR threshold until the quarter ended March 31, 2012. The DSCR is calculated as the ratio of earnings – before the deduction of interest, taxes, depreciation and amortization, plus the net cash received and refunded for entrance fees – to principal and interest, including interest related to interest rate swap agreements, for the period. A failure to achieve a DSCR of at least 1.00:1 will constitute an event of default. In addition, beginning June 30, 2012, and semiannually thereafter on each December 31st and June 30th, the Company must deliver computations of Excess Cash Flow (ECF), noting any prior prepayments from ECF, and at Nordbank's option, prepay a portion of the loan not to exceed 50% of ECF. ECF is a measure of the cumulative increase in cash from the Closing Date through the quarter preceding the measurement date, less certain adjustments.

On September 28, 2012, the Second Amendment to the Loan Agreement was executed. This agreement extended the maturity date of the second extension option to December 31, 2014 and the maturity date of the third extension option to December 31, 2015. Additionally, the margin with respect to LIBOR was increased to 3.75% effective September 28, 2012. Under the new Loan Agreement, the maximum percentage of ECF was increased to 90% and the DSCR was increased to 1.15:1.0 as a condition for the third extension. Effective with this amendment, the second extension option was exercised.

The Company determined this amendment to be a modification in accordance with ASC 470, *Debt*, which requires the calculation of a new effective interest rate. As noted above, this was determined to be 3.85%.

The DSCR was met for all quarters of 2014 and 2013. The June 30, 2013 ECF calculation resulted in a prepayment on the loan in 2013 in the amount of $1,731,821. The December 31, 2013 and June 30, 2014 ECF calculations resulted in prepayments on the loan made by the Parent Company in March and September 2014 of $6,440,175 and $4,108,706, respectively. The December 31, 2014 ECF calculation resulted in prepayment on the loan made by the Parent Company in March 2015 of $5,988,353.

Under the Loan Agreement, the Company is subject to certain nonfinancial covenants. The Company is in compliance with all debt covenants as of December 31, 2014 and 2013.

The fair value of the Company's note payable is estimated based on current rates offered for debt with the same remaining maturities and comparable collateralizing assets. Changes in assumptions or methodologies used to make estimates may have a material effect on the estimated fair value. In accordance with ASC 820, management has applied Level 2 inputs to determine that the estimated fair value of the Company's long-term debt was $264,599,210 and $283,009,770 at December 31, 2014 and 2013, respectively.

The Company executed a five-year installment loan agreement with Wells Fargo Equipment Finance, Inc. in April 2012 in the amount of $99,929 of which $51,388 remained outstanding as of December 31, 2014.

The proceeds were used to purchase a new bus at Fountains at Bronson Place. The loan bears an interest rate of 4.95% and is secured by the bus. Payments of interest and principal are due monthly.

Scheduled annual principal maturities of the note payable until maturity, and the installment loan are as follows:

2015	$ 265,311,500
2016	21,559
2017	9,309
Total scheduled principal maturities	265,342,368
Unamortized waived interest	775,916
Total note payable	266,118,284
Less current maturities	266,087,416
Note payable – less current maturities	$ 30,868

The Company executed a new interest rate swap agreement with Nordbank effective September 28, 2012. The swap agreement is designated as a hedge in accordance with ASC 815, *Derivatives and Hedging*. This interest rate swap was held to reduce to the risk of changes in LIBOR on the interest payments on the note payable. The swap agreement expired December 29, 2014.

The fair value of the interest rate swap at December 31, 2013 was a liability of $402,586. As the Company's interest rate swap agreement is not traded on a market exchange, the fair value is obtained from quoted prices that are determined through a discounted cash flow approach using market-based interest rate yield curves, which are considered Level 2 inputs in accordance with ASC 820. The fair value of the interest rate swap agreement is recorded in the derivative liability in the accompanying consolidated balance sheets. Changes in fair value of the interest rate swap agreement are included in other (expense) income in the accompanying consolidated statements of operations.

The Company utilized this interest-rate related derivative instrument (interest rate swap agreement) to manage its exposure on its debt instruments. The Company does not enter into derivative instruments for any purpose other than to mitigate the impact of changes in interest rates on its cash flows. That is, the Company does not speculate using derivative instruments.

ASC 820 requires that nonperformance risk be considered in measuring the fair value of assets and liabilities. For derivatives, nonperformance risk refers to the risk that one of the parties to a derivative transaction will be unable to perform under the contractual terms of that derivative, such as the risk that one party will be unable to make cash payments at periodic net settlement dates or upon termination. The Company has considered the counterparty's credit risk as well as the effect of its own credit standing in determining the fair value of its interest rate swap agreements. The Company minimizes the credit risk in derivative instruments by entering into transactions with high-quality counterparties.

(6) Capital Lease Obligation

The Company leased five vehicles under capital leases in 2013 and an additional three vehicles in 2014. The following is a schedule of future minimum lease payments under these capital leases together with the present value of net minimum lease payments as of December 31, 2014:

Year ending December 31:		
2015	$	128,451
2016		128,451
2017		128,451
2018		101,336
2019		22,244
Total minimum lease payments		508,933
Less amount representing interest		(59,823)
Present value of net minimum lease payments		449,110
Less current portion		(103,818)
Capital lease obligation–less current portion	$	345,292

(7) Member's Deficit

The operating agreement details the commitments of the member and provides the procedures for the return of capital to the member with defined priorities. All profits and losses, net cash flow from operations and capital proceeds, if any, are to be distributed according to the priorities specified in the operating agreement. As of December 31, 2014 and 2013, US SLI is the sole member.

(8) Lease Income

The Company receives lease income from nonresidential tenants under operating leases. Future minimum lease receipts as of December 31, 2014 are as follows:

Year ending December 31:		
2015	$	4,849,806
2016		2,669,843
2017		1,456,263
2018		1,478,107
Total	$	10,454,019

No single tenant accounts for more than 2.3% of the Company's total revenue in 2014 and 2013. The tenant base includes nursing homes, assisted living providers, and homeowners' associations. Future minimum lease payments do not include amounts received for reimbursement of the facility operating expenses.

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Additionally, future minimum lease payments do not include revenues earned from temporary tenants with lease commitments that span less than one year.

(9) Lease Expense

The Company entered into a contingent lease agreement for the use of a health center. The rent expense is based on the actual costs allocable to the premises for a lease year. There is not a fixed minimum lease payment. The lease is for a term of 99 years or the useful life of the building, whichever is shorter. The lease expense for the years ended December 31, 2014 and 2013 was $732,408 in both years and is included in lease expense in the accompanying consolidated statements of operations.

In addition to the health center lease, the Company is obligated to reimburse the related homeowner's association (HOA) for fees charged for independent living residents. These fees include dues, basic food service fee, second person fees and parking. The fees paid to the HOA for the years ended December 31, 2014 and 2013 were $2,591,264 and $2,503,786, respectively, and are included in lease expense in the accompanying consolidated statements of operations.

(10) Commitments and Contingencies

The Company is involved in claims and lawsuits incidental to the ordinary course of business. While the outcome of these claims and lawsuits cannot be predicted with certainty, management of the Company does not believe the ultimate resolution of these matters will have a material adverse effect on the Company's consolidated financial statements.

Watermark has provided the Company limited indemnifications against actions taken on behalf of the Company in Watermark's capacity as manager. The Watermark indemnity rights may not protect the Company against all of the risks and possible losses faced by the Company from Watermark's role as manager.

The Company acquired the Facilities subject to a potential contingent liability of $23,032,890 to refund certain entrance fees collected prior to the acquisition date. Since these fees were collected by the prior owner of the Facilities and did not represent a legal obligation to the Company unless the residents vacated their units prior to certain contractually determined dates, no liability was recorded at the time of the acquisition. As of December 31, 2014 and 2013, the remaining amount of this contingent liability was $2,656,629 and $3,530,155, respectively. As it is not probable the Company will have to pay this amount, no liability has been recorded as of December 31, 2014 and 2013.

At December 31, 2014 and 2013, the Company had entered into approximately $823,000 and $1,340,000, respectively, in firm commitments for the completion of construction projects.

(11) Employee Benefit Plans

The Company offers a 401(k) retirement plan (the 401(k) Plan) under Watermark Services IV, LLC for the benefit of the employees. Employees that complete six months of service and are 21 years of age or older may participate in the 401(k) Plan. Employees may make pretax salary deferrals of 1% to 75% of their compensation, subject to annual dollar limits determined by the Internal Revenue Service. Employer matching contributions for the 401(k) Plan are on a discretionary year-end match. To receive the match, employees must be actively employed as of the last day of the year. The Company contributed a total of approximately $176,505 and $151,265 during the years ended December 31, 2014 and 2013, respectively, to the 401(k) Plan.

(12) Subsequent Events

In preparing the consolidated financial statements, the Company evaluated subsequent events occurring through April 30, 2015, the date the consolidated financial statements were available to be issued, in accordance with the Company's procedures related to disclosure of subsequent events.

The Company executed a purchase and sale agreement ("PSA") on February 18, 2015 in which the Company, along with all the subsidiaries of the Company, is a party to the agreement whereby each subsidiary will sell its respective property and transfer licenses to the buyer. The closing date has not yet been determined as of the issuance of these financial statements. Proceeds from the sale are anticipated to be sufficient to repay the Nordbank loan in full at closing and no loss on the sale is anticipated.

FOUNTAINS CARLOTTA SL, L.P.

Supplementary Information

December 31, 2014

(With Independent Auditors' Report on
Supplementary Information Thereon)

RECEIVED
MAY 05 2015
CONTINUING CARE
CONTRACTS BRANCH

KPMG

KPMG LLP
Suite 800
60 East Rio Salado Parkway
Tempe, AZ 85281-9125

Independent Auditors' Report on Supplementary Information

The Partners
Fountains Carlotta SL, L.P.:

We have audited the financial statements of Fountains Carlotta SL, L.P. (an indirect wholly owned subsidiary of Fountains Senior Living Holdings, LLC) as of and for the year ended December 31, 2014, and have issued our report thereon dated April 30, 2015, which contained an unmodified opinion on those financial statements. Our audit was performed for the purpose of forming an opinion on the financial statements as a whole. The accompanying Forms 5-1 through 5-5 (the Forms) are presented for the purpose of additional analysis and are not a required part of the financial statements. Such information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the financial statements. The information has been subjected to the auditing procedures applied in the audit of the financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the financial statements or to the financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the Forms are fairly stated in all material respects in relation to the financial statements as a whole.

Restriction of Use

Our report is intended solely for the information and use of Fountains Carlotta SL, L.P. and the California Department of Social Services and is not intended to be and should not be used by anyone other than these specified parties.

KPMG LLP

Phoenix, Arizona
April 30, 2015

FORM 5-1
LONG-TERM DEBT INCURRED IN A PRIOR FISCAL YEAR
(Including Balloon Debt)

Long-Term Debt Obligation	(a) Date Incurred	(b) Principal Paid During Fiscal Year	(c) Interest Paid During Fiscal Year	(d) Credit Enhancement Premiums Paid in Fiscal Year	(e) Total Paid (columns (b) + (c) + (d))
1	07/01/05	$540,121	$914,977		$1,455,098
2					$0
3					$0
4					$0
5					$0
6					$0
7					$0
8					$0
		TOTAL:	$914,977	$0	$1,455,098

(Transfer this amount to Form 5-3, Line 1)

NOTE: For column (b), do not include voluntary payments made to pay down principal.

PROVIDER: Fountains Senior Living Holdings, LLC

FORM 5-2
LONG-TERM DEBT INCURRED
DURING FISCAL YEAR
(Including Balloon Debt)

Long-Term Debt Obligation	(a) Date Incurred	(b) Total Interest Paid During Fiscal Year	(c) Amount of Most Recent Payment on the Debt	(d) Number of Payments over next 12 months	(e) Reserve Requirement (see instruction 5) (columns (c) x (d))
1					$0
2					$0
3					$0
4					$0
5					$0
6					$0
7					$0
8					$0
	TOTAL:	$0	$0	0	$0

(Transfer this amount to Form 5-3, Line 2)

NOTE: For column (b), do not include voluntary payments made to pay down principal.

PROVIDER: Fountains Senior Living Holdings, LLC

FORM 5-3
CALCULATION OF LONG-TERM DEBT RESERVE AMOUNT

Line		TOTAL
1	Total from Form 5-1 bottom of Column (e)	$1,455,098
2	Total from Form 5-2 bottom of Column (e)	$0
3	Facility leasehold or rental payment paid by provider during fiscal year (including related payments such as lease insurance)	
4	**TOTAL AMOUNT REQUIRED FOR LONG-TERM DEBT RESERVE:**	$1,455,098

PROVIDER: Fountains Senior Living Holdings, LLC

FORM 5-4
CALCULATION OF NET OPERATING EXPENSES

Line			Amounts	TOTAL
1		Total operating expenses from financial statements		$15,143,842
2		Deductions:		
	a.	Interest paid on long-term debt (see instructions)	$914,977	
	b.	Credit enhancement premiums paid for long-term debt (see instructions)	$0	
	c.	Depreciation	$1,289,197	
	d.	Amortization	$0	
	e.	Revenues received during the fiscal year for services to persons who did not have a continuing care contract	$8,260,454	
	f.	Extraordinary expenses approved by the Department	$0	
3		Total Deductions		$10,464,628
4		Net Operating Expenses		$4,679,214
5		Divide Line 4 by 365 and enter the result.		$12,820
6		**Multiply Line 5 by 75 and enter the result.** This is the provider's operating expense reserve amount.		$961,482

PROVIDER: Fountains Senior Living Holdings, LLC
COMMUNITY: The Fountains at The Carlotta

FORM 5-5
ANNUAL RESERVE CERTIFICATION

Provider Name: Fountains Senior Living Holdings, LLC
Fiscal Year Ended: December 31, 2014

We have reviewed our debt service reserve and operating expense reserve requirements as of, and for the period ended December 31, 2014 and are in compliance with those requirements.

Our liquid reserve requirements, computed using the audited financial statements for the fiscal year are as follows:

		Amount
[1]	Debt Service Reserve Amount	$1,455,098
[2]	Operating Expense Reserve Amount	$961,482
[3]	**Total Liquid Reserve Amount:**	$2,416,580

Qualifying assets sufficient to fulfill the above requirements are held as follows:

	Qualifying Asset Description	Amount (market value at end of quarter) Debt Service Reserve		Operating Reserve
[4]	Cash and Cash Equivalents	$1,500,000		$1,000,000
[5]	Investment Securities			
[6]	Equity Securities			
[7]	Unused/Available Lines of Credit			
[8]	Unused/Available Letters of Credit			
[9]	Debt Service Reserve			(not applicable)
[10]	Other: (describe qualifying asset)			
	Total Amount of Qualifying Assets Listed for Reserve Obligation: [11]	$1,500,000	[12]	$1,000,000
	Reserve Obligation Amount: [13]	$1,455,098	[14]	$961,482
	Surplus/(Deficiency): [15]	$44,902	[16]	$38,518

Signature:

(Authorized Representative)

Date:

(Title)

Attachment A to Form 5-4

Fountains Carlotta SL, L.P.

Year ended December 31, 2014

Line 1:		
Total operating expenses	$	14,203,077
Long-term debt Interest paid		940,765
Total operating expenses line 1	$	15,143,842
Line 2a:		
Interest paid	$	928,242
Less nondebt interest		(13,265)
Interest paid on long-term debt line 2a	$	914,977

Line 2e		Revenue per audited financial statements	Received from residents with continuing care contracts		Received from persons without continuing care contracts
Resident fees	$	6,625,509	4,922,044		1,703,465
Healthcare revenue		6,476,057	234		6,475,823
Amortization of entrance fees		1,146,283	1,146,283		—
Other income		170,113	88,947		81,166
Total operating revenue	$	14,417,962	6,157,508		8,260,454
Assisted living resident service fees				$	1,711,682
Guest food service revenue					37,597
Guest apartment					21,845
Health center (skilled nursing facility revenue)					6,489,330
Total line 2e				$	8,260,454

Attachment B to Form 5-5

Fountains Carlotta SL, L.P.

Designated Cash Reserves

December 31, 2014

	Balance at December 31, 2013	Designated funds	Not designated	Designated use
Fountains Senior Living, Holdings, LLC:				
Wells Fargo operating account	$ 12,346,439	8,288,000	4,058,439	Carlotta required reserves and loan prepayment
Wells Fargo Capex account	995,230	995,230	—	Capital expenditures
	13,341,669	9,283,230	4,058,439	
Fountains at Carlotta SL, LP:				
Wells Fargo operating account	467,150	200,000	267,150	Operating reserve
Total	$ 13,808,819	9,483,230	4,325,589	

Provider: Fountains Senior Living Holdings, LLC

Community: The Fountains at the Carlotta

Date Prepared: 4/29/15

Continuing Care Retirement Community
Disclosure Statement
General Information

FACILITY NAME: The Fountains at The Carlotta

ADDRESS: 41505 Carlotta Drive, Palm Desert, CA ZIP CODE: 92211 PHONE: 706 346-5420

PROVIDER NAME: Fountains Senior Living Holdings, LLC FACILITY OPERATOR: Fountains Senior Living Holdings, LLC

RELATED FACILITIES: RELIGIOUS AFFILIATION: None

YEAR OPENED: 1997 # OF ACRES: 20 ☐ SINGLE STORY ☐ MULTI-STORY ☑ OTHER: Both MILES TO SHOPPING CTR: 1 MILES TO HOSPITAL: 5

* *

NUMBER OF UNITS:

RESIDENTIAL LIVING

APARTMENTS – STUDIO: 0
APARTMENTS – 1 BDRM: 23
APARTMENTS – 2 BDRM: 88
COTTAGES/HOUSES: 63
RLU OCCUPANCY (%) AT YEAR END: 83.33

HEALTH CARE

ASSISTED LIVING: 35
SKILLED NURSING: 46
SPECIAL CARE: N/A
DESCRIPTION: > N/A
>

* *

TYPE OF OWNERSHIP: ☐ NOT-FOR-PROFIT ☑ FOR- PROFIT ACCREDITED?: ☐ YES ☐ NO BY:

FORM OF CONTRACT: *(Check all that apply)* ☑ CONTINUING CARE ☐ LIFE CARE ☑ ENTRANCE FEE ☐ FEE FOR SERVICE ☐ ASSIGNMENT OF ASSETS ☐ EQUITY ☐ MEMBERSHIP ☑ RENTAL

REFUND PROVISIONS: *(Check all that apply)* ☐90% ☐75% ☑50% ☐FULLY AMORTIZED ☐OTHER:

RANGE OF ENTRANCE FEES: $ 130,000.00 - $ 225,000.00 **LONG-TERM CARE INSURANCE REQUIRED?** ☐ YES ■ NO

HEALTH CARE BENEFITS INCLUDED IN CONTRACT: 10 Lifecare days

ENTRY REQUIREMENTS: MIN. AGE: 60 PRIOR PROFESSION: N/A OTHER: N/A

RESIDENT REPRESENTATIVE(S) TO THE BOARD (briefly describe their involvement): >
>

* *

FACILITY SERVICES AND AMENITIES

COMMON AREA AMENITIES	AVAILABLE	FEE FOR SERVICE
BEAUTY/BARBER SHOP	☐	☑
BILLIARD ROOM	☑	☐
BOWLING GREEN	☐	☐
CARD ROOMS	☑	☐
CHAPEL	☑	☐
COFFEE SHOP	☑	☐
CRAFT ROOMS	☑	☐
EXERCISE ROOM	☑	☐
GOLF COURSE ACCESS	☑	☐
LIBRARY	☑	☐
PUTTING GREEN	☑	☐
SHUFFLEBOARD	☑	☐
SPA	☑	☐
SWIMMING POOL-INDOOR	☐	☐
SWIMMING POOL-OUTDOOR	☑	☐
TENNIS COURT	☐	☐
WORKSHOP	☐	☐
OTHER ______	☐	☐

SERVICES AVAILABLE	INCLUDED IN FEE	FOR EXTRA CHARGE
HOUSEKEEPING (2 TIMES/MONTH)	☑	☐
MEALS (1 /DAY)	☑	☐
SPECIAL DIETS AVAILABLE	☑	☐
24-HOUR EMERGENCY RESPONSE	☑	☐
ACTIVITIES PROGRAM	☑	☐
ALL UTILITIES EXCEPT PHONE	☑	☐
APARTMENT MAINTENANCE	☑	☐
CABLE TV	☑	☐
LINENS FURNISHED	☐	☐
LINENS LAUNDERED	☐	☐
MEDICATION MANAGEMENT	☐	☑
NURSING/WELLNESS CLINIC	☑	☑
PERSONAL HOME CARE	☐	☑
TRANSPORTATION-PERSONAL	☑	☑
TRANSPORTATION-PREARRANGED	☑	☑
OTHER ______	☐	☐

All providers are required by Health and Safety Code section 1789.1 to provide this report to prospective residents before executing a deposit agreement or continuing care contract, or receiving any payment. Many communities are part of multi-facility operations which may influence financial reporting. Consumers are encouraged to ask questions of the continuing care retirement community that they are considering and to seek advice from professional advisors.

PROVIDER NAME: FOUNTAINS SENIOR LIVING HOLDINGS, LLC

CCRC	Location (City)	State	Phone with Area Code
The Fountains at Bronson Place	Kalamazoo	MI	269-382-3546
The Fountains at Canterbury	Oklahoma City	OK	405-751-3600
The Fountains at The Carlotta	Palm Desert	CA	760-346-5420
The Fountains at Lake Pointe Woods	Sarasota	FL	941-929-2400
The Fountains at Washington House	Alexandria	VA	703-845-5000

MLRC (MULTI-LEVEL RETIREMENT COMMUNITIES)	City	State	Phone with Area Code
The Fountains at The Albemarle	Tarboro	NC	252-823-2799
The Fountains at Boca Ciega Bay	St. Petersburg	FL	727-381-5411
The Fountains at Crystal Lake	Crystal Lake	IL	815-455-8400
The Fountains at Franklin	Southfield	MI	248-353-2810
The Fountains at Greenbriar	Independence	MO	816-257-5100
The Fountains at La Cholla	Tucson	AZ	816-797-2001
The Fountains at Pacific Regent-Bellevue	Bellevue	WA	425-646-9808
The Fountains at Millbrook	Millbrook	NY	845-677-8550
The Fountains at Rivervue	Tuckahoe	NY	914-768-6000
The Fountains at Sea Bluffs	Dana Point	CA	949-234-3000

PROVIDER NAME: Fountains Senior Living Holdings, LLC

	2011	2012	2013	2014
INCOME FROM ONGOING OPERATIONS				
OPERATING INCOME (Excluding amortization of entrance fee income)	$12,389,101	$12,461,577	$12,471,898	$13,271,679
LESS OPERATING EXPENSES (Excluding depreciation, amortization, and interest)	12,801,910	12,130,746	12,676,935	$12,913,880
NET INCOME FROM OPERATIONS	-412,809	330,831	-205,037	357,799
LESS INTEREST EXPENSE	1,048,148	876,373	989,940	940,765
PLUS CONTRIBUTIONS				
PLUS NON-OPERATING INCOME (EXPENSES) (excluding extraordinary items)	492,696	265,658	2,974	87,869
NET INCOME (LOSS) BEFORE ENTRANCE FEES, DEPRECIATION AND AMORTIZATION	-968,259	-279,884	-1,192,003	-670,835
NET CASH FLOW FROM ENTRANCE FEES (Total Deposits Less Refunds)	2,177,004	-314,918	2,836,644	3,006,603

* *

DESCRIPTION OF SECURED DEBT *(as of most recent fiscal year end)*

LENDER	OUTSTANDING BALANCE	INTEREST RATE	DATE OF ORIGINATION	DATE OF MATURITY	AMORTIZATION PERIOD
Nordbank	$21,074,562	LIBOR + 3.75%	7/1/05	12/31/15	12 months

* *

FINANCIAL RATIOS (see next page for ratio formulas)

	2013 CCAC Medians 50th Percentile *(optional)*	2012	2013	2014
DEBT TO ASSET RATIO		102.9	102.8	0
OPERATING RATIO		97.4	101.6	97.3
DEBT SERVICE COVERAGE RATIO		105.47	184.71	225.18
DAYS CASH ON HAND RATIO		21	23	13

* *

HISTORICAL MONTHLY SERVICE FEES (Average Fee and Change Percentage)

	2011	%	2012	%	2013	%	2014
STUDIO	2,871	-1.9	2,817	2.9	2,900	3.0	2,987
ONE BEDROOM	1,782	.2	1,785	12.0	2,000	3.0	2,060
TWO BEDROOM	2,481	-.8	2,462	-1.5	2,425	3.0	2,498
COTTAGE/HOUSE	2,587	3.0	2,664	5.7	2,815	3.0	2,899
ASSISTED LIVING	3,808	6.9	4,070	-.5	4,050	3.0	4,172
SKILLED NURSING	7,057	22.8	8,669	.4	8,700	.0	8,700
SPECIAL CARE							

* *

COMMENTS FROM PROVIDER: >

>

>

PROVIDER NAME: Fountains Senior Living Holdings, LLC

FINANCIAL RATIO FORMULAS

LONG-TERM DEBT TO TOTAL ASSETS RATIO

$$\frac{\text{Long-Term Debt, less Current Portion}}{\text{Total Assets}}$$

OPERATING RATIO

$$\frac{\text{Total Operating Expenses} - \text{Depreciation Expense} - \text{Amortization Expense}}{\text{Total Operating Revenues} - \text{Amortization of Deferred Revenue}}$$

DEBT SERVICE COVERAGE RATIO

$$\frac{\text{Total Excess of Revenues over Expenses} + \text{Interest, Depreciation, and Amortization Expenses} \text{ Amortization of Deferred Revenue} + \text{Net Proceeds from Entrance Fees}}{\text{Annual Debt Service}}$$

DAYS CASH ON HAND RATIO

$$\frac{\text{Unrestricted Current Cash \& Investments} + \text{Unrestricted Non-Current Cash \& Investments}}{(\text{Operating Expenses} - \text{Depreciation} - \text{Amortization})/365}$$

NOTE: These formulas are also used by the Continuing Care Accreditation Commission. For each formula, that organization also publishes annual median figures for certain continuing care retirement communities.

FORM 7-1
REPORT ON CCRC MONTHLY SERVICE FEES

		RESIDENTIAL LIVING	ASSISTED LIVING	SKILLED NURSING
[1]	Monthly service fees at beginning of reporting period: (Indicate range, if applicable)	$2,175 -$3,085	$2,500 - $4,050	$7,360 - $8,820.
[2]	Indicate percentage of increase in fees imposed during reporting period: (Indicate range, if applicable)	3.00%	3.00%	No rate increase

☐ Check here if monthly service fees at this community were not increased during the reporting period. (If you checked this box, please skip down to the bottom of this form and specify the names of the provider and the community.)

[3] Indicate the date the fee increase was implemented: IL 10/1/14, AL 11/1/14, SNF no increase
(if more than 1 increase was implemented, indicate the dates for each increase.)

[4] Check each of the appropriate boxes:

☒ Each fee increase is based on the provider's projected costs, prior year per capita costs, and economic indicators.

☒ All affected residents were given written notice of this fee increase at least 30 days prior to its implementation.

☒ At least 30 days prior to the increase in monthly service fees, the designated representative of the provider convened a meeting that all residents were invited to attend.

☒ At the meeting with residents, the provider discussed and explained the reasons for the increase, the basis for determining the amount of the increase, and the data used for calculating the increase.

☒ The provider provided residents with at least 14 days advance notice of each meeting held to discuss the fee increases.

☒ The governing body of the provider, or the designated representative of the provider posted notice of, and the agenda for, the meeting in a conspicuous place in the community at least 14 days prior to the meeting.

[5] On an attached page, provide a concise explanation for the increase in monthly service fees including the amount of the increase.

PROVIDER: Fountains Senior Living Holdings, Inc.

COMMUNITY: The Carlotta

The Carlotta

FORM 7-1a

REPORT ON CCRC MONTHLY SERVICE FEES

Monthly Service Fee Increase Explanation

IL Fees were increased in Oct and AL fees were increased in Nov both by 3%. There was no increase in fees for existing residents in 2013. The community updated the nurse call system and also made major unit renovations in 2014. With the renovations, increased utilities as well as general cost increases, there was a need to increase the fees in 2014.

SNF Fees were not increased in 2014

WATERMARK

2020 W. Rudasill Road Tucson, AZ 85704

May 22, 2015

California Department of Social Services
Continuing Care Contracts Branch
744 P Street, MS 8-3-90
Sacramento, CA 95814
ATTN: Allison Nakatomi

Dear Ms. Nakatomi:

Enclosed please find the 2014 Key Indicators Report for Fountains Senior Living Holdings, LLC which includes Fountains Carlotta SL, LP (Fountains at The Carlotta) located at 41-505 Carlotta Drive, Palm Desert, CA 92211.

Should you need additional information or have any questions, please contact me at 520-797-4000, ext 49.

Sincerely,

Theresa Varner

Theresa Varner
Senior Accountant
Watermark Retirement Communities, Inc.
On Behalf of Fountains at the Carlotta

KEY INDICATORS REPORT

Date Prepared: 5/18/2015

Fountains Senior Living Holdings, LLC (Carlotta)

Chief Executive Officer Signature

RECEIVED
MAY 26 2015
CONTINUING CARE CONTRACTS BRANCH

Please attach an explanatory memo that summarizes significant trends or variances in the key operational indicators.

	2010	2011	2012	2013	2014	Projected 2015	Forecast 2016	2017	2018	2019	Preferred Trend Indicator
OPERATIONAL STATISTICS											
1. Average Annual Occupancy by Site (%)	86.47%	86.08%	84.12%	84.06%	86.52%	87.30%	88.28%	88.48%	88.67%	88.87%	N/A
MARGIN (PROFITABILITY) INDICATORS											
2. Net Operating Margin (%)	12.93%	3.20%	5.42%	1.25%	10.75%	13.95%	13.95%	13.95%	13.95%	13.95%	↑
3. Net Operating Margin - Adjusted (%)	24.29%	16.88%	3.19%	19.35%	26.07%	29.89%	29.51%	29.13%	28.77%	28.41%	↓
LIQUIDITY INDICATORS											
4. Unrestricted Cash and Investments ($000)	$0	$136	$702	$793	$476	$500	$500	$500	$500	$500	↑
5. Days Cash on Hand (Unrestricted)	0	4.12	21.12	22.56	13.44	14.46	14.03	13.63	13.23	12.84	↑
CAPITAL STRUCTURE INDICATORS											
6. Deferred Revenue from Entrance Fees ($000)	$599	$836	$1,225	$1,160	$1,146	$653	$653	$653	$653	$653	N/A
7. Net Annual E/F proceeds ($000)	$1,868	$2,177	-$315	$2,837	$3,007	$3,335	$3,335	$3,335	$3,335	$3,335	N/A
8. Unrestricted Net Assets ($000)	$19,760	$20,178	$22,213	$21,424	$22,371	$22,371	$22,371	$22,371	$22,371	$22,371	N/A
9. Annual Capital Asset Expenditure ($000)	$1,159	$1,274	$1,291	$1,221	$2,462	$927	$955	$983	$1,013	$1,043	N/A
10. Annual Debt Service Coverage Revenue Basis (x)	1.50	0.87	0.76	-0.26	0.19	0.96	0.98	1.00	1.03	1.05	↑
11. Annual Debt Service Coverage (x)	3.07	2.23	0.56	1.73	2.25	3.25	3.27	3.3	3.32	3.35	↑
12. Annual Debt Service/Revenue (%)	9.56%	12.17%	11.00%	11.00%	10.01%	9.83%	9.55%	9.27%	9.00%	8.74%	↓
13. Average Annual Effective Interest Rate (%)	4.64%	4.40%	3.83%	4.49%	4.46%	4.58%	4.71%	4.84%	4.97%	5.12%	↓
14. Unrestricted Cash & Investments/ Long-Term Debt (%)	0.00%	0.57%	3.07%	3.60%	2.26%	2.43%	2.50%	2.57%	2.64%	2.72%	↑
15. Average Age of Facility (years)	24	25	26	27	28	29	30	31	32	33	↓