

CareTrust REIT, Inc.  
Form 10-Q  
November 02, 2016  
Table of Contents

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

FORM 10-Q

(Mark One)

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

For the quarterly period ended September 30, 2016

OR

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

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

Commission File Number: 001-36181

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

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

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

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

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

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

Large accelerated filer  Accelerated filer

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

Non-accelerated filer  (Do not check if a smaller reporting company)  Smaller reporting company   
Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).  Yes  No

As of November 1, 2016, there were 58,078,786 shares of common stock outstanding.

---

Table of Contents

INDEX

PART I—FINANCIAL INFORMATION

Item 1. <u>Financial Statements</u> (unaudited)	
<u>Condensed Consolidated Balance Sheets</u>	<u>1</u>
<u>Condensed Consolidated Income Statements</u>	<u>2</u>
<u>Condensed Consolidated Statements of Equity</u>	<u>3</u>
<u>Condensed Consolidated Statements of Cash Flows</u>	<u>4</u>
<u>Notes to Condensed Consolidated Financial Statements</u>	<u>5</u>
Item 2. <u>Management’s Discussion and Analysis of Financial Condition and Results of Operations</u>	<u>29</u>
Item 3. <u>Quantitative and Qualitative Disclosures About Market Risk</u>	<u>36</u>
Item 4. <u>Controls and Procedures</u>	<u>37</u>

PART II—OTHER INFORMATION

Item 1. <u>Legal Proceedings</u>	<u>37</u>
Item 1A. <u>Risk Factors</u>	<u>38</u>
Item 6. <u>Exhibits</u>	<u>38</u>
<u>Signatures</u>	<u>39</u>

---

Table of Contents

## PART I—FINANCIAL INFORMATION

## Item 1. Financial Statements.

## CARETRUST REIT, INC.

## CONDENSED CONSOLIDATED BALANCE SHEETS

(in thousands, except share and per share amounts)

(unaudited)

	September 30, 2016	December 31, 2015
Assets:		
Real estate investments, net	\$809,121	\$645,614
Other real estate investments	13,595	8,477
Cash and cash equivalents	11,878	11,467
Accounts receivable	5,666	2,342
Prepaid expenses and other assets	1,755	2,083
Deferred financing costs, net	3,074	3,183
Total assets	\$845,089	\$673,166
Liabilities and Equity:		
Senior unsecured notes payable, net	\$255,028	\$254,229
Senior unsecured term loan, net	99,398	—
Unsecured revolving credit facility	103,000	45,000
Mortgage notes payable, net	—	94,676
Accounts payable and accrued liabilities	15,015	9,269
Dividends payable	9,873	7,704
Total liabilities	482,314	410,878
Commitments and contingencies (Note 11)		
Equity:		
Preferred stock, \$0.01 par value; 100,000,000 shares authorized, no shares issued and outstanding as of September 30, 2016 and December 31, 2015	—	—
Common stock, \$0.01 par value; 500,000,000 shares authorized, 57,741,888 and 47,664,742 shares issued and outstanding as of September 30, 2016 and December 31, 2015, respectively	577	477
Additional paid-in capital	519,204	410,217
Cumulative distributions in excess of earnings	(157,006 )	(148,406 )
Total equity	362,775	262,288
Total liabilities and equity	\$845,089	\$673,166
See accompanying notes to condensed consolidated financial statements.		

Table of Contents

CARETRUST REIT, INC.  
 CONDENSED CONSOLIDATED INCOME STATEMENTS  
 (in thousands, except per share amounts)  
 (unaudited)

	For the Three Months Ended September 30, 2016		For the Nine Months Ended September 30, 2015	
Revenues:				
Rental income	\$24,179	\$15,778	\$67,857	\$45,869
Tenant reimbursements	2,089	1,320	5,815	3,866
Independent living facilities	766	626	2,177	1,868
Interest and other income	72	261	587	716
Total revenues	27,106	17,985	76,436	52,319
Expenses:				
Depreciation and amortization	8,248	5,815	23,433	17,093
Interest expense	5,743	7,221	17,370	19,111
Property taxes	2,089	1,320	5,815	3,866
Independent living facilities	708	610	1,926	1,778
Acquisition costs	203	—	203	—
General and administrative	2,283	2,292	6,724	5,440
Total expenses	19,274	17,258	55,471	47,288
Net income	\$7,832	\$727	\$20,965	\$5,031
Earnings per common share:				
Basic	\$0.13	\$0.02	\$0.38	\$0.14
Diluted	\$0.13	\$0.02	\$0.38	\$0.14
Weighted-average number of common shares:				
Basic	57,595	39,125	54,403	33,916
Diluted	57,595	39,125	54,403	33,916
Dividends declared per common share	\$0.17	\$0.16	\$0.51	\$0.48

See accompanying notes to condensed consolidated financial statements.

Table of Contents

CARETRUST REIT, INC.  
 CONDENSED CONSOLIDATED STATEMENTS OF EQUITY  
 (in thousands, except share and per share amounts)  
 (unaudited)

	Common Stock		Additional	Cumulative	Total
	Shares	Amount	Paid-in Capital	Distributions in Excess of Earnings	Equity
Balance as of December 31, 2014	31,251,157	\$ 313	\$246,041	\$(132,892 )	\$113,462
Issuance of common stock, net	16,330,000	163	162,800	—	162,963
Vesting of restricted common stock, net of shares withheld for employee taxes	83,585	1	(146 )	—	(145 )
Amortization of stock-based compensation	—	—	1,522	—	1,522
Common dividends (\$0.64 per share)	—	—	—	(25,548 )	(25,548 )
Net income	—	—	—	10,034	10,034
Balance as of December 31, 2015	47,664,742	477	410,217	(148,406 )	262,288
Issuance of common stock, net	9,958,012	99	108,296	—	108,395
Vesting of restricted common stock, net of shares withheld for employee taxes	119,134	1	(516 )	—	(515 )
Amortization of stock-based compensation	—	—	1,207	—	1,207
Common dividends (\$0.51 per share)	—	—	—	(29,565 )	(29,565 )
Net income	—	—	—	20,965	20,965
Balance as of September 30, 2016	57,741,888	\$ 577	\$519,204	\$(157,006 )	\$362,775

See accompanying notes to condensed consolidated financial statements.

Table of Contents

## CARETRUST REIT, INC.

## CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

(in thousands)

(unaudited)

	For the Nine Months Ended September 30,	
	2016	2015
Cash flows from operating activities:		
Net income	\$20,965	\$5,031
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization (including a below-market ground lease)	23,444	17,093
Amortization of deferred financing costs	1,678	1,649
Write-off of deferred financing costs	326	1,208
Amortization of stock-based compensation	1,207	1,095
Straight-line rental income	(78 )	—
Noncash interest income	(587 )	(697 )
Change in operating assets and liabilities:		
Accounts receivable	(3,246 )	(2,945 )
Accounts receivable due from related party	—	2,275
Prepaid expenses and other assets	3	(90 )
Accounts payable and accrued liabilities	5,801	4,416
Net cash provided by operating activities	49,513	29,035
Cash flows from investing activities:		
Acquisitions of real estate	(185,284)	(231,501)
Improvements to real estate	(258 )	(143 )
Purchases of equipment, furniture and fixtures	(139 )	(256 )
Preferred equity investments	(4,531 )	—
Escrow deposit for acquisition of real estate	(1,000 )	—
Net proceeds from sale of vacant land	—	30
Net cash used in investing activities	(191,212)	(231,870)
Cash flows from financing activities:		
Proceeds from the issuance of common stock, net	108,395	163,466
Proceeds from the issuance of senior unsecured term loan	100,000	—
Borrowings under unsecured revolving credit facility	150,000	45,000
Payments on unsecured revolving credit facility	(92,000 )	—
Borrowings under senior secured revolving credit facility	—	35,000
Repayments of borrowings under senior secured revolving credit facility	—	(35,000 )
Payments on the mortgage notes payable	(95,022 )	(2,509 )
Payments of deferred financing costs	(1,352 )	(2,113 )
Net-settle adjustment on restricted stock	(515 )	(145 )
Dividends paid on common stock	(27,396 )	(14,086 )
Net cash provided by financing activities	142,110	189,613
Net increase (decrease) in cash and cash equivalents	411	(13,222 )
Cash and cash equivalents beginning of period	11,467	25,320
Cash and cash equivalents end of period	\$11,878	\$12,098
Supplemental disclosures of cash flow information:		
Interest paid	\$12,173	\$12,338
Supplemental schedule of noncash investing and financing activities:		

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

Increase in dividends payable	\$2,169	\$3,758
Increase in offering costs payable	\$—	\$503
Application of escrow deposit to acquisition of real estate	\$1,250	\$500
See accompanying notes to condensed consolidated financial statements.		

4

---



Table of Contents

CARETRUST REIT, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS —

(Unaudited)

1. ORGANIZATION

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

Description of Business—The Company’s primary business consists of acquiring, financing and owning real property to be leased to third-party tenants in the healthcare sector. As of September 30, 2016, the Company owned and leased to independent operators, including Ensign, 149 skilled nursing, assisted living and independent living facilities consisting of 14,304 operational beds and units located in Arizona, California, Colorado, Florida, Georgia, Idaho, Indiana, Iowa, Maryland, Michigan, Minnesota, Nebraska, Nevada, North Carolina, Ohio, Texas, Utah, Virginia, Washington and Wisconsin. The Company also owns and operates three independent living facilities consisting of 264 units located in Texas and Utah. As of September 30, 2016, the Company also had three other real estate investments, consisting of \$13.6 million of preferred equity investments.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Basis of Presentation—The accompanying condensed consolidated financial statements of the Company reflect, for all periods presented, the historical financial position, results of operations and cash flows of the Company and its consolidated subsidiaries consisting of (i) the leased skilled nursing, assisted living and independent living facilities, (ii) the operations of the three independent living facilities and (iii) the preferred equity investments.

The accompanying condensed consolidated financial statements of the Company were prepared in accordance with accounting principles generally accepted in the United States (“GAAP”) for interim financial information and Article 10 of Regulation S-X. Accordingly, the condensed consolidated financial statements do not include all of the disclosures required by GAAP for a complete set of annual audited financial statements. The condensed consolidated financial statements should be read in conjunction with the audited consolidated and combined financial statements and notes thereto included in the Company’s Annual Report on Form 10-K for the fiscal year ended December 31, 2015. In the opinion of management, all adjustments which are of a normal and recurring nature and considered necessary for a fair presentation of the results of the interim periods presented have been included. The results of operations for the interim periods are not necessarily indicative of results for the full year. All intercompany transactions and account balances within the Company have been eliminated.

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

Real Estate Depreciation and Amortization—Costs related to the acquisition and improvement of properties are capitalized and amortized over the expected useful life of the asset on a straight-line basis. Repair and maintenance costs are expensed as incurred while significant replacements and betterments are capitalized. Repair and maintenance costs include all costs that do not extend the useful life of the real estate asset. The Company considers the period of future benefit of an asset to determine its appropriate useful life. Expenditures for tenant improvements are capitalized

and amortized over the shorter of the tenant's lease term or expected useful life. The Company anticipates the estimated useful lives of its assets by class to be generally as follows:

5

---

Table of Contents

CARETRUST REIT, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS —

(Unaudited)

Buildings	25-40 years
Building improvements	10-25 years
Tenant improvements	Shorter of lease term or expected useful life
Integral equipment, furniture and fixtures	5 years
Identified intangible assets	Shorter of lease term or expected useful life

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

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

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

As part of our asset acquisitions, the Company may commit to provide contingent payments to a seller or lessee (e.g., an earn-out payable upon the applicable property achieving certain financial metrics). Typically, when the contingent payments are funded, cash rent is increased by the amount funded multiplied by a rate stipulated in the agreement. Generally, if the contingent payment is an earn-out provided to the seller, the payment is capitalized to the property's basis. If the contingent payment is an earn-out provided to the lessee, the payment is recorded as a lease incentive and is amortized as a yield adjustment over the life of the lease.

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

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

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

Table of Contents

CARETRUST REIT, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS —

(Unaudited)

While the Company believes its assumptions are reasonable, changes in these assumptions may have a material impact on financial results.

**Other Real Estate Investments** — Preferred equity investments are accounted for at unpaid principal balance, plus accrued return, net of reserves. The Company recognizes return income on the applicable basis set forth in the preferred equity instrument based on the outstanding investment including any accrued and unpaid return. As the preferred member of any joint venture in which the Company has an investment, the Company is not entitled to share in such joint venture's earnings or losses. Rather, the Company is entitled to receive a preferred return, which is deferred if the cash flow of the joint venture is insufficient to pay all of the accrued preferred return. The unpaid accrued preferred return is added to the balance of the preferred equity investment up to the estimated economic outcome assuming a hypothetical liquidation of the book value of the joint venture. Any unpaid accrued preferred return, whether recorded or unrecorded by the Company, will be repaid upon redemption.

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

**Cash and Cash Equivalents**—Cash and cash equivalents consist of bank term deposits and money market funds with original maturities of three months or less at time of purchase and therefore approximate fair value. The fair value of these investments is determined based on “Level 1” inputs, which consist of unadjusted quoted prices in active markets that are accessible at the measurement date for identical, unrestricted assets. The Company places its cash and short-term investments with high credit quality financial institutions.

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

**Deferred Financing Costs**—External costs incurred from placement of the Company's debt are capitalized and amortized on a straight-line basis over the terms of the related borrowings, which approximates the effective interest method. Amortization of deferred financing costs is classified as interest expense in the Company's condensed consolidated income statements. Accumulated amortization of deferred financing costs was \$3.7 million and \$3.3 million as of September 30, 2016 and December 31, 2015, respectively.

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

**Revenue Recognition** —The Company recognizes rental revenue, including rental abatements, lease incentives and contractual fixed increases attributable to operating leases, if any, from tenants under lease arrangements with minimum fixed and determinable increases on a straight-line basis over the non-cancellable term of the related leases when collectability is reasonably assured. Tenant reimbursements of real estate taxes, insurance, repairs and maintenance, and other operating expenses are recognized as revenue in the period the expenses are incurred and presented gross if the Company is the primary obligor and, with respect to purchasing goods and services from third-party suppliers, has discretion in selecting the supplier and bears the associated credit risk. For each of the three and nine months ended September 30, 2016 and 2015, such tenant reimbursement revenues consist of real estate taxes. Contingent revenue, if any, is not recognized until all possible contingencies have been eliminated.

The Company evaluates the collectability of rents and other receivables on a regular basis based on factors including payment history, the operations, the asset type and current economic conditions. If the Company's evaluation of these factors indicates it may not recover the full value of the receivable, it provides a reserve against the portion of the receivable that it estimates may not be recovered. This analysis requires the Company to determine whether there are

factors indicating a receivable may not be fully collectible and to estimate the amount of the receivable that may not be collected. The Company did not reserve any receivables as of September 30, 2016 or December 31, 2015.

7

---

Table of Contents

CARETRUST REIT, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS —

(Unaudited)

**Income Taxes**—The Company has elected to be taxed as a real estate investment trust ("REIT") under the Internal Revenue Code of 1986, as amended (the "Code"). The Company believes it has been organized and has operated, and the Company intends to continue to operate, in a manner to qualify for taxation as a REIT under the Code. To qualify as a REIT, the Company must meet certain organizational and operational requirements, including a requirement to distribute to its stockholders at least 90% of the Company's annual REIT taxable income (computed without regard to the dividends paid deduction or net capital gain and which does not necessarily equal net income as calculated in accordance with GAAP). As a REIT, the Company generally will not be subject to federal income tax to the extent it distributes as qualifying dividends all of its REIT taxable income to its stockholders. If the Company fails to qualify as a REIT in any taxable year, it will be subject to federal income tax on its taxable income at regular corporate income tax rates and generally will not be permitted to qualify for treatment as a REIT for federal income tax purposes for the four taxable years following the year during which qualification is lost unless the Internal Revenue Service grants the Company relief under certain statutory provisions.

**Stock-Based Compensation**—The Company accounts for share-based payment awards in accordance with ASC Topic 718, Compensation – Stock Compensation ("ASC 718"). ASC 718 requires that the cost resulting from all share-based payment transactions be recognized in the financial statements. ASC 718 requires all entities to apply a fair value-based measurement method in accounting for share-based payment transactions with directors, officers and employees except for equity instruments held by employee share ownership plans. Net income reflects stock-based compensation expense of \$0.3 million and \$0.4 million for the three months ended September 30, 2016 and 2015, respectively, and \$1.2 million and \$1.1 million for the nine months ended September 30, 2016 and 2015, respectively.

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

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

**Earnings (Loss) Per Share**—The Company calculates earnings (loss) per share ("EPS") in accordance with ASC Topic 260, Earnings Per Share. Basic EPS is computed by dividing net income applicable to common stock by the weighted-average number of common shares outstanding during the period. Diluted EPS reflects the additional dilution for all potentially-dilutive securities.

**Recently Issued Accounting Standards**—In May 2014, the FASB issued Accounting Standards Update ("ASU") No. 2014-09, Revenue from Contracts with Customers (Topic 606) ("ASU No. 2014-09"). ASU No. 2014-09 requires an entity to recognize the revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods and services. ASU No. 2014-09 supersedes the revenue requirements in Revenue Recognition (Topic 605) and most industry-specific guidance throughout the Industry Topics of the Codification. ASU No. 2014-09 does not apply to lease contracts within the scope of Leases (Topic 840). In August 2015, the FASB issued ASU No. 2015-14, which deferred the effective date of its new revenue recognition standard by one year. The standard will be effective for annual reporting periods, and interim periods therein, beginning after December 15, 2017. The Company is currently assessing the impact of adopting ASU No. 2014-09 but does not believe it will have a material effect on the Company's consolidated financial statements when adopted.

In January 2016, the FASB issued ASU No. 2016-01, Financial Instruments-Overall (Subtopic 825-10) ("ASU No. 2016-01"). ASU No. 2016-01 updates guidance related to recognition and measurement of financial assets and financial liabilities. ASU No. 2016-01 requires all equity investments to be measured at fair value with changes in the fair value recognized through net income (other than those accounted for under equity method of accounting or those

that result in consolidation of the investee). The amendments in ASU No. 2016-01 also require an entity to present separately in other comprehensive income the portion of the total change in the fair value of a liability resulting from a change in the instrument-specific credit risk when the entity has elected to measure the liability at fair value in accordance with the fair value option for financial instruments. In addition, the amendments in ASU No. 2016-01 eliminate the requirement to disclose the methods and significant assumptions used to estimate the fair value that is required to be disclosed for financial instruments measured at amortized cost on the balance sheet for public business entities. ASU No. 2016-01 is effective for fiscal years and interim periods within those years beginning after December 15, 2017, with early adoption permitted. The Company is currently evaluating the impact this guidance will have on its consolidated financial statements when adopted.



Table of Contents

CARETRUST REIT, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS —

(Unaudited)

In February 2016, the FASB issued ASU No. 2016-02, Leases (Topic 842) (“ASU No. 2016-02”). ASU No. 2016-02 supersedes guidance related to accounting for leases. ASU No. 2016-02 updates guidance around the recognition of lease assets and lease liabilities by lessees for those leases classified as operating leases under previous GAAP. The objective of ASU No. 2016-02 is to establish the principles that lessees and lessors shall apply to report useful information to users of financial statements about the amount, timing, and uncertainty of cash flows arising from a lease. ASU No. 2016-02 does not fundamentally change lessor accounting. However, some changes have been made to lessor accounting to conform and align the guidance in ASU No. 2016-02 with the lessee guidance and other areas within GAAP. ASU No. 2016-02 is effective for fiscal years and interim periods within those years beginning after December 15, 2018, with early adoption permitted. The Company is currently evaluating the impact this guidance will have on its consolidated financial statements when adopted.

In March 2016, the FASB issued ASU No. 2016-09, Compensation - Stock Compensation: Improvements to Employee Share-Based Payment Accounting (“ASU No. 2016-09”), which simplifies several aspects of the accounting for share-based payment transactions, including the income tax consequences, classification of awards as either equity or liabilities, and classification on the statement of cash flows. ASU No. 2016-09 is effective for annual periods and interim periods within those annual periods beginning after December 15, 2016, and early adoption is permitted. The Company is currently evaluating the impact the adoption will have on its consolidated financial statements.

In August 2016, the FASB issued ASU No. 2016-15, Statement of Cash Flows - Classification of Certain Cash Receipts and Cash Payments (“ASU 2016-15”), which provided guidance on certain specific cash flow issues, including, but not limited to, debt prepayment or extinguishment costs, contingent consideration payments made after a business combination and distributions received from equity method investees. ASU 2016-15 is effective for periods beginning after December 15, 2017, with early adoption permitted and shall be applied retrospectively where practicable. The Company is in the process of evaluating the impact the adoption will have on its consolidated financial statements.

Recently Adopted Accounting Standards—In August 2015, the FASB issued ASU No. 2015-15, Presentation and Subsequent Measurement of Debt Issuance Costs Associated with Line-of-Credit Arrangements - Amendments to SEC Paragraphs Pursuant to Staff Announcement at June 18, 2015 EITF Meeting (SEC Update) (“ASU No. 2015-15”). ASU No. 2015-15 was issued by the FASB in response to questions that arose after the issuance of ASU No. 2015-03, to incorporate a Securities and Exchange Commission (“SEC”) staff announcement that the SEC staff will not object to an entity presenting the cost of securing a revolving line of credit as an asset, regardless of whether a balance is outstanding. ASU No. 2015-15 was effective upon announcement.

On December 31, 2015, the Company retrospectively early adopted, for all comparative periods presented, ASU No. 2015-03, Simplifying the Presentation of Debt Issuance Costs (“ASU No. 2015-03”). The amendments in ASU No. 2015-03 require that debt issuance costs related to a recognized debt liability be presented in the balance sheet as a direct deduction from the carrying amount of that debt liability, consistent with debt discounts. The adoption of ASU No. 2015-03 resulted in a change to the location where debt issuance costs are presented in the balance sheet and did not have any other material impact on the Company's consolidated financial statements.

In February 2015, the FASB issued ASU No. 2015-02, Consolidation (Topic 810): Amendments to the Consolidation Analysis (“ASU No. 2015-02”), which makes certain changes to both the variable interest model and the voting model, including changes to (1) the identification of variable interests (fees paid to a decision maker or service provider), (2) the variable interest entity characteristics for a limited partnership or similar entity and (3) the primary beneficiary

determination. ASU No. 2015-02 was effective for fiscal years, and interim periods within these fiscal years, beginning after December 15, 2015. The adoption of ASU No. 2015-02 did not have a significant impact on the Company's consolidated financial statements.

In September 2015, the FASB issued ASU No. 2015-16, Business Combinations (Topic 805), Simplifying the Accounting for Measurement-Period Adjustments (“ASU No. 2015-16”). ASU No. 2015-16 eliminates the requirement that an acquirer in a business combination account for measurement-period adjustments retrospectively. Instead, an acquirer will recognize a measurement-period adjustment during the period in which it determines the amount of the adjustment, including the effect on earnings of any amounts it would have recorded in previous periods if the accounting had been completed at the acquisition date. ASU No. 2015-16 was effective for fiscal years, and interim periods within these fiscal years, beginning after December 15, 2015, with early adoption permitted. The adoption of ASU No. 2015-16 did not have a significant impact on the Company's consolidated financial statements.

Table of Contents

CARETRUST REIT, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS —

(Unaudited)

## 3. REAL ESTATE INVESTMENTS, NET

The following tables summarize our investment in owned properties as of September 30, 2016, and December 31, 2015 (dollars in thousands):

	September 30, 2016	December 31, 2015
Land	\$ 107,243	\$ 91,311
Buildings and improvements	788,895	627,453
Integral equipment, furniture and fixtures	62,051	54,388
Identified intangible assets	1,914	—
Real estate investments	960,103	773,152
Accumulated depreciation and amortization	(150,982 )	(127,538 )
Real estate investments, net	\$ 809,121	\$ 645,614

As of September 30, 2016, 94 of the Company's 152 facilities were leased to subsidiaries of Ensign under eight master leases (the "Ensign Master Leases") which commenced on June 1, 2014. The obligations under the Ensign Master Leases are guaranteed by Ensign. A default by any subsidiary of Ensign with regard to any facility leased pursuant to an Ensign Master Lease will result in a default under all of the Ensign Master Leases. The initial annual revenues from the Ensign Master Leases were \$56.0 million during each of the first two years of the Ensign Master Leases.

Commencing on June 1, 2016, the annual revenues from the Ensign Master Leases are escalated annually by an amount equal to the product of (1) the lesser of the percentage change in the Consumer Price Index ("CPI") (but not less than zero) or 2.5%, and (2) the prior year's rent. In addition to rent, the subsidiaries of Ensign that are tenants under the Ensign Master Leases are solely responsible for the costs related to the leased properties (including property taxes, insurance, and maintenance and repair costs).

As of September 30, 2016, 55 of the Company's 152 facilities were leased to various other operators under triple-net leases. All of these leases contain annual escalators based on CPI some of which are subject to a cap, or fixed rent escalators.

The Company's three remaining properties as of September 30, 2016 are the independent living facilities that the Company owns and operates.

The Company has only two identified intangible assets which relate to a below-market ground lease and three acquired operating leases. The ground lease has a remaining term of 81 years.

As of September 30, 2016, our total future minimum rental revenues for all of our tenants were (dollars in thousands):

Year	Amount
Remaining 2016	\$ 24,430
2017	97,906
2018	98,085
2019	96,181
2020	94,855
Thereafter	897,986
	\$ 1,309,443

## Recent Real Estate Acquisitions

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

10

---

Table of Contents

CARETRUST REIT, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS —

(Unaudited)

New Haven Assisted Living, LLC

In February 2016, the Company acquired New Haven of San Angelo, a 30-unit assisted living and memory care facility located in San Angelo, Texas, for \$4.9 million, which includes capitalized acquisition costs. In connection with the acquisition, the Company entered into a triple-net master lease with New Haven Assisted Living, LLC. The lease carries an initial term of 12.5 years with two five-year renewal options and CPI-based rent escalators. The Company anticipates initial annual lease revenues of \$0.4 million following this acquisition.

Trillium Healthcare Group, LLC

In February 2016, the Company acquired a nine facility 518-bed skilled nursing portfolio in Iowa for \$32.7 million, which includes capitalized acquisition costs. In connection with the acquisition, the Company amended its triple-net master lease with Trillium Healthcare Group, LLC. The amended lease carries a remaining term of 15 years with two five-year renewal options and CPI-based rent escalators. The base rent under the amended master lease increased by \$3.2 million per year following this acquisition. In March 2016, the Company acquired Cedar Falls Health Care Center, an 82-bed skilled nursing facility located in Cedar Falls, Iowa, for \$5.0 million, which includes capitalized acquisition costs. In connection with the acquisition, the Company further amended its triple-net master lease with Trillium Healthcare Group, LLC. The Company anticipates additional initial annual lease revenues of \$0.5 million following this acquisition.

Priority Life Care, LLC

In March 2016, the Company acquired three assisted living facilities consisting of 336 units located in Baltimore, Maryland, Fort Wayne, Indiana and West Allis, Wisconsin, for \$21.2 million, which includes capitalized acquisition costs. In connection with the acquisition, the Company entered into a triple-net master lease with Priority Life Care, LLC. The lease carries an initial term of 15 years with two five-year renewal options and CPI-based rent escalators. The Company anticipates initial annual lease revenues of \$1.8 million following this acquisition.

Better Senior Living Consulting, LLC

In March 2016, the Company acquired Lamplight Inn of Fort Myers, a 74-unit assisted living facility located in Fort Myers, Florida, for \$5.7 million, which includes capitalized acquisition costs. In connection with the acquisition, the Company amended its triple-net master lease with Better Senior Living Consulting, LLC. The amended lease carries a remaining term of 14 years with two five-year renewal options and CPI-based rent escalators. The Company anticipates additional initial annual lease revenues of \$0.5 million following this acquisition.

Pristine Senior Living, LLC

In April 2016, the Company acquired Victory Park Nursing Home, a 55-bed skilled nursing facility, and Victoria Retirement Community, a skilled nursing and assisted living campus with 90 skilled nursing beds and 69 assisted living beds, both located in Cincinnati, Ohio, for \$14.7 million, which includes capitalized acquisition costs. In connection with the acquisition, the Company amended its triple-net master lease with Pristine Senior Living, LLC. The Company anticipates additional initial annual lease revenues of \$1.4 million following this acquisition.

Cascadia Healthcare, LLC

In May 2016, the Company acquired Shaw Mountain at Cascadia, a 98-bed skilled nursing facility located in Boise, Idaho, for \$8.9 million, which includes capitalized acquisition costs. In connection with the acquisition, the Company entered into a triple-net master lease with Cascadia Healthcare, LLC. The lease carries an initial term of 15 years with three five-year renewal options and CPI-based rent escalators. The Company anticipates initial annual lease revenues of \$0.9 million following this acquisition.

Twenty/20 Management, Inc.



Table of Contents

CARETRUST REIT, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS —

(Unaudited)

In May 2016, the Company acquired English Meadows Elks' Home, a 175-unit independent and assisted living campus located in Bedford, Virginia, for \$10.1 million and a contingent \$5.0 million earn-out (subject to the achievement of certain financial metrics), which includes capitalized acquisition costs. In connection with the acquisition, the Company amended its triple-net master lease with Twenty/20 Management, Inc. The Company anticipates additional initial annual lease revenues of \$0.9 million following this acquisition.

**Premier Senior Living, LLC**

In May 2016, the Company acquired Croatan Village, a 46-unit assisted living and memory care facility located in New Bern, North Carolina, and Countryside Village, a 21-unit memory care facility located in Pikeville, North Carolina, for \$11.8 million, which includes capitalized acquisition costs. In connection with the acquisition, the Company entered into a triple-net master lease with Premier Senior Living, LLC. The lease carries an initial term of 15 years with two five-year renewal options and CPI-based rent escalators. The Company anticipates initial annual lease revenues of \$1.0 million following this acquisition. Additionally, in June 2016, the Company acquired a four facility 188-bed assisted living and memory care portfolio located in Michigan for \$30.7 million, which includes capitalized acquisition costs. In connection with the acquisition, the Company amended its triple-net master lease with Premier Senior Living. The Company anticipates additional initial annual lease revenues of \$2.5 million following this acquisition.

**West Harbor Healthcare, LLC**

In August 2016, the Company acquired The Oaks at Petaluma, a 59-bed skilled nursing facility located in Petaluma, California, for \$6.8 million, which includes capitalized acquisition costs. In connection with the acquisition, the Company entered into a triple-net master lease with West Harbor Healthcare, LLC. The lease carries an initial term of 15 years with two five-year renewal options and CPI-based rent escalators. The Company anticipates initial annual lease revenues of \$0.7 million following this acquisition.

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

**Covenant Care, LLC**

In August 2016, the Company acquired two skilled nursing and two assisted living properties located in California, for approximately \$34.3 million. For the three separate transactions, approximately \$0.2 million of estimated transaction costs were expensed during the three months ended September 30, 2016. The four properties are triple-net leased to Covenant Care under three leases. The Company anticipates initial annual lease revenues of \$3.1 million following these acquisitions. The leases expire in 2019 and have two five-year renewal options, and have CPI-based rent escalators (with a 3% floor). The Company estimated the fair value of the assets acquired on the acquisition date based on certain valuation analyses that have yet to be finalized, and accordingly, as detailed, are subject to adjustment once the analysis is completed.

**4. OTHER REAL ESTATE INVESTMENTS**

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

In July 2016, the Company completed a \$2.2 million preferred equity investment with an affiliate of Cascadia Development, LLC. The preferred equity investment yields a return equal to prime plus 9.5% but in no event less than

12% calculated on a quarterly basis on the outstanding carrying value of the investment. The investment will be used to develop a 99-bed skilled nursing facility in Nampa, Idaho. In connection with its investment, CareTrust obtained an option to purchase

12

---



Table of Contents

CARETRUST REIT, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS —

(Unaudited)

the development at a fixed-formula price upon stabilization, with an initial lease yield of at least 9.0%. The project is expected to be completed by October 2017.

In September 2016, the Company completed a \$2.3 million preferred equity investment with an affiliate of Cascadia Development, LLC. The preferred equity investment yields a return equal to prime plus 9.5% but in no event less than 12% calculated on a quarterly basis on the outstanding carrying value of the investment. The investment will be used to develop a 99-bed skilled nursing facility in Boise, Idaho. In connection with its investment, CareTrust obtained an option to purchase the development at a fixed-formula price upon stabilization, with an initial lease yield of at least 9.0%. The project is expected to be completed by early 2018.

During the three months ended September 30, 2016 and 2015, respectively, the Company recognized \$0.1 million and \$0.3 million of interest income and these unpaid amounts were added to the outstanding carrying values of the investments. During the nine months ended September 30, 2016 and 2015, respectively, the Company recognized \$0.6 million and \$0.7 million of interest income and these unpaid amounts were added to the outstanding carrying values of the investments.

**5. FAIR VALUE MEASUREMENTS**

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

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

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

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

Financial Instruments: Considerable judgment is necessary to estimate the fair value of financial instruments. The estimates of fair value presented herein are not necessarily indicative of the amounts that could be realized upon disposition of the financial instruments. A summary of the face values, carrying amounts and fair values of the Company's financial instruments as of September 30, 2016 and December 31, 2015 using Level 2 inputs, for the senior unsecured notes payable, and Level 3 inputs, for all other financial instruments, is as follows (dollars in thousands):

	September 30, 2016			December 31, 2015		
	Face Value	Carrying Amount	Fair Value	Face Value	Carrying Amount	Fair Value
Financial assets:						
Preferred equity investments	\$12,031	\$13,595	\$13,829	\$7,500	\$8,477	\$8,477
Financial liabilities:						
Senior unsecured notes payable	\$260,000	\$255,028	\$268,450	\$260,000	\$254,229	\$263,575

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

Mortgage notes payable	\$—	\$—	\$—	\$95,022	\$94,676	\$97,067
------------------------	-----	-----	-----	----------	----------	----------

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

Preferred equity investments: The carrying amounts were accounted for at the unpaid principal balance, plus accrued return, net of reserves, assuming a hypothetical liquidation of the book values of the joint ventures. The fair value of the preferred equity investments were estimated using an internal valuation model that considered the expected future cash flows of the investment, the underlying collateral value and other credit enhancements. In future periods, the fair value of the preferred equity investments may not be equal to the carrying amount.

Table of Contents

CARETRUST REIT, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS —

(Unaudited)

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

Unsecured revolving credit facility and senior unsecured term loan: The fair values approximate their carrying values as the interest rates are variable and approximate prevailing market interest rates for similar debt arrangements.

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

**6. RELATED PARTY TRANSACTIONS**

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

Christopher R. Christensen, one of the Company's directors from June 1, 2014 through April 15, 2015, served as the chief executive officer of Ensign as well as a member of Ensign's board of directors during such period. As such, all rental income and tenant reimbursements earned related to the Ensign Master Leases during Mr. Christensen's tenure on our board are considered related party in nature. For the nine months ended September 30, 2015, the Company recognized \$16.3 million in rental income from Ensign while Mr. Christensen sat on the Board of the Company as well as \$1.4 million of tenant reimbursements. After April 15, 2015, the effective date of Mr. Christensen's resignation from our board of directors, rental income and tenant reimbursements related to the Ensign Master Leases, and any related accounts receivable, are not considered earned or due from a related party.

**7. DEBT**

The following table summarizes the balance of our indebtedness as of September 30, 2016 and December 31, 2015 (in thousands):

	September 30, 2016			December 31, 2015		
	Principal Amount	Deferred Loan Fees	Carrying Value	Principal Amount	Deferred Loan Fees	Carrying Value
Senior unsecured notes payable	\$260,000	\$(4,972)	\$255,028	\$260,000	\$(5,771)	\$254,229
Senior unsecured term loan	100,000	(602)	99,398	—	—	—
Unsecured revolving credit facility	103,000	—	103,000	45,000	—	45,000
Mortgage notes payable	—	—	—	\$95,022	\$(346)	94,676
	\$463,000	\$(5,574)	\$457,426	\$400,022	\$(6,117)	\$393,905

**Senior Unsecured Notes Payable**

On May 30, 2014, the Company's wholly owned subsidiary, CTR Partnership, L.P. (the "Operating Partnership"), and its wholly owned subsidiary, CareTrust Capital Corp. (together with the Operating Partnership, the "Issuers"), completed a private offering of \$260.0 million aggregate principal amount of 5.875% Senior Notes due 2021 (the "Notes"). The Notes were issued at par, resulting in gross proceeds of \$260.0 million and net proceeds of approximately \$253.0

million after deducting underwriting fees and other offering expenses. The Company transferred approximately \$220.8 million of the net proceeds of the offering of the Notes to Ensign, and used the remaining portion of the net proceeds of the offering to pay the cash portion of

Table of Contents

CARETRUST REIT, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS —

(Unaudited)

the December 2014 special dividend. The Notes mature on June 1, 2021 and bear interest at a rate of 5.875% per year. Interest on the Notes is payable on June 1 and December 1 of each year, beginning on December 1, 2014.

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

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

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

As of September 30, 2016, the Company was in compliance with all applicable financial covenants under the indenture.

#### Unsecured Revolving Credit Facility and Term Loan

On August 5, 2015, the Company, CareTrust GP, LLC, the Operating Partnership, as the borrower, and certain of its wholly-owned subsidiaries entered into a credit and guaranty agreement with KeyBank National Association, as administrative agent, an issuing bank and swingline lender, and the lenders party thereto (the “Credit Agreement”). The Credit Agreement initially provided for an unsecured asset-based revolving credit facility (the “Credit Facility”) with commitments in an aggregate principal amount of \$300.0 million from a syndicate of banks and other financial institutions. A portion of the proceeds of the Credit Facility were used to pay off and terminate the Company’s existing secured asset-based revolving credit facility under a credit agreement dated May 30, 2014, with SunTrust Bank, as administrative agent, and the lenders party thereto. On February 1, 2016, the Company entered into the First Amendment (the “Amendment”) to the Credit Agreement. Pursuant to the Amendment, (i) commitments in respect of the Credit Facility were increased by \$100.0 million to \$400.0 million, (ii) a new \$100.0 million non-amortizing unsecured term loan (the “Term Loan”) was funded, and (iii) the uncommitted incremental facility was increased by \$50.0 million to \$250.0 million. The Credit Facility continues to mature on August 5, 2019, subject to two, six-month extension options. The Term Loan, which matures on February 1, 2023, may be prepaid at any time subject to a 2% premium in the first year after issuance and a 1% premium in the second year after issuance. Approximately \$95.0

million of the proceeds of the Term Loan were used to pay off and terminate the Company's existing secured mortgage indebtedness under the Fifth Amended and Restated Loan Agreement, dated May 30, 2014 (the "GECC Loan"), with General Electric Capital Corporation, as agent and lender, and the other lenders party thereto (the "Refinancing"). The Company expects to use borrowings under the Credit Facility for working capital purposes, to fund acquisitions and for general corporate purposes.

As of September 30, 2016, there was \$103.0 million outstanding under the Credit Facility.

Table of Contents

CARETRUST REIT, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS —

(Unaudited)

The interest rates applicable to loans under the Credit Facility are, at the Company's option, equal to either a base rate plus a margin ranging from 0.75% to 1.40% per annum or applicable LIBOR plus a margin ranging from 1.75% to 2.40% per annum based on the debt to asset value ratio of the Company and its subsidiaries (subject to decrease at the Company's election if the Company obtains certain specified investment grade ratings on its senior long term unsecured debt). In addition, the Company pays a commitment fee on the unused portion of the commitments under the Credit Facility of 0.15% or 0.25% per annum, based upon usage of the Credit Facility (unless the Company obtains certain specified investment grade ratings on its senior long term unsecured debt and elects to decrease the applicable margin as described above, in which case the Company will pay a facility fee on the revolving commitments ranging from 0.125% to 0.30% per annum based upon the credit ratings of its senior long term unsecured debt).

Pursuant to the Amendment, the interest rates applicable to the Term Loan are, at the Company's option, equal to either a base rate plus a margin ranging from 0.95% to 1.60% per annum or applicable LIBOR plus a margin ranging from 1.95% to 2.60% per annum based on the debt to asset value ratio of the Company and its subsidiaries (subject to decrease at the Company's election if the Company obtains certain specified investment grade ratings on its senior long term unsecured debt).

The Credit Facility and Term Loan are guaranteed, jointly and severally, by the Company and its wholly-owned subsidiaries that are party to the Credit Agreement (other than the Operating Partnership). The Credit Agreement contains customary covenants that, among other things, restrict, subject to certain exceptions, the ability of the Company and its subsidiaries to grant liens on their assets, incur indebtedness, sell assets, make investments, engage in acquisitions, mergers or consolidations, amend certain material agreements and pay certain dividends and other restricted payments. The Credit Agreement requires the Company to comply with financial maintenance covenants to be tested quarterly, consisting of a maximum debt to asset value ratio, a minimum fixed charge coverage ratio, a minimum tangible net worth, a maximum cash distributions to operating income ratio, a maximum secured debt to asset value ratio and a maximum secured recourse debt to asset value ratio. The Credit Agreement also contains certain customary events of default, including that the Company is required to operate in conformity with the requirements for qualification and taxation as a REIT.

As of September 30, 2016, the Company was in compliance with all applicable financial covenants under the Credit Agreement.

**GECC Loan**

Ten of the Company's properties were subject to secured mortgage indebtedness which it assumed in connection with the Spin-Off. On February 1, 2016, the GECC Loan was paid off in conjunction with the Refinancing.

**Interest Expense**

During the three months ended September 30, 2016, the Company incurred \$5.7 million of interest expense. Included in interest expense was \$0.6 million of amortization of deferred financing costs. During the three months ended September 30, 2015, the Company incurred \$7.2 million of interest expense. Included in interest expense was \$0.5 million of amortization of deferred financing costs and a \$1.2 million write-off of deferred financing costs associated with the payoff of the senior secured revolving credit facility. During the nine months ended September 30, 2016, the Company incurred \$17.4 million of interest expense. Included in interest expense was \$1.7 million of amortization of deferred financing costs and a \$0.3 million write-off of deferred financing costs associated with the Refinancing. During the nine months ended September 30, 2015, the Company incurred \$19.1 million of interest expense. Included in interest expense was \$1.6 million of amortization of deferred financing costs and a \$1.2 million write-off of deferred financing costs associated with the payoff of the senior secured revolving credit facility. As of September 30, 2016 and December 31, 2015, the Company's interest payable was \$5.1 million and \$1.9 million, respectively.

**8. EQUITY**

Common Stock

Offering of Common Stock—On March 28, 2016, the Company completed an underwritten public offering of 9.78 million newly issued shares of its common stock pursuant to an effective registration statement. The Company received net proceeds of \$105.8 million from the offering, after giving effect to the issuance and sale of all 9.78 million shares of common stock (which included 1.28 million shares sold to the underwriters upon exercise of their option to purchase additional shares), at a price to the public of \$11.35 per share.



Table of Contents

CARETRUST REIT, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS —

(Unaudited)

**At-The-Market Offering**—During the second quarter of 2016, the Company entered into an equity distribution agreement to issue and sell, from time to time, up to \$125.0 million in aggregate offering price of shares of our common stock (the "ATM Program"). Sales of common stock may be made by means of ordinary brokers' transactions, which may include block trades, or transactions that are deemed to be "at the market" offerings. During the three and nine months ended September 30, 2016, the Company sold 183,012 shares of common stock under the ATM Program at an average price of \$15.61 per share for \$2.9 million in gross proceeds. In conjunction with the sale of common stock, we reclassified \$0.2 million of prepaid accumulated costs associated with the ATM Program to additional paid in capital. At September 30, 2016, the Company had \$122.2 million available under the ATM Program.

**Dividends on Common Stock**—During the first quarter of 2016, the Company's Board of Directors declared a quarterly cash dividend of \$0.17 per share of common stock, payable on April 15, 2016 to common stockholders of record as of March 31, 2016. During the second quarter of 2016, the Company's Board of Directors declared a quarterly cash dividend of \$0.17 per share of common stock, payable on July 15, 2016 to common stockholders of record as of June 30, 2016. During the third quarter of 2016, the Company's Board of Directors declared a quarterly cash dividend of \$0.17 per share of common stock, payable on October 14, 2016 to common stockholders of record as of September 30, 2016.

## 9. STOCK-BASED COMPENSATION

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

**Restricted Stock Awards** — In connection with the Spin-Off, employees of Ensign who had unvested shares of restricted stock were given one share of CareTrust unvested restricted stock totaling 207,580 shares at the Spin-Off. These restricted shares are subject to a time vesting provision only and the Company does not recognize any stock compensation expense associated with these awards. During the nine months ended September 30, 2016, 38,000 shares vested or were forfeited. As of September 30, 2016, there were 50,830 unvested restricted stock awards outstanding.

In May 2016, the Compensation Committee of the Company's Board of Directors granted 20,770 shares of restricted stock to members of the Board of Directors. Each share had a fair market value on the date of grant of \$13.13 per share, based on the market price of the Company's common stock on that date, and the shares vest over one year. During the three months ended September 30, 2016 and 2015, the Company recognized \$0.3 million and \$0.4 million of stock-based compensation expense, respectively. During the nine months ended September 30, 2016 and 2015, the Company recognized \$1.2 million and \$1.1 million of stock-based compensation expense, respectively. As of September 30, 2016, there was \$2.7 million of unamortized stock-based compensation expense related to unvested awards and the weighted-average remaining vesting period of such awards was 2.5 years.

## 10. EARNINGS PER COMMON SHARE

The following table presents the calculation of basic and diluted EPS for the Company's common stock for the three and nine months ended September 30, 2016 and 2015, and reconciles the weighted-average common shares outstanding used in the calculation of basic EPS to the weighted-average common shares outstanding used in the calculation of diluted EPS (amounts in thousands, except per share amounts):



Table of Contents

CARETRUST REIT, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS —

(Unaudited)

	For the Three Months Ended September 30, 2016		For the Nine Months Ended September 30, 2015	
Numerator:				
Net income	\$7,832	\$727	\$20,965	\$5,031
Less: Net income allocated to participating securities	(58 )	(80 )	(205 )	(209 )
Numerator for basic and diluted earnings available to common stockholders	\$7,774	\$647	\$20,760	\$4,822
Denominator:				
Weighted-average basic common shares outstanding	57,595	39,125	54,403	33,916
Weighted-average diluted common shares outstanding	57,595	39,125	54,403	33,916
Earnings per common share, basic	\$0.13	\$0.02	\$0.38	\$0.14
Earnings per common share, diluted	\$0.13	\$0.02	\$0.38	\$0.14

The Company's unvested restricted shares associated with its incentive award plan and unvested restricted shares issued to employees of Ensign at the Spin-Off have been excluded from the above calculation of earnings per diluted share for both the three and nine months ended September 30, 2016 and 2015, as their inclusion would have been anti-dilutive.

## 11. COMMITMENTS AND CONTINGENCIES

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

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

Participation in federal healthcare programs by Ensign is not affected by the Settlement Agreement or the CIA. In the event of an uncured material breach of the CIA, Ensign could be excluded from participation in federal healthcare programs and/or subject to prosecution. The Company is subject to certain continuing operational obligations as part of Ensign's compliance program pursuant to the CIA, but otherwise has no liability related to the DOJ investigation. **Legal Matters**—None of the Company or any of its subsidiaries is a party to, and none of their respective properties are the subject of, any material legal proceedings.

## 12. CONCENTRATION OF RISK

Major operator concentration – As of September 30, 2016, Ensign leased 94 skilled nursing, assisted living and independent living facilities which had a total of 10,121 licensed beds and are located in Arizona, California, Colorado, Idaho, Iowa, Nebraska, Nevada, Texas, Utah and Washington. The four states in which Ensign leases the highest concentration of properties are California, Texas, Utah and Arizona.

Additionally, on October 1, 2015, the Company acquired the Liberty Healthcare Portfolio, a 14 facility skilled nursing and assisted living portfolio in Ohio, for \$176.5 million inclusive of transaction costs. The Company has leased these 14 facilities to subsidiaries of Pristine Senior Living, LLC ("Pristine") pursuant to a triple-net master lease entered into effective as of October 1, 2015, which has an initial term of 15 years, two five-year renewal options and no purchase options.

Table of Contents

CARETRUST REIT, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS —

(Unaudited)

The annual revenues from the Pristine master lease are \$17.0 million and will be escalated annually by an amount equal to the product of (1) the lesser of the percentage change in the Consumer Price Index (but not less than zero) or 3.0%, and (2) the prior year's rent. The Pristine master lease is guaranteed by Pristine and two of its principals. Further, in April 2016, the Company acquired a 55-bed skilled nursing facility and a skilled nursing and assisted living campus with 90 skilled nursing beds and 69 assisted living beds, both located in Cincinnati, Ohio, for \$14.7 million inclusive of transaction costs. In connection with the acquisition, the Company amended its triple-net master lease with Pristine Senior Living and anticipates additional initial annual lease revenues of approximately \$1.4 million following this acquisition.

Ensign is subject to the registration and reporting requirements of the SEC and is required to file with the SEC annual reports containing audited financial information and quarterly reports containing unaudited financial information. Ensign's financial statements, as filed with the SEC, can be found at Ensign's website <http://www.ensigngroup.net>. Audited financial statements of Pristine are available in Amendment No. 1 to the Company's Annual Report on Form 10-K for the year ended December 31, 2015, as filed with the SEC on March 16, 2016.

### 13. SUMMARIZED CONDENSED CONSOLIDATING INFORMATION

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

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

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

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

Subsidiary Guarantors – Each of the Subsidiary Guarantors is a wholly owned subsidiary of the Parent Guarantor. Prior to the consummation of the Spin-Off, each of the Subsidiary Guarantors was a wholly owned subsidiary of Ensign. These subsidiary entities consist of the Subsidiary Guarantors (other than the general partner of the Operating Partnership which was formed on May 8, 2014 in anticipation of the Spin-Off and the related transactions) and the Non-Guarantor Subsidiaries.

Pursuant to Rule 3-10 of Regulation S-X, the following summarized consolidating information is provided for the Parent Guarantor, the Issuers, the Subsidiary Guarantors and the Non-Guarantor Subsidiaries with respect to the Notes. This summarized financial information has been prepared from the financial statements of the Company and the books and records maintained by the Company.



Table of Contents

CARETRUST REIT, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS —

(Unaudited)

## CONDENSED CONSOLIDATING BALANCE SHEETS

SEPTEMBER 30, 2016

(in thousands, except share and per share amounts)

	Parent Guarantor	Issuers	Combined Subsidiary Guarantors	Combined Non- Guarantor Subsidiaries	Elimination	Consolidated
Assets:						
Real estate investments, net	\$—	\$434,803	\$335,485	\$38,833	\$—	\$809,121
Other real estate investments	—	—	13,595	—	—	13,595
Cash and cash equivalents	—	11,878	—	—	—	11,878
Accounts receivable	—	2,801	2,609	256	—	5,666
Prepaid expenses and other assets	—	1,752	3	—	—	1,755
Deferred financing costs, net	—	3,074	—	—	—	3,074
Investment in subsidiaries	372,648	392,158	—	—	(764,806 )	—
Intercompany	—	—	88,351	—	(88,351 )	—
Total assets	\$372,648	\$846,466	\$440,043	\$39,089	\$(853,157 )	\$845,089
Liabilities and Equity:						
Senior unsecured notes payable, net	\$—	\$255,028	\$—	\$—	\$—	\$255,028
Senior unsecured term loan, net	—	99,398	—	—	—	99,398
Unsecured revolving credit facility	—	103,000	—	—	—	103,000
Accounts payable and accrued liabilities	—	11,615	3,144	256	—	15,015
Dividends payable	9,873	—	—	—	—	9,873
Intercompany	—	4,777	—	83,574	(88,351 )	—
Total liabilities	9,873	473,818	3,144	83,830	(88,351 )	482,314
Equity:						
Common stock, \$0.01 par value; 500,000,000 shares authorized, 57,741,888 shares issued and outstanding as of September 30, 2016	577	—	—	—	—	577
Additional paid-in capital	519,204	347,340	374,660	(52,899 )	(669,101 )	519,204
Cumulative distributions in excess of earnings	(157,006 )	25,308	62,239	8,158	(95,705 )	(157,006 )
Total equity	362,775	372,648	436,899	(44,741 )	(764,806 )	362,775
Total liabilities and equity	\$372,648	\$846,466	\$440,043	\$39,089	\$(853,157 )	\$845,089

Table of Contents

CARETRUST REIT, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS —

(Unaudited)

## CONDENSED CONSOLIDATING BALANCE SHEETS

DECEMBER 31, 2015

(in thousands, except share and per share amounts)

	Parent Guarantor	Issuers	Combined Subsidiary Guarantors	Combined Non- Guarantor Subsidiaries	Elimination	Consolidated
<b>Assets:</b>						
Real estate investments, net	\$—	\$256,209	\$348,454	\$40,951	\$—	\$645,614
Other real estate investments	—	—	8,477	—	—	8,477
Cash and cash equivalents	—	11,467	—	—	—	11,467
Accounts receivable	—	519	1,695	128	—	2,342
Prepaid expenses and other assets	—	2,079	4	—	—	2,083
Deferred financing costs, net	—	3,183	—	—	—	3,183
Investment in subsidiaries	269,992	365,368	—	—	(635,360 )	—
Intercompany	—	—	59,160	4,186	(63,346 )	—
Total assets	\$269,992	\$638,825	\$417,790	\$45,265	\$(698,706 )	\$673,166
<b>Liabilities and Equity:</b>						
Senior unsecured notes payable, net	\$—	\$254,229	\$—	\$—	\$—	\$254,229
Unsecured revolving credit facility	—	45,000	—	—	—	45,000
Mortgage notes payable, net	—	—	—	94,676	—	94,676
Accounts payable and accrued liabilities	—	6,258	2,433	578	—	9,269
Dividends payable	7,704	—	—	—	—	7,704
Intercompany	—	63,346	—	—	(63,346 )	—
Total liabilities	7,704	368,833	2,433	95,254	(63,346 )	410,878
<b>Equity:</b>						
Common stock, \$0.01 par value; 500,000,000 shares authorized, 47,664,742 shares issued and outstanding as of December 31, 2015	477	—	—	—	—	477
Additional paid-in capital	410,217	266,929	374,660	(52,899 )	(588,690 )	410,217
Cumulative distributions in excess of earnings	(148,406 )	3,063	40,697	2,910	(46,670 )	(148,406 )
Total equity	262,288	269,992	415,357	(49,989 )	(635,360 )	262,288
Total liabilities and equity	\$269,992	\$638,825	\$417,790	\$45,265	\$(698,706 )	\$673,166



Table of Contents

CARETRUST REIT, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS —

(Unaudited)

## CONDENSED CONSOLIDATING INCOME STATEMENTS

FOR THE THREE MONTHS ENDED SEPTEMBER 30, 2016

(in thousands)

	Parent Guarantor	Issuers	Combined Subsidiary Guarantors	Combined Non- Guarantor Subsidiaries	Elimination	Consolidated
Revenues:						
Rental income	\$ —	\$10,063	\$ 11,368	\$ 2,748	\$—	\$ 24,179
Tenant reimbursements	—	875	1,091	123	—	2,089
Independent living facilities	—	—	766	—	—	766
Interest and other income	—	—	72	—	—	72
Total revenues	—	10,938	13,297	2,871	—	27,106
Expenses:						
Depreciation and amortization	—	3,194	4,356	698	—	8,248
Interest expense	—	5,742	—	1	—	5,743
Property taxes	—	875	1,091	123	—	2,089
Independent living facilities	—	—	708	—	—	708
Acquisition costs	—	203	—	—	—	203
General and administrative	410	1,873	—	—	—	2,283
Total expenses	410	11,887	6,155	822	—	19,274
Income in Subsidiary	8,242	9,191	—	—	(17,433 )	—
Net income	\$ 7,832	\$8,242	\$ 7,142	\$ 2,049	\$(17,433 )	\$ 7,832

Table of Contents

CARETRUST REIT, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS —

(Unaudited)

## CONDENSED CONSOLIDATING INCOME STATEMENTS

FOR THE THREE MONTHS ENDED SEPTEMBER 30, 2015

(in thousands)

	Parent Guarantor	Issuers	Combined Subsidiary Guarantors	Combined Non- Guarantor Subsidiaries	Elimination	Consolidated
Revenues:						
Rental income	\$ —	\$1,778	\$ 11,275	\$ 2,725	\$ —	\$ 15,778
Tenant reimbursements	—	91	1,112	117	—	1,320
Independent living facilities	—	—	626	—	—	626
Interest and other income	—	19	242	—	—	261
Total revenues	—	1,888	13,255	2,842	—	17,985
Expenses:						
Depreciation and amortization	—	600	4,483	732	—	5,815
Interest expense	—	5,807	2	1,412	—	7,221
Property taxes	—	91	1,112	117	—	1,320
Independent living facilities	—	—	610	—	—	610
General and administrative	435	1,855	2	—	—	2,292
Total expenses	435	8,353	6,209	2,261	—	17,258
Income in Subsidiary	1,162	7,627	—	—	(8,789 )	—
Net income	\$ 727	\$1,162	\$ 7,046	\$ 581	\$ (8,789 )	\$ 727

Table of Contents

CARETRUST REIT, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS —

(Unaudited)

## CONDENSED CONSOLIDATING INCOME STATEMENTS

FOR THE NINE MONTHS ENDED SEPTEMBER 30, 2016

(in thousands)

	Parent Guarantor	Issuers	Combined Subsidiary Guarantors	Combined Non- Guarantor Subsidiaries	Elimination	Consolidated
Revenues:						
Rental income	\$ —	\$25,702	\$ 33,949	\$ 8,206	\$ —	\$ 67,857
Tenant reimbursements	—	2,138	3,290	387	—	5,815
Independent living facilities	—	—	2,177	—	—	2,177
Interest and other income	—	—	587	—	—	587
Total revenues	—	27,840	40,003	8,593	—	76,436
Expenses:						
Depreciation and amortization	—	8,118	13,197	2,118	—	23,433
Interest expense	—	16,548	—	822	—	17,370
Property taxes	—	2,138	3,290	387	—	5,815
Independent living facilities	—	—	1,926	—	—	1,926
Acquisition costs	—	203	—	—	—	203
General and administrative	1,281	5,377	49	17	—	6,724
Total expenses	1,281	32,384	18,462	3,344	—	55,471
Income in Subsidiary	22,246	26,790	—	—	(49,036 )	—
Net income	\$ 20,965	\$22,246	\$ 21,541	\$ 5,249	\$ (49,036 )	\$ 20,965

Table of Contents

CARETRUST REIT, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS —

(Unaudited)

## CONDENSED CONSOLIDATING INCOME STATEMENTS

FOR THE NINE MONTHS ENDED SEPTEMBER 30, 2015

(in thousands)

	Parent Guarantor	Issuers	Combined Subsidiary Guarantors	Combined Non- Guarantor Subsidiaries	Elimination	Consolidated
Revenues:						
Rental income	\$ —	\$3,869	\$ 33,825	\$ 8,175	\$—	\$ 45,869
Tenant reimbursements	—	220	3,297	349	—	3,866
Independent living facilities	—	—	1,868	—	—	1,868
Interest and other income	—	19	697	—	—	716
Total revenues	—	4,108	39,687	8,524	—	52,319
Expenses:						
Depreciation and amortization	—	1,308	13,546	2,239	—	17,093
Interest expense	—	14,872	18	4,221	—	19,111
Property taxes	—	220	3,297	349	—	3,866
Independent living facilities	—	—	1,778	—	—	1,778
General and administrative	744	4,572	97	27	—	5,440
Total expenses	744	20,972	18,736	6,836	—	47,288
Income in Subsidiary	5,775	22,639	—	—	(28,414 )	—
Net income	\$ 5,031	\$5,775	\$ 20,951	\$ 1,688	\$ (28,414 )	\$ 5,031

Table of Contents

CARETRUST REIT, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS —

(Unaudited)

## CONDENSED CONSOLIDATING STATEMENTS OF CASH FLOWS

FOR THE NINE MONTHS ENDED SEPTEMBER 30, 2016

(in thousands)

	Parent Guarantor	Issuers	Combined Subsidiary Guarantors	Combined Non-Guarantor Subsidiaries	Elimination	Consolidated
Cash flows from operating activities:						
Net cash (used in) provided by operating activities	\$ (73 )	\$ 8,332	\$ 33,993	\$ 7,261	\$ —	\$ 49,513
Cash flows from investing activities:						
Acquisitions of real estate	—	(185,284)	—	—	—	(185,284 )
Improvements to real estate	—	(56 )	(202 )	—	—	(258 )
Purchases of equipment, furniture and fixtures	—	(70 )	(69 )	—	—	(139 )
Preferred equity investments	—	—	(4,531 )	—	—	(4,531 )
Escrow deposit for acquisition of real estate	—	(1,000 )	—	—	—	(1,000 )
Distribution from subsidiary	27,396	—	—	—	(27,396)	—
Intercompany financing	(107,807)	(58,570 )	—	—	166,377	—
Net cash used in investing activities	(80,411)	(244,980)	(4,802 )	—	138,981	(191,212 )
Cash flows from financing activities:						
Proceeds from the issuance of common stock, net	108,395	—	—	—	—	108,395
Proceeds from the issuance of senior unsecured term loan	—	100,000	—	—	—	100,000
Borrowings under unsecured revolving credit facility	—	150,000	—	—	—	150,000
Payments on unsecured revolving credit facility	—	(92,000 )	—	—	—	(92,000 )
Payments on the mortgage notes payable	—	—	—	(95,022 )	—	(95,022 )
Payments of deferred financing costs	—	(1,352 )	—	—	—	(1,352 )
Net-settle adjustment on restricted stock	(515 )	—	—	—	—	(515 )
Dividends paid on common stock	(27,396)	—	—	—	—	(27,396 )
Distribution to Parent	—	(27,396 )	—	—	27,396	—
Intercompany financing	—	107,807	(29,191 )	87,761	(166,377)	—
Net cash provided by (used in) financing activities	80,484	237,059	(29,191 )	(7,261 )	(138,981)	142,110
Net increase in cash and cash equivalents	—	411	—	—	—	411
Cash and cash equivalents beginning of period	—	11,467	—	—	—	11,467
Cash and cash equivalents end of period	\$ —	\$ 11,878	\$ —	\$ —	\$ —	\$ 11,878

Table of Contents

CARETRUST REIT, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS —

(Unaudited)

## CONDENSED CONSOLIDATING STATEMENTS OF CASH FLOWS

FOR THE NINE MONTHS ENDED SEPTEMBER 30, 2015

(in thousands)

	Parent Guarantor	Issuers	Combined Subsidiary Guarantors	Combined Non-Guarantor Subsidiaries	Elimination	Consolidated
Cash flows from operating activities:						
Net cash (used in) provided by operating activities	\$ (239 )	\$ (7,997 )	\$ 33,181	\$ 4,090	\$ —	\$ 29,035
Cash flows from investing activities:						
Acquisition of real estate	—	(231,501)	—	—	—	(231,501 )
Improvements to real estate	—	(20 )	(123 )	—	—	(143 )
Purchases of equipment, furniture and fixtures	—	(186 )	(70 )	—	—	(256 )
Net proceeds from sale of vacant land	—	—	30	—	—	30
Distribution from subsidiary	14,086	—	—	—	(14,086 )	—
Intercompany financing	(163,082 )	34,599	—	—	128,483	—
Net cash used in investing activities	(148,996 )	(197,108 )	(163 )	—	114,397	(231,870 )
Cash flows from financing activities:						
Proceeds from the issuance of common stock, net	163,466	—	—	—	—	163,466
Borrowings under unsecured revolving credit facility	—	45,000	—	—	—	45,000
Borrowings under senior secured revolving credit facility	—	35,000	—	—	—	35,000
Repayments of borrowings under senior secured revolving credit facility	—	(35,000 )	—	—	—	(35,000 )
Payments on the mortgage notes payable	—	—	(558 )	(1,951 )	—	(2,509 )
Payments of deferred financing costs	—	(2,113 )	—	—	—	(2,113 )
Net-settle adjustment on restricted stock	(145 )	—	—	—	—	(145 )
Dividends paid on common stock	(14,086 )	—	—	—	—	(14,086 )
Distribution to Parent	—	(14,086 )	—	—	14,086	—
Intercompany financing	—	163,082	(32,460 )	(2,139 )	(128,483 )	—
Net cash provided by (used in) financing activities	149,235	191,883	(33,018 )	(4,090 )	(114,397 )	189,613
Net decrease in cash and cash equivalents	—	(13,222 )	—	—	—	(13,222 )
Cash and cash equivalents beginning of period	—	25,320	—	—	—	25,320
Cash and cash equivalents end of period	\$ —	\$ 12,098	\$ —	\$ —	\$ —	\$ 12,098

Table of Contents

CARETRUST REIT, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS —

(Unaudited)

14. SUBSEQUENT EVENTS

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

Table of Contents

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

Forward-Looking Statements

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

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

Although we believe that the assumptions underlying the forward-looking statements are reasonable, we can give no assurance that our expectations will be attained. Factors which could have a material adverse effect on our operations and future prospects or which could cause actual results to differ materially from our expectations include, but are not limited to: (i) the ability to achieve some or all of the benefits that we expect to achieve from the completed Spin-Off (as defined below); (ii) the ability and willingness of the Ensign Group, Inc. ("Ensign") to meet and/or perform its obligations under the contractual arrangements that it entered into with us in connection with the Spin-Off, including the Ensign Master Leases (as defined below), and any of its obligations to indemnify, defend and hold us harmless from and against various claims, litigation and liabilities; (iii) the ability of our tenants to comply with laws, rules and regulations in the operation of the properties we lease to them; (iv) the ability and willingness of our tenants, including Ensign, to renew their leases with us upon their expiration, and the ability to reposition our properties on the same or better terms in the event of nonrenewal or in the event we replace an existing tenant, and obligations, including indemnification obligations, we may incur in connection with the replacement of an existing tenant; (v) the availability of and the ability to identify suitable acquisition opportunities and the ability to acquire and lease the respective properties on favorable terms; (vi) the ability to generate sufficient cash flows to service our outstanding indebtedness; (vii) access to debt and equity capital markets; (viii) fluctuating interest rates; (ix) the ability to retain our key management personnel; (x) the ability to maintain our status as a real estate investment trust ("REIT"); (xi) changes in the U.S. tax law and other state, federal or local laws, whether or not specific to REITs; (xii) other risks inherent in the real estate business, including potential liability relating to environmental matters and illiquidity of real estate investments; and (xiii) any additional factors included in our Annual Report on Form 10-K for the year ended December 31, 2015, including in the section entitled "Risk Factors" in Item 1A of Part I of such report. Forward-looking statements speak only as of the date of this report. Except in the normal course of our public disclosure obligations, we expressly disclaim any obligation to release publicly any updates or revisions to any forward-looking statements to reflect any change in our expectations or any change in events, conditions or circumstances on which any statement is based.

Overview

CareTrust REIT, Inc. ("CareTrust", the "Company", "we", "our", or "us") was formed on October 29, 2013, as a wholly owned subsidiary of Ensign. On June 1, 2014, Ensign completed the separation of its healthcare business and its real estate business into two separate and independent publicly traded companies through the distribution of all of the outstanding shares of common stock to Ensign stockholders on a pro rata basis (the "Spin-Off"). The Spin-Off was effective from and after June 1, 2014, with shares of our common stock distributed to Ensign stockholders on June 2, 2014. CareTrust holds substantially all of the real property that was previously owned by Ensign. As of September 30, 2016, we owned and leased to independent operators, including Ensign, 149 skilled nursing ("SNFs"), assisted living ("ALFs") and independent living ("ILFs") facilities which had a total of 14,304 operational beds and units located in Arizona, California, Colorado, Florida, Georgia, Idaho, Indiana, Iowa, Maryland, Michigan, Minnesota, Nebraska, Nevada, North Carolina, Ohio, Texas, Utah, Virginia, Washington and Wisconsin. We also own and operate three independent living facilities which had a total of 264 units located in Texas and Utah. As of September 30, 2016, we



also had three other real estate investments, consisting of \$13.6 million of preferred equity investments. We are a separate and independent publicly traded, self-administered, self-managed REIT primarily engaged in the ownership, acquisition and leasing of healthcare-related properties. We generate revenues primarily by leasing healthcare-related properties to healthcare operators in triple-net lease arrangements, under which the tenant is solely responsible for the costs related to the property (including property taxes, insurance, and maintenance and repair costs). We conduct and manage our business as one operating segment for internal reporting and internal decision making purposes. We expect to grow our

## Table of Contents

portfolio by pursuing opportunities to acquire additional properties that will be leased to a diverse group of local, regional and national healthcare providers, which may include Ensign, as well as senior housing operators and related businesses. We also anticipate further diversifying our portfolio over time, including by acquiring properties in different geographic markets, and in different asset classes.

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

### Recent Transactions

#### Offering of Common Stock

On March 28, 2016, we completed an underwritten public offering of 9.78 million newly issued shares of our common stock pursuant to an effective registration statement. We received net proceeds of \$105.8 million from the offering, after giving effect to the issuance and sale of all 9.78 million shares of common stock (which included 1.28 million shares sold to the underwriters upon exercise of their option to purchase additional shares), at a price to the public of \$11.35 per share.

#### At-The-Market Offering of Common Stock

During 2016, we entered into an equity distribution agreement to issue and sell, from time to time, up to \$125.0 million in aggregate offering price of our common stock through an "at-the-market" equity offering program (the "ATM Program"). During the three and nine months ended September 30, 2016, the Company sold 183,012 shares of common stock at an average price of \$15.61 per share for \$2.9 million in gross proceeds. At September 30, 2016, we had \$122.2 million available under the ATM Program.

#### Unsecured Revolving Credit Facility and Term Loan

See "- Liquidity and Capital Resources" below for a description of the Company's unsecured credit facility, which the Company entered into in August 2015 and amended in February 2016. We used approximately \$95.0 million of proceeds from the \$100.0 million non-amortizing unsecured term loan funded in February 2016 to pay off and terminate our secured mortgage indebtedness with General Electric Capital Corporation (the "GECC Loan").

### Recent Acquisitions

From January 1, 2016 through November 1, 2016, we acquired 30 properties, comprising 14 ALFs, 15 SNFs and 1 skilled nursing facility campus, for approximately \$186.6 million inclusive of estimated capitalized transaction costs. During this period, we also completed two preferred equity investments totaling \$4.5 million. See Note 3, Real Estate Investments, Net, and Note 4, Other Real Estate Investments in the Notes to Condensed Consolidated Financial Statements for additional information.



Table of Contents

## Results of Operations

## Operating Results

Three Months Ended September 30, 2016 Compared to Three Months Ended September 30, 2015:

	Three Months Ended		Increase	Percentage	
	September 30,	September 30,	(Decrease)	Difference	
	2016	2015			
(dollars in thousands)					
Revenues:					
Rental income	\$24,179	\$15,778	\$ 8,401	53	%
Tenant reimbursements	2,089	1,320	769	58	%
Independent living facilities	766	626	140	22	%
Interest and other income	72	261	(189 )	(72 )	%
Expenses:					
Depreciation and amortization	8,248	5,815	2,433	42	%
Interest expense	5,743	7,221	(1,478 )	(20 )	%
Property taxes	2,089	1,320	769	58	%
Independent living facilities	708	610	98	16	%
Acquisition costs	203	—	203	*	
General and administrative	2,283	2,292	(9 )	—	%

\* Not meaningful

**Rental income.** Rental income was \$24.2 million for the three months ended September 30, 2016 compared to \$15.8 million for the three months ended September 30, 2015. The \$8.4 million or 53% increase in rental income is primarily due to new investments made after July 1, 2015.

**Independent living facilities.** Revenues from our three ILFs that we own and operate were \$766,000 for the three months ended September 30, 2016 compared to \$626,000 for the three months ended September 30, 2015. The \$140,000 or 22% increase was primarily due to increased occupancy at the facilities and a higher average rental rate per unit. Expenses were \$708,000 for the three months ended September 30, 2016 compared to \$610,000 for the three months ended September 30, 2015. The \$98,000 increase was primarily due to the increased occupancy.

**Interest and other income.** Interest and other income decreased \$189,000 for the three months ended September 30, 2016 to \$72,000 compared to \$261,000 for the three months ended September 30, 2015. The net decrease was due to the cessation of accruing interest on one preferred equity investment slightly offset by two new preferred equity investments that closed during the three months ended September 30, 2016.

**Depreciation and amortization.** Depreciation and amortization expense increased \$2.4 million or 42% for the three months ended September 30, 2016 to \$8.2 million compared to \$5.8 million for the three months ended September 30, 2015. The \$2.4 million increase in depreciation and amortization was due to new investments made after July 1, 2015.

**Interest expense.** Interest expense decreased \$1.5 million or 20% for the three months ended September 30, 2016 to \$5.7 million compared to \$7.2 million for the three months ended September 30, 2015. The decrease was due primarily to lower interest expense of \$1.4 million resulting from the pay off of the GECC loan with the unsecured term loan, a \$1.2 million write-off of deferred financing fees associated with the payoff and termination of our senior secured revolving credit facility and \$0.2 million related to the secured revolving credit facility, partially offset by an increase in interest expense of \$0.6 million from our unsecured term loan, \$0.5 million from greater borrowings under our unsecured credit facility, and \$0.2 million related to amortization of deferred financing fees.

**General and administrative expense.** General and administrative expense decreased \$9,000 for the three months ended September 30, 2016 to \$2.3 million compared to \$2.3 million for the three months ended September 30, 2015. The \$9,000 decrease is primarily related to lower cash and noncash wages offset by increased corporate type costs and state taxes.



Table of Contents

## Nine Months Ended September 30, 2016 Compared to Nine Months Ended September 30, 2015:

	Nine Months Ended		Increase	Percentage	
	September 30,	September 30,	(Decrease)	Difference	
	2016	2015			
(dollars in thousands)					
Revenues:					
Rental income	\$67,857	\$45,869	\$ 21,988	48	%
Tenant reimbursements	5,815	3,866	1,949	50	%
Independent living facilities	2,177	1,868	309	17	%
Interest and other income	587	716	(129 )	(18 )	%
Expenses:					
Depreciation and amortization	23,433	17,093	6,340	37	%
Interest expense	17,370	19,111	(1,741 )	(9 )	%
Property taxes	5,815	3,866	1,949	50	%
Independent living facilities	1,926	1,778	148	8	%
Acquisition costs	203	—	203	*	
General and administrative	6,724	5,440	1,284	24	%

\* Not meaningful

Rental income. Rental income was \$67.9 million for the nine months ended September 30, 2016 compared to \$45.9 million for the nine months ended September 30, 2015. The \$22.0 million or 48% increase in rental income is primarily due to new investments made after January 1, 2015.

Independent living facilities. Revenues from our three ILFs that we own and operate were \$2.2 million for the nine months ended September 30, 2016 compared to \$1.9 million for the nine months ended September 30, 2015. The \$0.3 million or 17% increase was primarily due to increased occupancy at the facilities and a higher average rental rate per unit. Expenses were \$1.9 million for the nine months ended September 30, 2016 compared to \$1.8 million for the nine months ended September 30, 2015. The increase was primarily due to the increased occupancy.

Interest and other income. Interest and other income decreased \$129,000 or 18% for the nine months ended September 30, 2016 to \$587,000 compared to \$716,000 for the nine months ended September 30, 2015. The net decrease was due to the cessation of accruing interest on one preferred equity investment in the three months ended September 30, 2016 slightly offset by two new preferred equity investments that closed during the three months ended September 30, 2016.

Depreciation and amortization. Depreciation and amortization expense increased \$6.3 million or 37% for the nine months ended September 30, 2016 to \$23.4 million compared to \$17.1 million for the nine months ended September 30, 2015. The \$6.3 million increase in depreciation and amortization was due to new investments made after January 1, 2015.

Interest expense. Interest expense decreased \$1.7 million or 9% for the nine months ended September 30, 2016 to \$17.4 million compared to \$19.1 million for the nine months ended September 30, 2015. The decrease was due primarily to lower interest expense of \$3.6 million resulting from the pay off of the GECC loan with the unsecured term loan, a \$1.2 million write-off of deferred financing fees associated with the payoff and termination of our senior secured revolving credit facility and \$0.7 million related to the secured revolving credit facility, partially offset by an increase in interest expense of \$1.7 million from our unsecured term loan, \$1.1 million from greater borrowings under our credit facility, \$0.8 million related to amortization of deferred financing fees and a \$0.3 million write-off of deferred financing fees associated with the payoff and termination of the GECC loan.

General and administrative expense. General and administrative expense increased \$1.3 million or 24% for the nine months ended September 30, 2016 to \$6.7 million compared to \$5.4 million for the nine months ended September 30, 2015. The \$1.3 million increase is primarily related to higher cash and noncash wages as well as increased staffing.

Liquidity and Capital Resources

32

---

Table of Contents

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

During the nine months ended September 30, 2016, we issued 9.78 million shares of our common stock for net proceeds, before expenses, of \$106.2 million and refinanced our Credit Agreement (as defined below), including entering into a new \$100.0 million term loan and using approximately \$95.0 million of the proceeds to pay off and terminate our then-existing secured mortgage indebtedness. As of September 30, 2016, there was \$103.0 million outstanding under the Credit Facility (as defined below). See Note 7, Debt, and Note 8, Equity, in the Notes to Condensed Consolidated Financial Statements for additional information. We believe that our available cash, expected operating cash flows and the availability under our Credit Facility will provide sufficient funds for our operations, anticipated scheduled debt service payments and dividend requirements for at least the next twelve months.

On May 13, 2016, we commenced the ATM Program. Pursuant to the ATM Program, sales of shares of our common stock, if any, will be made through the sales agents acting as agent and, subject to certain conditions, may be made through the sales agents acting as principal, and will be made by means of ordinary brokers' transactions on the NASDAQ Global Select Market or otherwise at market prices prevailing at the time of sale, at prices related to prevailing market prices or at negotiated prices. Prior to July 1, 2016, we had not sold any common stock under the ATM program. During the three months ended September 30, 2016, we sold 183,012 shares of our common stock at an average price of \$15.61 per share resulting in gross proceeds of \$2.9 million.

We intend to invest in additional healthcare properties as suitable opportunities arise and adequate sources of financing are available. We expect that future investments in properties, including any improvements or renovations of current or newly-acquired properties, will depend on and will be financed by, in whole or in part, our existing cash, borrowings available to us under the Credit Facility (as defined below), future borrowings or the proceeds from sales of shares of our common stock pursuant to our ATM Program or additional issuances of common stock or other securities. In addition, we may seek financing from U.S. government agencies, including through Fannie Mae and the U.S. Department of Housing and Urban Development, in appropriate circumstances in connection with acquisitions and refinancings of existing mortgage loans.

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

**Cash Flows**

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

	Nine Months Ended September 30, 2016    2015 (dollars in thousands)	
Net cash provided by operating activities	\$49,513	\$29,035
Net cash used in investing activities	(191,212)	(231,870)
Net cash provided by financing activities	142,110	189,613
Net increase (decrease) in cash and cash equivalents	411	(13,222 )
Cash and cash equivalents at beginning of period	11,467	25,320



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

Cash and cash equivalents at end of period \$11,878 \$12,098

Nine Months Ended September 30, 2016 Compared to Nine Months Ended September 30, 2015

Net cash provided by operating activities for the nine months ended September 30, 2016 was \$49.5 million compared to \$29.0 million for the nine months ended September 30, 2015, an increase of \$20.5 million. The increase was

33

---

## Table of Contents

primarily due to an increase in net income of \$15.9 million and noncash income and expenses of \$5.6 million partially offset by a \$1.1 million change in operating assets and liabilities.

Net cash used in investing activities for the nine months ended September 30, 2016 was \$191.2 million compared to \$231.9 million for the nine months ended September 30, 2015, a decrease of \$40.7 million. The decrease was primarily the result of a \$46.2 million decrease in acquisitions partially offset by an increase of \$4.5 million of preferred equity investments and a \$1.0 million escrow deposit for an acquisition.

Net cash provided by financing activities for the nine months ended September 30, 2016 was \$142.1 million compared to \$189.6 million for the nine months ended September 30, 2015, a decrease of \$47.5 million. This decrease was due to lower net proceeds of \$55.1 million from common stock offerings, an increase in dividends paid of \$13.3 million and net-settlements of restricted stock of \$0.4 million offset by lower net borrowings of \$20.5 million and deferred financing fees of \$0.8 million.

### Indebtedness

#### Senior Unsecured Notes

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

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

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

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

As of September 30, 2016, we were in compliance with all applicable financial covenants under the indenture.

#### Unsecured Credit Facility and Term Loan



Table of Contents

On August 5, 2015, the Company, CareTrust GP, LLC, the Operating Partnership, as the borrower, and certain of its wholly owned subsidiaries entered into a credit and guaranty agreement with KeyBank National Association, as administrative agent, an issuing bank and swingline lender, and the lenders party thereto (the "Credit Agreement"). The Credit Agreement initially provided for an unsecured asset-based revolving credit facility (the "Revolving Facility") with commitments in an aggregate principal amount of \$300.0 million from a syndicate of banks and other financial institutions, and an accordion feature that allows the Operating Partnership to increase the borrowing availability by up to an additional \$200.0 million. A portion of the proceeds of the Revolving Facility were used to pay off and terminate the Company's existing secured asset-based revolving credit facility under a credit agreement dated May 30, 2014, with SunTrust Bank, as administrative agent, and the lenders party thereto.

On February 1, 2016, the Company, CareTrust GP, LLC, the Operating Partnership, as the borrower, and certain of its wholly owned subsidiaries entered into the First Amendment (the "Amendment") to the Credit Agreement. Pursuant to the Amendment, (i) commitments in respect of the Credit Facility (as defined below) were increased by \$100.0 million to \$400.0 million total, (ii) a new \$100.0 million non-amortizing unsecured term loan (the "Term Loan" and, together with the Revolving Facility, the "Credit Facility") was funded and (iii) the uncommitted incremental facility was increased by \$50.0 million to \$250.0 million. Approximately \$95.0 million of the proceeds of the Term Loan were used to pay off and terminate the GECC Loan (the "GECC Refinancing"). See "General Electric Capital Corporation Loan" below.

As of September 30, 2016, there was \$103.0 million outstanding under the Credit Facility.

The Credit Agreement has a maturity date of August 5, 2019, and includes two six-month extension options. The Term Loan, which matures on February 1, 2023, may be prepaid at any time subject to a 2% premium in the first year after issuance and a 1% premium in the second year after issuance.

The Credit Agreement initially provided that, subject to customary conditions, including obtaining lender commitments and pro forma compliance with financial maintenance covenants under the Credit Agreement, the Operating Partnership may seek to increase the aggregate principal amount of the revolving commitments and/or establish one or more new tranches of incremental revolving or term loans under the Credit Facility in an aggregate amount not to exceed \$200.0 million. Pursuant to the Amendment, the uncommitted incremental facility was increased by \$50.0 million to \$250.0 million effective February 1, 2016. The Company does not currently have any commitments for such increased loans.

The interest rates applicable to loans under the Revolving Facility are, at the Company's option, equal to either a base rate plus a margin ranging from 0.75% to 1.40% per annum or applicable LIBOR plus a margin ranging from 1.75% to 2.40% per annum based on the debt to asset value ratio of the Company and its subsidiaries (subject to decrease at the Company's election if the Company obtains certain specified investment grade ratings on its senior long term unsecured debt). Pursuant to the Amendment, the interest rates applicable to the Term Loan are, at the Company's option, equal to a base rate plus a margin ranging from 0.95% to 1.60% per annum or applicable LIBOR plus a margin ranging from 1.95% to 2.60% per annum based on the debt to asset value ratio of the Company and its subsidiaries (subject to decrease at the Company's election if the Company obtains certain specified investment grade ratings on its senior long term unsecured debt).

In addition, the Company pays a commitment fee on the unused portion of the commitments under the Revolving Facility of 0.15% or 0.25% per annum, based upon usage of the Revolving Facility (unless the Company obtains certain specified investment grade ratings on its senior long term unsecured debt and elects to decrease the applicable margin as described above, in which case the Company will pay a facility fee on the revolving commitments ranging from 0.125% to 0.30% per annum based upon the credit ratings of its senior long term unsecured debt).

The Credit Facility is guaranteed, jointly and severally, by the Company and its wholly owned subsidiaries that are party to the Credit Agreement (other than the Operating Partnership). The Credit Agreement contains customary covenants that, among other things, restrict, subject to certain exceptions, the ability of the Company and its subsidiaries to grant liens on their assets, incur indebtedness, sell assets, make investments, engage in acquisitions, mergers or consolidations, amend certain material agreements and pay certain dividends and other restricted payments. The Credit Agreement requires the Company to comply with financial maintenance covenants to be tested quarterly, consisting of a maximum debt to asset value ratio, a minimum fixed charge coverage ratio, a minimum

tangible net worth, a maximum cash distributions to operating income ratio, a maximum secured debt to asset value ratio and a maximum secured recourse debt to asset value ratio. The Credit Agreement also contains certain customary events of default, including that the Company is required to operate in conformity with the requirements for qualification and taxation as a REIT.

As of September 30, 2016, the Company was in compliance with all applicable financial covenants under the Credit Agreement.

Table of Contents

## General Electric Capital Corporation Loan

Ten of our properties were subject to secured mortgage indebtedness under the GECC Loan, which we assumed in connection with the Spin-Off. As of February 1, 2016, in connection with the Amendment, the GECC Loan was paid off and terminated as part of the GECC Refinancing.

## Obligations and Commitments

The following table summarizes our contractual obligations and commitments as of September 30, 2016 (in thousands):

	Payments Due by Period				
	Total	Less than 1 Year	1 Year to Less than 3 Years	3 Years to Less than 5 Years	More than 5 years
Senior unsecured notes payable (1)	\$ 336,375	\$ 15,275	\$ 30,550	\$ 290,550	\$—
Senior unsecured term loan (2)	116,547	2,610	5,220	5,227	103,490
Unsecured revolving credit facility (3)	112,191	3,232	108,959	—	—
Operating lease	463	132	277	54	—
Total	\$ 565,576	\$ 21,249	\$ 145,006	\$ 295,831	\$ 103,490

(1) Amounts include interest payments of \$76.4 million.

(2) Amounts include interest payments of \$16.5 million.

The unsecured revolving credit facility includes payments related to the unused credit facility fee due on the (3) amount of unused borrowings and assumes principal outstanding and interest rates in effect as of September 30, 2016.

## Capital Expenditures

We anticipate incurring average annual capital expenditures of \$400 to \$500 per unit in connection with the operations of our three ILFs. Capital expenditures for each property leased under our triple-net leases are generally the responsibility of the tenant, except that, for the facilities leased to subsidiaries of Ensign under eight master leases ("Ensign Master Leases"), the tenant will have an option to require us to finance certain capital expenditures up to an aggregate of 20% of our initial investment in such property, subject to a corresponding rent increase at the time of funding. For our other triple-net master leases besides the Ensign Master Leases, the tenants also have the option to request capital expenditure funding that would also be subject to a corresponding rent increase at the time of funding.

## Critical Accounting Policies and Estimates

Our Condensed Consolidated Financial Statements included in Item 1 of this Quarterly Report on Form 10-Q have been prepared in accordance with U.S. generally accepted accounting principles ("GAAP") for interim financial information set forth in the Accounting Standards Codification, as published by the Financial Accounting Standards Board. GAAP requires us to make estimates and assumptions regarding future events that affect the reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting periods. We base these estimates on our experience and assumptions we believe to be reasonable under the circumstances. However, if our judgment or interpretation of the facts and circumstances relating to various transactions or other matters had been different, we may have applied a different accounting treatment, resulting in a different presentation of our financial statements. We periodically reevaluate our estimates and assumptions, and in the event they prove to be different from actual results, we make adjustments in subsequent periods to reflect more current estimates and assumptions about matters that are inherently uncertain. Please refer to our Annual Report on Form 10-K for the year ended December 31, 2015, filed with the Securities and Exchange Commission (the "SEC") on February 11, 2016, for further information regarding the critical accounting policies that affect our more significant estimates and judgments used in the preparation of our Condensed Consolidated Financial Statements included in Part I, Item 1 of this Quarterly Report on Form 10-Q. There have been no material changes in such critical accounting policies during the three months ended September 30, 2016.

Item 3. Quantitative and Qualitative Disclosures About Market Risk.

36

---

## Table of Contents

Our primary market risk exposure is interest rate risk with respect to our variable rate indebtedness.

Our Credit Agreement provides for revolving commitments in an aggregate principal amount of \$400.0 million from a syndicate of banks and other financial institutions. As of September 30, 2016, we had \$103.0 million of outstanding borrowings under the Credit Facility. The interest rates per annum applicable to loans under the Credit Facility are, at the Company's option, equal to either a base rate plus a margin ranging from 0.75% to 1.40% per annum or applicable LIBOR plus a margin ranging from 1.75% to 2.40% per annum, based on the debt to asset value ratio of the Operating Partnership and its subsidiaries (subject to decrease at the Company's election if the Company obtains certain specified investment grade ratings on its senior long term unsecured debt). Pursuant to the Amendment, the interest rates applicable to the Term Loan are, at the Company's option, equal to a base rate plus a margin ranging from 0.95% to 1.60% per annum or applicable LIBOR plus a margin ranging from 1.95% to 2.60% per annum based on the debt to asset value ratio of the Company and its subsidiaries (subject to decrease at the Company's election if the Company obtains certain specified investment grade ratings on its senior long term unsecured debt). As of September 30, 2016, we had a \$100.0 million Term Loan outstanding.

An increase in interest rates could make the financing of any acquisition by us more costly as well as increase the costs of our variable rate debt obligations. Rising interest rates could also limit our ability to refinance our debt when it matures or cause us to pay higher interest rates upon refinancing and increase interest expense on refinanced indebtedness. Assuming a 100 basis point increase in the interest rates related to our variable rate debt, and assuming no change in our outstanding debt balance as described above, interest expense would have increased \$1.5 million for the nine months ended September 30, 2016.

We may, in the future, manage, or hedge, interest rate risks related to our borrowings by means of interest rate swap agreements. However, the REIT provisions of the Code substantially limit our ability to hedge our assets and liabilities. See "Risk Factors — Risks Related to Our Status as a REIT — Complying with REIT requirements may limit our ability to hedge effectively and may cause us to incur tax liabilities," which is included in our Annual Report on Form 10-K for the year ended December 31, 2015. As of September 30, 2016, we had no swap agreements to hedge our interest rate risks. We also expect to manage our exposure to interest rate risk by maintaining a mix of fixed and variable rates for our indebtedness.

### Item 4. Controls and Procedures.

#### Disclosure Controls and Procedures

We maintain disclosure controls and procedures (as such term is defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934, as amended ("Exchange Act")) that are designed to ensure that information required to be disclosed in our reports under the Exchange Act is processed, recorded, summarized and reported within the time periods specified in the SEC's rules and regulations and that such information is accumulated and communicated to management, including our Chief Executive Officer and Chief Financial Officer, as appropriate, to allow for timely decisions regarding required disclosure. In designing and evaluating the disclosure controls and procedures, management recognizes that any controls and procedures, no matter how well designed and operated, can provide only reasonable assurance of achieving the desired control objectives, and management is required to apply its judgment in evaluating the cost-benefit relationship of possible controls and procedures.

As of September 30, 2016, we carried out an evaluation, under the supervision and with the participation of management, including our Chief Executive Officer and Chief Financial Officer, regarding the effectiveness of our disclosure controls and procedures. Based on the foregoing, our Chief Executive Officer and Chief Financial Officer concluded that our disclosure controls and procedures were effective, at the reasonable assurance level, as of September 30, 2016.

#### Changes in Internal Control over Financial Reporting

There has been no change in our internal control over financial reporting (as such term is defined in Rules 13a-15(f) and 15d-15(f) under the Exchange Act) that occurred during the quarter ended September 30, 2016, that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.



PART II—OTHER INFORMATION

Item 1. Legal Proceedings.

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

37

---

Table of Contents

Item 1A. Risk Factors.

We have disclosed under the heading “Risk Factors” in our Annual Report on Form 10-K for the year ended December 31, 2015 risk factors which materially affect our business, financial condition, or results of operations. There have been no material changes from the risk factors previously disclosed.

Item 6. Exhibits.

Exhibit Number	Description of the Document
2.1	Separation and Distribution Agreement, dated as of May 23, 2014, by and between The Ensign Group, Inc. and CareTrust REIT, Inc. (Exhibit 2.1 to the Company’s Current Report on Form 8-K, filed on June 5, 2014, is incorporated herein by reference).
3.1	Articles of Amendment and Restatement of CareTrust REIT, Inc. (Exhibit 3.1 to the Company’s Registration Statement on Form 10, filed on May 13, 2014, is incorporated herein by reference).
3.2	Amended and Restated Bylaws of CareTrust REIT, Inc. (Exhibit 3.2 to the Company’s Registration Statement on Form 10, filed on May 13, 2014, is incorporated herein by reference).
4.1	Indenture, dated as of May 30, 2014, among CTR Partnership, L.P. and CareTrust Capital Corp., as Issuers, the guarantors named therein, and Wells Fargo Bank, National Association, as Trustee (Exhibit 4.1 to the Company’s Current Report on Form 8-K, filed on June 5, 2014, is incorporated herein by reference).
4.2	Form of Note (included in Exhibit 4.1 above).
4.3	Specimen Stock Certificate of CareTrust REIT, Inc. (Exhibit 4.1 to CareTrust REIT, Inc.’s Registration Statement on Form 10, filed on April 15, 2014, is incorporated herein by reference).
*31.1	Certification of Chief Executive Officer, as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
*31.2	Certification of Chief Financial Officer, as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
**32	Certification of Chief Executive Officer and Chief Financial Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
*101.INS	XBRL Instance Document
*101.SCH	XBRL Taxonomy Extension Schema Document
*101.CAL	XBRL Taxonomy Extension Calculation Linkbase Document
*101.DEF	XBRL Taxonomy Extension Definition Linkbase Document
*101.LAB	XBRL Taxonomy Extension Label Linkbase Document

\*101.PRE XBRL Taxonomy Extension Presentation Linkbase Document

\* Filed  
herewith

\*\*  
Furnished  
herewith

38

---

Table of Contents

SIGNATURES

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

CareTrust REIT, Inc.

November 2, 2016 By: /s/ Gregory K. Stapley  
Gregory K. Stapley  
President and Chief Executive Officer  
(duly authorized officer)

November 2, 2016 By: /s/ William M. Wagner  
William M. Wagner  
Chief Financial Officer and Treasurer  
(principal financial officer and  
principal accounting officer)