Exhibit 1

KPMG

CC-PALO ALTO, INC. AND SUBSIDIARY

Consolidated Financial Statements and Supplemental Schedules

December 31, 2012 and 2011

(With Independent Auditors' Report Thereon)

CC-PALO ALTO, INC. AND SUBSIDIARY

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KPMG

KPMG LLP
Aon Center
Suite 5500
200 East Randolph Drive
Chicago, IL 60601-6436

Independent Auditors' Report

The Board of Directors
CC-Palo Alto, Inc. and Subsidiary:

Report on the Financial Statements

We have audited the accompanying consolidated financial statements of CC-Palo Alto, Inc. and subsidiary (the Company), which comprise the consolidated balance sheets as of December 31, 2012 and 2011, and the related consolidated statements of operations, changes in stockholders' deficit, and cash flows for the years then ended, and the related notes to the consolidated financial statements.

Management's Responsibility for the Financial Statements

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

Auditors' Responsibility

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

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

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

Opinion

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of CC-Palo Alto, Inc. and subsidiary as of December 31, 2012 and 2011, and the results of their operations and their cash flows for the years then ended, in conformity with U.S. generally accepted accounting principles.

KPMG

Other Matters

Supplementary information

Our audit was conducted for the purpose of forming an opinion on the consolidated financial statements as a whole. The supplementary information included in Form 5-1 through Form 5-5 is presented for purposes of additional analysis and for compliance with the requirements of the California Health and Safety Code Section 1792 and is not a required part of the consolidated financial statements. Such information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the consolidated financial statements. The information has been subjected to the auditing procedures applied in the audits of the consolidated financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the consolidated financial statements or to the consolidated financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the information is fairly stated in all material respects in relation to the consolidated financial statements as a whole.

KPMG LLP

April 18, 2013

CC-PALO ALTO, INC. AND SUBSIDIARY

Consolidated Balance Sheets

December 31, 2012 and 2011

Assets	2012	2011
Current assets:		
Cash and cash equivalents	$ 367,396	1,567,575
Current portion of assets limited as to use	1,222,740	976,400
Resident accounts receivable	782,987	969,972
Prepaids and other	574,331	686,038
Total current assets	2,947,454	4,199,985
Assets limited as to use, net of amounts required for current liabilities	20,137,009	17,309,773
Property and equipment:		
Land improvements	15,289,790	15,229,895
Building and improvements	202,891,102	202,791,904
Furniture, fixtures, and equipment	24,803,878	23,934,638
Construction in progress	324,444	24,960
	243,309,214	241,981,397
Less accumulated depreciation	73,201,868	66,247,129
Property and equipment, net	170,107,346	175,734,268
Costs of acquiring initial continuing care contracts	9,019,064	11,043,723
Deferred tax asset, net	6,469,678	5,616,399
Deposits	1,212,428	1,005,350
Total assets	$ 209,892,979	214,909,498
Liabilities and Stockholders' Deficit		
Current liabilities:		
Accounts payable	$ 662,731	705,565
Accrued expenses	14,797,903	13,913,485
Prepaid resident service revenue	475,239	444,033
Resident deposits	1,222,740	976,400
Current portion of repayable entrance fees	3,807,765	13,179,108
Due to affiliate	863,303	697,397
Total current liabilities	21,829,681	29,915,988
Repayable entrance fees	450,376,724	431,773,927
Deferred revenue from nonrepayable entrance fees	38,720,835	35,290,256
Other liabilities	216,765	212,269
Total liabilities	511,144,005	497,192,440
Stockholders' deficit:		
Common stock, no par value, no assigned value. Authorized, issued, and outstanding, 100 shares	—	—
Distributions in excess of paid-in capital	(193,571,493)	(180,335,966)
Accumulated deficit	(107,679,533)	(101,946,976)
Total stockholders' deficit	(301,251,026)	(282,282,942)
Total liabilities and stockholders' deficit	$ 209,892,979	214,909,498

See accompanying notes to consolidated financial statements.

CC-PALO ALTO, INC. AND SUBSIDIARY

Consolidated Statements of Operations

Years ended December 31, 2012 and 2011

	2012	2011
Revenue:		
Net resident service revenue	$ 38,802,493	36,751,265
Amortization of entrance fees	6,321,532	7,487,108
Investment return	381,950	343,309
Other income	56,243	131,348
Total revenue	45,562,218	44,713,030
Expenses:		
Food and beverage	3,519,884	3,369,821
Dining room	1,956,756	1,925,022
Housekeeping	1,541,136	1,493,885
Laundry	222,649	204,131
Resident services	3,076,610	2,901,886
Resident care	7,080,020	6,639,161
Repairs and maintenance	1,727,146	1,651,879
Utilities	1,814,988	1,778,220
Sales and marketing	661,833	554,689
Total operating expenses	21,601,022	20,518,694
Management fees	3,114,451	2,971,665
Property taxes	5,699,657	15,719,957
Ground lease base rent	1,605,000	1,605,000
Ground lease participating rent	5,354,797	4,234,320
Depreciation and amortization	8,979,398	10,739,874
Administration	4,247,799	3,680,438
Insurance	1,545,930	1,409,436
Total expenses	52,148,054	60,879,384
Loss before income tax benefit	(6,585,836)	(16,166,354)
Income tax benefit	2,296,793	6,464,038
Net loss	$ (4,289,043)	(9,702,316)

See accompanying notes to consolidated financial statements.

CC-PALO ALTO, INC. AND SUBSIDIARY

Consolidated Statements of Changes in Stockholders' Deficit

Years ended December 31, 2012 and 2011

	Common stock		Distributions in excess of paid-in capital	Accumulated deficit	Total
	Shares	Amount			
Balance at December 31, 2010	100	$ —	(173,763,076)	(85,115,049)	(258,878,125)
Distributions to Parent, net	—	—	(6,572,890)	—	(6,572,890)
Tax adjustment	—	—	—	(7,129,611)	(7,129,611)
Net loss	—	—	—	(9,702,316)	(9,702,316)
Balance at December 31, 2011	100	—	(180,335,966)	(101,946,976)	(282,282,942)
Distributions to Parent, net	—	—	(13,235,527)	—	(13,235,527)
Tax adjustment	—	—	—	(1,443,514)	(1,443,514)
Net loss	—	—	—	(4,289,043)	(4,289,043)
Balance at December 31, 2012	100	$ —	(193,571,493)	(107,679,533)	(301,251,026)

See accompanying notes to consolidated financial statements.

CC-PALO ALTO, INC. AND SUBSIDIARY

Consolidated Statements of Cash Flows

Years ended December 31, 2012 and 2011

	2012	2011
Cash flows from operating activities:		
Cash received from residents	$ 39,043,558	37,245,531
Proceeds received from nonrepayable entrance fees	10,334,870	6,333,160
Interest received	319,962	330,108
Cash paid to suppliers and employees	(27,876,058)	(26,483,857)
Cash paid for management fees	(3,114,451)	(2,971,665)
Cash paid for real estate taxes	(5,699,657)	(5,548,856)
Cash paid for participating rent	(5,354,797)	(4,234,320)
Net cash provided by operating activities	7,653,427	4,670,101
Cash flows from investing activities:		
Additions to property and equipment	(1,327,817)	(464,954)
Net change in resident deposits	246,340	631,540
Net change in assets limited as to use	(3,218,666)	(3,336,648)
Net cash used in investing activities	(4,300,143)	(3,170,062)
Cash flows from financing activities:		
Distributions to Parent, net	(13,235,527)	(6,572,890)
Proceeds from repayable entrance fees	40,546,130	25,332,640
Refunds paid	(31,864,066)	(21,557,586)
Net cash used in financing activities	(4,553,463)	(2,797,836)
Net decrease in cash and cash equivalents	(1,200,179)	(1,297,797)
Cash and cash equivalents at beginning of year	1,567,575	2,865,372
Cash and cash equivalents at end of year	$ 367,396	1,567,575
Reconciliation of net loss to net cash provided by operating activities:		
Net loss	$ (4,289,043)	(9,702,316)
Adjustments to reconcile net loss to net cash provided by operating activities:		
Proceeds from nonrepayable entrance fees	10,334,870	6,333,160
Depreciation and amortization	8,979,398	10,739,874
Amortization of entrance fees	(6,321,532)	(7,487,108)
Net realized and unrealized gains (losses) on assets limited as to use	145,090	(13,201)
Utilization of repayable entrance fees in lieu of monthly fees	(33,369)	(56,273)
Income tax adjustment	(1,443,514)	(7,129,611)
Changes in assets and liabilities:		
Accounts receivable	186,985	417,052
Prepaids and other	111,707	(71,515)
Deposits	(207,078)	—
Accounts payable	(42,834)	36,873
Accrued expenses	884,418	10,992,519
Prepaid resident service revenue	31,206	2,139
Due to affiliates	165,906	(34,551)
Deferred tax asset	(853,279)	665,573
Other liabilities	4,496	(22,514)
Net cash provided by operating activities	$ 7,653,427	4,670,101

See accompanying notes to consolidated financial statements.

CC-PALO ALTO, INC. AND SUBSIDIARY

Notes to Consolidated Financial Statements

December 31, 2012 and 2011

(1) Purpose and Organization

The accompanying consolidated financial statements include the accounts of CC-Palo Alto, Inc. (the Company) and its consolidated affiliate, Palo Alto Care Center, Inc. The Company and Palo Alto Care Center, Inc. are both subsidiaries of CC-Development Group, Inc. (Parent).

The Company, a Delaware corporation, was incorporated on June 23, 1999 for the purpose of developing, owning, and operating a 494-unit senior living community (the Community) in Palo Alto, California. The Community comprises 388 units of independent living and a 106-unit care center that includes units of assisted living, memory support, and skilled nursing. The independent living component of the community opened in 2005, followed by the assisted living, memory support, and skilled nursing units of the care center in 2006.

Palo Alto Care Center, Inc. was incorporated for the purpose of owning the care center and leasing it back to the Company. The Company applies Accounting Standards Codification (ASC) Subtopic 810-10, *Consolidation—Overall*, to its variable interest in Palo Alto Care Center, Inc., whereby the entity is consolidated with the Company due to the Company's controlling financial interest in Palo Alto Care Center, Inc.

All significant intercompany balances and transactions have been eliminated in consolidation.

(2) Summary of Significant Accounting Principles

(a) Use of Estimates

The preparation of consolidated financial statements in conformity with U.S. generally accepted accounting principles 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 consolidated financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

(b) Cash and Cash Equivalents

Cash and cash equivalents include investments in highly liquid instruments with original maturities of three months or less, excluding amounts limited as to use.

(c) Fair Value Measurements

The Company applies the provisions of Accounting Standards Update (ASU) 2010-06, *Improving Disclosure about Fair Value Measurements* (ASU 2010-06). ASU 2010-06 amends ASC Subtopic 820-10, *Fair Value Measurements—Overall*, to provide additional disclosure requirements for transfers into and out of Levels 1 and 2 and for activity in Level 3 and to clarify other existing disclosure requirements.

ASC Subtopic 820-10 defines fair value as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. ASC Subtopic 820-10 also establishes a framework for measuring fair value and expands disclosures about fair value measurements.

CC-PALO ALTO, INC. AND SUBSIDIARY

Notes to Consolidated Financial Statements

December 31, 2012 and 2011

ASC Subtopic 820-10 establishes a fair value hierarchy that prioritizes the inputs to valuation techniques used to measure fair value. The hierarchy gives the highest priority to unadjusted quoted prices in active markets for identical assets or liabilities (Level 1 measurements) and the lowest priority to measurements involving significant unobservable inputs (Level 3 measurements). The three levels of the fair value hierarchy are as follows:

> Level 1 inputs are quoted prices (unadjusted) in active markets for identical assets or liabilities that the Company has the ability to access at the measurement date.
>
> Level 2 inputs are observable inputs other than Level 1 prices such as quoted prices for similar assets or liabilities, quoted prices in markets that are not active, or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the assets or liabilities.
>
> Level 3 inputs are unobservable inputs for the asset or liability.

The level in the fair value hierarchy within which a fair value measurement in its entirety falls is based on the lowest level input that is significant to the fair value measurement in its entirety.

In estimating the fair value of its financial instruments, the Company determined the carrying amounts reported in the consolidated balance sheets for cash and cash equivalents and assets limited as to use approximate fair value because of the short maturities of these instruments and are considered Level 1 investments within the fair value hierarchy.

(d) Assets Limited as to Use

Assets limited as to use include restricted resident deposits, assets held in escrow under state statutes, assets held by the Company under Ground Lease Agreement (note 5), and assets set aside by the Company for the Community's operations and capital improvements, in accordance with the Company's policies. Restricted resident deposits represent good faith deposits received by the Company upon the commitment of prospective residents to enter into a residency agreement. Assets held in escrow under state statutes represent funds designated to establish certain entrance fee repayments, debt service, and operating reserves as required by the State of California. Assets held by the Company under Ground Lease Agreement represent funds designated to secure payments under the ground lease (note 5). Assets held for operations are for funding operating reserves over which the Company retains control and may use in accordance with the Company's policies. Assets limited as to use for capital improvements represent funds designated by the Company for acquisition of property and equipment, in accordance with the Company's policies.

(e) Property and Equipment

Property and equipment are stated at cost. Depreciation is calculated on the straight-line method over the estimated useful lives of the assets ranging from 4 to 40 years.

(f) Impairment of Long-Lived Assets

Long-lived assets, such as property and equipment, are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable.

(Continued)

CC-PALO ALTO, INC. AND SUBSIDIARY

Notes to Consolidated Financial Statements

December 31, 2012 and 2011

Recoverability of assets to be held and used is measured by a comparison of the carrying amount of an asset to estimated undiscounted future cash flows expected to be generated by the asset. If the carrying amount of an asset exceeds its estimated future cash flows, an impairment charge is recognized by the amount by which the carrying amount of the asset exceeds the fair value of the asset. Assets to be disposed of would be separately presented in the consolidated balance sheet and reported at the lower of the carrying amount or fair value less costs to sell, and are no longer depreciated. The Company does not believe that there are any factors or circumstances indicating impairment of its property and equipment as of December 31, 2012 and 2011.

(g) ***Costs of Acquiring Initial Continuing Care Contracts***

Costs of acquiring initial continuing care contracts (the Costs) consist principally of marketing and advertising costs incurred directly in relation to the initial acquisition of continuing care contracts. In accordance with ASC Subtopic 720-35, *Advertising Costs*, the Company capitalizes costs incurred in connection with direct response advertising whose primary purpose is to secure deposits from residents who are shown to have responded specifically to the advertising. Such advertising costs include newspaper, magazine, television, radio, brochures, and other costs. The Costs are amortized using the straight-line method over the expected stay at the community of the first resident group, beginning in the first period in which revenues associated with the costs are earned. Upon occupancy of the first resident group, additional costs are expensed as incurred. The Costs are shown net of accumulated amortization of $15,276,468 and $13,251,809 at December 31, 2012 and 2011, respectively.

(h) ***Obligation to Provide Future Services***

The Company annually calculates the present value of the estimated net cost of future services and the use of facilities to be provided to current residents and compares that amount with the balance of unearned revenue from entrance fees. If the present value of the net costs of future services and the use of facilities exceeds the unearned revenue from entrance fees, a liability is recorded (obligation to provide future services and the use of facilities) with the corresponding charge to income. The obligation is discounted at 5.5%, based on the expected long-term rate of return. The present value of the net cost of future services and the use of facilities was less than the deferred revenue from entrance fees at December 31, 2012 and 2011, and accordingly, no obligation to provide future services has been recognized in the accompanying consolidated balance sheets.

(i) ***Repayable Entrance Fees***

Residents enter into a residency agreement with the Company that requires the payment of a onetime entrance fee. Upon termination of the residency agreement, residents are entitled to a repayment of the portion of the entrance fee that has not been earned by the Company, payable upon the sooner of reoccupancy of the unit or 10 years after the unit is made available. The Company earns 2% of the fee per month up to 20% and 10% dependent on the contract provisions of the residency agreement. The Company amortizes the nonrepayable portion of the entrance fee over the estimated life of the residents. The Company has recorded the repayable portion of the entrance fees separately from the nonrepayable portion within the accompanying consolidated balance sheets. If all contracts terminated on December 31, 2012, the repayable portion of the entrance fees due to all residents would be approximately $453,179,000.

CC-PALO ALTO, INC. AND SUBSIDIARY

Notes to Consolidated Financial Statements

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(j) ***Net Resident Service Revenue***

Resident revenue related to independent living units, assisted living units, memory support units, and non-Medicare skilled care units is recognized on a fee-for-service basis in the month in which occupancy and services are provided. Net resident service revenue related to Medicare skilled care units is reported at the estimated net realizable amounts from residents and third-party payors.

(k) ***Ground Lease Participating Rent***

Pursuant to its Ground Lease Agreement with The Board of Trustees of the Leland Stanford Junior University (note 5), beginning with initial occupancy of the Community, the Company pays a percentage of all gross receipts to Stanford University, as defined in the Ground Lease Agreement. Gross receipts include net resident service revenue, other income, and proceeds from entrance fees net of certain refunds. The payments are recognized as expense in their entirety in the period in which the related net resident service revenue and other income are recognized, and in the period in which the proceeds from entrance fees are received.

(l) ***Income Taxes***

The Company is included in the consolidated income tax return of its Parent. The Company uses the separate return method of determining its provision for income taxes. The consolidated financial statements reflect the provision for income taxes as if the Company were a separate taxpayer and a stand-alone enterprise. Accordingly, the consolidated financial statements may reflect tax attributes that may not exist in the Parent's consolidated income tax return. A valuation allowance on deferred tax assets is assessed using the sources of future taxable income available only to the Company.

Deferred income taxes are recognized for the tax consequences of "temporary differences" by applying enacted statutory tax rates applicable to future years to differences between the financial statement carrying amounts and the tax bases of existing assets and liabilities. The effect on deferred income taxes of a change in tax rates is recognized in income in the period that includes the enactment date.

The Company accounts for tax provisions in accordance with ASC Topic 740, *Income Taxes*. ASC Topic 740 clarifies the accounting for uncertainty in tax positions and also provides guidance on when the tax positions are recognized in an entity's financial statements and how the values of these positions are determined. The Company has recognized no liabilities as of December 31, 2012 and 2011 related to uncertain tax positions.

(m) ***Subsequent Events***

In connection with the preparation of the consolidated financial statements and in accordance with the recently issued ASC Topic 855, *Subsequent Events*, the Company evaluated subsequent events after the balance sheet date of December 31, 2012 through April 18, 2013, which was the date the consolidated financial statements were available to be issued.

(n) ***Reclassifications***

Certain prior year amounts have been reclassified to conform to current year presentation.

CC-PALO ALTO, INC. AND SUBSIDIARY

Notes to Consolidated Financial Statements

December 31, 2012 and 2011

(3) Concentration of Credit Risk

The Company grants credit to its self-pay residents as well as those that are insured under third-party payor agreements. The mix of receivables from patients and third-party payors as of December 31, 2012 and 2011 is as follows:

	2012	2011
Medicare	58%	41%
Self-pay and commercial insurance	42	59
	100%	100%

(4) Assets Limited as to Use

The Company reports investments in equity securities with readily determinable fair values and all investments in debt securities at fair value. Fair value is determined primarily on the basis of quoted market prices or observable market inputs. Money markets, certificates of deposit, and U.S. Treasury securities are considered cash equivalents and are considered Level 1 investments within the fair value hierarchy. Investment income or loss (including realized gains and losses on investments, changes in unrealized gains and losses on trading securities, interest, and dividends) is reported as investment return in the accompanying consolidated statements of operations. All assets limited as to use are considered by management to be trading securities.

A summary of the composition of the Company's investment portfolio at December 31, 2012 and 2011 is as follows:

	2012	2011
Cash	$ 2,843,842	985,458
Money markets and certificates of deposit	7,451,090	7,575,355
U.S. Treasury securities	11,064,817	9,725,360
	$ 21,359,749	18,286,173

CC-PALO ALTO, INC. AND SUBSIDIARY

Notes to Consolidated Financial Statements

December 31, 2012 and 2011

Investments are reported in the accompanying consolidated balance sheets as follows:

	2012	2011
Current portion of assets limited as to use: Resident deposits	$ 1,222,740	976,400
Assets limited as to use – by Company for capital improvements	11,092,920	9,897,796
Assets limited as to use – by Company for operations	2,158,603	1,411,977
Assets limited as to use – by State for entrance fee repayments	885,486	—
Assets limited as to use – by Company for ground lease	6,000,000	6,000,000
Assets limited as to use, net of amounts required for current liabilities	20,137,009	17,309,773
Total assets limited as to use	$ 21,359,749	18,286,173

The composition of investment return on the Company's investment portfolio for the years ended December 31, 2012 and 2011 is as follows:

	2012	2011
Interest and dividend income	$ 527,040	330,108
Net realized and change in unrealized gains and losses during the holding period	(145,090)	13,201
	$ 381,950	343,309

(5) Ground Lease

On August 1, 2000, the Company entered into a 75-year Ground Lease Agreement with The Board of Trustees of the Leland Stanford Junior University (Lessor). During the construction period, the lease called for monthly payments of $125,000 plus annual Consumer Price Index (CPI) increases. The lease payments began with the commencement of the construction of the Community in July 2003. After initial occupancy, the monthly payments reset to $125,000 and are adjusted every five years to reflect increases in CPI; the maximum CPI increase is 7% for a five-year period. The monthly payments for the years ended December 31, 2012 and 2011 totaled $1,605,000. The ground lease also requires participating rent of approximately 6% of all gross receipts, payable monthly beginning with the initial occupancy, as defined.

In February 2002, the Company paid a $1,000,000 deposit as required by the Ground Lease Agreement. The Ground Lease Agreement also requires that the Company maintain a letter of credit in the amount of $6,000,000 as security for the Company's performance of its obligations under the lease.

(6) Income Taxes

The operating results of the Company are included in the Parent's consolidated federal income tax return. The Company is party to a tax sharing agreement that provides that, among other things, the Company shall not be entitled to any reimbursement for utilization of its tax attributes in the consolidated federal

CC-PALO ALTO, INC. AND SUBSIDIARY

Notes to Consolidated Financial Statements

December 31, 2012 and 2011

income tax return of the Parent. The tax sharing agreement also provides that the Company shall not be entitled to any reimbursement for utilization of its tax attributes in the various combined state income tax returns of the Parent and its subsidiaries. The Company is required to pay the Parent for any tax liability that may arise from its operations, computed on a separate return basis. For the years ended December 31. 2012 and 2011, the Company sustained losses for federal and state income tax purposes. Accordingly, the current tax benefit attributable to the Company in the Parent's income tax return, as required pursuant to the provision of ASC Topic 740, has been eliminated through an adjustment to stockholders' deficit.

The income tax benefit for the years ended December 31, 2012 and 2011 comprises the following:

		2012	2011
Current:			
U.S. federal	$	(1,227,753)	(6,070,366)
State		(215,761)	(1,059,245)
Total current		(1,443,514)	(7,129,611)
Deferred:			
U.S. federal		(987,324)	571,714
State		134,045	93,859
Total deferred		(853,279)	665,573
Income tax benefit	$	(2,296,793)	(6,464,038)

The tax effects of temporary differences that give rise to significant portions of the deferred tax assets and deferred tax liabilities at December 31, 2012 and 2011 are presented below:

		2012	2011
Deferred tax assets:			
Deferred revenue from nonrefundable entrance fees	$	14,676,762	13,443,727
Other		616,079	1,122,984
Net operating loss carryforwards – state		296,135	296,135
Gross deferred tax assets		15,588,976	14,862,846
Less valuation allowance		(296,135)	—
Net deferred tax assets		15,292,841	14,862,846
Deferred tax liabilities:			
Depreciation		(5,148,255)	(4,746,571)
Costs of acquiring initial continuing care contracts		(3,674,908)	(4,499,876)
Gross deferred tax liabilities		(8,823,163)	(9,246,447)
Total deferred tax asset, net	$	6,469,678	5,616,399

(Continued)

CC-PALO ALTO, INC. AND SUBSIDIARY

Notes to Consolidated Financial Statements

December 31, 2012 and 2011

As of December 31, 2012, a valuation allowance of $296,135 is considered necessary as management believes that it is more likely than not that the results of future operations will not generate sufficient taxable income to realize the deferred tax asset as it relates to state net operating loss carryforwards. As of December 31, 2011, no valuation allowance was considered necessary.

Income tax benefit was $2,296,793 and $6,464,038 for the years ended December 31, 2012 and 2011, respectively, and differed from the amounts computed by applying the U.S. federal income tax rate of 35% to pretax income from continuing operations as a result of the following:

		2012	2011
Computed "expected" tax benefit	$	(2,305,043)	(5,658,224)
Change in income tax benefit resulting from:			
State and local income taxes, net of federal income tax expense		(302,335)	(547,214)
Change in valuation allowance		296,135	—
Other, net		14,450	(258,600)
	$	(2,296,793)	(6,464,038)

(7) Transactions with Related Parties

The Company entered into a management agreement dated August 1, 2000 between the Company and Classic Residence Management Limited Partnership (Classic), an affiliate of the Company, whereby Classic manages the operations of the Company. The agreement is for a term of 55 years and requires the Company to pay an annual management fee equal to 8% of annual resident service revenue excluding certain items as defined in the management agreement. The Company incurred management fee expense of $3,114,451 and $2,971,665 for the years ended December 31, 2012 and 2011, respectively.

Classic also contracts with third parties on behalf of the Company to provide property, health, and liability insurance, and various marketing and other services. Classic advances the funds to the third parties on behalf of the Company. Such advances amounted to $3,894,205 and $3,803,622 for the years ended December 31, 2012 and 2011, respectively. There is no interest associated with these advances as they are reimbursed on a current basis. Amounts due to Classic of $863,303 and $697,397 at December 31, 2012 and 2011, respectively, are reflected as due to affiliate in the accompanying consolidated balance sheets.

(8) Defined Contribution Plan

The employees of the Company participate in a savings plan (the Plan) administered by Classic. The Plan is qualified under Section 401(k) of the Internal Revenue Code for all full-time employees who are 21 years of age with six months of service. The Plan allows eligible employees to defer up to 25% of their income on a pretax basis through contributions to the Plan. In accordance with the provisions of the Plan, for every dollar up to 4% of a participant's salary, the Company matches each participant's contribution in an amount equal to 100% of the participant's deferral. For every dollar in excess of 4% of a participant's salary and limited to 6% of a participant's salary, the Company matches each participant's contribution in an amount equal to 50% of the participant's deferral. For the years ended December 31, 2012 and 2011, the

(Continued)

CC-PALO ALTO, INC. AND SUBSIDIARY

Notes to Consolidated Financial Statements

December 31, 2012 and 2011

Company recorded matching contribution expense of $239,818 and $216,795, respectively. Contributions are funded subsequent to year-end.

(9) Commitments and Contingencies

(a) State Regulatory Requirements

The Company is subject to regulatory requirements as set forth by the Department of Social Services in the State of California. Such requirements set forth the establishment of a restricted cash escrow account for resident deposits until execution of the residency agreement (note 2) and the submission of schedules detailing the availability of debt service and operating expense reserves.

(b) Federal Regulatory Compliance

The laws and regulations governing the Medicare programs are extremely complex and subject to interpretation, making compliance an ongoing challenge for long-term care organizations. Recently, the federal government has increased its enforcement activity, including audits and investigations related to billing practices, clinical documentation, and related matters. The Company maintains a compliance program designed to educate employees and to detect and correct possible violations.

(c) Internal Revenue Service Audit

The Company is currently undergoing audits by Internal Revenue Service for its tax years ended December 31, 2011, 2010, 2009, 2008, 2007, and 2006. Management anticipates the audits will be resolved without material adverse effect on the Company's consolidated financial position, results of operations, or cash flow.

CC-PALO ALTO, INC. AND SUBSIDIARY

Notes to Consolidated Financial Statements

December 31, 2012 and 2011

(d) Real Estate Tax Assessment

The Company is contesting the Company's real estate taxes for each year from November 2005 and forward. On April 1, 2011, the Santa Clara County Assessor issued a notice of intent to seek a further increase in the total assessed value of the Community for the period of time from November 2005 through June 2008. On April 18 – 20, 2011, a hearing was held by the County's Assessment Appeals Board covering the period from November 3, 2005 through June 30, 2008. On March 6, 2012, the Assessment Appeals Board rendered its decision increasing the base-year value of the real property to $480,000,000, an amount in excess of the valuation that was being sought by the County Assessor. The Company has challenged this decision through the filing of a complaint with the Superior Court of Santa Clara County. The Company has been billed in arrears based on the increased assessed value during the period under question. The incremental real estate taxes due through December 31, 2012 as a result of the decision by the Assessment Appeals Board approximate $12,041,000. This amount is included with accrued expenses in the accompanying consolidated balance sheets and a corresponding charge to property tax expense has been reflected in the accompanying 2011 consolidated statement of operations. The amounts are expected to be paid in five annual installments starting in 2013. The Company intends to vigorously pursue a reduction in the assessed value, however, it has not recognized any amounts as of December 31, 2012 related to a successful reduction.

CC-PALO ALTO, INC. AND SUBSIDIARY

Form 5-1

Long-Term Debt Incurred in a Prior Fiscal Year
(Including Balloon Debt)

Long-term debt obligation	(a) Date incurred		(b) Principal paid during fiscal year	(c) Interest paid during fiscal year	(d) Credit enhancement premiums paid in fiscal year	(e) Total paid (columns (b)+ (c) + (d))
1		$	—	—	—	—
2			—	—	—	—
3			—	—	—	—
4			—	—	—	—
5			—	—	—	—
6			—	—	—	—
7			—	—	—	—
8			—	—	—	—
		$	—	—	—	—
						(Transfer this amount to Form 5-3, line 1)

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

PROVIDER: CC-Palo Alto, Inc.

COMMUNITY: CC-Palo Alto, Inc.

See accompanying independent auditors' report.

CC-PALO ALTO, INC. AND SUBSIDIARY

Form 5-2

Long-Term Debt Incurred during Fiscal Year
(Including Balloon Debt)

Long-term debt obligation	(a) Date incurred		(b) Total interest paid during fiscal year	(c) Amount of most recent payment on the debt	(d) Number of payments over next 12 months	(e) Reserve requirement (columns (c)*(d))
1		$	—	—	—	—
2			—	—	—	—
3			—	—	—	—
4			—	—	—	—
5			—	—	—	—
6			—	—	—	—
7			—	—	—	—
8			—	—	—	—
		$	—	—	—	—
						(Transfer this amount to Form 5-3, line 2)

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

PROVIDER: CC-Palo Alto, Inc.

COMMUNITY: CC-Palo Alto, Inc.

See accompanying independent auditors' report.

CC-PALO ALTO, INC. AND SUBSIDIARY

Form 5-3

Calculation of Long-Term Debt Reserve Amount

Line		Total
1	Total from Form 5-1 bottom of Column (e)	$ —
2	Total from Form 5-2 bottom of Column (e)	—
3	Facility leasehold or rental payment paid by provider during fiscal year (including related payments such as lease insurance)	3,936,524
4	Total amount required for long-term debt reserve (A)	$ 3,936,524

(A) Amount comprises the following (see note 5 in the notes to the consolidated financial statements):

Ground lease base rent		$ 1,605,000
Resident service and other revenue	$ 38,858,736	
Participating rent percentage	6.0%	
2012 participating rent on resident service and other revenue (B)		2,331,524
Total		$ 3,936,524

(B) As described in note 5 to the consolidated financial statements, pursuant to its Ground Lease Agreement, the Provider pays the lessee approximately 6.0% of resident service revenue and approximately 6.3% of gross entrance fee proceeds collected. Based on discussions with the State of California Department of Social Services (DSS), and consistent with prior years, facility leasehold or rental payments reportable on Form 5-3 should only include base rent and participating rent attributable to resident service and other revenue.

PROVIDER: CC-Palo Alto, Inc.

COMMUNITY: CC-Palo Alto, Inc.

See accompanying independent auditors' report.

CC-PALO ALTO, INC. AND SUBSIDIARY

Form 5-4

Calculation of Net Operating Expenses

Line		Amounts	Total
1	Total operating expenses from financial statements		$ 52,148,054
2	Deductions:		
	(a) Interest paid on long-term debt (see instructions)	$ —	
	(b) Credit enhancement premiums paid for long-term debt (see instructions)	—	
	(c) Depreciation	6,954,739	
	(d) Amortization	2,024,659	
	(e) Revenues received during fiscal year for services to residents who did not have a continuing care contract	8,624,936	
	(f) Extraordinary expenses approved by the Department (A)	3,936,524	
3	Total deductions		21,540,858
4	Net operating expenses		30,607,196
5	Divide Line 4 by 365 and enter the result		83,855
6	**Multiply Line 5 by 75 and enter the result.** This is the provider's operating expense reserve amount		$ 6,289,125

(A)	Extraordinary expenses approved by the department consist of amounts classified as debt service as follows:	
	Ground lease base rent (see Form 5-3)	1,605,000
	Participating rent on resident service and other revenue (see Form 5-3)	2,331,524
		$ 3,936,524

PROVIDER: CC-Palo Alto, Inc.

COMMUNITY: CC-Palo Alto, Inc.

See accompanying independent auditors' report.

CC-PALO ALTO, INC. AND SUBSIDIARY

Form 5-5

Annual Reserve Certification

Provider Name: CC-Palo Alto, Inc.

Fiscal Year Ended: December 31, 2012

We have reviewed our debt service reserve and operating expense reserve requirements as of and for the fiscal year ended December 31, 2012 and are in compliance with those requirements.

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

		Amount
(1)	Debt service reserve amount	$ 3,936,524
(2)	Operating expense reserve amount	6,289,125
(3)	Total liquid reserve amount	$ 10,225,649

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

	Qualifying asset description		Amount (market value at end of quarter) Debt service reserve		Operating reserve
(4)	Cash and cash equivalents		$ —		367,396
(5)	Investment securities		3,936,524		10,200,485
(6)	Equity securities		—		—
(7)	Unused available lines of credit		—		—
(8)	Unused available letters of credit		—		—
(9)	Debt service reserve		—		—
(10)	Other (describe quality asset)		—		—
	Total amount of qualifying assets listed for liquid reserve	(11)	3,936,524	(12)	10,567,881
	Total amount required	(13)	3,936,524	(14)	6,289,125
	Surplus	(15)	$ —	(16)	4,278,756

Signature

Date

(Authorized representative)

(Title)

See accompanying independent auditors' report.

Exhibit 1

CC-PALO ALTO, INC. AND SUBSIDIARY

Consolidating Statement of Operations

Year ended December 31, 2012

	Ownership	Operations	CC-Palo Alto, Inc.	Palo Alto Care Center, Inc.	Total Consolidated
Revenue:					
Net resident service revenue	$ 55,004	38,747,489	38,802,493	—	38,802,493
Amortization of entrance fees	6,321,532	—	6,321,532	—	6,321,532
Interest income	238,482	143,468	381,950	—	381,950
Other income	8,000	48,243	56,243	—	56,243
Total revenue	6,623,018	38,939,200	45,562,218	—	45,562,218
Expenses:					
Food and beverage	—	3,519,884	3,519,884	—	3,519,884
Dining room	—	1,956,756	1,956,756	—	1,956,756
Housekeeping	—	1,541,136	1,541,136	—	1,541,136
Laundry	—	222,649	222,649	—	222,649
Resident services	—	3,076,610	3,076,610	—	3,076,610
Resident care	—	7,080,020	7,080,020	—	7,080,020
Repairs and maintenance	—	1,727,146	1,727,146	—	1,727,146
Utilities	—	1,814,988	1,814,988	—	1,814,988
Sales and marketing	—	661,833	661,833	—	661,833
Total operating expenses	—	21,601,022	21,601,022	—	21,601,022
Management fees	—	3,114,451	3,114,451	—	3,114,451
Property taxes	1,422,242	4,277,415	5,699,657	—	5,699,657
Ground lease base rent	—	1,605,000	1,605,000	—	1,605,000
Ground lease participating rent	5,354,797	—	5,354,797	—	5,354,797
Depreciation and amortization	8,888,495	90,903	8,979,398	—	8,979,398
Administration	277,288	3,970,511	4,247,799	—	4,247,799
Insurance	—	1,545,930	1,545,930	—	1,545,930
Total expenses	15,942,822	36,205,232	52,148,054	—	52,148,054
Income (loss) before income tax benefit	(9,319,804)	2,733,968	(6,585,836)	—	(6,585,836)
Income tax benefit	2,096,502	—	2,096,502	200,291	2,296,793
Net income (loss)	$ (7,223,302)	2,733,968	(4,489,334)	200,291	(4,289,043)

The above information is presented for purposes of additional analysis on the 2012 consolidated income statement of CC-Palo Alto, Inc. and subsidiary. The above statement is not a part of the 2012 audited financial statements and has not been subject to audit procedures specific to the divisions of the Company as presented, only to the Company as a whole.

CC-PALO ALTO, INC.

Statement of Operations - Reconciliation to Margin Neutral

Year ended December 31, 2012

		Operations	Surplus Adjustments	Total
Revenue:				
Net resident service revenue	$	38,747,489	—	38,747,489
Amortization of entrance fees		—	—	—
Interest income		143,468	—	143,468
Other income		48,243	—	48,243
Total revenue		38,939,200	—	38,939,200
Expenses:				
Food and beverage		3,519,884	—	3,519,884
Dining room		1,956,756	—	1,956,756
Housekeeping		1,541,136	—	1,541,136
Laundry		222,649	—	222,649
Resident services		3,076,610	—	3,076,610
Resident care		7,080,020	—	7,080,020
Repairs and maintenance		1,727,146	—	1,727,146
Utilities		1,814,988	—	1,814,988
Sales and marketing		661,833	—	661,833
Total operating expenses		21,601,022	—	21,601,022
Management fees		3,114,451	—	3,114,451
Property taxes		4,277,415	—	4,277,415
Ground lease base rent		1,605,000	—	1,605,000
Ground lease participating rent		—	—	—
Depreciation and amortization		—	—	—
Administration		3,970,511	—	3,970,511
Insurance		1,545,930	—	1,545,930
Total expenses		36,114,329	—	36,114,329
Income before CIRR contribution		2,824,871	—	2,824,871
Contribution to CIRR		(2,078,245)	—	(2,078,245)
Increase in COS	$	746,626	—	746,626

The above information is presented for purposes of additional analysis on the 2012 consolidated income statement of CC-Palo Alto, Inc. and subsidiary. The above statement is not a part of the 2012 audited financial statements and has not been subject to audit procedures specific to the divisions of the Company as presented, only to the Company as a whole.

CC-PALO ALTO, INC.

Balance Sheet - Reconciliation of Assets Limited as to Use for Operations

Year ended December 31, 2012

Noncurrent assets limited as to use for operations, December 31, 2011	$	1,411,977
Operating surplus generated during 2012		746,626
Noncurrent assets limited as to use, December 31, 2012	$	2,158,603

The above information is presented for purposes of additional analysis on page 12 of the 2012 notes to the consolidated financial statements of CC-Palo Alto, Inc. and subsidiary. The above statement is not a part of the 2012 audited financial statements and has not been subject to audit procedures specific to the divisions of the Company as presented, only to the Company as a whole.

Exhibit 2

A Place Like no Other

Senior Living with the Hyatt Touch®

CLASSIC RESIDENCE

BY

HYATT®

IN PALO ALTO

The gently rolling landscape delights the eye with a dozen shades of green. Through it, the San Francisquito Creek works its timeless way to the Bay. At Classic Residence by Hyatt in Palo Alto, you will share in the magnificence that has bloomed there for more than a century. It's part of Founder and Chairman Penny Pritzker's unique vision—to bring to senior living the same award-winning excellence and experience that Hyatt has provided for more than four decades. Our aim at this premier continuing care retirement community is to exceed your expectations. Here you'll have the freedom to enjoy an active, vibrant lifestyle with the peace of mind that, should your needs change, they'll be taken care of with the Hyatt Touch.® Nestled among meadows ornamented with ancient oaks, this eagerly anticipated community will complement the beautiful natural setting of Stanford University, and will be a place like no other.

neless elegance

Why is there an entrance fee? What does it cover?

To have the financial resources needed to operate as a CCRC, retirement communities in California typically need to charge an entrance fee and a monthly fee. The fees cover independent living; services such as dining, housekeeping, 24-hour concierge service, and maintenance of the grounds and homes; access to community amenities; and the benefits of the continuing care program.

Classic Residence—At Classic Residence by Hyatt in Palo Alto, residents will be able to move to our on-site assisted living or care center, should the need arise, and receive services with virtually no increase in their monthly fee. Except for additional meals and ancillary items that are not normally included in the daily rate, such as physicians' visits, medications, therapies, and ancillary supplies and services. The entrance fee that residents pay is at least 90 percent repayable to residents or their estate.

Why is there an entrance fee for a second person?

An additional entrance fee is charged for a second person to help cover the cost of services and continuing care benefits for that person.

Who monitors or regulates CCRCs and the fees collected by these communities? What guarantee do I have that my reservation deposit and my entrance fee are secure?

The financial operation and solvency of CCRCs in California are closely monitored by the DSS. State law requires that reservation deposits be placed in an escrow account at a financial institution approved by the Department. The funds remain in the escrow account until the community proves that it has met stringent State requirements. The California DSS continues to regulate the community after the release of the funds and requires the community to maintain certain cash reserves in amounts sufficient to meet State requirements. The CCRC must also file annual reports with the State that demonstrate continuing strong fiscal management and financial solvency.

What happens to the interest that my reservation deposit earns for the brief period of time it is in the escrow account?

You will receive the interest that accrues while your reservation deposit is held in the escrow account, in accordance with the effective rates for that account.

Are there any tax advantages to living in a CCRC?

Under current IRS guidelines, the portion of your entrance fee that is associated with the health care component of the CCRC is considered a pre-paid medical expense in the year in which the full entrance fee is paid, and potentially can be claimed as a medical deduction on your taxes.

In addition, annually, in January, the community will provide you with written documentation of the monthly fee allocation that is considered a pre-paid medical expense for the previous year, which potentially can be claimed as a medical tax deduction. We encourage you to consult your tax adviser for more information, since we are not in a position to provide tax advice.

Who determines if I need to move to assisted living or to a higher level of care?

At Classic Residence by Hyatt in Palo Alto, an interdisciplinary team, consisting of our Executive Director, Care Center Administrator, Medical Director and other health care professionals, will evaluate the needs of each resident. Decisions to transfer will be based on consultation with the Care Team as well as with the resident and his or her family and physician.

If a couple is living in the community and one spouse requires a higher level of care, does the couple have to move to the care center or can the independent spouse remain in his or her home? Will any additional charges apply?

One of the biggest benefits of CCRCs for couples is that a spouse who is independent can continue living in his or her home while the spouse who ongoing monthly fees until a new buyer is found and closes on the property. Should a resident of a CCRC vacate the home for reasons other than to move to the Care Center, ongoing monthly fees generally terminate upon move-out.

Most "ownership" communities are developed by companies whose primary focus is to sell all the residences and fill the community. These developers generally contract with managers to operate the community. Most CCRCs, however, are developed and operated by organizations that specialize in operating retirement communities, bringing depth of experience in delivering quality services and care while containing costs.

Also, at many "ownership" communities, residents who need care must make their own arrangements for such care. This may necessitate moving to another location—one that may not be as convenient for a spouse or friends to visit.

Life Care Communities—In California, life care communities cover the cost of hospital care and physicians' visits, which may already be covered by a resident's private health insurance and/or Medicare. This extension of coverage beyond the traditional continuum of care offering may result in higher entrance fees and monthly fees. In addition, life care entrance fees typically amortize down to a 0 percent refund, leaving nothing to the resident or their estate.

Classic Residence—At Classic Residence by Hyatt in Palo Alto, should residents require temporary assistance in their home, the on-site Wellness Center staff can provide such assistance on a fee-for-service basis, as allowed under DSS regulations. Residents who develop a need for more care will be able to transfer to assisted living or the care center, which are conveniently located on site. Rather than paying standard daily rates in assisted living or the care center, residents will continue to pay the applicable monthly fee for their independent living home, plus a fee for additional meals and ancillary items that are not normally included in the daily rate, such as physicians' visits, medications, therapies, and ancillary supplies and services. Upon resale of their home and termination of the residency agreement, up to 90 percent or more of the entrance fee is repaid to the resident or the resident's estate.

How does a CCRC differ from a rental retirement community? What are the advantages of a CCRC?

The biggest difference between rental and continuing care retirement communities is that rental communities typically do not offer a continuum of care that includes independent living, assisted living, memory support services and skilled nursing care.

At many rental communities, the cost of higher levels of care is the sole responsibility of the resident. In contrast, residents of a CCRC typically continue to pay the same monthly fee for independent living should they need assisted living, skilled nursing or memory support care.

Also, at many rental communities, residents who need a higher level of care are required to move out of the community because assisted living, skilled nursing or memory support care is not available. Residents must plan yet another move, which may be to a location that is not as convenient for a spouse or friends to visit.

Another key difference between CCRCs and rental communities is that rental communities are not subject to the same State of California oversight and regulations, which are designed to ensure that strong financial management is in place at CCRCs.

Unlike CCRCs, where residents may be younger because they are planning for the future, residents of rental communities often are older and more need-driven. This can lead to greater turnover, which can make rental communities feel more transient.

Classic Residence—At Classic Residence by Hyatt in Palo Alto, residents who develop a need for more care will be able to move to assisted living or the care center that is conveniently located on site. Rather than paying standard daily rates for assisted living, memory support or skilled nursing in the care center, residents will continue to pay the applicable monthly fee for their independent living home plus a fee for additional meals and ancillary items that are not normally included in the daily rate, such as physicians' visits, medications, therapies, and ancillary supplies and services.

Exhibit 3

STATE OF CALIFORNIA—HEALTH AND HUMAN SERVICES AGENCY
DEPARTMENT OF SOCIAL SERVICES
744 P Street • Sacramento, CA 95814 • www.cdss.ca.gov

CDSS
LIGHTBOURNE
DIRECTOR

EDMUND G. BROWN JR.
GOVERNOR

August 2, 2012

Ms. Stephanie Fields, Senior Vice President and General Counsel
Ms. Tara Cope, Senior Counsel
Mr. Gary Smith, Chief Financial Officer
Vi Living
71 S. Wacker Drive, Suite 900
Chicago, Illinois 60606

Dear Stephanie, Tara and Gary:

As we discussed during our telephone conversation on July 17, 2012, the Department of Social Services (Department) has concerns regarding CC-Palo Alto, Inc.'s (CC-PA) financial position as reported in both its Consolidated Financial Statements (audited) for the fiscal year ending (FYE) December 31, 2011, and the Actuarial Study for Vi Palo Alto as of the same date. Reduced to simplest terms, the GAAP financial statements show: (1) total liabilities that exceed total assets by $282 million; (2) net losses (after tax benefit offsets) of $9.7 million and $5.5 million for 2011 and 2010, respectively; (3) net negative cash flows of $1.29 million and $686,000 for 2011 and 2010, respectively; and (4) CC-PA's practice of making substantial upstream cash distributions to parent CC-Development Group, Inc. (CC-DG) for 2011 and 2010 that amounted to $6.57 million and $8.43 million, respectively.

At the same time, the Vi at Palo Alto actuarial study produced an actuarial balance sheet showing a deficit of $152.8 million (32% of assets) indicating that CC-PA "does not possess sufficient resources for current residents (including the actuarial present value of periodic fees expected to be paid in the future by present residents) to cover the actuarial present value of the expected costs of performing all remaining obligations to such residents under their contracts." As a result, the study concluded that the Vi at Palo Alto community "is not in Satisfactory Actuarial Balance" under the Actuarial Standards of Practice. Not coincidentally, CC-PA's cumulative distributions of cash to CC-DG (in excess of paid-in capital) of $180.3 million more than account for the $152.8 million deficit on CC-PA's actuarial balance sheet. A deficit that, in both the GAAP and ASOP financials, is primarily attributable to CC-PA's large liability for repayable entrance fees.

The issue arising from CC-PA's financial reports is not whether CC-PA has been successful financially or whether Vi at Palo Alto's business model is sound. CC-PA's success and business model are beyond question. Rather, the issue is whether CC-PA's distributions of cash to its *non-provider* parent have weakened CC-PA's financial position so that it is (or the Department may have reason to believe that it is) "insolvent, is in imminent danger of becoming insolvent, is in a financially unsound or unsafe condition, or that its condition is such that it may otherwise be unable to fully perform its obligations pursuant to continuing care contracts" within the meaning of Health & Safety Code (H&SC) sections 1792(d) [stating the bases for increasing and/or escrowing a provider's liquid reserves], 1793.13(a) [stating the bases for requiring a financial plan to resolve a provider's unsound financial condition], and 1793.50(a) [stating the bases for seeking a judicially appointed administrator]. Before it determines whether any of the preceding H&SC provisions apply, however, the Department is affording CC-PA 60 days to explain in writing why they do not. In short, CC-PA must establish that it is solvent, will remain solvent, is financially sound and safe, and is able to fully perform its continuing care contract obligations. To the extent that it is unable to show it meets each of these standards, CC-PA must submit a financial plan outlining how it intends to achieve and maintain those standards.

In the context of establishing its ability to fully perform its continuing care contract obligations, CC-PA must specifically explain its financial capacity to perform its entrance fee repayment obligations for existing and new residents. CC-PA's financial statements show declining cash and cash equivalents (to approximately $1.56 million as of December 31, 2011) and an increasing entrance fee repayment obligation (reported as $431.7 million in the 2011 GAAP financials). Moreover, CC-PA's repayment obligation applies to an increasing number Health Center residents. As those residents' units are likely to be resold before they leave the Health Center (and their contracts are terminated), the obligation to repay those entrance fees will not necessarily (and probably will not) coincide with any offsetting revenue from the resale of the payee residents' residential units. If the entrance fee from the resale of a Health Center resident's unit has already been collected and distributed to CC-DG when the Health Center resident's contract terminates, CC-PA's cash will not be sufficient to make the entrance fee repayment due.

The issue of adequate available cash will also arise whenever the contingent-on-resale condition on CC-PA's repayment obligation expires. If a residential unit remains unsold for 10 years, the entrance fee repayment obligation will again mature without any offsetting revenue from the resale of the resident payee's residential unit. Similarly, the contingent-on-resale condition is extinguished if a resident's contract is terminated due to a fire or other casualty (or condemnation or appropriation). CC-PA's capacity to make any repayment under those circumstances will depend on the adequacy and Ms.

availability of CC-PA's insurance or compensation. Accordingly, CC-PA's explanation must specify how it will perform its entrance fee repayment obligations under each of these scenarios.

The Department is charged by the continuing care statutes to take some action to protect current and/or prospective continuing care residents in the event a provider's financial condition falls below that necessary to fully perform its continuing care contract obligations. Although the continuing care statutes do not preclude distributions of surplus cash to a provider's principal (in fact, the statutes specifically contemplate such distributions), the statutes do require the provider entity to remain financially sound after making those distributions. Moreover, to the extent an upstream entity has exercised control over a subsidiary provider's finances or resources to the downstream provider's detriment (such control being manifest in the case of excessive distributions out of the provider's cash), the parent itself may be characterized by the Department as a co-provider. In short, there is a symmetry in the statutes that relates control over a continuing care provider's finances to responsibility for performing the financial obligations contained in the continuing care contracts that generated the provider's financial resources in the first place. Under the circumstances, CC-PA must show it is sufficiently sound financially to fully perform its continuing care obligations or CC-DG will be subject to characterization as a co-provider on the Vi at Palo Alto contracts.

I look forward to receiving your response and, in the meantime, will be pleased to answer any questions you may have.

Regards,

Robert W. Thompson
Attorney for the
Continuing Care Contracts Branch

Exhibit 4

Stephanie Fields
Senior Vice President
& General Counsel
71 South Wacker Drive, Ste. 900
Chicago, IL 60606
P: 312.803.8520
F: 312.896.5177
sfields@viliving.com

March 15, 2012

Ms. Mary Goerz
Chair, Resident Advisory Council
Vi at Palo Alto
620 Sand Hill Road #417E
Palo Alto, CA 94304

Re: Request for Establishment of a Reserve

Dear Ms. Goerz:

I write in response to your February 22, 2012, letter (received on February 28, 2012). Pursuant to the residency agreements for Vi at Palo, entrance fee repayments are due the earlier of (i) resale of the unit and (ii) 10 years.[1] The inclusion of a 10 year outside date for repayment of the repayable portion of an entrance fee does not create a "refundable contract" subject to the provisions of California Health and Safety Code Section 1792.6. CC- Palo Alto has not received an exemption from Section 1792.6; it simply does not apply in this context. Further, as noted in your letter the regulating agency, the Department of Social Services, agrees that Section 1792.6 is inapplicable.

As clearly stated in the residency agreement, CC-Palo Alto, Inc. is the provider and the sole entity responsible for the repayment of the repayable portion of the entrance fees. This is a contractual obligation of the Provider. Neither the Provider nor any Vi affiliated entity has ever defaulted on an entrance fee repayment obligation.

Entrance Fee repayments are made from proceeds of new sales or other funds which may be available to the Provider. Mr. Smith was correct in stating that there is no entrance fee repayment reserve. Even in this most difficult economic and housing market environment, resales at the community have been more than sufficient to support repayments. Further, if the community is damaged by a natural disaster such as, an earthquake, insurance proceeds would be available to support

[1] The only exceptions to this are if a resident terminates his or her agreement within the first 90 days or in the unlikely event that the Provider terminates the agreement for cause, as described in the agreement.

both the repair of the community and the associated business interruption if any. Finally, the reduction of entrance fee repayment obligations over time as contemplated by the Ground Lease will serve to reduce future obligations and will not necessarily impact price as you assert in your letter or the ability to make repayment obligations with proceeds from new sales or other funds which may be available.

We do understand that the Resident Council is concerned about this issue and we would like to continue this dialogue in greater detail during our next meeting with the resident representatives and the Resident Council (generally schedule to occur after the audit is finalized).

Very truly yours,

Stephanie Fields

SWF/rb

cc: Steve Brudnick, Executive Director, Vi at Palo Alto
Gary Smith, Director, CC-Palo Alto, Inc. William Sciortino, Director, CC-Palo Alto, Inc. Kevin Poorman, Director, CC-Development Group, Inc.