ASSISTED LIVING CONCEPTS INC
Form 10-K
March 14, 2013

UNITED STATES SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549
Form 10-K

(Mark One)

R Annual Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934
For the fiscal year ended December 31, 2012
Or
£ Transition Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934

Commission file number: 001-13498

Assisted Living Concepts, Inc.
(Exact name of registrant as specified in its charter)

Nevada	93-1148702
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

W140 N8981 Lilly Road, Menomonee Falls, Wisconsin 53051
(Address of Principal Executive Offices)
Telephone: (262) 257-8888
(Registrant's telephone number, including area code)
Securities registered pursuant to Section 12(b) of the Act:

Title of Each Class	Name of Each Exchange On Which Registered
Class A Common Stock, $0.01 par value per share	New York Stock Exchange

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

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes £ No R
Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act. Yes £ No R

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 R 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 during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes R Noo

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K (229.405 of this chapter) is not contained herein, and will not be contained, to the best of Registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-KR

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 definition 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 R Non-accelerated filer £ Smaller reporting company £
(Do not check if a 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 R

The aggregate market value of the voting and non-voting common equity held by non-affiliates of the registrant on June 30, 2012 (the last business day of the registrant's most recently completed second fiscal quarter) was approximately $129 million. For purposes of this computation shares of Class B Common Stock were assumed to have the same market value as Class A Common Stock. Common shares held as of June 30, 2012 by executive officers, directors and holders of more than 5% of the outstanding common shares have been excluded from this computation because such persons or institutions may be deemed to be affiliates. This determination of affiliate status is not a conclusive determination for any other purpose.

As of March 8, 2013, the registrant had 20,073,025 shares of its Class A Common Stock, $0.01 par value outstanding and 2,897,516 shares of its Class B Common Stock, $0.01 par value outstanding.

ASSISTED LIVING CONCEPTS, INC.

FORM 10-K
FOR THE YEAR ENDED DECEMBER 31, 2012
TABLE OF CONTENTS

Table of Contents

ASSISTED LIVING CONCEPTS, INC.
PART I

ITEM— BUSINESS
1

The Company

As of December 31, 2012, the 211 senior living residences of Assisted Living Concepts, Inc. ("ALC") and its subsidiaries are located in 20 states in the United States and total 9,348 units. ALC's residences typically range from 40 to 60 units and offer residents a supportive, home-like setting and assistance with the activities of daily living.

ALC became an independent, publicly traded company listed on the New York Stock Exchange on November 10, 2006 (the "Separation Date") when shares of ALC Class A and Class B Common Stock were distributed by Extendicare Inc. ("Extendicare"), to its stockholders ("the Separation").

References in this report to "Assisted Living Concepts," "ALC," "we," "our," and "us" refer to Assisted Living Concepts, Inc. and its consolidated subsidiaries, as constituted after the Separation, unless the context otherwise requires.

Effective March 16, 2009, ALC implemented a one-for-five reverse stock split of its Class A and Class B Common Stock and effective May 20, 2011, ALC implemented a two-for-one stock split of its Class A and Class B Common Stock. All share amounts, stock prices, and per share data in this report have been adjusted to reflect these stock splits.

History

ALC was formed as a Nevada corporation in 1994. ALC operated as an independent company until January 31, 2005 when it was acquired by Extendicare Health Services, Inc. ("EHSI") (the "ALC Purchase"), a wholly-owned subsidiary of Extendicare. Following the ALC Purchase, Extendicare consolidated its assisted living operations with ALC's until the Separation.

The following table summarizes the changes in the number of residences and units under operation by ALC since December 31, 2007:

	Residences	Units
December 31, 2007	208	8,535
Acquisition of eight leased residences	8	541
Expansion of four residences	—	78
December 31, 2008	216	9,154
Expansion of twelve residences	—	244
Combined two residences on one campus	(1)	—
December 31, 2009	215	9,398
Discontinued operations – formerly leased operations	(4)	(118)
Expansion of one residence	—	25
December 31, 2010	211	9,305
Expansion of one residence	—	20
December 31, 2011	211	9,325
Expansion of one residence	—	23
December 31, 2012	211	9,348

On June 19, 2006, ALC formed Pearson Insurance Company, LTD ("Pearson"), a wholly-owned, consolidated, Bermuda- based captive insurance company, to self-insure general and professional liability risks. On July 30, 2009, ALC formed Swan Home Health, LLC ("Swan Home Health"), a wholly-owned consolidated subsidiary, to provide health care services in certain of our residences. In addition, on October 14, 2010, ALC formed Swan Companion Care, LLC ("Swan Companion Care"), a wholly-owned consolidated subsidiary, to provide health care services in our independent residence located in Alabama.

Financial Presentation

The consolidated financial statements include all senior living residences operated by ALC in the respective periods, and include Pearson, Swan Home Health and Swan Companion Care since their formation.

Table of Contents

ALC operates in a single business segment with all revenues generated from those properties located within the United States.

Our Business

We operate senior living residences that provide seniors with a supportive, home-like setting with care and services, including 24-hour assistance with activities of daily living, medication management, life enrichment, health and wellness, and other services either directly from ALC employees or indirectly through wholly-owned health care service subsidiaries. See "Our Services" below. Our residences are in the middle of a broad spectrum of senior living options that ranges from apartments to skilled nursing facilities. In general, the type of senior living residence that is appropriate for a senior depends on his or her particular preferences and life circumstances, especially health and physical condition and the corresponding level of care that he or she requires. Seniors may move into one of our residences by choice or by necessity. As of December 31, 2012, we have 211 residences containing 9,348 units located in 20 states of which at December 31, 2012, 173 were owned and 38 were leased.

Our residences are purpose-built to meet the special needs of seniors and typically are located in targeted, middle-market suburban bedroom communities that were selected on the basis of a number of factors, including the size of our targeted demographic resident pool in the community. Our residences include features designed to appeal to seniors and their decision makers. The majority of our residences are 40 to 60 units, single story, square shaped buildings with an enclosed courtyard, a mix of studio and one-bedroom apartments, and wide hallways to accommodate our residents who use walkers and wheelchairs. The relatively small number of units in our residences and the design of our buildings enhance our ability to provide effective security and care, while also appealing to seniors who generally prefer easy access to their living quarters, pleasing aesthetics, and simplicity of design.

Our Services

Seniors in our residences are individuals who, for a variety of reasons, elect not to live alone, but do not need the 24-hour medical care provided in skilled nursing facilities. We design the services provided to these residents to respond to their individual needs and to improve their quality of life. This individualized assistance is available 24 hours a day and includes routine health-related services, which are made available and are provided according to the residents' individual needs and state regulatory requirements. Available services include:

§ general services, such as meals, activities, laundry and housekeeping;

§ support services, such as assistance with medication, monitoring health status, coordination of transportation, and coordination with physician offices;

§ personal care, such as dressing, grooming and bathing; and

§ a safe and secure environment with 24-hour access to assistance.

We also arrange access to additional services from third-party providers beyond basic housing and related services, including physical, occupational and respiratory therapy, home health, hospice, and pharmacy services.

Although a typical package of basic services provided to a resident includes meals, housekeeping, laundry and personal care, we accommodate the varying needs of our residents through the use of individual service plans and flexible staffing patterns. Our rate structure for services is based upon the acuity, or level, of services needed by each resident and individual service plans are based on periodic assessments of the residents' care needs. Supplemental and specialized health-related services for those residents requiring 24-hour supervision or more extensive assistance with activities of daily living, are provided by third-party providers who are reimbursed directly by the resident or a third-party payer (such as Medicare, Medicaid or long-term care insurance).

Because we own rather than lease a significant number of our properties, we have the ability to add additional units onto existing properties without complications such as renegotiating leases with landlords. Expansions are targeted where existing residences have demonstrated the ability to support increased capacity. We continually evaluate ways to expand our portfolio of properties. In 2012, we expanded one residence in Indiana, increasing it by 23 units. See Item 7, “Management’s Discussion and Analysis of Financial Condition and Results of Operations – Executive Overview,” in this Annual Report for a discussion of our business strategies.

Table of Contents

Servicemarks

We market and operate all of our residences under their own unique names. We do not consider servicemarks to be important to our business.

The Merger Agreement

On February 25, 2013, we entered into an Agreement and Plan of Merger (the “Merger Agreement”) with Aid Holdings, LLC, a Delaware limited liability company (“Aid Holdings”), and Aid Merger Sub, LLC, a Delaware limited liability company and a wholly owned subsidiary of Aid Holdings (“Aid Merger Sub”), providing for the merger of Aid Merger Sub with and into the Company (the “Merger”), with the Company surviving the Merger as a wholly-owned subsidiary of Aid Holdings. Aid Holdings and Aid Merger Sub are affiliates of TPG Capital, L.P. At the effective time of the Merger, each share of Class A Common Stock issued and outstanding immediately prior to the effective time of the Merger (other than shares owned by the Company, Aid Holdings or any direct or indirect subsidiary of either of them) will be converted automatically into the right to receive $12.00 in cash, without interest (the “Class A Per Share Merger Consideration”). Each share of Class B Common Stock issued and outstanding immediately prior to the effective time of the Merger (other than shares owned by the Company, Aid Holdings or any direct or indirect subsidiary of either of them or stockholders who have properly exercised and perfected dissenters’ rights under Nevada law) will be converted automatically into the right to receive $12.90 in cash, without interest (as required under the Company’s amended and restated articles of incorporation based on the Class A Per Share Merger Consideration).

Consummation of the Merger is subject to various conditions, including, without limitation: (i) the approval by the holders of a majority of the voting power of outstanding shares of Class A Common Stock and Class B Common Stock, voting as a single class (with each share of Class A Common Stock entitled to one vote and each share of Class B Common Stock entitled to ten votes), (ii) the approval by the holders of a majority of the voting power of outstanding shares of Class A Common Stock, excluding shares owned, directly or indirectly, by holders of Class B Common Stock, Aid Holdings, Aid Merger Sub or officers or directors of the Company, or any of their respective affiliates, voting as a single separate class (which condition, pursuant to the terms of the Merger Agreement, may not be waived), (iii) the absence of any law, injunction, judgment or ruling that prohibits, restrains or makes illegal the consummation of the Merger and (iv) the accuracy of the parties’ respective representations and warranties and the performance of the parties’ respective covenants (in each case, subject to certain materiality thresholds). In addition, the obligation of Aid Holdings and Aid Merger Sub to consummate the Merger is subject to (a) the absence, since the date of the Merger Agreement, of any change, effect, event, development, fact, occurrence or circumstance that, individually or in the aggregate, has had or would reasonably be expected to have a Material Adverse Effect (as defined in the Merger Agreement) and (b) the receipt by Aid Holdings of certain state licenses and permits to operate the Company’s facilities. The Merger is expected to close in the summer of 2013, but we cannot be certain when or if the conditions to the closing of the Merger will be satisfied or, to the extent permitted, waived.

Seasonality

While our business generally does not experience significant fluctuations from seasonality, winter months tend to result in more residents exiting our residences due to illnesses requiring hospitalization or skilled nursing facility services. Approximately 23%, 24%, and 23% of our residence operating expenses came from property related costs, including utilities, in 2012, 2011, and 2010, respectively. Because we operate in many “four season states”, utility costs associated with heating and cooling our residences tend to fluctuate by season. Generally, our first and third quarter utility costs tend to exceed our second and fourth quarter utility expenses by approximately 25% to 35%, respectively.

Working Capital

It is not unusual for us to operate with a negative working capital position because our revenues are collected more quickly, often in advance, than our obligations are required to be paid. This can result in a low level of current assets to the extent cash has been deployed in business development opportunities or used to repay longer term liabilities. Because our borrowings under the $125 million revolving credit facility with U.S. Bank National Association, as administrative agent and collateral agent ("U.S. Bank"), and certain other lenders (the "U.S. Bank Credit Facility") are due within the current year, the $108.0 million outstanding under the U.S. Bank Credit Facility was classified as a current liability in our consolidated financial statements.

Table of Contents

Customers

Payments from residents (or their responsible parties) who pay us directly ("private pay") comprised approximately 100%, 99% and 98% of our revenues in 2012, 2011 and 2010, respectively. Our business is not materially dependent upon any single customer. See Item 7, "Management's Discussion and Analysis of Financial Condition and Results of Operations" and "Medicaid Programs" below.

Government Regulation

State licensing agencies regulate certain of our operations and, where applicable, monitor our compliance with a variety of state and local laws governing licensure, changes of ownership, personal and nursing services, accommodations, construction, life safety, food service, and cosmetology. Generally, the state oversight and monitoring of senior living operators has been less burdensome than experienced in the skilled nursing industry. Areas most often regulated by these state agencies include:

§ qualifications of management and health care personnel;

§ minimum staffing levels;

§ dining services and overall sanitation;

§ personal care and nursing services;

§ assistance or administration of medication/pharmacy services;

§ residency agreements;

§ admission and retention criteria;

§ discharge and transfer requirements; and

§ resident rights.

Our residences may be subject to periodic unannounced surveys by state and other local government agencies to assess and assure compliance with the respective regulatory requirements. A survey can also occur following a state's receipt of a complaint regarding a residence. If one of our residences is cited for alleged deficiencies by the respective state or other agencies, we may be required to implement a plan of correction within a prescribed timeframe. Upon notification or receipt of a deficiency report, our regional and corporate teams assist the residence to develop, implement and submit an appropriate corrective action plan. Most state citations and deficiencies are resolved through the submission of a plan of correction that is reviewed and approved by the state agency. The survey team will conduct a re-visit to validate substantial compliance with the state rules and regulations.

In the third quarter of 2012, we agreed to a resolution with the State of Alabama in which we voluntarily surrendered the assisted living license for 50 units which are part of a campus consisting of 164 independent living and assisted living units in Alabama, and the State of Alabama withdrew its notice of revocation asserting past regulatory noncompliance. The apartments have reopened as independent living units. We have several other residences with various degrees of regulatory issues. The outcomes of these issues cannot be determined at this time.

Health Privacy Regulations and Health Insurance Portability and Accountability Act

Our residences are subject to state laws to protect the confidentiality of our residents' health information. We have implemented procedures to meet the requirements of the state laws and we train our residence personnel on those requirements.

We are not a covered entity in respect of the Health Insurance Portability and Accountability Act of 1996, or HIPAA. However, residences which electronically invoice state Medicaid programs are considered covered entities and are subject to HIPAA and its implementing regulations. As of December 31, 2012, we electronically invoice the Medicaid program for one residence in the State of New Jersey. We use state provided software to reduce the complexity and risk in compliance with the HIPAA regulations. HIPAA requires us to comply with standards for the exchange of health information at that residence and to protect the confidentiality and security of health data. The Department of Health and Human Services has issued four rules that mandate the standards with respect to certain healthcare transactions and health information under HIPAA. The four rules pertain to:

§ privacy standards to protect the privacy of certain individually identifiable health information;

Table of Contents

- § standards for electronic data transactions and code sets to allow entities to exchange medical, billing and other information and to process transactions in a more effective manner;
- § security of electronic health information privacy; and
- § use of a unique national provider identifier.

We believe we are in compliance with these rules as they currently affect our residence that electronically invoices state Medicaid programs. We monitor compliance with health privacy rules including the HIPAA standards. Should it be determined that we have not complied with the new standards, we could be subject to criminal penalties and civil sanctions.

Backlog

The nature of our business does not result in backlogs.

Competition

Although short-term data indicates limited new supply coming into the markets we serve, long-term, we expect to face increased competition from new market entrants as the demand for senior living grows. Providers of senior living residences compete for residents primarily on the basis of quality of care, price, reputation, physical appearance of the residences, services offered, family preferences, physician referrals, and location. Some of our competitors operate on a not-for-profit basis or as charitable organizations. In addition, we compete with home-based residential care, either provided by family members or other third parties. As the general economy declines and unemployment increases, families are less able to afford our residences or are more willing or available to care for family members at home.

We compete directly with companies that provide living services to seniors as well as other companies that provide similar long-term care alternatives. In most of the communities in which we operate, we face two or three competitors that offer senior living residences similar to ours in size, price and range of services offered. In addition, we face competition from other providers in the senior living industry including companies that provide adult day care in the home, congregate care residences where residents elect the services to be provided, continuing care retirement centers on campus-like settings, and nursing homes that provide long-term care services.

We prefer to own our residences and, therefore, compete with various real estate investors, such as joint ventures, real estate investment trusts (“REITs”) and real estate developers, for land and facility purchases. Generally, real estate investors purchase or construct senior living residences and enter into management agreements with operators. In July 2008, the Health Care REIT provision of the REIT Improvement Diversification and Empowerment Act was passed as part of the Housing Assistance Act of 2008 allowing REITs to realize more value from their existing properties. Real estate investment companies which may have substantially more resources and greater access to capital markets may compete with us for acquisitions in markets in which we operate or in which we look to operate.

The senior living industry, and specifically the independent living and assisted living segments, is large and fragmented. It is characterized by numerous local and regional operators, although there are several national operators similar in size or larger than us. The independent and senior living industry can be segregated into different market segments based upon the resources of the target population and the geographic area surrounding the operating residence. We compete with the national operators, as well as a combination of local and regional companies, several of which may have substantially more resources than us, directly or indirectly in the middle-market, suburban bedroom communities that we target.

7

Table of Contents

We believe that some markets, including some of the markets in which we operate, may have been overbuilt, in part because regulations and other barriers to entry into the assisted living industry are not substantial. In addition, because the number of people who can afford to pay our daily resident fee is limited, the supply of senior living residences may outpace demand in some markets. The impacts of such overbuilding include:

- § increased time to reach capacity at assisted living residences;
- § loss of existing residents to new residences;
- § pressure to lower or refrain from increasing rates;
- § competition for workers in tight labor markets; and
- § lower margins until excess units are absorbed.

In general, we believe that the markets in which we currently operate are capable of supporting only three or four senior living residences.

We believe that each local market is different, and our responses to the specific competitive environment in any market will vary. However, if a competitor were to attempt to enter one of the markets in which we operate, we may be required to reduce our rates, provide additional services, or expand our residence to meet perceived additional demand. We may not be able to compete effectively in markets that become overbuilt.

We believe our major competitive strengths are:

- § the size and breadth of our portfolio, and the depth of our experience in the senior living industry;
- § our ownership of 173 assisted living residences, or 82% of the total number of our residences, which increases our operating flexibility by allowing us to refurbish or expand residences to meet changing consumer demands without having to obtain landlord consent, and divest residences and exit markets at our discretion;