NATIONAL HEALTH INVESTORS INC
Form 10-K
February 18, 2016
UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

FORM 10-K
(Mark One)
[x] ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the fiscal year ended December 31, 2015

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

For the transition period from _____ to _____

Commission File Number 001-10822
National Health Investors, Inc.
(Exact name of registrant as specified in its charter)

Maryland	62-1470956
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)
222 Robert Rose Drive, Murfreesboro, Tennessee	37129
(Address of principal executive offices)	(Zip Code)
(615) 890-9100	
(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
Common stock, $.01 par value	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 [x] No [ ]

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 [x]

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 [x] No [ ]

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

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K (§292.405 of this chapter) is not contained herein, and will not be contained, to the best of the registrant's knowledge, in the definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K [ ]

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.

Large accelerated filer	[x]	Accelerated filer	[ ]
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 [x]

The aggregate market value of shares of common stock held by non-affiliates on June 30, 2015 (based on the closing price of these shares on the New York Stock Exchange) was approximately $2,238,337,000. There were 38,400,276 shares of the registrant’s common stock outstanding as of February 16, 2016.

DOCUMENTS INCORPORATED BY REFERENCE

Portions of the Registrant’s definitive proxy statement for its 2016 annual meeting of stockholders are incorporated by reference into Part III, Items 10, 11, 12, 13, and 14 of this Form 10-K.

Table of Contents

Table of Contents

PART I.

Forward Looking Statements

References throughout this document to NHI or the Company include National Health Investors, Inc., and its consolidated subsidiaries. In accordance with the Securities and Exchange Commission's "Plain English" guidelines, this Annual Report on Form 10-K has been written in the first person. In this document, the words "we", "our", "ours" and "us" refer only to National Health Investors, Inc. and its consolidated subsidiaries and not any other person. Unless the context indicates otherwise, references herein to "the Company" include all of our consolidated subsidiaries.

This Annual Report on Form 10-K and other materials we have filed or may file with the Securities and Exchange Commission, as well as information included in oral statements made, or to be made, by our senior management contain certain "forward-looking" statements as that term is defined by the Private Securities Litigation Reform Act of 1995. All statements regarding our expected future financial position, results of operations, cash flows, funds from operations, continued performance improvements, ability to service and refinance our debt obligations, ability to finance growth opportunities, and similar statements including, without limitation, those containing words such as "may", "will", "believes", "anticipates", "expects", "intends", "estimates", "plans", and other similar expressions are forward-l statements.

Forward-looking statements involve known and unknown risks and uncertainties that may cause our actual results in future periods to differ materially from those projected or contemplated in the forward-looking statements. Such risks and uncertainties include, among other things, the following risks described in more detail under the heading "Risk Factors" under Item 1A:

* We depend on the operating success of our tenants and borrowers for collection of our lease and interest income;

* We depend on the success of property development and construction activities, which may fail to achieve the operating results we expect;

* We are exposed to the risk that our tenants and borrowers may become subject to bankruptcy or insolvency proceedings;

* We are exposed to risks related to governmental regulations and payors, principally Medicare and Medicaid, and the effect that lower reimbursement rates would have on our tenants' and borrowers' business;

* We are exposed to the risk that the cash flows of our tenants and borrowers would be adversely affected by increased liability claims and liability insurance costs;

* We are exposed to risks related to environmental laws and the costs associated with liabilities related to hazardous substances;

* We are exposed to the risk that we may not be fully indemnified by our lessees and borrowers against future litigation;

* We depend on the success of our future acquisitions and investments;

* We depend on our ability to reinvest cash in real estate investments in a timely manner and on acceptable terms;

*

We may need to refinance existing debt or incur additional debt in the future, which may not be available on terms acceptable to us;

* We have covenants related to our indebtedness which impose certain operational limitations and a breach of those covenants could materially adversely affect our financial condition and results of operations;

* We are exposed to the risk that the illiquidity of real estate investments could impede our ability to respond to adverse changes in the performance of our properties;

* Certain tenants in our portfolio account for a significant percentage of the rent we expect to generate from our portfolio, and the failure of any of these tenants to meet their obligations to us could materially and adversely affect our business, financial condition and results of operations and our ability to make distributions to our stockholders.

* We are exposed to risks associated with our investments in unconsolidated entities, including our lack of sole decision-making authority and our reliance on the financial condition of other interests;

Table of Contents

* We are subject to additional risks related to healthcare operations associated with our investments in unconsolidated entities, which could have a material adverse effect on our results of operations.

* We depend on revenues derived mainly from fixed rate investments in real estate assets, while a portion of our debt capital used to finance those investments bear interest at variable rates. This circumstance creates interest rate risk to the Company;

* We are exposed to the risk that our assets may be subject to impairment charges;

* We depend on the ability to continue to qualify for taxation as a real estate investment trust;

* We have ownership limits in our charter with respect to our common stock and other classes of capital stock which may delay, defer or prevent a transaction or a change of control that might involve a premium price for our common stock or might otherwise be in the best interests of our stockholders;

* We are subject to certain provisions of Maryland law and our charter and bylaws that could hinder, delay or prevent a change in control transaction, even if the transaction involves a premium price for our common stock or our stockholders believe such transaction to be otherwise in their best interests.

See the notes to the annual audited consolidated financial statements, and “Business” and “Risk Factors” under Item 1 and Item 1A therein for a further discussion of these and of various governmental regulations and other operating factors relating to the healthcare industry and the risk factors inherent in them. You should carefully consider these risks before making any investment decisions in the Company. These risks and uncertainties are not the only ones we face. There may be additional risks that we do not presently know of or that we currently deem immaterial. If any of the risks actually occur, our business, financial condition, results of operations, or cash flows could be materially adversely affected. In that case, the trading price of our shares of stock could decline and you may lose part or all of your investment. Given these risks and uncertainties, we can give no assurance that these forward-looking statements will, in fact, occur and, therefore, caution investors not to place undue reliance on them.

ITEM 1. BUSINESS

General

National Health Investors, Inc., established in 1991 as a Maryland corporation, is a self-managed real estate investment trust ("REIT") specializing in sale-leaseback, joint-venture, mortgage and mezzanine financing of need-driven and discretionary senior housing and medical investments. Our portfolio consists of real estate investments in independent living facilities, assisted living facilities, entrance-fee communities, senior living campuses, skilled nursing facilities, specialty hospitals and medical office buildings. Other investments include mortgages and other notes, marketable securities, and a joint venture structured to comply with the provisions of the REIT Investment Diversification Empowerment Act of 2007 (“RIDEA”). Through a RIDEA joint venture, we invest in facility operations managed by independent third-parties. We fund our real estate investments primarily through: (1) operating cash flow, (2) debt offerings, including bank lines of credit and term debt, both unsecured and secured, and (3) the sale of equity securities.

At December 31, 2015, we had investments in real estate and mortgage and other notes receivable involving 189 facilities located in 31 states. These investments involve 116 senior housing properties, 68 skilled nursing facilities, 3 hospitals, 2 medical office buildings and other notes receivable. These investments (excluding pre-development costs of $168,000 and our corporate office of $920,000) consisted of properties with an original cost of $2,094,778,000, rented under triple-net leases to 26 lessees, and $135,031,000 aggregate carrying value of mortgage and other notes

receivable due from 14 borrowers.

Our investments in real estate and mortgage loans are secured by real estate located within the United States. We are managed as one reporting unit, rather than multiple reporting units, for internal reporting purposes and for internal decision making. Therefore, we have concluded that we operate as a single segment. Information about revenues from our tenants and borrowers, a measure of our income, and total assets can be found in Item 8 of this Form 10-K.

Classification of Properties in our Portfolio

Senior Housing

As of December 31, 2015, our portfolio included 113 senior housing properties (“SHO”) leased to operators and mortgage loans secured by 3 SHOs. SHOs within our portfolio are either need-driven or discretionary for end users and consist of assisted

Table of Contents

living facilities, independent living facilities, entrance-fee communities and senior living campuses which are more fully described below.

Need-Driven Senior Housing

Assisted Living Facilities. As of December 31, 2015, our portfolio included 69 assisted living facilities (“ALF”) leased to operators and mortgage loans secured by 2 ALFs. ALFs are free-standing facilities that provide basic room and board functions for elderly residents. As residents typically receive assistance with activities of daily living such as bathing, grooming, memory care services and administering medication, we consider these facilities to be need-driven senior housing. On-site staff personnel are available to assist in minor medical needs on an as-needed basis. Operators of ALFs are typically paid from private sources without assistance from government. ALFs may be licensed and regulated in some states, but do not require the issuance of a Certificate of Need (“CON”) as required for skilled nursing facilities.

Senior Living Campuses. As of December 31, 2015, our portfolio included 9 senior living campuses ("SLC") leased to operators. SLCs are either freestanding or multi-site campuses that include skilled nursing beds combined with an independent or assisted living facility that provides basic room and board functions for elderly residents. They may also provide assistance to residents with activities of daily living such as bathing, grooming and administering medication and as such are considered need-driven senior housing. On-site staff personnel are available to assist in minor medical needs on an as-needed basis. As the decision to transition to a senior living campus is typically more than a lifestyle choice and is usually driven by the need to receive some moderate level of care, we consider this facility type to be need-driven. Operators of SLCs are typically paid from private sources and from government programs such as Medicare and Medicaid for skilled nursing residents.

Discretionary Senior Housing

Entrance-Fee Communities. As of December 31, 2015, our portfolio included 7 entrance-fee communities ("EFC") leased to operators and a mortgage loan secured by 1 EFC. Entrance-fee communities, frequently referred to as continuing care retirement communities, or CCRCs, typically include a combination of detached homes, an independent living facility, an assisted living facility and a skilled nursing facility on one campus. These communities appeal to residents because there is no need to relocate when health and medical needs change. EFCs are classified as either Type A, B, or C depending upon the amount of healthcare benefits included in the entrance fee. “Type A” EFCs, or “Lifecare” communities, include substantially all future healthcare costs. Communities providing a modified healthcare contract offering access to skilled nursing care but only paying for a maximum number of days are referred to as “Type B.” Finally, "Type C" EFCs, the type in our portfolio, are fee-for-service communities which do not provide any healthcare benefits and correspondingly have the lowest entrance fees. However, monthly fees may be higher to reflect the current healthcare components delivered to each resident. EFC licensure is state-specific, but generally the skilled nursing beds included in our EFC portfolio are subject to state licensure and regulation. As the decision to transition to an EFC is typically made as a lifestyle choice and not as the result of a pressing medical concern, we consider the decision to transition to an EFC to be discretionary. Similarly, the predominant source of revenue for operators of EFCs is from private payor sources.

Independent Living Facilities. As of December 31, 2015, our portfolio included 28 independent living facilities (“ILF”) leased to operators. ILFs offer specially designed residential units for the active senior adults and provide various ancillary services for their residents including restaurants, activity rooms and social areas. Services provided by ILF operators are generally paid from private sources without assistance from government programs. ILFs may be licensed and regulated in some states, but do not require the issuance of a CON as required for skilled nursing facilities. As ILFs typically do not provide assistance with activities of daily living, we consider the decision to transition to an ILF facility to be discretionary.

Medical

As of December 31, 2015, our portfolio included 67 medical facilities leased to operators and mortgage loans secured by 6 medical facilities. The medical facilities within our portfolio consist of skilled nursing facilities, hospitals and medical office buildings, which are more fully described below.

Skilled Nursing Facilities. As of December 31, 2015, our portfolio included 62 skilled nursing facilities ("SNF") leased to operators and mortgage loans secured by 6 SNFs. SNFs provide some combination of skilled and intermediate nursing and rehabilitative care, including speech, physical and occupational therapy. As the decision to utilize the services of a SNF is typically made as the result of a pressing medical concern, we consider this to be a need driven medical facility. The operators of the SNFs receive payment from a combination of private pay sources and government programs such as Medicaid and Medicare. SNFs are required to obtain state licenses and are highly regulated at the federal, state and local

Table of Contents

level. Most SNFs must obtain a CON from the state before opening or expanding such facilities. Some SNFs also include assisted living beds.

Hospitals. As of December 31, 2015, our portfolio included 3 hospitals ("HOSP") leased to operators. Hospitals provide a wide range of inpatient and outpatient services, including acute psychiatric and rehabilitation services, and are subject to extensive federal, state and local legislation and regulation. Hospitals undergo periodic inspections regarding standards of medical care, equipment and hygiene as a condition of licensure. Services provided by hospitals are generally paid for by a combination of private pay sources and government programs. As the decision to utilize the services of a hospital is typically made as the result of a pressing medical concern, we consider this to be a need driven medical facility.

Medical Office Buildings. As of December 31, 2015, our portfolio included 2 medical office buildings ("MOB") leased to operators. MOBs are specifically configured office buildings whose tenants are primarily physicians and other medical practitioners. As the decision to utilize the services of an MOB is typically made as a the result of a pressing medical concern, we consider this to be a need driven medical facility. MOBs differ from conventional office buildings due to the special requirements of the tenants. Each of our MOBs is leased to one lessee, and is either physically attached to or located on an acute care hospital campus. The lessee sub-leases individual office space to the physicians or other medical practitioners. The lessee is responsible to us for the lease obligations of the entire building, regardless of their ability to sub-lease the individual office space.

Nature of Investments

Our investments are typically structured as acquisitions of properties through purchase-leaseback transactions, acquisitions of properties from other real estate investors, mortgage loans or, in operations through structures allowed by RIDEA. We have also provided construction loans for facilities for which we were already committed to provide long-term financing or for which the operator agreed to enter into a purchase option and lease with us upon completion of construction or after the facility is stabilized. The annual lease rates on our leases and the annual interest rates on our mortgage, construction and mezzanine loans ranged between 6.75% and 13.50% during 2015. We believe our lease and loan terms are competitive within our peer group. Typical characteristics of these transactions are as follows:

Leases. Our leases generally have an initial leasehold term of 10 to 15 years with one or more 5-year renewal options. The leases are "triple net leases" under which the tenant is responsible for the payment of all taxes, utilities, insurance premium costs, repairs and other charges relating to the ownership and operation of the properties, including required levels of capital expenditure each year. The tenant is obligated at its expense to keep all improvements, fixtures and other components of the properties covered by "all risk" insurance in an amount equal to at least the full replacement cost thereof, and to maintain specified minimal personal injury and property damage insurance, protecting us as well as the tenant. The leases also require the tenant to indemnify and hold us harmless from all claims resulting from the use and occupancy of each facility by the tenant and related activities, and to indemnify us against all costs related to any release, discovery, clean-up and removal of hazardous substances or materials on, or other environmental responsibility with respect to each facility.

Most of our existing leases contain annual escalators in rent payments. For financial statement purposes, rental income is recognized on a straight-line basis over the term of the lease. Certain of our operators hold purchase options allowing them to acquire properties they currently lease from NHI. When present, tenant purchase options generally give the lessee an option to purchase the underlying property for consideration determined by i) a sliding base dependent upon the extent of appreciation in the property plus a specified proportion of any appreciation; ii) our acquisition costs plus a specified proportion of any appreciation; iii) an agreed capitalization rate applied to the current rental; or iv) our acquisition costs plus a profit floor plus a specified proportion of any appreciation. Where stipulated

above, appreciation is to be established by independent appraisal.

Some of the obligations under the leases are guaranteed by the parent corporation of the lessee, if any, or affiliates or individual principals of the lessee. In some leases, the third party operator will also guarantee some portion of the lease obligations. Some obligations are backed further by other collateral such as security deposits, machinery, equipment, furnishings and other personal property.

We monitor our triple-net lessee tenant credit quality and identify any material changes by performing the following activities:

- Obtaining financial statements on a monthly, quarterly and/or annual basis to assess the operational trends of our tenants and the financial position and capability of those tenants
- Calculating the operating cash flow for each of our tenants
- Calculating the lease service coverage ratio and other ratios pertinent to our tenants
- Obtaining property-level occupancy rates for our tenants

Table of Contents

- Verifying the payment of taxes by our tenants
- Obtaining certificates of insurance for each tenant
- Obtaining financial statements of our lessee guarantors on an annual basis
- Conducting a periodic inspection of our properties to ascertain proper maintenance, repair and upkeep
- Monitoring those tenants with indications of continuing and material deteriorating credit quality through discussions with our executive management and Board of Directors

RIDEA Transactions. Our arrangement with Bickford Senior Living ("Bickford") is structured to be compliant with the provisions of RIDEA which permits NHI to receive rent payments through a triple-net lease between a property company and an operating company and gives NHI the opportunity to capture additional value on the improving performance of the operating company through distributions to a Taxable REIT Subsidiary ("TRS"). Accordingly, the TRS holds our 85% equity interest in an unconsolidated operating company, which we do not control, and provides an organizational structure that will allow the TRS to engage in a broad range of activities and share in revenues that would otherwise be non-qualifying income under the REIT gross income tests. The TRS is subject to state and federal income taxes.

Mortgage loans. We have first mortgage loans with maturities of at least 5 years from inception with varying amortization schedules from interest only to fully amortizing. Most of the loans are at a fixed interest rate; however, some interest rates increase based on a fixed schedule of rate increases. In most cases, the owner of the facility is committed to make minimum annual capital expenditures for the purpose of maintaining or upgrading their respective facility. Additionally, most of our loans are collateralized by first mortgage liens and corporate or personal guarantees.

We have made mortgage loans to borrowers secured by a second deed-of-trust where there is a process in place for the borrower to obtain long-term financing, primarily with a U.S. government agency, and where the historical financial performance of the underlying facility meets our loan underwriting criteria. We currently have one second mortgage loan with an interest rate of 12%.

Construction loans. From time to time, we also provide construction loans that by their terms convert to mortgage loans upon the completion of the construction of the facility. We may also obtain a purchase option to acquire the facility at a future date and lease the facility back to the operator. The terms of such construction loans are for a period which commences upon the closing of such loans and terminates upon the earlier of (a) the completion of the construction of the applicable facility or (b) a specific date. During the term of the construction loan, funds are usually advanced pursuant to draw requests made by the borrower in accordance with the terms and conditions of the loan. Interest is typically assessed on these loans at rates equivalent to the eventual mortgage rate upon conversion. In addition to the security of the lien against the property, we will generally require additional security and collateral in the form of either payment and performance completion bonds or completion guarantees by the borrower's parent, affiliates of the borrower or one or more of the individuals who control the borrower.

Other notes receivable. We have provided a revolving credit facility to a borrower whose business is to provide bridge loans to owner-operators who are qualifying for long-term HUD financing secured by real estate. Our interest rate on the credit facility is 13.5%. We have provided loans to borrowers involved in the skilled nursing and senior housing industries who have pledged personal and business guarantees as security for the loans. The interest rates on these loans currently range from 8% to13.5%.

Investment in marketable securities. At December 31, 2015, we invested a portion of our funds in various marketable securities with quoted market prices, including the common shares of other publicly-held REITs. We classify these highly-liquid securities as available-for-sale and carry the investments at their then quoted fair market value at the balance sheet date. We may choose to liquidate these investments to invest the proceeds into real estate assets. With

respect to the safekeeping of certain security deposits or where liquidity is otherwise of significant concern, a portion of our funds may be invested in government agency debt securities, long-term certificates of deposit, or other risk-appropriate securities as determined by management.

Table of Contents

Competition and Market Conditions

We compete with other REITs, private equity funds and other investors (including, but not limited to, banks, insurance companies, and investment banks who market securities in mortgage funds) in the acquisition, leasing and financing of health care real estate.

Operators of our facilities compete on a local and regional basis with operators of facilities that provide comparable services. Operators compete for residents and/or patients and staff based on quality of care, reputation, physical appearance of facilities, services offered, family preference, physicians, staff and price. Competition is with independent operators as well as companies managing multiple facilities, some of which are substantially larger and have greater resources than the operators of our facilities. Some of these facilities are operated for profit while others are owned by governmental agencies or tax exempt not-for-profit organizations.

The SNFs which either secure our mortgage loans or we lease to operators receive the majority of their revenues from Medicare, Medicaid and other government programs. From time to time, these facilities have experienced Medicare and Medicaid revenue reductions brought about by the enactment of legislation to reduce government costs. In particular, the establishment of a Medicare Prospective Payment System (“PPS”) for SNF services to replace the cost-based reimbursement system significantly reduced Medicare reimbursement to SNF providers. While Congress subsequently took steps to mitigate the impact of PPS on SNFs, other federal legislative policies have been adopted and continue to be proposed that would reduce the growth rate of Medicare and/or Medicaid payments to SNFs. State Medicaid funding is not expected to keep pace with inflation according to industry studies. Any changes in government reimbursement methodology that reduce reimbursement to levels that are insufficient to cover the operating costs of our borrowers and lessees could adversely impact us.

Senior housing communities generally rely on private-pay residents who may be negatively impacted in an economic downturn. The success of these facilities is often impacted by the existence of comparable, competing facilities in a local market.

Operator Diversification

For the year ended December 31, 2015, approximately 21% of our portfolio revenue was from publicly-owned operators, 53% was from regional operators, 22% from national chains which are privately owned and 5% was from smaller operators. We consider the creditworthiness of the operator to be an important factor in our underwriting of the investment, and we generally have the right to approve any changes in operators.

For the year ended December 31, 2015, operators of facilities which provided more than 3% of our total revenues were (in alphabetical order): Bickford Senior Living; Fundamental; Health Services Management; Holiday Retirement; Legend Healthcare; National HealthCare Corporation; and Senior Living Communities.

Major Customers

We have four operators, an affiliate of Holiday Retirement ("Holiday"), Senior Living Communities, LLC ("Senior Living"), National HealthCare Corporation (“NHC”) and Bickford Senior Living ("Bickford"), from whom we individually derive at least 10% of our income.

Holiday

In December 2013 we acquired 25 independent living facilities from an affiliate of Holiday for $491,000,000 plus transaction costs of $1,959,000. We have leased this portfolio to Holiday AL Holdings, LP, a subsidiary of Holiday.

Our tenant operates the facilities pursuant to a management agreement with a Holiday-affiliated manager. The master lease term of 17 years began in December 2013 and provided for initial base rent of $31,915,000 plus annual escalators of 4.5% in the first 3 years and a minimum of 3.5% each year thereafter.

Of our total revenue from continuing operations, $43,817,000 (19%) and $43,817,000 (25%) were recorded as rental income from Holiday, including straight-line revenues of $10,466,000 and $11,902,000 for the years ended December 31, 2015 and 2014, respectively.

Table of Contents

Senior Living Communities

In December 2014, we acquired a portfolio of eight retirement communities (the “Senior Living Portfolio”) with a total of 1,671 units from Health Care REIT, Inc. and certain of its affiliates for a cash purchase price of $476,000,000. The Senior Living Portfolio includes seven entrance-fee communities and one senior living campus.

We have leased the Senior Living Portfolio under a triple-net master lease with an affiliate of Senior Living which continues to manage the facilities. The 15-year master lease contains two 5-year renewal options and provides for year one cash rent of $31,000,000, subject to annual escalators of 4% in years two through four and 3% thereafter.

In connection with the Senior Living acquisition, we provided a $15,000,000 revolving line of credit to Senior Living, the maturity of which mirrors the term of the master lease. Borrowings will be used primarily to finance construction projects within the Senior Living Portfolio, including building additional units. Amounts outstanding under the facility, $6,282,000 at December 31, 2015, bear interest at an annual rate equal to the 10-year U.S. Treasury rate, 2.27% at December 31, 2015, plus 6%.

Of our total revenue from continuing operations, $39,422,000 (17%), and $1,533,000 (1%), including $8,422,000 and $328,000 of straight-line revenues, were recorded as rental income from Senior Living, in 2015 and 2014, respectively.

NHC

NHC is a publicly-held company and the lessee of our legacy properties. We lease 42 facilities to NHC comprised of 3 independent living facilities and 39 skilled nursing facilities (4 of which are subleased to other parties for whom the lease payments are guaranteed to us by NHC). These facilities are leased to NHC under the terms of an amended Master Lease Agreement dated October 17, 1991 ("the 1991 lease") which includes our 35 remaining legacy properties and a Master Lease Agreement dated August 30, 2013 ("the 2013 lease") which includes 7 skilled nursing facilities acquired from a third party. Under the terms of the 1991 lease, base annual rental of $30,750,000 escalates by 4% of the increase, if any, in each facility’s revenue over a 2007 base year. Similarly, the 2013 lease provides for base annual rental of $3,450,000 plus percentage rent equal to 4% of the increase, if any, in each facility's annual revenue over a 2014 base year.

Of our total revenue from continuing operations, $36,625,000 (16%), $36,446,000 (21%) and $34,756,000 (29%) in 2015, 2014 and 2013, respectively, were derived from the two lease agreements with NHC.

NHC owned 1,630,462 shares of our common stock at December 31, 2015. The chairman of our board of directors is also a director on NHC’s board.

Bickford

As of December 31, 2015, we owned an 85% equity interest, and Sycamore Street, LLC ("Sycamore"), an affiliate of Bickford, owned a 15% equity interest in our consolidated subsidiary ("PropCo"), which owns 32 assisted living/memory care facilities, plus 5 facilities under development. The facilities are leased to an operating company, ("OpCo"), in which we retain an 85/15 non-controlling ownership interest with Sycamore. The facilities are managed by Bickford. This joint venture is structured to comply with the provisions of RIDEA.

The current annual contractual rent from OpCo to PropCo is $25,529,000, plus fixed annual escalators. NHI has an exclusive right to Bickford's future acquisitions, development projects and refinancing transactions.

Of our total revenue from continuing operations, $24,121,000 (11%), $21,421,000 (12%) and $14,586,000 (12%) were recorded as rental income from Bickford for the years ended December 31, 2015, 2014, and 2013, respectively.

Commitments and Contingencies

The following table summarizes information as of December 31, 2015 related to our outstanding commitments and contingencies which are more fully described in the notes to the consolidated financial statements, included herein.

Table of Contents

	Asset Class	Type	Total	Funded	Remaining
Commitments:					
Life Care Services	SHO	Construction Loan	$154,500,000	$(83,411,000)	$71,089,000
Bickford Senior Living	SHO	Construction	$55,000,000	$(17,436,000)	$37,564,000
Senior Living Communities	SHO	Revolving Credit	$15,000,000	$(6,282,000)	$8,718,000
Capital Funding Group	Mezz. Note	Revolving Credit	$15,000,000	$(15,000,000)	$—
Chancellor Health Care	SHO	Construction	$650,000	$(33,000)	$617,000
Santé Partners	SHO	Renovation	$3,500,000	$(2,621,000)	$879,000
Senior Living Management	SHO	Renovation	$1,430,000	$(1,165,000)	$265,000
Bickford Senior Living	SHO	Renovation	$620,000	$(575,000)	$45,000
Sycamore Street (Bickford affiliate)	SHO	Revolving Credit	$500,000	$(461,000)	$39,000
East Lake Capital Management	SHO	Renovation	$400,000	$—	$400,000
Contingencies:					
East Lake Capital Management	SHO	Lease Inducement	$8,000,000	$—	$8,000,000
East Lake Capital Management	SHO	Seller Earnout	$750,000	$—	$750,000
Sycamore Street (Bickford affiliate)	SHO	Letter-of-credit	$3,550,000	$—	$3,550,000
Discovery Senior Living	SHO	Lease Inducement	$2,500,000	$—	$2,500,000
Santé Partners	SHO	Lease Inducement	$2,000,000	$—	$2,000,000

Sources of Revenues

General. Our revenues are derived primarily from rental income, mortgage and other note interest income and income from our other investments, substantially all of which are in marketable securities, including the common stock of other healthcare REITs. During 2015, rental income was $214,447,000 (94%), interest income from mortgages and other notes was $9,978,000 (4%) and income from our other investments was $4,563,000 (2%) of total revenue from continuing operations of $228,988,000. Our revenues depend on the operating success of our facility operators whose source and amount of revenues are determined by (i) the licensed beds or other capacity of the facility, (ii) the occupancy rate of the facility, (iii) the extent to which the services provided at each facility are utilized by the patients, (iv) the mix of private pay, Medicare and Medicaid patients at the facility, and (v) the rates paid by private paying patients and by the Medicare and Medicaid programs.

Governmental and other concerns regarding health care costs have and may continue to result in significant downward pressure on payments to health care facilities, and there can be no assurance that future payment rates for either governmental or private health care plans will be sufficient to cover cost increases in providing services to patients. Any changes in reimbursement policies which reduce reimbursement to levels that are insufficient to cover the cost of providing patient care could have an adverse effect on revenues of our lessees and borrowers and thereby adversely affect those lessees' and borrowers' abilities to make their lease or debt payments to us. Failure of the lessees or borrowers to make their lease or debt payments would have a direct and material adverse impact on us.

Medicare and Medicaid. A significant portion of the revenue of our SNF lessees and borrowers is derived from government funded reimbursement programs, such as Medicare and Medicaid. Reimbursement under these programs is subject to periodic payment review and other audits by federal and state authorities. Medicare is uniform nationwide and reimburses skilled nursing centers under a Prospective Payment System (“PPS”) which is based on a predetermined, fixed amount. PPS is an acuity based classification system that uses nursing and therapy indexes adjusted by geographical wage indexes to calculate per diem rates for each Medicare patient. Payment rates are updated annually and are generally adjusted each October when the federal fiscal year begins. The current acuity classification system is

named Resource Utilization Groups IV (“RUGs IV”) and was effective October 1, 2010. Federal legislative policies have been adopted and continue to be proposed that would provide smaller increases in annual Medicare payments to nursing facilities. For example, the Centers for Medicare and Medicaid Services ("CMS") announced the Skilled Nursing Facilities – PPS final rule for fiscal year 2016 which increases Medicare payments to SNF operators by only 1.2% beginning October 1, 2015. The fiscal year 2015 increase was 2.0%, the fiscal year 2014 increase was 1.4% and the fiscal year 2013 increase was 1.8%.

In the future, any failure of Congress to agree on spending reductions to meet long-term mandated deficit reduction goals would trigger automatic spending cuts of 2% to Medicare.

Table of Contents

RUGs IV incorporated changes to PPS that significantly altered how SNFs are paid for rendering care. Some examples are as follows:

- A shift to 66 payment categories from 53 payment categories;
- Changes related to assessment reference dates and qualifiers that will significantly reduce utilization of rehabilitation and extensive service categories;
- Modification to therapy services related to estimating treatments and utilization of concurrent therapy that will likely result in RUG classifications at much lower levels of therapy than previous results; and
- Adjustments related to assistance with activities of daily living (ADLs) and an increased emphasis on ADL scores in the nursing case mix indices and related RUG payment rates.

Medicaid is a joint federal and state program designed to provide medical assistance to “eligible needy persons.” Medicaid programs are operated by state agencies that adopt their own medical reimbursement methodology and standards. Payment rates and covered services vary from state to state. In many instances, revenues from Medicaid programs are insufficient to cover the actual costs incurred in providing care to those patients. With regard to Medicaid payment increases to skilled nursing operators, changes in federal funding coupled with state budget problems have produced uncertainty. States will more than likely be unable to keep pace with nursing center inflation. States are under pressure to pursue other alternatives to long term care such as community and home-based services. Furthermore, several of the states in which we have investments have actively sought to reduce or slow the increase of Medicaid spending for nursing home care.

Medicare and Medicaid programs are highly regulated and subject to frequent and substantial changes resulting from legislation, adoption of rules and regulations and administrative and judicial interpretations of existing law. Moreover, as health care facilities have experienced increasing pressure from private payors attempting to control health care costs, reimbursement from private payors has in many cases effectively been reduced to levels approaching those of government payors. Healthcare reimbursement will likely continue to be of significant importance to federal and state authorities. We cannot make any assessment as to the ultimate timing or the effect that any future legislative reforms may have on our lessees’ and borrowers’ costs of doing business and on the amount of reimbursement by government and other third-party payors. There can be no assurance that future payment rates for either government or private payors will be sufficient to cover cost increases in providing services to patients. Any changes in reimbursement policies which reduce reimbursement to levels that are insufficient to cover the cost of providing patient care could adversely affect the operating revenues of our SNF and hospital lessees and borrowers, and thereby adversely affect their ability to make their lease or debt payments to us. Failure of our lessees and borrowers to make their scheduled lease and loan payments to us would have a direct and material adverse impact on us.

Government Regulation

Licensure and Certification. The health care industry is highly regulated by federal, state and local law and is directly affected by state and local licensing requirements, facility inspections, state and federal reimbursement policies, regulations concerning capital and other expenditures, certification requirements and other such laws, regulations and rules. Sanctions for failure to comply with these regulations and laws include (but are not limited to) loss of licensure, fines and loss of certification to participate in the Medicare and Medicaid programs, as well as potential criminal penalties. The failure of any lessee or borrower to comply with such laws, requirements and regulations could affect their ability to operate the facility or facilities and could adversely affect such lessee's or borrower's ability to make lease or debt payments to us.

In the past several years, due to rising health care costs, there has been an increased emphasis on detecting and eliminating fraud and abuse in the Medicare and Medicaid programs. Payment of any consideration in exchange for referral of Medicare and Medicaid patients is generally prohibited by federal statute, which subjects violators to severe penalties, including exclusion from the Medicare and Medicaid programs, fines and even prison sentences. In recent years, both federal and state governments have significantly increased investigation and enforcement activity to detect and punish wrongdoers. In addition, legislation has been adopted at both state and federal levels which severely restrict the ability of physicians to refer patients to entities in which they have a financial interest.

It is anticipated that the trend toward increased investigation and enforcement activity in the area of fraud and abuse, as well as self-referral, will continue in future years. Certain of our investments are with lessees or borrowers which are partially or wholly owned by physicians. In the event that any lessee or borrower were to be found in violation of laws regarding fraud and abuse or self-referral, that lessee's or borrower's ability to operate the facility could be jeopardized, which could adversely affect the lessee's or borrower's ability to make lease or debt payments to us and thereby adversely affect us.

Table of Contents

Certificates of Need. The SNFs and hospitals in which we invest are also generally subject to state statutes which may require regulatory approval in the form of a CON prior to the construction or expansion of facilities to accommodate new beds (or addition of new beds to existing facilities), the addition of services or certain capital expenditures. CON requirements are not uniform throughout the United States and are subject to change. We cannot predict the impact of regulatory changes with respect to CONs on the operations of our lessees and borrowers; however, in our primary market areas, a significant reduction in new construction of long-term care beds has occurred.

Investment Policies

Our investment objectives are (i) to provide consistent and growing current income for distribution to our stockholders through investments primarily in health care related facilities or in the operations thereof through independent third-party management, (ii) to provide the opportunity to realize capital growth resulting from appreciation, if any, in the residual value of our portfolio properties, and (iii) to preserve and protect stockholders' capital through a balance of diversity, flexibility and liquidity. There can be no assurance that these objectives will be realized. Our investment policies include making investments in real estate, mortgage and other notes receivable, marketable securities, including the common stock of other REITs, and joint ventures structured to comply with the provisions of RIDEA.

As described in Item 7 and in Notes 2 and 4 to the consolidated financial statements, included herein, we have funded or made commitments to fund new investments in real estate and loans since January 1, 2015 totaling $310,075,000, and we anticipate making additional investments in 2016 that meet our underwriting criteria. In making new investments, we consider such factors as (i) the geographic area and type of property, (ii) the location, construction quality, condition and design of the property, (iii) the current and anticipated cash flow and its adequacy to meet operational needs, and lease or mortgage obligations to provide a competitive income return to our investors, (iv) the growth, tax and regulatory environments of the communities in which the properties are located, (v) occupancy and demand for similar facilities in the same or nearby communities, (vi) the quality, experience and creditworthiness of the management operating the facilities located on the property and (vii) the mix of private and government-sponsored residents. There can be no assurances that investments meeting our standards regarding these attributes will be found or closed.

We will not, without the approval of a majority of the Board of Directors, and review of a committee comprised of independent directors, enter into any joint venture relationships with or acquire from or sell to any director, officer or employee of NHI, or any affiliate thereof, as the case may be, any of our assets or other property.

The Board of Directors, without the approval of the stockholders, may alter our investment policies if it determines that such a change is in our best interests and our stockholders’ best interests. The methods of implementing our investment policies may vary as new investment and financing techniques are developed or for other reasons. Management may recommend changes in investment criteria from time to time.

Future investments in health care related facilities may utilize borrowed funds or issuance of equity when it is advisable in the opinion of the Board of Directors. We may negotiate lines of credit or arrange for other short or long-term borrowings from lenders. We may arrange for long-term borrowings from institutional investors or through public offerings. We have previously invested and may in the future invest in properties subject to existing loans or secured by mortgages, deeds of trust or similar liens with favorable terms or in mortgage investment pools.

Executive Officers of the Company

The table below sets forth the name, position and age of each of our executive officers. Each executive officer is appointed by the Board of Directors, serves at its pleasure and holds office for a term of one year. There is no “family relationship” among any of the named executive officers or with any director. All information is given as of February

15, 2016:

Name	Position	Age
Eric Mendelsohn	President and Chief Executive Officer	54
Roger R. Hopkins	Chief Accounting Officer	54
Kristin S. Gaines	Chief Credit Officer	44
Kevin Pascoe	Executive Vice President Investments	35

Eric Mendelsohn, formerly Executive Vice President of Corporate Finance and interim Chief Executive Officer since early August 2015, joined NHI in January 2015. He has over 15 years of healthcare real estate and financing experience. Previously, Mr. Mendelsohn was with Emeritus Senior Living for 9 years, most recently as a Senior Vice President of Corporate Development

Table of Contents

where he was responsible for the financing and acquisition of assisted living properties, home health care companies, administration of joint venture relationships and executing corporate finance strategies. Prior to Emeritus, he was with the University of Washington as a Transaction Officer where he worked on the development, acquisition and financing of research, clinic and medical properties and has been a practicing transaction attorney, representing lenders and landlords. Mr. Mendelsohn holds a BS from American University in International Relations, a Law Degree from Pepperdine University, and a Masters (LLM) in Banking and Finance from Boston University. Mr. Mendelsohn is a member of the Florida and Washington State Bar Associations.

Roger R. Hopkins joined the former management advisor of NHI in July 2006 and was named Chief Accounting Officer for NHI in December 2006. With over 33 years of combined financial experience in public accounting and the real estate industry, he positioned companies to access public and private capital markets for equity and debt. Mr. Hopkins is responsible at NHI for the development of financial and tax strategies, reporting metrics, supplemental data reports and NHI's internal control system. He has accounted for significant acquisitions and financings by NHI, including the successful executions of convertible debt and follow-on equity offerings, private debt placements and bank financing arrangements. Mr. Hopkins was an Audit Partner in the Nashville office of Rodefer Moss & Co, a regional accounting firm with five offices in Tennessee and Kentucky, where he brought extensive experience in Securities and Exchange Commission filing requirements and compliance issues. He was previously a Senior Manager in the Nashville office of Deloitte. Mr. Hopkins received his Bachelor of Science in Accounting from Tennessee Technological University in 1982 and is a CPA licensed in Tennessee.
Kristin S. Gaines was appointed NHI's Chief Credit Officer in February 2010. She joined NHI in 1998 as a Credit Analyst. During her tenure with NHI, Ms. Gaines has had a progressive career in the areas of finance and operations. Her experience has resulted in a breadth of expertise in underwriting, portfolio oversight and real estate finance. Ms. Gaines holds an MBA and a Bachelor of Business Administration in Accounting from Middle Tennessee State University.

Kevin Pascoe joined NHI in June 2010. Mr. Pascoe oversees NHI's portfolio of assets, relationship management with existing tenants and conducts operational due diligence on NHI's existing investments and new investment opportunities. He has over 10 years of health care real estate background including his experience with General Electric - Healthcare Financial Services (2006 – 2010) where he most recently served as a Vice-President. With GE HFS he moved up through the organization while working on various assignments including relationship management, deal restructuring, and special assets. He also was awarded an assignment in the GE Capital Global Risk Rotation Program. Mr. Pascoe holds an MBA and a Bachelor of Business Administration in Economics from Middle Tennessee State University.

We have a staff of 12, all serving in our corporate office in Murfreesboro, TN. Essential services such as internal auditing, tax compliance, information technology and legal services are outsourced to third-party professional firms.

Investor Information

We publish our annual report on Form 10-K, quarterly reports on Form 10-Q, quarterly Supplemental Information, current reports on Form 8-K, and press releases to our website at www.nhireit.com. We have a policy of publishing these on the website within two (2) business days after public release or filing with the SEC.

We also maintain the following documents on our web site:

The NHI Code of Business Conduct and Ethics. This has been adopted for all employees, officers and directors of the Company.

Information on our “NHI Valuesline” which allows all interested parties to communicate with NHI executive officers and directors. The toll free number is 877-880-2974 and the communications may be made anonymously, if desired.

The NHI Restated Audit Committee Charter.

The NHI Revised Compensation Committee Charter.

The NHI Revised Nominating and Corporate Governance Committee Charter.

The NHI Corporate Governance Guidelines.

We will furnish, free of charge, a copy of any of the above documents to any interested investor upon receipt of a written request.

Our transfer agent is Computershare. Computershare will assist registered owners with the NHI Dividend Reinvestment plan, change of address, transfer of ownership, payment of dividends, replacement of lost checks or stock certificates. Computershare’s

Table of Contents

contact information is: Computershare Trust Company, N.A., P.O. Box 43078, Providence, RI 02940-3078. The toll free number is 800-942-5909 and the website is www.computershare.com.

The Annual Stockholders' meeting will be held at 1:00 p.m. local time on Thursday, May 5, 2016 at Stones River Country Club, 1830 NW Broad Street, Murfreesboro, TN.

ITEM 1A. RISK FACTORS

We depend on the operating success of our tenants and borrowers for collection of our lease and interest income.

Revenues to operators of our facilities are primarily driven by occupancy, Medicare and Medicaid reimbursement and private pay rates. Revenues from government reimbursement have, and may continue to, come under pressure due to reimbursement cuts and from widely-publicized federal and state budget shortfalls and constraints. Periods of weak economic growth in the U.S. which affect housing sales, investment returns and personal incomes may adversely affect senior housing occupancy rates. Expenses for the facilities are driven by the costs of labor, food, utilities, taxes, insurance and rent or debt service. Liability insurance and staffing costs continue to increase for our operators. To the extent any decrease in revenues and/or any increase in operating expenses results in a facility not generating enough cash to make scheduled payments to us, our revenues, net income and funds from operations would be adversely affected. Such events and circumstances would cause us to evaluate whether there was an impairment of the real estate or mortgage loan that should be charged to earnings. Such impairment would be measured as the amount by which the carrying amount of the asset exceeded its fair value. Consequently, we might be unable to maintain or increase our current dividend and the market price of our stock may decline.

We depend on the success of property development and construction activities, which may fail to achieve the operating results we expect.

When we decide to invest in the renovation of an existing property or in the development of a new property, we make assumptions about the future potential cash flows of that property. We estimate our return based on expected occupancy, rental rates and future capital costs. If our projections prove to be inaccurate due to increased capital costs, lower occupancy or other factors, our investment in that property may not generate the cash flow we expected. Recently developed properties, including our Bickford construction, may take longer than expected to achieve stabilized operating levels, if at all. To the extent such facilities fail to reach stabilized operating levels or achieve stabilization later than expected, it could materially adversely affect our RIDEA operations or our tenants' abilities to make payments to us under their leases and thus adversely affect our business and results of operations.

We are exposed to the risk that our tenants and borrowers may not be able to meet the rent, principal and interest or other payments due us, which may result in an operator bankruptcy or insolvency, or that an operator might become subject to bankruptcy or insolvency proceedings for other reasons.

Although our operating lease agreements provide us the right to evict an operator, demand immediate payment of rent and exercise other remedies, and our mortgage loans provide us the right to terminate any funding obligations, demand immediate repayment of principal and unpaid interest, foreclose on the collateral and exercise other remedies, the bankruptcy laws afford certain rights to a party that has filed for bankruptcy or reorganization. An operator in bankruptcy may be able to limit or delay our ability to collect unpaid rent in the case of a lease or to receive unpaid principal and/or interest in the case of a mortgage loan and to exercise other rights and remedies. We may be required to fund certain expenses (e.g. real estate taxes, maintenance and capital improvements) to preserve the value of a facility, avoid the imposition of liens on a facility and/or transition a facility to a new operator. In some instances, we have terminated our lease with an operator and leased the facility to another operator. In some of those situations, we provided working capital loans to, and limited indemnification of, the new operator. If we cannot transition a leased

facility to a new operator, we may take possession of that facility, which may expose us to certain successor liabilities. Should such events occur, our revenue and operating cash flow may be adversely affected.

We are exposed to risks related to governmental regulations and payors, principally Medicare and Medicaid, and the effect that lower reimbursement rates would have on our tenants' and borrowers' business.

Our operators' businesses are affected by government reimbursement and private payor rates. To the extent that any of our facilities receive a significant portion of their revenues from governmental payors, primarily Medicare and Medicaid, such revenues may be subject to statutory and regulatory changes, retroactive rate adjustments, recovery of program overpayments or set-offs, administrative rulings, policy interpretations, payment or other delays by fiscal intermediaries, government funding restrictions (at a program level or with respect to specific facilities) and interruption or delays in payments due to any ongoing governmental investigations and audits at such facilities. In recent years, governmental payors have frozen or reduced payments to health care providers due to budgetary pressures. Such reductions in Medicare reimbursement will have an adverse effect on the financial

Table of Contents

operations of our borrowers and lessees who operate SNFs. Changes in health care reimbursement will likely continue to be of paramount importance to federal and state authorities. We cannot make any assessment as to the ultimate timing or effect any future legislative reforms may have on the financial condition of the health care industry. There can be no assurance that adequate reimbursement levels will continue to be available for services provided by any facility operator, whether the facility receives reimbursement from Medicare, Medicaid or private payors. Significant limits on the scope of services reimbursed and on reimbursement rates and fees could have a material adverse effect on an operator's liquidity, financial condition and results of operations, which could adversely affect the ability of an operator to meet its obligations to us. In addition, the replacement of an operator that has defaulted on its lease or loan could be delayed by the approval process of any federal, state or local agency necessary for the transfer of the facility or the replacement of the operator licensed to manage the facility.

We are exposed to the risk that the cash flows of our tenants and borrowers would be adversely affected by increased liability claims and liability insurance costs.

ALF and SNF operators have experienced substantial increases in both the number and size of patient care liability claims in recent years, particularly in the states of Texas and Florida. As a result, general and professional liability costs have increased and may continue to increase. Nationwide, long-term care liability insurance rates are increasing because of large jury awards in states like Texas and Florida. Both Texas and Florida have now adopted SNF liability laws that modify or limit tort damages. Despite some of these reforms, the long-term care industry overall continues to experience very high general and professional liability costs. Insurance companies have responded to this claims crisis by severely restricting their capacity to write long-term care general and professional liability policies. No assurance can be given that the climate for long-term care general and professional liability insurance will improve in any of the foregoing states or any other states where the facility operators conduct business. Insurance companies may continue to reduce or stop writing general and professional liability policies for ALFs and SNFs. Thus, general and professional liability insurance coverage may be restricted, very costly or not available, which may adversely affect the facility operators' future operations, cash flows and financial condition and may have a material adverse effect on the facility operators' ability to meet their obligations to us.

We are exposed to risks related to environmental laws and the costs associated with liabilities related to hazardous substances.

Under various federal and state laws, owners or operators of real property may be required to respond to the release of hazardous substances on the property and may be held liable for property damage, personal injuries or penalties that result from environmental contamination. These laws also expose us to the possibility that we may become liable to reimburse the government for damages and costs it incurs in connection with the contamination. Generally, such liability attaches to a person based on the person's relationship to the property. Our tenants or borrowers are primarily responsible for the condition of the property and since we are a passive landlord, we do not "participate in the management" of any property in which we have an interest. Moreover, we review environmental site assessment of the properties that we own or encumber prior to taking an interest in them. Those assessments are designed to meet the "all appropriate inquiry" standard, which qualifies us for the innocent purchaser defense if environmental liabilities arise. Based upon such assessments, we do not believe that any of our properties are subject to material environmental contamination. However, environmental liabilities, including mold, may be present in our properties and we may incur costs to remediate contamination, which could have a material adverse effect on our business or financial condition.

We are exposed to the risk that we may not be fully indemnified by our lessees and borrowers against future litigation.

Our leases require that the lessee name us as an additional insured party on the tenant's insurance policy in regard to claims made for professional liability or personal injury. The leases also require the tenant to indemnify and hold us harmless for all claims resulting from the occupancy and use of each facility. We cannot give any assurance that these

protective measures will completely eliminate any risk to us related to future litigation, the costs of which could have a material adverse impact on us.

We depend on the success of our future acquisitions and investments.

We are exposed to the risk that our future acquisitions may not prove to be successful. We could encounter unanticipated difficulties and expenditures relating to any acquired properties, including contingent liabilities, and newly acquired properties might require significant management attention that would otherwise be devoted to our existing business. If we agree to provide construction funding to an operator and the project is not completed, we may need to take steps to ensure completion of the project or we could lose the property. Moreover, if we issue equity securities or incur additional debt, or both, to finance future acquisitions, it may reduce our per share financial results. These costs may negatively affect our results of operations.

Table of Contents

We depend on our ability to reinvest cash in real estate investments in a timely manner and on acceptable terms.

From time to time, we will have cash available from (1) the proceeds of sales of our securities, (2) principal payments on our notes receivable and (3) the sale of properties, including non-elective dispositions, under the terms of master leases or similar financial support arrangements. We must reinvest these proceeds, on a timely basis, in health care investments or in qualified short-term investments. We compete for real estate investments with a broad variety of potential investors. This competition for attractive investments may negatively affect our ability to make timely investments on terms acceptable to us. Delays in acquiring properties may negatively impact revenues and the amount of distributions to stockholders.

We may need to refinance existing debt or incur additional debt in the future, which may not be available on terms acceptable to us.

We operate with a policy of incurring debt when, in the opinion of our Board of Directors, it is advisable. Currently, we believe that our current liquidity, availability under our unsecured credit facility, and our capacity to service additional debt will enable us to meet our obligations, including dividends, and continue to make investments in healthcare real estate. While we currently have a very low debt ratio, in the future, we may increase our borrowings. We may incur additional debt by borrowing under our unsecured credit facility, mortgaging properties we own and/or issuing debt securities in a public offering or in a private transaction. We believe we will be able to raise additional debt and equity capital at reasonable costs to refinance our existing indebtedness at or prior to its maturity. Our ability to raise reasonably priced capital is not guaranteed; we may be unable to raise reasonably priced capital because of reasons related to our business or for reasons beyond our control, such as market conditions. If our access to capital becomes limited, it could have an impact on our ability to refinance our debt obligations, fund dividend payments, acquire properties and fund acquisition activities.

We have covenants related to our indebtedness which impose certain operational limitations and a breach of those covenants could materially adversely affect our financial condition and results of operations.

The terms of our current indebtedness as well as debt instruments that the Company may enter into in the future are subject to customary financial and operational covenants. Among other things, these provisions require us to maintain certain financial ratios and minimum net worth and impose certain limits on our ability to incur indebtedness, create liens and make investments or acquisitions. Our continued ability to incur debt and operate our business is subject to compliance with these covenants, which limit operational flexibility. Breaches of these covenants could result in a default under applicable debt instruments, even if payment obligations are satisfied. Financial and other covenants that limit our operational flexibility, as well as defaults resulting from a breach of any of these covenants in our debt instruments, could have a material adverse effect on our financial condition and results of operations.

We are exposed to the risk that the illiquidity of real estate investments could impede our ability to respond to adverse changes in the performance of our properties.

Real estate investments are relatively illiquid and, therefore, our ability to quickly sell or exchange any of our properties in response to changes in economic and other conditions may be limited. All of our properties are "special purpose" properties that cannot be readily converted to general residential, retail or office use. Facilities that participate in Medicare or Medicaid must meet extensive program requirements, including physical plant and operational requirements, which are revised from time to time. Transfers of operations of facilities are subject to regulatory approvals not required for transfers of other types of commercial operations and other types of real estate. Thus, if the operation of any of our properties becomes unprofitable due to competition, age of improvements or other factors such that our lessee or borrower becomes unable to meet its obligations on the lease or mortgage loan, the liquidation value of the property may be less than the net book value or the amount owed on any related mortgage

loan, because the property may not be readily adaptable to other uses. The sale of the property or the replacement of an operator that has defaulted on its lease or loan could also be delayed by the approval process of any federal, state or local agency necessary for the transfer of the property or the replacement of the operator with a new operator licensed to manage the facility. No assurances can be given that we will recognize full value for any property that we are required to sell for liquidity reasons. Should such events occur, our results of operations and cash flows could be adversely affected.

Certain tenants/operators in our portfolio account for a significant percentage of the rent we expect to generate from our portfolio, and the failure of any of these tenants/operators to meet their obligations to us could materially and adversely affect our business, financial condition and results of operations and our ability to make distributions to our stockholders.

The successful performance of our real estate investments is materially dependent on the financial stability of our tenants/operators. Approximately 63% of our total revenue from continuing operations is generated by Holiday (19%), Senior Living (17%), NHC (16%), and Bickford (11%). Lease or interest payment defaults by Holiday, Senior Living, NHC, Bickford or other

Table of Contents

significant tenants/operators or declines in their operating performance could materially and adversely affect our business, financial condition and results of operations and our ability to make distributions to our stockholders. In the event of a tenant default, we may experience delays in enforcing our rights as landlord and may incur substantial costs in protecting our investment and re-leasing our property. Further, we cannot assure you that we will be able to re-lease the property for the rent previously received, or at all, or that lease terminations will not cause us to sell the property at a loss. The result of any of the foregoing risks could materially and adversely affect our business, financial conditions and results of operations and our ability to make distributions to our stockholders.

We are exposed to risks associated with our investments in unconsolidated entities, including our lack of sole decision-making authority and our reliance on the financial condition of other interests.

Our investments in unconsolidated entities could be adversely affected by our lack of sole decision-making authority regarding major decisions, our reliance on the financial condition of other interests, any disputes that may arise between us and other partners, and our exposure to potential losses from the actions of partners. Risks of dealing with parties outside NHI include limitations on unilateral major decisions opposed by other interests, the prospect of divergent goals of ownership including the likelihood of disputes regarding management, ownership or disposition of a property, or limitations on the transfer of our interests without the consent of our partners. Risks of the unconsolidated entity extend to areas in which the financial health of our partners may impact our plans. Our partners might become bankrupt or fail to fund their share of required capital contributions, which may hinder significant action in the entity. We may disagree with our partners about decisions affecting a property or the entity itself, which could result in litigation or arbitration that increases our expenses, distracts our officers and directors and disrupts the day-to-day operations of the property, including by delaying important decisions until the dispute is resolved; and finally, we may suffer losses as a result of actions taken by our partners with respect to our investments.

We are subject to additional risks related to healthcare operations associated with our investments in unconsolidated entities, which could have a material adverse effect on our results of operations.

We invest in other entities in compliance with RIDEA. As such, we are exposed to various operational risks with respect to those operating properties that may increase our costs or adversely affect our ability to increase revenues. These risks include fluctuations in resident occupancy, operating expenses, economic conditions; competition; certification and inspection laws, regulations, and standards; the availability of and increases in cost of general and professional liability insurance coverage; litigation; federal, state and local regulations; costs associated with government investigations and enforcement actions; the availability and increases in cost of labor; and other risks applicable to any operating business. Any one or a combination of these factors may adversely affect our revenue and operations.

We depend on revenues derived mainly from fixed rate investments in real estate assets, while a portion of our debt used to finance those investments bear interest at variable rates. This circumstance creates interest rate risk to the Company.

Our business model assumes that we can earn a spread between the returns earned from our investments in real estate as compared to our cost of capital, including debt and/or equity. Current interest rates on our debt are at historically low levels, and, as a result, the spread and our profitability on our investments have been at high levels. We are exposed to interest rate risk in the potential for a narrowing of our spread and profitability if interest rates increase in the future. Certain of our debt obligations are floating rate obligations with interest rates that vary with the movement of LIBOR or other indexes. Our revenues are derived mainly from fixed rate investments in real estate assets. Although our leases generally contain escalating rent clauses that provide a partial hedge against interest rate fluctuations, if interest rates rise, our interest costs for our existing floating rate debt and any new debt we incur would also increase. This increasing cost of debt could reduce our profitability by increasing the cost of financing our

existing portfolio and our investment activity. Rising interest rates could limit our ability to refinance existing debt upon maturity or cause us to pay higher rates upon refinancing. We manage a portion of our exposure to interest rate risk by accessing debt with staggered maturities and through the use of derivative instruments, primarily interest rate swap agreements with major financial institutions. Increased interest rates may also negatively affect the market price of our common stock and increase the cost of new equity capital.

We are exposed to the risk that our assets may be subject to impairment charges.

We periodically, but not less than quarterly, evaluate our real estate investments and other assets for impairment indicators. The judgment regarding the existence of impairment indicators is based on factors such as market conditions, operator performance and legal structure. If we determine that a significant impairment has occurred, we would be required to make an adjustment to the net carrying value of the asset, which could have a material adverse effect on our reported results of operations in the period in which the impairment charge occurs.

Table of Contents

We depend on the ability to continue to qualify for taxation as a REIT.

We intend to operate as a REIT under the Internal Revenue Code of 1986, as amended (the “Internal Revenue Code”) and believe we have and will continue to operate in such a manner. Since REIT qualification requires us to meet a number of complex requirements, it is possible that we may fail to fulfill them, and if we do, our earnings will be reduced by the amount of federal taxes owed. A reduction in our earnings would affect the amount we could distribute to our stockholders.

We have ownership limits in our charter with respect to our common stock and other classes of capital stock which may delay, defer or prevent a transaction or a change of control that might involve a premium price for our common stock or might otherwise be in the best interests of our stockholders.

Our charter, subject to certain exceptions, contains restrictions on the ownership and transfer of our common stock and preferred stock that are intended to assist us in preserving our qualification as a REIT. Our charter, provides that any transfer that would cause NHI to be beneficially owned by fewer than 100 persons or would cause NHI to be “closely held” under the Internal Revenue Code would be void, which, subject to certain exceptions, results in no person or entity being allowed to own, actually or constructively, more than 9.9% of the outstanding shares of our stock. Our Board of Directors, in its sole discretion, may exempt a proposed transferee from the ownership limit and such an exemption has been granted through Excepted Holder Agreements to members of the Carl E. Adams family. Based on the Excepted Holder Agreements currently outstanding, the individual ownership limit for all other stockholders is approximately 7.5%. Our charter gives our Board of Directors broad powers to prohibit and rescind any attempted transfer in violation of the ownership limits. These ownership limits may delay, defer or prevent a transaction or a change of control that might involve a premium price for our common stock or might otherwise be in the best interests of our stockholders.

We are subject to certain provisions of Maryland law and our charter and bylaws that could hinder, delay or prevent a change in control transaction, even if the transaction involves a premium price for our common stock or our stockholders believe such transaction to be otherwise in their best interests.

The Maryland Business Combination Act provides that, unless exempted, a Maryland corporation may not engage in business combinations, including mergers, dispositions of 10% or more of its assets, issuances of shares of stock and other specified transactions with an "interested stockholder" or an affiliate of an interested stockholder for five years after the most recent date on which the interested stockholder became an interested stockholder, and thereafter, unless specified criteria are met. An interested stockholder is generally a person owning or controlling, directly or indirectly, 10% or more of the voting power of the outstanding stock of a Maryland corporation. Unless our Board of Directors takes action to exempt us, generally or with respect to certain transactions, from this statute in the future, the Maryland Business Combination Act will be applicable to business combinations between us and other persons. The Company’s Charter and Bylaws also contain certain provisions that could have the effect of making it more difficult for a third party to acquire, or discouraging a third party from attempting to acquire, control of the Company. Such provisions could limit the price that certain investors might be willing to pay in the future for the common stock. These provisions include a staggered board of directors, blank check preferred stock, and the application of Maryland corporate law provisions on business combinations and control shares. The foregoing matters may, together or separately, have the effect of discouraging or making more difficult an acquisition or change of control of the Company.

Other risks.

See the notes to the consolidated financial statements, “Business” under Item 1 and “Legal Proceedings” under Item 3 herein for a discussion of various governmental regulations and operating factors relating to the health care industry

and other factors and the risks inherent in them. You should carefully consider each of the foregoing risks before making any investment decisions in the Company. These risks and uncertainties are not the only ones facing us. There may be additional risks that we do not presently know of or that we currently deem immaterial. If any of the risks actually occur, our business, financial condition or results of operations could be materially adversely affected. In that case, the trading price of our shares of stock could decline, and you may lose all or part of your investment. Given these risks and uncertainties, we can give no assurance that any forward-looking statements will, in fact, occur and, therefore, caution investors not to place undue reliance on them.

ITEM 1B. UNRESOLVED STAFF COMMENTS.

None.

Table of Contents

ITEM 2. PROPERTIES OWNED OR ASSOCIATED WITH MORTGAGE LOAN INVESTMENTS AS OF DECEMBER 31, 2015

Center	City	State	Lease (L)/ Mortgage (M)	Licensed Beds
SKILLED NURSING				
NHC HealthCare, Anniston	Anniston	AL	L	151
NHC HealthCare, Moulton	Moulton	AL	L	136
Sunbridge Estrella Care & Rehabilitation	Avondale	AZ	L	161
Ayers Health & Rehabilitation Center	Trenton	FL	L	120
Bayonet Point Health & Rehabilitation Center	Hudson	FL	L	180
Bear Creek Nursing Center	Hudson	FL	L	120
Brooksville Healthcare Center	Brooksville	FL	L	180
Cypress Cove Care Center	Crystal River	FL	L	120
Heather Hill Healthcare Center	New Port Richey	FL	L	120
Parkway Health & Rehabilitation Center	Stuart	FL	L	177
Royal Oak Nursing Center	Dade City	FL	L	120
The Health Center of Merritt Island	Merritt Island	FL	L	180
The Health Center of Plant City	Plant City	FL	L	180
Grangeville Health and Rehabilitation Center	Grangeville	ID	L	60
NHC HealthCare, Glasgow	Glasgow	KY	L	206
Buckley HealthCare Center	Greenfield	MA	L	120
Holyoke Health Care Center	Holyoke	MA	L	102
John Adams HealthCare Center	Quincy	MA	L	71
Longmeadow of Taunton	Taunton	MA	L	100
NHC Healthcare, Desloge	Desloge	MO	L	120
NHC Healthcare, Joplin	Joplin	MO	L	126
NHC Healthcare, Kennett	Kennett	MO	L	170
NHC Healthcare, Maryland Heights	Maryland Heights	MO	L	220
NHC HealthCare, St. Charles	St. Charles	MO	L	120
Maple Leaf HealthCare Center	Manchester	NH	L	114
Villa Crest HealthCare Center	Manchester	NH	L	165
Epsom Manor HealthCare Center	Epsom	NH	L	108
Timberview Care Center	Albany	OR	L	62
Creswell Health and Rehabilitation Center	Creswell	OR	L	53
Forest Grove Rehabilitation and Care Center	Forest Grove	OR	L	81
NHC Healthcare, Anderson	Anderson	SC	L	290
NHC Healthcare, Greenwood	Greenwood	SC	L	152
NHC HealthCare, Laurens	Laurens	SC	L	176
UniHealth Post-Acute Care-Orangeburg	Orangeburg	SC	L	88
NHC Healthcare, Athens	Athens	TN	L	98
NHC Healthcare, Chattanooga	Chattanooga	TN	L	207
NHC HealthCare, Dickson	Dickson	TN	L	211
NHC HealthCare, Franklin	Franklin	TN	L	80
NHC Healthcare, Hendersonville	Hendersonville	TN	L	122
NHC Healthcare, Johnson City	Johnson City	TN	L	160
NHC Healthcare, Lewisburg	Lewisburg	TN	L	102
NHC HealthCare, McMinnville	McMinnville	TN	L	150
NHC HealthCare, Milan	Milan	TN	L	122

NHC Healthcare, Oakwood	Lewisburg	TN	L	60
NHC HealthCare, Pulaski	Pulaski	TN	L	102
NHC Healthcare, Scott	Lawrenceburg	TN	L	62
NHC HealthCare, Sequatchie	Dunlap	TN	L	120

Table of Contents

Center	City	State	Lease (L)/ Mortgage (M)	Licensed Beds
SKILLED NURSING				
NHC HealthCare, Smithville	Smithville	TN	L	120
NHC Healthcare, Somerville	Somerville	TN	L	84
NHC Healthcare, Sparta	Sparta	TN	L	120
Canton Oaks	Canton	TX	L	120
Corinth Rehabilitation Suites	Corinth	TX	L	134
Legend Healthcare & Rehabilitation	Paris	TX	L	120
Legend Oaks Healthcare & Rehabilitation Center (East)	Houston	TX	L	125
Legend Oaks Healthcare & Rehabilitation Center (Northwest)	Houston	TX	L	125
Legend Oaks Healthcare & Rehabilitation Center	San Antonio	TX	L	125
Legend Oaks Healthcare & Rehabilitation Center - Ennis	Ennis	TX	L	124
Legend Healthcare & Rehabilitation	Greenville	TX	L	125
Legend Oaks Healthcare & Rehabilitation Center	Houston	TX	L	124
Legend Oaks Healthcare & Rehabilitation Center	Houston	TX	L	125
Legend Oaks Healthcare & Rehabilitation Center	Kyle	TX	L	126
Heritage Hall - Brookneal	Brookneal	VA	M	60
Heritage Hall - Grundy	Grundy	VA	M	120
Heritage Hall - Laurel Meadows	Laurel Fork	VA	M	60
Heritage Hall - Virginia Beach	Virginia Beach	VA	M	90
Heritage Hall - Front Royal	Front Royal	VA	M	60
Heritage Hall - Lexington	East Lexington	VA	M	60
NHC HealthCare, Bristol	Bristol	VA	L	120
ASSISTED LIVING				
Regency Pointe Retirement Community	Rainbow City	AL	L	120
The Place at Gilbert	Gilbert	AZ	L	40
The Place at Glendale	Glendale	AZ	L	38
The Place at Tanque Verde	Tucson	AZ	L	42
The Place at Tucson	Tucson	AZ	L	60
Revere Court Memory Care	Sacramento	CA	L	56
Savannah Court of Bartow	Bartow	FL	L	30
Savannah Court of Lakeland	Lakeland	FL	L	30
Indigo Palms at Maitland	Maitland	FL	L	116
Discovery Village at Naples	Naples	FL	M	120
Savannah Court of St. Cloud	St. Cloud	FL	L	30
Savannah Court at Lake Oconee	Greensboro	GA	L	64
Bickford of Ames	Ames	IA	L	37
Bickford of Burlington	Burlington	IA	L	44
Bickford of Cedar Falls	Cedar Falls	IA	L	