

HEALTH CARE REIT INC /DE/

Form 10-Q

November 07, 2007

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**UNITED STATES SECURITIES AND EXCHANGE COMMISSION  
WASHINGTON, D.C. 20549  
FORM 10-Q**

(Mark One)

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

For the quarterly period ended September 30, 2007

or

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

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

**Commission File number 1-8923  
HEALTH CARE REIT, INC.**

(Exact name of registrant as specified in its charter)

**Delaware**

**34-1096634**

(State or other jurisdiction of incorporation or organization)

(I.R.S. Employer Identification No.)

**One SeaGate, Suite 1500, Toledo, Ohio**

**43604**

(Address of principal executive office)

(Zip Code)

**(419) 247-2800**

(Registrant's telephone number, including area code)

(Former name, former address and former fiscal year, if changed since last report)

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 the filing requirements for at least the past 90 days.

Yes  No

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

Large accelerated filer  Accelerated filer  Non-accelerated filer

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

Yes  No

As of October 31, 2007, the registrant had 81,499,265 shares of common stock outstanding.

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**Table of Contents****PART I. FINANCIAL INFORMATION****Item 1. Financial Statements****CONSOLIDATED BALANCE SHEETS****HEALTH CARE REIT, INC. AND SUBSIDIARIES**

|  | <b>September<br/>30,<br/>2007<br/>(Unaudited)</b> | <b>December 31,<br/>2006<br/>(Note)</b> |
|--|---|---|
|  | <b>(In thousands)</b>                             |   |
| <b>Assets</b>  |   |   |
| Real estate investments:                                     |   |   |
| Real property owned  |   |   |
| Land and land improvements                                   | \$ 440,365  | \$ 386,693                              |
| Buildings and improvements                                   | 4,165,573   | 3,659,065                               |
| Acquired lease intangibles                                   | 129,533   | 84,082                                  |
| Real property held for sale, net of accumulated depreciation | 6,908   | 14,796                                  |
| Construction in progress                                     | 229,134   | 138,222                                 |
|  | <b>4,971,513</b>                                  | <b>4,282,858</b>                        |
| Less accumulated depreciation and amortization               | <b>(449,831)</b>                                  | <b>(347,007)</b>                        |
| Total real property owned                                    | <b>4,521,682</b>                                  | <b>3,935,851</b>                        |
| Loans receivable   | <b>271,985</b>                                    | <b>194,448</b>                          |
| Less allowance for losses on loans receivable                | <b>(7,406)</b>                                    | <b>(7,406)</b>                          |
|  | <b>264,579</b>                                    | <b>187,042</b>                          |
| Net real estate investments                                  | <b>4,786,261</b>                                  | <b>4,122,893</b>                        |
| Other assets:  |   |   |
| Equity investments   | <b>4,617</b>                                      | <b>4,700</b>                            |
| Deferred loan expenses                                       | <b>32,082</b>                                     | <b>20,657</b>                           |
| Cash and cash equivalents                                    | <b>31,440</b>                                     | <b>36,216</b>                           |
| Receivables and other assets                                 | <b>117,427</b>                                    | <b>96,144</b>                           |
|  | <b>185,566</b>                                    | <b>157,717</b>                          |
| Total assets   | <b>\$ 4,971,827</b>                               | <b>\$ 4,280,610</b>                     |
| <b>Liabilities and stockholders equity</b>                   |   |   |
| Liabilities:   |   |   |
| Borrowings under unsecured lines of credit arrangements      | \$ 145,000  | \$ 225,000                              |
| Senior unsecured notes                                       | 1,890,344   | 1,541,814                               |
| Secured debt   | 513,058   | 378,972                                 |
| Liability to subsidiary trust issuing preferred securities   | 52,184  | 52,215                                  |
| Accrued expenses and other liabilities                       | 105,629   | 101,588                                 |
| Total liabilities  | <b>2,706,215</b>                                  | <b>2,299,589</b>                        |

|  |                     |              |
|--|---------------------|--------------|
| Minority interests   | <b>4,928</b>        | 2,228        |
| Stockholders' equity:  |                     |              |
| Preferred stock, \$1.00 par value:   | <b>338,993</b>      | 338,993      |
| Authorized 50,000,000 shares   |                     |              |
| Issued and outstanding 13,174,989 shares at September 30, 2007 and December 31, 2006           |                     |              |
| Common stock, \$1.00 par value:  | <b>81,253</b>       | 73,152       |
| Authorized 225,000,000 shares  |                     |              |
| Issued 81,488,325 shares at September 30, 2007 and 73,272,052 shares at December 31, 2006      |                     |              |
| Outstanding 81,384,156 shares at September 30, 2007 and 73,192,128 shares at December 31, 2006 |                     |              |
| Capital in excess of par value   | <b>2,200,030</b>    | 1,873,811    |
| Treasury stock   | <b>(3,952)</b>      | (2,866)      |
| Cumulative net income  | <b>1,025,309</b>    | 932,853      |
| Cumulative dividends   | <b>(1,386,899)</b>  | (1,238,860)  |
| Accumulated other comprehensive income   | <b>3,302</b>        | (135)        |
| Other equity   | <b>2,648</b>        | 1,845        |
| Total stockholders' equity   | <b>2,260,684</b>    | 1,978,793    |
| Total liabilities and stockholders' equity   | <b>\$ 4,971,827</b> | \$ 4,280,610 |

NOTE: The consolidated balance sheet at December 31, 2006 has been derived from the audited financial statements at that date but does not include all of the information and footnotes required by U.S. generally accepted accounting principles for complete financial statements.

See notes to unaudited consolidated financial statements

Table of Contents**CONSOLIDATED STATEMENTS OF INCOME (UNAUDITED)  
HEALTH CARE REIT, INC. AND SUBSIDIARIES**

|   | <b>Three Months Ended</b>                    |             | <b>Nine Months Ended</b> |             |
|---|--|-------------|--------------------------|-------------|
|   | <b>September 30,</b>                         |             | <b>September 30,</b>     |             |
|   | <b>2007</b>                                  | <b>2006</b> | <b>2007</b>              | <b>2006</b> |
|   | <b>(In thousands, except per share data)</b> |             |                          |             |
| Revenues:   |  |             |                          |             |
| Rental income   | <b>\$ 117,930</b>                            | \$ 73,328   | <b>\$ 332,907</b>        | \$ 214,032  |
| Interest income   | <b>5,947</b>                                 | 4,436       | <b>17,673</b>            | 13,178      |
| Other income  | <b>1,199</b>                                 | 1,019       | <b>3,935</b>             | 3,049       |
|   | <b>125,076</b>                               | 78,783      | <b>354,515</b>           | 230,259     |
| Expenses:   |  |             |                          |             |
| Interest expense  | <b>34,869</b>                                | 23,290      | <b>99,570</b>            | 68,482      |
| Property operating expenses                                 | <b>10,426</b>                                | 0           | <b>26,251</b>            | 0           |
| Depreciation and amortization                               | <b>39,933</b>                                | 22,947      | <b>108,434</b>           | 66,839      |
| General and administrative                                  | <b>8,626</b>                                 | 5,010       | <b>28,304</b>            | 15,788      |
| Loan expense  | <b>1,504</b>                                 | 782         | <b>4,006</b>             | 2,199       |
| Provision for loan losses                                   | <b>0</b>                                     | 250         | <b>0</b>                 | 750         |
|   | <b>95,358</b>                                | 52,279      | <b>266,565</b>           | 154,058     |
| Income from continuing operations before minority interests | <b>29,718</b>                                | 26,504      | <b>87,950</b>            | 76,201      |
| Minority interests  | <b>(121)</b>                                 | 0           | <b>(407)</b>             | 0           |
| Income from continuing operations                           | <b>29,597</b>                                | 26,504      | <b>87,543</b>            | 76,201      |
| Discontinued operations:                                    |  |             |                          |             |
| Net gain (loss) on sales of properties                      | <b>766</b>                                   | 108         | <b>2,775</b>             | 2,590       |
| Income (loss) from discontinued operations, net             | <b>483</b>                                   | 201         | <b>2,138</b>             | 1,000       |
|   | <b>1,249</b>                                 | 309         | <b>4,913</b>             | 3,590       |
| Net income  | <b>30,846</b>                                | 26,813      | <b>92,456</b>            | 79,791      |
| Preferred stock dividends                                   | <b>6,317</b>                                 | 5,333       | <b>18,952</b>            | 15,998      |
| Net income available to common stockholders                 | <b>\$ 24,529</b>                             | \$ 21,480   | <b>\$ 73,504</b>         | \$ 63,793   |
| Average number of common shares outstanding:                |  |             |                          |             |
| Basic   | <b>80,710</b>                                | 62,524      | <b>77,686</b>            | 60,766      |

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|  |                |         |                  |         |
|--|----------------|---------|------------------|---------|
| Diluted  | <b>81,163</b>  | 62,866  | <b>78,234</b>    | 61,102  |
| Earnings per share:  |                |         |                  |         |
| Basic:   |                |         |                  |         |
| Income from continuing operations available to common stockholders | \$ <b>0.29</b> | \$ 0.34 | \$ <b>0.88</b>   | \$ 0.99 |
| Discontinued operations, net                                       | <b>0.02</b>    | 0.00    | <b>0.06</b>      | 0.06    |
| Net income available to common stockholders*                       | \$ <b>0.30</b> | \$ 0.34 | \$ <b>0.95</b>   | \$ 1.05 |
| Diluted:   |                |         |                  |         |
| Income from continuing operations available to common stockholders | \$ <b>0.29</b> | \$ 0.34 | \$ <b>0.88</b>   | \$ 0.99 |
| Discontinued operations, net                                       | <b>0.02</b>    | 0.00    | <b>0.06</b>      | 0.06    |
| Net income available to common stockholders*                       | \$ <b>0.30</b> | \$ 0.34 | \$ <b>0.94</b>   | \$ 1.04 |
| Dividends declared and paid per common share                       | \$ <b>0.66</b> | \$ 0.64 | \$ <b>1.6191</b> | \$ 1.90 |

\* Amounts may not sum due to rounding

See notes to unaudited consolidated financial statements

**Table of Contents****CONSOLIDATED STATEMENTS OF STOCKHOLDERS EQUITY (UNAUDITED)  
HEALTH CARE REIT, INC. AND SUBSIDIARIES**

Nine Months Ended September 30, 2007

|  | Preferred<br>Stock | Common<br>Stock | Capital in<br>Excess of<br>Par Value | Treasury<br>Stock | Cumulative<br>Net Income | Cumulative<br>Dividends | Accumulated<br>Other<br>Comprehensive<br>Income | Other<br>Equity | Total       |
|--|--------------------|-----------------|--------------------------------------|-------------------|--------------------------|-------------------------|---|-----------------|-------------|
| (In thousands)   |                    |                 |                                      |                   |                          |                         |   |                 |             |
| Balances at beginning of period  | \$338,993          | \$73,152        | \$1,873,811                          | \$(2,866)         | \$ 932,853               | \$(1,238,860)           | (\$135)   | \$1,845         | \$1,978,793 |
| Comprehensive income:  |                    |                 |                                      |                   |                          |                         |   |                 |             |
| Net income   |                    |                 |                                      |                   | 92,456                   |                         |   |                 | 92,456      |
| Other comprehensive income:  |                    |                 |                                      |                   |                          |                         |   |                 |             |
| Unrealized gain (loss) on securities   |                    |                 |                                      |                   |                          |                         | (83)  |                 | (83)        |
| Cash flow hedge activity   |                    |                 |                                      |                   |                          |                         | 3,520   |                 | 3,520       |
| Total comprehensive income   |                    |                 |                                      |                   |                          |                         |   |                 | 95,893      |
| Issuance of common shares from dividend reinvestment and stock incentive plans, net of forfeitures |                    | 1,776           | 67,250                               | (1,086)           |                          |                         |   | (116)           | 67,824      |
| Proceeds from issuance of common shares  |                    | 6,325           | 258,969                              |                   |                          |                         |   |                 | 265,294     |
| Compensation expense related to stock options  |                    |                 |                                      |                   |                          |                         |   | 919             | 919         |
| Cash dividends paid:   |                    |                 |                                      |                   |                          |                         |   |                 |             |
| Common stock-\$1.6191 per share  |                    |                 |                                      |                   |                          | (129,088)               |   |                 | (129,088)   |
| Preferred stock, Series D-\$1.4766 per share   |                    |                 |                                      |                   |                          | (5,906)                 |   |                 | (5,906)     |



|  |           |          |             |           |             |               |         |         |             |
|--|-----------|----------|-------------|-----------|-------------|---------------|---------|---------|-------------|
| Preferred stock,<br>Series E-\$1.125<br>per share  |           |          |             |           |             | (84)          |         |         | (84)        |
| Preferred stock,<br>Series F-\$1.4297<br>per share |           |          |             |           |             | (10,008)      |         |         | (10,008)    |
| Preferred stock,<br>Series G-\$1.4064<br>per share |           |          |             |           |             | (2,953)       |         |         | (2,953)     |
| Balances at end<br>of period                       | \$338,993 | \$81,253 | \$2,200,030 | \$(3,952) | \$1,025,309 | \$(1,386,899) | \$3,302 | \$2,648 | \$2,260,684 |

**Nine Months Ended September 30, 2006**

|  | <b>Preferred<br/>Stock</b> | <b>Common<br/>Stock</b> | <b>Capital in<br/>Excess of<br/>Par Value</b> | <b>Treasury<br/>Stock</b> | <b>Cumulative<br/>Net<br/>Income<br/>(In thousands)</b> | <b>Cumulative<br/>Dividends<br/>Income</b> | <b>Accumulated<br/>Other<br/>Comprehensive<br/>Income</b> | <b>Other<br/>Equity</b> | <b>Total</b> |
|--|----------------------------|-------------------------|---|---------------------------|---|--|---|-------------------------|--------------|
| Balances at<br>beginning of<br>period  | \$ 276,875                 | \$ 58,050               | \$ 1,306,471                                  | \$(2,054)                 | \$ 830,103  | \$(1,039,032)                              | \$ 0  | \$ 343                  | \$ 1,430,756 |
| Comprehensive<br>income:   |                            |                         |   |                           |   |  |   |                         |              |
| Net income   |                            |                         |   |                           | 79,791  |  |   |                         | 79,791       |
| Other<br>comprehensive<br>income:  |                            |                         |   |                           |   |  |   |                         | 0            |
| Total<br>comprehensive<br>income   |                            |                         |   |                           |   |  |   |                         | 79,791       |
| Issuance of<br>common shares<br>from dividend<br>reinvestment and<br>stock incentive<br>plans, net of<br>forfeitures |                            | 1,732                   | 57,015  | (660)                     |   |  |   | (18)                    | 58,069       |
| Proceeds from<br>issuance of<br>common shares  |                            | 3,223                   | 106,526                                       |                           |   |  |   |                         | 109,749      |
| SFAS123(R)<br>reclassification   |                            |                         | (521)   |                           |   |  |   | 521                     | 0            |
| Compensation<br>expense related to<br>stock options  |                            |                         |   |                           |   |  |   | 874                     | 874          |

|  |            |           |              |            |            |                |      |          |              |
|--|------------|-----------|--------------|------------|------------|----------------|------|----------|--------------|
| Cash dividends paid:                         |            |           |              |            |            |                |      |          |              |
| Common stock-\$1.90 per share                |            |           |              |            |            | (116,272)      |      |          | (116,272)    |
| Preferred stock, Series D-\$1.4766 per share |            |           |              |            |            | (5,906)        |      |          | (5,906)      |
| Preferred stock, Series E-\$1.125 per share  |            |           |              |            |            | (84)           |      |          | (84)         |
| Preferred stock, Series F-\$1.4297 per share |            |           |              |            |            | (10,008)       |      |          | (10,008)     |
| Balances at end of period                    | \$ 276,875 | \$ 63,005 | \$ 1,469,491 | \$ (2,714) | \$ 909,894 | \$ (1,171,302) | \$ 0 | \$ 1,720 | \$ 1,546,969 |

See notes to unaudited consolidated financial statements

**Table of Contents****CONSOLIDATED STATEMENTS OF CASH FLOWS (UNAUDITED)  
HEALTH CARE REIT, INC. AND SUBSIDIARIES**

|   | <b>Nine Months Ended<br/>September 30,<br/>2007                      2006<br/>(In thousands)</b> |           |
|---|--|-----------|
| <b>Operating activities</b>   |  |           |
| Net income  | \$ 92,456  | \$ 79,791 |
| Adjustments to reconcile net income to net cash provided from operating activities: |  |           |
| Depreciation and amortization   | 109,545  | 71,918    |
| Other amortization expenses   | 4,211  | 2,199     |
| Capitalized interest  | (8,058)  | (2,494)   |
| Provision for loan losses   | 0  | 750       |
| Stock-based compensation expense  | 5,753  | 4,191     |
| Minority interests share of earnings  | 407  | 0         |
| Rental income less than (in excess of) cash received                                | (1,873)  | 9,756     |
| Amortization of above/below market leases   | (656)  | 0         |
| (Gain) loss on sales of properties  | (2,775)  | (2,590)   |
| Increase (decrease) in accrued expenses and other liabilities                       | (2,800)  | 9,853     |
| Decrease (increase) in receivables and other assets                                 | (4,839)  | (14,390)  |
| Net cash provided from (used in) operating activities                               | <b>191,371</b>   | 158,984   |
| <b>Investing activities</b>   |  |           |
| Investment in real property   | (587,681)  | (290,596) |
| Investment in loans receivable  | (121,338)  | (74,126)  |
| Other investments, net of payments  | (2,192)  | (2,100)   |
| Principal collected on loans receivable   | 45,058   | 42,468    |
| Proceeds from sales of properties   | 65,940   | 35,288    |
| Other   | (3,325)  | (738)     |
| Net cash provided from (used in) investing activities                               | <b>(603,538)</b>   | (289,804) |
| <b>Financing activities</b>   |  |           |
| Net increase (decrease) under unsecured lines of credit arrangements                | (80,000)   | 81,000    |
| Proceeds from issuance of senior notes  | 389,166  | 0         |
| Principal payments on senior notes  | (52,500)   | 0         |
| Principal payments on secured debt  | (26,494)   | (2,184)   |
| Net proceeds from the issuance of common stock                                      | 327,419  | 165,808   |
| Decrease (increase) in deferred loan expense  | (4,454)  | (2,281)   |
| Contributions by minority interests   | 2,600  | 0         |
| Distributions to minority interests   | (307)  | 0         |
| Cash distributions to stockholders  | (148,039)  | (132,270) |
| Net cash provided from (used in) financing activities                               | <b>407,391</b>   | 110,073   |
| Increase (decrease) in cash and cash equivalents                                    | (4,776)  | (20,747)  |
| Cash and cash equivalents at beginning of period                                    | 36,216   | 36,237    |

|   |                   |           |
|---|-------------------|-----------|
| Cash and cash equivalents at end of period                      | <b>\$ 31,440</b>  | \$ 15,490 |
| Supplemental cash flow information-interest paid                | <b>\$ 78,530</b>  | \$ 64,549 |
| Supplemental schedule of non-cash activities:                   |                   |           |
| Assets and liabilities assumed from real property acquisitions: |                   |           |
| Secured debt  | <b>\$ 160,001</b> | \$ 25,049 |
| Other liabilities   | <b>11,916</b>     |           |
| Other assets  | <b>3,897</b>      |           |

See notes to unaudited consolidated financial statements

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**Table of Contents****HEALTH CARE REIT, INC.****NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS****NOTE A Basis of Presentation**

The accompanying unaudited consolidated financial statements have been prepared in accordance with U.S. generally accepted accounting principles ( U.S. GAAP ) for interim financial information and with instructions to Quarterly Report on Form 10-Q and Article 10 of Regulation S-X. Accordingly, they do not include all of the information and footnotes required by U.S. GAAP for complete financial statements. In the opinion of management, all adjustments (consisting of normal recurring accruals) considered for a fair presentation have been included. Operating results for the nine months ended September 30, 2007 are not necessarily an indication of the results that may be expected for the year ending December 31, 2007. For further information, refer to the financial statements and footnotes thereto included in our Annual Report on Form 10-K/A for the year ended December 31, 2006.

**NOTE B Windrose Medical Properties Trust Merger**

As discussed in our Annual Report on Form 10-K/A for the year ended December 31, 2006, we completed our merger with Windrose Medical Properties Trust on December 20, 2006. These operations are the principal component of our operating property segment (see Note L). During the nine months ended September 30, 2007, we updated the purchase price allocation for the Windrose merger, as required by Statement of Financial Accounting Standards No. 141, Business Combinations. The updated purchase price allocation reflects reallocations between identifiable tangible and intangible assets. However, these adjustments did not have a significant impact on our consolidated results of operations. Allocation of the purchase price has not been finalized and is subject to adjustment. The following table presents the updated purchase price calculation and the allocation to assets acquired and liabilities assumed, based upon their estimated fair values (in thousands):

|  |            |
|--|------------|
| Common stock   | \$ 396,846 |
| Preferred stock  | 62,118     |
| Cash consideration   | 183,139    |
| Assumed debt   | 301,641    |
| Assumed liabilities and minority interests                 | 21,192     |
| Acquisition costs  | 29,139     |
| <br>   |            |
| Purchase price   | 994,075    |
| Merger-related expenses                                    | 5,213      |
| Capitalized equity issuance costs                          | 912        |
| <br>   |            |
| Net purchase price   | \$ 987,950 |
| <br>   |            |
| Land and land improvements                                 | \$ 126,078 |
| Buildings and improvements                                 | 769,769    |
| Acquired lease intangibles                                 | 42,594     |
| Above market lease intangibles                             | 32,352     |
| Cash and cash equivalents                                  | 15,591     |
| Receivables and other assets                               | 22,547     |
| <br>   |            |
| Total assets acquired                                      | 1,008,931  |
| Below market lease intangibles                             | 20,981     |
| <br>   |            |
| Purchase price   | 987,950    |
| Secured debt   | 249,424    |
| Liability to subsidiary trust issuing preferred securities | 52,217     |

|  |            |
|--|------------|
| Accrued expenses and other liabilities | 18,977     |
| Total liabilities acquired             | 320,618    |
| Minority interests                     | 2,215      |
| Net assets acquired                    | \$ 665,117 |

**NOTE C Real Estate Investments**

During the nine months ended September 30, 2007, we invested \$587,681,000 of cash in real property (including \$180,563,000 of cash advances for construction in progress) and provided cash loan financings of \$121,338,000. Additionally, \$97,609,000 of completed construction projects were placed into service and began earning rent during the nine months ended September 30, 2007. As of September 30, 2007, we had \$593,428,000 of unfunded construction commitments relating to existing construction in progress projects. Also during the nine months ended September 30, 2007, we sold real property generating \$65,940,000 of net cash proceeds and collected \$45,058,000 of cash as repayment of principal on loans receivable.

**Table of Contents****HEALTH CARE REIT, INC.****NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

In May 2007, we completed the acquisition of 17 medical office buildings and Paramount Real Estate Services from affiliates of Rendina Companies for an aggregate purchase price of approximately \$294,473,000. The results of operations for these properties and Paramount have been included in our consolidated results of operations from the date of acquisition. Allocation of the purchase price has not been finalized and is subject to adjustment.

**NOTE D Distributions Paid to Common Stockholders**

On February 20, 2007, we paid a dividend of \$0.2991 per share to stockholders of record on January 31, 2007. This represents a total dividend of \$0.64 per share when combined with the prorated dividend of \$0.3409 per share paid on December 28, 2006 in connection with the Windrose merger. These dividends related to the period from October 1, 2006 through December 31, 2006.

On May 21, 2007, we paid a dividend of \$0.66 per share to stockholders of record on May 4, 2007. These dividends related to the period from January 1, 2007 through March 31, 2007.

On August 20, 2007, we paid a dividend of \$0.66 per share to stockholders of record on August 3, 2007. These dividends related to the period from April 1, 2007 through June 30, 2007.

**NOTE E Fair Value of Derivative Instruments**

We are exposed to various market risks, including the potential loss arising from adverse changes in interest rates. We may elect to use financial derivative instruments to hedge interest rate exposure. These decisions are principally based on our policy to match our variable rate investments with comparable borrowings, but are also based on the general trend in interest rates at the applicable dates and our perception of the future volatility of interest rates. Derivatives are recorded at fair market value on the balance sheet as assets or liabilities.

On May 6, 2004, we entered into two interest rate swap agreements (the 2004 Swaps ) for a total notional amount of \$100,000,000 to hedge changes in fair value attributable to changes in the LIBOR swap rate of \$100,000,000 of fixed rate debt with a maturity date of November 15, 2013. The 2004 Swaps were treated as fair-value hedges for accounting purposes and we utilized the short-cut method to assess effectiveness. The 2004 Swaps were with highly rated counterparties in which we received a fixed rate of 6.0% and paid a variable rate based on six-month LIBOR plus a spread. On September 12, 2007, we terminated the 2004 Swaps and we received a \$2,125,000 cash settlement. The unamortized amount of this settlement at September 30, 2007 was \$2,059,000 and is recorded as an adjustment to the hedged item. This amount will be amortized to interest expense over the life of the hedged debt using the effective interest method. For the three and nine months ended September 30, 2007, we generated \$73,000 and \$23,000 of savings, respectively, related to the 2004 Swaps that was recorded as a reduction of interest expense. For the three and nine months ended September 30, 2006, we incurred \$29,000 and \$100,000 of losses, respectively, related to the 2004 Swaps that was recorded as an addition to interest expense.

On July 2, 2007, we entered into two forward-starting interest rate swaps (the July 2007 Swaps ), with an aggregate notional amount of \$200,000,000 that were designated as cash flow hedges of the variability in forecasted interest payments attributable to changes in the LIBOR swap rate, on long-term fixed rate debt forecasted to be issued in 2007. The July 2007 Swaps have the economic effect of fixing \$200,000,000 of our debt at 4.913% for five years. The July 2007 Swaps were settled on July 17, 2007, which was the day after the forecasted debt was priced. The cash settlement value of these contracts at July 17, 2007, was \$733,000. This amount represented the effective portion of the hedges as there was no hedge ineffectiveness. Therefore, the \$733,000 settlement value was deferred in accumulated other comprehensive income ( AOCI ) and will be amortized to interest expense using the effective interest method. The unamortized amount of AOCI related to these contracts at September 30, 2007 is \$704,000. For the three and nine months ended September 30, 2007, we reclassified \$29,000 out of AOCI as a reduction of interest expense.

On September 12, 2007, we entered into two forward-starting interest rate swaps (the September 2007 Swaps ) for a total notional amount of \$250,000,000 to hedge 10 years of interest payments associated with a long-term borrowing that is expected to occur in 2008. The September 2007 Swaps each have an effective date of September 12, 2008 and a maturity date of September 12, 2018. We expect to settle the September 2007 Swaps when the debt is priced. The September 2007 Swaps have the economic effect of fixing \$250,000,000 of our future debt at 4.469% for 10 years.

The September 2007 Swaps have been designated as cash flow hedges and we expect the September 2007 Swaps to be highly effective at offsetting changes in cash flows of interest payments on \$250,000,000 of our future debt due to changes in the LIBOR swap rate. Therefore, effective changes in the fair value of the September 2007 Swaps will be recorded in AOCI and reclassified to interest expense when the hedged forecasted transactions affect earnings (as interest payments are made on the expected debt issuance). The ineffective portion of the changes in fair value will be recorded directly in earnings. At September 30, 2007, the September 2007 Swaps were reported at their fair value of \$2,684,000 and are included in other assets and AOCI.



**Table of Contents****HEALTH CARE REIT, INC.****NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

The valuation of derivative instruments requires us to make estimates and judgments that affect the fair value of the instruments. Fair values for our derivatives are estimated by a third party consultant, which utilizes pricing models that consider forward yield curves and discount rates. Such amounts and the recognition of such amounts are subject to significant estimates that may change in the future.

**NOTE F Discontinued Operations**

One independent living facility and one assisted living facility were held for sale as of September 30, 2007. We did not recognize an impairment loss on these assets as the fair value less estimated costs to sell exceeded our carrying values. During the nine months ended September 30, 2007, we sold nine assisted living facilities, one skilled nursing facility and one parcel of land with carrying values of \$63,165,000 for a net gain of \$2,775,000. In accordance with Statement of Financial Accounting Standards No. 144, Accounting for the Impairment or Disposal of Long-Lived Assets, we have reclassified the income and expenses attributable to all properties sold and attributable to the properties held for sale at September 30, 2007 to discontinued operations. Expenses include an allocation of interest expense based on property carrying values and our weighted average cost of debt. The following illustrates the reclassification impact of Statement No. 144 as a result of classifying properties as discontinued operations for the periods presented (in thousands):

|   | <b>Three Months Ended</b> |             | <b>Nine Months Ended</b> |             |
|---|---------------------------|-------------|--------------------------|-------------|
|   | <b>September 30,</b>      |             | <b>September 30,</b>     |             |
|   | <b>2007</b>               | <b>2006</b> | <b>2007</b>              | <b>2006</b> |
| Revenues:                                       |                           |             |                          |             |
| Rental income                                   | <b>\$ 900</b>             | \$ 2,976    | <b>\$ 4,387</b>          | \$ 9,924    |
| Expenses:                                       |                           |             |                          |             |
| Interest expense                                | <b>213</b>                | 984         | <b>1,138</b>             | 3,117       |
| Provision for depreciation                      | <b>204</b>                | 1,579       | <b>1,111</b>             | 5,078       |
| General and administrative                      | <b>0</b>                  | 212         | <b>0</b>                 | 729         |
| Income (loss) from discontinued operations, net | <b>\$ 483</b>             | \$ 201      | <b>\$ 2,138</b>          | \$ 1,000    |

**NOTE G Contingent Liabilities**

We have an outstanding letter of credit issued for the benefit of certain insurance companies that provide workers compensation insurance to one of our tenants. Our obligation under the letter of credit matures in 2009. At September 30, 2007, our obligation under the letter of credit was \$2,450,000.

As of September 30, 2007, we had \$593,428,000 of unfunded construction commitments.

**NOTE H Accumulated Other Comprehensive Income**

Accumulated other comprehensive income includes amounts related to our cash flow hedge activity, unrealized gains or losses on our equity investments and unrecognized actuarial gains/losses from the adoption of Financial Accounting Standards No. 158, Employers Accounting for Defined Benefit Pension and Other Postretirement Plans An amendment of FASB Statements No. 87, 88, 106 and 132(R) on December 31, 2006. These items are included as a component of stockholders' equity. We did not recognize any comprehensive income related to unrecognized actuarial gains/losses for the nine months ended September 30, 2007. Please see Note E for a discussion of our cash flow hedge activity. We did not recognize any comprehensive income other than the recorded net income for the nine months ended September 30, 2006.

Table of Contents**HEALTH CARE REIT, INC.****NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS (Continued)****NOTE I Earnings Per Share**

The following table sets forth the computation of basic and diluted earnings per share (in thousands, except per share data):

|  | <b>Three Months Ended<br/>September 30,</b> |           | <b>Nine Months Ended<br/>September 30,</b> |           |
|--|---|-----------|--|-----------|
|  | <b>2007</b>                                 | 2006      | <b>2007</b>                                | 2006      |
| Numerator for basic and diluted earnings per share net income available to common stockholders | <b>\$ 24,529</b>                            | \$ 21,480 | <b>\$ 73,504</b>                           | \$ 63,793 |
| Denominator for basic earnings per share weighted average shares                               | <b>80,710</b>                               | 62,524    | <b>77,686</b>                              | 60,766    |
| Effect of dilutive securities:   |   |           |  |           |
| Employee stock options   | <b>55</b>                                   | 81        | <b>150</b>                                 | 75        |
| Non-vested restricted shares   | <b>398</b>                                  | 261       | <b>398</b>                                 | 261       |
| Dilutive potential common shares   | <b>453</b>                                  | 342       | <b>548</b>                                 | 336       |
| Denominator for diluted earnings per share adjusted weighted average shares                    | <b>81,163</b>                               | 62,866    | <b>78,234</b>                              | 61,102    |
| Basic earnings per share   | <b>\$ 0.30</b>                              | \$ 0.34   | <b>\$ 0.95</b>                             | \$ 1.05   |
| Diluted earnings per share   | <b>\$ 0.30</b>                              | \$ 0.34   | <b>\$ 0.94</b>                             | \$ 1.04   |

The diluted earnings per share calculation excludes the dilutive effect of 124,000 stock options for both the three and nine months ended September 30, 2007 because the exercise prices were greater than the average market price. The diluted earnings per share calculation excludes the dilutive effect of 0 and 112,000 stock options for the three and nine months ended September 30, 2006, respectively, because the exercise prices were greater than the average market price. The Series E Cumulative Convertible and Redeemable Preferred Stock, the Series G Cumulative Convertible Preferred Stock, the \$345,000,000 senior unsecured convertible notes due December 2026 and the \$400,000,000 senior unsecured convertible notes due July 2027 were not included in these calculations as the effect of the conversions into common stock was anti-dilutive for the relevant periods presented.

**NOTE J Other Equity**

Other equity consists of accumulated option compensation expense which represents the amount of amortized compensation costs related to stock options awarded to employees and directors subsequent to January 1, 2003. Expense, which is recognized as the options vest based on the market value at the date of the award, totaled \$188,000 and \$919,000 for the three and nine months ended September 30, 2007, respectively, and \$191,000 and \$874,000 for the same periods in 2006.

**NOTE K Stock Incentive Plans**

Our 2005 Long-Term Incentive Plan authorizes up to 2,200,000 shares of common stock to be issued at the discretion of the Compensation Committee of the Board of Directors. The 2005 Plan replaced the 1995 Stock Incentive Plan and the Stock Plan for Non-Employee Directors. The options granted to officers and key employees under the 1995 Plan continue to vest through 2010 and expire ten years from the date of grant. Our non-employee

directors, officers and key employees are eligible to participate in the 2005 Plan. The 2005 Plan allows for the issuance of, among other things, stock options, restricted stock, deferred stock units and dividend equivalent rights. Vesting periods for options, deferred stock units and restricted shares generally range from three years for non-employee directors to five years for officers and key employees. Options expire ten years from the date of grant.

**Table of Contents****HEALTH CARE REIT, INC.****NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS (Continued)****Valuation Assumptions**

The fair value of each option grant is estimated on the date of grant using the Black-Scholes-Merton option pricing model with the following weighted-average assumptions:

|                                 | <b>Nine Months<br/>Ended<br/>September 30,<br/>2007</b> | <b>Nine Months<br/>Ended<br/>September 30,<br/>2006</b> |
|---------------------------------|---|---|
| Dividend yield (1)              | <b>5.60%</b>  | 6.79%   |
| Expected volatility             | <b>19.9%</b>  | 20.3%   |
| Risk-free interest rate         | <b>4.74%</b>  | 4.35%   |
| Expected life (in years)        | <b>5</b>  | 5   |
| Weighted-average fair value (1) | <b>\$ 8.31</b>  | \$ 5.26   |

(1) Certain options granted to employees include dividend equivalent rights ( DERs ). The fair value of options with DERs also includes the net present value of projected future dividend payments over the expected life of the option discounted at the dividend yield rate.

The dividend yield represented the dividend yield of our common stock on the dates of grant. Our computation of expected volatility was based on historical volatility. The risk-free interest rates used were the 10-year U.S. Treasury Notes yield on the dates of grant. The expected life was based on historical experience of similar awards, giving consideration to the contractual terms, vesting schedules and expectations regarding future employee behavior.

**Option Award Activity**

The following table summarizes information about stock option activity for the nine months ended September 30, 2007:

|                      | <b>Number<br/>of<br/>Shares</b> | <b>Weighted<br/>Average<br/>Exercise<br/>Price</b> | <b>Weighted<br/>Average<br/>Remaining<br/>Contract Life</b> | <b>Aggregate<br/>Intrinsic<br/>Value</b> |
|----------------------|---------------------------------|--|---|--|
| <b>Stock Options</b> | <b>(000 s)</b>                  |  | <b>(years)</b>  | <b>(\$000 s)</b>                         |

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|  |       |    |       |     |          |
|--|-------|----|-------|-----|----------|
| Options at beginning of year                                     | 917   | \$ | 30.79 | 7.9 |          |
| Options granted  | 124   |    | 45.73 |     |          |
| Options exercised  | (372) |    | 28.04 |     |          |
| Options terminated   | (2)   |    | 39.72 |     |          |
| Options at end of period   | 667   | \$ | 35.08 | 7.8 | \$ 5,883 |
| Options exercisable at end of period                             | 285   | \$ | 31.52 | 6.9 | \$ 3,531 |
| Weighted average fair value of options granted during the period |       | \$ | 8.31  |     |          |

The aggregate intrinsic value is calculated as the difference between the exercise price of the underlying options and the quoted price of our common stock for the options that were in-the-money at September 30, 2007. During the nine months ended September 30, 2007, the aggregate intrinsic value of options exercised under our stock incentive plans was \$6,014,000 determined as of the date of option exercise. During the nine months ended September 30, 2006, the aggregate intrinsic value of options exercised under our stock incentive plans was \$3,025,000 determined as of the date of option exercise. Cash received from option exercises under our stock incentive plans for the nine months ended September 30, 2007 was \$10,429,000. Cash received from option exercises under our stock incentive plans for the nine months ended September 30, 2006 was \$4,601,000.

As of September 30, 2007, there was approximately \$2,712,000 of total unrecognized compensation cost related to unvested stock options granted under our stock incentive plans. That cost is expected to be recognized over a weighted average period of four years. As of September 30, 2007, there was approximately \$12,141,000 of total unrecognized compensation cost related to unvested restricted stock granted under our stock incentive plans. That cost is expected to be recognized over a weighted average period of three years.

**Table of Contents****HEALTH CARE REIT, INC.****NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

The following table summarizes information about non-vested stock incentive awards as of September 30, 2007 and changes for the nine months ended September 30, 2007:

|                                  | Stock Options            |  | Restricted Stock         |  |
|----------------------------------|--------------------------|--|--------------------------|--|
|                                  | Number of Shares (000 s) | Weighted Average Grant Date Fair Value | Number of Shares (000 s) | Weighted Average Grant Date Fair Value |
| Non-vested at December 31, 2006  | 478                      | \$ 5.35                                | 248                      | \$ 34.07                               |
| Vested                           | (218)                    | 3.78                                   | (121)                    | 35.21                                  |
| Granted                          | 124                      | 8.31                                   | 272                      | 44.66                                  |
| Terminated                       | (2)                      | 7.63                                   | (1)                      | 39.36                                  |
| Non-vested at September 30, 2007 | 382                      | \$ 7.20                                | 398                      | \$ 40.94                               |

**NOTE L Segment Reporting**

We invest across the full spectrum of senior housing and health care real estate. We evaluate our business and make resource allocations on our two business segments investment properties and operating properties. Under the investment property segment, we invest in senior housing and health care real estate through acquisition and financing of primarily single tenant properties. Properties acquired are primarily leased under triple-net leases and we are not involved in the management of the property. Our primary investment property types include skilled nursing facilities, assisted living facilities, independent living/continuing care retirement communities and specialty care facilities. Under the operating property segment, we primarily invest in medical office buildings that are typically leased under gross leases, modified gross leases or triple-net leases, to multiple tenants, and generally require a certain level of property management. The accounting policies of the segments are the same as those described in the summary of significant accounting policies (see Note 1 to our Annual Report on Form 10-K/A for the year ended December 31, 2006). There are no intersegment sales or transfers. We evaluate performance based upon net operating income of the combined properties in each segment.

Non-segment revenue consists mainly of interest income on non-real estate investments and other income. Non-segment assets consist of corporate assets including cash, accounts receivable and deferred financing costs among others. Non-property specific revenues and expenses are not allocated to individual segments in determining net operating income.

Summary information for the reportable segments during the three and nine months ended September 30, 2007 and 2006 is as follows (in thousands):

|  | Rental Income | Interest Income | Other Income | Total Revenues | Property Operating Expenses | Net Operating Income | Real Estate Depreciation/Amortization | Interest Expense | Total Assets |
|--|---------------|-----------------|--------------|----------------|-----------------------------|----------------------|---------------------------------------|------------------|--------------|
|  | (1)           | (1)             | (1)          | (1)            | (1)                         | (2)                  | (1)                                   | (1)              | (1)          |
| Three months ended September 30, 2007: |               |                 |              |                |                             |                      |                                       |                  |              |
| Investment Properties                  | \$ 86,036     | \$ 5,947        |              | \$ 91,983      |                             | \$ 91,983            | \$ 25,668                             | \$ 2,125         | \$ 3,478,316 |
| Operating Properties                   | 32,794        |                 |              | 32,794         | \$ 10,426                   | 22,368               | 14,469                                | 5,760            | 1,307,945    |
| Non-segment/Corporate                  |               |                 | \$ 1,199     | 1,199          |                             | 1,199                |                                       | 27,197           | 185,566      |
|  | \$ 118,830    | \$ 5,947        | \$ 1,199     | \$ 125,976     | \$ 10,426                   | \$ 115,550           | \$ 40,137                             | \$ 35,082        | \$ 4,971,827 |

Three months ended  
September 30, 2006:

|   |           |          |          |           |      |           |           |           |              |
|---|-----------|----------|----------|-----------|------|-----------|-----------|-----------|--------------|
| Investment Properties                         | \$ 76,304 | \$ 4,436 |          | \$ 80,740 |      | \$ 80,740 | \$ 24,526 | \$ 2,357  | \$ 3,094,828 |
| Operating Properties<br>Non-segment/Corporate |           |          | \$ 1,019 | 1,019     |      | 1,019     |           | 21,917    | 106,001      |
|   | \$ 76,304 | \$ 4,436 | \$ 1,019 | \$ 81,759 | \$ 0 | \$ 81,759 | \$ 24,526 | \$ 24,274 | \$ 3,200,829 |

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**HEALTH CARE REIT, INC.**  
**NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

|  | <b>Rental<br/>Income<br/>(1)</b> | <b>Interest<br/>Income</b> | <b>Other<br/>Income</b> | <b>Total<br/>Revenues<br/>(1)</b> | <b>Property<br/>Operating<br/>Expenses</b> | <b>Net<br/>Operating<br/>Income<br/>(2)</b> | <b>Real<br/>Estate<br/>Depreciation/<br/>Amortization<br/>(1)</b> | <b>Interest<br/>Expense<br/>(1)</b> | <b>Total<br/>Assets</b> |
|--|----------------------------------|----------------------------|-------------------------|-----------------------------------|--|---|---|-------------------------------------|-------------------------|
| Nine months ended<br>September 30, 2007: |                                  |                            |                         |                                   |  |   |   |                                     |                         |
| Investment Properties                    | \$ 250,712                       | \$ 17,673                  |                         | \$ 268,385                        |  | \$ 268,385                                  | \$ 75,104   | \$ 6,747                            | \$ 3,478,316            |
| Operating Properties                     | 86,582                           |                            |                         | 86,582                            | \$ 26,251                                  | 60,331                                      | 34,441  | 13,852                              | 1,307,945               |
| Non-segment/Corporate                    |                                  |                            | \$ 3,935                | 3,935                             |  | 3,935                                       |   | 80,109                              | 185,566                 |
|  | \$ 337,294                       | \$ 17,673                  | \$ 3,935                | \$ 358,902                        | \$ 26,251                                  | \$ 332,651                                  | \$ 109,545  | \$ 100,708                          | \$ 4,971,827            |
| Nine months ended<br>September 30, 2006: |                                  |                            |                         |                                   |  |   |   |                                     |                         |
| Investment Properties                    | \$ 223,956                       | \$ 13,178                  |                         | \$ 237,134                        |  | \$ 237,134                                  | \$ 71,917   | \$ 6,704                            | \$ 3,094,828            |
| Operating Properties                     |                                  |                            |                         |                                   |  |   |   |                                     |                         |
| Non-segment/Corporate                    |                                  |                            | \$ 3,049                | 3,049                             |  | 3,049                                       |   | 64,895                              | 106,001                 |
|  | \$ 223,956                       | \$ 13,178                  | \$ 3,049                | \$ 240,183                        | \$ 0                                       | \$ 240,183                                  | \$ 71,917   | \$ 71,599                           | \$ 3,200,829            |

- (1) Includes amounts from discontinued operations.
- (2) Net operating income ( NOI ) is used to evaluate the operating performance of our properties. We define NOI as total revenues, including tenant reimbursements, less property level operating expenses, which exclude depreciation and amortization, general and administrative



expenses,  
impairments,  
interest expense  
and discontinued  
operations. We  
believe NOI  
provides  
investors  
relevant and  
useful  
information  
because it  
measures the  
operating  
performance of  
our properties at  
the property  
level on an  
unleveraged  
basis. We use  
NOI to make  
decisions about  
resource  
allocations and  
to assess the  
property level  
performance of  
our properties.

**NOTE M New Accounting Pronouncements**

On January 1, 2007, we adopted Financial Accounting Standards Board ( FASB ) Interpretation No. 48, Accounting for Uncertainty in Income Taxes. The Interpretation clarifies the accounting for uncertainty in income taxes recognized in an enterprise's financial statements in accordance with Statement of Financial Accounting Standards No. 109, Accounting for Income Taxes. The Interpretation prescribes guidance for recognizing, measuring, reporting and disclosing a tax position taken or expected to be taken in a tax return. The adoption of the Interpretation did not have a material impact on our financial position or results of operations.

In September 2006, the FASB also issued Statement of Financial Accounting Standards No. 157, Fair Value Measurements ( SFAS 157 ), which defines fair value, establishes a framework for measuring fair value in generally accepted accounting principles, and expands disclosures about fair value measurements. SFAS 157 will be effective for fiscal year 2008. Adoption of SFAS 157 is not expected to have a material impact on our financial position, although additional disclosures may be required.

In February 2007, the FASB issued Statement of Financial Accounting Standards No. 159, The Fair Value Option for Financial Assets and Financial Liabilities ( SFAS 159 ), which permits companies to elect to measure certain eligible items at fair value. Subsequent unrealized gains and losses on those items will be reported in earnings. Upfront costs and fees related to those items will be reported in earnings as incurred and not deferred. SFAS 159 will be effective for fiscal year 2008. If a company elects to apply the provisions of SFAS 159 to eligible items existing at that date, the effect of the remeasurement to fair value will be reported as a cumulative effect adjustment to the opening balance of retained earnings. Retrospective application will not be permitted. We are currently assessing whether we will elect to use the fair value option for any eligible items.

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**HEALTH CARE REIT, INC.**

**NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

**NOTE N Subsequent Events**

At September 30, 2007, we had a \$52,184,000 liability to a subsidiary trust that had issued trust preferred securities, which liability was assumed in the Windrose merger. On March 24, 2006, Windrose's wholly-owned subsidiary, Windrose Capital Trust I (the Trust), completed the issuance and sale in a private placement of \$50,000,000 in aggregate principal amount of fixed/floating rate preferred securities. The trust preferred securities are scheduled to mature on March 30, 2036, are redeemable at our option beginning March 30, 2011, and require quarterly distributions to the holders of the trust preferred securities. Distributions on the trust preferred securities accumulate at a fixed rate per annum equal to 7.22% through March 30, 2011, and a variable rate per annum equal to LIBOR plus 2.05% thereafter.

The common stock of the Trust was purchased by an operating partnership of Windrose for \$1,000,000. The Trust used the proceeds from the sale of the trust preferred securities together with the proceeds from the sale of the common stock to purchase \$51,000,000 in aggregate principal amount of unsecured fixed/floating junior subordinated notes due March 30, 2036 issued by the operating partnership. The operating partnership received approximately \$49,000,000 in net proceeds, after the payment of fees and expenses, from the sale of the junior subordinated notes to the Trust. In accordance with FASB Interpretation No. 46(R), Consolidation of Variable Interest Entities, we have not consolidated the Trust because the operating partnership is not considered the primary beneficiary of the Trust.

On November 6, 2007, we purchased all \$50,000,000 of the outstanding trust preferred securities at par for the purpose of unwinding this financing arrangement and extinguishing the liability of the operating partnership to the Trust.

**NOTE O Convertible Notes Issuance**

On July 20, 2007, we completed the issuance of \$400,000,000 4.75% convertible senior unsecured notes due July 15, 2027. We generated net proceeds of approximately \$389,166,000.

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

The following discussion and analysis is based primarily on the consolidated financial statements of Health Care REIT, Inc. for the periods presented and should be read together with the notes thereto contained in this Quarterly Report on Form 10-Q. Other important factors are identified in our Annual Report on Form 10-K/A for the year ended December 31, 2006, including factors identified under the headings Business, Risk Factors and Management's Discussion and Analysis of Financial Condition and Results of Operations.

**Executive Overview****Business**

Health Care REIT, Inc. is an equity real estate investment trust that invests in the full spectrum of senior housing and health care real estate. Founded in 1970, we were the first REIT to invest exclusively in health care facilities. The following table summarizes our portfolio as of September 30, 2007:

| Type of Property           | Investments(1)<br>(in thousands) | Percentage<br>of<br>Revenues(2) | Investments<br>(in thousands) | Percentage<br>of<br>Revenues(2) | Number #<br>of Beds/Units<br>or<br>Sq.<br>Ft. | Investment<br>per<br>metric<br>(3) | Operators/<br>Tenants | States |
|----------------------------|----------------------------------|---------------------------------|-------------------------------|---------------------------------|---|------------------------------------|-----------------------|--------|
| Independent living/CCRCs   | \$ 678,145                       | 14%                             | \$ 33,060                     | 9%                              | 57 6,615 units                                | \$154,493 per unit                 | 22                    | 22     |
| Assisted living facilities | 1,002,599                        | 21%                             | 86,314                        | 24%                             | 201 12,052 units                              | \$93,352 per unit                  | 25                    | 33     |
| Skilled nursing facilities | 1,544,271                        | 32%                             | 118,007                       | 33%                             | 234 31,680 beds                               | \$49,177 per bed                   | 22                    | 28     |
| Medical office buildings   | 1,233,327                        | 26%                             | 81,332                        | 23%                             | 14,837,991 sq. ft.                            | 270 per sq. ft.                    | 874                   | 17     |
| Specialty care facilities  | 337,775                          | 7%                              | 18,581                        | 5%                              | 22 1,541 beds                                 | \$245,289 per bed                  | 11                    | 10     |
| Interest income            |                                  |                                 | 17,673                        | 5%                              |   |                                    |                       |        |
| Other income               |                                  |                                 | 3,935                         | 1%                              |   |                                    |                       |        |
| Totals                     | \$ 4,796,117                     | 100%                            | \$ 358,902                    | 100%                            | 631   |                                    |                       |        |

(1) Investments include gross real estate investments and credit enhancements which amounted to \$4,793,667,000 and \$2,450,000, respectively.

(2) Revenues include gross revenues and revenues from

discontinued  
operations for  
the nine months  
ended  
September 30,  
2007.

- (3) Investment per  
metric was  
computed by  
using the total  
investment  
amount of  
\$5,389,545,000,  
which includes  
gross real estate  
investments,  
credit  
enhancements  
and unfunded  
construction  
commitments  
for which initial  
funding has  
commenced  
which amounted  
to  
\$4,793,667,000,  
\$2,450,000 and  
\$593,428,000,  
respectively.

Our primary objectives are to protect stockholder capital and enhance stockholder value. We seek to pay consistent cash dividends to stockholders and create opportunities to increase dividend payments to stockholders as a result of annual increases in rental and interest income and portfolio growth. To meet these objectives, we invest across the full spectrum of senior housing and health care real estate and diversify our investment portfolio by property type, operator/tenant and geographic location.

Substantially all of our revenues and sources of cash flows from operations are derived from operating lease rentals and interest earned on outstanding loans receivable. These items represent our primary source of liquidity to fund distributions and are dependent upon our obligors' continued ability to make contractual rent and interest payments to us. To the extent that our obligors experience operating difficulties and are unable to generate sufficient cash to make payments to us, there could be a material adverse impact on our consolidated results of operations, liquidity and/or financial condition. To mitigate this risk, we monitor our investments through a variety of methods determined by the type of property and operator/tenant. Our asset management process includes review of monthly financial statements for each property, periodic review of obligor credit, periodic property inspections and review of covenant compliance relating to licensure, real estate taxes, letters of credit and other collateral. In monitoring our portfolio, our personnel use a proprietary database to collect and analyze property-specific data. Additionally, we conduct extensive research to ascertain industry trends and risks. Through these asset management and research efforts, we are typically able to intervene at an early stage to address payment risk, and in so doing, support both the collectibility of revenue and the value of our investment.

In addition to our asset management and research efforts, we also structure our investments to help mitigate payment risk. We typically limit our investments to no more than 90% of the appraised value of a property. Operating

leases and loans are normally credit enhanced by guaranties and/or letters of credit. In addition, operating leases are typically structured as master leases and loans are generally cross-defaulted and cross-collateralized with other loans, operating leases or agreements between us and the obligor and its affiliates.

For the nine months ended September 30, 2007, rental income and interest income represented 94% and 5%, respectively, of total gross revenues (including revenues from discontinued operations). Substantially all of our operating leases are designed with either fixed or contingent escalating rent structures. Leases with fixed annual rental escalators are generally recognized on a straight-line basis over the

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initial lease period, subject to a collectibility assessment. Rental income related to leases with contingent rental escalators is generally recorded based on the contractual cash rental payments due for the period. Our yield on loans receivable depends upon a number of factors, including the stated interest rate, the average principal amount outstanding during the term of the loan and any interest rate adjustments.

Depending upon the availability and cost of external capital, we anticipate investing in additional properties. New investments are generally funded from temporary borrowings under our unsecured line of credit arrangement, internally generated cash and the proceeds from sales of real property. Our investments generate internal cash from rent and interest receipts and principal payments on loans receivable. Permanent financing for future investments, which replaces funds drawn under the unsecured lines of credit arrangements, is expected to be provided through a combination of public and private offerings of debt and equity securities and the incurrence or assumption of secured debt. We believe our liquidity and various sources of available capital are sufficient to fund operations, meet debt service obligations (both principal and interest), make dividend distributions and finance future investments.

Depending upon market conditions, we believe that new investments will be available in the future with spreads over our cost of capital that will generate appropriate returns to our stockholders. During the nine months ended September 30, 2007, we completed \$891,806,000 of gross new investments and had \$101,260,000 of investment payoffs, resulting in net investments of \$790,546,000. We expect to complete gross new investments of \$1.1 billion to \$1.2 billion during 2007, including acquisitions of approximately \$850,000,000 to \$950,000,000 and funded new development of approximately \$250,000,000. We anticipate the sale of real property and the repayment of loans receivable totaling approximately \$100,000,000 to \$150,000,000 resulting in net new investments of \$950,000,000 to \$1.1 billion during 2007. It is possible that additional loan repayments or sales of real property may occur in the future. To the extent that loan repayments and real property sales exceed new investments, our revenues and cash flows from operations could be adversely affected. We expect to reinvest the proceeds from any loan repayments and real property sales in new investments. To the extent that new investment requirements exceed our available cash on hand, we expect to borrow under our unsecured lines of credit arrangements. At September 30, 2007, we had \$31,440,000 of cash and cash equivalents and \$1,005,000,000 of available borrowing capacity under our unsecured line of credit arrangement.

***Windrose Medical Properties Trust Merger***

As discussed in our Annual Report on Form 10-K/A for the year ended December 31, 2006, we completed our merger with Windrose Medical Properties Trust on December 20, 2006. These operations are the principal component of our operating property segment (see Note L to our unaudited consolidated financial statements). The results of operations for this segment represent the primary change in our consolidated results of operations from the prior year. Allocation of the purchase price has not been finalized and is subject to adjustment.

***Rendina/Paramount Acquisition***

In May 2007, we completed the acquisition of 17 medical office buildings and Paramount Real Estate Services from affiliates of Rendina Companies for an aggregate purchase price of approximately \$294,473,000. The results of operations for these properties and Paramount have been included in our consolidated results of operations from the date of acquisition. Allocation of the purchase price has not been finalized and is subject to adjustment.

***Key Transactions in 2007***

We have completed the following key transactions to date in 2007:

our Board of Directors increased our quarterly dividend to \$0.66 per share, which represents a two cent increase from the quarterly dividend of \$0.64 paid for 2006. The dividend declared for the quarter ended September 30, 2007 represents the 146<sup>th</sup> consecutive dividend payment;

we completed \$891,806,000 of gross investments and had \$101,260,000 of investment payoffs during the nine months ended September 30, 2007;

we completed a public offering of 6,325,000 shares of common stock with net proceeds to the company of approximately \$265,294,000 in April 2007;

we issued \$400,000,000 of 4.75% convertible senior unsecured notes due July 2027 with net proceeds to the company of approximately \$389,166,000 in July 2007; and

we closed on a \$1,150,000,000 unsecured revolving credit facility in August 2007 to replace our \$700,000,000 facility which was scheduled to mature in July 2009 and our \$40,000,000 facility which was scheduled to mature in May 2008. Among other things, the new facility provides us with additional financial flexibility and borrowing capacity, extends our agreement to August 2011 and reduces our incremental borrowing cost from 80 basis points to 60 basis points over LIBOR based on our then current ratings.

**Table of Contents****Key Performance Indicators, Trends and Uncertainties**

We utilize several key performance indicators to evaluate the various aspects of our business. These indicators are discussed below and relate to operating performance, concentration risk and credit strength. Management uses these key performance indicators to facilitate internal and external comparisons to our historical operating results, in making operating decisions and for budget planning purposes.

*Operating Performance.* We believe that net income available to common stockholders ( NICS ) is the most appropriate earnings measure. Other useful supplemental measures of our operating performance include funds from operations ( FFO ) and funds available for distribution ( FAD ); however, these supplemental measures are not defined by U.S. generally accepted accounting principles ( U.S. GAAP ). Please refer to the section entitled Non-GAAP Financial Measures for further discussion of FFO and FAD and for reconciliations of FFO and FAD to NICS. These earnings measures and their relative per share amounts are widely used by investors and analysts in the valuation, comparison and investment recommendations of companies. The following table reflects the recent historical trends of our operating performance measures for the periods presented (in thousands, except per share data):

|   | Three Months Ended |                  |                          |                         |                   |                  |                          |
|---|--------------------|------------------|--------------------------|-------------------------|-------------------|------------------|--------------------------|
|   | March 31,<br>2006  | June 30,<br>2006 | September<br>30,<br>2006 | December<br>31,<br>2006 | March 31,<br>2007 | June 30,<br>2007 | September<br>30,<br>2007 |
| Net income<br>(loss) available to<br>common<br>stockholders | \$ 19,645          | \$ 22,668        | \$ 21,480                | \$ 17,494               | \$ 23,356         | \$ 25,620        | \$ 24,529                |
| Funds from<br>operations                                    | 41,354             | 45,870           | 45,898                   | 44,459                  | 56,207            | 59,979           | 63,830                   |
| Funds available for<br>distribution                         | 49,975             | 47,071           | 48,032                   | 46,809                  | 53,825            | 59,016           | 66,379                   |
| Per share data (fully<br>diluted):                          |                    |                  |                          |                         |                   |                  |                          |
| Net income<br>(loss) available to<br>common<br>stockholders | \$ 0.34            | \$ 0.37          | \$ 0.34                  | \$ 0.27                 | \$ 0.32           | \$ 0.32          | \$ 0.30                  |
| Funds from<br>operations                                    | 0.71               | 0.74             | 0.73                     | 0.69                    | 0.76              | 0.75             | 0.79                     |
| Funds available for<br>distribution                         | 0.85               | 0.76             | 0.76                     | 0.72                    | 0.73              | 0.74             | 0.82                     |

*Credit Strength.* We measure our credit strength both in terms of leverage ratios and coverage ratios. Our leverage ratios include debt to book capitalization and debt to market capitalization. The leverage ratios indicate how much of our balance sheet capitalization is related to long-term debt. The coverage ratios indicate our ability to service interest and fixed charges (interest, secured debt principal amortization and preferred dividends). We expect to maintain capitalization ratios and coverage ratios sufficient to maintain investment grade ratings with Moody's Investors Service, Standard & Poor's Ratings Services and Fitch Ratings. The coverage ratios are based on earnings before interest, taxes, depreciation and amortization ( EBITDA ) which is discussed in further detail, and reconciled to net income, below in Non-GAAP Financial Measures. Leverage ratios and coverage ratios are widely used by investors, analysts and rating agencies in the valuation, comparison, investment recommendations and rating of companies. The following table reflects the recent historical trends for our credit strength measures for the periods presented:



## Three Months Ended

|                                     | March<br>31,<br>2006 | June 30,<br>2006 | September<br>30,<br>2006 | December<br>31,<br>2006 | March<br>31,<br>2007 | June 30,<br>2007 | September<br>30,<br>2007 |
|-------------------------------------|----------------------|------------------|--------------------------|-------------------------|----------------------|------------------|--------------------------|
| Debt to book capitalization ratio   | 52%                  | 49%              | 51%                      | 53%                     | 54%                  | 52%              | 53%                      |
| Debt to market capitalization ratio | 38%                  | 37%              | 36%                      | 39%                     | 40%                  | 41%              | 40%                      |
| Interest coverage ratio             | 2.99x                | 3.16x            | 2.98x                    | 2.75x                   | 2.82x                | 2.83x            | 2.81x                    |
| Fixed charge coverage ratio         | 2.41x                | 2.52x            | 2.41x                    | 2.23x                   | 2.28x                | 2.30x            | 2.31x                    |

*Concentration Risk.* We evaluate our concentration risk in terms of asset mix, investment mix, customer mix and geographic mix. Concentration risk is a valuable measure in understanding what portion of our investments could be at risk if certain sectors were to experience downturns. Asset mix measures the portion of our investments that are real property. In order to qualify as an equity REIT, at least 75% of our real estate investments must be real property whereby each property, which includes the land, buildings, improvements, intangibles and related rights, is owned by us and leased to a tenant pursuant to a long-term operating lease. Investment mix measures the portion of our investments that relate to our various property types. Customer mix measures the portion of our investments that relate to our top five customers. Geographic mix measures the portion of our investments that relate to our top five states. The following table reflects our recent historical trends of concentration risk for the periods presented:

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|                                    | March<br>31,<br>2006 | June 30,<br>2006 | September<br>30,<br>2006 | December<br>31,<br>2006 | March<br>31,<br>2007 | June 30,<br>2007 | September<br>30,<br>2007 |
|------------------------------------|----------------------|------------------|--------------------------|-------------------------|----------------------|------------------|--------------------------|
| Asset mix:                         |                      |                  |                          |                         |                      |                  |                          |
| Real property                      | 94%                  | 94%              | 93%                      | 95%                     | 94%                  | 95%              | 94%                      |
| Loans receivable                   | 6%                   | 6%               | 7%                       | 5%                      | 6%                   | 5%               | 6%                       |
| Investment mix:                    |                      |                  |                          |                         |                      |                  |                          |
| Independent living/CCRCs           | 15%                  | 15%              | 16%                      | 13%                     | 13%                  | 13%              | 14%                      |
| Assisted living facilities         | 33%                  | 33%              | 32%                      | 25%                     | 24%                  | 22%              | 21%                      |
| Skilled nursing facilities         | 45%                  | 45%              | 46%                      | 34%                     | 36%                  | 33%              | 32%                      |
| Medical office buildings           |                      |                  |                          | 22%                     | 21%                  | 26%              | 26%                      |
| Specialty care facilities          | 7%                   | 7%               | 6%                       | 6%                      | 6%                   | 6%               | 7%                       |
| Customer mix:                      |                      |                  |                          |                         |                      |                  |                          |
| Emeritus Corporation               | 12%                  | 12%              | 11%                      | 9%                      | 8%                   | 8%               | 7%                       |
| Brookdale Senior Living Inc.       | 10%                  | 10%              | 9%                       | 7%                      | 7%                   | 6%               | 5%                       |
| Life Care Centers of America, Inc. | 7%                   | 8%               | 7%                       | 6%                      | 6%                   | 5%               | 5%                       |
| Home Quality Management, Inc.      |                      |                  | 8%                       | 6%                      | 6%                   | 5%               | 5%                       |
| Merrill Gardens L.L.C.             | 7%                   | 7%               | 6%                       | 4%                      | 4%                   | 4%               | 4%                       |
| Tara Cares, LLC                    |                      | 6%               |                          |                         |                      |                  |                          |
| Delta Health Group, Inc.           | 6%                   |                  |                          |                         |                      |                  |                          |
| Remaining operators/tenants        | 58%                  | 57%              | 59%                      | 68%                     | 69%                  | 72%              | 74%                      |
| Geographic mix:                    |                      |                  |                          |                         |                      |                  |                          |
| Florida                            | 14%                  | 14%              | 15%                      | 17%                     | 16%                  | 16%              | 16%                      |
| Texas                              | 8%                   | 8%               | 8%                       | 11%                     | 13%                  | 13%              | 13%                      |
| Massachusetts                      | 12%                  | 11%              | 11%                      | 8%                      | 8%                   | 7%               | 7%                       |
| California                         |                      |                  |                          | 7%                      | 7%                   | 7%               | 7%                       |
| Ohio                               | 9%                   | 9%               | 8%                       | 6%                      | 6%                   | 6%               | 6%                       |
| North Carolina                     | 7%                   | 7%               | 6%                       |                         |                      |                  |                          |
| Remaining states                   | 50%                  | 51%              | 52%                      | 51%                     | 50%                  | 51%              | 51%                      |

We evaluate our key performance indicators in conjunction with current expectations to determine if historical trends are indicative of future results. Our expected results may not be achieved and actual results may differ materially from our expectations. Factors that may cause actual results to differ from expected results are described in more detail in Forward-Looking Statements and Risk Factors and other sections of this Quarterly Report on Form 10-Q. Management regularly monitors economic and other factors to develop strategic and tactical plans designed to improve performance and maximize our competitive position. Our ability to achieve our financial objectives is

dependent upon our ability to effectively execute these plans and to appropriately respond to emerging economic and company-specific trends. Please refer to our Annual Report on Form 10-K/A for the year ended December 31, 2006, under the headings Business, Risk Factors and Management's Discussion and Analysis of Financial Condition and Results of Operations for further discussion of these risk factors.

#### **Portfolio Update**

*Investment Properties.* Payment coverages of the operators in our investment property portfolio continue to remain strong. Our overall payment coverage is at 1.96 times, which is consistent with the prior year. The table below reflects our recent historical trends of portfolio coverages. Coverage data reflects the 12 months ended for the periods presented. CBMF represents the ratio of facilities' earnings before interest, taxes, depreciation, amortization, rent and management fees to contractual rent or interest due us. CAMF represents the ratio of earnings before interest, taxes, depreciation, amortization, and rent (but after imputed management fees) to contractual rent or interest due us.

|                              | June 30, 2005 |       | June 30, 2006 |       | June 30, 2007 |       |
|------------------------------|---------------|-------|---------------|-------|---------------|-------|
|                              | CBMF          | CAMF  | CBMF          | CAMF  | CBMF          | CAMF  |
| Independent living/CCRCs (1) |               |       | 1.47x         | 1.25x | 1.46x         | 1.26x |
| Assisted living facilities   | 1.51x         | 1.28x | 1.51x         | 1.30x | 1.59x         | 1.37x |
| Skilled nursing facilities   | 2.20x         | 1.65x | 2.16x         | 1.55x | 2.21x         | 1.60x |
| Specialty care facilities    | 3.53x         | 2.91x | 3.18x         | 2.65x | 2.57x         | 2.01x |
| Weighted averages            | 1.91x         | 1.54x | 1.95x         | 1.53x | 1.96x         | 1.52x |

(1) As a result of our significant independent living/continuing care retirement community acquisitions in the fourth quarter of 2005, we began to separately disclose this facility classification in our portfolio reporting. We adopted the National Investment Center definitions and reclassified certain of our existing facilities to this classification.

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*Operating Properties.* The primary performance measure for our operating properties is net operating income ( NOI ) as discussed below in Non-GAAP Financial Measures. At September 30, 2007, we had 117 medical office buildings and four specialty care facilities in our operating properties portfolio. The following table summarizes and reconciles our net operating income for the periods indicated (in thousands):

|  | Rental<br>Income | Property<br>Operating<br>Expenses | Net<br>Operating<br>Income |
|--|------------------|-----------------------------------|----------------------------|
| Three months ended September 30, 2007: |                  |                                   |                            |
| Medical office buildings               | \$ 30,984        | \$ 10,296                         | \$ 20,688                  |
| Specialty care facilities              | 1,810            | 130                               | 1,680                      |
| Totals                                 | \$ 32,794        | \$ 10,426                         | \$ 22,368                  |
| Nine months ended September 30, 2007:  |                  |                                   |                            |
| Medical office buildings               | \$ 81,332        | \$ 26,044                         | \$ 55,288                  |
| Specialty care facilities              | 5,250            | 207                               | 5,043                      |
| Totals                                 | \$ 86,582        | \$ 26,251                         | \$ 60,331                  |

**Corporate Governance**

Maintaining investor confidence and trust has become increasingly important in today's business environment. Health Care REIT, Inc.'s Board of Directors and management are strongly committed to policies and procedures that reflect the highest level of ethical business practices. Our corporate governance guidelines provide the framework for our business operations and emphasize our commitment to increase stockholder value while meeting all applicable legal requirements. In March 2004, the Board of Directors adopted its Corporate Governance Guidelines. These guidelines meet the listing standards adopted by the New York Stock Exchange and are available on our Web site at [www.hcreit.com](http://www.hcreit.com) and from us upon written request sent to the Senior Vice President Administration and Corporate Secretary, Health Care REIT, Inc., One SeaGate, Suite 1500, P.O. Box 1475, Toledo, Ohio 43603-1475.

**Liquidity and Capital Resources****Sources and Uses of Cash**

Our primary sources of cash include rent and interest receipts, borrowings under unsecured lines of credit arrangements, public and private offerings of debt and equity securities, proceeds from the sales of real property and principal payments on loans receivable. Our primary uses of cash include dividend distributions, debt service payments (including principal and interest), real property investments (including construction advances), loan advances and general and administrative expenses. These sources and uses of cash are reflected in our Consolidated Statements of Cash Flows and are discussed in further detail below.

The following is a summary of our sources and uses of cash flows (dollars in thousands):

|   | Nine Months Ended |                  | Change    |      |
|---|-------------------|------------------|-----------|------|
|   | Sep. 30,<br>2007  | Sep. 30,<br>2006 | \$        | %    |
| Cash and cash equivalents at beginning of period  | \$ 36,216         | \$ 36,237        | \$ (21)   | 0%   |
| Cash provided from (used in) operating activities | 191,371           | 158,984          | 32,387    | 20%  |
| Cash provided from (used in) investing activities | (603,538)         | (289,804)        | (313,734) | 108% |
| Cash provided from (used in) financing activities | 407,391           | 110,073          | 297,318   | 270% |

|  |           |           |           |      |
|--|-----------|-----------|-----------|------|
| Cash and cash equivalents at end of period | \$ 31,440 | \$ 15,490 | \$ 15,950 | 103% |
|--|-----------|-----------|-----------|------|

*Operating Activities.* The change in net cash provided from operating activities is primarily attributable to an increase in net income, excluding depreciation and amortization, and to changes in straight-line rent. The increase in net income is discussed below in Results of Operations.

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The following is a summary of our straight-line rent and above/below market amortization (dollars in thousands):

|   | Nine Months Ended |                  | Change    |      |
|---|-------------------|------------------|-----------|------|
|   | Sep. 30,<br>2007  | Sep. 30,<br>2006 | \$        | %    |
| Gross straight-line rental income                 | \$ 12,664         | \$ 6,520         | \$ 6,144  | 94%  |
| Cash receipts due to real property sales          | (2,670)           | (1,623)          | (1,047)   | 65%  |
| Prepaid rent receipts                             | (8,121)           | (14,653)         | 6,532     | -45% |
| Amortization related to above/below market leases | 656               | 0                | 656       | n/a  |
|   | \$ 2,529          | \$ (9,756)       | \$ 12,285 | n/a  |

Gross straight-line rental income represents the non-cash difference between contractual cash rent due and the average rent recognized pursuant to Statement of Financial Accounting Standards No. 13, Accounting for Leases ( SFAS 13 ), for leases with fixed rental escalators, net of collectibility reserves. This amount is positive in the first half of a lease term (but declining every year due to annual increases in cash rent due) and is negative in the second half of a lease term. The increase in gross straight-line rental income is primarily attributable to leases in our operating properties segment, assumed in connection with the Windrose merger on December 20, 2006. The decrease in prepaid rent receipts is primarily attributable to cash received in connection with the acquisition of Commonwealth Communities Holdings LLC by Kindred Healthcare, Inc. in February 2006 as discussed in our Annual Report on Form 10-K for the year ended December 31, 2005.

*Investing Activities.* The changes in net cash used in investing activities are primarily attributable to net changes in real property and loans receivable. The following is a summary of our investment and disposition activities (dollars in thousands):

|   | Nine Months Ended |           |               |           |
|---|-------------------|-----------|---------------|-----------|
|   | Sep. 30, 2007     |           | Sep. 30, 2006 |           |
|   | Facilities        | Amount    | Facilities    | Amount    |
| Real property acquisitions:                 |                   |           |               |           |
| Independent living/CCRCs                    | 1                 | \$ 43,000 | 2             | \$ 25,337 |
| Assisted living facilities                  | 3                 | 14,975    | 4             | 30,650    |
| Skilled nursing facilities                  | 8                 | 122,875   | 16            | 141,482   |
| Medical office buildings                    | 25                | 356,518   |               | 0         |
| Specialty care facilities                   | 1                 | 11,923    |               | 0         |
| Land parcels                                |                   | 8,928     |               | 3,274     |
| Total acquisitions                          | 38                | 558,219   | 22            | 200,743   |
| Less: Assumed debt                          |                   | (160,001) |               | (25,049)  |
| Assumed other assets/(liabilities), net     |                   | (8,019)   |               | 0         |
| Cash disbursed for acquisitions             |                   | 390,199   |               | 175,694   |
| Construction in progress cash advances      |                   | 180,563   |               | 103,237   |
| Capital improvements to existing properties |                   | 16,919    |               | 11,665    |
| Total cash invested in real property        |                   | 587,681   |               | 290,596   |
| Real property dispositions:                 |                   |           |               |           |

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|  |    |            |    |            |
|--|----|------------|----|------------|
| Assisted living facilities                       | 9  | 57,794     | 4  | 26,974     |
| Skilled nursing facilities                       | 1  | 4,500      | 3  | 7,827      |
| Land parcels                                     |    | 3,646      |    | 487        |
| Proceeds from real property sales                | 10 | 65,940     | 7  | 35,288     |
| Net cash investments in real property            | 28 | \$ 521,741 | 15 | \$ 255,308 |
| Advances on loans receivable:                    |    |            |    |            |
| Investments in new loans                         |    | \$ 106,213 |    | \$ 64,319  |
| Draws on existing loans                          |    | 15,125     |    | 9,807      |
| Total investments in loans                       |    | 121,338    |    | 74,126     |
| Receipts on loans receivable:                    |    |            |    |            |
| Loan payoffs                                     |    | 38,095     |    | 30,046     |
| Principal payments on loans                      |    | 6,963      |    | 12,422     |
| Total principal receipts on loans                |    | 45,058     |    | 42,468     |
| Net cash advances (receipts) on loans receivable |    | \$ 76,280  |    | \$ 31,658  |

*Financing Activities.* The changes in net cash provided from or used in financing activities are primarily attributable to changes related to our long-term debt arrangements, proceeds from the issuance of common stock and dividend payments.

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For the nine months ended September 30, 2007, we had a net decrease of \$80,000,000 on our unsecured lines of credit arrangements as compared to a net increase of \$81,000,000 for the same period in 2006.

The changes in our senior unsecured notes are due to the issuance of \$400,000,000 of 4.75% convertible senior unsecured notes in July 2007 and the repayment of \$52,500,000 of 7.5% senior unsecured notes that matured in August 2007. The increase in secured debt principal payments is primarily attributable to the extinguishment of \$20,506,000 of loans during the three months ended June 30, 2007. See the discussion of interest expense below in Results of Operations for additional information.

The following is a summary of our common stock issuances (dollars in thousands, except per share amounts):

|                            | Shares<br>Issued | Issue<br>Price | Gross<br>Proceeds | Net<br>Proceeds |
|----------------------------|------------------|----------------|-------------------|-----------------|
| April 2006 public issuance | 3,222,800        | \$ 36.00       | \$ 116,021        | \$ 109,749      |
| 2006 DRIP                  | 1,440,341        | 35.28          | 50,811            | 50,811          |
| 2006 Options               | 210,585          | 21.93          | 4,619             | 4,619           |
| 2006 Totals                | 4,873,726        |                | \$ 171,451        | \$ 165,179      |
| April 2007 public issuance | 6,325,000        | \$ 44.01       | \$ 278,363        | \$ 265,294      |
| 2007 DRIP                  | 1,254,851        | 41.54          | 52,123            | 52,123          |
| 2007 Options               | 354,473          | 28.22          | 10,002            | 10,002          |
| 2007 Totals                | 7,934,324        |                | \$ 340,488        | \$ 327,419      |

In order to qualify as a REIT for federal income tax purposes, we must distribute at least 90% of our taxable income (including 100% of capital gains) to our stockholders. The increase in dividends is primarily attributable to an increase in our common stock outstanding (as discussed above) and dividends paid on our Series G Preferred Stock issued in December 2006 in conjunction with the Windrose merger in December 2006.

The following is a summary of our dividend payments (in thousands, except per share amounts):

|                          | Nine Months Ended |            |               |            |
|--------------------------|-------------------|------------|---------------|------------|
|                          | Sep. 30, 2007     |            | Sep. 30, 2006 |            |
|                          | Per<br>Share      | Amount     | Per<br>Share  | Amount     |
| Common Stock             | \$ 1.6191         | \$ 129,088 | \$ 1.9000     | \$ 116,272 |
| Series D Preferred Stock | 1.4766            | 5,906      | 1.4766        | 5,906      |
| Series E Preferred Stock | 1.1250            | 84         | 1.1250        | 84         |
| Series F Preferred Stock | 1.4297            | 10,008     | 1.4297        | 10,008     |
| Series G Preferred Stock | 1.4064            | 2,953      |               | 0          |
| Totals                   |                   | \$ 148,039 |               | \$ 132,270 |

**Off-Balance Sheet Arrangements**

We have an outstanding letter of credit issued for the benefit of certain insurance companies that provide workers compensation insurance to one of our tenants. Our obligation under the letter of credit matures in 2009. At September 30, 2007, our obligation under the letter of credit was \$2,450,000.



We are exposed to various market risks, including the potential loss arising from adverse changes in interest rates. We may or may not elect to use financial derivative instruments to hedge interest rate exposure. These decisions are principally based on the general trend in interest rates at the applicable dates, our perception of the future volatility of interest rates and our relative levels of variable rate debt and variable rate investments. As of September 30, 2007, we participated in two forward-starting interest rate swap agreements related to our long-term debt. Please see Note E to our unaudited consolidated financial statements for additional information.

**Table of Contents****Contractual Obligations**

The following table summarizes our payment requirements under contractual obligations as of September 30, 2007 (in thousands):

| Contractual Obligations                | Total               | Payments Due by Period |                   |                   |                     |
|--|---------------------|------------------------|-------------------|-------------------|---------------------|
|  |                     | 2007                   | 2008-2009         | 2010-2011         | Thereafter          |
| Unsecured lines of credit arrangements | \$ 145,000          | \$ 0                   | \$ 0              | \$ 145,000        | \$ 0                |
| Senior unsecured notes (1)             | 1,887,330           |                        | 42,330            |                   | 1,845,000           |
| Secured debt (1)                       | 512,036             | 2,133                  | 81,260            | 67,601            | 361,042             |
| Trust preferred liability (1)          | 51,000              | 51,000                 |                   |                   |                     |
| Contractual interest obligations       | 1,432,552           | 44,369                 | 294,355           | 276,501           | 817,327             |
| Capital lease obligations              | 0                   |                        |                   |                   |                     |
| Operating lease obligations            | 53,795              | 921                    | 6,350             | 5,643             | 40,881              |
| Purchase obligations                   | 626,653             | 29,692                 | 297,642           | 281,686           | 17,633              |
| Other long-term liabilities            | 0                   |                        |                   |                   |                     |
| <b>Total contractual obligations</b>   | <b>\$ 4,708,366</b> | <b>\$ 128,115</b>      | <b>\$ 721,937</b> | <b>\$ 776,431</b> | <b>\$ 3,081,883</b> |

(1) Amounts represent principal amounts due and do not reflect unamortized premiums/discounts or other fair value adjustments as reflected on the balance sheet.

At September 30, 2007, we had an unsecured credit arrangement with a consortium of seventeen banks providing for a revolving line of credit ( revolving credit ) in the amount of \$1.15 billion, which is scheduled to expire on August 5, 2011. Borrowings under the agreement are subject to interest payable in periods no longer than three months at either the agent bank's prime rate of interest or the applicable margin over LIBOR interest rate, at our option (5.73% at September 30, 2007). The applicable margin is based on our ratings with Moody's Investors Service and Standard & Poor's Ratings Services and was 0.6% at September 30, 2007. In addition, we pay a facility fee annually to each bank based on the bank's commitment under the revolving credit facility. The facility fee depends on our ratings with Moody's Investors Service and Standard & Poor's Ratings Services and was 0.15% at September 30, 2007. We also pay an annual agent's fee of \$50,000. Principal is due upon expiration of the agreement. At September 30, 2007, we had \$145,000,000 outstanding under the unsecured line of credit arrangement and estimated total contractual interest obligations of \$34,585,000. Contractual interest obligations are estimated based on the assumption that the balance of \$145,000,000 at September 30, 2007 is constant until maturity at interest rates in effect at September 30, 2007.

We have \$1,887,330,000 of senior unsecured notes principal outstanding with fixed annual interest rates ranging from 4.75% to 8.0%, payable semi-annually. Total contractual interest obligations on senior unsecured notes totaled \$1,205,275,000 at September 30, 2007. Additionally, we have mortgage loans with total outstanding principal of \$512,036,000, collateralized by owned properties, with fixed annual interest rates ranging from 4.89% to 8.21%, payable monthly. The carrying values of the properties securing the mortgage loans totaled \$983,851,000 at September 30, 2007. Total contractual interest obligations on mortgage loans totaled \$192,321,000 at September 30,

2007.

At September 30, 2007, we had \$51,000,000 of trust preferred liability principal outstanding with a fixed annual interest rate of 7.22%. On November 6, 2007, we purchased all \$50,000,000 of the outstanding trust preferred securities at par for the purpose of unwinding this financing arrangement and extinguishing the liability of an operating partnership to a subsidiary trust. At September 30, 2007, we had \$371,000 of contractual interest obligations for this liability. Please see Note N to our unaudited consolidated financial statements for additional information.

At September 30, 2007, we had operating lease obligations of \$53,795,000 relating primarily to ground leases at certain of our properties and office space leases.

Purchase obligations are comprised of unfunded construction commitments and contingent purchase obligations. At September 30, 2007, we had outstanding construction financings of \$229,134,000 for leased properties and were committed to providing additional financing of approximately \$593,428,000 to complete construction. At September 30, 2007, we had contingent purchase obligations totaling \$33,225,000. These contingent purchase obligations primarily relate to deferred acquisition fundings and capital improvements. Deferred acquisition fundings are contingent upon a tenant satisfying certain conditions in the lease. Upon funding, amounts due from the tenant are increased to reflect the additional investment in the property.

### ***Capital Structure***

As of September 30, 2007, we had stockholders' equity of \$2,260,684,000 and a total outstanding debt balance of \$2,600,586,000, which represents a debt to total book capitalization ratio of 53%. Our ratio of debt to market capitalization was 40% at September 30, 2007. For the nine months ended September 30, 2007, our interest coverage ratio was 2.82 to 1.00. For the nine months ended September 30, 2007, our fixed charge coverage ratio was 2.30 to 1.00. Also, at September 30, 2007, we had \$31,440,000 of cash and cash equivalents and \$1,005,000,000 of available borrowing capacity under our unsecured lines of credit arrangements.

Our debt agreements contain various covenants, restrictions and events of default. 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. As of September 30, 2007, we were in compliance with all of the covenants under our debt agreements. None of our debt agreements contain provisions for acceleration which could be triggered by our debt ratings with Moody's Investors

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Service and Standard & Poor's Ratings Services. However, under our unsecured lines of credit arrangements, these ratings on our senior unsecured notes are used to determine the fees and interest payable.

As of October 31, 2007, our senior unsecured notes were rated Baa2 (stable), BBB- (positive) and BBB (stable) by Moody's Investors Service, Standard & Poor's Ratings Services and Fitch Ratings, respectively. We plan to manage the company to maintain investment grade status with a capital structure consistent with our current profile. Any downgrades in terms of ratings or outlook by any or all of the noted rating agencies could have a material adverse impact on our cost and availability of capital, which could in turn have a material adverse impact on our consolidated results of operations, liquidity and/or financial condition.

On May 12, 2006, we filed an open-ended automatic or universal shelf registration statement with the Securities and Exchange Commission covering an indeterminate amount of future offerings of debt securities, common stock, preferred stock, depositary shares, warrants and units. As of October 31, 2007, we had an effective registration statement on file in connection with our enhanced DRIP program under which we may issue up to 10,760,247 shares of common stock. As of October 31, 2007, 9,856,325 shares of common stock remained available for issuance under this registration statement. Depending upon market conditions, we anticipate issuing securities under our registration statements to invest in additional properties and to repay borrowings under our unsecured lines of credit arrangements.

**Results of Operations**

Our primary sources of revenue include rent and interest. Our primary expenses include interest expense, depreciation and amortization, property operating expenses and general and administrative expenses. These revenues and expenses are reflected in our Consolidated Statements of Income and are discussed in further detail below. The following is a summary of our results of operations (dollars in thousands):

|   | Three Months Ended |                  | Change    |      | Nine Months Ended |                  | Change    |      |
|---|--------------------|------------------|-----------|------|-------------------|------------------|-----------|------|
|   | Sep. 30,<br>2007   | Sep. 30,<br>2006 | \$        | %    | Sep. 30,<br>2007  | Sep. 30,<br>2006 | \$        | %    |
| Net income available to common stockholders | \$ 24,529          | \$ 21,480        | \$ 3,049  | 14%  | \$ 73,504         | \$ 63,793        | \$ 9,711  | 15%  |
| Funds from operations                       | 63,830             | 45,898           | 17,932    | 39%  | 180,018           | 133,120          | 46,898    | 35%  |
| Funds available for distribution            | 66,379             | 48,032           | 18,347    | 38%  | 179,220           | 145,075          | 34,145    | 24%  |
| EBITDA                                      | 107,546            | 76,465           | 31,081    | 41%  | 306,634           | 225,588          | 81,046    | 36%  |
| Per share data (fully diluted):             |                    |                  |           |      |                   |                  |           |      |
| Net income available to common stockholders | \$ 0.30            | \$ 0.34          | \$ (0.04) | -12% | \$ 0.94           | \$ 1.04          | \$ (0.10) | -10% |
| Funds from operations                       | 0.79               | 0.73             | 0.06      | 8%   | 2.30              | 2.18             | 0.12      | 6%   |
| Funds available for distribution            | 0.82               | 0.76             | 0.06      | 8%   | 2.29              | 2.37             | (0.08)    | -3%  |
| Interest coverage ratio                     | 2.81x              | 2.98x            | -0.17x    | -6%  | 2.82x             | 3.04x            | -0.22x    | -7%  |
|   | 2.31x              | 2.41x            | -0.10x    | -4%  | 2.30x             | 2.44x            | -0.14x    | -6%  |

Fixed charge  
coverage ratio

Revenues were comprised of the following (dollars in thousands):

|                                      | Three Months Ended |                  | Change    |     | Nine Months Ended |                  | Change     |     |
|--------------------------------------|--------------------|------------------|-----------|-----|-------------------|------------------|------------|-----|
|                                      | Sep. 30,<br>2007   | Sep. 30,<br>2006 | \$        | %   | Sep. 30,<br>2007  | Sep. 30,<br>2006 | \$         | %   |
| Rental income                        | \$ 117,930         | \$ 73,328        | \$ 44,602 | 61% | \$ 332,907        | \$ 214,032       | \$ 118,875 | 56% |
| Interest income                      | 5,947              | 4,436            | 1,511     | 34% | 17,673            | 13,178           | 4,495      | 34% |
| Transaction fees<br>and other income | 1,199              | 1,019            | 180       | 18% | 3,935             | 3,049            | 886        | 29% |
| Totals                               | \$ 125,076         | \$ 78,783        | \$ 46,293 | 59% | \$ 354,515        | \$ 230,259       | \$ 124,256 | 54% |

The increase in gross revenues is primarily attributable to increased rental income resulting from the acquisitions of new properties from which we receive rent. See the discussion of investing activities in Liquidity and Capital Resources above for further information. Certain of our leases contain annual rental escalators that are contingent upon changes in the Consumer Price Index and/or changes in the gross operating revenues of the tenant's properties. These escalators are not fixed, so no straight-line rent is recorded; however, rental income is recorded based on the contractual cash rental payments due for the period. If gross operating revenues at our facilities and/or the Consumer Price Index do not increase, a portion of our revenues may not continue to increase. Sales of real property would offset revenue increases and, to the extent that they exceed new acquisitions, could result in decreased revenues. Our leases could renew above or below current rent rates, resulting in an increase or decrease in rental income.

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Interest income increased from 2006 primarily due to an increase in the balance of outstanding loans. Expenses were comprised of the following (dollars in thousands):

|  | Three Months Ended |               | Change |   | Nine Months Ended |               | Change |   |
|--|--------------------|---------------|--------|---|-------------------|---------------|--------|---|
|  | Sep. 30, 2007      | Sep. 30, 2006 | \$     | % | Sep. 30, 2007     | Sep. 30, 2006 | \$     | % |

The following is a summary of our interest expense (dollars in thousands):

|                            | Three Months Ended |               | Change    |      | Nine Months Ended |               | Change    |      |
|----------------------------|--------------------|---------------|-----------|------|-------------------|---------------|-----------|------|
|                            | Sep. 30, 2007      | Sep. 30, 2006 | \$        | %    | Sep. 30, 2007     | Sep. 30, 2006 | \$        | %    |
| Senior unsecured notes     | \$ 26,951          | \$ 19,574     | \$ 7,377  | 38%  | \$ 74,295         | \$ 58,722     | \$ 15,573 | 27%  |
| Secured debt               | 7,885              | 2,357         | 5,528     | 235% | 20,599            | 6,704         | 13,895    | 207% |
| Unsecured lines of credit  | 2,647              | 3,698         | (1,051)   | -28% | 11,280            | 8,567         | 2,713     | 32%  |
| Subsidiary trust liability | 863                | 0             | 863       | n/a  | 2,644             | 0             | 2,644     | n/a  |
| Capitalized interest       | (3,162)            | (1,384)       | (1,778)   | 128% | (8,058)           | (2,494)       | (5,564)   | 223% |
| SWAP losses (savings)      | (102)              | 29            | (131)     | n/a  | (52)              | 100           | (152)     | n/a  |
| Discontinued operations    | (213)              | (984)         | 771       | -78% | (1,138)           | (3,117)       | 1,979     | -63% |
| Totals                     | \$ 34,869          | \$ 23,290     | \$ 11,579 | 50%  | \$ 99,570         | \$ 68,482     | \$ 31,088 | 45%  |

The increase in interest expense on senior unsecured notes is due to higher average borrowings offset by lower average interest rates. The following is a summary of our senior note activity (dollars in thousands):

|                    | Three Months Ended<br>September 30, 2007 |                                      | Three Months Ended<br>September 30, 2006 |                                      | Nine Months Ended<br>September 30, 2007 |                                      | Nine Months Ended<br>September 30, 2006 |                                      |
|--------------------|--|--------------------------------------|--|--------------------------------------|---|--------------------------------------|---|--------------------------------------|
|                    | Face<br>Amount                           | Weighted<br>Avg.<br>Interest<br>Rate | Face<br>Amount                           | Weighted<br>Avg.<br>Interest<br>Rate | Face<br>Amount                          | Weighted<br>Avg.<br>Interest<br>Rate | Face<br>Amount                          | Weighted<br>Avg.<br>Interest<br>Rate |
| Beginning balance  | \$ 1,539,830                             | 6.159%                               | \$ 1,194,830                             | 6.566%                               | \$ 1,539,830                            | 6.159%                               | \$ 1,194,830                            | 6.566%                               |
| Debt issued        | 400,000                                  | 4.750%                               |  |                                      | 400,000                                 | 4.750%                               |   |                                      |
| Principal payments | (52,500)                                 | 7.500%                               |  |                                      | (52,500)                                | 7.500%                               |   |                                      |
| Ending balance     | \$ 1,887,330                             | 5.823%                               | \$ 1,194,830                             | 6.566%                               | \$ 1,887,330                            | 5.823%                               | \$ 1,194,830                            | 6.566%                               |
|                    | \$ 1,813,580                             | 5.907%                               | \$ 1,194,830                             | 6.566%                               | \$ 1,649,330                            | 6.048%                               | \$ 1,194,830                            | 6.566%                               |

Monthly  
averages

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The change in interest expense on secured debt is due to the net effect and timing of assumptions, extinguishments and principal amortizations. The following is a summary of our secured debt principal activity (dollars in thousands):

|                    | Three Months Ended<br>September 30, 2007 |                                      | Three Months Ended<br>September 30, 2006 |                                      | Nine Months Ended<br>September 30, 2007 |                                      | Nine Months Ended<br>September 30, 2006 |                                      |
|--------------------|--|--------------------------------------|--|--------------------------------------|---|--------------------------------------|---|--------------------------------------|
|                    | Amount                                   | Weighted<br>Avg.<br>Interest<br>Rate | Amount                                   | Weighted<br>Avg.<br>Interest<br>Rate | Amount                                  | Weighted<br>Avg.<br>Interest<br>Rate | Amount                                  | Weighted<br>Avg.<br>Interest<br>Rate |
| Beginning balance  | \$ 500,435                               | 6.137%                               | \$ 131,178                               | 7.135%                               | \$ 378,400                              | 6.348%                               | \$ 107,540                              | 7.328%                               |
| Debt assumed       | 13,623                                   | 5.700%                               |  |                                      | 159,958                                 | 5.814%                               | 25,049                                  | 6.315%                               |
| Debt extinguished  |  |                                      |  |                                      | (20,506)                                | 7.732%                               |   |                                      |
| Principal payments | (2,022)                                  | 6.222%                               | (773)                                    | 7.213%                               | (5,816)                                 | 6.381%                               | (2,184)                                 | 7.264%                               |
| Ending balance     | \$ 512,036                               | 6.125%                               | \$ 130,405                               | 7.135%                               | \$ 512,036                              | 6.125%                               | \$ 130,405                              | 7.135%                               |
| Monthly averages   | \$ 502,830                               | 6.134%                               | \$ 130,794                               | 7.135%                               | \$ 441,870                              | 6.233%                               | \$ 124,024                              | 7.185%                               |

The change in interest expense on unsecured lines of credit arrangements is due primarily to the net effect and timing of average draws, paydowns and variable interest rate changes. The following is a summary of our unsecured lines of credit arrangements (dollars in thousands):

|  | Three Months Ended<br>September 30, |            | Nine Months Ended<br>September 30, |            |
|--|-------------------------------------|------------|------------------------------------|------------|
|  | 2007                                | 2006       | 2007                               | 2006       |
| Balance outstanding at quarter end   | \$ 145,000                          | \$ 276,000 | \$ 145,000                         | \$ 276,000 |
| Maximum amount outstanding at any month end  | \$ 145,000                          | \$ 276,000 | \$ 381,000                         | \$ 276,000 |
| Average amount outstanding (total of daily principal balances divided by days in period)           | \$ 142,392                          | \$ 209,662 | \$ 218,607                         | \$ 168,518 |
| Weighted average interest rate (actual interest expense divided by average borrowings outstanding) | 7.43%                               | 7.05%      | 6.88%                              | 6.78%      |

At September 30, 2007, we had \$51,000,000 of trust preferred liability principal outstanding with a fixed annual interest rate of 7.22%. On November 6, 2007, we purchased all \$50,000,000 of the outstanding trust preferred securities at par for the purpose of unwinding this financing arrangement and extinguishing the liability of an operating partnership to a subsidiary trust. Please see Note N to our unaudited consolidated financial statements for additional information.

We capitalize certain interest costs associated with funds used to finance the construction of properties owned directly by us. The amount capitalized is based upon the borrowings outstanding during the construction period using the rate of interest that approximates our cost of financing. Our interest expense is reduced by the amount capitalized. Capitalized interest for the three and nine months ended September 30, 2007 totaled \$3,162,000 and \$8,058,000, respectively, as compared with \$1,384,000 and \$2,494,000 for the same periods in 2006.



On May 6, 2004, we entered into two interest rate swap agreements (the 2004 Swaps ) for a total notional amount of \$100,000,000 to hedge changes in fair value attributable to changes in the LIBOR swap rate of \$100,000,000 of fixed rate debt with a maturity date of November 15, 2013. The 2004 Swaps were treated as fair-value hedges for accounting purposes and we utilized the short-cut method to assess effectiveness. The 2004 Swaps were with highly rated counterparties in which we received a fixed rate of 6.0% and paid a variable rate based on six-month LIBOR plus a spread. On September 12, 2007, we terminated the 2004 Swaps and we received a \$2,125,000 cash settlement. The unamortized amount of this settlement at September 30, 2007 was \$2,059,000 and is recorded as an adjustment to the hedged item. This amount will be amortized to interest expense over the life of the hedged debt using the effective interest method. For the three and nine months ended September 30, 2007, we generated \$73,000 and \$23,000 of savings, respectively, related to the 2004 Swaps that was recorded as a reduction of interest expense. For the three and nine months ended September 30, 2006, we incurred \$29,000 and \$100,000 of losses, respectively, related to the 2004 Swaps that was recorded as an addition to interest expense.

On July 2, 2007, we entered into two forward-starting interest rate swaps, with an aggregate notional amount of \$200,000,000 that were designated as cash flow hedges of the variability in forecasted interest payments attributable to changes in the LIBOR swap rate, on long-term fixed rate debt forecasted to be issued in 2007. The 2007 Swaps have the economic effect of fixing \$200,000,000 of our debt at 4.913% for five years. The 2007 Swaps were settled on July 17, 2007, which was the day after the forecasted debt was priced. The cash settlement value of these contracts at July 17, 2007, was \$733,000. This amount represented the effective portion of the hedges as there was no hedge ineffectiveness. Therefore, the \$733,000 settlement value was deferred in accumulated other comprehensive income ( AOCI ) and will be amortized to interest expense using the effective interest method. The unamortized amount of AOCI related to these contracts at September 30, 2007 is \$704,000. For the three and nine months ended September 30, 2007, we reclassified \$29,000 out of AOCI as a reduction of interest expense.

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As discussed in our Annual Report on Form 10-K/A for the year ended December 31, 2006, we completed our merger with Windrose Medical Properties Trust on December 20, 2006. These operations are the principal component of our property operating expenses. There was no similar activity in the prior year periods.

Depreciation and amortization increased primarily as a result of additional investments in properties owned directly by us. See the discussion of investing activities in Liquidity and Capital Resources above for additional details. To the extent that we acquire or dispose of additional properties in the future, our provision for depreciation and amortization will change accordingly.

General and administrative expenses as a percentage of revenues (including revenues from discontinued operations) for the three and nine months ended September 30, 2007, were 6.85% and 7.89%, respectively, as compared with 6.39% and 6.88% for the same periods in 2006. The increase from 2006 is primarily related to \$1,750,000 of acquisition finders fees paid during the three months ended June 30, 2007 and costs associated with our initiatives to attract and retain appropriate personnel to achieve our business objectives. During the quarter ended June 30, 2007, we recorded \$1,750,000 of one-time acquisition finders fees paid to former Windrose management in connection with the closing of the Rendina/Paramount transaction. These fees relate to services rendered prior to the consummation of the Windrose merger in December 2006. Due to the recipients current employment status with the company, the fees have been expensed as compensation rather than included in the purchase price of the acquisition, as is typical with such fees.

Loan expense represents the amortization of deferred loan costs incurred in connection with the issuance and amendments of debt. The change in loan expense is primarily due to costs associated with the issuance of \$345,000,000 of senior unsecured convertible notes in November and December 2006, costs related to the assumption of secured debt in connection with the Windrose merger in December 2006, the issuance of \$400,000,000 of senior unsecured convertible notes in July 2007 and costs associated with the amendment of our unsecured line of credit in August 2007.

As a result of our quarterly evaluation, we concluded that the allowance for loan losses at December 31, 2006 remained appropriate as of September 30, 2007. The provision for loan losses is related to our critical accounting estimate for the allowance for loan losses and is discussed below in Critical Accounting Policies.

Other items were comprised of the following (dollars in thousands):

|                                    | Three Months Ended |                  | Change   |      | Nine Months Ended |                  | Change     |      |
|------------------------------------|--------------------|------------------|----------|------|-------------------|------------------|------------|------|
|                                    | Sep. 30,<br>2007   | Sep. 30,<br>2006 | \$       | %    | Sep. 30,<br>2007  | Sep. 30,<br>2006 | \$         | %    |
| Minority interests                 | \$ (121)           | \$ 0             | \$ (121) | n/a  | \$ (407)          | \$ 0             | \$ (407)   | n/a  |
| Gain (loss) on sales of properties | 766                | 108              | 658      | 609% | 2,775             | 2,590            | 185        | 7%   |
| Discontinued operations, net       | 483                | 201              | 282      | 140% | 2,138             | 1,000            | 1,138      | 114% |
| Preferred dividends                | (6,317)            | (5,333)          | (984)    | 18%  | (18,952)          | (15,998)         | (2,954)    | 18%  |
| Totals                             | \$ (5,189)         | \$ (5,024)       | \$ (165) | 3%   | \$ (14,446)       | \$ (12,408)      | \$ (2,038) | 16%  |

Minority interests primarily relate to certain joint venture properties acquired in connection with the Windrose merger in December 2006. There were no similar investments in the prior year period.

One independent living facility and one assisted living facility were held for sale as of September 30, 2007. We did not recognize an impairment loss on these assets as the fair value less estimated costs to sell exceeded our carrying values. During the nine months ended September 30, 2007, we sold nine assisted living facilities, one skilled nursing facility and one parcel of land with carrying values of \$63,165,000 for a net gain of \$2,775,000. These properties generated \$2,138,000 of income after deducting depreciation and interest expense from rental revenue for the nine

months ended September 30, 2007. All properties sold subsequent to January 1, 2005 and held for sale at September 30, 2007 generated \$1,000,000 of income after deducting depreciation and interest expense from rental revenue for the nine months ended September 30, 2006. Please refer to Note F to our unaudited consolidated financial statements for further discussion.

The increase in preferred stock dividends is due to an increase in average outstanding preferred shares as a result of the issuance of 2,100,000 shares of 7.5% Series G Cumulative Convertible Preferred Stock in connection with the Windrose merger in December 2006.

**Table of Contents****Non-GAAP Financial Measures**

We believe that net income, as defined by U.S. GAAP, is the most appropriate earnings measurement. However, we consider FFO and FAD to be useful supplemental measures of our operating performance. Historical cost accounting for real estate assets in accordance with U.S. GAAP implicitly assumes that the value of real estate assets diminishes predictably over time as evidenced by the provision for depreciation. However, since real estate values have historically risen or fallen with market conditions, many industry investors and analysts have considered presentations of operating results for real estate companies that use historical cost accounting to be insufficient. In response, the National Association of Real Estate Investment Trusts ( NAREIT ) created FFO as a supplemental measure of operating performance for REITs that excludes historical cost depreciation from net income. FFO, as defined by NAREIT, means net income, computed in accordance with U.S. GAAP, excluding gains (or losses) from sales of real estate, plus depreciation and amortization, and after adjustments for unconsolidated partnerships and joint ventures. FAD represents FFO excluding the non-cash straight-line rental adjustments.

EBITDA stands for earnings before interest, taxes, depreciation and amortization. We believe that EBITDA, along with net income and cash flow provided from operating activities, is an important supplemental measure because it provides additional information to assess and evaluate the performance of our operations. Additionally, restrictive covenants in our long-term debt arrangements contain financial ratios based on EBITDA. We primarily utilize EBITDA to measure our interest coverage ratio, which represents EBITDA divided by total interest, and our fixed charge coverage ratio, which represents EBITDA divided by fixed charges. Fixed charges include total interest, secured debt principal amortization and preferred dividends.

During the quarter ended June 30, 2007, we recorded \$1,750,000 (\$0.02 per diluted share) of one-time acquisition finders fees paid to former Windrose management in connection with the closing of the Rendina/Paramount transaction. These fees relate to services rendered prior to the consummation of the Windrose merger in December 2006. Due to the recipients current employment status with the company, the fees have been expensed as compensation rather than included in the purchase price of the acquisition, as is typical with such fees. These fees have not been added back for the calculations of FFO, FAD or EBITDA.

Net operating income ( NOI ) is used to evaluate the operating performance of certain real estate properties such as medical office buildings. We define NOI as rental revenues, including tenant reimbursements, less property level operating expenses, which exclude depreciation and amortization, general and administrative expenses, impairments, interest expense and discontinued operations. We believe NOI provides investors relevant and useful information because it measures the operating performance of our medical office buildings at the property level on an unleveraged basis. We use NOI to make decisions about resource allocations and to assess the property level performance of our medical office buildings.

Our supplemental measures are financial measures that are widely used by investors, equity and debt analysts and rating agencies in the valuation, comparison, rating and investment recommendations of companies. Management uses these financial measures to facilitate internal and external comparisons to our historical operating results and in making operating decisions. Additionally, these measures are utilized by the Board of Directors to evaluate management. Our supplemental measures do not represent net income or cash flow provided from operating activities as determined in accordance with U.S. GAAP and should not be considered as alternative measures of profitability or liquidity. Finally, the supplemental measures, as defined by us, may not be comparable to similarly entitled items reported by other real estate investment trusts or other companies.

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The table below reflects the reconciliation of FFO to net income available to common stockholders, the most directly comparable U.S. GAAP measure, for the periods presented. The provisions for depreciation and amortization include provisions for depreciation and amortization from discontinued operations. Amounts are in thousands except for per share data.

|   | Three Months Ended |                  |                          |                         |                   |                  |                          |
|---|--------------------|------------------|--------------------------|-------------------------|-------------------|------------------|--------------------------|
|   | March 31,<br>2006  | June 30,<br>2006 | September<br>30,<br>2006 | December<br>31,<br>2006 | March 31,<br>2007 | June 30,<br>2007 | September<br>30,<br>2007 |
| <b>FFO Reconciliation:</b>                  |                    |                  |                          |                         |                   |                  |                          |
| Net income available to common stockholders | \$ 19,645          | \$ 22,668        | \$ 21,480                | \$ 17,494               | \$ 23,356         | \$ 25,620        | \$ 24,529                |
| Depreciation and amortization               | 23,262             | 24,131           | 24,526                   | 25,645                  | 33,860            | 35,547           | 40,137                   |
| Loss (gain) on sales of properties          | (1,553)            | (929)            | (108)                    | 1,324                   | (977)             | (1,033)          | (766)                    |
| Minority interests                          | 0                  | 0                | 0                        | (4)                     | (32)              | (155)            | (70)                     |
| Funds from operations                       | \$ 41,354          | \$ 45,870        | \$ 45,898                | \$ 44,459               | \$ 56,207         | \$ 59,979        | \$ 63,830                |
| <b>Average common shares outstanding:</b>   |                    |                  |                          |                         |                   |                  |                          |
| Basic                                       | 58,178             | 61,548           | 62,524                   | 64,277                  | 73,224            | 79,060           | 80,710                   |
| Diluted                                     | 58,535             | 61,868           | 62,866                   | 64,687                  | 73,791            | 79,546           | 81,163                   |
| <b>Per share data:</b>                      |                    |                  |                          |                         |                   |                  |                          |
| Net income available to common stockholders |                    |                  |                          |                         |                   |                  |                          |
| Basic                                       | \$ 0.34            | \$ 0.37          | \$ 0.34                  | \$ 0.27                 | \$ 0.32           | \$ 0.32          | \$ 0.30                  |
| Diluted                                     | 0.34               | 0.37             | 0.34                     | 0.27                    | 0.32              | 0.32             | 0.30                     |
| Funds from operations                       |                    |                  |                          |                         |                   |                  |                          |
| Basic                                       | \$ 0.71            | \$ 0.75          | \$ 0.73                  | \$ 0.69                 | \$ 0.77           | \$ 0.76          | \$ 0.79                  |
| Diluted                                     | 0.71               | 0.74             | 0.73                     | 0.69                    | 0.76              | 0.75             | 0.79                     |

|   | Nine Months Ended     |                       |
|---|-----------------------|-----------------------|
|   | September 30,<br>2006 | September 30,<br>2007 |
| <b>FFO Reconciliation:</b>                  |                       |                       |
| Net income available to common stockholders | \$ 63,793             | \$ 73,504             |
| Depreciation and amortization               | 71,917                | 109,545               |

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|   |           |           |
|---|-----------|-----------|
| Loss (gain) on sales of properties          | (2,590)   | (2,775)   |
| Minority interests                          | 0         | (256)     |
| Funds from operations                       | \$133,120 | \$180,018 |
| Average common shares outstanding:          |           |           |
| Basic                                       | 60,766    | 77,686    |
| Diluted                                     | 61,102    | 78,234    |
| Per share data:                             |           |           |
| Net income available to common stockholders |           |           |
| Basic                                       | \$ 1.05   | \$ 0.95   |
| Diluted                                     | 1.04      | 0.94      |
| Funds from operations                       |           |           |
| Basic                                       | \$ 2.19   | \$ 2.32   |
| Diluted                                     | 2.18      | 2.30      |

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The table below reflects the reconciliation of FAD to net income available to common stockholders, the most directly comparable U.S. GAAP measure, for the periods presented. The provisions for depreciation and amortization include provisions for depreciation and amortization from discontinued operations. Amounts are in thousands except for per share data.

|  | Three Months Ended |                  |                          |                         |                   |                  |                          |
|--|--------------------|------------------|--------------------------|-------------------------|-------------------|------------------|--------------------------|
|  | March 31,<br>2006  | June 30,<br>2006 | September<br>30,<br>2006 | December<br>31,<br>2006 | March 31,<br>2007 | June 30,<br>2007 | September<br>30,<br>2007 |
| FAD Reconciliation:                                  |                    |                  |                          |                         |                   |                  |                          |
| Net income available to common stockholders          | \$ 19,645          | \$ 22,668        | \$ 21,480                | \$ 17,494               | \$ 23,356         | \$ 25,620        | \$ 24,529                |
| Depreciation and amortization                        | 23,262             | 24,131           | 24,526                   | 25,645                  | 33,860            | 35,547           | 40,137                   |
| Loss (gain) on sales of properties                   | (1,553)            | (929)            | (108)                    | 1,324                   | (977)             | (1,033)          | (766)                    |
| Gross straight-line rental income                    | (2,400)            | (2,216)          | (1,904)                  | (2,912)                 | (4,231)           | (3,878)          | (4,555)                  |
| Prepaid/straight-line rent receipts                  | 10,310             | 2,710            | 3,256                    | 4,285                   | 2,078             | 2,832            | 5,881                    |
| Rental income related to above/(below) market leases | 0                  | 0                | 0                        | (60)                    | (460)             | (464)            | 268                      |
| Amortization of deferred loan expenses               | 711                | 707              | 782                      | 1,056                   | 1,267             | 1,236            | 1,504                    |
| Cap Ex, tenant improvements, lease commissions       | 0                  | 0                | 0                        | (21)                    | (1,063)           | (762)            | (704)                    |
| Minority interests                                   | 0                  | 0                | 0                        | (2)                     | (5)               | (82)             | 85                       |
| Funds available for distribution                     | \$ 49,975          | \$ 47,071        | \$ 48,032                | \$ 46,809               | \$ 53,825         | \$ 59,016        | \$ 66,379                |
| Average common shares outstanding:                   |                    |                  |                          |                         |                   |                  |                          |
| Basic  | 58,178             | 61,548           | 62,524                   | 64,277                  | 73,224            | 79,060           | 80,710                   |
| Diluted  | 58,535             | 61,868           | 62,866                   | 64,687                  | 73,791            | 79,546           | 81,163                   |
| Per share data:                                      |                    |                  |                          |                         |                   |                  |                          |
| Net income available to common stockholders          |                    |                  |                          |                         |                   |                  |                          |
| Basic  | \$ 0.34            | \$ 0.37          | \$ 0.34                  | \$ 0.27                 | \$ 0.32           | \$ 0.32          | \$ 0.30                  |
| Diluted  | 0.34               | 0.37             | 0.34                     | 0.27                    | 0.32              | 0.32             | 0.30                     |
| Funds available for distribution                     |                    |                  |                          |                         |                   |                  |                          |

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|         |         |         |         |         |         |         |         |
|---------|---------|---------|---------|---------|---------|---------|---------|
| Basic   | \$ 0.86 | \$ 0.76 | \$ 0.77 | \$ 0.73 | \$ 0.74 | \$ 0.75 | \$ 0.82 |
| Diluted | 0.85    | 0.76    | 0.76    | 0.72    | 0.73    | 0.74    | 0.82    |

|  | Nine Months Ended     |                       |
|--|-----------------------|-----------------------|
|  | September 30,<br>2006 | September 30,<br>2007 |
| FAD Reconciliation:                                  |                       |                       |
| Net income available to common stockholders          | \$ 63,793             | \$ 73,504             |
| Depreciation and amortization                        | 71,917                | 109,545               |
| Loss (gain) on sales of properties                   | (2,590)               | (2,775)               |
| Gross straight-line rental income                    | (6,520)               | (12,664)              |
| Prepaid/straight-line rent receipts                  | 16,276                | 10,791                |
| Rental income related to above/(below) market leases | 0                     | (656)                 |
| Amortization of deferred loan expenses               | 2,199                 | 4,006                 |
| Cap Ex, tenant improvements, lease commissions       | 0                     | (2,529)               |
| Minority interests                                   | 0                     | (2)                   |
| <br>Funds available for distribution                 | <br>\$145,075         | <br>\$179,220         |
| <br>Average common shares outstanding:               |                       |                       |
| Basic  | 60,766                | 77,686                |
| Diluted  | 61,102                | 78,234                |
| <br>Per share data:                                  |                       |                       |
| Net income available to common stockholders          |                       |                       |
| Basic  | \$ 1.05               | \$ 0.95               |
| Diluted  | 1.04                  | 0.94                  |
| <br>Funds available for distribution                 |                       |                       |
| Basic  | \$ 2.39               | \$ 2.31               |
| Diluted  | 2.37                  | 2.29                  |



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The table below reflects the reconciliation of EBITDA to net income, the most directly comparable U.S. GAAP measure, for the periods presented. Interest expense and the provisions for depreciation and amortization includes discontinued operations. Tax expense represents income-based taxes. Amortization represents the amortization of deferred loan expenses. Adjusted EBITDA represents EBITDA as adjusted below for items pursuant to covenant provisions of our unsecured lines of credit arrangements. Dollars are in thousands.

|  | Three Months Ended |                  |                          |                         |                   |                  |                          |
|--|--------------------|------------------|--------------------------|-------------------------|-------------------|------------------|--------------------------|
|  | March 31,<br>2006  | June 30,<br>2006 | September<br>30,<br>2006 | December<br>31,<br>2006 | March 31,<br>2007 | June 30,<br>2007 | September<br>30,<br>2007 |
| EBITDA                                       |                    |                  |                          |                         |                   |                  |                          |
| Reconciliation:                              |                    |                  |                          |                         |                   |                  |                          |
| Net income                                   | \$24,978           | \$28,001         | \$26,813                 | \$22,958                | \$29,673          | \$ 31,937        | \$ 30,846                |
| Interest expense                             | 24,238             | 23,087           | 24,274                   | 25,235                  | 31,999            | 33,624           | 35,082                   |
| Tax expense<br>(benefit)                     | 0                  | 12               | 70                       | 0                       | 11                | (69)             | (23)                     |
| Depreciation and<br>amortization             | 23,262             | 24,131           | 24,526                   | 25,645                  | 33,860            | 35,547           | 40,137                   |
| Amortization of<br>deferred loan<br>expenses | 711                | 707              | 782                      | 1,056                   | 1,267             | 1,236            | 1,504                    |
| EBITDA                                       | 73,189             | 75,938           | 76,465                   | 74,894                  | 96,810            | 102,275          | 107,546                  |
| Stock-based<br>compensation<br>expense       | 2,514              | 838              | 839                      | 2,789                   | 3,177             | 1,276            | 1,301                    |
| Provision for loan<br>losses                 | 250                | 250              | 250                      | 250                     | 0                 | 0                | 0                        |
| Adjusted EBITDA                              | \$75,953           | \$77,026         | \$77,554                 | \$77,933                | \$99,987          | \$103,551        | \$108,847                |
| Interest Coverage<br>Ratio:                  |                    |                  |                          |                         |                   |                  |                          |
| Interest expense                             | \$24,238           | \$23,087         | \$24,274                 | \$25,235                | \$31,999          | \$ 33,624        | \$ 35,082                |
| Capitalized interest                         | 202                | 909              | 1,384                    | 1,976                   | 2,327             | 2,570            | 3,162                    |
| Total interest                               | 24,440             | 23,996           | 25,658                   | 27,211                  | 34,326            | 36,194           | 38,244                   |
| EBITDA                                       | \$73,189           | \$75,938         | \$76,465                 | \$74,894                | \$96,810          | \$102,275        | \$107,546                |
| Interest coverage<br>ratio                   | 2.99x              | 3.16x            | 2.98x                    | 2.75x                   | 2.82x             | 2.83x            | 2.81x                    |
| Adjusted EBITDA                              | \$75,953           | \$77,026         | \$77,554                 | \$77,933                | \$99,987          | \$103,551        | \$108,847                |
| Interest coverage<br>ratio-adjusted          | 3.11x              | 3.21x            | 3.02x                    | 2.86x                   | 2.91x             | 2.86x            | 2.85x                    |

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|                                      |          |          |          |          |          |           |           |
|--------------------------------------|----------|----------|----------|----------|----------|-----------|-----------|
| Fixed Charge Coverage Ratio:         |          |          |          |          |          |           |           |
| Total interest                       | \$24,440 | \$23,996 | \$25,658 | \$27,211 | \$34,326 | \$ 36,194 | \$ 38,244 |
| Secured debt principal amortization  | 643      | 768      | 773      | 849      | 1,894    | 1,894     | 2,022     |
| Preferred dividends                  | 5,333    | 5,333    | 5,333    | 5,464    | 6,317    | 6,317     | 6,317     |
| Total fixed charges                  | 30,416   | 30,097   | 31,764   | 33,524   | 42,537   | 44,405    | 46,583    |
| EBITDA                               | \$73,189 | \$75,938 | \$76,465 | \$74,894 | \$96,810 | \$102,275 | \$107,546 |
| Fixed charge coverage ratio          | 2.41x    | 2.52x    | 2.41x    | 2.23x    | 2.28x    | 2.30x     | 2.31x     |
| EBITDA adjusted                      | \$75,953 | \$77,026 | \$77,554 | \$77,933 | \$99,987 | \$103,551 | \$108,847 |
| Fixed charge coverage ratio-adjusted | 2.50x    | 2.56x    | 2.44x    | 2.32x    | 2.35x    | 2.33x     | 2.34x     |

|  | Nine Months Ended  |                    |
|--|--------------------|--------------------|
|  | September 30, 2006 | September 30, 2007 |
| EBITDA Reconciliation:                 |                    |                    |
| Net income                             | \$ 79,791          | \$ 92,456          |
| Interest expense                       | 71,599             | 100,708            |
| Tax expense (benefit)                  | 82                 | (81)               |
| Depreciation and amortization          | 71,917             | 109,545            |
| Amortization of deferred loan expenses | 2,199              | 4,006              |
| EBITDA                                 | 225,588            | 306,634            |
| Stock-based compensation expense       | 4,191              | 5,753              |
| Provision for loan losses              | 750                | 0                  |
| Adjusted EBITDA                        | \$230,529          | \$312,387          |
| Interest Coverage Ratio:               |                    |                    |
| Interest expense                       | \$ 71,599          | \$100,708          |
| Capitalized interest                   | 2,494              | 8,058              |
| Total interest                         | 74,093             | 108,766            |
| EBITDA                                 | \$225,588          | \$306,634          |
| Interest coverage ratio                | 3.04x              | 2.82x              |
| Adjusted EBITDA                        | \$230,529          | \$312,387          |
| Interest coverage ratio-adjusted       | 3.11x              | 2.87x              |
| Fixed Charge Coverage Ratio:           |                    |                    |

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|                                      |           |           |
|--------------------------------------|-----------|-----------|
| Total interest                       | \$ 74,093 | \$108,766 |
| Secured debt principal amortization  | 2,184     | 5,816     |
| Preferred dividends                  | 15,998    | 18,952    |
| Total fixed charges                  | 92,275    | 133,534   |
| EBITDA                               | \$225,588 | \$306,634 |
| Fixed charge coverage ratio          | 2.44x     | 2.30x     |
| EBITDA adjusted                      | \$230,529 | \$312,387 |
| Fixed charge coverage ratio-adjusted | 2.50x     | 2.34x     |

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Our consolidated financial statements are prepared in accordance with U.S. GAAP, which requires us to make estimates and assumptions. Management considers an accounting estimate or assumption critical if:

the nature of the estimates or assumptions is material due to the levels of subjectivity and judgment necessary to account for highly uncertain matters or the susceptibility of such matters to change; and

the impact of the estimates and assumptions on financial condition or operating performance is material.

Management has discussed the development and selection of its critical accounting policies with the Audit Committee of the Board of Directors and the Audit Committee has reviewed the disclosure presented below relating to them. Management believes the current assumptions and other considerations used to estimate amounts reflected in our consolidated financial statements are appropriate and are not reasonably likely to change in the future. However, since these estimates require assumptions to be made that were uncertain at the time the estimate was made, they bear the risk of change. If actual experience differs from the assumptions and other considerations used in estimating amounts reflected in our consolidated financial statements, the resulting changes could have a material adverse effect on our consolidated results of operations, liquidity and/or financial condition. Please refer to our Annual Report on Form 10-K/A for the year ended December 31, 2006 for further information regarding significant accounting policies that impact us. There have been no material changes to these policies in 2007. See Note M to our unaudited consolidated financial statements for the impact of new accounting pronouncements.

The following table presents information about our critical accounting policies, as well as the material assumptions used to develop each estimate:

| <b>Nature of Critical Accounting Estimate</b>   | <b>Assumptions/Approach Used</b>   |
|---|--|
| <p data-bbox="87 1058 422 1089">Allowance for Loan Losses</p> <p data-bbox="87 1129 726 1892">We maintain an allowance for loan losses in accordance with Statement of Financial Accounting Standards No. 114, Accounting by Creditors for Impairment of a Loan, as amended, and SEC Staff Accounting Bulletin No. 102, Selected Loan Loss Allowance Methodology and Documentation Issues. The allowance for loan losses is maintained at a level believed adequate to absorb potential losses in our loans receivable. The determination of the allowance is based on a quarterly evaluation of all outstanding loans. If this evaluation indicates that there is a greater risk of loan charge-offs, additional allowances or placement on non-accrual status may be required. A loan is impaired when, based on current information and events, it is probable that we will be unable to collect all amounts due as scheduled according to the contractual terms of the original loan agreement. Consistent with this definition, all loans on non-accrual are deemed impaired. To the extent circumstances improve and the risk of collectibility is diminished, we will return these loans to full accrual status.</p> | <p data-bbox="794 1129 1493 1409">The determination of the allowance is based on a quarterly evaluation of all outstanding loans, including general economic conditions and estimated collectibility of loan payments and principal. We evaluate the collectibility of our loans receivable based on a combination of factors, including, but not limited to, delinquency status, historical loan charge-offs, financial strength of the borrower and guarantors and value of the underlying property.</p> <p data-bbox="794 1444 1493 1682">As a result of our quarterly evaluation, we concluded that the allowance for loan losses at December 31, 2006 remained appropriate as of September 30, 2007, resulting in an allowance for loan losses of \$7,406,000 relating to loans with outstanding balances of \$111,499,000. Also at September 30, 2007, we had a loan with an outstanding balance of \$799,000 on non-accrual status.</p> |



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**Nature of Critical Accounting Estimate**

**Assumptions/Approach Used**

**Business Combinations**

Substantially all of the properties owned by us are leased under operating leases and are recorded at cost. The cost of our real property is allocated to land, buildings, improvements and intangibles in accordance with Statement of Financial Accounting Standards No. 141, Business Combinations. The allocation of the acquisition costs of properties is based on appraisals commissioned from independent real estate appraisal firms.

We compute depreciation and amortization on our properties using the straight-line method based on their estimated useful lives which range from 15 to 40 years for buildings and five to 15 years for improvements. Lives for intangibles are based on the remaining term of the underlying leases.

For the nine months ended September 30, 2007, we recorded \$87,259,000, \$12,333,000 and \$9,953,000 as provisions for depreciation and amortization relating to buildings, improvements and intangibles, respectively, including amounts reclassified as discontinued operations. The average useful life of our buildings, improvements and intangibles was 32.1 years, 11.9 years and 4.8 years, respectively, for the nine months ended September 30, 2007.

**Impairment of Long-Lived Assets**

We review our long-lived assets for potential impairment in accordance with Statement of Financial Accounting Standards No. 144, Accounting for the Impairment and Disposal of Long-Lived Assets. An impairment charge must be recognized when the carrying value of a long-lived asset is not recoverable. The carrying value is not recoverable if it exceeds the sum of the undiscounted cash flows expected to result from the use and eventual disposition of the asset. If it is determined that a permanent impairment of a long-lived asset has occurred, the carrying value of the asset is reduced to its fair value and an impairment charge is recognized for the difference between the carrying value and the fair value.

The net book value of long-lived assets is reviewed quarterly on a property by property basis to determine if there are indicators of impairment. These indicators may include anticipated operating losses at the property level, the tenant's inability to make rent payments, a decision to dispose of an asset before the end of its estimated useful life and changes in the market that may permanently reduce the value of the property. If indicators of impairment exist, then the undiscounted future cash flows from the most likely use of the property are compared to the current net book value. This analysis requires us to determine if indicators of impairment exist and to estimate the most likely stream of cash flows to be generated from the property during the period the property is expected to be held.

We did not record any impairment charges for the nine months ended September 30, 2007.

**Fair Value of Derivative Instruments**

The valuation of derivative instruments is accounted for in accordance with Statement of Financial Accounting Standards No. 133, Accounting for

The valuation of derivative instruments requires us to make estimates and judgments that affect the fair value of the instruments. Fair values for our derivatives are

Derivative Instruments and Hedging Activities ( SFAS133 ), as amended by Statement of Financial Accounting Standards No. 138, Accounting for Certain Derivative Instruments and Certain Hedging Activities. SFAS133, as amended, requires companies to record derivatives at fair market value on the balance sheet as assets or liabilities.

estimated by a third party consultant, which utilizes pricing models that consider forward yield curves and discount rates. Such amounts and the recognition of such amounts are subject to significant estimates which may change in the future. At September 30, 2007, we participated in two forward-starting interest rate swap agreements. At September 30, 2007, the swaps were reported at their fair value of \$2,684,000 and are included in other assets and accumulated other comprehensive income.

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| <b>Nature of Critical Accounting Estimate</b>   | <b>Assumptions/Approach Used</b>  |
|---|---|
| <p>Revenue Recognition</p> <p>Revenue is recorded in accordance with Statement of Financial Accounting Standards No. 13, Accounting for Leases, and SEC Staff Accounting Bulletin No. 104, Revenue Recognition in Financial Statements, as amended ( SAB104 ). SAB104 requires that revenue be recognized after four basic criteria are met. These four criteria include persuasive evidence of an arrangement, the rendering of service, fixed and determinable income and reasonably assured collectibility. If the collectibility of revenue is determined incorrectly, the amount and timing of our reported revenue could be significantly affected. Interest income on loans is recognized as earned based upon the principal amount outstanding subject to an evaluation of collectibility risk. Substantially all of our operating leases contain fixed and/or contingent escalating rent structures. Leases with fixed annual rental escalators are generally recognized on a straight-line basis over the initial lease period, subject to a collectibility assessment. Rental income related to leases with contingent rental escalators is generally recorded based on the contractual cash rental payments due for the period.</p>   | <p>We evaluate the collectibility of our revenues and related receivables on an on-going basis. We evaluate collectibility based on assumptions and other considerations including, but not limited to, the certainty of payment, payment history, the financial strength of the investment s underlying operations as measured by cash flows and payment coverages, the value of the underlying collateral and guaranties and current economic conditions.</p> <p>If our evaluation indicates that collectibility is not reasonably assured, we may place an investment on non-accrual or reserve against all or a portion of current income as an offset to revenue.</p> <p>For the nine months ended September 30, 2007, we recognized \$17,673,000 of interest income and \$337,294,000 of rental income, including discontinued operations. Cash receipts on leases with deferred revenue provisions were \$10,791,000 as compared to gross straight-line rental income recognized of \$12,664,000 for the nine months ended September 30, 2007. At September 30, 2007, our straight-line receivable balance was \$55,093,000, net of reserves totaling \$1,152,000. Also at September 30, 2007, we had a loan with an outstanding balance of \$799,000 on non-accrual status.</p> |
| <p><b>Forward-Looking Statements and Risk Factors</b></p> <p>This Quarterly Report on Form 10-Q may contain forward-looking statements as defined in the Private Securities Litigation Reform Act of 1995. These forward-looking statements concern and are based upon, among other things, the possible expansion of the company s portfolio; the sale of properties; the performance of its operators/tenants and properties; its occupancy rates; its ability to acquire or develop properties; its ability to manage properties; its ability to enter into agreements with new viable tenants for vacant space or for properties that the company takes back from financially troubled tenants, if any; its ability to make distributions; its policies and plans regarding investments, financings and other matters; its tax status as a real estate investment trust; its ability to appropriately balance the use of debt and equity; its ability to access capital markets or other sources of funds; its critical accounting policies; and its ability to meet its earnings guidance. When the company uses words such as may, will, intend, should, believe, expect, anticipate, project, estimate or similar expressions, it is making forward-looking statements. Forward-looking statements are not guarantees of future performance and involve risks and uncertainties. The company s expected results may not be achieved, and actual results may differ materially from expectations. This may be a result of various factors, including, but not limited to: the status of the economy; the status of capital markets, including prevailing interest rates; issues facing the health care industry, including compliance with, and changes to, regulations and payment policies and operators /tenants difficulty in cost-effectively obtaining and maintaining adequate liability and other insurance; changes in financing terms; competition within the health care and senior housing industries; negative developments in the operating results or financial condition of operators/tenants, including, but not limited</p> |   |



to, their ability to pay rent and repay loans; the company's ability to transition or sell facilities with a profitable result; the failure of closings to occur as and when anticipated; acts of God affecting the company's properties; the company's ability to timely reinvest sale proceeds at similar rates to assets sold; the company's ability to re-lease space at similar rates as vacancies occur; operator/tenant bankruptcies or insolvencies; government regulations affecting Medicare and Medicaid reimbursement rates; liability or contract claims by or against operators and tenants; unanticipated difficulties and/or expenditures relating to future acquisitions and the integration of multi-property acquisitions; environmental laws affecting the company's properties; changes in rules or practices governing the company's financial reporting; and legal and operational matters, including real estate investment trust qualification and key management personnel recruitment and retention. Other important factors are identified in our Annual Report on Form 10-K/A for the year ended December 31, 2006, including factors identified under the headings "Business," "Risk Factors" and "Management's Discussion and Analysis of Financial Condition and Results of Operations." Finally, we assume no obligation to update or revise any forward-looking statements or to update the reasons why actual results could differ from those projected in any forward-looking statements.

**Table of Contents****Item 3. Quantitative and Qualitative Disclosures about Market Risk**

We are exposed to various market risks, including the potential loss arising from adverse changes in interest rates. We seek to mitigate the effects of fluctuations in interest rates by matching the terms of new investments with new long-term fixed rate borrowings to the extent possible. We may or may not elect to use financial derivative instruments to hedge interest rate exposure. These decisions are principally based on our policy to match our variable rate investments with comparable borrowings, but are also based on the general trend in interest rates at the applicable dates and our perception of the future volatility of interest rates. This section is presented to provide a discussion of the risks associated with potential fluctuations in interest rates.

We historically borrow on our unsecured lines of credit arrangements to acquire, construct or make loans relating to health care and senior housing properties. Then, as market conditions dictate, we will issue equity or long-term fixed rate debt to repay the borrowings under the unsecured lines of credit arrangements.

A change in interest rates will not affect the interest expense associated with our fixed rate debt. Interest rate changes, however, will affect the fair value of our fixed rate debt. Changes in the interest rate environment upon maturity of this fixed rate debt could have an effect on our future cash flows and earnings, depending on whether the debt is replaced with other fixed rate debt, variable rate debt, or equity or repaid by the sale of assets. The following table illustrates the impact of a 1% increase in interest rates on the fair value of our fixed rate debt as of the dates indicated (in thousands):

|   | September 30, 2007 |                      | September 30, 2006 |                      |
|---|--------------------|----------------------|--------------------|----------------------|
|   | Principal balance  | Change in fair value | Principal balance  | Change in fair value |
| Senior unsecured notes  | \$ 1,887,330       | \$ (96,359)          | \$ 1,194,830       | \$ (33,301)          |
| Secured debt  | 512,036            | (24,422)             | 130,405            | (5,445)              |
| Liability to a subsidiary trust issuing preferred securities(1) | 51,000             | (1,618)              |                    |                      |
| Totals  | \$ 2,450,366       | \$ (122,399)         | \$ 1,325,235       | \$ (38,746)          |

(1) At September 30, 2007, we had \$51,000,000 of trust preferred liability principal outstanding with a fixed annual interest rate of 7.22%. On November 6, 2007, we purchased all \$50,000,000 of the outstanding trust preferred securities at par for the purpose

of unwinding  
this financing  
arrangement and  
extinguishing  
the liability of  
an operating  
partnership to a  
subsidiary trust.  
Please see Note  
N to our  
unaudited  
consolidated  
financial  
statements for  
additional  
information.

On September 12, 2007, we entered into two forward-starting interest rate swaps ( the 2007 Swaps ) for a total notional amount of \$250,000,000 to hedge 10 years of interest payments associated with a long-term borrowing that is expected to occur in 2008. The 2007 Swaps each have an effective date of September 12, 2008 and a maturity date of September 12, 2018. We expect to settle the 2007 Swaps when the debt is priced. The 2007 Swaps have the economic effect of fixing \$250,000,000 of our future debt at 4.469% for 10 years. The 2007 Swaps have been designated as cash flow hedges and we expect the 2007 Swaps to be highly effective at offsetting changes in cash flows of interest payments on \$250,000,000 of our future debt due to changes in the LIBOR swap rate. Therefore, effective changes in the fair value of the 2007 Swaps will be recorded in accumulated other comprehensive income and reclassified to interest expense when the hedged forecasted transactions affect earnings (as interest payments are made on the expected debt issuance). The ineffective portion of the changes in fair value will be recorded directly in earnings. At September 30, 2007, the 2007 Swaps were reported at their fair value of \$2,684,000 and are included in other assets and accumulated other comprehensive income. A 1% increase in interest rates would result in an increase in fair value of our 2007 Swaps by approximately \$17,463,000 at September 30, 2007.

Our variable rate debt, including our unsecured lines of credit arrangements, is reflected at fair value. At September 30, 2007, we had \$145,000,000 outstanding related to our variable rate debt and assuming no changes in outstanding balances, a 1% increase in interest rates would result in increased annual interest expense of \$1,450,000. At September 30, 2006, we had \$276,000,000 outstanding related to our variable rate debt and assuming no changes in outstanding balances, a 1% increase in interest rates would have resulted in increased annual interest expense of \$2,760,000.

We are subject to risks associated with debt financing, including the risk that existing indebtedness may not be refinanced or that the terms of refinancing may not be as favorable as the terms of current indebtedness. The majority of our borrowings were completed under indentures or contractual agreements that limit the amount of indebtedness we may incur. Accordingly, in the event that we are unable to raise additional equity or borrow money because of these limitations, our ability to acquire additional properties may be limited.

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**Item 4. Controls and Procedures**

Our management, under the supervision and with the participation of our Chief Executive Officer and Chief Financial Officer, has evaluated the effectiveness of our disclosure controls and procedures (as defined in Rule 13a-15(e) of the Securities Exchange Act of 1934, as amended (the Exchange Act)) as of the end of the period covered by this Quarterly Report on Form 10-Q. Based on that evaluation, the Chief Executive Officer and Chief Financial Officer have concluded that our disclosure controls and procedures are effective in providing reasonable assurance that information required to be disclosed by us in the reports we file with or submit to the Securities and Exchange Commission (SEC) under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in the SEC's rules and forms. No changes in our internal control over financial reporting (as defined in Rule 13a-15(f) under the Exchange Act) occurred during the fiscal quarter covered by this Quarterly Report on Form 10-Q that have materially affected, or are reasonably likely to materially affect our internal control over financial reporting.

**PART II. OTHER INFORMATION**

**Item 1A. Risk Factors**

Except as provided in Item 2 Management's Discussion and Analysis of Financial Condition and Results of Operations Forward Looking Statements and Risk Factors, there have been no material changes from the risk factors identified under the heading Risk Factors in our Annual Report on Form 10-K/A for the year ended December 31, 2006.

**Item 6. Exhibits**

- 4.1 Indenture, dated as of November 20, 2006, between Health Care REIT, Inc. and The Bank of New York Trust Company, N.A. (filed with the SEC as Exhibit 4.1 to Health Care REIT, Inc.'s Form 8-K filed November 20, 2006, and incorporated herein by reference thereto).
- 4.2 Supplemental Indenture No. 1, dated as of November 20, 2006, between Health Care REIT, Inc. and The Bank of New York Trust Company, N.A. (filed with the SEC as Exhibit 4.2 to Health Care REIT, Inc.'s Form 8-K filed November 20, 2006, and incorporated herein by reference thereto).
- 4.3 Supplemental Indenture No. 2, dated as of July 20, 2007, between Health Care REIT, Inc. and The Bank of New York Trust Company, N.A. (filed with the SEC as Exhibit 4.1 to Health Care REIT, Inc.'s Form 8-K filed July 20, 2007, and incorporated herein by reference thereto).
- 10.1 Fourth Amended and Restated Loan Agreement, dated as of August 6, 2007, by and among Health Care REIT, Inc. and certain of its subsidiaries, the banks signatory thereto, KeyBank National Association, as administrative agent, Deutsche Bank Securities Inc., as syndication agent, and UBS Securities LLC, Bank of America, N.A., JPMorgan Chase Bank, N.A., Barclays Bank PLC, Calyon New York Branch and Fifth Third Bank, as documentation agents (filed with the SEC as Exhibit 10.2 to Health Care REIT, Inc.'s Form 10-Q filed August 9, 2007, and incorporated herein by reference thereto).
- 31.1 Rule 13a-14(a)/15d-14(a) Certification of Chief Executive Officer.
- 31.2 Rule 13a-14(a)/15d-14(a) Certification of Chief Financial Officer.
- 32.1 Certification pursuant to 18 U.S.C. Section 1350 by Chief Executive Officer.
- 32.2 Certification pursuant to 18 U.S.C. Section 1350 by Chief Financial Officer.

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

**HEALTH CARE REIT, INC.**

Date: November 7, 2007

By: /s/ George L. Chapman  
George L. Chapman,  
Chairman and Chief Executive Officer  
(Principal Executive Officer)

Date: November 7, 2007

By: /s/ Scott A. Estes  
Scott A. Estes,  
Senior Vice President and Chief  
Financial Officer (Principal Financial  
Officer)

Date: November 7, 2007

By: /s/ Paul D. Nungester, Jr.  
Paul D. Nungester, Jr.,  
Vice President and Controller (Principal  
Accounting Officer)