

KINDRED HEALTHCARE, INC
Form DEF 14A
March 30, 2006

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

SCHEDULE 14A INFORMATION

PROXY STATEMENT PURSUANT TO SECTION 14(a)
OF THE SECURITIES EXCHANGE ACT OF 1934

Filed by the Registrant

Filed by a Party other than the Registrant

Check the appropriate box:

- Preliminary Proxy Statement
- Definitive Proxy Statement
- Definitive Additional Materials
- Soliciting Material Pursuant to Rule 14a-12

**CONFIDENTIAL, FOR USE OF THE COMMISSION
ONLY (AS PERMITTED BY RULE 14A-6(E)(2))**

KINDRED HEALTHCARE, INC.

(Name of Registrant as Specified in Its Charter)

(Name of Person(s) Filing Proxy Statement, if other than the Registrant)

Payment of Filing Fee (Check the appropriate box):

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(2) Aggregate number of securities to which transaction applies:

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(1) Amount Previously Paid:

(2) Form, Schedule or Registration Statement No.:

(3) Filing Party:

(4) Date Filed:

KINDRED HEALTHCARE, INC.

March 30, 2006

Dear Shareholder:

You are cordially invited to attend the Annual Meeting of Shareholders of Kindred Healthcare, Inc. (Kindred), to be held at 10:00 a.m. (EDT) on Thursday, May 25, 2006, at Kindred s principal office at 680 South Fourth Street, Louisville, Kentucky 40202-2412.

Information concerning the business to be conducted at the meeting is included in the accompanying Notice of Annual Meeting of Shareholders and Proxy Statement. Please give all of the information contained in the Proxy Statement your careful attention.

YOUR VOTE IS VERY IMPORTANT. Whether or not you plan to attend the meeting, it is important that your shares be represented. Therefore, we urge you to sign, date and promptly return the enclosed proxy in the enclosed postage paid envelope. Please refer to the enclosed voting form for instructions. If you attend the meeting, you will, of course, have the right to vote in person.

I look forward to greeting you personally, and on behalf of the Board of Directors and management, I would like to express our appreciation for your interest in Kindred.

Sincerely,

Paul J. Diaz

President and Chief Executive Officer

Kindred Healthcare, Inc.

680 South Fourth Street

Louisville, Kentucky 40202-2412

KINDRED HEALTHCARE, INC.

680 SOUTH FOURTH STREET

LOUISVILLE, KENTUCKY 40202-2412

NOTICE OF ANNUAL MEETING OF SHAREHOLDERS

TO BE HELD ON MAY 25, 2006

To the Shareholders of Kindred Healthcare, Inc.:

The Annual Meeting of Shareholders of Kindred Healthcare, Inc. (Kindred) will be held at 10:00 a.m. (EDT) on Thursday, May 25, 2006, at Kindred s principal office at 680 South Fourth Street, Louisville, Kentucky 40202-2412 for the following purposes:

- (1) To elect a board of eight directors;
- (2) To ratify the appointment of PricewaterhouseCoopers LLP as Kindred s independent auditor for fiscal year 2006;
- (3) To consider a shareholder proposal to urge the Board of Directors to arrange for the spin-off of Kindred s pharmacy division to its shareholders; and
- (4) To transact such other business as may properly come before the meeting.

Only shareholders of record at the close of business on March 29, 2006 will be entitled to notice of, and to vote at, the meeting and any adjournments thereof.

IT IS IMPORTANT THAT YOU VOTE YOUR SHARES. WHETHER YOU PLAN TO ATTEND THE MEETING OR NOT, PLEASE SUBMIT YOUR PROXY AS SOON AS POSSIBLE IN THE ENCLOSED POSTAGE PAID ENVELOPE IN ORDER TO AVOID ADDITIONAL SOLICITING EXPENSES TO KINDRED. THE PROXY IS REVOCABLE AND WILL NOT AFFECT YOUR RIGHT TO VOTE IN PERSON IN THE EVENT YOU FIND IT CONVENIENT TO ATTEND THE MEETING.

March 30, 2006

Paul J. Diaz

President and Chief Executive Officer

PROXY STATEMENT

FOR ANNUAL MEETING OF SHAREHOLDERS

TO BE HELD ON MAY 25, 2006

GENERAL INFORMATION

This Proxy Statement and the accompanying form of proxy are furnished in connection with the solicitation of proxies by the Board of Directors of Kindred Healthcare, Inc. (Kindred or the Company) for use at the Annual Meeting of Shareholders (the Annual Meeting), to be held at 10:00 a.m. (EDT) on May 25, 2006, at the Company's principal office at 680 South Fourth Street, Louisville, Kentucky 40202-2412, and at any adjournment or postponement thereof. Only shareholders of record on the books of the Company at the close of business on March 29, 2006 will be entitled to notice of, and to vote at, the Annual Meeting. This Proxy Statement is dated March 30, 2006 and will be mailed to shareholders on or about April 4, 2006.

Proxies are solicited by the Board of Directors in order to provide each shareholder an opportunity to vote on all matters scheduled to come before the Annual Meeting, whether or not he or she attends the Annual Meeting in person. When the enclosed proxy card is returned properly signed, the shares represented by the proxy card will be voted by the proxy holders named on the proxy card in accordance with the shareholder's directions. You are urged to specify your choice by marking the appropriate box on the proxy card. If the proxy card is signed and returned without specifying a choice, the shares will be voted as recommended by the Board of Directors.

The cost of preparing, assembling and mailing the notice of the Annual Meeting, Proxy Statement and proxy card will be borne by the Company. In addition to the use of the mail, proxies may be solicited by directors, officers and other employees of the Company, without additional compensation, in person, by telephone or other electronic means. Furthermore, the Company may retain an investor relations firm to solicit proxies from brokers, banks and institutional holders by telephone or mail. Kindred will reimburse brokerage houses and other nominees for their expenses in forwarding proxy materials to beneficial owners of the Company's common stock.

Revocability of Proxy

Executing and returning the enclosed proxy card will not affect your right to attend the Annual Meeting and vote in person. If you do attend, you may vote by ballot at the Annual Meeting, thereby effectively canceling any proxies previously given. In addition, a shareholder giving a proxy may revoke it at any time before it is voted at the Annual Meeting by filing with the Corporate Secretary of the Company any instrument revoking it, or by filing with the Company a duly executed proxy bearing a later date.

Voting Rights and Outstanding Shares

Each share of common stock, \$0.25 par value (Common Stock), of the Company outstanding at the close of business on March 29, 2006 is entitled to one vote at the Annual Meeting. As of March 29, 2006, there were 38,884,519 shares of Common Stock outstanding.

The presence at the Annual Meeting in person or by proxy of holders of record of a majority of the outstanding shares of Common Stock is required to constitute a quorum for the transaction of all business at the Annual Meeting. The vote of a plurality of the outstanding shares of Common Stock present in person or by proxy will be necessary to elect the director-nominees listed in this Proxy Statement. The affirmative vote of a majority of the outstanding shares of Common Stock present in person or by proxy will be necessary (1) to ratify the appointment of PricewaterhouseCoopers LLP as the Company's independent auditor for fiscal year 2006, (2) to approve a shareholder proposal to urge the Board of Directors to arrange for the spin-off of the Company's pharmacy division to its shareholders, and (3) to approve any other matters that may properly come before the

Annual Meeting for shareholder consideration. Abstentions and proxies relating to street name shares for which brokers have not received voting instruction from the beneficial owner (Broker Non-Votes) are counted in determining whether a quorum is present. In the election of directors, the nominees receiving the highest number of votes will be elected. Therefore, abstentions or Broker Non-Votes for a director-nominee will have no effect. With respect to any matters submitted to the shareholders for their consideration other than the election of directors, abstentions will be counted as shares present and entitled to vote on such proposals in determining whether the proposals have received the requisite number of favorable votes, whereas Broker Non-Votes will not be counted as shares present and entitled to vote on such proposals. Thus, abstentions will have the same effect as votes against any such proposal, whereas Broker Non-Votes will have no effect in determining whether any such proposal has been approved by the shareholders. Therefore, it is important that you complete and return your proxy early so that your vote may be recorded.

Votes cast by proxy or in person at the Annual Meeting will be tabulated by the inspectors of election appointed for the Annual Meeting, who also will determine whether a quorum is present.

1. PROPOSAL TO ELECT DIRECTORS

The Board of Directors of the Company (the Board or the Board of Directors) currently consists of eight persons. The Board of Directors has nominated the eight persons listed below to be elected as directors at the Annual Meeting. Each director elected at the Annual Meeting will serve, subject to the provisions of the Company s bylaws, until the next annual meeting of shareholders and until his successor is duly elected and qualified. The names and ages of the nominees proposed for election as directors, all of whom are presently directors of the Company, together with certain information concerning the nominees, are set forth below.

THE BOARD OF DIRECTORS RECOMMENDS A VOTE FOR THE ELECTION AS DIRECTORS OF EACH OF THE NOMINEES LISTED BELOW.

Nominees For Director

EDWARD L. KUNTZ (60) has served as the Executive Chairman of the Board of Directors since January 1, 2004. He served as the Company s Chairman of the Board and Chief Executive Officer from January 1999 to December 31, 2003. He served as President of the Company from November 1998 until January 2002. He also served as Chief Operating Officer and a director of the Company from November 1998 to January 1999. Mr. Kuntz was Chairman and Chief Executive Officer of Living Centers of America, Inc., a leading provider of long-term healthcare, from 1992 to 1997. Mr. Kuntz is a director of Rotech Healthcare, Inc., a provider of home medical equipment and related products and services.

THOMAS P. COOPER, M.D. (61) has served as a director of the Company since May 22, 2003. Dr. Cooper is the founder, Chairman and Chief Executive Officer of Vericare, Inc., a provider of mental health services to patients in long-term care facilities, since 1991. Dr. Cooper also is an adjunct professor at the Columbia University School of Business. From November 2000 to December 2001, Dr. Cooper was the Chief Executive Officer of Oncall Healthcare, Inc., a start-up venture that provided nurse triage services. He also was the founder and Chief Executive Officer of Cove Healthcare, Inc., a provider of physician hospitalists to acute care hospitals, from June 1997 to November 1999. Dr. Cooper is a director of Hanger Orthopedic Group, Inc., the largest operator of orthotic and prosthetic patient-care centers in the United States. (1)(2)

PAUL J. DIAZ (44) has served as a director of the Company since May 2002, as Chief Executive Officer of the Company since January 1, 2004 and as President of the Company since January 2002. He served as the Chief Operating Officer of the Company from January 2002 to December 31, 2003. From 1996 to July 1998, he served in various executive capacities with Mariner Health Group, Inc. (Mariner Health), a long-term healthcare provider, most recently as Executive Vice President and Chief Operating Officer. Prior to joining

Mariner Health, Mr. Diaz was Chief Executive Officer of Allegis Health Services, Inc., a long-term healthcare provider, where he also previously served as Chief Financial Officer and General Counsel. Since leaving Mariner Health and prior to joining the Company, he served as the managing member of Falcon Capital Partners, LLC, a private investment and consulting firm specializing in healthcare restructurings, and as Chairman and Chief Executive Officer of Capella Senior Living, LLC, a start-up venture to provide long-term healthcare services.

MICHAEL J. EMBLER (41) has served as a director of the Company since July 2001. Since July 2001, Mr. Emblar has served as an officer of Franklin Mutual Advisers, LLC, an investment advisory firm. From October 1992 to May 2001, he served in various positions with Nomura Holding America, Inc., an investment advisory firm, most recently as Managing Director. Mr. Emblar is a director of AboveNet, Inc., a telecommunication services company. (1)(2)(3)

GARRY N. GARRISON (59) has served as a director of the Company since April 2001. From 1997 to 2000, Mr. Garrison served as Senior Vice President of Dynamic Healthcare Solutions, Inc., a venture capital firm specializing in high-growth, health related businesses. From 1996 to 1997, he served as President and Chief Executive Officer, Specialty Services Division of Foundation Health Systems, Inc., an integrated managed care organization, overseeing operations for various specialty services companies. Mr. Garrison also served as President and Chief Operating Officer of Integrated Pharmaceutical Services from 1994 to 1996. (1)(2)

ISAAC KAUFMAN (58), a certified public accountant, has served as a director of the Company since April 2001. Since September 1998, Mr. Kaufman has served as the Senior Vice President and Chief Financial Officer of Advanced Medical Management Inc., a manager of medical practices and an outpatient surgical center. From February 1998 to September 1998, he served as the Chief Financial Officer of Bio Science Contract Production Corp., a contract manufacturer of bulk pharmaceuticals and biologics. Mr. Kaufman also served as Chief Financial Officer of VSI Group, Inc. from October 1996 to February 1998. Mr. Kaufman is a director of TransWorld Entertainment Corporation, a leading specialty retailer of music and video products, and Hanger Orthopedic Group, Inc., the largest operator of orthotic and prosthetic patient care centers in the United States. (3)(4)

JOHN H. KLEIN (59) has served as a director of the Company since April 2001. Mr. Klein has served as Chairman and Managing Director of Aston Partners, a private equity fund, since 2001. He also has served as Chairman and Chief Executive Officer of DAVA Pharmaceuticals Co., a generic pharmaceutical company, since March 2004. He has been the Chairman and Chief Executive Officer of Strategic Business and Technology Solutions, LLC, a strategic business and technology advisory firm, since June 1998. Mr. Klein also has served as the Chairman and Chief Executive Officer of BI Logix, Inc., a business intelligence software solutions company, since May 1998. In addition, he has served as Chairman and Chief Executive Officer of DentalLine.com, a group benefit and internet company, since July 1999. From March 1998 to August 2000, he served as Director and Vice Chairman of Image Vision, a developer and marketer of imaging systems and products. (1)(3)(4)(5)

EDDY J. ROGERS, JR. (65) has served as a director of the Company since August 12, 2003. Mr. Rogers has been a partner with the law firm of Andrews Kurth LLP since October 2001. From January 1995 to October 2001, he was a partner with the law firm of Mayor, Day, Caldwell & Keeton, L.L.P., a firm which merged with Andrews Kurth. (3)(4)

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- (1) Member of the Executive Compensation Committee, of which Mr. Klein is Chairman.
 - (2) Member of the Compliance and Quality Committee, of which Dr. Cooper is Chairman.
 - (3) Member of the Nominating and Governance Committee, of which Mr. Klein is Chairman.
 - (4) Member of the Audit Committee, of which Mr. Kaufman is Chairman.
 - (5) Mr. Klein serves as the lead independent director for the Board of Directors.

As noted above, Mr. Diaz served as Executive Vice President and Chief Operating Officer of Mariner Health until July 1998. On July 31, 1998, Paragon Health Network, Inc., the predecessor to Mariner Post-Acute

Networks, Inc. (Mariner Post-Acute) acquired Mariner Health. Mariner Post-Acute and substantially all of its subsidiaries, including Mariner Health, filed voluntary petitions under Chapter 11 of Title 11 of the United States Bankruptcy Code in the United States Bankruptcy Court for the District of Delaware on January 18, 2000.

The information contained in this Proxy Statement concerning the nominees is based upon statements made or confirmed to the Company by or on behalf of such nominees, except to the extent certain information appears in its records. Directors' ages are given as of January 1, 2006.

SHARES OF COMMON STOCK OF THE COMPANY REPRESENTED BY PROXIES EXECUTED AND RECEIVED IN THE ACCOMPANYING FORM WILL BE VOTED FOR THE ELECTION AS DIRECTORS OF ALL OF THE NOMINEES, UNLESS OTHERWISE SPECIFIED ON THE PROXY. The Board of Directors does not contemplate that any of the nominees will be unable to serve as a director. However, in the event that one or more nominees are unable or unwilling to accept or are unavailable to serve, the persons named in the proxies or their substitutes will have the authority, according to their judgment, to vote or refrain from voting for other individuals as directors.

CERTAIN INFORMATION CONCERNING THE BOARD OF DIRECTORS

The Board of Directors has determined that the following six directors are independent, as defined under the listing standards of the New York Stock Exchange (NYSE) and the Nasdaq Stock Market (NASDAQ): Thomas P. Cooper, M.D., Mr. Michael J. Embler, Mr. Garry N. Garrison, Mr. Isaac Kaufman, Mr. John H. Klein and Mr. Eddy J. Rogers, Jr. The Board's determination was based on a review in which each director's independence was evaluated on a case-by-case basis. The Board considered any matters that could affect the ability of each outside director to exercise independent judgment in carrying out his responsibilities as a director, including all transactions and relationships between each such director, the director's family members and organizations with which the director or the director's family members have an affiliation and the Company, its subsidiaries and its management. Any such matters were evaluated both from the standpoint of the director and from that of persons or organizations with which the director has an affiliation. These independent directors have regularly scheduled meetings at which members of management are not present.

During 2005, the Board of Directors held 11 meetings, including five regular and six special meetings. Each director attended more than 75% of the total number of meetings of the Board and the applicable committees during the periods on which each served. The Board of Directors has established an Audit Committee, a Compliance and Quality Committee, an Executive Compensation Committee, and a Nominating and Governance Committee. Each committee has a written charter which is available on the Company's website at www.kindredhealthcare.com. The Company's Corporate Governance Guidelines also are available on the Company's website at www.kindredhealthcare.com. Information on the Company's website is not part of this Proxy Statement. Shareholders may request a copy of the charters or the Corporate Governance Guidelines by contacting the Company, care of the Corporate Secretary, at the Company's principal office.

Audit Committee. The Audit Committee has three members consisting of Mr. Isaac Kaufman (Chairman), Mr. John H. Klein and Mr. Eddy J. Rogers, Jr. Each member of the Audit Committee is independent as defined under the listing standards of the NYSE and NASDAQ. The Board of Directors has determined that Mr. Kaufman is the Audit Committee's financial expert as defined in Item 401 of Regulation S-K promulgated under the Securities Act of 1933, as amended, and the Securities Exchange Act of 1934, as amended. The Audit Committee held eight meetings during 2005. The Audit Committee assists the Board of Directors in monitoring (1) the adequacy of the Company's system of internal controls, accounting policies, financial reporting practices, and the quality and integrity of the Company's financial reporting; (2) the independent auditor's qualifications and independence; and (3) the performance of the Company's internal audit function and independent auditor.

Compliance and Quality Committee. The Compliance and Quality Committee has three members consisting of Thomas P. Cooper, M.D. (Chairman), Mr. Michael J. Embler and Mr. Garry N. Garrison. Each

member of the Compliance and Quality Committee is independent as defined under the listing standards of the NYSE and NASDAQ. The Compliance and Quality Committee held five meetings in 2005. The Compliance and Quality Committee assists the Board of Directors in monitoring (1) the Company's compliance with applicable laws, regulations and policies; (2) the Company's compliance with its Corporate Integrity Agreement and its Code of Conduct; and (3) the Company's programs, policies and procedures that support and enhance the quality of care provided by the Company.

Executive Compensation Committee. The Executive Compensation Committee has four members consisting of Mr. John H. Klein (Chairman), Thomas P. Cooper, M.D., Mr. Michael J. Embler and Mr. Garry N. Garrison. Each member of the Executive Compensation Committee is independent as defined under the listing standards of the NYSE and NASDAQ. The Executive Compensation Committee held seven meetings in 2005. The Executive Compensation Committee assists the Board of Directors in fulfilling its responsibility to the shareholders, potential shareholders and the investment community by ensuring that the Company's key executives, officers and Board members are compensated in accordance with the Company's overall compensation policies and executive compensation policies. The Executive Compensation Committee recommends and approves compensation policies, programs and pay levels that are necessary to support the Company's objectives and that are rational and reasonable to the value of the services rendered.

Nominating and Governance Committee. The Nominating and Governance Committee has four members consisting of Mr. John H. Klein (Chairman), Mr. Michael J. Embler, Mr. Isaac Kaufman and Mr. Eddy J. Rogers, Jr. Each member of the Nominating and Governance Committee is independent as defined under the listing standards of the NYSE and NASDAQ. The Nominating and Governance Committee held five meetings in 2005. The Nominating and Governance Committee assists the Board of Directors by (1) identifying individuals qualified to become Board members, and approving the director nominees for the next annual meeting of shareholders and approving nominees to fill vacancies on the Board; (2) recommending to the Board nominees for director and chairperson(s) for each committee; (3) leading the Board in its annual review of the Board's performance; and (4) recommending to the Board the corporate governance guidelines applicable to the Company.

It is the policy of the Nominating and Governance Committee to consider director candidates recommended by shareholders who appear to be qualified to serve on the Company's Board of Directors. The Committee has not established any specific qualifications for directors. The Nominating and Governance Committee may choose not to consider an unsolicited recommendation if no vacancy exists on the Board of Directors. The Nominating and Governance Committee may recommend increasing the size of the Board of Directors if it perceives specialized needs for the Board of Directors and if qualified director candidates are identified. In order to avoid the unnecessary use of the Nominating and Governance Committee's resources, the Nominating and Governance Committee will consider only those director candidates recommended in accordance with the procedures set forth below. There have been no material changes to the procedures by which shareholders may recommend director candidates since the Company last disclosed such procedures.

To submit a recommendation of a director candidate to the Nominating and Governance Committee, a shareholder should submit the following information in writing, addressed to the Chairman of the Nominating and Governance Committee, care of the Corporate Secretary, at the Company's principal office:

1. The name of the person recommended as a director candidate;
2. All information relating to such person that is required to be disclosed in solicitations of proxies for election of directors pursuant to Regulation 14A promulgated under the Securities Exchange Act of 1934, as amended;
3. The written consent of the person being recommended as a director candidate to being named in the proxy statement as a nominee and to serving as a director if elected;

4. As to the shareholder making the recommendation, the name and address, as they appear on the Company's books, of such shareholder; provided, however, that if the shareholder is not a registered holder of the Company's Common Stock, the shareholder should submit his or her name and address along with a current written statement from the record holder of the shares that reflects ownership of the Company's Common Stock, and the number and class of all shares of each class of stock of the Company owned of record or beneficially by such holder; and

5. A statement disclosing whether such shareholder is acting with or on behalf of any other person and, if applicable, the identity of such person.

In order for a director candidate to be considered for nomination at the Company's annual meeting of shareholders to be held in 2007, the recommendation must be received in accordance with the requirements for other shareholder proposals. See Shareholder Proposals and Director Nominations.

The Nominating and Governance Committee has generally identified director nominees based upon suggestions by outside directors, management members and/or shareholders, and has interviewed and evaluated those persons on its own. On occasion, the Company employs outside search firms to identify and screen potential director candidates. The Company seeks directors who possess integrity, a high level of education and business experience, broad-based business acumen, an understanding of the Company's businesses and the healthcare industry generally, strategic thinking and a willingness to share ideas, a network of contacts and diversity of experiences, expertise and background. The Nominating and Governance Committee uses these criteria to evaluate potential nominees, and does not evaluate proposed nominees differently depending upon who has made the proposal.

Attendance at the Annual Meeting. The Board of Directors does not require directors to attend the annual meeting of shareholders. Mr. Diaz was the only director in attendance at the 2005 annual meeting of shareholders.

COMPENSATION OF DIRECTORS

During 2005, non-employee directors received (1) \$3,000 for each Board meeting attended and \$2,000 for each committee meeting attended unless the meeting was held telephonically; (2) \$1,000 for each telephonic meeting of the Board or any committee meeting attended; (3) a \$12,000 quarterly retainer; and (4) an additional \$2,500 quarterly retainer for the Audit Committee chairman and an additional \$2,000 quarterly retainer for the other committee chairmen. In addition, the lead independent director received a quarterly retainer of \$2,000.

Pursuant to the Company's 2001 Stock Option Plan for Non-Employee Directors (the Directors Plan), on January 10, 2005 the Company issued to each non-employee director an option to purchase 5,000 shares of Common Stock having an exercise price of \$27.90 per share. These options are exercisable in four equal annual installments beginning on the first anniversary of their grant date and have a ten-year term. Pursuant to the Directors Plan, the Company issues, on January 10 of each year during the term of the Directors Plan, an option to purchase 5,000 shares of Common Stock to each non-employee director. These options will have an exercise price equal to the fair market value of the Common Stock on the date the option is granted, vest in four equal annual installments beginning on the first anniversary of their date of grant, and have a ten-year term.

In addition, upon the appointment or election of a person as a non-employee director for the first time, such director will receive a one-time grant of an option to purchase 15,000 shares of Common Stock under the Directors Plan. These options will have an exercise price equal to the fair market value of the Common Stock on the date the option is granted, vest in four equal annual installments beginning on the first anniversary of their date of grant, and have a ten-year term.

CODE OF ETHICS

The Company has adopted a Code of Conduct that serves as its code of ethics and applies to all of the Company's employees, including the principal executive officer, principal financial officer, principal accounting officer, and certain other persons performing similar functions. The text of the Company's Code of Conduct is posted on the Company's website located at www.kindredhealthcare.com under the Investor Information section and is available in print to any requesting shareholder. In addition, the Company intends to disclose on its website (1) the nature of any amendment to a provision of the Code of Conduct that applies to the Company's principal executive officer, principal financial officer, principal accounting officer, or persons performing similar functions and (2) the nature of any waiver, including an implied waiver, from provisions of the Code of Conduct that is granted to one of these specified individuals, the name of the person to whom the waiver was granted and the date of the waiver. Such disclosure will be made within five business days following the date of the applicable amendment or waiver. Information contained on the Company's website is not part of this Proxy Statement.

SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT

The following table sets forth certain information regarding beneficial ownership of Common Stock and the Company's Series A and Series B warrants, as of January 1, 2006 (except as otherwise noted), by (1) each shareholder known by the Company to be the beneficial owner of more than 5% of its outstanding shares of Common Stock, (2) each person who is a director or nominee for director, (3) each of the Company's Named Executive Officers (as defined herein), and (4) all of the persons who are directors and executive officers of the Company, as a group.

Name of Beneficial Owner	Amount and Nature of					
	Beneficial Ownership (1)			Percent of Class (1)		
	Common Stock	Series A Warrants	Series B Warrants	Common Stock	Series A Warrants	Series B Warrants
Directors, Nominees and Named Executive Officers						
Edward L. Kuntz	207,631			*		
Paul J. Diaz	776,007			2.1		
Thomas P. Cooper, M.D.	9,250			*		
Michael J. Embler (2) (3)	10,247,808	560,242	1,400,603	24.8	30.1	30.2
Garry N. Garrison	34,750			*		
Isaac Kaufman	34,750			*		
John H. Klein	34,750			*		
Eddy J. Rogers, Jr.	14,250			*		
Richard A. Lechleiter	173,201			*		
Frank J. Battafarano	157,319			*		
Lane M. Bowen	81,997			*		
Richard E. Chapman	99,648			*		
All Directors and Executive Officers as a Group (18 persons) (2)	12,168,581	560,242	1,400,603	28.7	30.1	30.2
Other Security Holders with More than 5% Ownership						
Barclays Global Investors, NA., Barclays Global Fund Advisors, Barclays Global Investors, Ltd., and Barclays Global Investors Japan Trust and Banking Company Limited (4)	5,291,951			14.2		
Boston Partners Asset Management, L.L.C. (5)	1,985,330			5.3		
Dimensional Fund Advisors Inc. (6)	2,412,674			6.5		
Franklin Mutual Advisers, LLC (2)(3)(7)	10,247,808	560,242	1,400,603	24.8	30.1	30.2
Jana Partners LLC (8)	3,650,600			9.8		
Leon G. Cooperman (9)	1,949,100			5.2		

* Denotes less than 1%.

- (1) Includes shares subject to options or warrants and which are exercisable within 60 days from January 1, 2006. Other than shares subject to warrants as expressly indicated in the table, the number of shares of Common Stock that may be acquired through exercise of options, which are exercisable as of, or within 60 days after, January 1, 2006, are as follows: Mr. Kuntz 65,754 shares; Mr. Diaz 443,606 shares; Dr. Cooper 9,250 shares; Mr. Embler 34,750 shares; Mr. Garrison 34,750 shares; Mr. Kaufman 34,750 shares; Mr. Klein 34,750 shares; Mr. Rogers 14,250 shares; Mr. Lechleiter 95,573 shares; Mr. Battafarano 70,966 shares; Mr. Bowen 34,426 shares; and Mr. Chapman 48,530 shares. Unless otherwise noted, the Company believes that all persons named in the table have sole voting and investment power with respect to all shares of Common Stock and/or warrants beneficially owned by them. The total for Mr. Battafarano includes 50 shares held jointly with his mother.

- (2) The number of shares of Common Stock shown in the table includes shares issuable upon the exercise of the Series A warrants and the Series B warrants. Two shares of Common Stock are issuable upon the exercise of each series of warrants. See notes 3 and 7 below.
- (3) Mr. Embler disclaims beneficial ownership of the securities held by Franklin Mutual Advisers, LLC (FMA). In addition, Mr. Embler disclaims beneficial ownership of shares underlying options issued by the Company to Mr. Embler. Mr. Embler is an officer of FMA and serves on the Board at the request of FMA. In accordance with FMA's internal policy, all cash and non-cash compensation issued to Mr. Embler in connection with his service on the Board of Directors has or will be distributed directly to the advisory clients of FMA. See note 7 below.
- (4) Based on a Schedule 13G filed jointly by Barclays Global Investors, NA. (BGI), Barclays Global Fund Advisors (BGFA), Barclays Global Investors, Ltd. (BGIL) and Barclays Global Investors Japan Trust and Banking Company Limited (Barclays Japan) (collectively, Barclays) dated December 31, 2005 with the Securities and Exchange Commission (SEC). According to the Schedule 13G, Barclays has sole power to vote 4,885,161 shares and sole power to dispose of 5,291,951 shares and holds the shares in trust accounts for the economic beneficiaries of the accounts. The address of BGI and BGFA is 45 Fremont Street, San Francisco, CA 94105. The address of BGIL is Murray House, 1 Royal Mint Court, London, EC3N 4HH. The address of Barclays Japan is Ebisu Prime Square Tower, 8th Floor, 1-1-39 Hiroo Shibuya-Ku, Tokyo 150-0012 Japan.
- (5) Based on a Schedule 13G filed by Boston Partners Asset Management, L.L.C. (BPAM) dated December 31, 2005 with the SEC. According to the Schedule 13G, BPAM holds all of these shares under management for its clients. The address for BPAM is 28 State Street, 20th Floor, Boston, Massachusetts 02109.
- (6) Based on a Schedule 13G/A filed by Dimensional Fund Advisors Inc. (Dimensional) dated December 31, 2005 with the SEC. According to the Schedule 13G/A, Dimensional furnishes investment advice to four investment companies and serves as investment manager to certain other commingled group trusts and separate accounts (collectively, the Funds). According to the Schedule 13G/A, Dimensional, in its role as investment advisor or manager, possesses investment and/or voting power over these shares that are owned by the Funds. Dimensional disclaims beneficial ownership of these shares. The address of Dimensional is 1299 Ocean Avenue, 11th Floor, Santa Monica, California 90401.
- (7) FMA has advised the Company that advisory clients of FMA own the referenced securities. FMA has indicated that the Common Stock and warrants are beneficially owned by one or more open-end investment companies or other management accounts of FMA. Under its advisory contracts, FMA has sole voting and investment power over these securities owned by its clients which FMA manages. The number of shares of Common Stock shown in the table includes shares issuable upon the exercise of 560,242 Series A warrants and 1,400,603 Series B warrants which are currently exercisable. Michael J. Embler is an officer of FMA. Mr. Embler and FMA disclaim beneficial ownership of the securities held by FMA. See notes 2 and 3 above. The address of FMA is 101 John F. Kennedy Parkway, Short Hills, New Jersey 07078.
- (8) Based on a Schedule 13G filed by Jana Partners LLC (Jana) dated January 11, 2006 with the SEC. According to the Schedule 13G, Jana is a private money management firm which holds the shares in various accounts under its management and control. The address of Jana is 201 Post Street, Suite 1000, San Francisco, California 94108.
- (9) Based on a Schedule 13G filed with the SEC by Leon G. Cooperman (Cooperman) in his capacity as Managing Member of Omega Associates, L.L.C. (Associates) and President and majority stockholder of Omega Advisors, Inc. (Advisors), dated January 27, 2006. Associates is the general partner of Omega Capital Partners, L.P. (Capital LP), Omega Equity Investors, L.P. (Equity LP) and Omega Capital Investors, L.P. (Investors LP). Advisors serves as the investment manager to Omega Overseas Partners, Ltd. (Overseas). According to the Schedule 13G, Cooperman has sole power to vote and dispose of 1,135,100 shares, all of which are owned by Capital LP, Equity LP, Investors LP and Overseas, and shared

power to vote and dispose of 814,000 shares, all of which are owned by managed accounts over which Advisors serves as discretionary investment advisor. The 1,135,100 shares consist of 590,800 shares owned by Capital LP, 116,100 shares owned by Equity LP, 48,000 shares owned by Investors LP and 380,200 shares owned by Overseas. The address of each of Cooperman, Capital LP, Equity LP, Investors LP, Overseas, Associates and Advisors is 88 Pine Street, Wall Street Plaza 31 Floor, New York, New York 10005.

SECTION 16(a) BENEFICIAL OWNERSHIP REPORTING COMPLIANCE

Section 16(a) of the Securities Exchange Act of 1934 requires the Company's directors and executive officers and persons who own more than 10% of the Common Stock to file initial stock ownership reports and reports of changes in ownership with the SEC. Based on a review of these reports and on written representations from the reporting persons that no other reports were required, the Company believes that the applicable Section 16(a) reporting requirements were complied with for all transactions which occurred in 2005 except as follows.

On May 2, 2005, John J. Lucchese, Vice President, Finance and Corporate Controller, was one day late in filing a Form 4 that, as amended, reflected the acquisition of 913 shares of Common Stock.

EXECUTIVE COMPENSATION AND OTHER INFORMATION

The following Summary Compensation Table sets forth compensation earned during the three fiscal years ended December 31, 2005 by (1) the Chief Executive Officer of the Company and (2) the other four most highly compensated executive officers of the Company (collectively, the Named Executive Officers).

Summary Compensation Table

Name and Principal Position	Year	Annual Compensation			Long-Term Compensation		All Other Compensation(8)
		Salary	Bonus(1)	Other Annual Compensation(2)	Restricted Stock Awards(3)	Securities Underlying Options	
Paul J. Diaz President and Chief Executive Officer	2005	\$ 828,000	\$ 1,449,000	\$ 64,498	\$ 4,121,111(4)	160,507	\$ 7,831
	2004	800,000	1,400,000	51,289	1,204,414(5)	67,220	
	2003	618,000	1,142,585	52,343	3,007,615(6)	197,184(7)	
Richard A. Lechleiter Executive Vice President and Chief Financial Officer	2005	\$ 356,070	\$ 606,339		\$ 1,134,599(4)	36,418	\$24,991
	2004	317,240	523,446		272,442(5)	15,206	20,288
	2003	309,500	596,934		209,453(6)	25,330(7)	21,256
Frank J. Battafarano Executive Vice President and President, Hospital Division	2005	\$ 368,200	\$ 590,820		\$ 1,412,696(4)	47,471	\$39,298
	2004	328,080	541,332		272,442(5)	15,206	37,499
	2003	309,500	613,183		209,453(6)	25,330(7)	35,034
Lane M. Bowen Executive Vice President and President, Health Services Division	2005	\$ 356,070	\$ 571,339		\$ 824,821(4)	24,357	\$35,647
	2004	317,240	523,446		272,442(5)	15,206	19,585
	2003	309,500	483,263		209,453(6)	25,330(7)	40,436
Richard E. Chapman Executive Vice President and Chief Administrative and Information Officer	2005	\$ 356,070	\$ 571,339		\$ 970,307(4)	30,019	\$10,250
	2004	317,240	523,446		272,442(5)	15,206	11,062
	2003	309,500	521,934		209,453(6)	25,330(7)	5,000

- (1) The amounts shown include cash bonuses awarded under the Company's short-term incentive plan and amounts earned under the Company's long-term incentive plan. For the periods presented, the amounts earned under the long-term incentive plan by the Named Executive Officers were as follows:

Year	Mr. Diaz	Mr. Lechleiter	Mr. Battafarano	Mr. Bowen	Mr. Chapman
2005	\$ 828,000	\$ 325,080	\$ 336,150	\$ 325,080	\$ 325,080
2004	800,000	285,516	295,272	285,516	285,516
2003	361,530	181,058	181,058	181,058	181,058

Under the long-term incentive plan, amounts are earned based upon annual performance criteria and, subject to continued employment, are paid in equal annual installments over the three succeeding years.

In addition, the amount shown for Mr. Lechleiter for 2005 includes a special bonus of \$35,000 to recognize his efforts in recouping a \$55 million favorable hospital Medicare settlement during 2005. The amounts shown for 2003 also include a special performance award granted to the Company's key employees based upon the successful execution of several strategic and operational initiatives that resulted in a significant enhancement in shareholder value during 2003. The amounts awarded to the Named Executive Officers were as follows: Mr. Diaz \$350,000; Mr. Lechleiter \$200,000; Mr. Battafarano \$200,000; Mr. Bowen \$175,000; and Mr. Chapman \$125,000.

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- (2) These amounts represent (i) transportation-related benefits of \$64,498, \$35,904 and \$38,081 for 2005, 2004 and 2003, respectively, and (ii) cash compensation related to the payment of certain paid time off benefits of \$15,385 and \$14,262 for 2004 and 2003, respectively. For purposes of determining the value of transportation-related benefits for 2005, the Company based the calculation on the aggregate incremental cost to the Company to provide such transportation. The aggregate incremental cost for the Company

aircraft is based on a cost-per-flight-hour charge developed from the annual direct costs to operate the Company's aircraft. The incremental cost for any chartered aircraft is the actual cost of the chartered aircraft paid by the Company. For 2004 and 2003, the value of the transportation-related benefits was based on the taxable value calculated under the per-mile Standard Industry Fare Level rate established by the Department of Transportation.

- (3) As of December 31, 2005, the Named Executive Officers held the following number of shares of restricted common stock with the following values (based upon the closing price of \$25.76 reported on the NYSE for the Common Stock on December 30, 2005): Mr. Diaz 319,829 shares valued at \$8,238,795; Mr. Lechleiter 58,878 shares valued at \$1,516,697; Mr. Battafarano 86,293 shares valued at \$2,222,908; Mr. Bowen 47,571 shares valued at \$1,225,429; and Mr. Chapman 50,944 shares valued at \$1,312,317. The Company has not paid dividends on its Common Stock, but the holder of restricted stock is entitled to dividends if paid.

(4)