

ASSISTED LIVING CONCEPTS INC

Form 10-Q

May 14, 2003

Table of Contents

UNITED STATES SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

Form 10-Q

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

For the quarterly period ended March 31, 2003

or

TRANSITION REPORT PURSUANT TO SECTION 12 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the Transition period from **to**

Commission file number 1-13498

Assisted Living Concepts, Inc.

(Exact name of registrant as specified in its charter)

Nevada
*(State or other jurisdiction of
incorporation or organization)*

93-1148702
*(IRS Employer
Identification No.)*

1349 Empire Central, Suite 900
Dallas, TX 75247
(Address of principal executive offices)

(214)424-4000
(Registrant's telephone number, including area code)

11835 NE Glenn Widing Drive, Building E
Portland, Oregon 97220
(Former name, former address and former fiscal year, if changed since last report)

Indicate by check mark whether Registrant (1) has filed all reports 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 Registrants was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes No

Indicate by check mark whether the registrant is an accelerated filer (as defined in Rule 12b-2 of the Exchange Act).
Yes No

Edgar Filing: ASSISTED LIVING CONCEPTS INC - Form 10-Q

Indicate by check mark whether the registrant has filed all documents and reports required to be filed by Sections 12, 13 or 15(d) of the Securities Exchange Act of 1934 subsequent to the distribution of securities under a plan confirmed by a court.

Yes No

The Registrant had 6,431,759 shares of common stock, \$.01 par value, outstanding at May 8, 2003.

TABLE OF CONTENTS

PART I FINANCIAL INFORMATION

Item 1. Financial Statements

CONSOLIDATED BALANCE SHEETS

CONSOLIDATED STATEMENTS OF OPERATIONS

CONSOLIDATED STATEMENTS OF CASH FLOWS

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

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

Item 3. Quantitative and Qualitative Disclosure About Market Risk

Item 4. Controls and Procedures

PART II OTHER INFORMATION

Item 1. Legal Proceedings

Item 4. Submission of Matters to a Vote of Security Holders

Item 6. Exhibits and Reports on Form 8-K

SIGNATURES

EXHIBIT INDEX

EXHIBIT 12

EXHIBIT 99.1

EXHIBIT 99.2

Table of Contents

ASSISTED LIVING CONCEPTS, INC.

**FORM 10-Q
March 31, 2003**

INDEX

	Page
PART I FINANCIAL INFORMATION	
Item 1. Financial Statements	
Consolidated Balance Sheets, December 31, 2002 and March 31, 2003	2
Consolidated Statements of Operations, Three Months Ended March 31, 2002 and 2003	3
Consolidated Statements of Cash Flows, Three Months Ended March 31, 2002 and 2003	4
Notes to Consolidated Financial Statements	5
Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations	16
Item 3. Quantitative and Qualitative Disclosure About Market Risk	20
Item 4. Controls and Procedures	21
PART II OTHER INFORMATION	
Item 1. Legal Proceedings	21
Item 4. Submission of Matters to a Vote of Security Holders	21
Item 6. Exhibits and Reports on Form 8-K	21

Table of Contents**PART I - FINANCIAL INFORMATION****Item 1. Financial Statements**

ASSISTED LIVING CONCEPTS, INC
CONSOLIDATED BALANCE SHEETS
(In Thousands, Except Share Amounts)

	December 31, 2002	March 31, 2003
(Unaudited)		
ASSETS		
Current assets:		
Cash and cash equivalents	\$ 7,165	\$ 6,736
Cash restricted for resident security deposits	1,929	1,929
Accounts receivable, net of allowance for doubtful accounts of \$230 at December 31, 2002 and \$342 at March 31, 2003	2,715	3,313
Prepaid insurance	343	1,020
Prepaid expenses	991	931
Assets held for sale	9,727	
Cash restricted for workers compensation claims	4,696	4,375
Other current assets	3,193	2,886
Total current assets	30,759	21,190
Restricted cash	5,315	5,323
Property and equipment, net	177,930	184,738
Deferred income taxes		550
Other assets, net	2,036	2,320
Total assets	\$216,040	\$214,121
LIABILITIES AND SHAREHOLDERS EQUITY		
Current liabilities:		
Accounts payable	\$ 769	\$ 1,775
Accrued real estate taxes	4,836	3,626
Accrued interest expense	2,174	1,302
Accrued payroll expense	5,021	4,332
Other accrued expenses	5,718	6,315
Income taxes payable		700
Resident security deposits	1,991	1,776
Other current liabilities	976	449
Current portion of unfavorable lease adjustment	607	598
Current portion of long-term debt and capital lease obligation	11,521	2,701
Total current liabilities	33,613	23,574
Other liabilities	463	574
Unfavorable lease adjustment	2,508	2,362
Long-term debt and capital lease obligations, net of current portion	109,078	108,507
Senior and Junior Secured note	41,993	49,138
Total liabilities	187,655	184,155

Edgar Filing: ASSISTED LIVING CONCEPTS INC - Form 10-Q

Commitments and contingencies		
Shareholders' equity:		
Preferred stock, \$.01 par value; 3,250,000 shares authorized; none issued or outstanding		
Common Stock, \$.01 par value; 20,000,000 shares authorized; issued and outstanding 6,431,759 shares at December 31, 2002 and March 31, 2003 (68,241 shares to be issued upon settlement of pending claims)	65	65
Additional paid-in capital	32,734	33,284
Accumulated deficit	(4,414)	(3,383)
	<u> </u>	<u> </u>
Total shareholders' equity	28,385	29,966
	<u> </u>	<u> </u>
Total liabilities and shareholders' equity	\$216,040	\$214,121
	<u> </u>	<u> </u>

The accompanying notes are an integral part of these consolidated financial statements.

Table of Contents**ASSISTED LIVING CONCEPTS, INC.****CONSOLIDATED STATEMENTS OF OPERATIONS**
(in thousands, except per share amounts)
(unaudited)

	Three Months Ended March 31,	
	2002	2003
Revenue	\$37,014	\$41,144
Operating expenses:		
Residence operating expenses	25,468	27,723
Corporate general and administrative	4,317	4,342
Building rentals	3,038	3,105
Depreciation and amortization	1,612	1,676
Total operating expenses	<u>34,435</u>	<u>36,846</u>
Operating income	2,579	4,298
Other income (expense):		
Interest expense	(3,591)	(3,429)
Interest income	53	36
Other income, net	2	(4)
Total other expense, net	<u>(3,536)</u>	<u>(3,397)</u>
Income (loss) before debt restructure, reorganization costs, and discontinued operations	(957)	901
Debt restructure and reorganization costs	(447)	
Income (loss) from continuing operations before income taxes	(1,404)	901
Income tax expense		364
Income (loss) from continuing operations	(1,404)	537
Discontinued operations:		
Income (loss) from operations (including gain on sale of assets of \$899 in 2003)	(46)	830
Income tax expense		336
Income (loss) from discontinued operations	(46)	494
Net income (loss)	<u>\$ (1,450)</u>	<u>\$ 1,031</u>
Net income (loss) per common share:		
Basic	<u>\$ (0.22)</u>	<u>\$ 0.16</u>
Diluted	<u>\$ (0.22)</u>	<u>\$ 0.16</u>

The accompanying notes are an integral part of these consolidated financial statements.

Table of Contents**ASSISTED LIVING CONCEPTS, INC.****CONSOLIDATED STATEMENTS OF CASH FLOWS****(in thousands)****(unaudited)****Three Months Ended
March 31,****2002****2003**

	2002	2003
Operating Activities:		
Net income (loss)	\$(1,450)	\$ 1,031
Adjustment to reconcile net income (loss) to net cash used in operating activities:		
Depreciation and amortization	1,667	1,676
Amortization of debt issuance costs	20	27
Amortization of fair value adjustment to building rentals	(170)	(155)
Amortization of fair market adjustment to long-term debt	107	97
Amortization of discount on long-term debt	106	135
Straight line adjustment to building rentals	86	111
Interest paid-in-kind	305	330
Provision for doubtful accounts	13	252
Gain on sale of assets		(899)
Changes in assets and liabilities:		
Accounts receivable	(100)	(850)
Prepaid expenses	(2,321)	(617)
Other current assets	245	307
Other assets	(31)	(311)
Accounts payable	(254)	1,006
Accrued expenses	313	(2,174)
Other current liabilities	795	(42)
Other liabilities	(7)	
Net cash used in operating activities	(676)	(76)
Investing Activities:		
Decrease (increase) in restricted cash	(1,719)	313
Purchases of property and equipment	(625)	(427)
Sales of properties		2,569
Net cash provided by (used in) investing activities	(2,344)	2,455
Financing Activities:		
Proceeds from long-term debt	1,000	
Payments on long-term debt and capital lease obligation	(360)	(2,808)
Debt issuance costs	(79)	
Net cash provided by (used in) financing activities	561	(2,808)
Net decrease in cash and cash equivalents	(2,459)	(429)
Cash and cash equivalents, beginning of period	6,077	7,165
Cash and cash equivalents, end of period	\$ 3,618	\$ 6,736
Supplemental disclosure of cash flow information:		
Cash payments for interest	\$ 2,705	\$ 3,847

The accompanying notes are an integral part of these consolidated financial statements.

Table of Contents

ASSISTED LIVING CONCEPTS, INC.

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)**

1. The Company

Assisted Living Concepts, Inc., (the Company) owns, leases and operates assisted living residences which provide housing to older persons who need help with the activities of daily living such as bathing and dressing. The Company provides personal care and support services and makes available routine health care services, as permitted by applicable law, designed to meet the needs of its residents.

2. Basis of Presentation

The condensed consolidated financial statements included herein have been prepared by the Company without audit and in the opinion of management include all adjustments (all of which are normal and recurring) necessary for a fair presentation of the results of operations for the three months ended March 31, 2002 and 2003, pursuant to the rules and regulations of the Securities and Exchange Commission. The accompanying condensed consolidated financial statements include the accounts of the Company and its wholly owned subsidiaries. All significant intercompany accounts and transactions have been eliminated in consolidation. Certain reclassifications have been made to the prior period financial statements to conform to the current period presentation. Certain information and footnote disclosures normally included in financial statements in accordance with accounting principles generally accepted in the United States of America have been condensed or omitted pursuant to such rules and regulations; however the Company believes that the disclosures in the accompanying financial statements are adequate to make the information presented not misleading.

The accompanying condensed consolidated financial statements should be read in conjunction with the Company's annual report on Form 10-K for the fiscal year ended December 31, 2002 filed with the Securities and Exchange Commission. The results of operations for the three months ended March 31, 2003 are not necessarily indicative of the results for a full year.

The results of operations for the three months ended March 31, 2002 and 2003 reflect the continuing operations of 177 residences. Results of operations for five residences sold on September 30, 2002 and two residences sold in March 2003 are included in discontinued operations in the accompanying financial statements. (See Note 5).

Table of Contents**3. Long-Term Debt**

As of December 31, 2002 and March 31, 2003, long-term debt consists of the following (in thousands):

	December 31, 2002		March 31, 2003	
	Carrying Amount	Principal Amount	Carrying Amount	Principal Amount
Trust Deed Notes, payable to the State of Oregon Housing and Community Services Department (OHCS) due 2028	\$ 9,688	\$ 9,585	\$ 9,643	\$ 9,541
Variable Rate Multifamily Revenue Bonds, payable to the Washington State Housing Finance Commission Department due 2028	7,217	7,295	7,218	7,295
Variable Rate Demand Housing Revenue Bonds, Series 1997, payable to the Idaho Housing and Finance Association due 2017	6,277	6,345	6,278	6,345
Variable Rate Demand Housing Revenue Bonds, Series A-1 and A-2 payable to the State of Ohio Housing Finance Agency due 2018	11,451	11,575	10,453	10,575
Housing and Urban Development Insured Mortgages due 2035	7,329	7,410	7,317	7,397
New Senior Secured Notes due 2009	35,750	35,750	34,350	34,350
New Junior Secured Notes due 2012	13,925	16,225	14,788	16,824
Mortgages payable due 2008	27,995	27,948	27,859	27,813
G.E. Capital (Previously Heller Healthcare Finance, Inc.) Credit Facility due 2005	42,691	43,516	42,440	43,171
Capital lease obligations	269	269		3
Total long-term debt	162,592	\$ 165,918	160,346	\$ 163,314
Less current portion	11,521		2,701	
Long-term debt	\$ 151,071		\$ 157,645	

The Trust Deed Notes payable to OHCS are secured by buildings, land, furniture and fixtures of six Oregon residences. The notes are payable in monthly installments including interest at effective rates ranging from 7.375% to 9.0%.

The Variable Rate Multifamily Revenue Bonds are payable to the Washington State Housing Finance Commission Department and at March 31, 2003 are secured by a \$7.3 million letter of credit and by buildings, land, furniture and fixtures of the five Washington residences. The letter of credit expires in January 2004 and had an interest rate of 1.3% at March 31, 2003.

The Variable Rate Demand Housing Revenue Bonds, Series 1997 are payable to the State of Idaho Housing and Finance Association and at March 31, 2003 are secured by a \$6.3 million letter of credit and by buildings, land, furniture and fixtures of four Idaho residences. The letter of credit expires in 2004 and had an interest rate of 1.3% at March 31, 2003.

The Variable Rate Demand Housing Revenue Bonds with the State of Ohio Housing Finance Agency (OHFA) are due July 2018 and at March 31, 2003 are secured by a \$10.6 million letter of credit and by buildings, land, furniture and fixtures of seven Ohio residences. The letter of credit expires in 2005 and had an interest rate of 1.25% at March 31, 2003.

At March 31, 2003, mortgage loans include three fixed rate loans secured by seven Texas residences, three Oregon residences and three New Jersey residences. These loans collectively require monthly principal and interest payments of \$230,000, with balloon payments of \$11.8 million, \$5.3 million and \$7.2 million due at maturity in May 2008, August 2008 and September 2008, respectively. These loans bear fixed annual interest rates from 7.58% to 8.79%.

Edgar Filing: ASSISTED LIVING CONCEPTS INC - Form 10-Q

Prior to the Company's Plan of Reorganization, mortgage loans also included a \$5.9 million mortgage loan at a fixed annual interest rate of 8.79%, secured by one Pennsylvania residence and one South Carolina residence. In accordance with the Company's Plan of Reorganization, the Company conveyed two facilities to this lender in satisfaction of the \$5.9 million of debt. The Company continues to operate these residences under operating leases with the same lender.

Table of Contents

Housing and Urban Development (HUD) Insured mortgages include three separate loan agreements entered into in 2001. These are fixed rate mortgages, each of which is secured by one facility in Texas. These loans mature between July 1, 2036 and August 1, 2036 and collectively require monthly principal and interest payments of \$47,493. The loans bear fixed annual interest rates between 7.40% and 7.55%.

GE Capital credit facility is a secured line of credit up to \$44.0 million. This is a variable rate credit facility, secured by 31 facilities. This credit facility matures in January 2005, required monthly principal payments of \$50,000 for 2002, and requires monthly principal payments of \$65,000 for 2003 and \$80,000 for 2004. The interest on the credit facility is calculated at LIBOR plus 4.5%, floating monthly (not to be less than 8%) and is payable monthly in arrears.

On January 1, 2002 the Debtors emerged from the proceedings under Chapter 11 of the Bankruptcy Code. The Company's Plan of reorganization included the issuance of \$40.25 million aggregate principal amount of seven-year secured notes (the New Senior Secured Notes), bearing interest at 10% per annum, payable semi-annually in arrears, and \$15.25 million aggregate principal amount of ten-year secured notes (the New Junior Secured Notes and collectively with the New Senior Secured Notes, the New Notes), bearing interest payable in additional New Junior Secured Notes for three years at 8% per annum and thereafter payable in cash at 12% per annum, payable semi-annually in arrears. The New Junior Secured Notes were issued at a discount of \$2.6 million. The discount will be amortized over the life of the New Junior Secured Notes using the effective interest method. The New Notes are secured by 51 properties as of March 31, 2003.

Of the \$50.1 million outstanding in New Notes, \$20.0 million is payable to related parties.

As of the Effective Date, the Successor Company revalued its long-term debt in conjunction with the implementation of fresh-start reporting. At December 31, 2001, an adjustment of \$3.1 million was recorded to reduce long-term debt to its fair market value. Amortization of this adjustment is computed using the straight-line method over the individual loan life.

As of March 31, 2003, the following annual principal payments are required (in thousands):

April 1, 2003 through December 31, 2003	\$ 2,415
2004	3,152
2005	43,379
2006	2,258
2007	2,408
Thereafter	109,702
	<hr/>
Total	\$ 163,314
	<hr/>

The Company has a series of reimbursement agreements with U.S. Bank for letters of credit that secure certain of our Revenue bonds payable, which total approximately \$24.2 million as of March 31, 2003. As such letters of credit expire, beginning in January 2004, the Company will need to obtain replacement letters of credit, post cash collateral or refinance the underlying debt. There can be no assurance that replacement letters of credit will be procured from the same or other lending institutions on terms that are acceptable to the Company. In the event that the Company is unable to obtain a replacement letter of credit or provide alternate collateral prior to the expiration of any of these letters of credit, the underlying debt would be in default. The Company's agreements with U.S. Bank contain restrictive covenants that include compliance with certain financial ratios.

In May 2002, we amended our existing agreement with U.S. Bank, establishing new covenants, with which we were in compliance as of March 31, 2003. Failure to comply with these covenants would constitute an event of default, which would allow U.S. Bank to declare any amounts outstanding under the loan documents to be due and payable.

In addition to the debt agreements with OHCS related to the six owned residences in Oregon, the Company has entered into Lease Approval Agreements with OHCS and the lessor of the Oregon Leases, which obligates the Company to comply with the terms and conditions of the underlying trust deed relating to the leased buildings. Under the terms of the OHCS debt agreements, the Company is required to maintain a capital replacement escrow account to cover expected capital expenditure requirements for the Oregon Leases and the six OHCS loans.

As a further condition of the OHCS debt agreements, the Company is required to comply with the terms of certain regulatory agreements which provide, among other things, that in order to preserve the federal income tax exempt status of the bonds, the Company is required to lease at least 20% of the units of the projects to low or moderate income persons as defined in Section 142(d) of the Internal Revenue Code. There are additional requirements as to the age and physical condition of the residents with which the

Table of Contents

Company must also comply. Non-compliance with these restrictions may result in an event of default and cause acceleration of the scheduled repayment.

4. Income Taxes

The Company anticipates taxable income for both financial reporting and tax return purposes for the year ended December 31, 2003, and accordingly has provided for federal and state income taxes on income from continuing operations and discontinued operations for the three months ended March 31, 2003. The Company has recorded such income tax expense at the rate of 40.4%, the estimated effective tax rate for the full fiscal year.

The provision for income taxes differs from the applicable U.S. statutory federal rate as a result of the following items:

Statutory federal tax rate	34.0%
State income taxes, net of federal benefit	5.6
Non-deductible expenses	0.8
	—
Effective tax rate	40.4%
	—

At December 31, 2002, the Company had approximately \$101.4 million of net operating loss (NOL) carryforwards which will expire between 2009 and 2022. These NOLs have been reduced to \$22.3 million as a result of the discharge and cancellation of various prepetition liabilities under the Plan. The reduction of the NOLs was effective on January 1, 2003.

The NOLs remaining after the application of the cancellation of indebtedness provisions are subject to certain provisions of the Internal Revenue Code which restricts the utilization of the losses. In addition, any net unrealized built-in losses resulting from the excess of tax basis over the carrying value of the Company's assets (primarily property and equipment) as of the Effective Date, which are recognized within five years are also subject to these provisions. Section 382 of the Internal Revenue Code imposes limitations on the utilization of the loss carryforwards and built-in losses after certain changes of ownership of a loss company. The Company is deemed to be a loss company for these purposes. Under these provisions, the Company's ability to utilize these loss carryforwards and built-in losses in the future will generally be subject to an annual limitation of approximately \$1.6 million. For the full fiscal year ending December 31, 2003, the Company anticipates such limitation will be applied to recognized built-in losses, thus the Company's estimates include no utilization of NOLs in 2003.

There can be no assurances that the Company will be able to utilize these NOLs or built-in losses and therefore the Company has established a 100 percent valuation allowance to offset the associated net deferred tax asset at December 31, 2002. As of March 31, 2003, the Company anticipates that a portion of such net deferred tax asset will be offset against current taxable income. In the three-month period ended March 31, 2003, the Company reduced the valuation allowance by \$550,000, thus reinstating a net deferred tax asset of \$550,000 on the balance sheet at March 31, 2003. Pursuant to SOP 90-7, such income tax benefit has been recorded as an increase to additional paid-in capital.

Pursuant to SOP 90-7, the income tax benefit, if any, of any future realization of the remaining NOL carryforwards and other deductible temporary differences existing as of the Effective Date will be recorded as an adjustment to additional paid-in capital.

5. Discontinued Operations

During the three months ended March 31, 2003, the Company sold one residence in Ohio and one residence in Indiana. The total sales price for these residences was \$2.6 million, and the Company recognized a gain from these sales of \$899,000.

In accordance with SFAS No. 144, the results of operations for these residences and the gain from the sale have been included in Income (loss) from discontinued operations in the accompanying financial statements for the three months ended March 31, 2002 and 2003.

On September 30, 2002 the Company completed the sale of four Florida residences and one Georgia residence. Consequently, the results of operations for these residences are included in Income (loss) from discontinued operations in the accompanying financial statements for the three months ended March 31, 2002.

Table of Contents**6. Stock-based Compensation**

The company accounts for stock-based compensation plans under the recognition and measurement principles of APB Opinion No. 25, *Accounting for Stock Issued to Employees*, and related Interpretations. No stock-based employee compensation cost is reflected in net income, as all options granted under those plans had an exercise price equal to the market value of the underlying common stock on the date of grant. The following table illustrates the effect on net income and earnings per share if the company had applied the fair value recognition provisions of FASB Statement No. 123, *Accounting for Stock-Based Compensation*, to stock-based employee compensation.

	Three Months Ended March 31,	
	2002	2003
Net income (loss), as reported	\$ (1,450)	\$ 1,031
Deduct: Total stock-based employee compensation expense determined under fair value based method for all awards granted, net of related tax effects	(8)	(31)
Pro forma net income (loss)	\$ (1,458)	\$ 1,000
Net income (loss) per share:		
Basic - as reported	\$ (0.22)	\$ 0.16
Basic - pro forma	\$ (0.22)	\$ 0.15
Diluted - as reported	\$ (0.22)	\$ 0.16
Diluted - pro forma	\$ (0.22)	\$ 0.15

7. Income (Loss) Per Share

The weighted average common shares used for basic net income (loss) per common share were 6,500,000 for the three months ended March 31, 2002 and March 31, 2003. The effect of dilutive stock options added 8,976 shares for the three months ended March 31, 2003. The effect of options for the three months ended March 31, 2002 is not considered since their effect is antidilutive.

8. Subsidiary Guarantee of New Notes

The New Notes, issued by the Company, are publicly traded and the repayment of these notes is guaranteed by three wholly owned subsidiaries of the Company: ALC Indiana, Inc., Home and Community Care, Inc. (HCI) and Carriage House Assisted Living, Inc. (Carriage House). The following information is presented as required under the Securities and Exchange Commission Financial Reporting Release No. 55 in connection with the guarantee of the New Notes by the Company's wholly owned subsidiaries. The operating and investing activities of the separate legal entities included in the consolidating financial statements are fully interdependent and integrated with the Company and each other.

Table of Contents

ASSISTED LIVING CONCEPTS, INC.
CONSOLIDATING BALANCE SHEETS
MARCH 31, 2003

	Wholly-Owned Subsidiaries					Consolidating Adjustments	Consolidated Total
	ALC, Inc.	ALC Indiana, Inc.	Carriage House	HCI	Non- Participating Subsidiaries		
ASSETS							
Current Assets:							
Cash and cash equivalents	\$ 6,736	\$	\$	\$	\$	\$	\$ 6,736
Cash restricted for resident security deposit	1,929						1,929
Accounts receivable, net	3,068				245		3,313
Prepaid insurance	1,020						1,020
Prepaid expenses	909				22		931
Cash restricted for workers compensation claims	4,375						4,375
Other current assets	1,064				1,822		2,886
	<u>19,101</u>				<u>2,089</u>		<u>21,190</u>
Total current assets	19,101				2,089		21,190
Restricted cash	5,323						5,323
Receivable from subsidiaries/parent	3,432	4,578		3,264	1,310	(12,584)	
Property and equipment, net	84,966	12,478	3,524	4,143	79,627		184,738
Investment in subsidiaries	30,921					(30,921)	
Deferred income taxes	550						550
Other assets, net	1,891				429		2,320
	<u>\$ 146,184</u>	<u>\$ 17,056</u>	<u>\$ 3,524</u>	<u>\$ 7,407</u>	<u>\$ 83,455</u>	<u>\$ (43,505)</u>	<u>\$ 214,121</u>
	<u>\$ 146,184</u>	<u>\$ 17,056</u>	<u>\$ 3,524</u>	<u>\$ 7,407</u>	<u>\$ 83,455</u>	<u>\$ (43,505)</u>	<u>\$ 214,121</u>
LIABILITIES AND SHAREHOLDERS EQUITY							
Current liabilities:							
Accounts payable	\$ 1,263	\$	\$	\$	\$ 512	\$	\$ 1,775
Accrued real estate taxes	2,309	365	298	75	579		3,626
Accrued interest expense	1,256				46		1,302
Accrued payroll expense	4,320				12		4,332
Other accrued expenses	6,271				44		6,315
Resident security deposits	1,578				198		1,776
Other current liabilities	1,024	125					1,149
Current portion of unfavorable lease adjustment	517		81				598
Current portion of long-term debt and capital lease obligation	1,255				1,446		2,701
	<u>19,793</u>	<u>490</u>	<u>379</u>	<u>75</u>	<u>2,837</u>		<u>23,574</u>
Total current liabilities	19,793	490	379	75	2,837		23,574
Other liabilities	535		39				574
Unfavorable lease adjustment	1,971		328		63		2,362
Long-term debt and capital lease obligation, net of current portion	81,474				76,171		157,645
Payable to subsidiaries/parent	12,147		437			(12,584)	
	<u>115,920</u>	<u>490</u>	<u>1,183</u>	<u>75</u>	<u>79,071</u>	<u>(12,584)</u>	<u>184,155</u>
Total liabilities	115,920	490	1,183	75	79,071	(12,584)	184,155
Shareholders' equity:							

Edgar Filing: ASSISTED LIVING CONCEPTS INC - Form 10-Q

Common stock	65	16,342				(16,342)	65
Additional paid-in capital	33,457		2,549	7,365	5,667	(15,754)	33,284
Retained earnings (accumulated deficit)	(3,258)	224	(208)	(33)	(1,283)	1,175	(3,383)
	<u>30,264</u>	<u>16,566</u>	<u>2,341</u>	<u>7,332</u>	<u>4,384</u>	<u>(30,921)</u>	<u>29,966</u>
Total shareholders equity							
Total liabilities and shareholder s equity	\$ 146,184	\$ 17,056	\$ 3,524	\$ 7,407	\$ 83,455	\$ (43,505)	\$ 214,121
	<u>\$ 146,184</u>	<u>\$ 17,056</u>	<u>\$ 3,524</u>	<u>\$ 7,407</u>	<u>\$ 83,455</u>	<u>\$ (43,505)</u>	<u>\$ 214,121</u>

Table of Contents**ASSISTED LIVING CONCEPTS, INC.****CONSOLIDATING BALANCE SHEETS
DECEMBER 31, 2002**

	Wholly-Owned Subsidiaries					Consolidating Adjustments	Consolidated Total
	ALC, Inc.	ALC Indiana, Inc.	Carriage House	HCI	Non- Participating Subsidiaries		
ASSETS							
Current Assets:							
Cash and cash equivalents	\$ 7,165	\$	\$	\$	\$	\$	\$ 7,165
Cash restricted for resident security deposits	1,929						1,929
Accounts receivable, net	2,446			3	266		2,715
Prepaid insurance	343						343
Prepaid expenses	946				45		991
Assets held for sale	9,727						9,727
Cash restricted for workers compensation claims	4,696						4,696
Other current assets	1,199			3	1,991		3,193
Total current assets	28,451			6	2,302		30,759
Restricted cash	5,315						5,315
Receivable from subsidiaries/parent	9,745	6,454		2,780		(18,979)	
Property and equipment, net	81,328	12,565	3,558	4,176	76,303		177,930
Investment in subsidiaries	27,632					(27,632)	
Other assets, net	1,635				401		2,036
Total assets	\$ 154,106	\$ 19,019	\$ 3,558	\$ 6,962	\$ 79,006	\$ (46,611)	\$ 216,040
LIABILITIES AND SHAREHOLDERS EQUITY							
Current liabilities:							
Accounts payable	\$ 234	\$	\$	\$ 1	\$ 534	\$	\$ 769
Accrued real estate taxes	2,830	285	234	71	1,416		4,836
Accrued interest expense	2,147				27		2,174
Accrued payroll expense	4,960				61		5,021
Other accrued expenses	5,669				49		5,718
Resident security deposits	1,779			(1)	213		1,991
Other current liabilities	976						976
Current portion of unfavorable lease adjustment	525		82				607
Current portion of long-term debt and capital lease obligation	8,817				2,704		11,521
Total current liabilities	27,937	285	316	71	5,004		33,613
Other liabilities	430		33				463
Unfavorable lease adjustment	2,095		347		66		2,508
Long-term debt and capital lease obligation, net of current portion	78,852				72,219		151,071
Payable to subsidiaries/parent	16,234		1,236		1,509	(18,979)	
Total liabilities	125,548	285	1,932	71	78,798	(18,979)	187,655

Edgar Filing: ASSISTED LIVING CONCEPTS INC - Form 10-Q

Shareholders' equity:							
Common stock	65	16,342				(16,342)	65
Additional paid-in capital	32,907		2,548	7,365	5,667	(15,753)	32,734
Accumulated deficit	(4,414)	2,392	(922)	(474)	(5,459)	4,463	(4,414)
	<u>28,558</u>	<u>18,734</u>	<u>1,626</u>	<u>6,891</u>	<u>208</u>	<u>(27,632)</u>	<u>28,385</u>
Total shareholders' equity	28,558	18,734	1,626	6,891	208	(27,632)	28,385
	<u>28,558</u>	<u>18,734</u>	<u>1,626</u>	<u>6,891</u>	<u>208</u>	<u>(27,632)</u>	<u>28,385</u>
Total liabilities and shareholders' equity	\$ 154,106	\$ 19,019	\$ 3,558	\$ 6,962	\$ 79,006	\$ (46,611)	\$ 216,040
	<u>\$ 154,106</u>	<u>\$ 19,019</u>	<u>\$ 3,558</u>	<u>\$ 6,962</u>	<u>\$ 79,006</u>	<u>\$ (46,611)</u>	<u>\$ 216,040</u>

Table of Contents**ASSISTED LIVING CONCEPTS, INC.****CONSOLIDATING STATEMENTS OF OPERATIONS**
Three Months Ended March 31, 2003

	Wholly-Owned Subsidiaries					Consolidated Total
	ALC,INC.	ALC Indiana, Inc.	Carriage House	HCI	Non- participating Subsidiaries	
Revenue	\$37,481	\$	\$	\$	\$ 3,663	\$41,144
Operating expenses:						
Residence operating expenses	24,894	90	64		2,675	27,723
Corporate general and administrative	4,342					4,342
Building rentals	2,882		223			3,105
Depreciation and amortization	837	101	34	33	671	1,676
	<u> </u>	<u> </u>	<u> </u>	<u> </u>	<u> </u>	<u> </u>
Total operating expenses	32,955	191	321	33	3,346	36,846
Operating income	4,526	(191)	(321)	(33)	317	4,298
Other income (expense):						
Interest expense	(1,765)				(1,664)	(3,429)
Interest income	36					36
Management fee income (expense)	(177)		113		64	
Lease income (expense)	(540)	540				
Other income, net	(4)					(4)
	<u> </u>	<u> </u>	<u> </u>	<u> </u>	<u> </u>	<u> </u>
Total other expense, net	(2,450)	540	113		(1,600)	(3,397)
Income (loss) from continuing operations before income taxes	2,076	349	(208)	(33)	(1,283)	901
Income tax expense	239	125				364
Income (loss) from continuing operations	1,837	224	(208)	(33)	(1,283)	537
Income (loss) from discontinued operations (including gain on sale of assets)	830					830
Income tax expense	336					336
Income (loss) from discontinued operations	494					494
Net Income (loss)	\$ 2,331	\$ 224	\$(208)	\$(33)	\$(1,283)	\$ 1,031

Table of Contents**ASSISTED LIVING CONCEPTS, INC****CONSOLIDATING STATEMENTS OF OPERATIONS****Three Months Ended March 31, 2002**

	Wholly-Owned Subsidiaries					Consolidated Total
	ALC, Inc.	ALC Indiana, Inc.	Carriage House	HCI	Non- Participating Subsidiaries	
Revenue	\$33,541	\$	\$	\$	\$ 3,473	\$37,014
Operating expenses:						
Residence operating expenses	22,699	71	62		2,636	25,468
Corporate general and administrative	4,317					4,317
Building rentals	2,805		233			3,038
Depreciation and amortization	823	99	32	33	625	1,612
	<u> </u>	<u> </u>	<u> </u>	<u> </u>	<u> </u>	<u> </u>
Total operating expenses	30,644	170	327	33	3,261	34,435
	<u> </u>	<u> </u>	<u> </u>	<u> </u>	<u> </u>	<u> </u>
Operating income (loss)	2,897	(170)	(327)	(33)	212	2,579
Other income (expense):						
Interest expense	(2,063)				(1,528)	(3,591)
Interest income	53					53
Management fee income (expense)	(92)		75		17	
Lease income (expense)	(1,769)	540			1,229	
Other income, net	2					2
	<u> </u>	<u> </u>	<u> </u>	<u> </u>	<u> </u>	<u> </u>
Total other income (expense), net	(3,869)	540	75		(282)	(3,536)
	<u> </u>	<u> </u>	<u> </u>	<u> </u>	<u> </u>	<u> </u>
Income (loss) before debt restructure, and reorganization cost, and discontinued operations	(972)	370	(252)	(33)	(70)	(957)
Debt restructure and reorganization costs	447					447
	<u> </u>	<u> </u>	<u> </u>	<u> </u>	<u> </u>	<u> </u>
Income (loss) from continuing operations	(1,419)	370	(252)	(33)	(70)	(1,404)
Income (loss) from discontinued operations	(60)			(32)	46	(46)
	<u> </u>	<u> </u>	<u> </u>	<u> </u>	<u> </u>	<u> </u>
Net income (loss)	\$ (1,479)	\$ 370	\$ (252)	\$ (65)	\$ (24)	\$ (1,450)
	<u> </u>	<u> </u>	<u> </u>	<u> </u>	<u> </u>	<u> </u>

Table of Contents

ASSISTED LIVING CONCEPTS, INC.
CONSOLIDATING STATEMENT OF CASH FLOWS
Three months ended March 31, 2003

	Wholly-Owned Subsidiaries					Consolidated Total
	ALC, Inc.	ALC Indiana, Inc.	Carriage House	HCI	Non- Participating Subsidiaries	
Operating Activities:						
Net income (loss)	\$ 2,331	\$ 224	\$(208)	\$(33)	\$(1,283)	\$ 1,031
Adjustment to reconcile net loss to net cash provided by (used in) operating activities:						
Depreciation and amortization	837	101	34	33	671	1,676
Provision for doubtful accounts	239				13	252
Amortization of debt issuance costs	27					27
Amortization of fair value adjustments to building rentals	(138)		(20)		3	(155)
Interest paid-in-kind	330					330
Amortization of fair value adjustment of debt	97					97
Amortization of note discount	135					135
Straight-line adjustment to building rental	111					111
Gain on sale of assets	(899)					(899)
Changes in assets and liabilities:						
Receivable (payable) from subsidiaries/parent	(1,020)	(516)	124	(10)	1,422	
Accounts receivable	(874)			3	21	(850)
Prepaid expenses	(640)				23	(617)
Other current assets	135			3	169	307
Other assets	(283)				(28)	(311)
Accounts payable	1,029			(1)	(22)	1,006
Accrued expenses	(1,450)	80	64	4	(872)	(2,174)
Other current liabilities	(153)	125		1	(15)	(42)
Other liabilities	(6)		6			
Net cash provided by (used in) operating activities	(192)	14			102	(76)
Investing Activities:						
Increase in restricted cash	313					313
Purchases of property and equipment	(311)	(14)			(102)	(427)
Sale of properties	2,569					2,569
Net cash provided by (used in) investing	2,571	(14)			(102)	2,455
Financing Activities:						
Payments on long-term debt and capital lease obligation	(2,808)					(2,808)
Net cash provided by (used in) financing activities	(2,808)					(2,808)
Net decrease in cash and cash equivalents	(429)					(429)
Cash and cash equivalents, beginning of year	7,165					7,165
Cash and cash equivalents, end of year	\$ 6,736	\$	\$	\$	\$	\$ 6,736

Table of Contents

ASSISTED LIVING CONCEPTS, INC.
CONSOLIDATING STATEMENT OF CASH FLOWS
Three months ended March 31, 2002

	Wholly-Owned Subsidiaries					Consolidated Total
	ALC, Inc.	ALC Indiana, Inc	Carriage House	HCI	Non- Participating Subsidiaries	
Operating Activities:						
Net income (loss)	\$(1,479)	\$ 370	\$(252)	\$(65)	\$ (24)	\$(1,450)
Adjustment to reconcile net income (loss) to net cash provided by (used in) operating activities:						
Depreciation and amortization	845	99	32	51	640	1,667
Amortization of debt issuance costs	20					20
Amortization of fair value adjustment to building rentals	(144)		(23)		(3)	(170)
Amortization of fair market adjustment to long-term debt	4				103	107
Amortization of discount on long-term debt	106					106
Straight-line adjustment to building rentals	86					86
Interest paid-in-kind	305					305
Provision (recoveries) for doubtful accounts	26				(13)	13
Changes in assets and liabilities:						
Receivable from subsidiaries/parent	1,568	(531)	211	4	(1,252)	
Accounts receivable	(116)			11	5	(100)
Prepaid expenses	(2,343)				22	(2,321)
Other current assets	206	(9)	3		45	245
Other assets	(12)				(19)	(31)
Accounts payable	(213)			(4)	(37)	(254)
Accrued expenses	1,147	71	62	11	(978)	313
Other current liabilities	854				(59)	795
Other liabilities	(15)		8			(7)
Net cash provided by (used in) operating activities	845		41	8	(1,570)	(676)
Investing Activities:						
Increase in restricted cash	(1,719)					(1,719)
Purchases of property and equipment	(355)		(41)	(8)	(221)	(625)
Net cash provided by (used in) investing activities	(2,074)		(41)	(8)	(221)	(2,344)
Financing Activities:						
Proceeds from long-term debt	(791)				1,791	1,000
Payments on long-term debt and capital lease obligation	(360)					(360)
Debt issuance costs	(79)					(79)
Net cash provided by (used in) financing activities	(1,230)				1,791	561
Net decrease in cash and cash equivalents	(2,459)					(2,459)
Cash and cash equivalents, beginning of period	6,077					6,077
Cash and cash equivalents, end of period	\$ 3,618	\$	\$	\$	\$	\$ 3,618

Table of Contents

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

References in this section to ALC, the Company, us or we refer to Assisted Living Concepts, Inc. and its wholly owned subsidiaries.

General

We operate, own and lease free-standing assisted living residences. These residences are primarily located in small, middle-market, rural and suburban communities with a population typically ranging from 10,000 to 40,000. As of March 31, 2003, we had operations in 14 states.

We provide personal care and support services, and make available routine nursing services (as permitted by applicable law) designed to meet the personal and health care needs of our residents. We believe that this combination of residential, personal care, support and health care services provides a cost-efficient alternative to, and affords an independent lifestyle for, individuals who do not require the broader array of medical services that nursing facilities are required by law to provide.

As of March 31, 2003, we operated 177 assisted living residences (6,844 units), of which we owned 122 residences (4,739 units) and leased 55 residences (2,105 units). At March 31, 2003, we had an occupancy rate of 88.3% and an average combined monthly rate for rent and services of \$2,235 per unit.

We derive our revenues primarily from resident fees for room, board and care. Resident fees typically are paid monthly by residents, their families, state Medicaid agencies or other third parties. Resident fees include revenue derived from a multi-tiered rate structure, which varies based on the level of care provided. Resident fees are recognized as revenues when services are provided. Our expenses include:

- residence operating expenses, such as staff payroll, food, property taxes, utilities, insurance and other direct residence operating expenses;

- general and administrative expenses consisting of regional management and corporate support functions such as legal, accounting and other administrative expenses;

- building rentals;

- depreciation and amortization; and

- interest expense related to debt.

We anticipate that the majority of our revenues will continue to come from private pay sources. However, we believe that by having located some of our residences in states with favorable regulatory and reimbursement climates, we should have a stable source of residents eligible for Medicaid reimbursement to the extent that private pay residents are not available and, in addition, provide our private pay residents with alternative sources of income when their private funds are depleted and they become Medicaid eligible.

Although we manage the mix of private paying residents and Medicaid paying residents residing in our facilities, any significant increase in our Medicaid population could have an adverse effect on our financial position, results of operations or cash flows, particularly if states operating these programs continue to limit, or more aggressively seek limits on, reimbursement rates.

Certain Transactions and Events

Fresh-Start Reporting

Upon the Effective Date of our Plan of reorganization, we adopted fresh-start reporting in accordance with the American Institute of Certified Public Accountants Statement of Position 90-7, Financial Reporting By Entities in Reorganization Under the Bankruptcy Code (SOP 90-7). In connection with the adoption of fresh-start reporting, a new entity has been deemed created for financial reporting purposes. For financial reporting purposes, we adopted the provisions of fresh-start reporting effective December 31, 2001. In adopting the requirements of fresh-start reporting as of December 31, 2001, we were required to value our assets and liabilities at their estimated fair value and eliminate our accumulated deficit at December 31, 2001.

Table of Contents

Sales of Residences

During the three months ended March 31, 2003, the Company sold one residence in Ohio and one residence in Indiana. The total sales price for these residences was \$2.6 million, and the Company recognized a gain from these sales of \$899,000.

Due to the purchaser's inability to obtain suitable financing, the Company has entered into an agreement to terminate the proposed sale of the Company's nine South Carolina facilities. Six of the facilities are owned and pledged as collateral for the Senior Secured Notes and Junior Secured Notes; three of the facilities are leased from a national REIT. The Company had previously announced the pending sale of these properties and proposed use of the proceeds to redeem a portion of the Senior Secured Notes, which will now not occur.

Due to the recent improved operating performance of the South Carolina facilities, the Company has decided not to sell these assets at this time. For at least the near term, the Company intends to continue to operate the facilities on an on-going basis.

Critical Accounting Policies and Estimates

The discussion and analysis of our financial condition and results of operations are based upon our condensed consolidated financial statements, which have been prepared in accordance with accounting principles generally accepted in the United States of America. The preparation of these financial statements requires us to make estimates and judgments that affect the reported amounts of assets, liabilities, revenue and expenses and related disclosure of contingent assets and liabilities. On an on-going basis, we evaluate these estimates, including those related to bad debts, income taxes, the carrying value of long-lived assets, financing operations, contingencies and litigation. We base our estimates on historical experience and on various other assumptions that are believed to be reasonable under the circumstances, the results of which form the basis for making judgments about the carrying values of assets and liabilities that are not readily apparent from other sources. Actual results may differ from these estimates under different assumptions or conditions.

Table of Contents**Results of Operations**

The following table sets forth, for the periods presented, operating expenses as a percentage of revenue, the number of total residences and units operated, average occupancy and rental rates and the sources of our revenue. The portion of revenues received from state Medicaid agencies are labeled as Medicaid state paid portion while the portion of our revenues that a Medicaid-eligible resident must pay out of his or her own resources is labeled Medicaid resident paid portion.

	Three Months Ended March 31,	
	2002	2003
Revenue	100.0	100.0
Operating expenses:		
Residence operating expenses	68.8	67.4
Corporate general and administrative	11.7	10.6
Building rentals	8.2	7.5
Depreciation and amortization	4.3	4.0
	<u>93.0</u>	<u>89.5</u>
Operating income	7.0	10.5
Other income (expense):		
Interest expense	(9.7)	(8.4)
Interest income	0.1	0.1
Other income, net	0.0	(0.0)
	<u>(9.6)</u>	<u>(8.3)</u>
Income (loss) before debt restructure, reorganization costs, and discontinued operations	(2.6)	2.2
Debt restructure and reorganization costs	(1.2)	
	<u>(3.8)</u>	<u>2.2</u>
Income (loss) from continuing operations before income taxes	(3.8)	2.2
Income tax expense		0.9
	<u>(3.8)</u>	<u>1.3</u>
Income (loss) from continuing operations	(3.8)	1.3
Discontinued operations:		
Income (loss) from operations (including gain on sale of assets)	(0.1)	2.0
Income tax expense		0.8
	<u>(0.1)</u>	<u>1.2</u>
Income (loss) from discontinued operations	(0.1)	1.2
Net income (loss)	<u>(3.9)</u>	<u>2.5</u>

	Three Months Ended March 31,	
	2002	2003
Other Data Related to Continuing Operations:		
Residences operated (end of period)	\$ 177	\$ 177
Units operated (end of period)	6,842	6,844
Average occupancy rate (based on occupied units)	84.3%	88.3%
Average monthly rental rate	\$ 2,121	\$ 2,235
Sources of revenue:		
Medicaid state paid portion	12.13%	12.88%
Medicaid resident paid portion	7.50%	8.42%

Edgar Filing: ASSISTED LIVING CONCEPTS INC - Form 10-Q

Private resident paid portion	80.37%	78.70%
	<hr/>	<hr/>
Total	100.00%	100.00%
	<hr/>	<hr/>

Three months ended March 31, 2003 compared to three months ended March 31, 2002:

The Company recorded net income of \$1.0 million on revenues of \$41.1 million for the three months ended March 31, 2003 (the March 2003 Quarter) compared to a net loss of \$1.5 million on revenues of \$37.0 million for the three months ended March 31, 2002 (the March 2002 Quarter).

Table of Contents

Revenues increased \$4.1 million for the March 2003 Quarter compared to the March 2002 Quarter primarily due to an increase in average occupancy of approximately four percent and an increase in average rental rate received from residents of approximately \$114 per month. In March 2003 the Company instituted a rent increase in its residences.

Residence operating expenses increased \$2.3 million for the March 2003 Quarter compared to the March 2002 Quarter but decreased as a percentage of revenue from 68.8% to 67.4%. Of the increase, \$1.1 million is attributable to an increase in payroll expenses, which decreased slightly as a percentage of revenue. The increase in payroll is primarily due to an increase in benefits, additional personnel, and increased salaries and wages. An increase in utilities expense of \$0.4 million in addition to less significant increases in other expense categories comprise the remaining increase in residence operating expenses from the March 2002 Quarter to the March 2003 Quarter. These increases were offset primarily by a decrease of \$180,000 in insurance costs, primarily liability insurance, and less significant decreases in other expense categories.

Corporate, general and administrative expenses increased \$25,000 for the March 2003 Quarter compared to the March 2002 Quarter but decreased as a percentage of revenue from 11.7% to 10.6%. Increased expenses from the relocation of the Company's headquarters from Portland, Oregon to Dallas, Texas including rent, hiring expenses and temporary help expenses were offset by decreases in information technology related expenses and other payroll related expenses.

Building rentals increased \$67,000 for the March 2003 Quarter compared to the March 2002 Quarter but decreased as a percentage of revenue from 8.2% to 7.5%.

Depreciation and amortization expense increased by \$64,000 for the March 2003 Quarter compared to the March 2002 Quarter.

Interest expense decreased \$162,000 for the March 2003 Quarter compared to the March 2002 Quarter. The decrease is due to the overall reduction of indebtedness.

Debt restructure and reorganization costs were \$447,000 for the March 2002 Quarter. These are professional fees, including legal and investment advisory fees, related to the Company's Plan of reorganization which became effective January 1, 2002. The Company did not incur these expenses in the March 2003 Quarter.

Income tax expense was \$700,000 for the March 2003 Quarter, of which \$150,000 related to state income taxes. The Company anticipates taxable income for both financial reporting and tax return purposes for the year ended December 31, 2003, and accordingly has provided for federal and state income taxes on income from continuing operations and discontinued operations for the three months ended March 31, 2003. The Company has recorded such income tax expense at the rate of 40.4%, the estimated effective tax rate for the full fiscal year.

Liquidity and Capital Resources

At March 31, 2003, we had a working capital deficit of \$2.4 million and unrestricted cash and cash equivalents of \$6.7 million.

Net cash used in operating activities was \$76,000 during the March 2003 Quarter. The primary sources included net income of \$1.0 million and an increase in accounts payable of \$1.0 million. The increase in accounts payable was primarily due to increased operating expenses at the residences and expenses relating to the move of the corporate office. These sources were offset primarily by a decrease of \$2.2 million in accrued expenses, and increases of \$850,000 and \$617,000 in accounts receivable and prepaid expenses, respectively. The decrease in accrued expenses was primarily due to property tax payments made during the March 2003 Quarter, while the increases in accounts receivable and prepaid expenses were primarily due to increased revenues and insurance premium payments, respectively.

Net cash provided by investing activities was \$2.5 million during the March 2003 Quarter. The primary source resulted from the sales of properties for \$2.6 million.

Net cash used in financing activities was \$2.8 million during the March 2003 Quarter, all of which related to payments on long-term debt.

As of March 31, 2003, approximately \$24.2 million of our indebtedness was secured by letters of credit issued by U.S. Bank, which in some cases, have termination dates prior to the maturity of the underlying debt. As such letters of credit expire, beginning in January 2004, we will need to obtain replacement letters of credit, post cash collateral or refinance the underlying debt. There can be no assurance that we will be able to procure replacement letters of credit from the same or other lending institutions on terms that are acceptable to us. In the event that we are unable to obtain a replacement letter of credit or provide alternate collateral prior to the

Table of Contents

expiration of any of these letters of credit, we would be in default on the underlying debt. Any such default could have a material adverse effect on the Company.

Our credit agreements with U.S. Bank contain certain restrictive and financial covenants, including certain financial ratios. The agreements also require us to deposit \$500,000 in cash collateral with U.S. Bank in the event certain regulatory actions are commenced with respect to the properties securing our obligations to U.S. Bank. U.S. Bank is required to release such deposits upon satisfactory resolution of the regulatory action. As of the date of this filing, no such deposits have been required.

In May 2002, we amended our existing agreement with U.S. Bank, establishing new covenants, with which we were in compliance as of March 31, 2003. Failure to comply with these covenants would constitute an event of default, which would allow U.S. Bank to declare any amounts outstanding under the loan documents to be due and payable.

Certain of our leases and loan agreements contain covenants and cross-default provisions such that a default on one of those agreements could cause us to be in default on one or more other agreements which would have a material adverse effect on the Company.

Our ability to make payments on and to refinance any of our indebtedness, to satisfy our lease obligations and to fund planned capital expenditures will depend on our ability to generate cash in the future. This, to a certain extent, is subject to general economic, financial, competitive, legislative, regulatory and other factors that are beyond our control.

Based upon our current level of operations, we believe that our current cash on hand and cash flow from operations are sufficient to meet our liquidity needs for at least the next twelve months.

There can be no assurance, however, that our business will generate sufficient cash flow from operations, or that currently anticipated cost savings and operating improvements will be realized on schedule, both of which may be necessary to enable us to pay our indebtedness, to satisfy our lease obligations and to fund our other liquidity needs. As a result, we may need to refinance all or a portion of our indebtedness, on or before maturity. There can be no assurance that we will be able to refinance any of our indebtedness, on commercially reasonable terms or at all.

Item 3. *Quantitative and Qualitative Disclosure About Market Risk*

Market risk represents the risk of changes in value of a financial instrument, derivative or non-derivative, caused by fluctuations in interest rates, foreign exchange rates and equity prices. Changes in these factors could cause fluctuations in our results of operations and cash flows.

For fixed rate debt, changes in interest rates generally affect the fair market value of the debt instrument, but not our results of operations or cash flows. We do not have an obligation to prepay any of our fixed rate debt prior to maturity, and therefore, interest rate risk and changes in the fair market value of our fixed rate debt will not have an impact on our results of operations or cash flows until we decide, or are required, to refinance such debt.

For variable rate debt, changes in interest rates generally do not impact the fair market value of the debt instrument, but do affect our future results of operations and cash flows. We had variable rate debt of \$67.4 million outstanding at March 31, 2003 with a weighted average interest rate of 6.1%, of which \$43.2 million has an interest rate floor of 8.0%. Assuming that our balance of variable rate debt remains constant, each one-percent increase in interest rates would result in an annual increase in interest expense, and a corresponding decrease in net cash flows, of \$242,000. Conversely, each one-percent decrease in interest rates would result in an annual decrease in interest expense, and a corresponding increase in net cash flows, of \$242,000.

We are also exposed to market risks from fluctuations in interest rates and the effects of those fluctuations on market values of our cash equivalents and short-term investments. These investments generally consist of overnight investments that are not significantly exposed to interest rate risk, except to the extent that changes in interest rates will ultimately affect the amount of interest income earned and cash flow from these investments.

We do not have any derivative financial instruments in place to manage interest costs, but that does not mean we will not use them as a means to manage interest rate risk in the future.

We do not use foreign currency exchange forward contracts or commodity contracts and do not have foreign currency exposure.

Table of Contents

Item 4. *Controls and Procedures*

Evaluation of Disclosure Controls and Procedures

Our chief executive officer and our chief financial officer, after evaluating our disclosure controls and procedures (as defined in Securities Exchange Act of 1934 (the Exchange Act) Rules 13a-14(c) and 15-d-14(c)) as of a date (the Evaluation Date) within 90 days before the filing date of this Quarterly Report on Form 10-Q, have concluded that as of the Evaluation Date, our disclosure controls and procedures are effective to ensure that information we are required to disclose in reports that we file or submit under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in Securities and Exchange Commission rules and forms.

Changes in Internal Controls

Subsequent to the Evaluation Date, there were no significant changes in our internal controls or in other factors that could significantly affect our controls, nor, to our knowledge, were there any significant deficiencies or material weaknesses in our internal controls. As a result, no corrective actions were required or undertaken.

PART II OTHER INFORMATION

Item 1. *Legal Proceedings*

We are involved from time to time in ordinary, routine or regulatory legal proceedings incidental to our business. As of May 8, 2003, we believe that such legal proceedings should not have a material adverse effect on our business.

Item 4. *Submission of Matters to a Vote of Security Holders*

None.

Item 6. *Exhibits and Reports on Form 8-K*

(a) The following documents are filed as part of this report:

**Exhibit
Number**

12 Ratio of Earnings to Fixed Charges

99.1 Certification pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002

99.2 Certification pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002

(b) Reports on Form 8-K

We filed a report on Form 8-K on March 10, 2003 pursuant to Item 5 of Form 8-K announcing the Company's earnings for the fourth quarter and pending sale of its South Carolina facilities.

Table of Contents

CERTIFICATIONS

I, Steven Vick, certify that:

1. I have reviewed this quarterly report on Form 10-Q of Assisted Living Concepts, Inc;
2. Based on my knowledge, this quarterly report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this quarterly report;
3. Based on my knowledge, the financial statements, and other financial information included in this quarterly report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this quarterly report;
4. The registrant's other certifying officers and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-14 and 15d-14) for the registrant and we have:
 - a) designed such disclosure controls and procedures to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this quarterly report is being prepared;
 - b) evaluated the effectiveness of the registrant's disclosure controls and procedures as of a date within 90 days prior to the filing date of this quarterly report (the Evaluation Date); and
 - c) presented in this quarterly report our conclusions about the effectiveness of the disclosure controls and procedures based on our evaluation as of the Evaluation Date;
5. The registrant's other certifying officers and I have disclosed, based on our most recent evaluation, to the registrant's auditors and the audit committee of registrant's board of directors (or persons performing the equivalent function):
 - a) all significant deficiencies in the design or operation of internal controls which could adversely affect the registrant's ability to record, process, summarize and report financial data and have identified for the registrant's auditors any material weaknesses in internal controls; and
 - b) any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal controls; and
6. The registrant's other certifying officers and I have indicated in this quarterly report whether or not there were significant changes in internal controls or in other factors that could significantly affect internal controls subsequent to the date of our most recent evaluation, including any corrective actions with regard to significant deficiencies and material weaknesses.

Date: May 12, 2003

/s/ Steven L. Vick

Steven L. Vick
President and Chief Executive Officer

Table of Contents

CERTIFICATIONS

I, Matthew G. Patrick, certify that:

1. I have reviewed this quarterly report on Form 10-Q of Assisted Living Concepts, Inc;
2. Based on my knowledge, this quarterly report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this quarterly report;
3. Based on my knowledge, the financial statements, and other financial information included in this quarterly report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this quarterly report;
4. The registrant's other certifying officers and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-14 and 15d-14) for the registrant and we have:
 - a. designed such disclosure controls and procedures to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this quarterly report is being prepared;
 - b. evaluated the effectiveness of the registrant's disclosure controls and procedures as of a date within 90 days prior to the filing date of this quarterly report (the "Evaluation Date"); and
 - c. presented in this quarterly report our conclusions about the effectiveness of the disclosure controls and procedures based on our evaluation as of the Evaluation Date;
5. The registrant's other certifying officers and I have disclosed, based on our most recent evaluation, to the registrant's auditors and the audit committee of registrant's board of directors (or persons performing the equivalent function):
 - a. all significant deficiencies in the design or operation of internal controls which could adversely affect the registrant's ability to record, process, summarize and report financial data and have identified for the registrant's auditors any material weaknesses in internal controls; and
 - b. any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal controls; and
6. The registrant's other certifying officers and I have indicated in this quarterly report whether or not there were significant changes in internal controls or in other factors that could significantly affect internal controls subsequent to the date of our most recent evaluation, including any corrective actions with regard to significant deficiencies and material weaknesses.

Date: May 12, 2003

/s/ Matthew G. Patrick

Matthew G. Patrick
Chief Financial Officer

Table of Contents

EXHIBIT INDEX

**Exhibit
Number**

12	Ratio of Earnings to Fixed Charges
99.1	Certification pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002
99.2	Certification pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002