

FROM A RISK MANAGEMENT PERSPECTIVE**FINANCIAL REFORM OF THE OTC DERIVATIVES MARKET AND THE UNCERTAINTY THAT REMAINS FOR SENIOR LIVING PROVIDERS**

On July 21st President Obama signed into law the financial services regulatory reform bill now known as the Dodd-Frank Wall Street Reform and Consumer Protection Act ("Dodd-Frank"). The legislation contains vast provisions that will reshape almost every aspect of the financial system, including the over-the-counter ("OTC") derivatives market. Dodd-Frank substantially alters the regulation of the \$615 trillion OTC derivatives market; however, the true impact of this reform will not be known until the completion of the extensive mandated rulemakings. Congress has delegated to various regulators (primarily the Commodity Futures Trading Commission ("CFTC") and the Securities and Exchange Commission ("SEC") the responsibility to further define the 2,000-plus pages of legislation. Ziegler expects this rulemaking phase to take up to another 12 months from the enactment date.

While many questions remain unanswered, below are a few key points that senior living providers can take away from Dodd-Frank with the understanding that the next 12 months will (hopefully) provide further guidance and clarity on these and many other financial reform topics and their resulting implications.

Mandatory Clearing: Under Dodd-Frank, both Swap Dealers¹ and Major Swap Participants² (financial entities) will be required to clear most or all of their standardized swaps through a national exchange or swap execution facility. The clearing of swap transactions will lower risk

in the financial system and provide pricing transparency. The legislation does include two exemptions from the mandatory clearing requirement. The first exemption is for "end-users" hedging commercial risks (see below) and the second is an exemption for swaps that are not accepted by a trading facility (i.e. non-standardized swaps).

End-User Exemption: For non-financial entities (such as a senior living provider), an exemption to the mandatory clearing requirement exists for swaps entered into with the purpose of hedging or mitigating commercial risk. This exemption is critical and will provide senior living providers with continued access to the OTC derivatives market, eliminating the requirement of clearing trades through an exchange that would require standardized terms and collateral requirements. Dodd-Frank also requires uncleared swaps to be reported (by the Swap Dealer) directly to a Swap Data Repository³ or the appropriate regulator.

Margin Requirements for End-Users (Senior Living Providers): While the legislation provides for an end-user mandatory clearing exemption, it does not explicitly exempt end-users from potential and costly margin requirements on uncleared transactions. This margin would represent the collateral that regulators would require an end-user to set aside for the purpose of mitigating counterparty risk and potential market exposure. The final legislation is vague on end-user margin requirements and has prompted a significant

amount of debate on whether or not the reform is intended to provide a margin requirement exemption to end-users. It should be noted that Senator Dodd and Senator Lincoln have instructed the CFTC and the SEC not to make hedging so costly that it becomes prohibitively expensive for end-users to manage their risk. In a letter dated June 30, 2010, the senators specifically stated that it is not their intent that end-users be subject to margin requirements. Market participants are left somewhat confused on this topic as it appears congress did not intend for end-user margin requirements but yet the final legislation did not provide for an explicit exemption. The expectation is that regulators will clarify during the rulemaking process when margin requirements will apply to swaps in which one counterparty is an end-user.

Margin Requirements for Swap Dealers: On the other hand, Dodd-Frank is clear that swap dealers will be subject to "initial and variation" margin requirements on all uncleared swaps. As a result of the swap dealer margin requirement, (it can only be assumed) the dealer's cost of setting aside margin/collateral will be passed along to the end-user (i.e. the senior living provider) as a new cost of doing business in the OTC derivatives market. This new cost would either be priced into the trade (for example, as a higher rate on a pay-fixed swap) or the swap dealer will simply require their end-user counterparties to post margin as well. It will not be known what the cost will amount to on a typical senior living swap

1 An entity is a Swap Dealer if it holds itself out as a dealer in swaps, makes a market in swaps, regularly enters into swaps for its own account in the ordinary course of business, or engages in activities causing the person to be commonly known as a dealer or market maker in swaps.

2 An entity is a Major Swap Participant if it is not a dealer, but (i) it maintains a substantial position in outstanding swaps for any major swap category, excluding positions held for hedging commercial risk or, in the case of an employee benefit plan under ERISA, for hedging risk associated with the plan's operation; (ii) its outstanding swaps create substantial counterparty exposure that could have a serious adverse effect on the financial stability of the U.S. system or financial markets; or (iii) it is a financial entity that is highly leveraged relative to the amount of capital it holds, it is not subject to capital requirements established by a federal banking agency, and it maintains a substantial position in outstanding swaps for any major category of swap.

3 Any person that collects and maintains information or records with respect to transactions or positions in, or the terms and conditions of, swaps entered into by third parties for the purpose of providing a centralized recordkeeping facility for swaps.

transaction until the rulemaking period is complete and the swap dealers have a better understanding on what their margin requirements will be on uncleared transactions.

Business Conduct Standards: Dodd-Frank authorizes regulators to require a number of business conduct requirements on swap dealers including, but not limited to, disclosure to end-users of the material risks and characteristics of a swap. Additionally, swap dealers that enter into a transaction with a government agency or a municipality counterparty must have a reasonable basis to believe that the

counterparty has a knowledgeable independent advisor that is acting in the counterparty's best interest and will provide representations regarding fair pricing and the appropriateness of the transaction. While this "swap advisor" standard does not appear to directly apply to senior living providers as a non-profit, it is a clear sign the market will be moving in the direction of this "best-practice" measure.

While there is no doubt that the sweeping financial regulatory reform will have an impact on the derivatives market for senior living providers, many questions remain unanswered.

It is clear that senior living providers will continue to have access to the OTC derivative market and it does seem unlikely that regulators will impose direct margin requirements on end-users. The biggest questions remaining may revolve around the margin requirements imposed on the swap dealers — which will ultimately impact the cost and viability of these historically effective hedging products.

Regards,

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MARKET COMMENTARY

Government bonds continued to trade in a narrow range this week as persistent unemployment remains a major hurdle to the longer term economic recovery. Initial jobless claims climbed by 19,000 to 479,000 in the week ended July 31, the most since April and exceeding the highest estimates of economists surveyed by Bloomberg News. The slack in hiring means employers will resist taking on additional staff in the coming months, which raises the risk consumer spending will weaken

further. Retailers in the U.S. reported July sales missed estimates as consumers have reduced spending prior to the start of the back-to-school season. Sales at 30 chain stores climbed by 3% less than the 3.2% that had been expected. The benchmark 10-year note started the week yielding 2.91% and ended the week at 2.85%. Municipal prices moved modestly higher as record cash flows into mutual funds and strong support by investors buying individual securities continued. Underwriters

priced higher grade issues at aggressive levels and found receptive buyers, especially in the short and intermediate parts of the curve. Credit spreads have continued to tighten as investors looking for lower rated bonds have been forced to pay increasing higher prices as a result of strong inflows and a scarcity of new issues. For the week, high grade names improved by 3–5 basis points while yield paper selectively improved by 5–10 basis points.

See pages 5–6 for current market rates

FEATURED ARTICLE

2010 AAHSA ZIEGLER 100: SINGLE-CAMPUS COMMUNITIES AND PROVIDERS

The 2010 AAHSA Ziegler 100 (AZ 100) publication lists not only the largest not-for-profit multi-site senior living organizations (the [Primary Ranking](#)) but also the largest affordable (non-market rate) senior housing multi-site providers, single-campus senior living communities, and single-campus senior living providers (see Chapter 6 of the publication for these additional listings). Prior **Z-News** have highlighted the [Primary Ranking](#) and affordable senior housing providers. This week we will look at the largest single-campus communities and the largest single-campus providers.

Single-Campus Communities (Table 6-1a)

This is the seventh year the AZ 100 publication has tracked the largest not-for-profit single-campus communities. Many of these largest communities are part of multi-site senior living providers, or systems. In fact, eight of the 10 largest and 16 of the 25 largest belong to systems. Showing a similar trend as the universe of systems, these large single-campus communities, as a whole, are weighted more heavily toward the provision of independent living, rather than nursing. Just four of the 25 largest have a smaller number of independent living units than nursing units (Jewish Home Lifecare – Bronx Division (NY), Hebrew Home at Riverdale – main campus (NY), Charles E Smith Life Community (MD), and Franklin United Methodist Community (IN)).

Compared to 2009's largest 100 communities, 2010's list has 1,471 more independent living units, 173 more assisted living units (a reversal of prior years' trends), and 977 fewer nursing care beds. The size of the largest 100 single-campus communities covers a broad range, from more than 2,300 to just more than 500 total units. The table below lists the largest 10 of the 100 single-campus communities ranked in this year's publication.

CAMPUS/ 2010 RANK	SYSTEM AFFILIATION	STATE	Summary of Market Rate Units (as of 12/31/09)			
			ILU	ALU	NCB	TOTAL
Riderwood Village (1)	National Senior Campuses	MD	1,953	230	132	2,315
John Knox Village (2)		MO	1,310	141	430	1,881
Charlestown (3)		MD	1,537	131	207	1,875
Oak Crest Village (4)	National Senior Campuses	MD	1,525	145	200	1,870
Cedar Crest Village (5)	National Senior Campuses	NJ	1,507	82	113	1,702
Greenspring Village (6)	National Senior Campuses	VA	1,409	104	180	1,693
Shell Point Village (7)	CMA	FL	1,221	252	198	1,671
Ann's Choice (8)	National Senior Campuses	PA	1,493	66	66	1,625

Brooksby Village (9)	National Senior Campuses	MA	1,343	94	104	1,541
Masonic Village of Elizabethtown (10)	Masonic Villages	PA	913	125	453	1,491

See Table 6-1a of the 2010 AAHSA Ziegler 100 publication for a ranking of the largest 100 single-campus communities.

Single-Campus Organizations (Table 6-1b)

The publication also includes a listing that ranks the largest 100 single-campus senior living providers. This list excludes communities that are part of a larger system of communities and focuses instead on those communities that are stand-alone operations. The table below lists the largest 10 of the 100 single-campus organizations ranked in this year's publication.

RANK	CAMPUS	STATE	Summary of Market Rate Units (as of 12/31/09)			
			ILU	ALU	NCB	TOTAL
1	John Knox Village	MO	1,310	141	430	1,881
2	Charlestown	MD	1,537	131	207	1,875
3	Henry Ford Village	MI	855	98	89	1,042
4	Panorama City	WA	827	37	153	1,017
5	John Knox Village of Florida	FL	745	62	177	984
6	Charles E Smith Life Community	MD	250	60	556	866
7	Franklin United Methodist Community	IN	196	459	208	863
8	Westminster-Canterbury Richmond	VA	536	170	146	852
9	Cross Keys Village-The Brethren Home Community	PA	449	95	270	814
10	St. John's Senior Communities	NY	339	0	475	814

See Table 6-1b of the 2010 AAHSA Ziegler 100 publication for the largest 100 single-campus organizations.

AAHSA will be mailing copies of the publication to AZ 100 organizations shortly; by month's end, copies of the AZ 100 2010 publication will be available by visiting www.aahsa.org OR www.zieglerseniorkingfinance.com.

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NON-PROFIT SENIOR LIVING RATINGS ACTIONS

ORGANIZATION	RATING AGENCY	RATING/ OUTLOOK	TYPE OF ACTION	DATE
The Pines at Davidson (NC)	Fitch	A- Stable	Affirmed Rating	8/3/10
Covenant Retirement Communities (IL)	S&P	BBB+ Stable	Affirmed Rating	8/4/10
EMA Obligated Group (Fairhaven and Copper Ridge) (MD)	S&P	BB- Stable	Affirmed Rating	8/4/10
Porter Hills Presbyterian Village (MI)	S&P	BB Negative	Downgraded Rating	8/6/10
Presbyterian Senior Living (PA)	S&P	BBB+ Negative	Affirmed Rating	8/6/10

FEATURED FINANCING

BREWSTER PLACE  **PLACE**
 get the most out of life

\$9,765,000

City of Topeka, Kansas
 Housing and Health Care Improvement Revenue Bonds, Series 2010

BREWSTER PLACE

Topeka, KS

CCRC "FACTOIDS"

A number of CCRC developers of the past are no longer active today. Van Scoyoc Associates began its CCRC development with Gardner Van Scoyoc in 1955, and over the course of its history, Van Scoyoc developed 7 CCRCs. Its first CCRC was Goodwin House in Alexandria, VA. We believe that Constellation Senior Services exited the business.

INTEREST RATES

	CURRENT	CHANGE FROM LAST WEEK	52-WK AVG
30 Yr MMD	3.94%	3.97%	4.11%
Senior Living 30-Year "A"	5.80%	5.85%	5.90%
Senior Living 30-Year "BBB"	6.20%	6.25%	6.44%
Senior Living Unrated	7.20%	7.25%	8.06%
Senior Living New Campus	8.50%	8.50%	9.03%
SIFMA	0.25%	0.28%	0.27%

MARKET REVIEW
MONEY MARKET RATES

	<u>8/06/10</u>	<u>1 WEEK AGO</u>	<u>1 MONTH AGO</u>	<u>1 YEAR AGO</u>
Prime Rate	3.25	3.25	3.25	3.25
Federal Funds (weekly average)	0.20	0.18	0.18	0.18
90 Day T-Bills	0.14	0.14	0.14	0.17
30-Day Commercial Paper (taxable)	0.19	0.23	0.21	0.18
Libor (30-day)	0.29	0.30	0.34	0.27
7 Day Tax-Exempt VRDB	0.22	0.25	0.22	0.28
SIFMA Index	0.25	0.28	0.25	0.35
Daily Rate Average	0.12	0.20	0.12	0.18

COMPARATIVE YIELDS

	<u>GOVT.</u>	<u>TAXABLE REVENUE</u>			<u>BAB</u>	<u>TAX-EXEMPT REVENUE</u>				
		<u>NR*</u>	<u>A</u>	<u>A</u>		<u>NR**</u>	<u>NR*</u>	<u>BBB</u>	<u>A</u>	<u>AAA</u>
1 Year	0.25	3.71	2.15	1.80	1 Year	5.00	4.95	2.50	2.10	0.70
5 Year	1.51	5.50	4.95	3.80	5 Year	6.00	6.05	3.95	3.60	2.45
7 Year	2.22	6.54	5.70	4.55	10 Year	6.80	7.00	5.20	4.95	3.70
10 Year	2.85	7.16	6.20	5.20	15 Year	7.00	7.15	5.70	5.45	4.05
30 Year	4.02	8.16	6.90	6.45	30 Year	7.20	7.375	6.20	5.80	4.80
					5 year EXTRA		6.50			

* Representative of recent non-rated issues underwritten by Ziegler retail sales (** representative of institutional sales)

TAX-EXEMPT MARKET INDICATORS

	<u>THIS WEEK</u>	<u>LAST WEEK</u>	<u>CHANGE</u>	<u>2010</u>	
				<u>HIGH</u>	<u>LOW</u>
Bond Buyer					
20 Bond Index	4.16	4.21	-0.05	4.44	4.16
11 Bond Index	3.89	3.94	-0.05	4.15	3.89
Revenue Bond Index	4.79	4.80	-0.01	4.99	4.79
30 Year MMD	3.95	3.97	-0.02	4.23	3.95
Weekly Tax-Exempt Volume (Bil)	4.00	5.02	-1.02	10.60	3.02
30 Day T/E Visible Supply (Bil)	6.23	5.34	+0.89	9.77	4.05
30 year "A" Rated Hospitals as a % of 30 Year Treasuries	144.27%	146.90%	-2.63%	142.10%	122.00%

INTEREST RATE COMPARISON

DATE	7-DAY T/E VRDB	PRIME RATE	FED FUNDS WEEKLY AVG.	13-WEEK T-BILL RATE	C.P.RATE TAXABLE	LIBOR (30-DAY)	30-YEAR T/E BONDS (A-AAA)		
8/06/10	0.22	3.25	0.20	0.14	0.19	0.29	5.80	-	4.80
07/30/10	0.25	3.25	0.18	0.14	0.23	0.30	5.85	-	4.85
07/23/10	0.28	3.25	0.21	0.14	0.18	0.32	5.85	-	4.85
07/16/10	0.24	3.25	0.19	0.14	0.19	0.33	5.90	-	4.90
07/09/10	0.22	3.25	0.18	0.14	0.21	0.34	5.85	-	4.90
07/02/10	0.22	3.25	0.15	0.16	0.14	0.35	5.85	-	4.90
06/25/10	0.28	3.25	0.18	0.12	0.18	0.35	5.90	-	4.95
06/18/10	0.30	3.25	0.19	0.09	0.19	0.35	5.90	-	4.95
06/11/10	0.28	3.25	0.19	0.07	0.20	0.35	5.80	-	4.90
06/04/10	0.24	3.25	0.21	0.12	0.21	0.35	5.70	-	4.85
05/28/10	0.27	3.25	0.22	0.16	0.23	0.35	5.70	-	4.85
05/21/10	0.29	3.25	0.21	0.15	0.21	0.34	5.60	-	4.90
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05/07/10	0.25	3.25	0.22	0.10	0.21	0.34	5.55	-	4.95
04/02/10	0.28	3.25	0.18	0.16	0.16	0.23	5.95	-	5.35
03/05/10	0.15	3.25	0.16	0.14	0.13	0.23	5.85	-	5.25
02/05/10	0.15	3.25	0.14	0.08	0.09	0.23	6.00	-	5.30
01/08/10	0.13	3.25	0.11	0.04	0.14	0.23	6.05	-	5.35
12/04/09	0.20	3.25	0.14	0.05	0.13	0.23	6.15	-	5.35
11/06/09	0.21	3.25	0.13	0.04	0.10	0.24	6.10	-	5.40
09/04/09	0.25	3.25	0.16	0.12	0.13	0.24	6.05	-	5.50
08/07/09	0.28	3.25	0.18	0.17	0.18	0.27	6.35	-	5.80
07/03/09	0.25	3.25	0.26	0.16	0.18	0.30	6.15	-	5.50