HEALTHCARE TRUST OF AMERICA, INC.
Form 10-K
March 16, 2010

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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-K

(Mark One)

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

For the fiscal year ended **December 31, 2009**

or

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

For the transition period from __________ to __________.

Commission file number: **000-53206**

HEALTHCARE TRUST OF AMERICA, INC.
(Exact name of registrant as specified in its charter)

Maryland	**20-4738467**
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)
16427 N. Scottsdale Road, Scottsdale, Arizona	**85254**
(Address of principal executive offices)	(Zip Code)

Registrant s telephone number, including area code: **(480) 998-3478**

Securities registered pursuant to Section 12(b) of the Act:

Title of each class	Name of each exchange on which registered
None	**None**

Securities registered pursuant to Section 12(g) of the Act:

Common Stock, $0.01 par value per share
(Title of Class)

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes **o** No **þ**

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act. Yes **o** No **þ**

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes þ No o

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

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K (§ 229.405 of this chapter) is not contained herein, and will not be contained, to the best of registrant s knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K. o

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

Large accelerated filer	o	Accelerated filer	o
Non-accelerated filer	þ (Do not check if a smaller reporting company)	Smaller reporting company	o

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Act). Yes o No þ

While there is no established market for the registrant s common stock, the aggregate market value of the registrant s common stock held by non-affiliates of the registrant as of June 30, 2009, the last business day of the registrant s most recently completed second fiscal quarter, was approximately $1,137,042,000, assuming a market value of $10.00 per share which is the price per share in our current offering.

As of March 12, 2010, there were 144,959,351 shares of common stock of the registrant outstanding.

DOCUMENTS INCORPORATED BY REFERENCE
None

Healthcare Trust of America, Inc.
(A Maryland Corporation)

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PART I

Item 1. Business.

The use of the words we, us or our refers to Healthcare Trust of America, Inc. and its subsidiaries, including Healthcare Trust of America Holdings, LP, except where the context otherwise requires.

OUR COMPANY

Healthcare Trust of America, Inc., formerly known as Grubb & Ellis Healthcare REIT, Inc., a Maryland corporation, was incorporated on April 20, 2006. We were initially capitalized on April 28, 2006 and consider that our date of inception.

2009 Highlights

We successfully transitioned from a fee-based sponsored REIT to a self-managed REIT in the third quarter of 2009 and substantially reduced our cost structure.

We completed an extensive transition of moving approximately 33,000 stockholder accounts and investor services, as well as over 4,000 financial advisor accounts, to DST Systems, Inc., our new transfer agent, on August 10, 2009.

We changed our name to Healthcare Trust of America, Inc. on August 24, 2009.

We successfully transitioned the dealer manager for our initial public offering, or our initial offering, to Realty Capital Securities, LLC, or RCS, an unaffiliated third party, on August 29, 2009.

We implemented a customized property management structure aimed at improving property operational performance at the asset and service provider levels, including the elimination of oversight fees, and a company-directed leasing plan to optimize occupancy levels. Accordingly, we transitioned property management services to nationally recognized property management groups each to manage a specific region beginning September 1, 2009 and reduced the fees we pay for property management services by more than 50%.

In order to take the necessary steps to transition to self-management, we amended our advisory agreement with Grubb & Ellis Healthcare REIT Advisor, LLC, or our former advisor, in 2008 to reduce fees paid to our former advisor for acquisition and asset management through the expiration of the advisory agreement, which expired on September 20, 2009. With the reduced fees, in addition to completing the transition to self-management in the third quarter, we realized gross savings of approximately $10,812,000 for 2009.

We completed 14 acquisitions with an aggregate purchase price of approximately $493,895,000, comprised of 54 medical office buildings totaling approximately 2,258,000 square feet and one real estate-related asset.

We maintained a leverage ratio of our debt to total assets of 32% and had cash on hand of $219,001,000 as of December 31, 2009.

Our occupancy held stable at over 90% from 2008 to 2009.

Our modified funds from operations, or MFFO, represented 70% of distributions paid during the 2009 fourth quarter and our MFFO represented 62% of distributions paid during all of 2009, up 100% from 2008.

Our Business

We provide stockholders the potential for income and growth through investment in a diversified portfolio of real estate properties, focusing primarily on medical office buildings and healthcare-related facilities. We have also invested to a limited extent in commercial office properties and other real estate related assets.

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However, we do not presently intend to invest more than 15.0% of our total assets in other real estate related assets. We focus primarily on investments that produce recurring income. We have qualified and elected to be taxed as a real estate investment trust, or REIT, for federal income tax purposes and we intend to continue to be taxed as a REIT.

As of December 31, 2009, we had made 53 geographically diverse acquisitions, 41 of which are medical office properties, seven of which are healthcare-related facilities, three of which are quality commercial office properties, and two of which are other real estate-related assets, comprising 179 buildings with 7,407,000 square feet of gross leasable area, or GLA, for an aggregate purchase price of $1,460,311,000, in 21 states.

We are conducting a best efforts initial public offering, in which we are offering up to 200,000,000 shares of our common stock for $10.00 per share and up to 21,052,632 shares of our common stock pursuant to our distribution reinvestment plan, or the DRIP, for $9.50 per share, aggregating up to $2,200,000,000. The initial offering will expire no later than March 19, 2010. As of December 31, 2009, we had received and accepted subscriptions in our initial offering for 136,958,459 shares of our common stock, or $1,368,087,211, excluding shares of our common stock issued under the DRIP.

On April 6, 2009, we filed a Registration Statement on Form S-11 with the United States Securities and Exchange Commission, or the SEC, with respect to a proposed follow-on public offering, or our follow-on offering, of up to 221,052,632 shares of our common stock. Our follow-on offering would include up to 200,000,000 shares of our common stock to be offered for sale at $10.00 per share and up to 21,052,632 shares of our common stock to be offered for sale pursuant to the DRIP at $9.50 per share. We have not issued any shares under this registration statement as it has not been declared effective by the SEC.

We conduct substantially all of our operations through Healthcare Trust of America Holdings, LP, or our operating partnership. Our internal management team manages our day-to-day operations and oversees and supervises our employees and outside service providers. We were formerly advised under the terms of an advisory agreement, as amended and restated on November 14, 2008, effective as of October 24, 2008, between us, our former advisor and Grubb & Ellis Realty Investors, LLC, or Grubb & Ellis Realty Investors, the managing member of our former advisor, or Advisory Agreement. The Advisory Agreement expired on September 20, 2009.

Our former advisor engaged affiliated entities, including but not limited to Triple Net Properties Realty, Inc., or Realty, and Grubb & Ellis Management Services, Inc., to provide various services to us, including but not limited to property management and leasing services. On July 28, 2009, we entered into property management and leasing agreements with the following companies, each to manage 5,091,000 square feet of our properties located in a specific geographic region: CB Richard Ellis, PM Realty Group, Hokanson Companies, The Plaza Companies, and Nath Companies. The remaining 2,317,000 square feet of triple net leased properties is managed by our in-house asset management team. On August 31, 2009, each of our subsidiaries terminated its management agreement with Realty.

Upon the effectiveness of our initial offering, we entered into a dealer manager agreement with Grubb & Ellis Securities, Inc., or Grubb & Ellis Securities, or our former dealer manager. On May 21, 2009, we provided notice to Grubb & Ellis Securities pursuant to the dealer manager agreement that we would proceed with a dealer manager transition pursuant to which Grubb & Ellis Securities would cease to serve as our dealer manager for our initial offering at the end of the day on August 28, 2009. Commencing August 29, 2009, RCS assumed the role of dealer manager for the remainder of the offering period pursuant to a new dealer manager agreement.

Transition to Self-Management

Our main objectives in amending the Advisory Agreement on November 14, 2008 were to reduce acquisition and asset management fees, eliminate the need to pay disposition or internalization fees, to set the framework for our transition to self-management and to create an enterprise value for our company. We started our transition to self-management in the fourth quarter of 2008. This transition is now complete and we consider ourselves to be self-managed.

Self-management is a corporate model based on internal management rather than external management. In general, non-traded REIT s are externally managed. With external management, a REIT is dependent upon an external advisor. An externally-managed REIT typically pays acquisition fees, disposition fees, asset management fees, property management fees and other fees to its external advisor for services provided. In contrast, under self-management, we are internally managed by our management team led by Scott D. Peters, our Chief Executive Officer, President and Chairman of the board of directors, under the direction of our Board of Directors. With a self-managed REIT, services such as acquisitions and asset management is performed in-house by the company s employees and fees paid to third parties are expected to be at market rates.

We are conducting an ongoing review of advisory services and dealer manager services previously provided by our former advisor and former dealer manager, to ensure that such services have been performed consistent with applicable agreements and standards. Based on our review to date, as well as ongoing actions by our former advisor and former dealer manager, we believe that our former advisor and our former dealer manager did not comply with all of their obligations under applicable agreements. As a result, we have provided them with notice of our claims under the agreements, as well as notice of other claims. They have disagreed with our positions, and we are engaged in ongoing discussions to resolve these issues. However, we do not anticipate that the disputes will have a material impact on our financial results or operations in the future.

Management Team. In July 2008, Mr. Peters assumed the positions of President and Chief Executive officer of our company on a full-time and exclusive basis. This was the first major step toward self-management. We have assembled a highly qualified and experienced management team which is focused on efficiency and performance to increase stockholder value. Our internal management team includes (1) Mr. Peters, our President and Chief Executive Officer, (2) Kellie S. Pruitt, our Chief Accounting Officer, Treasurer and Secretary, (3) Mark Engstrom, our Executive Vice President Acquisitions, (4) Amanda Houghton, Senior Vice President Asset Management and Finance, and (5) Katherine E. Black, Controller. We believe that our management team has the experience and expertise to efficiently and effectively operate our company.

Governance. An integral part of self-management is our experienced board of directors. Our board of directors spent a substantial amount of time overseeing our transition to self-management and continues to provide significant assistance to us as a self-managed company. We believe that our board of directors provides effective ongoing governance for our company and that our governance and management framework is one of our key strengths.

Significantly Reduced Cost. From inception through December 31, 2009, we incurred to our former advisor and its affiliates approximately $39,217,000 in acquisition fees; approximately $11,550,000 in asset management fees; approximately $5,252,000 in property management fees; and approximately $3,168,000 in leasing fees. We expect third party expenses associated with on-site property management and third party acquisition expenses, including legal fees, due diligence fees and closing costs, to remain approximately the same as under external management, relative to the amount of acquisitions completed. We believe that the total cost of self-management will be substantially less than the cost of external management. While our board of directors, including a majority of our independent directors, previously determined that the fees to our former advisor were competitive and commercially reasonable to us and on terms and conditions not less favorable to us than those available from other sponsors of non-traded REITs based on circumstances at that time, we now believe that by having our own employees manage our operations and retain third party providers, we will significantly reduce our cost structure.

No Internalization Fees. Unlike many other non-listed REITs that internalize or pay to acquire various management functions and personnel, such as advisory and asset management services, from their sponsor or advisor prior to listing on a national securities exchange for substantial fees, we will not be required to pay such fees under self-management.

We believe that by not paying such fees, as well as by operating more cost-effectively under self-management, we will save a substantial amount of money for the benefit of our stockholders. To the extent that our management and board of directors determine that utilizing third party service providers for certain services is more cost-effective than performing such services internally, we will pay for these services based on negotiated terms and conditions consistent with the current marketplace for such services on an as-needed basis.

Funding of Self-Management. We believe that the cost of self-management will be substantially less than the cost of external management. The initial step in becoming self-managed was amending the Advisory Agreement, on November 14, 2008, whereby we reduced acquisition fees from 3% to 2.5% of the purchase price (with further tiered adjustments based on gross acquisition value to accomplish an average acquisition fee of 2.25%) and reduced asset management fees from 1% to 0.5% of average invested assets. Upon expiration of the Advisory Agreement, we no longer pay asset management fees and we did not have to pay an internalization fee. Acquisition fees will not be recurring, except for any remaining acquisition fees to our former advisor for assets acquired with those remaining funds raised in our initial offering by our former dealer manager. In the third quarter of 2009, we became fully self-managed and also transitioned our property management services to nationally recognized property management groups for market-based fees. The reduced acquisition and asset management fees along with the savings from market-based property management fees in the third and fourth quarter resulted in a total gross savings of approximately $10,812,000 in 2009. The costs of self-management during 2009 was approximately $5,000,000, excluding one-time, non-recurring transition costs of $1,973,000, resulting in net savings of approximately $3,839,000. Therefore, the additional costs related to the transition to self-management was effectively funded by the cost savings in 2009. We anticipate that we will achieve substantial cost savings in the future as a result of reduced and/or eliminated acquisition fees, disposition fees, asset management fees, internalization fees and other outside fees.

Dedicated Management and Increased Accountability. Under self-management, our officers and employees work directly for our company and are not associated with any outside advisor or other third party service providers. Our management team has direct oversight of our employees, independent consultants and third party service providers. We believe that these direct reporting relationships along with our performance-based compensation programs and ongoing oversight by our management team create an environment for and will achieve increased accountability and efficiency.

Conflicts of Interest. We believe that self-management works to remove inherent conflicts of interest that exist between an externally advised REIT and its advisor. The elimination or reduction of these inherent conflicts of interest is one of the major reasons that we elected to proceed with self-management.

Developments During 2010

Pending Acquisitions

On February 10, 2010, we entered into a purchase and sale agreement for approximately $29,250,000 to acquire the Triad Technology Center in Baltimore, Maryland. The building is approximately 101,400 square feet and is 100% leased to the U.S. government and is occupied primarily by the National Institutes of Health.

On February 19, 2010, we entered into a purchase and sale agreement for approximately $45,700,000 to acquire a five building medical office portfolio located in Evansville, Indiana. The approximately 260,500 square foot portfolio is 100% master-leased to the Deaconess Clinic which is part of the Deaconess Health System. Deaconess Health System carries an A+ rating from both Standard & Poor s and Fitch and is the largest health system in Southern Indiana.

On February 22, 2010, we entered into a purchase and sale agreement for approximately $15,300,000 to acquire a three building, approximately 53,700 square feet medical office portfolio located in Hilton Head, South Carolina. The portfolio is located less than two miles from the Hilton Head Hospital, a wholly-owned hospital of Tenet Healthcare Corporation. Two of the three buildings in the portfolio are currently 100% occupied, and 35% of the portfolio is occupied by Hilton Head Hospital.

On February 24, 2010, we entered into a purchase and sale agreement for approximately $12,400,000 to acquire a three story, approximately 60,300 square foot medical office building in Sugar Land, Texas. The building is 100% leased with 83% of the space occupied by Texas Children s Health Centers through 2019.

On February 25, 2010, we entered into a purchase and sale agreement for approximately $10,500,000 to acquire an approximately 54,800 square foot medical office portfolio in Pearland, Texas. The portfolio consists of two buildings which are approximately ten miles south of the world-renowned Houston Medical Center and 15 miles south of Houston s central business district. The buildings are 100% and 98% occupied.

On March 2, 2010, we entered into a purchase and sale agreement for approximately $10,000,000 to acquire a 60,800 square foot medical office building located in located in Mount Pleasant, South Carolina, a suburb of Charleston. The Medical Center at East Cooper is 90% leased and is on the campus of East Cooper Regional Medical Center.

On March 3, 2010, we opened escrow with First American Title Company, and on or before March 26, 2010, our subsidiary plans to exercise its call option to buy for $3,900,000 100% of the interest owned by its joint venture partner in HTA Duke Chesterfield Rehab, LLC (Duke), which owns the Chesterfield Rehabilitation Center.

The completion of each of the pending acquisitions described above is subject to the satisfaction of a number of conditions, and we cannot guarantee that these acquisitions will be completed.

Completed Acquisitions

On March 4, 2010, we acquired an 80,652 square foot medical office portfolio for approximately $19,550,000 located in Atlanta, Georgia. The portfolio is 94% leased and is located approximately six miles west of South Fulton Medical Center, a 338-bed facility, rated Best Critical Care in Region by Healthgrades, a leading healthcare ratings organization.

On March 10, 2009, we acquired the King Street Medical Office Building for approximately $10,775,000. The 53,169 square foot building is located in Jacksonville, Florida. The King Street Medical Office Building is 100% occupied and is home to the Gary and Nancy Chartrand Heart & Vascular Center.

Offering Proceeds

As of March 12, 2010, we had received and accepted subscriptions in our initial offering for 144,959,351 shares of our common stock, or $1,448,044,000, excluding shares of our common stock issued under the DRIP.

Financing

In spite of the economic conditions impacting the debt market, we were able to secure long-term financing with certain life insurance companies for approximately $71,875,000 with an average loan term of 7.4 years and an average interest rate of 6.17%.

We received a commitment letter from one of our lenders to provide a senior secured loan facility in the amount of $35,000,000 with the ability to syndicate the facility with one or more financial institutions for up to $65,000,000. We are currently in discussions with various other lenders who have expressed an interest in participating in such a facility.

Our Structure

The following chart indicates our organizational structure.

(1) Our former advisor owns less than a 0.01% interest in our company and in our operating partnership.

Our principal executive offices are located at The Promenade, 16427 North Scottsdale Road, Suite 440, Scottsdale, AZ 85254 and our telephone number is (480) 998-3478. We maintain a web site at *www.htareit.com* at which there is additional information about us. The contents of that site are not incorporated by reference in, or otherwise a part of, this filing. We make our periodic and current reports available at *www.htareit.com* as soon as reasonably practicable after such materials are electronically filed with the SEC. They are also available for printing by any stockholder upon request.

INVESTMENT OBJECTIVES AND POLICIES

Investment Objectives

Our investment objectives are:

- to acquire quality properties that generate sustainable growth in cash flows from operations to pay regular cash distributions;
- to preserve, protect and return our stockholders capital contributions;
- to realize growth in the value of our investments upon our ultimate sale of such investments; and
- to be prudent, patient and deliberate, taking into account current real estate markets.

Each property we acquire is carefully and diligently reviewed and analyzed to make sure it is consistent with our investment objectives. Our goal is to at all times maintain a strong balance sheet and always have sufficient funds to deal with short- and long-term operating needs. Macro-economic disruptions have broadly impacted the economy and have caused an imbalance between buyers and sellers of real estate assets, including medical office buildings and other healthcare-related real estate assets. We anticipated that these tough economic conditions would create opportunities for our company to acquire such assets at higher capitalization rates, as the real estate market adjusted downward. In the fourth quarter of 2008 and first half of 2009, we opted not to proceed with certain deals which we determined merited re-pricing. As we entered the second half of 2009, we started to see attractive assets available for prices at higher capitalization rates. As a result, we were very active buying real estate in the third and fourth quarters of 2009. We had cash on hand of

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over $219,001,000 as of December 31, 2009, which we intend to use to continue to acquire assets that are priced at levels consistent with today s economy. We believe that during this turbulent economic cycle, our cash on hand will provide our company with opportunities to acquire medical office buildings and other healthcare-related real estate assets at favorable pricing.

We cannot assure our stockholders that we will attain these objectives or that our capital will not decrease. Our board of directors may change our investment objectives if it determines it is advisable and in the best interests of our stockholders.

Decisions relating to the purchase or sale of investments will be made by our management, subject to the oversight by our board of directors. See Item 10. Directors, Executive Officers and Corporate Governance for a description of the background and experience of our directors and officers.

Business Strategies

We seek to invest in a diversified portfolio of real estate and other real estate related assets, focusing primarily on investments that produce recurring income. Our real estate investments focus on medical office buildings and healthcare-related facilities. We have also invested to a limited extent in quality commercial office buildings and other real estate related assets. However, we do not presently intend to invest more than 15.0% of our total assets in other real estate related assets. Our investments in other real estate related assets will generally focus on forms of mortgage debt, common and preferred stock of public or private real estate companies and certain other securities. We seek to maximize long-term stockholder value by generating sustainable growth in cash flow and portfolio value. In order to achieve these objectives, we may invest using a number of investment structures which may include direct acquisitions, joint ventures, leveraged investments, issuing securities for property and direct and indirect investments in real estate. In order to maintain our exemption from regulation as an investment company under the Investment Company Act of 1940, as amended, or the Investment Company Act, we may be required to limit our investments in other real estate related assets.

In addition, when and as determined appropriate by our Chief Executive Officer, our board of directors and management, the portfolio may also include properties in various stages of development other than those producing current income. These stages would include, without limitation, unimproved land, both with and without entitlements and permits, property to be redeveloped and repositioned, newly constructed properties and properties in lease-up or other stabilization, all of which will have limited or no relevant operating histories and no current income. Our management makes this determination based upon a variety of factors, including the available risk adjusted returns for such properties when compared with other available properties, the appropriate diversification of the portfolio, and our objectives of realizing both recurring income and capital appreciation upon the ultimate sale of properties.

For each of our investments, regardless of property type, we seek to invest in properties with the following attributes:

> *Quality.* We seek to acquire properties that are suitable for their intended use with a quality of construction that is capable of sustaining the property s investment potential for the long-term, assuming funding of budgeted maintenance, repairs and capital improvements.
>
> *Location.* We seek to acquire properties that are located in established or otherwise appropriate markets for comparable properties, with access and visibility suitable to meet the needs of its occupants.
>
> *Market; Supply and Demand.* We focus on local or regional markets that have potential for stable and growing property level cash flow over the long-term. These determinations are based in part on an evaluation of local economic, demographic and regulatory factors affecting the property. For instance, we favor markets that

indicate a growing population and employment base or markets that exhibit potential limitations on additions to supply, such as barriers to new construction. Barriers to new construction include lack of available land, stringent zoning restrictions and regulatory restrictions. In addition, we generally seek to limit our investments in areas that have limited potential for growth.

Predictable Capital Needs. We seek to acquire properties where the future expected capital needs can be reasonably projected in a manner that would allow us to meet our objectives of growth in cash flow and preservation of capital and stability.

Cash Flow. We seek to acquire properties where the current and projected cash flow, including the potential for appreciation in value, would allow us to meet our overall investment objectives. We evaluate cash flow as well as expected growth and the potential for appreciation.

We will not invest more than 10.0% of the offering proceeds available for investment in unimproved or non-income producing properties or in other investments relating to unimproved or non-income producing property. A property: (1) not acquired for the purpose of producing rental or other operating income, or (2) with no development or construction in process or planned in good faith to commence within one year, will be considered unimproved or non-income producing property for purposes of this limitation. To date, we have not invested in unimproved or non-income producing properties or related investments.

We are not limited as to the geographic area where we may acquire properties. We are not specifically limited in the number or size of properties we may acquire or on the percentage of our assets that we may invest in a single property or investment. The number and mix of properties we acquire depends upon real estate and market conditions and other circumstances existing at the time we are acquiring our properties and making our investments and the amount of proceeds we raise in our offering and potential future offerings.

FINANCING POLICIES

We use and intend to continue to use secured and unsecured debt as a means of providing additional funds for the acquisition of properties and other real estate related assets. Our ability to enhance our investment returns and to increase our diversification by acquiring assets using additional funds provided through borrowing could be adversely impacted if banks and other lending institutions reduce the amount of funds available for the types of loans we seek. When interest rates are high or financing is otherwise unavailable on a timely basis, we may purchase certain assets for cash with the intention of obtaining debt financing at a later time.

We anticipate that aggregate borrowings, both secured and unsecured, will not exceed 60.0% of all of our properties combined fair market values, as determined at the end of each calendar year. For these purposes, the fair market value of each asset will be equal to the purchase price paid for the asset or, if the asset was appraised subsequent to the date of purchase, then the fair market value will be equal to the value reported in the most recent independent appraisal of the asset. Our policies do not limit the amount we may borrow with respect to any individual investment. As of December 31, 2009, our aggregate borrowings were 38.5% of all of our properties and other real estate related assets combined fair market values and 32% of our total assets.

Our aggregate secured and unsecured borrowings will be reviewed by our board of directors at least quarterly. Our charter precludes us from borrowing in excess of 300.0% of the value of our net assets. Net assets for purposes of this calculation are defined as our total assets (other than intangibles) valued at cost prior to deducting depreciation, reserves for bad debts and other non-cash reserves, less total liabilities. The preceding calculation is generally expected to approximate 75.0% of the sum of (1) the aggregate cost of our properties before non-cash reserves and depreciation and (2) the aggregate cost of our securities assets. However, we may temporarily borrow in excess of these amounts if such excess is approved by a majority of our independent directors and disclosed to stockholders in our next quarterly report, along with justification for such excess. In such event, we will review our debt levels at that time and take action to reduce any such excess as soon as practicable. As of March 15, 2010 and December 31, 2009, our leverage did not exceed 300.0% of the value of our net assets.

Our use of leverage increases the risk of default on loan payments and the resulting foreclosure of a particular asset. In addition, lenders may have recourse to assets other than those specifically securing the repayment of the indebtedness.

Our management will use its best efforts to obtain financing on the most favorable terms available to us and we will refinance assets during the term of a loan only in limited circumstances, such as when a decline in interest rates makes it beneficial to prepay an existing loan, when an existing loan matures or if an attractive investment becomes available and the proceeds from the refinancing can be used to purchase such investment. The benefits of the refinancing may include an increased cash flow resulting from reduced debt service requirements, an increase in distributions from proceeds of the refinancing, and an increase in diversification and assets owned if all or a portion of the refinancing proceeds are reinvested. We currently anticipate seeking fixed rate debt with longer-term maturities.

Our charter restricts us from borrowing money from any of our directors unless such loan is approved by a majority of our directors (including a majority of the independent directors) not otherwise interested in the transaction, as fair, competitive and commercially reasonable and no less favorable to us than comparable loans between unaffiliated parties.

BOARD REVIEW OF OUR INVESTMENT POLICIES

Our board of directors has established written policies on investments and borrowing. Our board is responsible for monitoring the administrative procedures, investment operations and performance of our company and our management to ensure such policies are carried out. Our charter requires that our independent directors review our investment policies at least annually to determine that our policies are in the best interest of our stockholders. Each determination and the basis thereof is required to be set forth in the minutes of our applicable meetings of our directors. Implementation of our investment policies also may vary as new investment techniques are developed.

As required by our charter, our independent directors have reviewed our policies outlined above and determined that they are in the best interest of our stockholders because: (1) they increase the likelihood that we will be able to acquire a diversified portfolio of income producing properties, thereby reducing risk in our portfolio; (2) there are sufficient property acquisition opportunities with the attributes that we seek; (3) our executive officers, directors and management have expertise with the type of real estate investments we seek; and (4) our borrowings have enabled us to purchase assets and earn rental income more quickly, thereby increasing our likelihood of generating income for our stockholders and preserving stockholder capital.

TAX STATUS

We have qualified and elected to be taxed as a REIT beginning with our taxable year ended December 31, 2007 under Sections 856 through 860 of the Code for federal income tax purposes and we intend to continue to be taxed as a REIT. To continue to qualify as a REIT for federal income tax purposes, we must meet certain organizational and operational requirements, including a requirement to pay distributions to our stockholders of at least 90.0% of our annual taxable income (computed without regard to the dividends paid deduction and excluding net capital gains). As a REIT, we generally are not subject to federal income tax on net income that we distribute to our stockholders.

If we fail to qualify as a REIT in any taxable year, we will then be subject to federal income taxes on our taxable income and will not be permitted to qualify for treatment as a REIT for federal income tax purposes for four years following the year during which qualification is lost unless the IRS grants us relief under certain statutory provisions. Such an event could have a material adverse effect on our results of operations and net cash available for distribution to stockholders.

DISTRIBUTION POLICY

In order to continue to qualify as a REIT for federal income tax purposes, among other things, we must distribute at least 90.0% of our annual taxable income to our stockholders. The amount of distributions we pay to our stockholders is determined by our board of directors and is dependent on a number of factors, including funds available for the payment of distributions, our financial condition, capital expenditure requirements and annual distribution requirements needed to maintain our status as a REIT under the Code. We have paid distributions monthly since February 2007 and if our investments produce sufficient cash flow, we expect to continue to pay distributions to our stockholders on a monthly basis. However, our board of directors could, at any time, elect to pay distributions quarterly to reduce administrative costs. Because our cash available for distribution in any year may be less than 90.0% of our taxable income for the year, we may obtain the necessary funds by borrowing, issuing new securities or selling assets to pay out enough of our taxable income to satisfy the distribution requirement.

See Item 5. Market for Registrant s Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities Distributions, for a further discussion on distribution rates approved by our board of directors.

COMPETITION

We compete with many other real estate investment entities, including financial institutions, institutional pension funds, real estate developers, other REITs, other public and private real estate companies and private real estate investors for the acquisition of medical office buildings and healthcare-related facilities. During the acquisitions process, we compete with others who have a comparative advantage in terms of size, capitalization, depth of experience, local knowledge of the marketplace, and extended contacts throughout the region. Any combination of these factors may result in an increased purchase price for real properties or other real estate related assets which may reduce the number of opportunities available that meet our investment criteria. If the number of opportunities that meet our investment criteria are limited, our ability to increase stockholder value may be adversely impacted.

We face competition in leasing available medical office buildings and healthcare-related facilities to prospective tenants. As a result, we may have to provide rent concessions, incur charges for tenant improvements, offer other inducements, or we may be unable to timely lease vacant space, all of which may have an adverse impact on our results of operations. At the time we elect to dispose of our properties, we will also be in competition with sellers of similar properties to locate suitable purchasers.

We believe our focus on medical office buildings and healthcare-related facilities and our relationships with healthcare providers allow us to effectively identify acquisition opportunities.

GOVERNMENT REGULATIONS

Many laws and governmental regulations are applicable to our properties and changes in these laws and regulations, or their interpretation by agencies and the courts, occur frequently.

Costs of Compliance with the Americans with Disabilities Act. Under the Americans with Disabilities Act of 1990, as amended, or the ADA, all places of public accommodation are required to comply with federal requirements related to access and use by disabled persons. Although we believe that we are in substantial compliance with present requirements of the ADA, none of our properties have been audited and we have only conducted investigations of a few of our properties to determine compliance. We may incur additional costs in connection with compliance with the ADA. Additional federal, state and local laws also may require modifications to our properties or restrict our ability to renovate our properties. We cannot predict the cost of compliance with the ADA or other legislation. We may incur substantial costs to comply with the ADA or any other legislation.

Costs of Government Environmental Regulation and Private Litigation. Environmental laws and regulations hold us liable for the costs of removal or remediation of certain hazardous or toxic substances which may be on our properties. These laws could impose liability without regard to whether we are responsible for the presence or release of the hazardous materials. Government investigations and remediation actions may have substantial costs and the presence of hazardous substances on a property could result in personal injury or similar claims by private plaintiffs. Various laws also impose liability on persons who arrange for the disposal or treatment of hazardous or toxic substances and such person often must incur the cost of removal or remediation of hazardous substances at the disposal or treatment facility. These laws often impose liability whether or not the person arranging for the disposal ever owned or operated the disposal facility. As the owner and operator of our properties, we may be deemed to have arranged for the disposal or treatment of hazardous or toxic substances.

Use of Hazardous Substances by Some of Our Tenants. Some of our tenants routinely handle hazardous substances and wastes on our properties as part of their routine operations. Environmental laws and regulations subject these tenants, and potentially us, to liability resulting from such activities. We require our tenants, in their leases, to comply with these environmental laws and regulations and to indemnify us for any related liabilities. We are unaware of any material noncompliance, liability or claim relating to hazardous or toxic substances or petroleum products in connection with any of our properties.

Other Federal, State and Local Regulations. Our properties are subject to various federal, state and local regulatory requirements, such as state and local fire and life safety requirements. If we fail to comply with these various requirements, we may incur governmental fines or private damage awards. While we believe that our properties are currently in material compliance with all of these regulatory requirements, we do not know whether existing requirements will change or whether future requirements will require us to make significant unanticipated expenditures that will adversely affect our ability to make distributions to our stockholders. We believe, based in part on engineering reports which are generally obtained at the time we acquire the properties, that all of our properties comply in all material respects with current regulations. However, if we were required to make significant expenditures under applicable regulations, our financial condition, results of operations, cash flow and ability to satisfy our debt service obligations and to pay distributions could be adversely affected.

SIGNIFICANT TENANTS

As of December 31, 2009, none of our tenants at our consolidated properties accounted for 10.0% or more of our aggregate annual rental revenue.

GEOGRAPHIC CONCENTRATION

As of December 31, 2009, we had interests in ten consolidated properties located in Texas, which accounted for 16.9% of our total rental income, interests in two consolidated properties located in South Carolina, which accounted for 13.0% of our total rental income, and interests in five consolidated properties located in Arizona, which accounted for 12.2% of our total rental income. This rental income is based on contractual base rent from leases in effect as of December 31, 2009. Accordingly, there is a geographic concentration of risk subject to fluctuations in each of these states economies

EMPLOYEES

As of December 31, 2009, we have 29 employees and all of our employees are 100% dedicated to our company on a full-time basis. Our current organizational structure is designed to support an asset base of $2.0 to $3.0 billion depending on the composition of the assets acquired, and we believe we have hired sufficient personnel to support this asset base. As we grow, we will add the appropriate staff to accommodate the increased size of our company.

FINANCIAL INFORMATION ABOUT INDUSTRY SEGMENTS

ASC 280, *Segment Reporting* (ASC 280) establishes standards for reporting financial and descriptive information about an enterprise s reportable segment. We have determined that we have one reportable segment, with activities related to investing in medical office buildings, healthcare-related facilities, commercial office properties and other real estate related assets. Our investments in real estate and other real estate related assets are geographically diversified and our chief operating decision maker evaluates operating performance on an individual asset level. As each of our assets has similar economic characteristics, tenants, and products and services, our assets have been aggregated into one reportable segment.

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Item 1A. Risk Factors.

Investment Risks

There is currently no public market for shares of our common stock. Therefore, it will be difficult for stockholders to sell their shares and, if they are able to sell their shares, they will likely sell them at a discount.

There currently is no public market for shares of our common stock. We do not expect a public market for our stock to develop prior to the listing of our shares on a national securities exchange, which we do not expect to occur in the near future and which may not occur at all. Additionally, our charter contains restrictions on the ownership and transfer of our shares, and these restrictions may inhibit our stockholders ability to sell their shares. We have adopted a share repurchase plan but it is limited in terms of the amount of shares which may be repurchased annually. Our board of directors may also limit, suspend, terminate or amend our share repurchase plan upon 30 days notice. Therefore, it will be difficult for our stockholders to sell their shares promptly or at all. If our stockholders are able to sell their shares, they may only be able to sell them at a substantial discount from the price paid. This may be the result, in part, of the fact that, at the time we make our investments, the amount of funds available for investment will be reduced by up to 11.5% of the gross offering proceeds which will be used to pay selling commissions and the dealer manager fee and organizational and offering expenses. We will also be required to use gross offering proceeds to pay acquisition expenses. Unless our aggregate investments increase in value to compensate for these fees and expenses, which may not occur, it is unlikely that our stockholders will be able to sell their shares, whether pursuant to our share repurchase plan or otherwise, without incurring a substantial loss. We cannot assure our stockholders that their shares will ever appreciate in value to equal the price paid for the shares. Thus, prospective stockholders should consider the purchase of shares of our common stock as illiquid and a long-term investment, and our stockholders must be prepared to hold their shares for an indefinite length of time.

We may not have sufficient cash available from operations to pay distributions, and, therefore, distributions may include a return of capital.

Distributions payable to stockholders may include a return of capital, rather than a return on capital. We expect to continue to make monthly distributions to our stockholders. The actual amount and timing of distributions will be determined by our board of directors in its discretion and typically will depend on the amount of funds available for distribution, which will depend on items such as current and projected cash requirements and tax considerations. As a result, our distribution rate and payment frequency may vary from time to time. We may not have sufficient cash available from operations to pay distributions required to maintain our status as a REIT and may need to use proceeds from our offerings or borrowed funds to make such cash distributions. Additionally, if the aggregate amount of cash distributed in any given year exceeds the amount of our REIT taxable income generated during the year, the excess amount will be deemed a return of capital, which will decrease our stockholders tax basis in their investment in shares of our common stock. Our organizational documents do not establish a limit on the amount of net proceeds we may use to fund distributions.

We may not have sufficient cash available from operations to pay distributions, and, therefore, distributions may be paid, without limitation, with offering proceeds or borrowed funds.

The amount of the distributions we make to our stockholders will be determined by our board of directors and is dependent on a number of factors, including funds available for payment of distributions, our financial condition, capital expenditure requirements and annual distribution requirements needed to maintain our status as a REIT. If our cash flow from operations is less than the distributions our board of directors determines to pay, we would be required to pay our distributions, or a portion thereof, with proceeds from our offerings or borrowed funds. As a result, the amount of proceeds available for investment and operations would be reduced, or we may incur additional interest expense as a result of borrowed funds.

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As of December 31, 2009, we had made 53 geographically diverse acquisitions and have identified a limited number of additional properties to acquire with the net proceeds we will receive from the future equity raise, and stockholders are therefore unable to evaluate the economic merits of most of our future investments prior to purchasing shares of our common stock.

As of December 31, 2009, we have made 53 geographically diverse acquisitions with the net proceeds from our initial offering. As of December 31, 2009, we have identified a limited number of additional potential properties to acquire with the net proceeds we will receive from our offerings. Other than these 53 geographically diverse acquisitions, our stockholderases in other operating costs are due to inflationary increases and increases in accruals for professional liability claims of $1,996,000. These increases were offset in part due to decreases in workers compensation ($226,000). In addition, salaries, wages and benefits and other operating expenses increased by $1,198,000 and $1,012,000 due to the acquisition of our 200 long-term care beds facility in March 2006.

Nine Months Ended September 30, 2006 Compared to Nine Months Ended September 30, 2005.

Results for the nine month period ended September 30, 2006 include a 4.6% increase in net revenues compared to the same period in 2005. Net income increased 10.0% after excluding the consideration of the after tax effect of the recovery of a note receivable previously written off. Net patient revenues increased $21,310,000 or 6.0% compared to the same period last year. Medicaid rate changes that became effective October 1, 2005 increased our revenues for the 2006 period by approximately $4,085,000. The acquisition of our 200 bed long-term care facility located in Town and Country, Missouri added approximately $4,925,000 to net patient revenues.

The total census at owned and leased centers for the nine months averaged 93.9% which is unchanged from the same period a year ago.

Other revenues decreased $2,690,000 or 5.6% in 2006 to $45,409,000 from $48,099,000 in 2005. The decrease is primarily due to decreased collections (compared to the prior year) of approximately $5,208,000 in management and accounting service fees and $3,507,000 in insurance service revenues. The prior year nine month period included approximately $4,500,000 of management fees that previously had been doubtful of collection. Insurance services revenues decreased due to decreased premiums for workers' compensation from our wholly-owned insurance subsidiary, partially offset by increased premiums for health insurance. As described in our critical accounting policies, revenues from accounting services fluctuate from period to period because collections for some customers are not certain of receipt. In the 2005 nine month period, we recognized $4,500,000 of fees received in 2005 but had been doubtful of collection in prior years. During the nine months ended September 30, 2006, NHC provided management and accounting and financial services for 32 facilities as compared to 37 facilities during the nine months ended September 30, 2005.

Decreases in other revenues were offset in part due to the recognition of our equity in the earnings of an unconsolidated investment (Caris HealthCare, L.P.) of approximately $2,892,000. In future quarters , earnings from Caris in 2006 are expected to total between $500,000 and $800,000 per quarter. Other revenues also increased due to increases in interest income.

Total costs and expenses for the 2006 nine months increased $7,500,000 or 2.0% to $379,646,000 from $372,146,000. Salaries, wages and benefits, the largest operating costs of this service company, increased $9,182,000 or 4.3% to $223,839,000 from $214,657,000. Other operating expenses increased $8,217,000 or 7.3% to $121,075,000 for the 2006 period compared to $112,858,000 in the 2005 period. Rent expense decreased $427,000 to $30,808,000 compared to $31,235,000 in the 2005 period. Depreciation and amortization decreased $729,000 or 6.5% to $10,472,000 from $11,201,000. Interest costs decreased $434,000 to $761,000.

Increases in salaries, wages and benefits compared to the nine months last year are due to inflationary wage increases and share compensation costs. Share compensation costs totaled $1,985,000 in the 2006 nine month period and are being expensed by us in 2006 due to the adoption of SFAS 123(R), Share-Based Payment. Approximately $860,000 of the $1,985,000 cost relates to the grant of stock options to independent directors which vested immediately upon grant and, therefore, will not add any expense in future quarters. These comparative cost increases were offset in part by approximately $4,339,000 in decreased workers compensation and health insurance claims accrued. Increases in other operating costs are due to inflationary increases offset in part due to decreases in the cost of health insurance ($1,347,000) and workers compensation ($851,000). In addition, salaries, wages and benefits and other operating expenses increased by $2,883,000 and $2,309,000 due to the acquisition of our 200 long-term care beds facility in March 2006.

Expenses for the nine months ended September 30, 2006 include the recovery of a note receivable ($7,309,000) from a health care center we manage in Nashville, Tennessee which had been previously written off. Expenses for the nine months ended September 30, 2005 included a loss of $1,000,000 for the write-off of a note receivable. This note receivable is due from a 120-bed long-term health care center in Missouri that we manage. During the nine months ended September 30, 2005, as a result of increased operating costs and the lack of increase in reimbursement rates, the cash flows of this center declined and the center has not made a principal payment on this note since December 31, 2001. Based on an analysis consistent with the provisions of Statement of Financial Accounting Standards No. 114, "Accounting by Creditors for Impairment of a Loan - an Amendment of FASB Statements No. 5 and 15", we concluded that a write-down of $1,000,000 was required. We continue to monitor closely our other notes receivable from centers to which we provide management or accounting services.

Liquidity and Capital Resources

Sources and Uses of Funds

Our primary sources of cash include revenues from the healthcare and senior living facilities we operate, insurance services, management services and accounting services. Our primary uses of cash include salaries, wages and other operating costs of our home office and the facilities we operate, the cost of additions to and acquisitions of real property, rent expenses, debt service payments (including principal and interest) and dividend distributions. These sources and uses of cash are reflected in our Consolidated Statements of Cash Flows and are discussed in further detail below. The following is a summary of our sources and uses of cash flows (dollars in thousands):

	Three Months Ended September 30		Three Month Change		Nine Months Ended September 30		Nine Month Change	
	2006	2005	$	%	2006	2005	$	%
Cash and Cash equivalents at beginning of period	$66,716	$40,764	$25,952	63.7%	$60,870	$40,601	$20,269	49.9%
Cash provided from operating activities	8,666	11,620	(2,954)	25.4%	35,673	39,138	(3,465)	8.9%
Cash used in investing activities	(22,812)	(5,201)	(17,611)	338.6%	(39,818)	(28,661)	(11,157)	38.9%
Cash provided by (used in) financing activities	(2,293)	(2,068)	(225)	10.8%	(6,448)	(5,963)	(485)	8.1%
Cash and cash equivalents at end of period	$50,277	$45,115	$ 5,162	11.4%	$50,277	$45,115	$ 5,162	11.4%

Net cash provided by operating activities during the first nine months of 2006 totaled $35,673,000 compared to $39,138,000 provided in the same period last year. Cash provided by operating activities is composed primarily of net income plus depreciation and increases in accrued liabilities and reserves and deferred income and other non-current liabilities, offset by increases in accounts receivable and decreases in accrued payroll.

Cash flows used in investing activities during the first nine months of 2006 totaled $39,818,000 compared to $28,661,000 used in investing activities in the same period in 2005. Cash used for additions to property and equipment totaled $26,210,000 in 2006 compared to $11,265,000 in 2005. Construction of one 30 bed and of one 60 bed addition have been completed this year, while construction is ongoing on two additional 60 bed additions. Additions also include the acquisition of one 200 bed center.

Investments in notes receivable were zero in 2006, compared to $1,205,000 used last year. Collections of notes receivable generated $1,601,000 in 2006 compared to $130,000 in 2005. Cash used to purchase marketable securities totaled $4,123,000 compared to $2,026,000 of cash used to purchase marketable securities in 2005. Distribution for unconsolidated investments totaled $151,000 in 2006 compared to $147,000 in 2005. In 2006, cash in the amount of $45,490,000 was used to purchase restricted marketable securities and cash was provided in the amount of $34,253,000 by a decrease in restricted cash. In the prior year, cash flows were decreased $15,175,000 for increases in restricted cash and cash in the amount of $733,000 was provided by the sale of restricted marketable securities. Restricted cash is primarily related to professional liability insurance, workers' compensation insurance and health insurance. Restricted marketable securities are related to professional liability insurance, workers' compensation insurance and health insurance.

Cash used in financing activities totaled $6,448,000 in the nine months ended September 30, 2006 compared to $5,936 used in financing activities for the same period in 2005. Cash used for payments of debt totaled $1,618,000 and dividend payments to shareholders totaled $5,893,000. In the prior year, cash flows used totaled $1,687,000 for payments on debt and $4,884,000 for payments of dividends. Tax benefits from exercise of stock options provided cash of $230,000 in 2006 and zero in 2005.

At September 30, 2006, our ratio of long-term debt to total capitalization (total debt plus deferred income plus shareholders equity) is 4.9%.

Table of Contractual Cash Obligations

Our contractual cash obligations for periods subsequent to September 30, 2006 are as follows:

	Total	Less than 1 Year	2-3 Years	4-5 years	After 5 Years
			(in thousands)		
Long-term debt - principal	$ 14,411	$ 2,525	$11,886	$ --	$ --
Long-term debt - interest	1,324	1,048	276	--	--
Guaranteed debt	1,044	--	--	--	1,044
Obligation to complete construction	6,374	6,374	--	--	--
Obligation to purchase senior secured notes from financial institutions	5,636	2,871	2,765	--	--
Operating leases	691,912	48,097	99,320	99,320	445,175
Total Contractual Cash Obligations	$720,701	$60,915	$114,247	$99,320	$446,219

The guaranteed debt obligation of $1,044,000 represents our estimated obligation under a loan guarantee to a long-term health care center. As discussed in the section "Debt Guarantees", the $5,636,000 obligation represents our estimated obligation related to senior secured notes between National and the National Health Corporation Leveraged Employee Stock Ownership Plan (the "ESOP") and certain lending institutions. In addition to the guaranteed debt obligation shown in the table above, we have guaranteed debt obligations of certain other entities totaling approximately $5,214,000. These guarantees are not included in the table above because we do not anticipate material obligations under these commitments.

Our current cash on hand, marketable securities, short-term notes receivable, operating cash flows, and as needed, our borrowing capacity are expected to be adequate to meet these contractual obligations and to finance our operating requirements, growth and development plans.

We started paying quarterly dividends in the second quarter of 2004 and anticipate the continuation of dividend payments as approved quarterly by the Board of Directors.

Guarantees and Contingencies

Debt Guarantees-

In addition to our primary debt obligations, which are included in our consolidated financial statements, we have guaranteed the debt obligations of certain other entities. Those guarantees, which are not included as debt obligations in our consolidated financial statements, total $10,850,000 at September 30, 2006 and include $5,214,000 of debt of managed and other long-term health care centers and $5,636,000 of debt of National Health Corporation ("National") and the National Health Corporation Leveraged Employee Stock Ownership Plan (the "ESOP").

The $5,214,000 of guarantees of debt of managed and other long-term health care centers relates to first mortgage debt obligations of three long-term health care centers to which we provide management or accounting services. We have agreed to guarantee these obligations in order to obtain management or accounting services agreements. For this service, we charge an annual guarantee fee of 1.0% to 2% of the outstanding principal balance guaranteed, which fee is in addition to our management or accounting services fee. All of this guaranteed indebtedness is secured by first mortgages, pledges of personal property, accounts receivable, marketable securities and, in certain instances, the personal guarantees of the owners of the facilities.

The $5,636,000 of guarantees of debt of National and the ESOP relates to senior secured notes held by financial institutions. The total outstanding balance of National and the ESOP's obligations under these senior secured notes is $9,090,000. Of this obligation, $3,454,000 has been included in our debt obligations because we are a direct obligor on this indebtedness. The remaining $5,636,000, which is not included in our debt obligations because we are not a direct obligor, is due from NHI to National and the ESOP. Additionally, under the amended terms (dated March 31, 2005) of these note agreements, the right of the lending institutions to require NHC to purchase the notes at par value under a guaranty and contingent purchase agreement has been removed.

As of September 30, 2006, our maximum potential loss related to the guarantees is $10,850,000 which is the outstanding balance of the guaranteed debt obligations. We have accrued approximately $1,044,000 representing the estimated fair value of our guarantees, which is included in other non-current liabilities in the consolidated balance sheets.

Debt Cross Defaults

Through a guarantee agreement, our $3,454,000 senior secured notes and our $5,636,000 guarantee described above have cross-default provisions with other debt of National and the ESOP. We currently believe that National and the ESOP are in compliance with the terms of their debt agreements.

New Accounting Pronouncements

In February 2006, the FASB issued FAS No. 155, "Accounting for Certain Hybrid Financial Instruments - an amendment to FASB Statements No. 133 and 140" (FAS 155). FAS 155 simplifies the accounting for certain hybrid financial instruments containing embedded derivatives. FAS 155 allows fair value measurement for any hybrid financial instrument that contains an embedded derivative that otherwise would require bifurcation under FAS 133. In addition, it amends FAS 140 to eliminate the prohibition on a qualifying special-purpose entity from holding a derivative financial instrument that pertains to a beneficial interest other than another derivative financial instrument. The Company will adopt the provisions of FAS 155 beginning in fiscal 2007. The implementation of FAS 155 is not expected to have a material impact on the Company's consolidated financial statements.

In March 2006, the FASB issued SFAS No. 156, "Accounting for Servicing of Financial Assets - an amendment of FASB Statement No. 140." This Statement amends FASB Statement No. 140, "Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities," with respect to the accounting for separately recognized servicing assets and servicing liabilities. This Statement clarifies when servicing rights should be separately accounted for, requires companies to account for separately recognized servicing rights initially at fair value, and gives companies the option of subsequently accounting for those servicing rights at either fair value or under the amortization method. SFAS 156 is effective for the Company beginning January 1, 2007. The implementation of FAS 156 is not expected to have a material impact on the Company's consolidated financial statements.

In July 2006, the FASB issued Interpretation No. 48 ("FIN 48"), "Accounting for Uncertainty in Income Taxes - An Interpretation of FASB Statement No. 109." FIN 48 prescribes a recognition threshold and measurement attribute for how a company should recognize, measure, present, and disclose in its financial statements uncertain tax positions that the company has taken or expects to take on a tax return. FIN 48 will require that the financial statements reflect expected future tax consequences of such positions presuming the taxing authorities' full knowledge of the position and all relevant facts, but without considering time values. FIN 48 is effective for annual periods beginning after December 15, 2006. We are currently evaluating the impact of adopting FIN 48 on our financial statements. Upon adoption, the cumulative effect of applying the provision of FIN 48 will be reported as an adjustment to the opening balance of retained earnings for that fiscal year.

Forward-Looking Statements

References throughout this document to the Company include National HealthCare Corporation and its wholly-owned subsidiaries. In accordance with the Securities and Exchange Commission's "Plain English" guidelines, this Quarterly Report on Form 10-Q has been written in the first person. In this document, the words "we", "our", "ours" and "us" refer only to National HealthCare Corporation and its wholly-owned subsidiaries and not any other person.

This Quarterly Report on Form 10-Q and other information we provide from time to time, contains certain "forward-looking" statements as that term is defined by the Private Securities Litigation Reform Act of 1995. All statements regarding our expected future financial position, results of operations or cash flows, continued performance improvements, ability to service and refinance our debt obligations, ability to finance growth opportunities, ability to control our patient care liability costs, ability to respond to changes in government regulations, ability to execute our three-year strategic plan, and similar statements including, without limitations, those containing words such as "believes", "anticipates", "expects", "intends", "estimates", "plans", and other similar expressions are forward-looking statements.

Forward-looking statements involve known and unknown risks and uncertainties that may cause our actual results in future periods to differ materially from those projected or contemplated in the forward-looking statements as a result of, but not limited to, the following factors:

* national and local economic conditions, including their effect on the availability and cost of labor, utilities and materials;

* the effect of government regulations and changes in regulations governing the healthcare industry, including our compliance with such regulations;

* changes in Medicare and Medicaid payment levels and methodologies and the application of such methodologies by the government and its fiscal intermediaries;

* liabilities and other claims asserted against us, including patient care liabilities, as well as the resolution of current litigation (see "Note 5: Legal Proceedings);

* the ability of third parties for whom we have guaranteed debt to refinance certain short term debt obligations;

* the ability to attract and retain qualified personnel;

* the availability and terms of capital to fund acquisitions and capital improvements;

* the competitive environment in which we operate;

* the ability to maintain and increase census levels; and

* demographic changes.

See the notes to the quarterly financial statements, and "Item 1. Business" as is found in our 2005 Annual Report on Form 10-K for a discussion of various governmental regulations and other operating factors relating to the healthcare industry and the risk factors inherent in them. This may be found on our web side at www.nhccare.com. You should carefully consider these risks before making any investment in the Company. These risks and uncertainties are not the only ones facing us. There may be additional risks that we do not presently know of or that we currently deem immaterial. If any of the risks actually occur, our business, financial condition or results of operations could be materially adversely affected. In that case, the trading price of our shares of stock could decline, and you may lose all or part of your investment. Given these risks and uncertainties, we can give no assurances that these forward-looking statements will, in fact, transpire and, therefore, caution investors not to place undue reliance on them.

Item 3. Quantitative and Qualitative Disclosure About Market Risk.

Interest Rate Risk

Our cash and cash equivalents consist of highly liquid investments with an original maturity of less than three months. As a result of the short-term nature of our cash instruments, a hypothetical 10% change in interest rates would have no impact on our future earnings and cash flows related to these instruments. Approximately $19.2 million of our notes receivable bear interest at fixed interest rates. As the interest rates on these notes receivable are fixed, a hypothetical 10% change in interest rates would have no impact on our future earnings and cash flows related to these instruments. Approximately $1.2 million of our notes receivable bear interest at variable rates (generally at prime plus 2%). Because the interest rates of these instruments are variable, a hypothetical 10% change in interest rates would result in a related increase or decrease in annual interest income of approximately $12,000. As of September 30, 2006, $10.3 million of our long-term debt bear interest at fixed interest rates. Because the interest rates of these instruments are fixed, a hypothetical 10% change in interest rates would have no impact on our future earnings and cash flows related to these instruments. The remaining $4.1 million of our long-term debt and debt serviced by other parties bear interest at variable rates. Because the interest rates of these instruments are variable, a hypothetical 10% change in interest rates would result in a related increase or decrease in annual interest expense of approximately $24,000.

Equity Price Risk

We consider our investments in marketable securities as "available for sale" securities and unrealized gains and losses are recorded in stockholders' equity in accordance with Statement of Financial Accounting Standards No. 115. The investments in marketable securities are recorded at their fair market value based on quoted market prices. Thus, there is exposure to equity price risk, which is the potential change in fair value due to a change in quoted market price. Hypothetically, a 10% change in quoted market prices would result in a related 10% change in the fair value of our investments in marketable securities.

Item 4. Controls and Procedures.

As of September 30, 2006, an evaluation was performed under the supervision and with the participation of the Company's management, including the Chief Executive Officer ("CEO") and Principal Accounting Officer ("PAO"), of the effectiveness of the design and operation of the Company's disclosure controls and procedures. Based on that evaluation, the Company's management, including the CEO and PAO, concluded that the Company's disclosure controls and procedures were effective as of September 30, 2006. There have been no changes in the Company's internal controls over financial reporting during the quarter ended September 30, 2006 that have materially affected, or are reasonably likely to materially affect, the Company's internal control over financial reporting.

PART II. OTHER INFORMATION

Item 1. Legal Proceedings.

For a discussion of prior, current and pending litigation of material significance to NHC, please see Note 4 of this Form 10-Q.

Item 1A. Risk Factors.

During the nine months ended September 30, 2006, there were no material changes to the risk factors that were disclosed in Item 1A of National HealthCare Corporation's Annual Report on Form 10-K for the year ended December 31, 2005.

Item 2. Unregistered Sales of Equity Securities and Use of Proceeds. Not applicable

Item 3. Defaults Upon Senior Securities. None

Item 4. Submission of Matters to Vote of Security Holders. None

Item 5. Other Information. None

Item 6. Exhibits.

(a) List of exhibits

Exhibit No.	Description
31.1	Rule 13a-14(a)/15d-14(a) Certification of Chief Executive Officer
31.2	Rule 13a-14(a)/15d-14(a) Certification of Principal Financial Officer
32	Certification pursuant to 18 U.S.C. Section 1350 by Chief Executive Officer and Principal Financial Officer

SIGNATURES

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

	NATIONAL HEALTHCARE CORPORATION (Registrant)
Date November 9, 2006	/s/ Robert G. Adams Robert G. Adams President Chief Executive Officer
Date November 9, 2006	/s/ Donald K. Daniel Donald K. Daniel Senior Vice President and Controller (Principal Financial Officer)