

15-037

Alden Management Services, Inc.

Memo

To: John Kniery
From: Steve Kroll
cc: Joan Carl; Randi Schullo
Date: August 19,
Re: Waterford Courts CON Application

RECEIVED

AUG 19 2015

HEALTH FACILITIES &
SERVICES REVIEW BOARD

His letter will clarify our phone conversation of Monday, August 17th. Courts of Waterford is financed with a mortgage insured by the US Department of Housing and Urban Development. The loan requires that the project maintain a replacement reserve to be used to repair, replace or improve the project. Monthly deposits are made to this account and the funds are held by the lender. These funds are assets of the project. We will be using this reserve fund to pay the expenses related to this application. As a result no new additional debt will be incurred nor will operating cash be used.

I have attached a copy of the audited financial statements of the project as of December 31, 2014. The Balance sheet on Page 3 of the audit report reflects this asset under the **Restricted Funds** section and reflects a balance of \$812,607 designated as replacement reserve. If you have any further questions, please feel free to call me at (773) 724-6305.

Steve Kroll

WATERFORD REHAB AND COURTS, LLC

(FHA Project No. 071-43233 / 071-15035)

Aurora, Illinois

FINANCIAL STATEMENTS

Including Independent Auditors' Report

As of and for the Years Ended December 31, 2014 and 2013

The following name is the independent auditor
contact regarding the above project:

Corey Tremaine, CPA, Partner
Baker Tilly Virchow Krause, LLP
777 E Wisconsin Avenue, Floor 32
Milwaukee, Wisconsin 53202
414 777 5500
EIN: 39-0859910

WATERFORD REHAB AND COURTS, LLC

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INDEPENDENT AUDITORS' REPORT

To the Members
Waterford Rehab and Courts, LLC
Aurora, Illinois

Report on the Financial Statements

We have audited the accompanying financial statements of Waterford Rehab and Courts, LLC (the company) which comprise the balance sheets as of December 31, 2014 and 2013, and the related statements of operations, members' deficit and cash flows for the years then ended, and the related notes to the financial statements.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditors' Responsibility

Our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditors' judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the company's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the company's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

To the Members
Waterford Rehab and Courts, LLC

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Waterford Rehab and Courts, LLC as of December 31, 2014 and 2013, and the results of its operations, changes in members' deficit and cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

Other Matters

Other Information

Our audits were conducted for the purpose of forming an opinion on the financial statements as a whole. The supplemental information provided, as identified in the table of contents, is presented for purposes of additional analysis as required by the *Consolidated Audit Guide for Audits of HUD-Assisted Programs (the Guide)*, issued by the U.S. Department of Housing and Urban Development, Office of the Inspector General and is not a required part of the financial statements. Such information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the financial statements. The information has been subjected to the auditing procedures applied in the audit of the financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the financial statements or to the financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the information is fairly stated in all material respects in relation to the financial statements as a whole.

Other Reporting Required by Government Auditing Standards

In accordance with *Government Auditing Standards*, we have also issued our report dated March 18, 2015 on our consideration of the company's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, grant agreements, and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the company's internal control over financial reporting and compliance.

Baker Tilly Vachow Knause, LLP

Milwaukee, Wisconsin
March 18, 2015

WATERFORD REHAB AND COURTS, LLC

BALANCE SHEETS
As of December 31, 2014 and 2013

	<u>2014</u>	<u>2013</u>
ASSETS		
CURRENT ASSETS		
Cash and cash equivalents	\$ 79,301	\$ 111,621
Current portion of note receivable - related party	50,965	48,109
Accrued interest receivable - related party	14,473	14,705
Prepaid expenses	<u>64,821</u>	<u>50,184</u>
Total Current Assets	<u>209,560</u>	<u>224,619</u>
RESTRICTED FUNDS		
Escrow deposits	139,941	159,205
Replacement reserve	<u>812,607</u>	<u>1,039,511</u>
Total Restricted Funds	<u>952,548</u>	<u>1,198,716</u>
NET PROPERTY AND EQUIPMENT	<u>14,872,614</u>	<u>15,392,594</u>
OTHER ASSETS		
Deferred financing costs, net	244,961	256,701
Note receivable - related party, net of current portion	<u>2,953,918</u>	<u>3,004,883</u>
Total Other Assets	<u>3,198,879</u>	<u>3,261,584</u>
TOTAL ASSETS	<u>\$ 19,233,601</u>	<u>\$ 20,077,513</u>
LIABILITIES AND MEMBERS' DEFICIT		
CURRENT LIABILITIES		
Accounts payable	\$ -	\$ 4,236
Accrued interest - mortgage	65,019	65,765
Accrued interest - operating loss loan	13,199	13,432
Accrued property taxes	101,600	117,400
Prepaid tenant rents	140,330	112,705
Current portion of long-term debt	<u>301,106</u>	<u>289,140</u>
Total Current Liabilities	621,254	602,678
LONG-TERM LIABILITIES		
Long-term debt	<u>22,633,128</u>	<u>22,934,234</u>
Total Liabilities	23,254,382	23,536,912
MEMBERS' DEFICIT	<u>(4,020,781)</u>	<u>(3,459,399)</u>
TOTAL LIABILITIES AND MEMBERS' DEFICIT	<u>\$ 19,233,601</u>	<u>\$ 20,077,513</u>

See accompanying notes to financial statements.

WATERFORD REHAB AND COURTS, LLC

STATEMENTS OF OPERATIONS For the Years Ended December 31, 2014 and 2013

	<u>2014</u>	<u>2013</u>
REVENUES		
Net rental revenue	\$ 1,296,504	\$ 1,336,362
RENTAL EXPENSES		
General and administrative	7,476	9,890
Operating and maintenance	-	7,806
Taxes and insurance	<u>100,938</u>	<u>140,264</u>
Total Rental Expenses	<u>108,414</u>	<u>157,960</u>
Net Rental Income	<u>1,188,090</u>	<u>1,178,402</u>
FINANCIAL INCOME (EXPENSE)		
Interest income	175,844	178,706
Interest expense	(944,040)	(955,568)
Mortgage insurance	<u>(115,338)</u>	<u>(111,919)</u>
Net Financial Expense	<u>(883,534)</u>	<u>(888,781)</u>
Income Before Other Expenses	<u>304,556</u>	<u>289,621</u>
OTHER INCOME (EXPENSE)		
Gain on involuntary conversion	70,075	-
Depreciation	(786,425)	(769,352)
Amortization	<u>(11,740)</u>	<u>(11,896)</u>
Net Other Expense	<u>(728,090)</u>	<u>(781,248)</u>
NET LOSS	<u>\$ (423,534)</u>	<u>\$ (491,627)</u>

See accompanying notes to financial statements.

WATERFORD REHAB AND COURTS, LLC

STATEMENTS OF MEMBERS' DEFICIT For the Years Ended December 31, 2014 and 2013

BALANCE , December 31, 2012	\$ (2,890,191)
Net loss	(491,627)
Members' contributions	57,728
Members' distributions	<u>(135,309)</u>
BALANCE , December 31, 2013	(3,459,399)
Net loss	(423,534)
Members' distributions	<u>(137,848)</u>
BALANCE , December 31, 2014	<u>\$ (4,020,781)</u>

See accompanying notes to financial statements.

Statements of Cash Flows Follow

WATERFORD REHAB AND COURTS, LLC

STATEMENTS OF CASH FLOWS For the Years Ended December 31, 2014 and 2013

	<u>2014</u>	<u>2013</u>
CASH FLOWS FROM OPERATING ACTIVITIES		
Cash received from tenants, agencies and other sources	\$ 1,324,129	\$ 1,331,864
Interest received	176,076	178,925
General and administrative expenses paid	(11,712)	(10,959)
Operating and maintenance expenses paid	-	(7,806)
Taxes and insurance paid	(246,713)	(220,108)
Interest paid	<u>(945,019)</u>	<u>(956,507)</u>
Net Cash flows From Operating Activities	<u>296,761</u>	<u>315,409</u>
CASH FLOWS FROM INVESTING ACTIVITIES		
Capital expenditures	(277,278)	(523,831)
Proceeds from involuntary conversion	80,908	-
Funded deposits and restricted fund activity, net	246,168	505,823
Cash received from repayment of note receivable - related party	<u>48,109</u>	<u>45,413</u>
Net Cash Flows from Investing Activities	<u>97,907</u>	<u>27,405</u>
CASH FLOWS FROM FINANCING ACTIVITIES		
Cash used to retire debt	(289,140)	(277,650)
Distributions paid to members	(137,848)	(135,309)
Contributions from members	-	<u>57,728</u>
Net Cash Flows from Financing Activities	<u>(426,988)</u>	<u>(355,231)</u>
Net Change in Cash and Cash Equivalents	(32,320)	(12,417)
CASH AND CASH EQUIVALENTS - Beginning of Year	<u>111,621</u>	<u>124,038</u>
CASH AND CASH EQUIVALENTS - END OF YEAR	<u>\$ 79,301</u>	<u>\$ 111,621</u>

	<u>2014</u>	<u>2013</u>
RECONCILIATION OF NET LOSS TO NET CASH FLOWS FROM OPERATING ACTIVITIES		
Net loss	\$ (423,534)	\$ (491,627)
Adjustments to reconcile net loss to net cash flows from operating activities		
Noncash items included in loss		
Depreciation	786,425	769,352
Amortization	11,740	11,896
Nonoperational items included in loss		
Gain on involuntary conversion	(70,075)	-
Changes in noncash components of working capital		
Accrued interest receivable - related party	232	219
Prepaid expenses	(14,637)	23,175
Accounts payable	(4,236)	(1,069)
Accrued property taxes	(15,800)	8,900
Accrued interest	(979)	(939)
Prepaid tenant rents	<u>27,625</u>	<u>(4,498)</u>
NET CASH FLOWS FROM OPERATING ACTIVITIES	<u>\$ 296,761</u>	<u>\$ 315,409</u>

See accompanying notes to financial statements.

WATERFORD REHAB AND COURTS, LLC

NOTES TO FINANCIAL STATEMENTS
As of and for the Years Ended December 31, 2014 and 2013

NOTE 1 - Summary of Significant Accounting Policies

Nature of Operations

Waterford Rehab and Courts, LLC (the company) was formed under the laws of the State of Illinois on October 1, 1999. The company was formed for the purpose of constructing and leasing a 99-bed skilled nursing facility and a 66-bed Alzheimer's sheltered care facility located in Aurora, Illinois.

The company is financed by a mortgage insured by the U.S. Department of Housing and Urban Development (HUD) under Section 232 of the National Housing Act, and is regulated by HUD with respect to rental charges and operating methods. The company is also financed by an operating loss loan insured by HUD under Section 223(d) of the National Housing Act. The company's major programs are its HUD-insured mortgage and operating loss loan. The company leases the facilities to related parties (See Notes 6 and 7).

Cash disbursements are limited by agreements between the company and HUD to the extent of surplus cash as defined by HUD.

Cash and Cash Equivalents

The company defines cash and cash equivalents as highly liquid, short-term investments with a maturity at the date of acquisition of three months or less.

Impairment of Long-Lived Assets

The company reviews long-lived assets, including property and equipment and intangible assets, for impairment whenever events or changes in business circumstances indicate that the carrying amount of an asset may not be fully recoverable. An impairment loss would be recognized when the estimated future cash flows from the use of the asset are less than the carrying amount of that asset. To date, there have been no such losses.

Property and Equipment

Property and equipment are being depreciated using the straight-line method over the following estimated useful lives:

	<u>Years</u>
Land	None
Land improvements	10 - 25
Buildings and improvements	5 - 40
Building equipment (portable)	3 - 20
Furnishings and fixtures	5 - 20
Office furniture and equipment	3 - 10

Property and equipment are stated at cost. Major expenditures for property and equipment are capitalized. Maintenance, repairs, and minor renewals are expensed as incurred. When assets are retired or otherwise disposed of, their costs and related accumulated depreciation are removed from the accounts and resulting gains or losses are included in other income and expense.

WATERFORD REHAB AND COURTS, LLC

NOTES TO FINANCIAL STATEMENTS
As of and for the Years Ended December 31, 2014 and 2013

NOTE 1 - Summary of Significant Accounting Policies (cont.)

Amortization

Financing costs are amortized over the term of the mortgage loan using the effective interest method (See Note 4).

Income Taxes

The company is treated as a partnership for federal and state income tax purposes. As such, the company's income and losses are included in the income tax returns of its members.

The company evaluates tax positions taken within its returns for any uncertainty on an annual basis. Uncertain tax positions can result in the recognition of additional liability, including any applicable fines and penalties identified by the company requiring recognition of a liability or disclosure. As of December 31, 2014 and 2013, there were no uncertain tax positions identified by the company requiring recognition of a liability or disclosure. The company's tax returns for the tax years 2011 and later for federal and state remain subject to examination by taxing authorities.

Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

Property taxes are subject to a substantial measure of uncertainty. This requires management to make estimates and assumptions that affect the reported amounts of accrued property taxes and property tax expense.

NOTE 2 - Restricted Funds

Monthly mortgage escrow deposits are required to accumulate reserves for real estate taxes and insurance. The escrow deposits were funded as required during 2014 and 2013.

The company is required to maintain a replacement reserve held by the mortgagee and funded in an amount equal to \$1,000 per month. The replacement reserve is available for the replacement of fixed assets, major repairs and certain company expenditures. Any disbursement from this reserve requires the approval of HUD. The required monthly deposits to the replacement reserve were suspended beginning June 2011 and continued through November 2014 as approved by HUD. The replacement reserve was funded as required during 2014 and 2013.

WATERFORD REHAB AND COURTS, LLC

NOTES TO FINANCIAL STATEMENTS
As of and for the Years Ended December 31, 2014 and 2013

NOTE 3 - Property and Equipment

The change in the major categories of property and equipment for the year ended December 31, 2014 is summarized as follows:

Assets	Cost			Balance 12/31/2014
	Balance 1/1/2014	Additions	Reductions	
1410 Land	\$ 1,104,554	\$ -	\$ -	\$ 1,104,554
1410 Land improvements	1,600,689	65,029	-	1,665,718
1420 Buildings and improvements	18,728,944	65,468	-	18,794,412
1440 Building equipment (portable)	2,455,871	136,081	(64,998)	2,526,954
1460 Furnishings and fixtures	504,212	6,747	-	510,959
1465 Office furniture and equipment	<u>23,865</u>	<u>3,953</u>	<u>-</u>	<u>27,818</u>
Totals	<u>\$ 24,418,135</u>	<u>\$ 277,278</u>	<u>\$ (64,998)</u>	<u>\$ 24,630,415</u>
		Accumulated Depreciation		
Assets	Balance 1/1/2014	Additions	Reductions	Balance 12/31/2014
1495 Accumulated depreciation	<u>\$ 9,025,541</u>	<u>\$ 786,425</u>	<u>\$ (54,165)</u>	<u>\$ 9,757,801</u>
Net Property and Equipment	<u>\$ 15,392,594</u>			<u>\$ 14,872,614</u>

NOTE 4 - Deferred Financing Costs

The costs incurred to obtain financing have been capitalized and are being amortized as follows:

	Amortization Period	2014	2013
	Financing costs	391 - 480 mos.	\$ 283,216
Less: Accumulated amortization		<u>(38,255)</u>	<u>(26,515)</u>
Net Deferred Financing Costs		<u>\$ 244,961</u>	<u>\$ 256,701</u>

WATERFORD REHAB AND COURTS, LLC

NOTES TO FINANCIAL STATEMENTS As of and for the Years Ended December 31, 2014 and 2013

NOTE 4 - Deferred Financing Costs (cont.)

Financing costs are amortized over the term of the mortgage loan using the effective interest method. Amortization expense was \$11,740 and \$11,896 for the year ended December 31, 2014 and 2013, respectively. The following is a schedule of future amortization as of December 31, 2014:

2015	\$	11,579
2016		11,412
2017		11,237
2018		11,055
2019		10,866
2020 and thereafter		<u>188,812</u>
Total	\$	<u>244,961</u>

NOTE 5 - Long-Term Debt

Long-term debt consists of the following as of December 31:

	<u>2014</u>	<u>2013</u>
<p>The first mortgage note, which was refinanced in April 2011, is held by Cambridge Realty Capital, Ltd. of Illinois in the original amount of \$19,440,000. The note bears interest at 4.17% per annum. Monthly installments of principal and interest of \$83,315 are based on a 480-month amortization of the original note balance and are payable by the company beginning June 2011 and continuing through May 2051. The mortgage note is collateralized by real and personal property of the company. The mortgage is insured by HUD under Section 232 of the National Housing Act.</p>	\$ 18,710,404	\$ 18,925,076

WATERFORD REHAB AND COURTS, LLC

NOTES TO FINANCIAL STATEMENTS
As of and for the Years Ended December 31, 2014 and 2013

NOTE 5 - Long-Term Debt (cont.)

	<u>2014</u>	<u>2013</u>
In May 2012, the company financed an operating loss loan with Cambridge Realty Capital, Ltd. of Illinois in the original amount of \$4,404,900 that is subordinated to the first mortgage. The note bears interest at 3.75% per annum. Monthly installments of principal and interest of \$19,532 are based on a 391-month amortization of the original note balance and are payable by the company beginning July 2012 and continuing through January 2045. The loan is collateralized by real and personal property of the company. The operating loss loan is insured by HUD under Section 223(d) of the National Housing Act.	<u>\$ 4,223,830</u>	<u>\$ 4,298,298</u>
Totals	22,934,234	23,223,374
Less: Current portion	<u>(301,106)</u>	<u>(289,140)</u>
Long-Term Portion	<u>\$ 22,633,128</u>	<u>\$ 22,934,234</u>

Principal requirements on long-term debt for years ending after December 31, 2014 are as follows:

2015	\$ 301,106
2016	313,568
2017	326,547
2018	340,065
2019	354,143
2020 and thereafter	<u>21,298,805</u>
Total	<u>\$ 22,934,234</u>

WATERFORD REHAB AND COURTS, LLC

NOTES TO FINANCIAL STATEMENTS
As of and for the Years Ended December 31, 2014 and 2013

NOTE 6 - Rental Income Under Operating Leases

The company has entered into an operating lease with The Alden Master Tenant Associate, LLC (Master Tenant). The member of the Master Tenant has an interest in a member of the company. The Master Tenant sub-leases the facility to Alden of Waterford, LLC and Alden Courts of Waterford, LLC, (the subtenants), related parties, under an operating lease. The lease expires December 31, 2021 and the Master Tenant has three options to renew, each for an additional ten-year period. The Master Tenant is responsible for rent payments equal to 105% of (i) the monthly mortgage payment of principal and interest owed by the company pursuant to its U.S. Department of Housing and Urban Development (HUD) loan; plus (ii) the monthly deposit required by the company to the replacement reserve, as required by such HUD loan and/or HUD for reimbursement of the company's costs of replacement of certain components of its facility during the term of the lease; plus (iii) the monthly mortgage insurance premium as required by such HUD loan to maintain the HUD contract of mortgage insurance in connection with the financing of the facility, as may be required by HUD. In addition, the Master Tenant is responsible for reimbursing the company for real estate taxes and property insurance under the terms of the Master Tenant Lease. The balance received in advance for rent from the subtenants under this agreement was \$140,330 and \$112,705 as of December 31, 2014 and 2013, respectively.

Minimum future rentals to be received under the noncancellable operating lease are as follows:

2015	\$ 1,569,997
2016	1,569,997
2017	1,569,997
2018	1,569,997
2019	1,569,997
2020 and thereafter	<u>3,139,994</u>
Total	<u>\$ 10,989,979</u>

NOTE 7 - Related Party Transactions

Management

The company is managed by Alden Management Services, Inc. (AMS). The sole stockholder of AMS (The Alden Group, Ltd.) is an affiliate of the member. A member of the company is an employee and officer of AMS. During 2014 and 2013 no fee was incurred under this agreement.

Operating Lease

The company has entered into an operating lease with a related party as the lessor as discussed in Note 6.

WATERFORD REHAB AND COURTS, LLC

NOTES TO FINANCIAL STATEMENTS
As of and for the Years Ended December 31, 2014 and 2013

NOTE 7 - Related Party Transactions (cont.)

Note Receivable - Related Party

The company received a note for \$1,963,959 from Alden of Waterford, LLC for advances made in prior years. The note bears interest at 5.78%, and is receivable in monthly installments of principal and interest of \$11,166 until maturity in January 2041. During 2014 and 2013, the company earned \$104,982 and \$106,607, respectively, in interest income. As of December 31, 2014 and 2013, the balance due for accrued interest is \$8,684 and \$8,823, respectively.

	<u>2014</u>	<u>2013</u>
Beginning balance, January 1	\$ 1,831,795	\$ 1,859,043
Issuance of note receivable	-	-
Payments received	(28,865)	(27,248)
Interest added to note	-	-
Ending balance, December 31	<u>\$ 1,802,930</u>	<u>\$ 1,831,795</u>

The company received a note for \$1,309,306 from Alden Courts of Waterford, LLC for advances made in prior years. The note bears interest at 5.78%, and is receivable in monthly installments of principal and interest of \$7,444 until maturity in January 2041. During 2014 and 2013, the company earned \$69,988 and \$71,071, respectively in interest income. As of December 31, 2014 and 2013, the balance due for accrued interest is \$5,789 and \$5,882, respectively.

	<u>2014</u>	<u>2013</u>
Beginning balance, January 1	\$ 1,221,197	\$ 1,239,362
Issuance of note receivable	-	-
Payments received	(19,244)	(18,165)
Interest added to note	-	-
Ending balance, December 31	<u>\$ 1,201,953</u>	<u>\$ 1,221,197</u>

NOTE 8 - Members, Members' Interests, and Members' Deficit

The company has two members. Alden of Waterford Investments, LLC has a 99% interest and Joan Carl has a 1% interest.

NOTE 9 - Company Profits, Losses, and Distributions

The company's distribution of cash flow and net proceeds from special sources is restricted by the provisions of the HUD regulatory agreement. In the event of any conflict or inconsistency between the provisions of the company agreement and those of the HUD regulatory agreement, the provisions of the HUD regulatory agreement govern. The company's regulatory agreement restricts distributions to investors to the amount of surplus cash, as defined.

Net profits, net losses, tax allocations, and federal tax credits, if any, are allocated in accordance with the member's respective profit-sharing interests, except as otherwise provided in the special allocation provisions of the company agreement.

WATERFORD REHAB AND COURTS, LLC

NOTES TO FINANCIAL STATEMENTS
As of and for the Years Ended December 31, 2014 and 2013

NOTE 10 - Concentrations

The company's real estate is concentrated in two locations and operates in a heavily regulated environment as defined by HUD.

The company leases its premises and equipment to the subtenants (See Note 6) which operate the facility. The subtenants' revenues are heavily dependent on third-party payers, primarily the Illinois Medicaid and Federal Medicare programs.

There are ongoing federal and state initiatives and legislative proposals to reduce the costs of services and benefits to residents in long-term care facilities. The impact of these various proposals, if any, on the subtenants and the company are not readily determinable.

NOTE 11 - Involuntary Conversion

On January 6, 2014, flooding damaged building equipment (portable) which resulted in a gain on involuntary conversion of \$70,075. Insurance proceeds of \$80,908 were received during 2014. The carrying cost of the asset when the damage occurred was \$10,833.

NOTE 12 - Subsequent Events

The company has evaluated subsequent events occurring through March 18, 2015, the date that the financial statements were available to be issued, for events requiring recording or disclosure in the company's financial statements.

SUPPLEMENTAL INFORMATION

WATERFORD REHAB AND COURTS, LLC

SUPPLEMENTAL INFORMATION For the Year Ended December 31, 2014

REPLACEMENT RESERVE

1320P	Balance, January 1, 2014	\$ 1,039,511
1320DT	Required deposits	11,754
1320INT	Interest earned	874
1320WT	Withdrawals for project improvements	<u>(239,532)</u>
1320	Balance, December 31, 2014	<u>\$ 812,607</u>
1320R	Deposits Suspended or Waiver Indicator	Y

ANNUAL COMPUTATION OF SURPLUS CASH

S1300-010	Cash and cash equivalents	<u>\$ 79,301</u>
S1300-040	Total Cash	<u>79,301</u>
S1300-050	Accrued interest - mortgage	65,019
S1300-050	Accrued interest - operating loss loan	<u>13,199</u>
S1300-140	Total Current Obligations	<u>78,218</u>
S1300-150	Surplus Cash (Deficit) at December 31, 2014	<u>\$ 1,083</u>
S1300-200	Amount available for distribution during next fiscal period	<u>\$ 1,083</u>

MID-YEAR COMPUTATION OF SURPLUS CASH

S1400-010	Semi-Annual Period Ended	<u>June 30, 2014</u>
S1400-020	Cash and cash equivalents	<u>\$ 198,372</u>
S1400-050	Total Cash	<u>198,372</u>
S1400-060	Accrued interest - mortgage	65,396
S1400-060	Accrued interest - operating loss loan	<u>13,316</u>
S1400-180	Total Current Obligations	<u>78,712</u>
S1400-190	Surplus Cash (Deficit) at June 30, 2014	<u>\$ 119,660</u>
S1400-240	Amount available for distribution during next fiscal period	<u>\$ 119,660</u>

WATERFORD REHAB AND COURTS, LLC

SUPPLEMENTAL INFORMATION
For the Year Ended December 31, 2014

SCHEDULE OF CHANGES IN FIXED ASSET ACCOUNTS

1410P	Beginning Balance for 1410		\$ 2,705,243
1410AT	Additions for 1410		
	Landscaping	65,029	
	Miscellaneous	-	65,029
		-	65,029
1410	Land		<u>\$ 2,770,272</u>
1420P	Beginning Balance for 1420		\$ 18,728,944
1420AT	Additions for 1420		
	Parking lot	54,877	
	Light fixtures	6,085	
	Fire protection	4,506	
	Miscellaneous	-	65,468
		-	65,468
1420	Buildings and improvements		<u>\$ 18,794,412</u>
1440P	Beginning Balance for 1440		\$ 2,455,871
1440AT	Additions for 1440		
	HVAC equipment	83,745	
	Housekeeping equipment	25,910	
	Safety features	11,903	
	Kitchen equipment	7,441	
	Nurse call stations	4,172	
	Wheelchairs	1,807	
	Light poles	1,103	
	Miscellaneous	-	136,081
		-	136,081
1440DT	Reductions for 1440		
	Building equipment (involuntary conversion)	(64,998)	
	Miscellaneous	-	(64,998)
		-	(64,998)
1440	Building equipment (portable)		<u>\$ 2,526,954</u>
1460P	Beginning Balance for 1460		\$ 504,212
1460AT	Additions for 1460		
	Aquarium	3,044	
	Window coverings	1,550	
	Ceiling tile	1,472	
	Firepit	681	
	Miscellaneous	-	6,747
		-	6,747
1460	Furnishings and fixtures		<u>\$ 510,959</u>
1465P	Beginning Balance for 1465		\$ 23,865
1465AT	Additions for 1465		
	Time clocks	3,953	
	Miscellaneous	-	3,953
		-	3,953
1465	Office furniture and equipment		<u>\$ 27,818</u>

WATERFORD REHAB AND COURTS, LLC

SUPPLEMENTAL INFORMATION
For the Year Ended December 31, 2014

SCHEDULE OF RELATED PARTY TRANSACTIONS

S3100-210	Company Name	Alden of Waterford, LLC & Alden Courts of Waterford, LLC	
S3100-220	Amount Received	\$ 1,324,129	Lease Revenue - Section 232 Received
S3100-210	Company Name	Alden of Waterford, LLC	
S3100-220	Amount Received	\$ 28,865	Principal Received on Note Receivable
S3100-210	Company Name	Alden Courts of Waterford, LLC	
S3100-220	Amount Received	\$ 19,244	Principal Received on Note Receivable
S3100-210	Company Name	Alden of Waterford, LLC	
S3100-220	Amount Received	\$ 105,121	Interest Received on Note Receivable
S3100-210	Company Name	Alden Courts of Waterford, LLC	
S3100-220	Amount Received	\$ 70,081	Interest Received on Note Receivable

WATERFORD REHAB AND COURTS, LLC

BALANCE SHEET DATA
As of December 31, 2014

SCHEDULE OF ASSETS				
	Description of Account	Account	Amount	
1100 CURRENT ASSETS	Cash - Operations	1120	79,301	
	Construction Cash Account	1121	-	
	Cash - Entity	1125	-	
	Tenant/Members Accounts Receivable (Coops)	1130	-	
	Allowance for Doubtful Accounts	1131	-	
	Accounts Receivable - HUD	1135	-	
	Medicare/Medicaid/Other Insurance Receivable	1137	-	
	Accounts and Notes Receivable - Operations	1140	-	
	Accounts and Notes Receivable - Entity	1145	-	
	Accounts Receivable - Interest	1160	14,473	
	Interest Reduction Payment Receivable	1165	-	
	Short Term Investments - Operations	1170	-	
	Short Term Investments - Entity	1175	-	
	Miscellaneous Current Assets	1190	50,965	*
	Miscellaneous Prepaid Expenses	1200	64,821	**
	TOTAL CURRENT ASSETS	1100T		209,560
1191	Tenant/Patient Deposits Held in Trust	1191		-
1300 FUNDED RESERVES	Escrow Deposits	1310	139,941	
	Replacement Reserve	1320	812,607	
	Other Reserves	1330	-	
	Residual Receipts Reserve	1340	-	
	Bond Reserves	1355	-	
	General Operating Reserve (Coops)	1365	-	
	Sinking Fund	1367	-	
	Deposits to Coops	1370	-	
	Management Improvement and Operating Plan	1381	-	
		Total Funded Reserves	1300T	
1400 FIXED ASSETS	Land	1410	2,770,272	
	Buildings	1420	18,794,412	
	Building Equipment (portable)	1440	2,526,954	
	Furniture for Project/Tenant Use	1450	-	
	Furnishings	1460	510,959	
	Office Furniture and Equipment	1465	27,818	
	Maintenance Equipment	1470	-	
	Motor Vehicles	1480	-	
	Miscellaneous Fixed Assets	1490	-	
	Gross Fixed Assets	1400T	24,630,415	
1495 ALLOWANCE ACCOUNTS	Accumulated Depreciation	1495	9,757,801	
	Total Accumulated Depreciation		9,757,801	
	Net Fixed Assets	1400N		14,872,614
1500 INVESTMENTS	Investments - Operations	1510	-	
	Investments - Entity	1515	-	
	Deferred Financing Costs	1520	244,961	
	Cash Restricted for Long-Term Investment	1525	-	
	Miscellaneous Other Assets	1590	2,953,918	***
	TOTAL OTHER ASSETS	1500T	3,198,879	
	TOTAL ASSETS	1000T		19,233,601

* - Current portion of note receivable - related party

** - Prepaid insurance

*** - Long-term portion of note receivable - related party

WATERFORD REHAB AND COURTS, LLC

BALANCE SHEET DATA (cont.)

As of December 31, 2014

SCHEDULE OF LIABILITIES AND EQUITY				
	Description of Account	Account	Amount	Totals
2100 CURRENT LIABILITIES	Bank Overdraft - Operations	2105	-	
	Accounts Payable - Operations	2110	-	
	Accounts Payable - Construction/Development	2111	-	
	Accounts Payable - Project Improvements Items	2112	-	
	Accounts Payable - Entity	2113	-	
	Accounts Payable - 236 Excess Income Due HUD	2115	-	
	Accounts Payable - Section 8 & Other	2116	-	
	Accrued Wages Payable	2120	-	
	Accrued Payroll Taxes Payable	2121	-	
	Accrued Management Fee Payable	2123	-	
	Accrued Interest Payable - Section 236	2130	-	
	Accrued Interest Payable - First Mortgage (or Bonds)	2131	65,019	
	Accrued Interest Payable - Second Mortgage	2132	-	
	Accrued Interest Payable - Other Loans & Notes (Surplus Cash)	2133	-	
	Accrued Interest Payable - Other Loans and Notes	2134	-	
	Accrued Interest Payable - Flexible Subsidy Loan	2135	-	
	Accrued Interest Payable - Capital Improvement Loan	2136	-	
	Accrued Interest Payable - Operating Loss Loan	2137	13,199	
	Accrued Interest Payable - Capital Recovery Payment (M2M)	2137	-	
	Accrued Property Taxes	2150	101,600	
	Notes Payable (Short Term)	2160	-	
	Mortgage Payable - First Mortgage (Short Term)	2170	223,797	
	Other Mortgages Payable (Short Term)	2172	-	
	Other Loans and Notes Payable - Surplus Cash (Short Term)	2173	-	
	Other Loans and Notes (Short Term)	2174	-	
	Flexible Subsidy Loan Payable (Short Term)	2175	-	
	Capital Improvement Loan Payable (Short Term)	2176	-	
	Operating Loss Loan Payable (Short Term)	2177	77,309	
	Capital Recovery Payment Payable (Short Term - M2M)	2179	-	
	Utility Allowances	2180	-	
Miscellaneous Current Liabilities/Preservation Fee	2190	-		
Prepaid Revenue	2210	140,330	****	
Deposits to Coops	2230	-		
	TOTAL CURRENT LIABILITIES	2122T		621,254
2191	Tenant Security Deposits - CONTRA ASSET	2191		-
2300 LONG-TERM LIABILITIES	Notes Payable (Long Term)	2310	-	
	Notes Payable - Surplus Cash	2311	-	
	Mortgage Payable - First Mortgage	2320	18,486,607	
	Other Mortgages Payable (Long Term)	2322	-	
	Other Loans and Notes Payable - Surplus Cash	2323	-	
	Other Loans and Notes Payable	2324	-	
	Flexible Subsidy Loan Payable	2325	-	
	Capital Improvement Loan Payable	2326	-	
	Operating Loss Loan Payable	2327	4,146,521	
	Capital Recovery Payment Payable (M2M)	2329	-	
	Interest on Loans or Notes Payable (Long Term)	2330	-	
	Miscellaneous Long Term Liabilities	2390	-	
		Total Long Term Liabilities	2300T	
	TOTAL LIABILITIES	2000T		23,254,382
TOTAL EQUITY	Total Equity (Deficit)	3130	(4,020,781)	
	TOTAL LIABILITIES AND EQUITY/RETAINED EARNINGS	2033T		19,233,601

**** - Leased nursing home prepaid rent - related party

WATERFORD REHAB AND COURTS, LLC

PROFIT AND LOSS DATA
For the Year Ended December 31, 2014

	Description of Account	Acct. No.	Amount	Totals
5100 RENTAL REVENUE	Rent Revenue - Gross Potential	5120	-	
	Tenant Assistance Payments	5121	-	
	Rent Revenue - Commercial/Stores @ 100%	5140	-	
	Rent Revenue - Garage/Parking @ 100%	5170	-	
	Flexible Subsidy Revenue	5180	-	
	Miscellaneous Rent Revenue	5190	-	
	Excess Rent	5191	-	
	Rent Revenue/Insurance	5192	-	
	Special Claims Revenue	5193	-	
	Retained Excess Income	5194	-	
	Lease Revenue - Nursing Homes	5195	1,296,504	
	Total Revenue Potential	5100T		1,296,504
5200 VACANCIES	Apartment Vacancies	5220	-	
	Stores/Commercial Vacancies or Concessions	5240	-	
	Rental Concessions	5250	-	
	Garage/Parking Vacancies or Concessions	5270	-	
	Miscellaneous	5290	-	
	Total Vacancies or Concessions	5200T		-
	Net Rental Revenue (Rent Revenue less Vacancies)	5152N		1,296,504
5300	Total Service Income	5300		-
5400 FINANCIAL REVENUE	Financial Revenue - Project Operations	5410	-	
	Revenue from Investments - Residual Receipts	5430	-	
	Revenue from Investments - Replacement Reserve	5440	874	
	Revenue from Investments - Miscellaneous	5490	174,970	
	Total Financial Revenue	5400T		175,844
5900 MISC. REVENUE	Laundry/Vending Income (Net)	5910	-	
	Tenant Charges	5920	-	
	Interest Reduction Payments Revenue	5945	-	
	Miscellaneous Revenue	5990	-	
	Total Other Revenue	5900T		-
	Total Revenue	5000T		1,472,348
ADMIN. EXPENSE	Conventions and Meetings	6203	-	
	Management Consultants	6204	-	
	Advertising/Marketing Expense	6210	-	
	Apartment Resale Expense	6235	-	
	Other Rent Expense	6250	-	
	Office Salaries	6310	-	
	Office Expenses	6311	-	
	Office or Model Apartment Rent	6312	-	
	Management Fee - Residential Rents	6320	-	
	Manager/Superintendent Salaries	6330	-	
	Administrative Rent-free Unit	6331	-	
	Legal Expense - project only	6340	-	
	Audit Expense - project only	6350	6,550	
	Bookkeeping Fees/Accounting Services	6351	-	
	Bad Debt Expense	6370	-	
	Miscellaneous Administrative Expense	6390	926	
	Total Administrative Expense	6263T		7,476
6400 UTILITIES EXPENSE	Fuel Oil	6420	-	
	Electricity	6450	-	
	Water	6451	-	
	Gas	6452	-	
	Sewer	6453	-	
	Total Utilities Expense	6400T		-

* - Interest income from note receivable - related party

WATERFORD REHAB AND COURTS, LLC

PROFIT AND LOSS DATA (cont.)
For the Year Ended December 31, 2014

	Description of Account	Acct. No.	Amount	Totals
6500 OPERATING & MAINTENANCE EXPENSE	Payroll	6510	-	
	Supplies	6515	-	
	Contracts	6520	-	
	Operating and Maintenance Rent Free Unit	6521	-	
	Garbage & Trash Removal	6525	-	
	Security Payroll/Contract (incl. taxes and benefits)	6530	-	
	Security Rent Free Unit	6531	-	
	Heating/Cooling Repairs & Maintenance	6546	-	
	Snow Removal	6548	-	
	Vehicle/Maintenance Equipment Operation & Repairs	6570	-	
	Misc. Operating & Maintenance Expense	6590	-	
	Total Operating & Maintenance Expense	6500T		-
	6700 TAXES AND INSURANCE	Real Estate & Personal Property Taxes	6710	82,804
Payroll Taxes (Project's Share)		6711	-	
Property & Liability Insurance (Hazard)		6720	18,134	
Fidelity Bond Insurance		6721	-	
Workmen's Compensation		6722	-	
Health Insurance and Other Employee Benefits		6723	-	
Miscellaneous Taxes, Licenses, Permits and Insurance		6790	-	
Total Taxes and Insurance		6700T		100,938
	Total Operating Expenses			108,414
	Net Operating Income (NOI)			1,363,934
6800 FINANCIAL EXPENSE	Interest on Mortgage Payable	6820	944,040	
	Interest on Notes Payable (Long Term)	6830	-	
	Interest on Notes Payable (Short Term)	6840	-	
	Interest on Capital Recovery Payment (M2M)	6845	-	
	Mortgage Insurance Premium/Service Charge	6850	115,338	
	Miscellaneous Financial Expense/Preservation Fee	6890	-	
	Total Financial Expense	6800T		1,059,378
6900	Total Service Expense	6900		-
	Total Expenses of Operations Before Depreciation	6000T		1,167,792
	Profit or (Loss) Before Depreciation	5060T		304,556
6600	Depreciation Expense (Total)	6601		786,425
	Amortization Expense	6610		11,740
	Operating Profit or Loss	5060N		(493,609)
7100 CORPORATE OR MORTGAGOR REVENUE/ EXPENSE	Entity Revenue	7105	-	
	Officer's Salaries	7110	-	
	Incentive Performance Fee	7115	-	
	Legal Expenses	7120	-	
	Federal, State and Other Income Taxes	7130	-	
	Interest Income	7140	-	
	Interest on Notes Payable	7141	-	
	Interest on Mortgage Payable	7142	-	
	Other Expenses	7190	(70,075)	**
	Net Entity Expenses	7100T		(70,075)
	NET PROFIT OR (LOSS)	3250		(423,534)
S1000-010	Total mortgage principal payments made during the year			214,672
S1000-020	Total of 12 monthly deposits during the year into the replacement reserve account, as required by the regulatory agreement			12,000
S1000-030	Replacement reserve or residual reserve releases which are included as expense items on this profit and loss statement			-

** - Gain on involuntary conversion

WATERFORD REHAB AND COURTS, LLC

STATEMENT OF MEMBERS' DEFICIT DATA For the Year Ended December 31, 2014

STATEMENT OF MEMBERS' DEFICIT DATA						
	Description of Account	ID	Account	Amount	Totals	
3130 EQUITY	Beginning of Year Balance		S1100-010	(3,459,399)		
	Net Income or (Loss)		3250	(423,534)		
	Distributions		S1200-420	(137,848)		
	Contributions		S1200-430	-		
	Prior Period Adjustments		S3100-030	-		
	End of Year Balance		3130			(4,020,781)

WATERFORD REHAB AND COURTS, LLC

STATEMENT OF CASH FLOWS DATA For the Year Ended December 31, 2014

STATEMENT OF CASH FLOWS DATA					
	Description of Account	ID	Account	Amount	Totals
CASH FLOWS FROM OPERATING ACTIVITIES	Rental Receipts		S1200-010	1,324,129	
	Interest Receipts		S1200-020	176,076	
	Other Operating Receipts		S1200-030	-	
	Total Receipts		S1200-040		1,500,205
	Administrative		S1200-050	(11,712)	
	Management Fee		S1200-070	-	
	Utilities		S1200-090	-	
	Salaries and Wages		S1200-100	-	
	Operating and Maintenance		S1200-110	-	
	Real Estate Taxes		S1200-120	(98,604)	
	Property Insurance		S1200-140	(33,412)	
	Miscellaneous Taxes and Insurance		S1200-150	-	
	Tenant Security Deposits		S1200-160	-	
	Other Operating Expenses		S1200-170	-	
	Interest on First Mortgages		S1200-180	(785,104)	
	Interest Payments - Second Mortgage		S1200-181	(159,915)	
	Mortgage Insurance Premium (MIP)		S1200-210	(114,697)	
	Miscellaneous Financial		S1200-220	-	
	Total Disbursements		S1200-230		(1,203,444)
	Net Cash Flow From Operating Activities		S1200-240		296,761
CASH FLOWS FROM INVESTING ACTIVITIES	Net Deposits to the Mortgage Escrow account		S1200-245	19,264	
	Net Deposits to the Reserve for Replacement account		S1200-250	226,904	
	Net Deposits to Other Reserves		S1200-255	-	
	Net Deposits to the Residual Receipts account		S1200-260	-	
	Net Purchases of Fixed Assets		S1200-330	(277,278)	
	Other Investing Activities		S1200-340	129,017	
		Net Cash Flow From Investing Activities		S1200-350	
CASH FLOWS FROM FINANCING ACTIVITIES	Principal Payments - First Mortgage (or Bonds)		S1200-360	(214,672)	
	Principal Payments - Second Mortgage		S1200-361	-	
	Principal Payments - Third Mortgage		S1200-362	-	
	Proceeds from Mortgage Loans or Notes Payable		S1200-365	-	
	Principal Payments on Operating Loss Loan Payable		S1200-410	(74,468)	
	Distributions		S1200-420	(137,848)	
	Contributions		S1200-430	-	
	Other Financing Activities		S1200-450	-	
		Net Cash Flow From Financing Activities		S1200-460	
	Net Increase (Decrease) in Cash		S1200-470		(32,320)
	Beginning of Period Cash		S1200-480		111,621
	End of Period Cash		S1200T		79,301

* - Cash received from repayment of note receivable - related party \$48,109; Proceeds from involuntary conversion \$80,908

WATERFORD REHAB AND COURTS, LLC

STATEMENT OF CASH FLOWS DATA (cont.) For the Year Ended December 31, 2014

STATEMENT OF CASH FLOWS DATA						
	Description of Account	ID	Account	Amount	Totals	
RECONCILIATION OF NET INCOME (LOSS) TO NET	Profit or Loss (Net Income or Loss)		3250	(423,534)		
	Adjustments to Reconcile Net Profit (Loss) to Net Cash Provided by (Used in) Operating Activities:					
CASH PROVIDED BY (USED IN) OPERATING ACTIVITIES	Depreciation Expense		6600	786,425		
	Amortization Expense		6610	11,740		
	Decrease (increase) in Tenant/Member Account Rec.		S1200-490	-		
	Decrease (increase) in Accounts Receivable - other		S1200-500	232		
	Decrease (increase) in Prepaid Expenses		S1200-520	(14,637)		
	Decrease (increase) in Cash Restricted for Tenant Security Deposits		S1200-530	-		
	Increase (decrease) in Accounts Payable		S1200-540	(4,236)		
	Increase (decrease) in Accrued Liabilities		S1200-560	10,846		
	Increase (decrease) in Tenant Security Deposits held in trust		S1200-580	-		
	Other adjustments to reconcile net profit (loss) to Net Cash provided by (used in) Operating Activities		S1200-600	(70,075)	**	
		Net Cash Flow From Operating Activities		S1200-610		296,761

** - Gain on involuntary conversion

WATERFORD REHAB AND COURTS, LLC

MANAGING AGENT'S CERTIFICATION
December 31, 2014

I hereby certify that I have examined the foregoing financial statements and supplemental information of Waterford Rehab and Courts, LLC and, to the best of my knowledge and belief, the same are complete and accurate.

ALDEN MANAGEMENT SERVICES, INC.

Floyd A. Schlossberg, President
Alden Management Services, Inc.

Date

Managing Agent's Employer Identification
Number: 36-4444035

WATERFORD REHAB AND COURTS, LLC

MORTGAGOR'S CERTIFICATION
December 31, 2014

I hereby certify that I have examined the foregoing financial statements and supplemental information of Waterford Rehab and Courts, LLC and, to the best of my knowledge and belief, the same are complete and accurate.

WATERFORD REHAB AND COURTS, LLC

Joan Carl, Member

Date

Mortgagor's Employer Identification
Number: 36-3973187



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INDEPENDENT AUDITOR'S REPORT ON INTERNAL CONTROL OVER
FINANCIAL REPORTING AND ON COMPLIANCE AND OTHER MATTERS
BASED ON AN AUDIT OF FINANCIAL STATEMENTS PERFORMED IN
ACCORDANCE WITH *GOVERNMENT AUDITING STANDARDS*

To the Members
Waterford Rehab and Courts, LLC
Aurora, Illinois

We have audited, in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States, the financial statements of Waterford Rehab and Courts, LLC (the company), which comprise the balance sheet as of December 31, 2014, and the related statements of operations, changes in members' deficit and cash flows for the year then ended, and the related notes to the financial statements, and have issued our report thereon dated March 18, 2015.

Internal Control Over Financial Reporting

In planning and performing our audit of the financial statements, we considered the company's internal control over financial reporting (internal control) to determine the audit procedures that are appropriate in the circumstances for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the company's internal control. Accordingly, we do not express an opinion on the effectiveness of the company's internal control.

A deficiency in internal control exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct misstatements on a timely basis. A material weakness is a deficiency, or combination of deficiencies, in internal control, such that there is a reasonable possibility that a material misstatement of the company's financial statements will not be prevented, or detected and corrected on a timely basis. A significant deficiency is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

Our consideration of internal control was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies. Given these limitations, during our audit we did not identify any deficiencies in internal control that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified.

To the Members
Waterford Rehab and Courts, LLC

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the company's financial statements are free from material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under Government Auditing Standards.

Purpose of this Report

The purpose of this report is solely to describe the scope of our testing of internal control and compliance and the results of that testing, and not to provide an opinion on the effectiveness of the company's internal control or on compliance. This report is an integral part of an audit performed in accordance with Government Auditing Standards in considering the company's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

Baker Tilly Unchou Krause, LLP

Milwaukee, Wisconsin
March 18, 2015



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**INDEPENDENT AUDITOR'S REPORT ON COMPLIANCE FOR EACH MAJOR HUD PROGRAM
 AND REPORT ON INTERNAL CONTROL OVER COMPLIANCE REQUIRED BY THE
 CONSOLIDATED AUDIT GUIDE FOR AUDITS OF HUD PROGRAMS**

To the Members
 Waterford Rehab and Courts, LLC
 Aurora, Illinois

Report on Compliance for Each Major HUD Program

We have audited Waterford Rehab and Courts, LLC's (the company) compliance with the compliance requirements described in the *Consolidated Audit Guide for Audits of HUD Programs* (the Guide) that could have a direct and material effect on each of the company's major U.S. Department of Housing and Urban Development (HUD) programs for the year ended December 31, 2014. The company's major HUD programs and the related direct and material compliance requirements are as follows:

Name of Major HUD Programs	Direct and Material Compliance Requirements
Section 232 HUD Insured Mortgage	Mortgage status, replacement reserve, distributions to owners, equity skimming, cash disbursements, and leased nursing homes.

Management's Responsibility

Management is responsible for compliance with the requirements of laws, regulations, contracts, and grants applicable to its HUD programs.

Auditor's Responsibility

Our responsibility is to express an opinion on compliance for each of the company's major HUD programs based on our audit of the compliance requirements referred to above. We conducted our audit of compliance in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in Government Auditing Standards, issued by the Comptroller General of the United States; and the Guide. Those standards and the Guide require that we plan and perform the audit to obtain reasonable assurance about whether noncompliance with the compliance requirements referred to above that could have a direct and material effect on a major HUD program occurred. An audit includes examining, on a test basis, evidence about the company's compliance with those requirements and performing such other procedures as we consider necessary in the circumstances.

We believe that our audit provides a reasonable basis for our opinion on compliance for each major HUD program. However, our audit does not provide a legal determination of the company's compliance.

To the Members
Waterford Rehab and Courts, LLC

Opinion on Each Major HUD Program

In our opinion, Waterford Rehab and Courts, LLC complied, in all material respects, with the compliance requirements referred to above that could have a direct and material effect on each of its major HUD programs for the year ended December 31, 2014.

Report on Internal Control Over Compliance

Management of the company is responsible for establishing and maintaining effective internal control over compliance with the compliance requirements referred to above. In planning and performing our audit of compliance, we considered the company's internal control over compliance with the requirements that could have a direct and material effect on each major HUD program to determine the auditing procedures that are appropriate in the circumstances for the purpose of expressing an opinion on compliance for each major HUD program and to test and report on internal control over compliance in accordance with the Guide, but not for the purpose of expressing an opinion on the effectiveness of internal control over compliance. Accordingly, we do not express an opinion on the effectiveness of the company's internal control over compliance.

A deficiency in internal control over compliance exists when the design or operation of a control over compliance does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, noncompliance with compliance requirement of a HUD program on a timely basis. A material weakness in internal control over compliance is a deficiency, or combination of deficiencies, in internal control over compliance, such that there is a reasonable possibility that material noncompliance with a compliance requirement of a HUD program will not be prevented, or detected and corrected, on a timely basis. A significant deficiency in internal control over compliance is a deficiency, or a combination of deficiencies, in internal control over compliance with a compliance requirement of a HUD program that is less severe than a material weakness in internal control over compliance, yet important enough to merit attention by those charged with governance.

Our consideration of internal control over compliance was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control over compliance that might be material weaknesses or significant deficiencies. We did not identify any deficiencies in internal control over compliance that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified.

The purpose of this report on internal control over compliance is solely to describe the scope of our testing of internal control over compliance and the results of that testing based on the requirements of the Guide. Accordingly, this report is not suitable for any other purpose.

Baker Tilly Vorchow Krause, LLP

Milwaukee, Wisconsin
March 18, 2015

WATERFORD REHAB AND COURTS, LLC

SCHEDULE OF FINDINGS, QUESTIONED COSTS, AND RECOMMENDATIONS
As of and for the Year Ended December 31, 2014

Our audit disclosed no findings that are required to be reported herein under the HUD Consolidated Audit Guide.

WATERFORD REHAB AND COURTS, LLC

SCHEDULE OF THE STATUS OF PRIOR AUDIT FINDINGS, QUESTIONED COSTS, AND RECOMMENDATIONS

As of and for the Year Ended December 31, 2014

1. Findings and Questioned Costs from Prior Audit Reports:

There are no findings from the prior audit report dated March 7, 2014, as of and for the years ended December 31, 2013 and 2012, issued by Baker Tilly Virchow Krause, LLP which require corrective action by the company.

2. Findings from Audit, Attestation, or Other Studies Performed by HUD, another Federal Agency, or a Contract Administrator:

There were no reports issued by HUD OIG or other Federal agencies or contract administrators during the year ended December 31, 2014.

3. Letters or Reports issued by HUD Management:

There were no letters or reports issued by HUD management during the year ended December 31, 2014.