KINDRED HEALTHCARE INC
Form DEF 14A
March 08, 2002

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

SCHEDULE 14A INFORMATION

Proxy Statement Pursuant to Section 14(a)
of the Securities Exchange Act of 1934

Filed by the Registrant: [X]

Filed by a Party other than the Registrant: [_]

Check the appropriate box:

[_] Preliminary Proxy Statement

[_] Confidential, for Use of the Commission Only (as permitted by Rule 14a-6(e)(2))

[X] Definitive Proxy Statement

[_] Definitive Additional Materials

[_] Soliciting Material Pursuant to Rule 14a-11(c) or Rule 14a-12

KINDRED HEALTHCARE, INC.

(Name of Registrant as Specified in Its Charter)

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

Payment of filing fee (Check the appropriate box):

[X] No fee required.

[_] Fee computed on table below per Exchange Act Rules 14a-6(i)(1) and 0-11.
(1) Title of each class of securities to which transaction applies:

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

(3) Per unit price or other underlying value of transaction computed pursuant to Exchange Act Rule 0-11 (Set forth the amount on which the filing fee was calculated and state how it was determined):

(4) Proposed maximum aggregate value of transaction:

(5) Total fee paid:

[_] Fee paid previously with preliminary materials.

[_] Check box if any part of the fee is offset as provided by Exchange Act Rule 0-11(a)(2) and identify the filing for which the offsetting fee was paid previously. Identify the previous filing by registration statement number, or the Form or Schedule and the date of its filing.

(1) Amount Previously Paid:

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

(3) Filing Party:

(4) Date Filed:

[LOGO] Kindred
Healthcare

KINDRED HEALTHCARE, INC.

March 8, 2002

Dear Shareholder:

You are cordially invited to attend the Annual Meeting of Shareholders of Kindred Healthcare, Inc. ("Kindred"), to be held at 10:00 a.m. on Tuesday, April 16, 2002, at Kindred's offices at 680 South Fourth Street, Louisville, Kentucky 40202-2412.

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

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

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

Sincerely,

/s/ Edward L. Kuntz
Edward L. Kuntz
Chairman of the Board and Chief
Executive Officer
Kindred Healthcare, Inc.
680 South Fourth Street
Louisville, Kentucky 40202-2412

[LOGO] Kindred
Healthcare

KINDRED HEALTHCARE, INC.
680 SOUTH FOURTH STREET
LOUISVILLE, KENTUCKY 40202-2412

NOTICE OF ANNUAL MEETING OF SHAREHOLDERS

TO BE HELD ON APRIL 16, 2002

To the Shareholders of Kindred Healthcare, Inc.:

The Annual Meeting of Shareholders of Kindred Healthcare, Inc. will be held at 10:00 a.m. on Tuesday, April 16, 2002, at Kindred's offices at 680 South Fourth Street, Louisville, Kentucky 40202-2412 for the following purposes:

(1) To elect a board of seven directors;

(2) To consider and ratify the Kindred Healthcare, Inc. 2000 Stock Option Plan;

(3) To consider and approve the Kindred Healthcare, Inc. 2001 Stock Incentive Plan;

(4) To consider and ratify the Kindred Healthcare, Inc. 2000 Long-Term Incentive Plan;

(5) To consider and approve the Kindred Healthcare, Inc. Short-Term Incentive Plan;

(6) To consider and approve an amendment to Kindred's Amended and Restated Certificate of Incorporation to increase the number of authorized shares of common stock; and

(7) To transact such other business as may properly come before the meeting.

Only shareholders of record at the close of business on March 7, 2002 will be entitled to vote at the meeting and any adjournments thereof.

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

Edward L. Kuntz
Chairman of the Board and Chief
Executive Officer

PROXY STATEMENT
FOR ANNUAL MEETING OF SHAREHOLDERS
TO BE HELD ON APRIL 16, 2002

GENERAL INFORMATION

This Proxy Statement and the accompanying form of proxy are furnished in connection with the solicitation of proxies by the Board of Directors of Kindred Healthcare, Inc. ("Kindred" or the "Company") for use at the Annual Meeting of Shareholders (the "Annual Meeting"), to be held at 10:00 a.m. on April 16, 2002, at the Company's offices at 680 South Fourth Street, Louisville, Kentucky 40202-2412, and at any adjournment or postponement thereof. Only shareholders of record on the books of the Company at the close of business on March 7, 2002 (the "Record Date") will be entitled to notice of, and to vote at, the Annual Meeting. This Proxy Statement is dated March 8, 2002 and was first mailed to shareholders on or about March 11, 2002.

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

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

Revocability of Proxy

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

Voting Rights and Outstanding Shares

Each share of common stock, $0.25 par value ("Common Stock"), of the Company outstanding at the close of business on March 7, 2002 is entitled to one vote at the Annual Meeting. As of March 7, 2002, there were 17,682,917 shares of Common Stock outstanding.

The presence at the Annual Meeting in person or by proxy of holders of record of a majority of the outstanding shares of Common Stock is required to constitute a quorum for the transaction of all business at the Annual Meeting. The vote of a plurality of the outstanding shares of Common Stock present in person or by proxy will be necessary to elect the director-nominees listed in this Proxy Statement. The affirmative vote of a majority of the outstanding shares of Common Stock present in person or by proxy will be necessary to approve all other proposals and matters that may come before the Annual Meeting for shareholder consideration. Abstentions and proxies relating to "street name" shares for which brokers have not received voting instruction from the beneficial owner ("Broker Non-Votes") are counted in determining whether a quorum is present. In the election of directors, the nominees receiving the highest number of votes will be elected. Therefore, abstentions or Broker Non-Votes for a director-nominee will have no effect. With respect to any matters submitted to the

shareholders for their consideration other than the election of directors, abstentions will be counted as part of the total number of votes cast on such proposals in determining whether the proposals have received the requisite number of favorable votes, whereas Broker Non-Votes will not be counted as part of the total number of votes cast on such proposals. Thus, abstentions will have the same effect as votes against any such proposal, whereas Broker Non-Votes will have no effect in determining whether any such proposal has been approved by the shareholders. Therefore, it is important that you complete and return your proxy early so that your vote may be recorded.

Votes cast by proxy or in person at the Annual Meeting will be tabulated by the inspectors of election appointed for the meeting, who also will determine whether or not a quorum is present.

BACKGROUND INFORMATION

On May 1, 1998, Ventas, Inc. ("Ventas") completed the spin-off of its healthcare operations to its shareholders through the distribution of the Company's former common stock (the "Spin-off"). In anticipation of the Spin-off, the Company was incorporated on March 27, 1998 as a Delaware corporation.

As a result of decreased Medicare and Medicaid reimbursement rates introduced by the Balanced Budget Act of 1997 and other issues associated with the Company, the Company was unable to meet its then existing financial obligations, including rent payable to Ventas and debt service obligations under existing indebtedness. Accordingly, on September 13, 1999, the Company filed voluntary petitions for protection under Chapter 11 of Title 11 of the United States Bankruptcy Code in the United States Bankruptcy Court for the District of Delaware. From the date of the bankruptcy filing until it emerged from bankruptcy, the Company operated its businesses as a "debtor-in-possession" subject to the jurisdiction of the bankruptcy court. The bankruptcy court approved the Company's Fourth Amended Joint Plan of Reorganization (the "Plan of Reorganization") which became effective on April 20, 2001 (the "Effective Date").

Pursuant to the Plan of Reorganization, the Company issued to certain claimholders, including senior creditors and Ventas, in exchange for their claims an aggregate of (1) $300 million of senior secured notes, (2) 15,000,000 shares of Common Stock, (3) 2,000,000 Series A warrants to purchase Common Stock, and (4) 5,000,000 Series B warrants to purchase Common Stock. The Company also entered into amended and restated master lease agreements with Ventas covering 210 of the nursing centers and 44 of the hospitals that the Company operates. As part of the Plan of Reorganization, the Company's then existing senior indebtedness and debt and equity securities were canceled. As a result of the exchange described above, the holders of certain claims acquired control of the Company and the holders of the Company's former common stock relinquished control. In addition, the Company changed its name to Kindred Healthcare, Inc. and a new board of directors, including representatives of the principal security holders following the exchange, was appointed.

1. PROPOSAL TO ELECT DIRECTORS

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

EDWARD L. KUNTZ (56) has served as the Company's Chairman of the Board and Chief Executive Officer since January 1999. He served as the President, Chief Operating Officer and a director of the Company from November 1998 to January 1999. He served as President of the Company until January 2002. Mr. Kuntz was Chairman and Chief Executive Officer of Living Centers of America, Inc., a leading provider of long-term healthcare, from 1992 to 1997. After leaving Living Centers of America, Inc., he served as an advisor and consultant to a number of healthcare services and investment companies and was affiliated with Austin Ventures, a venture capital firm. In addition, Mr. Kuntz served as Associate General Counsel and later as Executive Vice President of ARA Living Centers until the formation of Living Centers of America, Inc. in 1992.

JAMES BOLIN (43) has served as a director of the Company since April 2001. Since 1995, Mr. Bolin has been Vice President and Secretary of Appaloosa Management L.P. Mr. Bolin serves as a director of Inamed Corporation, a global surgical and medical device company, and Bio-Plexus, Inc., a designer and manufacturer of safety medical products. (1)

MICHAEL J. EMBLER (37) has served as a director of the Company since July 2001. Since July 2001, Mr. Embler has been Vice President of Franklin Mutual Advisers, LLC. From October 1992 to May 2001, he served in various positions with Nomura Holding America, most recently as Managing Director.

GARRY N. GARRISON (55) has served as a director of the Company since April 2001. From 1997 to 2000, Mr. Garrison served as Senior Vice President of Dynamic Healthcare Solutions, Inc., a venture capital firm specializing in high-growth, health related businesses. From 1996 to 1997, he served as President and Chief Executive Officer, Specialty Services Division of the Foundation Health Systems, Inc., overseeing operations for various specialty services companies. Mr. Garrison also served as President and Chief Operating Officer of Integrated Pharmaceutical Services from 1994 to 1996. (1)(2)

ISAAC KAUFMAN (54), a certified public accountant, has served as a director of the Company since April 2001. Since September 1998, Mr. Kaufman has served as the Senior Vice President and Chief Financial Officer of Advanced Medical Management Inc., a manager of medical practices and an outpatient surgical center. From February 1998 to September 1998, he served as the Chief Financial Officer of Bio Science Contract Production Corp., a contract manufacturer of bulk pharmaceuticals and biologics. Mr. Kaufman also served as Chief Financial Officer of VSI Group, Inc. from October 1996 to February 1998. Mr. Kaufman serves as a director of TransWorld Entertainment Corporation, a leading specialty retailer of music and video products. (1)

JOHN H. KLEIN (55) has served as a director of the Company since April 2001. Mr. Klein has been the Chairman and Chief Executive Officer of Strategic Business and Technology Solutions, LLC, a strategy business and technology advisory firm, since June 1998. Since 2001, he also has served as Chairman and Managing Director of True North Partners, a consulting and private equity fund. Mr. Klein also has served as the Chairman and Chief Executive Officer of BI Logix, Inc., a business intelligence software solutions company, since May 1998. In addition, he has served as Chairman and Chief Executive Officer of DentalLine.com, a group benefit and internet company, since July 1999. From March 1998 to August 2000, he served as Director and Vice Chairman of Image Vision, a developer and marketer of imaging systems and products. Mr. Klein also served as Chairman and Chief Executive Officer of the MIM Corporation, a provider of pharmacy benefit services, from 1996 to May 1998. Mr. Klein is a director of U.S. Interactive, Inc. and Sunbeam Corporation. (1)(2)

DAVID A. TEPPER (44) has served as a director of the Company since April 2001. Mr. Tepper has been President of Appaloosa Management L.P. since 1993. Mr. Tepper also serves as a director of Inamed Corporation, a global surgical and medical device company. (2)

The information contained in this Proxy Statement concerning the nominees is based upon statements made or confirmed to the Company by or on behalf of such nominees, except to the extent certain information appears in its records. Directors' ages are given as of January 1, 2002.

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(1) Member of the Audit and Compliance Committee, of which Mr. Kaufman and Mr. Klein serve as Co-Chairmen.

(2) Member of the Executive Compensation Committee, of which Mr. Klein is Chairman.

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

CERTAIN INFORMATION CONCERNING THE BOARD OF DIRECTORS

In connection with the Company's emergence from bankruptcy, a new board of directors, including representatives of the principal security holders following the reorganization, was appointed. Each of the prior Board members resigned on April 20, 2001.

During 2001, the Board of Directors held twelve meetings, including four regular and eight special meetings. Each director attended more than 75% of the total number of meetings of the Board and the committees on which each served. The Board of Directors has established an Audit and Compliance Committee and an Executive Compensation Committee. The Company does not have a nominating or similar committee.

Audit and Compliance Committee. The Audit and Compliance Committee held five meetings during 2001. The Audit and Compliance Committee assists the Board of Directors in monitoring (a) the adequacy of the Company's system of internal controls, accounting policies, financial reporting practices, and the quality and integrity of the Company's financial reporting and (b) the Company's compliance with applicable laws, regulations and policies.

Executive Compensation Committee. The Executive Compensation Committee held four meetings in 2001. The Executive Compensation Committee assists the Board of Directors in fulfilling its responsibility to the shareholders and investment community to ensure that the Company's key executives and Board members are compensated in accordance with the Company's overall compensation policies. The Committee recommends and approves compensation policies, programs and pay levels that are necessary to support the Company's objectives and that are rational and reasonable to the value of the services rendered.

COMPENSATION OF DIRECTORS

During 2001, non-employee directors of the Company received $2,000 for each board meeting attended and $1,000 for each committee meeting attended. In addition, non-employee directors received a $2,500 retainer for each calendar quarter that they served as a director.

Pursuant to the Company's Stock Option Plan for Non-Employee Directors (the

''Directors Plan''), each non-employee member of the Board received an option to purchase 10,000 shares of Common Stock. Each non-employee director serving on May 21, 2001 received an option having an exercise price of $32.00 per share which was the Executive Compensation Committee's determination of the fair market value of the Common Stock on the date of grant. On July 17, 2001, Mr. Embler was granted an option to purchase 10,000 shares of Common Stock having an exercise price of $47.50 per share in connection with his appointment to the Board of Directors. All of these options are exercisable in four equal annual installments beginning on the first anniversary of their grant date and have a ten year term.

In addition, under the Directors Plan, the Company also will issue, on January 1 of each year during the term of the Directors Plan, an option to purchase 3,000 shares of Common Stock to each non-employee director. In addition, upon the appointment or election of a person as a non-employee director for the first time, such

director will receive a one-time grant of an option to purchase 10,000 shares of Common Stock. These options will have an exercise price equal to the fair market value of the Common Stock on the date the option is granted in accordance with the terms of the Directors Plan.

SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT

The following table sets forth certain information regarding beneficial ownership of Common Stock and the Company's Series A and Series B warrants, as of January 31, 2002, by (1) each shareholder known by the Company to be the beneficial owner of more than 5% of its outstanding shares of Common Stock, (2) each person who is a director or nominee for director, (3) each of the Company's Named Executive Officers (as defined herein), and (4) all of the persons who are directors and executive officers of the Company, as a group.

	Amount and Nature of Beneficial Ownership (1)			Percent of Class		
Name of Beneficial Owner	Common Stock	Series A Warrants	Series B Warrants	Common Stock	Series A Warrants	Series Warrant
Directors and Named Executive Officers						
Edward L. Kuntz	125,000	--	--	*	--	--
James Bolin (2)	4,996,822	720,398	1,800,996	24.7	36.0	36.0
Michael J. Embler	--	--	--	--	--	--
Garry N. Garrison	--	--	--	--	--	--
Isaac Kaufman	--	--	--	--	--	--
John H. Klein	--	--	--	--	--	--
David A. Tepper (2)	4,996,822	720,398	1,800,996	24.7	36.0	36.0
Frank J. Battafarano	30,905	--	--	*	--	--
Richard E. Chapman	31,062	--	--	*	--	--
Donald D. Finney	28,500	--	--	*	--	--
Richard A. Schweinhart (3)	31,050	--	--	*	--	--
All Directors and Executive Officers as a Group (16 persons) (4)	5,326,030	720,398	1,800,996	26.4	36.0	36.0
Other Security Holders with More than						

5% Ownership						
Appaloosa Management L.P., Appaloosa Partners, Inc. and David A. Tepper (2).	4,996,822	720,398	1,800,996	24.7	36.0	36.0
Stephen Feinberg (5)...................	1,181,451	--	--	5.7	--	--
Franklin Mutual Advisers, LLC (6).......	5,047,831	560,242	1,400,603	25.7	28.0	28.0
Goldman, Sachs & Co. and The Goldman Sachs Group, Inc. (7).................	1,778,704	170,594	426,484	9.7	8.5	8.5
Van Kampen Prime Rate Income Trust (8)...	978,504	--	--	5.5	--	--
Ventas, Inc. and Ventas Realty, Limited Partnership (9)......................	1,080,314	--	--	6.1	--	--

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* Denotes less than 1%.

(1) Such information assumes that (a) options or warrants that are held by such person (but not those held by any other person) and which are exercisable within 60 days from the date of this Proxy Statement have been exercised and (b) to the extent publicly available information does not specify which portion of certain shares of Common Stock is in the form of warrants, such shares are held in the form of Common Stock. Unless otherwise noted, the Company believes that all persons named in the table have sole voting and investment power with respect to all shares of Common Stock and/or warrants beneficially owned by them. With respect to Mr. Schweinhart, his total includes 50 shares held jointly with his spouse.

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(2) Based on a Schedule 13D/A jointly filed by Appaloosa Management L.P., Appaloosa Partners, Inc. and David A. Tepper dated November 14, 2001 with the Securities and Exchange Commission (the "SEC") and a Form 4 jointly filed with the SEC by Appaloosa Management L.P., Appaloosa Partners, Inc., David A. Tepper and James Bolin. According to these filings, Mr. Tepper is the sole stockholder and President of Appaloosa Partners, Inc. Mr. Bolin is Vice President and Secretary of Appaloosa Partners, Inc. Appaloosa Partners, Inc. is the general partner of Appaloosa Management L.P. Appaloosa Management L.P. is the general partner of Appaloosa Investment Limited Partnership I and acts as an investment advisor to Palomino Fund Ltd. According to the Schedule 13D/A, Appaloosa Management L.P., Appaloosa Partners, Inc. and Mr. Tepper may be deemed to have the sole voting and dispositive power with respect to 4,996,822 shares of Common Stock, of which 2,521,394 represent shares issuable upon exercise of the Series A and Series B warrants. The address of Appaloosa Management L.P., Appaloosa Partners, Inc., Mr. Tepper and Mr. Bolin is 26 Main Street, 1/st/ Floor, Chatham, New Jersey 07928.

(3) Mr. Schweinhart resigned from the Company effective February 25, 2002.

(4) The number of shares of Common Stock shown in the table includes shares issuable upon the exercise of 720,398 Series A warrants and 1,800,996 Series B warrants. See note 2.

(5) Based on a Schedule 13D filed by Stephen Feinberg on May 8, 2001 with the SEC and other information provided to the Company. Cerberus Institutional Partners, L.P. is the holder of 244,530 shares of Common Stock, Cerberus International, Ltd. is the holder of 630,157 shares of Common Stock and various other private investment funds own in the aggregate 306,764 shares of Common Stock. Based on the Schedule 13D, Stephen Feinberg possesses sole power to vote and direct the disposition of all securities described in the immediately preceding sentence. The address of Mr. Feinberg is 450 Park Avenue, 28/th/ Floor, New York, New York 10022.

(6) Based on a Schedule 13D/A filed by Franklin Mutual Advisers, LLC dated January 9, 2002 with the SEC and other information available to the Company. According to the Schedule 13D/A, the Common Stock is beneficially owned by one or more open-end investment companies or other management accounts of Franklin Mutual Advisers, LLC. Under its advisory contracts, Franklin Mutual Advisers, LLC has sole voting and investment discretion over these securities. The number of shares of Common Stock shown in the table includes shares issuable upon the exercise of 560,242 Series A warrants and 1,400,603 Series B warrants. Michael J. Embler is a Vice President of Franklin Mutual Advisers, LLC and disclaims beneficial ownership of shares held by Franklin Mutual Advisers, LLC. The address of Franklin Mutual Advisers, LLC is 51 John F. Kennedy Parkway, Short Hills, New Jersey 07078.

(7) Based on a Schedule 13G/A jointly filed by Goldman, Sachs & Co. and The Goldman Sachs Group, Inc. on February 14, 2002 with the SEC and other information available to the Company. According to the Schedule 13G/A, Goldman, Sachs & Co. and The Goldman Sachs Group, Inc. share voting and dispositive power with respect to these securities. The number of shares of Common Stock shown in the table includes shares issuable upon the exercise of 170,594 Series A warrants and 426,484 Series B warrants. The address of Goldman, Sachs & Co. and The Goldman Sachs Group, Inc. is 85 Broad Street, New York, New York 10004.

(8) Based on information provided to the Company by Van Kampen Prime Rate Income Trust. The address of Van Kampen Prime Rate Income Trust is 1 Parkview Plaza, Oakbrook Terrace, Illinois 60181.

(9) Based on a Schedule 13G/A jointly filed by Ventas, Inc. and Ventas Realty, Limited Partnership on January 22, 2002 with the SEC. According to the Schedule 13G/A, each of Ventas, Inc. and Ventas Realty, Limited Partnership has shared ownership and voting dispositive power with respect to these securities. Ventas, Inc. is the sole general partner of Ventas Realty, Limited Partnership, and the sole member of the only limited partner of Ventas Realty, Limited Partnership. The address of each of Ventas, Inc. and Ventas Realty, Limited Partnership is 4360 Brownsboro Road, Suite 115, Louisville, Kentucky 40207-1642.

SECTION 16(a) BENEFICIAL OWNERSHIP REPORTING COMPLIANCE

Section 16(a) of the Securities Exchange Act of 1934 requires the Company's directors and executive officers and persons who own more than 10% of the Common Stock to file initial stock ownership reports and reports of changes in ownership with the SEC. Based on a review of these reports and on written representations from the reporting persons that no other reports were required, the Company believes that the applicable Section 16(a) reporting requirements were complied with for all transactions which occurred in 2001 except for a late Form 3 filed by Franklin Mutual Advisers, LLC, reflecting the Company's securities distributed to it under the Plan of Reorganization. The Form 3 was subsequently filed by Franklin Mutual Advisers, LLC that reflects the securities of the Company it received under the Plan of Reorganization.

EXECUTIVE COMPENSATION AND OTHER INFORMATION

The following Summary Compensation Table sets forth compensation earned during the three fiscal years ended December 31, 2001 by the Chief Executive Officer of the Company and the other four most highly compensated executive officers of the Company (collectively, the "Named Executive Officers").

Summary Compensation Table

Name and Principal Position	Year	Annual Compensation: Salary	Annual Compensation: Bonus(1)	Annual Compensation: Other Annual Compensation(2)	Long-Term Compensation: Restricted Stock Awards	Long-Term Compensation: Securities Underlying Options
Edward L. Kuntz...............	2001	$795,700	$1,392,475	$123,902	$5,197,500(4)	135,000
Chairman of the Board and	2000	771,630	1,120,125	113,695	--	--
Chief Executive Officer	1999	735,385	337,500	115,911	450,000(5)	200,000
Richard A. Schweinhart(6).....	2001	$291,760	$ 481,404	--	$1,482,250(4)	38,500
Senior Vice President and	2000	282,935	390,886	--	--	--
Chief Financial Officer	1999	272,115	123,750	--	--	--
Donald D. Finney..............	2001	$291,760	$ 481,404	--	$1,482,250(4)	38,500
President, Health Services	2000	282,935	390,886	--	--	--
Division	1999	279,711	123,750	--	--	80,000
Frank J. Battafarano..........	2001	$257,500	$ 424,875	--	$1,305,150(4)	33,900
President, Hospital Division	2000	248,651	345,000	--	--	--
	1999	213,654	96,750	--	--	--
Richard E. Chapman............	2001	$291,760	$ 481,404	--	$1,482,250(4)	38,500
Chief Administrative and	2000	282,935	390,886	--	--	--
Information Officer and	1999	274,421	123,750	--	--	--
Senior Vice President						

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(1) The amounts shown represent cash bonuses awarded under the Company's short-term incentive plan and, for 2001 and 2000, amounts earned under the Kindred Healthcare, Inc. 2000 Long-Term Incentive Plan. For 2001 and 2000, the awards under the Long-Term Incentive Plan earned by the Named Executive Officers follow:

Year	Mr. Kuntz	Mr. Schweinhart	Mr. Finney	Mr. Battafarano	Mr. Chapman
2001...	$795,700	$262,584	$262,584	$231,750	$262,584
2000...	540,750	178,448	178,448	157,500	178,448

See "--Long-Term Incentive Plan."

(2) These amounts represent travel and living expenses (including a gross-up for applicable taxes) paid to Mr. Kuntz of $81,003 for each of 2001, 2000 and 1999 and certain transportation related benefits of $42,899, $32,692 and $34,908 for 2001, 2000 and 1999, respectively.

(3) In addition to certain amounts noted below, the amounts in this column include contributions for the benefit of the Named Executive Officers to the Company's Retirement Savings Plan ("RSP"), Deferred Compensation Plan ("DCP"), and for 1999, amounts funded and distributed from the Company's former Supplemental Executive Retirement Plan ("SERP") as follows:

	2001			2000			1999			
	RSP	DCP	Total	RSP	DCP	Total	RSP	DCP	SERP	Total
Mr. Kuntz......	$5,100	--	$ 5,100	$5,100	--	$ 5,100	$4,800	--	--	$ 4,800
Mr. Schweinhart	5,100	--	5,100	5,100	--	5,100	4,800	--	--	4,800
Mr. Finney.....	5,100	--	5,100	3,966	--	3,966	--	--	--	--
Mr. Battafarano	5,100	$7,963	13,063	5,100	$7,383	12,483	4,800	$5,902	$149,057	159,759
Mr. Chapman....	5,100	--	5,100	5,100	--	5,100	4,800	--	--	4,800

The amounts also include Retention Bonuses (as defined below) paid to the Named Executive Officers as follows:

Year	Mr. Kuntz	Mr. Schweinhart	Mr. Finney	Mr. Battafarano	Mr. Chapman
2001...	$625,000	$229,167	$229,167	$179,167	$229,167
2000...	--	--	--	--	--
1999...	312,500	114,583	114,583	89,583	114,583

In addition, the amounts for 2001 for Mr. Kuntz and Mr. Schweinhart include Performance Bonuses (as defined below) of $2,000,000 and $500,000, respectively, for the successful completion of the Plan of Reorganization. See "--Management Retention Plan." In addition, the amounts include certain transportation related benefits for the following years:

Year	Mr. Schweinhart	Mr. Battafarano	Mr. Chapman
2001...	$4,612	$10,475	$1,629
2000...	8,225	4,303	--
1999...	2,993	4,295	--

(4) These amounts represent the fair market value on the date of grant of shares of restricted stock granted on May 21, 2001 to the Named Executive Officers as follows: Mr. Kuntz--135,000 shares; Mr. Schweinhart--38,500 shares; Mr. Finney--38,500 shares; Mr. Battafarano--33,900 shares; and Mr. Chapman--38,500 shares. One-third of these shares vested on the date of grant and the remaining two-thirds will vest as follows: 15% on each of the first and second anniversaries of the grant date; 20% on the third anniversary of the grant date and 50% on the fourth anniversary of the grant date. Based on the closing price reported on the NASDAQ of $52.00 for the Common Stock on December 31, 2001, these awards would have been valued at the following amounts: Mr. Kuntz--$7,020,000; Mr. Schweinhart--$2,002,000; Mr. Finney--$2,002,000; Mr. Battafarano--$1,762,800; and Mr. Chapman--$2,002,000. The Company does not

pay dividends on its Common Stock, but the holder of restricted stock is entitled to dividends if paid.

(5) This amount represents the fair market value on the date of grant of 200,000 restricted shares of the Company's former common stock granted on February 12, 1999. These shares were scheduled to vest on January 1, 2000 but Mr. Kuntz voluntarily forfeited the restricted shares prior to the vesting date.

(6) Mr. Schweinhart resigned from the Company effective February 25, 2002.

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OPTION GRANTS IN LAST FISCAL YEAR

The following table sets forth information concerning options to purchase shares of Common Stock granted to the Named Executive Officers in 2001:

Name	Number of Securities Underlying Options Granted (1)	% of Total Options Granted to Employees in 2001	Exercise Price Per Share(2)	Market Price on the Date of Grant(3)	Expiration Date	Potential Realiz Assumed Annual R Price Apprec Option T 0%	5%
Edward L. Kuntz.......	135,000	13.5%	$32.00	$38.50	5/21/06	$877,500	$2,313,
Richard A. Schweinhart	38,500	3.9%	$32.00	$38.50	5/21/06	$250,250	$ 659,
Donald D. Finney......	38,500	3.9%	$32.00	$38.50	5/21/06	$250,250	$ 659,
Frank J. Battafarano..	33,900	3.4%	$32.00	$38.50	5/21/06	$220,350	$ 580,
Richard E. Chapman....	38,500	3.9%	$32.00	$38.50	5/21/06	$250,250	$ 659,

(1) All options shown in the above table become exercisable in three equal annual installments, beginning on the first anniversary of the date of grant, and have a five-year term. All options become fully exercisable upon a change in control of the Company (as defined in the Company's 2000 Stock Option Plan).

(2) The exercise price and any tax withholding obligations related to exercise may be paid, at the discretion of the Executive Compensation Committee, in cash, in shares of Common Stock or in any other reasonable consideration deemed appropriate.

(3) The Executive Compensation Committee set an exercise price of $32.00 per share based on its determination of the fair market value of the Common Stock on the date of grant. The Executive Compensation Committee determined that the minimal trading volume in the Common Stock between the date of the Company's emergence from bankruptcy and the grant date did not represent a fair trading value. Accordingly, the Executive Compensation Committee established the exercise price based on the weighted average purchase price of the Series A and Series B warrants issued in connection with the Plan of Reorganization.

(4) The dollar amounts in this table represent the potential realizable value of the stock options granted, assuming that the market price of the Common Stock appreciates in value from the date of grant to the end of the option term at annualized rates of 0%, 5% and 10% but before taxes associated with exercise. Therefore, these amounts are not the actual value of the options granted and are not intended to forecast possible future appreciation, if any, in the price of the Common Stock. No assurance can be given that the

price of the Common Stock will appreciate at these rates or experience any appreciation.

OPTION EXERCISES AND HOLDINGS

The following table sets forth information concerning the exercise of options during 2001 and unexercised options held as of December 31, 2001 by the Named Executive Officers.

Aggregate Option Exercises in 2001
and Year-end Option Values

Name	Shares Acquired on Exercise	Value Realized	Number of Securities Underlying Unexercised Options at 12/31/01		Value of Unexercised In-the-Money Options at 12/31/01(1)	
			Exercisable	Unexercisable	Exercisable	Unexercisable
Edward L. Kuntz.......	--	--	--	135,000	--	$2,700,000
Richard A. Schweinhart	--	--	--	38,500	--	$ 770,000
Donald D. Finney......	--	--	--	38,500	--	$ 770,000
Frank J. Battafarano..	--	--	--	33,900	--	$ 678,000
Richard E. Chapman....	--	--	--	38,500	--	$ 770,000

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(1) The value of unexercised options was calculated by subtracting the exercise price from the market value of the underlying Common Stock as of December 31, 2001. The market value of the Common Stock was $52.00 per share as of December 31, 2001, based on the closing price per share on the NASDAQ.

Long-Term Incentive Plan

During 2000, the Executive Compensation Committee adopted the Company's 2000 Long-Term Incentive Plan, subject to consummation of the Plan of Reorganization. This plan provides for the payment of cash bonus awards to key employees of the Company upon attainment by the Company of specified performance goals. For each performance period, the Executive Compensation Committee selects plan participants who are in a position to contribute materially to the success of the Company and establishes the performance goal or goals to be measured under the plan. The performance periods under the plan cover one year. The plan currently includes in excess of 600 employees, including hospital and nursing center administrators.

Participants are eligible to receive cash bonuses based upon a percentage of base salary and vary depending upon the participant's position within the Company and the extent to which the performance goals established by the Executive Compensation Committee are attained. The maximum awards eligible under the plan as a percentage of base salary are 100% for the Chief Executive Officer and 90% for the other Named Executive Officers. No awards are granted under the plan until certain minimum levels of performance are reached. Awards are generally payable in equal annual installments on or about each of the first, second and third anniversaries of the end of the relevant performance period, provided that the participant is employed by the Company at the time payments are due.

Based upon the goals established by the Executive Compensation Committee for the 2001 performance period, the Company achieved the maximum award under the plan. These awards will be paid in three equal annual installments beginning on or about December 31, 2002.

Management Retention Plan

In November 1999, the Company received approval from the bankruptcy court to implement a management retention plan (the "Retention Plan") to enhance the ability of the Company to retain key management employees during the reorganization period. The Retention Plan provided for the payment of up to an aggregate of $11 million in bonuses to various key employees of the Company. The Retention Plan consisted of two parts: (1) the payment of up to an aggregate of $7.3 million to key employees as retention bonuses ("Retention Bonuses") and (2) the payment of up to an aggregate of $3.7 million to certain employees who contributed significantly to the successful completion of the Plan of Reorganization ("Performance Bonuses"). The Retention Plan provided that

the Retention Bonuses would be paid in three equal installments upon: (a) the bankruptcy court's approval of the Retention Plan, (b) the effective date of the Plan of Reorganization and (c) three months following the effective date of the Plan of Reorganization. The Performance Bonuses were paid on the effective date of the Plan of Reorganization.

Supplemental Executive Retirement Plan

In 1998, the Executive Compensation Committee adopted the Supplemental Executive Retirement Plan which provided certain of the Named Executive Officers and certain other officers of the Company with supplemental deferred benefits in the form of retirement payments. Effective December 31, 1999, the SERP was amended to freeze accumulated benefits under the SERP and eliminate the accrual of any benefits thereafter. In February 2001, the SERP was further amended to eliminate any change in control provisions. Following this amendment, the SERP was terminated. The termination of the SERP will have no effect on the future payment of vested benefits under the SERP.

In January 1999, the Executive Compensation Committee approved a partial funding and distribution of individual annuity contracts to participants with five or more years of service with the Company to settle approximately one-third of the obligations under the SERP relating to such participants. In addition, the eligible participants received a tax payment to cover their estimated taxes associated with this distribution. Mr. Battafarano received an annuity contract and a tax payment totaling $149,057 in 1999. No other Named Executive Officer received any benefits under the SERP.

Employment and Other Agreements

In July 1998, the Company entered into employment agreements with its officers, including certain of the Named Executive Officers. In February 1999, the Company entered into a new employment agreement with Mr. Kuntz in connection with his appointment as Chairman of the Board, Chief Executive Officer and President. The Company also entered into an employment agreement with Mr. Finney in connection with his employment in January 1999 as President, Health Services Division. In November 1999, the Company also amended existing employment agreements with Mr. Battafarano and Mr. Finney to provide consistent benefits among the Company's executive officers. In December 2001, the Company further amended the employment agreements of the executive officers, other than Mr. Kuntz, to provide certain limited benefits for a voluntary termination following the employment of a new president and chief operating officer by the Company.

The agreements for the Named Executive Officers generally contain standard terms except as noted below. These agreements have a one year term but are extended automatically unless the Company notifies the Named Executive Officer. Upon such notification, the employment agreements will terminate in one year. The employment agreements provide a base salary and the ability of the Named Executive Officer to be eligible for bonuses and to participate in the Company's incentive and other employee benefit plans. Mr. Kuntz's agreement also provides that the Company will pay $6,750 per month (which includes a gross-up for applicable taxes), for travel and living expenses incurred by Mr. Kuntz. The base salaries for 2001 for the Named Executive Officers under the employment agreements were as follows: Mr. Kuntz--$795,700; Mr. Schweinhart--$291,760; Mr. Finney--$291,760; Mr. Battafarano--$257,500; and Mr. Chapman--$291,760. The Named Executive Officers may receive increases in their base salaries as approved by the Executive Compensation Committee.

Under certain circumstances, the employment agreements also provide for severance payments if the Named Executive Officer's employment is terminated. If employment is terminated by reason of death or disability, the Named Executive Officer is entitled to a prorated portion of his target bonus. If the Named Executive Officer's employment is terminated for cause, no additional payments are made under the employment agreements. If the Named Executive Officer's employment is terminated for good reason (as defined in the employment agreements) or other than for cause (collectively, an "Involuntary Termination"), certain levels of severance payments are provided under the employment agreements.

Upon an Involuntary Termination, Mr. Kuntz's agreement provides for a cash payment equal to the prorated portion of his target bonus in the year of termination and three times his base salary and target bonus in the year of termination. In addition, Mr. Kuntz would be entitled to coverage under the Company's employee benefit plans for three years, three years of additional vesting of restricted stock awards and stock options, and an additional three years in which to exercise such options. Mr. Kuntz's agreement also requires the Company to provide substantially similar office space and the services of an administrative assistant for three years.

Upon the Involuntary Termination of the other Named Executive Officers, their agreements provide for a cash payment equal to the prorated portion of their target bonus in the year of termination and one and one-half times their base salary and target bonus in the year of termination. In addition, they would be entitled to coverage under the Company's employee benefit plans for 18 months, 18 months of additional vesting of restricted stock awards and stock options, and an additional 18 months in which to exercise such options. The employment agreements for the Named Executive Officers, other than Mr. Kuntz, also provide for one year of additional vesting for all options if the executive voluntarily leaves the Company's employment within a 180 day period beginning on the six month anniversary of the first day of employment of the Company's new president and chief operating officer.

The Company also has entered into Change in Control Severance Agreements with certain of its key employees, including the Named Executive Officers. These agreements provide for the payment of severance benefits under certain circumstances. These benefits become payable at any time within two years after a change in control of the Company if: (a) the Company terminates the executive's employment without cause or (b) the executive terminates employment with the Company for good reason (as defined in the agreement) or within either of two 30-day periods commencing 30 days after the change in control and one year after the change in control, respectively. The benefits to be afforded the Named Executive Officers include: (a) a cash payment equal to three times base salary and target bonus as of the termination of employment; (b) continuation of health, life and disability insurance coverage for three years; (c) full vesting under the Company's retirement savings plan; and (d) an additional payment for any excise taxes the Named Executive Officer may incur as a result of the change in control payments.

Compensation Committee Interlocks and Insider Participation

Between January 1, 2001 and the Company's emergence from bankruptcy, the following persons served on the Executive Compensation Committee of the Board of Directors: Mr. Stanley C. Gault (Chairman), Mr. Ulysses L. Bridgeman, Jr., Ms. Donna R. Ecton and Mr. William H. Lomicka. Beginning April 20, 2001, the new members of the Executive Compensation Committee were John H. Klein (Chairman), Jeff Altman, Garry N. Garrison and David A. Tepper. Mr. Altman resigned from the Board of Directors effective June 19, 2001. None of the persons who served on the Executive Compensation Committee during 2001 were employees of the Company. Mr. Tepper engaged in certain transactions with the Company during 2001. See "Certain Relationships and Related Transactions."

REPORT OF THE EXECUTIVE COMPENSATION COMMITTEE

The Executive Compensation Committee of the Board of Directors is composed entirely of independent directors. The Executive Compensation Committee is responsible for establishing and administering the policies and programs that govern both annual compensation and stock-based incentive compensation plans for the executive officers of the Company. The Company's executive compensation policy is based upon principles designed to motivate and retain executive officers and to establish an appropriate relationship between executive pay and short-term and long-term performance. The key components of the Company's compensation program are base salary, annual incentive awards and equity participation. These components are administered to provide total compensation that is competitive in the marketplace, rewards successful short-term and long-term financial and non-financial performance and aligns executive officers' interests with those of shareholders.

The Executive Compensation Committee reviews each component of executive compensation on an annual basis with the assistance of an independent consultant and the use of executive compensation surveys from comparable healthcare and service companies. The companies surveyed include some, but not all, of the companies covered in the indices included in the Performance Graph. The Company's policy is to target total executive compensation between the 50/th/ and 75/th/ percentile of the marketplace as defined above.

The Company experienced certain extraordinary events in 2001, which influenced the Executive Compensation Committee's decisions relating to executive compensation in 2001. These events included: (a) the Company's successful reorganization and emergence from bankruptcy, (b) the cancellation of the previous equity securities of the Company, and (c) the cancellation of all equity-based incentive agreements previously provided to executive officers.

As part of its Plan of Reorganization, the Company adopted the 2000 Stock Option Plan, the 2000 Restricted Share Plan and the 2000 Long-Term Incentive Plan for the purpose of providing long-term incentive compensation awards to key employees of the Company following the consummation of the reorganization.

In November 1999, the Company received approval from the bankruptcy court to implement the Retention Plan to enhance the ability of the Company to retain key management employees during the reorganization period. The Retention Plan was established by the Company's former executive compensation committee. The Retention Plan provided for the payment of up to an aggregate of $11 million in bonuses to various key employees of the Company. The Retention Plan consisted of two parts: (1) the payment of up to an aggregate of $7.3 million to key employees as Retention Bonuses and (2) the payment of up to an aggregate of $3.7 million to certain employees who contributed significantly to the successful completion of the Plan of Reorganization.

Base Salary

Base salary for executive officers is determined by an assessment of overall Company performance, the individual executive officer's performance, changes in executive officer responsibility and relevant industry survey findings. While certain aspects of performance can be measured in financial terms, the Executive Compensation Committee also evaluates executives in areas of performance that are more subjective. These areas include the success of the executive officer in developing and executing the Company's strategic plans, addressing the significant changes affecting the healthcare industry, developing key employees and exercising leadership. The Company's policy is to target executive base salaries at the 50/th/ percentile of the marketplace as defined above.

Annual Incentive

The Executive Compensation Committee believes that a significant portion of total cash compensation for executive officers should be subject to the attainment of specific Company financial and quality criteria. This approach creates a direct incentive for executive officers to achieve desired performance goals and places a

significant percentage of each executive officer's compensation at risk. The Company's incentive compensation plans are designed to reward officers and other designated key employees for the attainment of financial and quality performance objectives approved annually by the Executive Compensation Committee. Incentive compensation objectives are constructed to encourage responsible and profitable growth while taking into account non-routine factors that may be integral to the success of the Company.

The Company maintains a short-term incentive compensation plan for executive officers and other key employees of the Company. The Executive Compensation Committee establishes performance goals upon which the annual bonuses are based. Typically, these goals are based upon financial performance, accounts receivable collections and individual performance goals for each eligible employee. Annual bonuses are based upon a percentage of the employee's salary. Target bonuses for 2001 were 60% for the Named Executive Officers. The annual incentive plan also provides additional compensation beyond the target bonuses for performance exceeding the targeted goals. Based on the achievement of the established goals, the Executive Compensation Committee awarded bonuses to the executive officers equal to 75% of their base salaries. For 2001, the short-term incentive bonuses earned by the Named Executive Officers were as follows: Mr. Kuntz--$596,775; Mr. Schweinhart--$218,820; Mr. Finney--$218,820; Mr. Battafarano--$193,125; and Mr. Chapman--$218,820.

The Long-Term Incentive Plan provides for the payment of cash bonus awards to key employees of the Company upon attainment by the Company of specified performance goals. For each performance period, the Executive Compensation Committee selects plan participants who are in a position to contribute materially to the success of the Company and establishes the performance goal or goals to be measured under the plan. The performance periods under the plan cover one year. Participants are eligible to receive cash bonuses based upon a percentage of salary and vary depending on the participant's position within the Company and the extent to which the performance goals established by the Executive Compensation Committee are attained. The maximum awards eligible under the plan as a percentage of base salary are 100% for the Chief Executive Officer and 90% for the other Named Executive Officers. No awards are granted under the plan until certain minimum levels of performance are reached. Cash awards are payable in equal annual installments on or about each of the first, second and third anniversaries of the end of the relevant performance period, provided that the participant is employed by the Company at the time payments are due. Based upon the goals established by the Executive Compensation Committee for the 2001 performance period, the Company achieved the maximum award under the plan.

Equity Participation

The Executive Compensation Committee believes that equity participation is a key component of its executive compensation program. The use of such awards provides a long-term link between the results achieved for the Company's shareholders and the rewards provided to executive officers. Stock options and other stock-based compensation are granted to executive officers primarily based on the executive officer's actual and potential contribution to the Company's growth, long-term performance and the practices of companies in the long-term care industry. Stock-based compensation is designed to retain executive officers and motivate them to enhance shareholder value by aligning the financial interests of executive officers with those of the Company's shareholders. Stock-based compensation also provides an effective incentive for management to create shareholder value over the long term since the full benefit of the compensation package cannot be realized unless an appreciation in the price of the Common Stock occurs over a number of years.

Following the consummation of the Plan of Reorganization, the Executive Compensation Committee granted a total of 600,000 restricted stock awards pursuant to the 2000 Restricted Share Plan and 592,700 stock options to the officers of the Company pursuant to the 2000 Stock Option Plan. The restricted stock and stock option awards, respectively, granted to the Named Executive Officers in 2001 were as follows: Edward L. Kuntz--135,000 shares and 135,000 options; Richard A. Schweinhart--38,500 shares and 38,500 options; Donald D. Finney--38,500 shares and 38,500 options; Frank J. Battafarano--33,900 shares and 33,900 options; and Richard E. Chapman--38,500 shares and 38,500 options.

The Executive Compensation Committee granted the stock options and restricted stock described above based upon its judgment that the number and terms were appropriate and desirable considering each executive officer's actual and potential contribution to the Company, including contributions to the completion of the Plan of Reorganization. The assessment of actual and potential contribution was based on the Executive Compensation Committee's subjective evaluation of each executive officer's ability, skills, efforts and leadership.

Retention Payments

In accordance with the Retention Plan, each Named Executive Officer received the final two installments of the Retention Bonuses in 2001 following the successful completion of the Plan of Reorganization. In addition, Mr. Kuntz and Mr. Schweinhart were awarded Performance Bonuses of $2,000,000 and $500,000, respectively, for their substantial efforts toward the successful reorganization of the Company. The amounts of these awards were established when the Retention Plan was adopted in 1999.

Compensation of the Chief Executive Officer

Consistent with the executive compensation policy and components described above, the Executive Compensation Committee determined the compensation received by Edward L. Kuntz, Chairman of the Board and Chief Executive Officer of the Company, for services rendered in 2001. Under Mr. Kuntz's guidance, the Company (a) successfully emerged from bankruptcy, (b) implemented its corporate integrity agreement, (c) improved its financial results and (d) completed an equity offering that established a public trading market for the Company's Common Stock. Based upon these accomplishments and upon executive compensation surveys, the Executive Compensation Committee believes that the base salary, incentive bonuses, restricted share award and option grant to Mr. Kuntz were fair and competitive. The assessment of actual and potential contribution was based on the Executive Compensation Committee's subjective evaluation of Mr. Kuntz's abilities, skills, efforts and leadership.

Executive Compensation Tax Deductibility

The Omnibus Budget Reconciliation Act of 1993 amended the Internal Revenue Code (the ''Code'') to provide generally that the compensation paid by publicly held corporations to the chief executive officer and the four most highly paid senior executive officers in excess of $1,000,000 per executive will be deductible by the Company only if paid pursuant to qualifying performance-based compensation plans approved by shareholders of the Company. Compensation as defined by the Code includes, among other things, base salary, incentive compensation and gains on stock options and restricted stock. It is the Executive Compensation Committee's policy to maximize the effectiveness of the Company's executive compensation plans. In that regard, the Executive Compensation Committee intends to maintain flexibility to take actions which are deemed to be in the best interests of the Company and its shareholders. Such actions may not always qualify for tax deductibility under the Code.

All members of the Executive Compensation Committee of the Company listed below submit the foregoing report.

EXECUTIVE COMPENSATION COMMITTEE

John H. Klein, Chairman
Garry N. Garrison
David A. Tepper

AUDIT AND COMPLIANCE COMMITTEE REPORT

The Audit and Compliance Committee (the "Audit Committee") of the Company is currently comprised of four directors. Each member is independent and financially literate as defined in the NASDAQ listing standards. The Board of Directors has adopted a written charter for the Audit Committee that is included as Appendix A to this Proxy Statement.

The Audit Committee reviews the Company's financial reporting processes on behalf of the Board of Directors. In fulfilling its responsibilities, the Audit

Committee has reviewed and discussed the audited consolidated financial statements contained in the Annual Report on Form 10-K for the year ended December 31, 2001 with the Company's management and its independent auditors, PricewaterhouseCoopers LLP ("PwC"). Management is responsible for the financial statements and the underlying financial reporting processes, including the system of internal accounting controls. PwC is responsible for expressing an opinion on the conformity of the consolidated financial statements with accounting principles generally accepted in the United States of America. Management has represented to PwC and the Audit Committee that the Company's consolidated financial statements were prepared in accordance with accounting principles generally accepted in the United States of America.

The Audit Committee held five meetings during 2001. The Audit Committee discussed with PwC the matters required to be discussed by Statement on Auditing Standards No. 61, Communication with Audit Committees, as amended. In addition, the Audit Committee has discussed with PwC the auditors' independence from the Company and its management including the matters in the written disclosures required by Independence Standards Board Standard No. 1, Independence Discussions with Audit Committees. In connection with this discussion, the Audit Committee also reviewed the fees paid by the Company to PwC for the year ended December 31, 2001. During 2001, fees for services provided by PwC were as follows:

Audit fees...	$ 800,000
Financial information systems design and implementation fees	--
All other fees...	1,399,000
Total..	$ 2,199,000

The Audit Committee has considered whether the provisions of non-audit services is compatible with maintaining the auditors' independence.

The Audit Committee also discussed with the Company's internal auditors and with PwC the overall scope and plans for their respective audits. The Audit Committee meets periodically with the Company's internal auditors and with PwC, with and without management present, to discuss the results of their examinations, the evaluation of the Company's internal controls and the overall quality of the Company's financial reporting.

In reliance upon the reviews and discussions referenced above and the report of the independent auditors included in the independent auditors opinion with respect to the audited financial statements, the Audit Committee recommended to the Board of Directors, and the Board has approved, that the audited consolidated financial statements be included in the Company's Annual Report on Form 10-K for the year ended December 31, 2001 filed with the SEC.

All members of the Audit and Compliance Committee of the Company listed below submit the foregoing report:

AUDIT AND COMPLIANCE COMMITTEE

Isaac Kaufman, Co-Chairman
John H. Klein, Co-Chairman
James Bolin
Garry N. Garrison

CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS

Pursuant to the Plan of Reorganization, the Company issued to certain claimholders in exchange for their claims an aggregate of (1) $300 million of senior secured notes, bearing interest at the London Interbank Offered Rate (as defined in the agreement) plus 4 1/2%, which began accruing interest approximately two quarters after the Effective Date (the "Senior Secured Notes"), (2) 15,000,000 shares of Common Stock, (3) 2,000,000 Series A warrants, and (4) 5,000,000 Series B warrants. Each of the Series A warrants and the Series B warrants have a five-year term with an exercise price of $30.00 and $33.33 per share, respectively. As a result of the exchange described above, the holders of certain claims acquired control of the Company and the holders of the Company's former common stock relinquished control.

Certain of the Company's existing shareholders were claimholders in the bankruptcy and accordingly, participated in the distributions under the Plan of Reorganization. To the knowledge of the Company, the holders of more than five percent of the Company's Common Stock listed below received the following distributions under the Plan of Reorganization: Appaloosa Management L.P., Appaloosa Partners, Inc. and David A. Tepper received 2,975,428 shares of Common Stock, 720,398 Series A warrants, 1,800,996 Series B warrants and approximately $44.6 million of the Senior Secured Notes; Stephen Feinberg and certain related entities received 1,181,451 shares of Common Stock and approximately $30.1 million of the Senior Secured Notes; Franklin Mutual Advisers, LLC received 3,462,336 shares of Common Stock, 560,242 Series A warrants, 1,400,603 Series B warrants and approximately $66.3 million of the Senior Secured Notes; Goldman, Sachs & Co. and The Goldman Sachs Group, Inc. received 1,416,412 shares of Common Stock, 170,594 Series A warrants, 426,484 Series B warrants and approximately $30.7 million of the Senior Secured Notes; Van Kampen Prime Rate Income Trust received 1,064,604 shares of Common Stock and approximately $32.5 million of the Senior Secured Notes; and Ventas received 1,498,500 shares of Common Stock. Mr. David A. Tepper, a director of the Company, is the sole stockholder and President of Appaloosa Partners, Inc. Mr. James Bolin, a director of the Company, is Vice President and Secretary of Appaloosa Partners, Inc. Mr. Tepper also is the general partner of Appaloosa Management L.P. Mr. Michael J. Embler, a director of the Company, is a Vice President of Franklin Mutual Advisers, LLC.

In connection with the Plan of Reorganization, the Company also entered into a registration rights agreement with Appaloosa Management L.P., Franklin Mutual Advisers, LLC, Goldman, Sachs & Co. and Ventas Realty, Limited Partnership (the "Registration Rights Agreement"). The Registration Rights Agreement requires the Company to use its reasonable best efforts to file, cause to be declared effective and keep effective for at least two years or until all of their shares of Common Stock or warrants are sold, a "shelf" registration statement covering sales of such security holders' shares of Common Stock and warrants or, in the case of Ventas, the distribution of some or all of the shares of the Common Stock that it owns to the Ventas stockholders. The Company filed the shelf registration statement on Form S-3 with the SEC on September 19, 2001. The shelf registration statement became effective on November 7, 2001.

The Registration Rights Agreement also provides that, subject to certain limitations, each security holder party thereto has the right to demand that the Company register all or a part of the Common Stock and warrants acquired by that security holder pursuant to the Plan of Reorganization, provided that the estimated market value of the Common Stock and warrants to be registered is at least $10 million in the aggregate or not less than 5% of the Common Stock and warrants. The Company is required to use its reasonable best efforts to effect any such registration. Such registrations will be at the Company's expense, subject to certain exceptions.

In addition, under the Registration Rights Agreement, the security holders party thereto have certain rights to require the Company to include in any registration statement that it files with respect to any offering of equity securities (whether for the Company's own account or for the account of any holders of the Company's securities) such amount of Common Stock and warrants as are requested by the security holder to be included in the registration statement, subject to certain exceptions. Such registrations will be at the Company's expense, subject to certain exceptions.

Pursuant to Amendment No. 1 to the Registration Rights Agreement dated as of August 13, 2001, the parties to the Registration Rights Agreement agreed to extend the deadline for the Company to file a "shelf" registration statement from 120 days to 150 days after the Effective Date. As noted above, the Company filed a shelf registration statement with the SEC on September 19, 2001 and the shelf registration statement was declared effective on November 7, 2001.

Pursuant to Amendment No. 2 to the Registration Rights Agreement dated as of October 22, 2001, the parties to the Registration Rights Agreement agreed to an exception to certain restrictions in the Registration Rights Agreement to allow Ventas to distribute up to 350,000 shares of Common Stock that it owns to its stockholders on or after December 24, 2001.

In the fourth quarter of 2001, the Company completed a public offering of approximately 3.57 million shares of Common Stock priced at $46.00 per share. In the offering, the Company sold approximately 2.08 million newly issued shares and certain of the holders of five percent or more of the Common Stock participated in the offering as selling shareholders. The parties that participated and the number of shares sold in the offering were as follows: Appaloosa Management L.P., Appaloosa Partners, Inc. and David A. Tepper--500,000 shares; Franklin Mutual Advisers, LLC--400,000 shares; Goldman, Sachs & Co. and The Goldman Sachs Group, Inc.--250,000 shares; Van Kampen Prime Rate Income Trust--86,100 shares; and Ventas--83,300 shares.

In addition, Goldman, Sachs & Co. acted as co-lead manager in the public offering. In accordance with the underwriting agreement entered into between various parties, including the Company and Goldman, the Company paid Goldman approximately $2.9 million in underwriting commissions.

In connection with the Plan of Reorganization, the Company also entered into and assumed several agreements with Ventas. In addition to the Common Stock received by Ventas, the Company amended and restated its master lease agreements with Ventas and paid Ventas a $4.5 million cash payment in April 2001 as additional future rent. The Company also assumed and agreed to continue to perform its obligations under various agreements (the "Spin-off Agreements") entered into at the time of the Spin-off. Descriptions of these agreements with Ventas are summarized below.

Master Lease Agreements

Under the Plan of Reorganization, the Company assumed the original master lease agreements with Ventas and its affiliates and simultaneously amended and restated the agreements into four new master leases (collectively, the "Master Lease Agreements"). The following summary description of the Master Lease Agreements is qualified in its entirety by reference to the Master Lease Agreements, as filed by the Company with the SEC.

Term and Renewals

Each Master Lease Agreement includes land, buildings, structures and other improvements on the land, easements and similar appurtenances to the land and improvements, and permanently affixed equipment, machinery and other fixtures relating to the operation of the leased properties. There are several bundles of leased properties under each Master Lease Agreement, with each bundle containing approximately 7 to 12 leased properties. Each bundle contains both nursing centers and hospitals. All leased properties within a bundle have base terms ranging from 10 to 15 years beginning from May 1, 1998, subject to certain exceptions.

At the Company's option, all, but not less than all, of the leased properties in a bundle may be extended for one five-year renewal term beyond the base term at the then existing rental rate plus the then existing escalation amount per annum. The Company may further extend for two additional five-year renewal terms beyond the first renewal term at the greater of the then existing rental rate plus the then existing escalation amount per annum or the then fair market value rental rate. The rental rate during the first renewal term and any additional renewal

term in which rent due is based on the then existing rental rate will escalate each year during such term(s) at the applicable escalation rate.

The Company may not extend the Master Lease Agreements beyond the base term or any previously exercised renewal term if, at the time the Company seeks such extension and at the time such extension takes effect, (1) an event of default has occurred and is continuing or (2) a Medicare/Medicaid event of default (as described below) and/or a licensed bed event of default (as described below) has occurred and is continuing with respect to three or more leased properties subject to a particular Master Lease Agreement. The base term and renewal term of each Master Lease Agreement are subject to termination upon default by the Company (subject to certain exceptions) and certain other conditions described in the Master Lease Agreements.

Rental Amounts and Escalators

Each Master Lease Agreement is commonly known as a triple-net lease or an absolute-net lease. Accordingly, in addition to rent, the Company is required to pay the following: (1) all insurance required in connection with the leased properties and the business conducted on the leased properties, (2) all taxes levied on or with respect to the leased properties (other than taxes on the net income of Ventas) and (3) all utilities and other services necessary or appropriate for the leased properties and the business conducted on the leased properties.

Under each Master Lease Agreement, the aggregate annual rent is referred to as base rent. Base rent equals the sum of current rent and accrued rent. The Company is obligated to pay the portion of base rent that is current rent, and unpaid accrued rent will be paid as set forth below.

From the effective date of the Master Lease Agreements through April 30, 2004, base rent will equal the current rent. Under the Master Lease Agreements, the annual aggregate base rent owed by the Company currently is $180.7 million. For the period from May 1, 2001 through April 30, 2004, annual aggregate base rent payable in cash will escalate at an annual rate of 3 1/2% over the prior period base rent if certain revenue parameters are obtained. During the year ended December 31, 2001, the Company paid Ventas approximately $181 million in rents.

Each Master Lease Agreement also provides that beginning May 1, 2004, the annual aggregate base rent payable in cash will escalate at an annual rate of 2% (plus, upon the occurrence of certain events, an additional annual accrued escalator amount of 1 1/2 % of the prior period base rent) which will accrete from year to year including an interest accrual at the London Interbank Offered Rate plus 4 1/2% to be added to the annual accreted amount. This interest will not be added to the aggregate base rent in subsequent years.

The unpaid accrued rent will become payable upon the refinancing of the Company's existing credit agreements or the termination or expiration of the applicable Master Lease Agreement.

Reset Rights

During the one-year period commencing in July 2006, Ventas will have a one time option to reset the base rent, current rent and accrued rent under each Master Lease Agreement to the then fair market rental of the leased properties. Upon exercising this reset right, Ventas will pay the Company a fee equal to a prorated portion of $5 million based upon the proportion of base rent payable under the Master Lease Agreement(s) with respect to which rent is reset to the total base rent payable under all of the Master Lease Agreements. The determination of the fair market rental will be effectuated through the appraisal procedures in the Master Lease Agreements.

Use of the Leased Property

The Master Lease Agreements require that the Company utilize the leased properties solely for the provision of healthcare services and related uses and as Ventas may otherwise consent. The Company is responsible for

maintaining or causing to be maintained all licenses, certificates and permits necessary for the leased properties to comply with various healthcare regulations. The Company also is obligated to operate continuously each leased property as a provider of healthcare services.

Events of Default

Under each Master Lease Agreement, an "Event of Default" will be deemed to occur if, among other things:

- the Company fails to pay rent or other amounts within five days after notice,

- the Company fails to comply with covenants, which failure continues for 30 days or, so long as diligent efforts to cure such failure are being made, such longer period (not over 180 days) as is necessary to cure such failure,

- certain bankruptcy or insolvency events occur, including filing a petition of bankruptcy or a petition for reorganization under the bankruptcy code,

- an event of default arising from the Company's failure to pay principal or interest on the Senior Secured Notes or any other indebtedness exceeding $50 million,

- the maturity of the Senior Secured Notes or any other indebtedness exceeding $50 million is accelerated,

- the Company ceases to operate any leased property as a provider of healthcare services for a period of 30 days,

- a default occurs under any guaranty of any lease or the indemnity agreements with Ventas,

- the Company or its subtenant loses any required healthcare license, permit or approval or fails to comply with any legal requirements as determined by a final unappealable determination,

- the Company fails to maintain insurance,

- the Company creates or allows to remain certain liens,

- the Company breaches any material representation or warranty,

- a reduction occurs in the number of licensed beds in a facility, generally in excess of 10% (or less than 10% if the Company has voluntarily "banked" licensed beds) of the number of licensed beds in the applicable facility on the commencement date (a "licensed bed event of default"),

- Medicare or Medicaid certification with respect to a participating facility is revoked and re-certification does not occur for 120 days (plus an additional 60 days in certain circumstances) (a "Medicare/Medicaid event of default"),

- the Company becomes subject to regulatory sanctions as determined by a final unappealable determination and fails to cure such regulatory sanctions within its specified cure period for any facility, the Company fails to cure a breach of any permitted encumbrance within the applicable cure period and, as a result, a real property interest or other beneficial property right of Ventas is at material risk of being terminated, or

- the Company fails to cure the breach of any of the obligations of Ventas as lessee under any existing ground lease within the applicable cure period and, if such breach is a non-monetary, non-material breach, such existing ground lease is at material risk of being terminated.

Remedies for an Event of Default

Except as noted below, upon an Event of Default under one of the Master Lease Agreements, Ventas may, at its option, exercise the following remedies:

(1) after not less than ten days' notice to the Company, terminate the Master Lease Agreement to which such Event of Default relates, repossess any leased property, relet any leased property to a third party and require

that the Company pay to Ventas, as liquidated damages, the net present value of the rent for the balance of the term, discounted at the prime rate,

(2) without terminating the Master Lease Agreement to which such Event of Default relates, repossess the leased property and relet the leased property with the Company remaining liable under such Master Lease Agreement for all obligations to be performed by the Company thereunder, including the difference, if any, between the rent under such Master Lease Agreement and the rent payable as a result of the reletting of the leased property, and

(3) seek any and all other rights and remedies available under law or in equity.

In addition to the remedies noted above, under the Master Lease Agreements, in the case of a facility-specific event of default, Ventas may terminate a Master Lease Agreement as to the leased property to which the Event of Default relates, and may, but need not, terminate the entire Master Lease Agreement. Each of the Master Lease Agreements includes special rules relative to Medicare/Medicaid events of default and licensed bed events of default. In the event a Medicare/Medicaid event of default and/or a licensed bed event of default occurs and is continuing (a) with respect to not more than two properties at the same time under a Master Lease Agreement that covers 41 or more properties and (b) with respect to not more than one property at the same time under a Master Lease Agreement that covers 21 to and including 40 properties, Ventas may not exercise termination or dispossession remedies against any property other than the property or properties to which the event of default relates. Thus, in the event Medicare/Medicaid events of default and licensed bed events of default would occur and be continuing (a) with respect to one property under a Master Lease Agreement that covers less than 20 properties, (b) with respect to two or more properties at the same time under a Master Lease Agreement that covers 21 to and including 40 properties, or (c) with respect to three or more properties at the same time under a Master Lease Agreement that covers 41 or more properties, then Ventas would be entitled to exercise all rights and remedies available to it under the Master Lease Agreements.

Assignment and Subletting

Except as noted below, the Master Lease Agreements provide that the Company may not assign, sublease or otherwise transfer any leased property or any portion of a leased property as a whole (or in substantial part), including by virtue of a change of control, without the consent of Ventas, which may not be unreasonably withheld if the proposed assignee (1) is a creditworthy entity with sufficient financial stability to satisfy its obligations under the related Master Lease Agreement, (2) has not less than four years experience in operating healthcare facilities, (3) has a favorable business and operational reputation and character and (4) has all licenses, permits, approvals and authorizations to operate the facility and agrees to comply with the use restrictions in the related Master Lease Agreement. The obligation of Ventas to consent to a subletting or assignment is subject to the reasonable approval rights of any mortgagee and/or the lenders under its credit agreement. The Company may sublease up to 20% of each leased property for restaurants, gift shops and other stores or services customarily found in hospitals or nursing centers without the consent of Ventas, subject, however, to there being no material alteration in the character of the leased property or in the nature of the business conducted on such leased property.

In addition, each Master Lease Agreement allows the Company to assign or sublease (a) without the consent of Ventas, 10% of the nursing center facilities in each Master Lease Agreement and (b) with Ventas' consent (which consent will not be unreasonably withheld, delayed or conditioned), two hospitals in each Master Lease Agreement, if either (i) the applicable regulatory authorities have threatened to revoke an authorization necessary to operate such leased property or (ii) the Company cannot profitably operate such leased property. Any such proposed assignee/sublessee must satisfy the requirements listed above and it must have all licenses, permits, approvals and other authorizations required to operate the leased properties in accordance with the applicable permitted use. With respect to any assignment or sublease made under this provision, Ventas agrees to execute a nondisturbance and attornment agreement with such proposed assignee or subtenant. Upon any assignment or subletting, the Company will not be released from its obligations under the applicable Master Lease Agreement.

Subject to certain exclusions, the Company must pay to Ventas 80% of any consideration received by the Company on account of an assignment and 80% (50% in the case of existing subleases) of sublease rent payments (roughly equal to revenue net of specified allowed expenses attributable to a sublease, and specifically defined in the Master Lease Agreements), provided that Ventas' right to such payments will be subordinate to that of the Company's lenders.

Ventas will have the right to approve the purchaser at a foreclosure of one or more of the Company's leasehold mortgages by the Company's lenders. Such approval will not be unreasonably withheld so long as such purchaser is creditworthy, reputable and has four years experience in operating healthcare facilities. Any dispute regarding whether Ventas has unreasonably withheld its consent to such purchaser will be subject to expedited arbitration.

Under the Master Lease Agreements, Ventas has a right to sever properties from the existing leases in order to create additional leases, a device adopted to facilitate its financing flexibility. In such circumstances, the Company's aggregate lease obligations remain unchanged. Ventas exercised this severance right with respect to Master Lease Agreement No. 1 to create a new lease of 40 nursing centers (the "CMBS Lease") and mortgaged these properties in connection with a securitized mortgage financing. The CMBS Lease is in substantially the same form as the other Master Lease Agreements with certain modifications requested by Ventas' lender and required to be made by the Company pursuant to the Master Lease Agreements. The transaction closed on December 12, 2001.

Spin-off Agreements and Other Arrangements Under the Plan of Reorganization

In order to govern certain of the relationships between the Company and Ventas after the Spin-off and to provide mechanisms for an orderly transition, the Company and Ventas entered into the Spin-off Agreements. Except as noted below, the following agreements between Ventas and the Company were assumed by the Company and certain of these agreements were simultaneously amended in accordance with the terms of the Plan of Reorganization.

Tax Allocation Agreement and Tax Refund Escrow Agreement

The Tax Allocation Agreement, entered into at the time of the Spin-off, was assumed by the Company under the Plan of Reorganization and then amended and supplemented by the Tax Refund Escrow Agreement (as defined below). Both of these agreements are described below.

The Tax Allocation Agreement provides that the Company will be liable for, and will hold Ventas harmless from and against, (1) any taxes of the Company and its then subsidiaries (the "Kindred Group") for periods after the Spin-off, (2) any taxes of Ventas and its then subsidiaries (the "Ventas Group") or the Kindred Group for periods prior to the Spin-off (other than taxes associated with the Spin-off) with respect to the portion of such taxes attributable to assets owned by the Kindred Group immediately after completion of the Spin-off and (3) any taxes attributable to the Spin-off to the extent that the Company derives certain tax benefits as a result of the payment of such taxes. Under the Tax Allocation Agreement, the Company would be entitled to any refund or credit in respect of taxes owed or paid by the Company under (1), (2) or (3) above. The Company's liability for taxes for purposes of the Tax Allocation Agreement would be measured by Ventas' actual liability for taxes after applying certain tax benefits otherwise available to Ventas other than tax benefits that Ventas in good faith determines would actually offset tax liabilities of Ventas in other taxable years or periods. Any right to a refund for purposes of the Tax Allocation Agreement would be measured by the actual refund or credit attributable to the adjustment without regard to offsetting tax attributes of Ventas.

Under the Tax Allocation Agreement, Ventas would be liable for, and would hold the Company harmless against, any taxes imposed on the Ventas Group or the Kindred Group other than taxes for which the Kindred Group is liable as described in the above paragraph. Ventas would be entitled to any refund or credit for taxes owed or paid by Ventas as described in this paragraph. Ventas' liability for taxes for purposes of the Tax

Allocation Agreement would be measured by the Kindred Group's actual liability for taxes after applying certain tax benefits otherwise available to the Kindred Group other than tax benefits that the Kindred Group in good faith determines would actually offset tax liabilities of the Kindred Group in other taxable years or periods. Any right to a refund would be measured by the actual refund or credit attributable to the adjustment without regard to offsetting tax attributes of the Kindred Group.

On the Effective Date, Ventas and the Company entered into the Tax Refund Escrow Agreement and First Amendment to the Tax Allocation Agreement (the "Tax Refund Escrow Agreement") governing their relative entitlement to certain tax refunds received on or after September 13, 1999 by Ventas or the Company for the tax periods prior to and including the Spin-off that each has received or may receive in the future. The Tax Refund Escrow Agreement amends and supplements the Tax Allocation Agreement. Under the terms of the Tax Refund Escrow Agreement, refunds ("Subject Refunds") received on or after September 13, 1999 by either Ventas or the Company with respect to federal, state or local income, gross receipts, windfall profits, transfer, duty, value-added, property, franchise, license, excise, sales and use, capital, employment, withholding, payroll, occupational or similar business taxes (including interest, penalties and additions to tax, but excluding certain refunds), for taxable periods ending on or prior to May 1, 1998 ("Subject Taxes") were deposited into an escrow account with a third-party escrow agent on the Effective Date.

The Tax Refund Escrow Agreement provides that each party shall notify the other of any asserted Subject Tax liability of which it becomes aware, that either party may request that asserted liabilities for Subject Taxes be contested, that neither party may settle such a contest without the consent of the other, that each party shall have a right to participate in any such contest, and that the parties generally shall cooperate with regard to Subject Taxes and Subject Refunds and shall mutually and jointly control any audit or review process related thereto. The funds in the escrow account (the "Escrow Funds") may be released from the escrow account to pay Subject Taxes and as otherwise provided therein.

The Tax Refund Escrow Agreement provides generally that Ventas and the Company waive their respective rights under the Tax Allocation Agreement to make claims against each other with respect to Subject Taxes satisfied by the Escrow Funds, notwithstanding the indemnification provisions of the Tax Allocation Agreement. To the extent that the Escrow Funds are insufficient to satisfy all liabilities for Subject Taxes that are finally determined to be due (such excess amount, "Excess Taxes"), the relative liability of Ventas and the Company to pay such Excess Taxes shall be determined as provided in the Tax Refund Escrow Agreement. Disputes under the Tax Refund Escrow Agreement, and the determination of the relative liability of Ventas and the Company to pay Excess Taxes, if any, are governed by the arbitration provision of the Tax

Allocation Agreement.

Interest earned on the Escrow Funds or included in refund amounts received from governmental authorities will be distributed equally to each of Ventas and the Company on an annual basis. For the year ended December 31, 2001, the Company has recorded approximately $368,000 of interest income related to the Escrow Funds. Any Escrow Funds remaining in the escrow account after no further claims may be made by governmental authorities with respect to Subject Taxes or Subject Refunds (because of the expiration of statutes of limitation or otherwise) will be distributed equally between Ventas and the Company.

Agreement of Indemnity-Third Party Leases

In connection with the Spin-off, Ventas assigned its former third-party lease obligations (i.e., leases under which an unrelated third party is the landlord) as a tenant or as a guarantor of tenant to the Company (the "Third Party Leases"). The lessors of these properties may claim that Ventas remains liable on the Third Party Leases assigned to the Company. Under the terms of the Agreement of Indemnity-Third Party Leases, the Company has agreed to indemnify and hold Ventas harmless from and against all claims against Ventas arising out of the Third Party Leases. Under the Plan of Reorganization, the Company assumed and agreed to fulfill its obligations under the Agreement of Indemnity-Third Party Leases.

Agreement of Indemnity-Third Party Contracts

In connection with the Spin-off, Ventas assigned its former third-party guaranty agreements to the Company (the "Third Party Guarantees"). Ventas may remain liable on the Third Party Guarantees assigned to the Company. Under the terms of the Agreement of Indemnity-Third Party Contracts, the Company has agreed to indemnify and hold Ventas harmless from and against all claims against Ventas arising out of the Third Party Guarantees assigned to the Company. The Third Party Guarantees were entered into in connection with certain acquisitions and financing transactions that occurred prior to the Spin-off. Under the Plan of Reorganization, the Company assumed and agreed to fulfill its obligations under the Agreement of Indemnity-Third Party Contracts.

Assumption of Other Liabilities

In connection with the Spin-off, the Company agreed to assume and to indemnify Ventas for any and all liabilities that may arise out of the ownership or operation of the healthcare operations either before or after the date of the Spin-off. The indemnification provided by the Company also covers losses, including costs and expenses, which may arise from any future claims asserted against Ventas based on these healthcare operations. In addition, at the time of the Spin-off, the Company agreed to assume the defense, on behalf of Ventas, of any claims that were pending at the time of the Spin-off, and which arose out of the ownership or operation of the healthcare operations. The Company also agreed to defend, on behalf of Ventas, any claims asserted after the Spin-off which arise out of the ownership and operation of the healthcare operations. Under the Plan of Reorganization, the Company assumed and agreed to perform its obligations under these indemnifications.

In connection with the Spin-off, the Company and Ventas entered into a Development Agreement and a Participation Agreement. Under the terms of the Development Agreement, the Company agreed that upon completion of each development property, Ventas would have the option to purchase the development property from the Company at a purchase price equal to the amount of the

Company's actual costs in acquiring, developing and improving such development property prior to the purchase date. If Ventas purchased the development property, the Company would lease the development property from Ventas. The annual base rent under such a lease would have been ten percent of the actual costs incurred by the Company in acquiring and developing the development property. The other terms of the lease for the development property would have been substantially similar to those set forth in the original master lease agreements.

Under the terms of the Participation Agreement, the Company had a right of first offer to become the lessee of any real property acquired or developed by Ventas which was to be operated as a hospital, nursing center or other healthcare facility, provided that the Company and Ventas negotiated a mutually satisfactory lease arrangement. The Participation Agreement also provided, subject to certain terms, that the Company would provide Ventas with a right of first offer to purchase or finance any healthcare related real property that the Company determined to sell or mortgage to a third party, provided that the Company and Ventas negotiated mutually satisfactory terms for such purchase or mortgage.

The Participation Agreement and the Development Agreement were terminated on the Effective Date. The Company and Ventas are deemed to have waived any and all damages, claims, liabilities, obligations, and causes of action related to or arising out of these agreements.

Terminated Arrangements with Ventas

The Company and Ventas also entered into certain agreements, stipulations and orders both prior to and during the pendency of the Company's bankruptcy proceedings governing certain aspects of the business relationships between the Company and Ventas prior to the Effective Date. In March 1999, the Company served Ventas with a demand for mediation seeking a reduction in rent and other concessions under its former master lease agreements with Ventas. Shortly thereafter, the Company and Ventas entered into a series of standstill and tolling agreements which provided that both companies would postpone any claims either may have against the

other and extend any applicable statutes of limitation. As a result of the Company's failure to pay rent, Ventas served the Company with notices of nonpayment under the original master lease agreements. Subsequently, the Company and Ventas entered into further amendments to the second standstill and the tolling agreements to extend the time during which no remedies may be pursued by either party and to extend the date by which the Company may cure its failure to pay rent.

In connection with the bankruptcy, the Company and Ventas entered into a stipulation (the "Stipulation") that provided for the payment by the Company of a reduced aggregate monthly rent of approximately $15.1 million. The bankruptcy court approved the Stipulation. The Stipulation also continued to toll any statutes of limitations for claims that might have been asserted by the Company against Ventas and provided that the Company would continue to fulfill its indemnification obligations arising from the Spin-off. The Stipulation automatically renewed for one-month periods unless either party provided a 14-day notice of termination.

In May 2000, the bankruptcy court approved a tax stipulation agreement between the Company and Ventas (the "Tax Stipulation"). The Tax Stipulation provided that certain refunds of federal, state and local taxes received by either party on or after September 13, 1999 would be held by the recipient of such refunds in segregated interest bearing accounts. The Tax Stipulation required notification before either party could withdraw funds from the segregated accounts.

The Stipulation and Tax Stipulation were each terminated on the Effective Date and are of no further force or effect.

Other Related Party Transactions

In connection with the Spin-off, the Company issued 17,700 shares of its former preferred stock to Ventas as part of the consideration for the assets transferred from Ventas to the Company. On April 30, 1998, Ventas offered and sold the preferred stock at $1,000 per share to certain officers of the Company for an aggregate consideration of $17.7 million. The following executive officers purchased the number of shares of the former preferred stock indicated: Mr. Frank J. Battafarano, President, Hospital Division--330 shares; Mr. Richard E. Chapman, Chief Administrative and Information Officer and Senior Vice President--360 shares; Mr. James H. Gillenwater, Jr., Senior Vice President, Planning and Development--510 shares; Mr. Richard A. Lechleiter, Vice President, Finance, Corporate Controller and Treasurer--350 shares; and Ms. M. Suzanne Riedman, Senior Vice President and General Counsel--315 shares. After April 30, 2002, each share of the former preferred stock was to be convertible, at the option of the holder, in whole or in part, into such number of shares of the Company's former common stock as was equal to the aggregate principal amount of the shares of the former preferred stock being converted divided by the conversion price. The conversion price was $12.50, which was equal to 118% of the average of the high and low sales price of the former common stock immediately following the Spin-off.

In connection with the purchases of the former preferred stock, the Company loaned certain officers, including certain Named Executive Officers, 90% of the purchase price of the former preferred stock (the "Preferred Stock Loans"). Each Preferred Stock Loan was evidenced by a promissory note, which had a ten-year term and bore interest at 5.74%, payable annually. No principal payments were due under the promissory notes until their maturity. The promissory notes were secured by a first priority security interest in the former preferred stock purchased by each such officer. The following executive officers were loaned the indicated amounts: Mr. Battafarano--$297,000; Mr. Chapman--$324,000; Mr. Gillenwater--$459,000; Mr. Lechleiter--$315,000; and Ms. Riedman--$283,500.

In August 1999, the Company entered into agreements with certain officers, including certain Named Executive Officers, which permitted each officer to put the former preferred stock to the Company for an amount equal to the outstanding principal and interest on the officer's Preferred Stock Loan ("Preferred Stock Agreements"). The officer could put the former preferred stock to the Company after January 1, 2000. During the pendency of the Company's bankruptcy, the Company could not honor the terms of the Preferred Stock Agreements. The Preferred Stock Agreements were entered into with each officer employed by the Company in

August 1999 who owned the former preferred stock, including Mr. Battafarano, Mr. Chapman, Mr. Gillenwater, Mr. Lechleiter and Ms. Riedman.

Under the terms of the Plan of Reorganization, the Preferred Stock Agreements were canceled in exchange for the cancellation of the Preferred Stock Loans. In addition, the former preferred stock was canceled without any consideration.

PERFORMANCE GRAPH

The following graph summarizes the cumulative total return to stockholders of the Company's Common Stock from April 26, 2001, the first day of its trading on the OTC Bulletin Board to December 31, 2001, compared to the cumulative total return on the Standard & Poor's 500 Stock Index ("S&P 500 Index") and the Standard & Poor's Super Health Care Facilities Index (the "S&P Super Health Care Facilities Index"). The graph assumes an investment of $100 in each of the Company's Common Stock, the S&P 500 Index, and the S&P Super Health Care Facilities Index on April 26, 2001, and also assumes the reinvestment of all dividends.

[CHART]

	Kindred Healthcare, Inc.	S&P 500	S&P Super Health Care Facilities Index
4/26/01	$100	$100	$100
12/31/01	168	94	103

	4/26/01	12/31/01
Kindred Healthcare, Inc.	$100	$168
S&P 500 Index	100	94
S&P Super Health Care Facilities Index	100	103

PROPOSALS 2 THROUGH 5

The next four proposals relate to compensation and incentive plans with respect to which the Company is seeking the approval of its shareholders. As outlined in the "Report of the Executive Compensation Committee" set forth above, the Company currently maintains two performance-based cash plans and three equity incentive plans.

The two cash plans are a short-term (annual) incentive plan in which employees are eligible to receive cash bonuses based on corporate performance and their individual performance over a one-year period, and a long-term incentive plan in which corporate performance is measured over a one-year period but awards are paid over three years from the end of that performance period. Taken together, these plans provide a combination of short-term and long-term cash incentives to encourage employees on an ongoing basis to contribute to the success of

the Company and to remain in the Company's employ. The long-term incentive plan was approved during the Company's reorganization process. The Company is seeking shareholder approval or ratification of both plans.

The three equity plans are the Restricted Share Plan, the 2000 Stock Option

Plan, and the 2001 Stock Option Plan. The Company adopted the Restricted Share Plan and the 2000 Stock Option Plan during its reorganization to provide incentives for key employees to assist in its emergence from bankruptcy and to remain in the Company's employ, by participating in the reallocation of equity upon emergence from bankruptcy. Both of these plans were approved during the reorganization process, and, consistent with the purposes of these plans, options and restricted shares were granted shortly after the Company emerged from bankruptcy. Substantially all of the shares of Common Stock available for grant under these plans were awarded.

The Company adopted the 2001 Stock Option Plan (the "2001 Option Plan") shortly after it emerged from bankruptcy. The 2001 Option Plan was intended to be a program of stock option grants for a broad group of employees, recognizing that equity incentives tie the incentives of employees most directly to the value realized by shareholders. The 2001 Option Plan is being restated and submitted for approval as the 2001 Stock Incentive Plan, an equity plan that provides for, in addition to stock options, other types of incentive awards, including stock appreciation rights, performance units, restricted stock and stock bonuses. The Board of Directors believes that this flexible program of equity incentives is needed to allow the Board and senior management to attract and retain quality employees.

The Board of Directors and the Executive Compensation Committee believe that these incentive plans create a compensation program that is well-designed to provide a full range of incentives that will attract new employees, retain existing employees, and tie incentive compensation directly to the Company's growth and shareholder returns.

2. PROPOSAL TO RATIFY THE KINDRED HEALTHCARE, INC. 2000 STOCK OPTION PLAN

The Kindred Healthcare, Inc. 2000 Stock Option Plan (the "2000 Option Plan") was established on September 26, 2000 (originally as the Vencor 2000 Stock Option Plan) to promote the interests of the Company and its shareholders by providing key employees and consultants of the Company and its affiliates, including the Named Executive Officers, with an appropriate incentive to continue in the employ of the Company or its affiliates and to improve the growth and profitability of the Company. The 2000 Option Plan provides for the grant to key employees of the Company of non-qualified and incentive stock options (collectively, "2000 Options"). The 2000 Option Plan was approved in the Plan of Reorganization, and the Company submits it now to the Company's current shareholders for ratification.

The following summary of the 2000 Option Plan is qualified in its entirety by the specific language of the 2000 Option Plan, which is attached as Appendix B.

Awards

The maximum number of shares of Common Stock of the Company that may be issued under the 2000 Option Plan is 600,000 shares. Shares of Common Stock issued under the 2000 Option Plan may be either newly issued shares or treasury shares.

The 2000 Option Plan is administered by the Executive Compensation Committee or such other committee as the Board of Directors shall appoint from time to time. The Chief Executive Officer of the Company recommends the key employees of the Company who may be granted 2000 Options (as defined below), the number of 2000 Options to be granted and the type of grant, all subject to approval by the Executive Compensation Committee. Approximately 600 employees are eligible to participate in the 2000 Option Plan.

2000 Options generally become exercisable over a period of three years, with one-third becoming exercisable on each of the first, second and third anniversaries of the date of grant, unless otherwise determined by the Executive Compensation Committee and set forth in the option agreement governing the award.

Each 2000 Option will entitle the holder to purchase a specified number of shares of Common Stock. No participant may be granted a 2000 Option to purchase more than 150,000 shares of Common Stock in any calendar year. The exercise price of each 2000 Option will be determined by the Executive Compensation Committee on the date of grant of such 2000 Option. The exercise price will be paid in cash or in shares of Common Stock valued at their fair market value on the date of exercise in accordance with the terms of the 2000 Option Plan. Each 2000 Option will be exercisable for a term of five years.

Benefits

Set forth below is a table showing the number of shares subject to 2000 Options granted during fiscal year 2001 to the Named Executive Officers and certain other individuals under the 2000 Option Plan. The closing trading price of the Common Stock as reported on the NASDAQ on March 7, 2002 was $39.03 per share. Because the 2000 Options granted under the 2000 Option Plan are discretionary, no data can be provided regarding planned grants.

2000 Option Plan

Name and Position	Number o
Edward L. Kuntz, Chairman of the Board and Chief Executive Officer	135,
Richard A. Schweinhart, Senior Vice President and Chief Financial Officer	38,
Donald D. Finney, President, Health Services Division	38,
Frank J. Battafarano, President, Hospital Division	33,
Richard E. Chapman, Chief Administrative and Information Officer and Senior Vice President	38,
All current executive officers as a group	382,
All employees, including all current officers who are not executive officers, as a group	210,

Termination of Employment

In the event that the employment of a participant terminates (1) for any reason other than Disability, Cause (as such terms are defined in the 2000 Option Plan) or death, 2000 Options granted to such participant, to the extent that they were exercisable at the time of termination, will remain exercisable for ninety days after such termination, and those not exercisable at such time will expire at such time; (2) on account of the Disability or death of the participant, such participant or his designated beneficiary, respectively, will be entitled to exercise, until the first anniversary of such termination, 2000 Options which were exercisable at the time of such termination, and all other 2000 Options will expire at such time; and (3) for Cause, all outstanding 2000 Options granted to such participant will expire at the commencement of business on the date of such termination. However, no 2000 Option may be exercised after the expiration of its term.

Company Change in Control

Upon the occurrence of a Change in Control of the Company (as defined in the 2000 Option Plan), each 2000 Option granted under the 2000 Option Plan and outstanding at such time will become fully and immediately exercisable.

General Plan Provisions

In the event that any outstanding 2000 Option expires, terminates or is canceled for any reason, the shares of Common Stock subject to the unexercised portion of such 2000 Option will again be available for award pursuant to the 2000 Option Plan.

The 2000 Option Plan provides for an adjustment in the number of shares of Common Stock available to be issued under the 2000 Option Plan, upon a change in the capitalization of the Company, a stock dividend or split, a merger or combination of shares and certain other similar events.

During the lifetime of a participant, each 2000 Option granted to a participant is exercisable only by the participant. No Option is transferable or assignable other than by will or the laws of descent and distribution.

Amendment or Termination of the 2000 Option Plan

With certain exceptions, the Board of Directors of the Company may amend the provisions of the 2000 Option Plan at any time and from time to time.

Principal Federal Income Tax Consequences of the 2000 Option Plan to Participants and the Company

The following is a summary of the principal United States federal income tax consequences generally applicable to the Company and to participants of the grant and exercise of incentive stock options ("ISOs") and non-qualified stock options ("NQSOs") under the 2000 Option Plan under the now applicable provisions of the Code and the regulations thereunder.

Incentive Stock Options. A participant is not deemed to have received taxable income upon grant or exercise of any ISO so long as the participant does not dispose of the shares received upon exercise within one year after the date of exercise and two years after the date of grant (the "ISO Holding Period"). Upon exercise of an ISO, the spread between the fair market value of the shares received and the exercise price will be an item of adjustment for purposes of the alternative minimum tax, unless the participant disposes of the shares in the same tax year as the ISO is exercised. If a participant does dispose of such shares within the ISO Holding Period (such disposition, a "Disqualifying Disposition"), any gain on such Disqualifying Disposition, up to the amount of the spread on exercise, will be ordinary income, with the balance being capital gain. All other gains upon dispositions of shares received upon exercise of an ISO will be capital gains in amounts equal to the excess of the proceeds received over the exercise price.

If the participant surrenders previously-owned shares acquired upon the exercise of an ISO which have not satisfied the ISO Holding Period in payment of any or all of the exercise price of an ISO, such surrender is a Disqualifying Disposition of the surrendered shares that will result in the recognition of ordinary income (although not of capital gain) as described in the immediately preceding paragraph. The number of shares received upon exercise of the ISO equal in number to the previously-owned shares so surrendered would have the tax basis, increased by the amount of ordinary income recognized upon the Disqualifying Disposition, and capital gain holding period applicable to such surrendered shares. The additional shares received upon exercise of the ISO would have a tax basis equal to the cash paid on exercise (if any) and a new capital gain holding period commencing on the date following the date of exercise. The ISO Holding Period with respect to all the shares acquired pursuant to the ISO would start on the date of exercise.

If the participant surrenders previously-owned shares (other than any shares acquired upon the exercise of an ISO which have not satisfied the ISO Holding Period) in payment of any or all of the exercise price of an ISO, the shares received upon exercise of the ISO equal in number to the previously-owned shares so surrendered would have the tax basis and capital gain holding period applicable to such surrendered shares. The additional shares received upon exercise of the ISO would have a tax basis equal to the cash paid on exercise (if any) and a new capital gain holding period commencing on the date following the date of exercise. The ISO Holding Period with respect to all the shares acquired pursuant to the ISO would start on the date of exercise.

Non-Qualified Stock Options. A participant is not taxed upon grant of a non-qualified stock option (an "NQSO"). A participant will have ordinary income upon exercise of an NQSO in an amount equal to the excess of the fair market value on the date of exercise of the shares purchased over the exercise price paid upon exercise.

If the participant surrenders previously-owned shares in payment of any or all of the exercise price of an NQSO, the shares received upon exercise of such NQSO equal in number to the previously-owned shares so surrendered would have the tax basis and capital gain holding period applicable to such surrendered shares. The additional shares received upon exercise would have a tax basis equal to the amount taxable as ordinary income upon such exercise (as described in the immediately preceding paragraph) plus the cash paid on exercise (if any) and a new capital gain holding period commencing on the date following the date of exercise.

In addition, according to proposed regulations issued by the U.S. Treasury Department, the surrender of previously-owned shares or shares acquired upon the exercise of an ISO which have not satisfied the ISO Holding Period in payment of any or all of the exercise price of an NQSO would not be a Disqualifying Disposition of the surrendered shares that would result in the recognition of ordinary income. Rather, if the participant surrenders previously-owned shares acquired upon the exercise of an ISO in payment of any or all of the exercise price of an NQSO, a number of shares received upon exercise of the NQSO equal to the number of previously-owned shares surrendered would be treated as shares received upon the exercise of the ISO and only the additional shares received upon exercise of the NQSO would be treated as such.

Tax Consequences to the Company. The Company or an affiliate that employs a participant generally will be entitled to a federal income tax deduction in an amount equal to the amount of compensation income, taxable as ordinary income, recognized by the participant as a result of the exercise of an option in the year of recognition by the participant.

The Board of Directors recommends a vote "FOR" Proposal No. 2.

3. PROPOSAL TO APPROVE THE KINDRED HEALTHCARE, INC. 2001 STOCK INCENTIVE PLAN

As described above, the Board of Directors has determined that it is in the Company's best interest to adopt a flexible program of equity incentive awards in order to allow the Board of Directors and senior management to address