

NATIONAL HEALTHCARE CORP

Form S-4/A

July 10, 2007

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**As filed with the Securities and Exchange Commission on July 10, 2007**

**Registration No. 333-142189**

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

**AMENDMENT NO. 2**

**FORM S-4  
REGISTRATION STATEMENT UNDER THE SECURITIES ACT OF 1933**

**NATIONAL HEALTHCARE CORPORATION**  
*(Exact name of registrant as specified in its charter)*

**Delaware**

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

**8051**

*(Primary Standard Industrial  
Classification Code Number)*

**52-2057472**

*(I.R.S. Employer  
Identification Number)*

**100 Vine Street, Suite 1400  
Murfreesboro, Tennessee 37130  
(615) 890-2020**

*(Address, including zip code, and telephone number, including area code, of registrant's principal executive offices)*

**Robert G. Adams  
President and Chief Executive Officer  
National HealthCare Corporation  
100 Vine Street, Suite 1400  
Murfreesboro, Tennessee 37130  
(615) 890-2020**

*(Name, address, including zip code, and telephone number, including area code, of agent for service)*

***Copies to:***

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**Approximate date of commencement of proposed sale to the public:** As soon as practicable after the date hereof.

If the securities being registered on this Form are being offered in connection with the formation of a holding company and there is compliance with General Instruction G, check the following box.

If this Form is filed to register additional securities for an offering pursuant to Rule 462(b) under the Securities Act, check the following box and list the Securities Act registration statement number of the earlier effective registration statement for the same offering.

If this Form is a post-effective amendment filed pursuant to Rule 462(d) under the Securities Act, check the following box and list the Securities Act registration statement number of the earlier effective registration statement for the same offering.

**The Registrant hereby amends this Registration Statement on such date or dates as may be necessary to delay its effective date until the Registrant shall file a further amendment which specifically states that this Registration Statement shall thereafter become effective in accordance with Section 8(a) of the Securities Act of 1933, as amended, or until the Registration Statement shall become effective on such date as the Commission, acting pursuant to Section 8(a), may determine.**

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The information in this prospectus is not complete and may be changed. These securities may not be sold until the registration statement filed with the Securities and Exchange Commission is effective. This prospectus is not an offer to sell these securities and it is not soliciting an offer to buy these securities in any state where the offer or sale is not permitted.

**SUBJECT TO COMPLETION, DATED JULY 10, 2007**

**National Health Realty, Inc.  
100 Vine Street, Suite 1402  
Murfreesboro, Tennessee 37130**

**National HealthCare Corporation  
100 Vine Street, Suite 1400  
Murfreesboro, Tennessee 37130**

**A MERGER PROPOSAL YOUR VOTE IS VERY IMPORTANT**

To the stockholders of National Health Realty, Inc. and National HealthCare Corporation:

On December 20, 2006, Davis Acquisition Sub LLC (an indirect wholly-owned subsidiary of National HealthCare Corporation), NHC/OP, L.P. (a direct and indirect wholly-owned subsidiary of National HealthCare Corporation), National HealthCare Corporation (NHC), and National Health Realty, Inc. (NHR), entered into an Agreement and Plan of Merger. Pursuant to the merger agreement and following stockholder approval on \_\_\_\_\_, 2007, NHR completed a consolidation with its wholly-owned subsidiary, NEW NHR, Inc., which resulted in the formation of a new Maryland corporation (the Consolidated Company). As used in this joint proxy statement/prospectus, references to NHR mean, with respect to periods prior to \_\_\_\_\_, 2007, National Health Realty, Inc., and with respect to periods after \_\_\_\_\_, 2007, the Consolidated Company.

Subject to stockholder approval as described herein and consummation of certain other transactions specified in the merger agreement, NHR will be merged with and into Davis Acquisition Sub LLC, and Davis Acquisition Sub LLC will continue as a wholly-owned subsidiary of NHC/OP, L.P. and shall succeed to and assume all the rights and obligations of NHR.

Pursuant to the merger agreement, each outstanding common share of NHR not owned by Davis Acquisition Sub LLC, NHC/OP, L.P. or NHC will be converted into the right to receive one share of NHC Series A Convertible Preferred Stock (the Preferred Stock), plus \$9.00 in cash. In addition, immediately prior to the consummation of the merger, NHR will declare a special dividend payable to each holder of record of NHR common stock who shall receive the merger consideration at the effective time of the merger in an amount equal to the dividend that NHR would have declared and paid in the ordinary course of business in order to qualify as a REIT for the taxable year commencing on January 1, 2007 and ending on the effective date of the merger if NHR had not entered into the merger agreement. Each share of the Preferred Stock will be entitled to cumulative annual preferred dividends of \$0.80 per share and will have a liquidation preference of \$15.75 per share. The Preferred Stock will be listed on the American Stock Exchange and will be convertible at any time at the option of the holder into 0.24204 shares of NHC common stock, subject to adjustment.

NHC will hold a special meeting of stockholders on \_\_\_\_\_, 2007 at \_\_\_\_\_ a.m., Central time, at the principal executive offices of NHC, located at 100 Vine Street, Suite 1400, Murfreesboro, Tennessee 37130. At this meeting, stockholders of NHC will be asked (1) to consider and vote upon a proposal to adopt an amendment to the certificate of incorporation of NHC to increase the maximum number of shares of undesignated preferred stock having a par value of \$.01 per share from 10,000,000 shares to 25,000,000 shares, (2) to consider and vote upon a proposal to approve

the issuance of Series A Convertible Preferred Stock having a par value of \$.01 per share, pursuant to the merger agreement ((1) and (2) collectively, the NHC Proposal ), (3) to approve the postponement or adjournment of the NHC special meeting for the solicitation of additional votes, if necessary, and (4) to transact any other business as may properly come before the NHC special meeting or any adjournment or postponement of the NHC special meeting.

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The affirmative vote of the holders of a majority of common shares outstanding and entitled to vote at the NHC special meeting is required to approve the amendment of the NHC certificate of incorporation. The affirmative vote of the holders of a majority of the outstanding common shares represented and voting at the NHC special meeting is required to approve the issuance of the Preferred Stock.

NHR will hold a special meeting of stockholders on \_\_\_\_\_, 2007 at \_\_\_\_\_ a.m., Central time, at the principal executive offices of NHR, located at 100 Vine Street, Suite 1402, Murfreesboro, Tennessee 37130. At this meeting, stockholders of NHR will be asked (1) to consider and vote upon the approval of the merger (the NHR Proposal), (2) to approve the postponement or adjournment of the NHR special meeting for the solicitation of additional votes, if necessary, and (3) to transact any other business as may properly come before the NHR special meeting or any adjournment or postponement of the NHR special meeting.

The affirmative vote of the holders of a majority of common shares outstanding and entitled to vote at the NHR special meeting and the affirmative vote of the holders of a majority of the common stock outstanding and entitled to vote, not owned by a director or officer of NHR, or any affiliate of NHR or NHC is required to approve the merger.

Before the merger can be completed, holders of the requisite number of outstanding shares of NHC common stock must vote in favor of the NHC Proposal at the NHC special meeting and holders of the requisite number of outstanding shares of NHR common stock must vote in favor of the NHR Proposal.

Holders of NHC common stock representing approximately 21.9% of the outstanding shares of NHC common stock as of March 1, 2007 have agreed to vote the shares of NHC common stock owned by them in favor of the NHC Proposal. NHR stockholders representing approximately 22.4% of the outstanding shares of NHR common stock as of March 1, 2007 have agreed to vote the shares of NHR common stock owned by them in favor of the NHR Proposal.

The merger agreement and the merger have been approved and declared advisable by (i) the sole managing member of Davis Acquisition Sub LLC, (ii) the general partner of NHC/OP, L.P., (iii) the board of directors of NHC, upon the unanimous recommendation of a special committee of its board of directors composed entirely of independent directors, and (iv) the board of directors of NHR, upon the unanimous recommendation of a special committee of its board of directors composed entirely of independent directors. Completion of the merger, which is expected to occur in the second quarter of 2007, is subject to the approval of certain matters by the requisite stockholders of NHC and NHR.

NHC's common shares are traded on the American Stock Exchange under the symbol NHC, and the closing price of NHC's common shares on \_\_\_\_\_, 2007 was \$ \_\_\_\_\_ per share. NHR's common stock is traded on the American Stock Exchange under the symbol NHR and the closing price of a share of NHR common stock on \_\_\_\_\_, 2007 was \$ \_\_\_\_\_ per share.

**The board of directors of NHC has approved the merger agreement and the merger and has determined that the merger is in the best interest of NHC's stockholders. The board of directors of NHC recommends that NHC's stockholders vote FOR the NHC Proposal.**

**The board of directors of NHR has approved the merger agreement and the merger and has determined that the merger is advisable and in the best interest of NHR stockholders. The board of directors recommends that NHR stockholders vote FOR the NHR Proposal.**

This joint proxy statement/prospectus provides NHC stockholders and NHR stockholders with detailed information about the special meetings and the proposed merger. You can also obtain information from publicly available documents filed by NHC and NHR with the Securities and Exchange Commission. **NHC and NHR encourage you**

**to read this entire document carefully, including the section entitled Risk Factors beginning on page 47.**

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Your vote is very important. Whether or not you plan to attend the NHC special meeting or the NHR special meeting, please take time to vote on the proposal by completing and mailing the enclosed proxy card.

Sincerely,

Donald K. Daniel  
*Senior Vice President & Controller*  
*Principal Accounting Officer*  
*National Health Realty, Inc.*

Robert G. Adams  
*President and Chief Executive Officer*  
*National HealthCare Corporation*

**Neither the Securities and Exchange Commission nor any state securities commission has approved or disapproved of the securities to be issued in connection with the merger approved or disapproved of the transaction, passed upon the merits or fairness of the transaction or determined if this joint proxy statement/prospectus is adequate, accurate or complete. Any representation to the contrary is a criminal offense.**

This joint proxy statement/prospectus is dated  
and is first being mailed to stockholders on or about



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**SOURCES OF ADDITIONAL INFORMATION**

**This joint proxy statement/prospectus includes information also set forth in documents filed by NHC and NHR with the SEC, and those documents include information about each company that is not included in or delivered with this document. You can obtain any of those documents filed with the SEC from NHC or NHR, as the case may be, or through the SEC or the SEC's web site. The address of that site is <http://www.sec.gov>. Stockholders of NHC or NHR may obtain documents filed with the SEC or documents incorporated by reference in this document, when available, free of cost, by directing a request to the appropriate company at:**

National Health Realty, Inc.  
100 Vine Street, Suite 1402  
Murfreesboro, Tennessee 37130  
Attention: Corporate Secretary  
Telephone Number: (615) 890-2020

National HealthCare Corporation  
100 Vine Street, Suite 1400  
Murfreesboro, Tennessee 37130  
Attention: Corporate Secretary  
Telephone Number: (615) 890-2020

**If you would like to request documents, in order to ensure timely delivery, you must do so at least five business days before the date of the respective special meeting. This means you must request this information no later than [redacted], 2007. NHC or NHR, as the case may be, will mail properly requested documents to requesting stockholders by first class mail, or another equally prompt means, within one business day after receipt of such requests.**

See Where You Can Find More Information.

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**NATIONAL HEALTHCARE CORPORATION**

**NOTICE OF SPECIAL  
MEETING OF STOCKHOLDERS**

**To Be Held On           , 2007**

*To the stockholders of National HealthCare Corporation:*

**NOTICE IS HEREBY GIVEN** that the special meeting of stockholders of National HealthCare Corporation, a Delaware corporation (NHC), will be held at            a.m., Central time, on           , 2007, at 100 Vine Street, Suite 1400, Murfreesboro, Tennessee 37130 for the following purposes:

1. To consider and vote upon a proposal to adopt an amendment to the certificate of incorporation of NHC to increase the maximum number of shares of undesignated preferred stock having a par value of \$.01 per share from 10,000,000 shares to 25,000,000 shares.
2. To consider and vote upon a proposal to approve the issuance of shares of NHC Series A convertible preferred stock pursuant to the merger agreement.
3. To approve the postponement or adjournment of the NHC special meeting for the solicitation of additional votes, if necessary.
4. To transact any other business as may properly come before the NHC special meeting or any adjournment or postponement of the NHC special meeting.

Only NHC stockholders of record at the close of business on           , 2007, the record date for the NHC special meeting, may vote at the NHC special meeting and any adjournments or postponements of the NHC special meeting. A complete list of NHC stockholders of record entitled to vote at the NHC special meeting will be available for the 10 days before the NHC special meeting at our executive offices for inspection for proper purposes by NHC stockholders during ordinary business hours.

**Your vote is very important. The NHC board of directors has approved the merger agreement and the merger and recommends that you vote FOR all of the proposals set forth above.** Whether or not you plan to attend the NHC special meeting, please submit your proxy card with voting instructions. If you hold your stock in your name as a stockholder of record, please sign, date and return the enclosed proxy card as soon as possible. If you hold your stock in street name through a bank or a broker, please direct your bank or broker to vote your stock in the manner described in the instructions you have received from your bank or broker.

**For more information about the merger and the other transactions contemplated by the merger agreement, please review the accompanying joint proxy statement/prospectus and the merger agreement attached to it as Annex A.**

By order of the NHC board of directors

John K. Lines,  
*Secretary*

Murfreesboro, Tennessee

, 2007

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**NATIONAL HEALTH REALTY, INC.**

**NOTICE OF SPECIAL  
MEETING OF STOCKHOLDERS**

**To Be Held On           , 2007**

*To the stockholders of National Health Realty, Inc.:*

**NOTICE IS HEREBY GIVEN** that the special meeting of stockholders of National Health Realty, Inc., a Maryland corporation (NHR ), will be held at   a.m., Central time, on           , 2007, at 100 Vine Street, Suite 1402, Murfreesboro, Tennessee 37130 for the following purposes:

1. To consider and vote upon a proposal to approve the merger of NHR with and into Davis Acquisition Sub LLC, an indirect wholly-owned subsidiary of National HealthCare Corporation (NHC ), in accordance with the terms of the Agreement and Plan of Merger, dated December 20, 2006, by and among Davis Acquisition Sub LLC (an indirect wholly-owned subsidiary of NHC), NHC/OP, L.P. (a direct and indirect wholly-owned subsidiary of NHC), NHC and NHR. Upon the effectiveness of the merger, the separate corporate existence of NHR will cease and Davis Acquisition Sub LLC will continue as the surviving company in the merger and will succeed to and assume all the rights and obligations of NHR in accordance with the Maryland General Corporation Law and the Delaware Limited Liability Company Act.
2. To approve the postponement or adjournment of the NHR special meeting for the solicitation of additional votes, if necessary.
3. To transact any other business as may properly come before the NHR special meeting or any adjournment or postponement of the NHR special meeting.

Only NHR stockholders of record at the close of business on           , 2007, the record date for the NHR special meeting, are entitled to notice of and may vote at the NHR special meeting and any adjournments or postponements of the NHR special meeting. A complete list of NHR stockholders of record entitled to vote at the NHR special meeting will be available for the 10 days before the NHR special meeting at our executive offices for inspection for proper purposes by NHR stockholders during ordinary business hours.

**Your vote is very important. The NHR board of directors, after giving consideration to the recommendation of the special committee to the board of directors, has approved the merger agreement and the merger and recommends that you vote FOR all of the proposals set forth above.** Whether or not you plan to attend the NHR special meeting, please submit your proxy card with voting instructions. If you hold your stock in your name as a stockholder of record, please sign, date and return the enclosed proxy card as soon as possible. If you hold your stock in   street name   through a bank or a broker, please direct your bank or broker to vote your stock in the manner described in the instructions you have received from your bank or broker.

**For more information about the merger and the other transactions contemplated by the merger agreement, please review the accompanying joint proxy statement/prospectus and the merger agreement attached to it as Annex A.**

By order of the NHR board of directors

John K. Lines,  
*Secretary*

Murfreesboro, Tennessee

, 2007

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**QUESTIONS AND ANSWERS ABOUT THE MERGER**

**Q: When and where are the special stockholders meetings?**

A1: The NHC special meeting will take place on \_\_\_\_\_, 2007, at \_\_\_\_\_ a.m. Central Time, at 100 Vine Street, Suite 1400, Murfreesboro, Tennessee 37130.

A2: The NHR special meeting will take place on \_\_\_\_\_, 2007, at \_\_\_\_\_ a.m. Central Time, at 100 Vine Street, Suite 1402, Murfreesboro, Tennessee 37130.

**Q: What is happening at each special meeting?**

A1: At the NHC special meeting, stockholders of NHC will be asked (1) to consider and vote upon a proposal to adopt an amendment to the certificate of incorporation of NHC to increase the maximum number of shares of undesignated preferred stock having a par value of \$.01 per share from 10,000,000 shares to 25,000,000 shares, (2) to consider and vote upon a proposal to approve the issuance of Series A convertible preferred stock, having a par value of \$.01 per share, pursuant to the merger agreement, (3) to approve the postponement or adjournment of the NHC special meeting for the solicitation of additional votes, if necessary, and (4) to transact any other business as may properly come before the NHC special meeting or any adjournment or postponement of the NHC special meeting.

A2: At the NHR special meeting, stockholders of NHR will be asked (1) to consider and vote upon the approval of the merger, (2) to approve the postponement or adjournment of the NHR special meeting for the solicitation of additional votes, if necessary, and (3) to transact any other business as may properly come before the NHR special meeting or any adjournment or postponement of the NHR special meeting.

**Q: What will happen in the merger?**

A: If the merger is approved and all other conditions to the merger have been satisfied or waived, NHR will merge with and into Davis Acquisition Sub LLC, upon the terms and subject to the conditions set forth in the merger agreement. Upon effectiveness of the merger, the separate corporate existence of NHR shall cease and Davis Acquisition Sub LLC shall continue as the surviving person in the merger and a wholly-owned subsidiary of NHC/OP, L.P., which is a wholly-owned subsidiary of NHC and shall succeed to and assume all the rights and obligations of NHR.

**Q: Why are the parties proposing to merge?**

A: The parties believe that the combined company will provide the present stockholders of each company with a more focused, flexible and efficient corporation whose purpose and activities are more closely aligned with those of its stockholders. See Special Factors NHC's Reasons for, and Advantages of, the Merger and Special Factors NHR's Reasons for, and Advantages of, the Merger.

**Q: What will NHR stockholders receive in the merger?**

A: Upon the effectiveness of the merger, each issued and outstanding share of common stock, par value \$0.01 per share, of NHR, other than any such shares directly owned by Davis Acquisition Sub LLC, NHC/OP, L.P. or NHC, will be converted into the right to receive cash and shares of the Preferred Stock, having the rights and

designations set forth in the Certificate of Designations, the form of which is attached to this proxy statement/prospectus as Annex C. In addition, immediately prior to the consummation of the merger, NHR will declare a special dividend payable to each holder of record of NHR common stock who shall receive the merger consideration at the effective time of the merger in an amount equal to the dividend that NHR would have declared and paid in the ordinary course of business in order to qualify as a real estate investment trust ( REIT ) for the taxable year commencing on January 1, 2007 and ending on the effective date of the merger if NHR had not entered into the merger agreement.

**Q: Are stockholders able to exercise dissenters rights?**

A1: The stockholders of NHC will not be entitled to exercise dissenters rights with respect to any matter to be voted upon at the NHC special meeting.

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A2: The stockholders of NHR will not be entitled to exercise dissenters' rights with respect to any matter to be voted upon at the NHR special meeting.

**Q: When do you expect to complete the merger?**

A: We expect to complete the merger in the second quarter of 2007.

**Q: How will the combined company's business be different?**

A: The merger will provide NHC with a larger asset and equity base that is anticipated to enhance NHC's future growth and prospects for long-term increases in stockholder value. Following the merger, NHC will no longer be required to make lease payments to NHR. Assuming the continuation of current operating trends, the elimination of such required lease payments will result in a substantial increase in the annual recurring free cash flow of NHC, even after providing for the dividends that NHC will be required to pay on the Preferred Stock. In addition, the merger will (i) reduce the expense and management time required to manage two public companies, (ii) eliminate the possibility that NHR could be acquired by a competitor of NHC, (iii) broaden NHC's access to debt financing sources and (iv) eliminate the financial uncertainty that resulted from the periodic negotiation and renegotiation of the leasing terms of the properties that NHR leased to NHC.

**Q: How will the combined company be managed?**

A: NHR is currently managed by a wholly-owned subsidiary of NHC pursuant to the Restated Advisory, Administrative Services and Facilities Agreement (the Management Agreement), which will be terminated upon the consummation of the merger. NHR does not have any officers or employees who are not also officers or employees of NHC. Following the merger, these officers and employees will be officers or employees of NHC only, and perform substantially the same functions as they did before the merger, except that they will not have the duties of managing NHR as a separate public company. The merger will not affect the composition of the current board of directors of NHC, except that, under certain circumstances, the holders of Preferred Stock will have the right to elect two directors to the NHC board of directors. The directors of NHR will resign following the merger.

**Q: What will be the composition of the board of directors of NHC and NHR following the merger?**

A: Immediately following the merger, NHC will have the same board of directors it has today. The certificate of designations governing the Preferred Stock will allow the holders of the Preferred Stock the right to elect two additional directors to the board of directors of NHC in limited circumstances. NHR, whose successor will be merged into Davis Acquisition Sub LLC, will cease to exist as a company. Davis Acquisition Sub LLC will continue to be managed by its sole managing member following the merger.

**Q: What are the U.S. federal income tax consequences of the merger?**

A: Assuming that the merger is completed as currently contemplated, it is expected that the receipt of cash and shares of the Preferred Stock by stockholders of NHR in exchange for their common stock of NHR pursuant to the merger should be a taxable transaction for U.S. federal income tax purposes. The specific tax consequences to stockholders of NHR of the merger will depend on their own particular situation.

**YOU SHOULD READ CERTAIN MATERIAL U.S. FEDERAL INCOME TAX CONSEQUENCES FOR A MORE COMPLETE DISCUSSION OF THE U.S. FEDERAL INCOME TAX CONSEQUENCES OF**

**THE MERGER. TAX MATTERS ARE COMPLICATED AND THE TAX CONSEQUENCES OF THE MERGER TO YOU WILL DEPEND UPON THE FACTS OF YOUR PARTICULAR SITUATION. BECAUSE INDIVIDUAL CIRCUMSTANCES MAY DIFFER, WE URGE YOU TO CONSULT WITH YOUR TAX ADVISOR AS TO THE SPECIFIC TAX CONSEQUENCES OF THE MERGER TO YOU, INCLUDING THE APPLICABILITY OF U.S. FEDERAL, STATE, LOCAL, FOREIGN AND OTHER TAX LAWS.**

**Q: How will NHC be treated for U.S. federal income tax purposes following the merger?**

A: NHR is organized and has operated in a way intended to qualify it as a real estate investment trust ( REIT ) for U.S. federal income tax purposes. Generally, a REIT, with certain limited exceptions, is not taxed at the corporate level on its ordinary net income or capital gains distributed currently to its

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stockholders. This treatment substantially eliminates the double taxation (at the corporate and stockholder levels) that typically results from the use of corporate investment vehicles. NHC is not and will not be a REIT and will be taxable as a corporation for U.S. federal income tax purposes. Consequently, NHC will be subject to tax (including applicable alternative minimum tax) on its taxable income at regular corporate rates. Distributions to holders of stock in NHC will not be deductible by NHC, nor are distributions required to be made. Generally, if NHC makes a distribution to holders of its stock, all such distributions will be taxable to such holders as dividends, to the extent of NHC's current or accumulated earnings and profits. Dividends to individual holders of stock of NHC may qualify as qualified dividend income for U.S. federal income tax purposes, taxable at reduced rates. Corporate holders of stock of NHC may be eligible for the dividends received deduction with respect to dividends on stock of NHC.

**Q: What stockholder vote is required to approve the items to be voted on at each special meeting, including the merger?**

A1: With respect to the NHC special meeting:

the affirmative vote of the holders of a majority of common shares outstanding and entitled to vote thereon at the NHC special meeting is required to approve the amendment of the NHC certificate of incorporation; and

the affirmative vote of the holders of a majority of the outstanding common shares represented and voting at the NHC special meeting is required to approve the issuance of shares of the Preferred Stock and on each other matter to be acted on, including any postponement or adjournment of the NHC special meeting to solicit additional votes.

A2: With respect to the NHR special meeting, approval of the merger is conditioned on receiving:

the affirmative vote of the holders of a majority of all common stock outstanding and entitled to vote thereon at the NHR special meeting; and

the affirmative vote of the holders of a majority of the common stock outstanding and entitled to vote thereon that are not owned by an affiliate of NHR, including any director or officer of NHR or NHC, or any of their affiliates.

On each other matter to be acted on at the NHR special meeting, including any postponement or adjournment of the NHR special meeting to solicit additional votes, the approval of a majority of the outstanding common stock present in person or represented by proxy at the NHR special meeting is required to approve such matter.

**Q: Do the boards recommend approval of the proposals?**

A: Yes. Based on the recommendation of their respective special committees, taking into consideration the fairness opinions of their respective financial advisors, which are attached to this proxy statement/prospectus as [Annex D](#) and [Annex E](#), the boards of directors of NHC and NHR each approved and adopted the merger agreement and the transactions contemplated thereby and recommend that you vote FOR approval of the NHC Proposal or the NHR Proposal, as the case may be.

**Q: What do I need to do now?**

A: We urge you to read carefully this joint proxy statement/prospectus, including its annexes and the documents incorporated by reference herein. You also may want to review the documents referenced under [Where You Can](#)

Find More Information and consult with your accounting, legal and tax advisors.

**Q: How do I vote my shares?**

A1: Holders of shares of NHC common stock may indicate how they want to vote on their proxy card and then sign and mail their proxy card in the enclosed return envelope as soon as possible so that their shares may be represented at the NHC special meeting. Holders of shares of NHC common stock may also attend the NHC special meeting in person instead of submitting a proxy.

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Unless such shares are held in a brokerage account, if holders of shares of NHC common stock sign, date and send their proxy and do not indicate how they want to vote, such proxies will be voted FOR the NHC Proposal and all other proposals to be voted on at the NHC special meeting. If such shares are held in a brokerage account, please see the answer to the next question. If holders of shares of NHC common stock fail either to return their proxy card or if they ABSTAIN with respect to the NHC Proposal to amend the NHC certificate of incorporation, the effect will be a vote AGAINST such proposal. With respect to the issuance of Preferred Stock pursuant to the merger, the postponement or adjournment of the NHC special meeting or any other business as may properly come before the NHC special meeting; if the holders of shares of NHC common stock fail to return their proxy card, such shares of NHC common stock will not be counted for purposes of the such vote.

A2: If you hold shares of NHR common stock in your name, please sign, date and return your proxy card with voting instructions. If your stock is held in street name through a bank or a broker, please direct your bank or broker to vote your stock in the manner described in the instructions you have received from your bank or broker. Also, you may attend the special meeting in person instead of submitting a proxy. Unless your shares are held in a brokerage account, if you sign, date and send your proxy and do not indicate how you want to vote, your proxy will be voted FOR the NHR Proposal and all other proposals to be voted on at the NHR special meeting. If your shares are held in a brokerage account, please see the answer to the next question.

Abstentions will be counted as shares that are present and entitled to vote for purposes of determining the number of shares that are present and entitled to vote with respect to any particular matter, but will not be counted as votes in favor of such matter. Accordingly, an abstention from voting on the NHR Proposal will have the same legal effect as a vote AGAINST the matter. With respect to any other matter to be voted on at the NHR special meeting, a vote to ABSTAIN will have no effect on the outcome of such other matters.

**Q: If my NHC common stock or NHR common stock are held in a brokerage account or in street name, will my broker vote my shares for me?**

A: If you are an NHC stockholder or NHR stockholder, and, in either case, if you do not provide your bank or broker with instructions on how to vote your street name shares, your bank or broker will not be permitted to vote them. Also, if your bank or broker has indicated on the proxy that it does not have discretionary authority to vote such street name shares, your bank or broker will not be permitted to vote them. Either of these situations results in a broker non-vote.

A broker non-vote with respect to the NHC special meeting will not be considered as present and entitled to vote with respect to any matter presented at the NHC special meeting, but will be counted for purposes of establishing a quorum. A broker non-vote with respect to the issuance of the Preferred Stock will have the effect of a vote AGAINST such matter. With respect to all other matters to be voted on at the NHC special meeting, a broker non-vote will have no effect on the outcome of such matter.

A broker non-vote on the NHR Proposal or any other proposal requiring a specified percentage of the outstanding voting stock will have the same effect as a vote AGAINST such proposal. With respect to all matters requiring a specified percentage of the votes cast to be voted on at the NHR special meeting, a broker non-vote will have no effect on the outcome of such matter.

You should, therefore, provide your bank or broker with instructions on how to vote your shares or arrange to attend the NHC special meeting and/or the NHR special meeting, as the case may be, and vote your shares in person to avoid a broker non-vote. You are urged to utilize telephone or Internet voting if your bank or broker has provided you with the opportunity to do so. See the relevant voting instruction form for instructions. If your



bank or broker holds your shares and you attend the special meeting in person, you should bring a letter from your bank or broker identifying you as the beneficial owner of the shares and authorizing you to vote your shares at the meeting.

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**Q: What do I do if I want to change my vote?**

A: You may change your vote at any time before the vote takes place at the NHC special meeting and/or the NHR special meeting, as the case may be. To do so, you may either complete and submit a new proxy card or send a written notice stating that you would like to revoke your proxy. In addition, you may elect to attend the NHC special meeting and/or the NHR special meeting, as the case may be, and vote in person, as described above.

**Q: Should I send in my NHR share certificates now?**

A: No. If the merger is completed, written instructions will be sent to stockholders of NHR with respect to the exchange of their share certificates for the merger consideration described in the merger agreement, including the appropriate number of shares of the Preferred Stock.

**Q: Who can I contact with any additional questions?**

A: You may call the Corporate Secretary of NHC or NHR at:

National HealthCare Corporation  
100 Vine Street, Suite 1400  
Murfreesboro, Tennessee 37130  
(615) 890-2020

National Health Realty, Inc.  
100 Vine Street, Suite 1402  
Murfreesboro, Tennessee 37130  
(615) 890-2020

**Q: Where can I find more information about the companies?**

A: You can find more information about NHC and NHR in the documents described under [Where You Can Find More Information](#) .

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**SUMMARY**

*This summary highlights selected information from this joint proxy statement/prospectus and may not contain all the information that is important to you. To fully understand the NHC proposal, the NHR proposal and for a more complete description of the legal terms of the merger, you should read carefully this entire document, including the annexes and documents incorporated by reference herein, and the other documents to which we have referred you. For information on how to obtain the documents that we have filed with the SEC, see *Where You Can Find More Information* .*

**NHC (page 81)**

NHC is a leading provider of long-term health care services. As of March 1, 2007, it operated or managed 73 long-term health care centers with 9,129 beds in 10 states and provided other services in two additional states. These operations are provided by separately funded and maintained subsidiaries. NHC provides long-term health care services to patients in a variety of settings, including long-term nursing centers, managed care specialty units, sub-acute care units, Alzheimer's care units, homecare programs, assisted living centers and independent living centers. In addition, it provides management and accounting services to owners of long-term health care centers and advisory services to NHR, and prior to November 1, 2004, to National Health Investors, Inc.

NHC common stock trades on the American Stock Exchange under the symbol *NHC* . NHC executive offices are located at 100 Vine Street, Suite 1400, Murfreesboro, Tennessee 37130 and its telephone number is (615) 890-2020.

**NHR (page 81)**

NHR is a Maryland corporation that began operations on January 1, 1998 and operates as a real estate investment trust, or REIT. Currently its assets, through its subsidiary NHR/OP, L.P., its operating partnership, include the real estate of 23 health care facilities, including 16 licensed skilled nursing facilities, six assisted living facilities and one independent living center. NHR also owns seven first and second promissory notes with outstanding principal balances totaling \$12,371,000 at March 31, 2007 that are secured by the real property of the health care facilities. Its revenues are derived primarily from rent and interest income from these real estate properties and mortgage notes receivable. Its primary lessee is NHC, which leases 14 of its 23 properties and guarantees the lease payments on the remaining nine properties.

NHR common stock trades on the American Stock Exchange under the symbol *NHR* . NHR executive offices are located at 100 Vine Street, Suite 1402, Murfreesboro, Tennessee 37130 and its telephone number is (615) 890-2020.

**The NHC Special Meeting (page 66)**

NHC will hold the NHC special meeting at  a.m., Central time, on  , at the principal executive offices of NHC located at 100 Vine Street, Suite 1400, Murfreesboro, Tennessee 37130. At the NHC special meeting, holders of NHC common stock will be asked (1) to consider and vote upon a proposal to adopt an amendment to the certificate of incorporation of NHC to increase the maximum number of shares of undesignated preferred stock having a par value of \$.01 per share from 10,000,000 shares to 25,000,000 shares, (2) to consider and vote upon a proposal to approve the issuance of Series A convertible preferred stock, having a par value of \$.01 per share; pursuant to the merger agreement, (3) to approve the postponement or adjournment of the NHC special meeting for the solicitation of additional votes, if necessary, and (4) to transact any other business as may properly come before the NHC special meeting or any adjournment or postponement of the NHC special meeting.

You can vote at the NHC special meeting only if you owned NHC common stock at the close of business on \_\_\_\_\_, 2007, which is the record date for the meeting.

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**The NHR Special Meeting (page 69)**

NHR will hold the NHR special meeting at a.m., Central time, on , at the principal executive offices of NHR located at 100 Vine Street, Suite 1402, Murfreesboro, Tennessee 37130, to vote upon the following items: (1) the approval of the merger, (2) the postponement or adjournment of the NHR special meeting for the solicitation of additional votes, if necessary, and (3) other business as may properly come before the NHR special meeting or any adjournment or postponement of the NHR special meeting.

You can vote at the NHR special meeting only if you owned NHR common stock at the close of business on , 2007, which is the record date for the meeting.

**The Merger Proposal (pages 12 and 72)**

Pursuant to Articles of Consolidation approved by the stockholders of NHR on , 2007 and filed and accepted for record with the Maryland State Department of Assessments and Taxation on , 2007, NHR consolidated with its wholly-owned subsidiary NEW NHR, Inc., forming the Consolidated Company, which is also named National Health Realty, Inc. The capital stock of the Consolidated Company consists solely of the issued and outstanding shares of common stock of NHR outstanding immediately prior to the effectiveness of the consolidation. Each issued and outstanding share of common stock of NEW NHR, Inc. was cancelled in the consolidation. The Consolidated Company succeeded by operation of the consolidation to the business, properties, assets and rights and became subject to all of the obligations and liabilities of NHR, including the merger agreement.

Under the terms of the merger agreement between Davis Acquisition Sub LLC, a Delaware limited liability company and an indirect wholly-owned subsidiary of NHC, NHC/OP, L.P., a wholly-owned subsidiary of NHC, NHC and NHR, NHR will merge with and into Davis Acquisition Sub LLC, whereby each issued and outstanding share of NHR common stock, par value \$0.01 per share, other than any such shares directly owned by Davis Acquisition Sub LLC, NHC/OP, L.P. and NHC, will be converted into the right to receive \$9.00 in cash and one share of Preferred Stock. In addition, promptly following the effectiveness of the merger each of the holders of NHR common stock on the NHR record date will receive a special dividend for the period from January 1, 2007 until the closing date of the merger in an amount consistent with NHR's past practice. Upon effectiveness of the merger, the separate corporate existence of NHR shall cease, and Davis Acquisition Sub LLC shall continue as the surviving company in the merger and shall succeed to and assume all the rights and obligations of NHR in accordance with the Maryland General Corporation Law and the Delaware Limited Liability Company Act.

**The Stockholders of NHR Will Receive Shares of NHC's Series A Convertible Preferred Stock and Cash in the Merger (page 72)**

If the merger is completed, each issued and outstanding share of common stock, par value \$0.01 per share, of NHR, other than any such shares directly owned by Davis Acquisition Sub LLC, NHC/OP, L.P., or NHC, will be converted into the right to receive cash and shares of Series A Convertible Preferred Stock, par value \$0.01 per share, of NHC having the rights and designations set forth in the Certificate of Designations. In addition, immediately prior to the consummation of the merger, NHR will declare a special dividend payable to each holder of record of NHR common stock who shall receive the merger consideration at the effective time of the merger in an amount equal to the dividend that NHR would have declared and paid in the ordinary course of business in order to qualify as a REIT for the taxable year commencing on January 1, 2007 and ending on the effective date of the merger if NHR had not entered into the merger agreement.

Please do not send in your stock certificates at this time. You will receive written instructions to do so after the merger is complete.

**Completion of the Merger**

It is currently expected that the merger will be completed after stockholders have approved the NHC Proposal and the NHR Proposal at the special meetings, if regulatory approvals and other required matters are

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completed by that time. NHC and NHR are working to complete the merger in the second quarter of 2007, but in no event later than August 31, 2007. See Description of the Merger Agreement Closing; Completion of the Merger.

### **Ownership of NHC After the Merger**

Immediately following the merger, the existing NHC stockholders will own approximately the same percentage of shares of NHC common stock issued and outstanding prior to the merger and the existing stockholders of NHR will hold 100% of the outstanding shares of the Preferred Stock.

### **Recommendations of the Special Committees and the Boards of Directors (pages 20 and 31)**

*Special Committee Recommendations.* Each special committee unanimously recommended to its respective board that the NHC Proposal and the NHR Proposal, as applicable, was advisable and in the best interests of each company and its stockholders, and that the merger agreement and the transactions contemplated thereby should be approved.

*NHC Board Recommendation.* The board of directors of NHC adopted the recommendation of its special committee that the merger agreement and the transactions contemplated thereby should be approved and that the NHC Proposal should be submitted to stockholders for approval. **The NHC board of directors believes that the NHC Proposal is advisable and in the best interests of the company's stockholders, and it recommends that the company's stockholders vote FOR approval of the NHC Proposal.**

*NHR Board Recommendation.* The board of directors of NHR adopted the recommendation of its special committee that the merger agreement and the transactions contemplated thereby should be approved and that the NHR Proposal should be submitted to stockholders for approval. **The NHR board of directors believes that the NHR Proposal is advisable and in the best interests of the stockholders of NHR, and it recommends that such stockholders vote FOR approval of the NHR Proposal.**

### **NHC's and NHR's Reasons for the Merger (pages 23 and 33)**

#### **NHC's Reasons for the Merger**

The following outline of factors considered by the NHC board of directors is not intended to be exhaustive, but includes the material factors considered by the NHC board of directors.

1. The financial presentation of Avondale Partners, LLP ( Avondale Partners ) to the NHC board of directors and Avondale Partners' opinion addressed to the NHC special committee that the merger consideration to be paid by Davis Acquisition Sub LLC in the merger was fair, from a financial point of view, to both Davis Acquisition Sub LLC and NHC;
2. the unanimous recommendation of the NHC special committee in favor of the merger and related transactions in light of (i) the composition of the two-member non-employee NHC special committee, each of whom the NHC board of directors had previously determined were unaffiliated with NHR, (ii) the in-depth review of NHR's business, assets, liabilities and financial condition by the NHC special committee, (iii) the protracted arms-length negotiations of the NHC special committee with the NHR special committee and (iv) the retention by the NHC special committee of independent legal and financial advisors possessing experience with transactions similar to the merger to assist the NHC special committee;

3. the increase in operating flexibility expected to result from the merger, which will allow NHC to renovate and expand its facilities;



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4. the expected increase in annual recurring free cash flow resulting from the elimination of annual lease payment obligations of NHC to NHR, even after providing for the dividends on the Preferred Stock. In addition, the merger will eliminate the financial uncertainty that resulted from the periodic negotiation and renegotiation of the leasing terms of the properties that NHC leased from NHR;
5. the benefits arising from a management team focused on NHC's core business and freed of the burden of managing two public companies;
6. the elimination of the possibility that NHR could be acquired by a competitor of NHC;
7. the belief that the expected increase in annual recurring free cash flow and larger asset base will allow NHC to more easily access a broader range of debt financing sources and obtain borrowings on improved terms; and
8. the expected reduction in redundant expenses relating to corporate overhead and the costs of managing a public company.

**NHR's Reasons for the Merger**

1. The merger consideration represents a premium on the trading price of NHR common stock. The face value of the per share merger consideration (a cash payment of \$9.00 and a share of Preferred Stock with a liquidation preference of \$15.75) represents (1) a 17.5% premium over the average of the closing prices of NHR stock on the 20 trading days prior to the merger announcement (\$21.07), (2) a 10% increase over NHC's initial proposal and (3) a 16.3% premium over the closing price of NHR's common stock on December 20, 2006, the last trading day prior to the announcement of the merger agreement.
2. The merger will provide the stockholders of NHR with ownership in a company with a larger and more diversified asset and equity base, and with greater access to capital.
3. The stockholders of NHR will receive the Preferred Stock, which has many of the same dividend characteristics as the NHR stock, but with a greater potential for growth and appreciation.
4. Following the merger, NHC and NHR expect to achieve operational efficiencies and eliminate duplication of functions between the two companies.

**Interests of NHC and NHR Management in the Merger (page 44)**

Members of the NHC board of directors and members of the NHR board of directors have interests in the merger that are different from, or in addition to, or that may conflict with, the interests they share with you as stockholders of NHC or NHR, as the case may be.

NHR is managed by a wholly-owned subsidiary of NHC pursuant to the Management Agreement. For its services, NHC is entitled to annual compensation of the greater of 2.5% of NHR's gross consolidated revenues or \$500,000. The amount accrued for advisory services in 2006 was \$524,000. All officers of NHR are appointed by NHC, and are also officers of NHC. The Management Agreement may be terminated by either party on 90 days notice and will be terminated upon the consummation of the merger.

**Anticipated Accounting Treatment of the Merger (page 45)**

NHC intends to account for the merger as a purchase transaction under accounting principles generally accepted in the United States. Under the purchase method of accounting, the assets and liabilities of NHR will be recorded, as of the completion of the merger, at their respective fair values and added to those of NHC. These allocations will be based upon valuations that have not yet been finalized. The financial condition and results of operations of NHC after completion of the merger will reflect NHR's balances and results after completion of the merger but will not be restated retroactively to reflect the historical financial position or results of operations of NHR.

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Following the completion of the merger, the earnings of the combined company will reflect purchase accounting adjustments, including the effect of changes in the cost bases for assets and liabilities on depreciation and amortization expense. Long-lived assets will be evaluated for impairment when events or changes in economic circumstances indicate the carrying amount of such assets may not be recoverable. The goodwill, if any, resulting from the merger, which is not subject to amortization, will be reviewed for impairment at least annually. Any future impairments or market value adjustments would reduce the asset carrying values and result in changes to earnings for the combined company.

**Dividends and Distributions (page 44)**

*Under the merger agreement, NHR is permitted to make normal quarterly cash dividends to the holders of its common stock.*

Under the merger agreement, NHR is permitted to make (i) the dividend, the record date for which was December 29, 2006, in the amount of \$0.4325 per share of NHR's common stock or as is otherwise equal to the dividend that NHR determines is necessary to qualify as a REIT for its taxable year ended December 31, 2006, and (ii) a special dividend payable immediately prior to the consummation of the merger in an amount equal to the dividend that NHR would have declared and paid in the ordinary course of business for the portion of 2007 preceding the effective time of the merger, in order to qualify as a REIT for its 2007 taxable year, if NHR had not entered into the merger agreement.

**Conditions to the Merger (page 75)**

The merger will be completed only if specific conditions, including, among others, the following, are met or waived by the parties to the merger agreement:

the NHR Proposal and the NHC Proposal shall have been approved by the requisite votes of the NHR and NHC stockholders, as applicable;

the registration statement, including this joint proxy statement/prospectus, shall have been declared effective by the SEC;

the shares of the Preferred Stock to be issued in the merger shall have been approved for listing on the American Stock Exchange;

the NHR reorganization shall have been consummated, including the merger of NHR and its wholly-owned subsidiary, NHR-Delaware, Inc., a Delaware corporation, with NHR as the surviving entity;

the limited partnership units of NHR/OP, L.P. held by Adams Mark, L.P. and National Health Corporation will be purchased by Davis Acquisition Sub LLC for consideration equivalent to the consideration paid in the merger for the shares of NHR common stock;

the representations and warranties of the parties to the merger agreement shall be true, except for inaccuracies that would not have a material adverse effect;

the requisite covenants of each of the parties shall have been performed in accordance with the merger agreement;

no limitations or other restraints (including any pending or threatened suit, action or proceeding by any governmental entity) shall be in effect which would prevent the consummation of the merger or cause a material adverse effect on Davis Acquisition Sub LLC, NHC/OP, L.P., on the one hand, or NHR, on the other hand; and

since the date of the merger agreement, there shall not have been a material adverse effect relating to NHR, on the one hand, or Davis Acquisition Sub LLC, NHC/OP, L.P. or NHC, on the other hand.

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**Termination of the Merger Agreement (page 76)**

Even if the stockholders of NHC and NHR approve the NHC Proposal and the NHR Proposal, as the case may be, Davis Acquisition Sub LLC and NHR can jointly agree to terminate the merger agreement by mutual written consent. Either Davis Acquisition Sub LLC and/or NHR may also terminate the merger agreement if, among others, any of the following occurs:

the merger shall not have been consummated by August 31, 2007, as long as the failure to complete the merger on or before that date is not the result of the failure by the terminating party to fulfill any of its obligations under the merger agreement;

either the requisite stockholders of NHC do not approve the NHC Proposal or the requisite stockholders of NHR do not approve the NHR Proposal;

any legal restraint or prohibition preventing the merger or which has a material adverse effect on either NHC or NHR shall have become final and nonappealable;

either NHR, on the one hand, or Davis Acquisition Sub LLC, NHC/OP, L.P. or NHC, on the other hand, shall have breached or failed to perform certain representations, warranties, covenants or agreements as set forth in the merger agreement;

NHR provides written notice that it is prepared, upon termination of the merger agreement, to enter into a binding definitive agreement in connection with a superior proposal; or

the board of directors of NHR fails (i) to recommend the NHR Proposal to its stockholders, (ii) to call or hold the NHR special meeting or to prepare and mail this joint proxy statement/prospectus, or (iii) to comply with its non-solicitation obligations under the merger agreement.

NHR is required to pay to Davis Acquisition Sub LLC a fee in the amount of \$9,444,000 if the merger agreement is terminated under certain circumstances. In addition, NHR, on the one hand, and Davis Acquisition Sub LLC, on the other hand, have agreed in the event of certain terminations to reimburse the reasonable out-of-pocket costs and expenses of the other party; provided, however, that neither party shall in any case be required to reimburse the aggregate costs and expenses of the other party in excess of \$2.0 million.

**Solicitation of Other Offers (page 75)**

The merger agreement contains provisions prohibiting NHR from actively seeking an alternate transaction prior to the time the merger agreement is terminated. The non-solicitation covenant generally prohibits NHR and its subsidiaries, as well as their officers, directors, employees, agents and representatives, from taking any action to solicit an alternative acquisition proposal.

**Listing of NHC Series A Convertible Preferred Stock (page 44)**

NHC has applied for the listing of the shares of the Preferred Stock on the American Stock Exchange.

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**SPECIAL FACTORS**

**General Description of the Merger**

Pursuant to the merger agreement, NHR will merge with and into Davis Acquisition Sub LLC, a Delaware limited liability company and an indirect wholly owned subsidiary of NHC. Pursuant to the merger agreement, each outstanding share of common stock of NHR, other than any such shares directly owned by Davis Acquisition Sub LLC, NHC/OP, L.P. or NHC, will be converted into the right to receive \$9.00 in cash and one share of Preferred Stock. In addition, promptly following the effectiveness of the merger, each of the holders of NHR common stock on the NHR record date will receive a special dividend for the period from January 1, 2007 until the closing date of the merger in an amount consistent with NHR's past practice. Upon effectiveness of the merger, the separate corporate existence of NHR shall cease and Davis Acquisition Sub LLC shall continue as the surviving person in the merger and shall succeed to and assume all the rights and obligations of NHR in accordance with the Maryland General Corporation Law and the Delaware Limited Liability Company Act. Set forth below is a diagram depicting the merger of NHR with and into Davis Acquisition Sub LLC.

**Background of the Merger**

NHR, which was spun off from NHC in 1998, has been managed by NHC, or an affiliate thereof, pursuant to the Management Agreement. NHR (through its operating subsidiary, NHR/OP, L.P.) has also leased

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most of its properties to NHC. In light of the foregoing, the NHR board of directors has periodically discussed and reviewed NHR's business, strategic direction and prospects.

In February 2006, the audit committee of the board of directors of NHC recommended to the full board of directors of NHC that Lawrence Tucker and Emil Hassan, each of whom the audit committee determined was not affiliated with NHR, undertake a study of the interfaces between the two companies, including a possible acquisition transaction. The board of directors accepted the recommendation of the audit committee and established a special committee consisting of Messrs. Tucker and Hassan, and requested that such special committee undertake such a study, with the assistance of NHC management. The NHC special committee was delegated the authority of the board to review, evaluate and, if appropriate, negotiate and recommend an acquisition transaction with NHR, and was authorized to retain independent legal and financial advisors to assist the NHC special committee. On February 24, 2006, the NHC special committee engaged Cahill Gordon & Reindel llp (Cahill Gordon), as its legal counsel.

In February and March of 2006, the NHC special committee reviewed the relationships, business dealings and potential synergies that might result from a transaction between NHC and NHR and determined that explanatory discussions with NHR were in the best interests of NHC. At various points during this period, Cahill Gordon discussed with the NHC special committee its fiduciary duties in considering a transaction with an affiliated party.

On March 8, 2006 the NHC board and the NHR board held meetings of their respective boards of directors. During the NHR board meeting, the NHC special committee informed the NHR board that it was prepared to discuss a potential acquisition transaction between NHC and NHR. Among other potential benefits, the NHC special committee indicated that such a transaction could potentially eliminate the regulatory burden and expenses resulting from the operation and management of the two public companies by, in many cases, the same personnel. Given the existing relationship and affiliations between the companies, the NHC special committee suggested that the NHR board form a committee consisting of independent directors and that such committee retain its own legal and financial advisors.

Immediately following its meeting with the NHC special committee, the NHR board met separately to discuss the matter. As a result of such discussions, the NHR board resolved to appoint a special committee to evaluate an acquisition transaction with NHC, consisting of Mr. Jobe and Mr. Swanson, and authorized such special committee to retain its own legal and financial advisors. The NHR special committee was delegated the authority of the board to review, evaluate and, if appropriate, negotiate and recommend a business combination with NHC.

Later that same day the NHR special committee informed the NHC special committee that NHR was willing to explore a potential transaction between NHC and NHR, that NHR had established a special committee of its board for the review and consideration of such matters and that such special committee had been authorized to retain independent legal and financial advisors. The NHC special committee requested that each of NHC and NHR execute a mutual confidentiality agreement in order to facilitate the discussion and exchange of information and presented to the NHR special committee a confidentiality agreement drafted by independent counsel. Mr. Andrew Adams, as chairman of both companies, reminded the board members at each of the NHC and NHR board meetings of their duties as board members regarding confidentiality of information.

Following the board of directors meetings on March 8, 2006, the NHR special committee met telephonically and discussed the engagement of legal and financial advisors. The NHR special committee contacted representatives of the Nashville law firm of Waller Lansden Dortch & Davis, LLP (Waller Lansden), and representatives of Waller Lansden joined the meeting. Waller Lansden discussed with the members of the NHR special committee their duties as directors in considering a transaction with an affiliated party and advised the NHR special committee of its recommendation to engage special Maryland counsel to advise on the legal obligations of the NHR special committee members because Maryland was NHR's state of incorporation. Waller Lansden and Cahill Gordon negotiated a mutual confidentiality agreement, and on March 17, 2006, the special committees executed such confidentiality agreement.





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During the remainder of March and April of 2006, the NHC special committee continued its analysis of a potential acquisition transaction between NHC and NHR, but neither the NHC special committee nor the NHR special committee retained a financial advisor, and the special committees did not communicate further.

On March 31, 2006, Joel Jobe, a member of the NHR special committee died unexpectedly. Pursuant to resolutions adopted at the April 26, 2006 meeting of the board of directors of NHR, Mr. Jobe was replaced on the NHR board of directors by his son, James Jobe. At the same meeting, the NHR special committee was formally dissolved by resolution of the board of directors, having had no discussions with the NHC special committee since the March 8 meeting.

On May 3, 2006, the NHC board of directors held a meeting. At the meeting, the NHC special committee reported to the full NHC board of directors with respect to its analysis of a potential acquisition transaction between NHC and NHR. Following discussions of the matter with the full NHC board of directors, the NHC special committee indicated that it would continue to explore the potential for a transaction with NHR and would focus on developing the specific terms on which NHC might consider an acquisition transaction with NHR. Later in May of 2006, based upon the further analyses of the terms of an acquisition transaction with NHR by the NHC special committee, the NHC board of directors, upon the recommendation of the NHC special committee, determined not to pursue the potential acquisition transaction with NHR.

During the period from May 2006 until July 26, 2006, the NHC special committee and NHC's board of directors continued informally to discuss and evaluate a potential acquisition transaction with NHR. On July 26, 2006, after consultation with the NHC board of directors, Mr. Tucker of the NHC special committee contacted Mr. Swanson, formerly of the NHR special committee and indicated that NHC was interested in pursuing further discussions regarding an acquisition transaction between NHC and NHR. Mr. Swanson and Mr. Tucker communicated further in August of 2006 and Mr. Swanson agreed that he would bring the issue to the NHR board of directors.

On August 7, 2006, the NHC board of directors held a meeting at which the NHC special committee presented to the NHC board of directors a proposed offer for an acquisition transaction with NHR. Following discussions of the proposed offer, including with respect to the appropriate amount and types of merger consideration, the NHC board of directors authorized the presentation of such offer to NHR.

At the August 14, 2006 meeting of the board of directors of NHR, the board of directors resolved to form another NHR special committee, now composed of Mr. Swanson and James Jobe, who were determined to be independent of NHC. The NHR board of directors suggested a meeting between the NHR special committee and the NHC special committee. The NHR special committee contacted the NHC special committee following the August 14th board meeting to schedule a meeting to discuss the matter.

The NHR special committee and the NHC special committee met on August 22, 2006. The NHC special committee verbally indicated its willingness to submit a proposal to the NHR special committee to acquire the stock of NHR for a combination of cash and preferred stock. More specifically, the NHC special committee described a potential transaction pursuant to which each holder of NHR common stock would receive per share consideration of an amount of \$6.75 in cash and one share of NHC preferred stock with a liquidation value of \$15.75 and paying a cumulative annual dividend of \$0.80 per share. The NHC preferred stock would be convertible at the option of the holder into NHC common stock at a conversion price of \$54.00. In addition, the NHC preferred stock would be convertible at NHC's option into common stock after the fifth anniversary of its issuance. On September 5, 2006, Mr. Hassan of the NHC special committee contacted Mr. Swanson of the NHR special committee and reported that the NHC special committee was proposing that the conversion price of the NHC preferred stock would not be fixed at \$54.00, but would instead float until the execution of a merger agreement along with the market price of NHC's common stock.

On September 5, 2006, the members of the NHR special committee met with Don Daniel, Senior Vice President and Controller of both companies, to ask questions regarding the financial condition and prospects of NHR and NHC. The NHR special committee met with Dr. J. Paul Abernathy, a member of the board of directors of both companies, on September 11, 2006 pursuant to his request. Mr. Abernathy requested that the NHR special committee consider the tax consequences of any potential transaction with NHC. Mr. Abernathy

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also asked that the NHR special committee consider issues relevant to the NHR stockholder base, including his perception that such stockholders were comfortable with the current characteristics of NHR as a secure, high-dividend, tax-preferred REIT stock, in contrast to the more typical, and possibly more volatile form, of equity NHR stockholders might receive as the result of a transaction with NHC. On September 12, 2006, the NHR special committee met with Robert Adams, the Chief Executive Officer and President and a director of both companies, in order to gather information that might aid in its evaluation of the proposal from the NHC special committee.

On September 19, 2006, the board of directors of NHR met and discussed the status of the discussions regarding a potential transaction with NHC. The NHR special committee reported to the full board the information conveyed by the NHC special committee on August 22nd and September 5th and noted the recent rise in the market price of NHC common stock. The NHR special committee reported to the NHR board of directors its conclusion that an acquisition transaction with NHC was worth pursuing based on the discussions to date. The NHR board of directors asked clarifying questions regarding the proposal by the NHC special committee and discussed the potential mix of consideration. The board of directors directed the NHR special committee to confirm the potential proposal presented on August 22nd, obtain any background projections or other financial information prepared by the NHC special committee and authorized the NHR special committee to retain advisors assuming the proposal was confirmed.

The NHR special committee contacted the NHC special committee on September 22, 2006 and received pro forma financial information giving effect to the proposed transaction prepared by internal finance staff at NHC and reviewed by the NHC special committee.

On September 28, 2006, the NHC board of directors held a special meeting to obtain a report from the NHC special committee on the status of the potential acquisition transaction. The NHC special committee began by reviewing the terms of the original offer discussed by the NHC board of directors at its August 7, 2006 meeting. Following such review, the NHC special committee reported to the NHC board of directors that, due to a recent increase in the price of NHC common stock, it would not recommend that the NHC preferred stock to be issued in connection with the merger convert into NHC common stock at a conversion price of \$54.00 per share. Under a revised proposal submitted by the NHC special committee to the NHC board of directors, the total merger consideration to be paid per share of NHR common stock would be equal to 120% of the average closing price of the NHR common stock for the 20 trading sessions prior to the execution of a merger agreement, but no more than \$24.75 per share and no less than \$22.50 per share. The consideration to be paid would consist of cash and NHC preferred stock with a face value equal to \$15.75, a cumulative annual dividend of \$0.80 per share, and a conversion price for each share of NHC preferred stock equal to 120% of the average closing price of the NHC common stock for the 20 trading sessions prior to the signing of the merger agreement, but in no case less than \$50 per share. The NHC board of directors agreed with the revised proposal and authorized the negotiation of the final terms of the merger transaction with NHR.

On October 16, 2006, the NHC special committee contacted representatives of Avondale Partners and discussed with its representatives the possibility of engaging Avondale Partners to render a fairness opinion regarding the proposed acquisition transaction to the NHC special committee. The NHC special committee later formally engaged Avondale Partners pursuant to an engagement letter, the executed version of which was dated October 27, 2006. The NHC special committee specifically requested that Avondale Partners advise the committee of the fairness of the proposed transaction with NHR from NHC's perspective. In connection with the rendering of a fairness opinion, Avondale Partners agreed to perform certain financial advisory for the NHC special committee. The NHC special committee selected Avondale Partners because of its expertise and its reputation in investment banking and mergers and acquisitions and its relevant experience with advisory assignments in the healthcare and REIT industries. Avondale Partners is a nationally recognized investment banking firm regularly engaged in the valuation of businesses and their securities in connection with mergers and acquisitions, leveraged buyouts, negotiated underwritings, secondary distributions of listed and unlisted securities and private placements.

On October 9, 2006, the NHC special committee requested that the NHR special committee execute an amendment to the confidentiality agreement entered into in March. In addition, Mr. Tucker, of the NHC

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special committee, and Mr. Jobe, of the NHR special committee, discussed the acquisition proposal. Following negotiations and discussions, Mr. Tucker tentatively agreed, on behalf of the NHC special committee, that the acquisition consideration would have a stated value per share of NHR common stock equal to 120% of the average closing price of NHR common stock for the 20 trading sessions prior to signing of the merger agreement, but no less than \$23.00 per share nor more than \$24.75 per share. At a stated value of \$23.00 per share, the consideration would consist of \$7.25 per share in cash and \$15.75 face amount of NHC preferred stock. The proportion of cash and stock could be changed prior to signing but in any event would not be less than \$7.25 per share. The conversion price for the NHC preferred stock would be equal to 120% of the average closing price of NHC common stock for the 20 trading sessions prior to signing of the merger agreement, but no less than \$60.00 per share. Messrs. Tucker and Jobe also discussed a proposal whereby all of NHC's and NHR's directors would enter into individual voting agreements, pursuant to which each would commit to vote any shares of either company owned or controlled by them in favor of the contemplated transactions. On that same day, Mr. Swanson contacted Waller Lansden and, following discussions with Mr. Jobe, confirmed the engagement of Waller Lansden as counsel to the NHR special committee.

On October 12, 2006, the NHR special committee, the NHC special committee and their respective counsel met by conference call to discuss the proposal put forward by the NHC special committee, the process for moving forward with formal negotiations and the preparation of definitive documents. The special committees agreed that the proposed business combination would be in the form of a statutory merger and agreed that Waller Lansden would produce the initial draft of the merger agreement. Cahill Gordon was tasked with preparing the initial draft of the voting agreement and the certificate of designations setting forth the rights and preferences of the proposed NHC preferred stock to be issued to the NHR stockholders as part of the merger consideration.

Immediately following the conference call with the NHC special committee, the NHR special committee convened to discuss the engagement of special Maryland counsel and a financial advisor. Based on Mr. Swanson's prior favorable experience with 2nd Generation Capital, LLC ( 2nd Generation ) in dealing with NHR's previous strategic initiatives, the NHR special committee determined that 2nd Generation would be the NHR special committee's first choice as financial advisor, if they were willing and able to serve in such capacity. The NHR special committee, with representatives of Waller Lansden, contacted 2nd Generation regarding its engagement as financial advisor to the NHR special committee. Following the call, representatives of Waller Lansden sent to 2nd Generation a term sheet regarding the proposed transaction, based on the October 12 conference call. The NHR special committee formally engaged 2nd Generation on October 17, 2006 pursuant to an executed engagement letter.

With the consent of the NHR special committee, on October 18, 2006, Waller Lansden contacted representatives of the Maryland law firm of Venable, LLP ( Venable ) to serve as counsel to the NHR special committee on matters of Maryland law. Representatives of the firms discussed whether NHC could merge with NHR obtaining a supermajority vote under the Maryland Business Combination Act or NHC complying with the fair price provisions of that statute. This discussion resulted from the fact that the NHR charter did not exempt business combinations with NHC from the Maryland Business Combination Act.

On October 17, 2006, Cahill Gordon distributed initial drafts of the certificate of designations relating to the NHC preferred stock and the voting agreement to the NHC special committee. Following the review by the NHC special committee and discussions with Cahill Gordon, on October 20, 2006, Cahill Gordon distributed initial drafts of the voting agreement and certificate of designations of the NHC preferred stock to the NHR special committee and its counsel.

The NHR special committee met by conference call on October 23, 2006 with representatives of Waller Lansden and 2nd Generation to discuss the draft merger agreement, which had been previously distributed to the NHR special committee and the other drafts of definitive documents received from Cahill Gordon. Following extensive discussion of the terms of the agreements, the NHR special committee requested that an initial draft of the merger agreement be

prepared and sent to the NHC special committee and its counsel.

Waller Lansden distributed the initial draft of the merger agreement to the NHC special committee and its counsel, on October 25, 2006. That same day, Waller Lansden sent a due diligence request to the general

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counsel of NHC and NHR, on behalf of the legal advisors and 2nd Generation, seeking additional due diligence information on the companies.

On October 27, 2006, the NHR special committee convened again by telephone to discuss the possible merger. Present on the call were representatives from Venable, Waller Lansden and 2nd Generation. 2nd Generation began the call with a detailed discussion of the financial background of the proposal and its evaluation of publicly available and certain confidential information regarding each of the companies and other comparable companies and transactions. The NHR special committee also heard from representatives of Venable, who discussed in detail Maryland law regarding the duties of the members of the NHR special committee in the present context.

During the period between October 23, 2006 and October 30, 2006, the NHC special committee, its counsel and members of NHC management had various discussions relating to (i) the structure and terms of the proposed transaction, including the potential tax consequences of such a transaction, (ii) issues raised by the initial drafts of the merger agreement and the comments on the certificate of designations and voting agreement and (iii) the fiduciary duties of the directors of NHC in the context of the contemplated transaction.

On October 30, 2006, 2nd Generation contacted Mr. Tucker of the NHC special committee, per the request of the NHR special committee. Mr. Tucker, on behalf of the NHC special committee, informed 2nd Generation that the NHC special committee's proposal was conditioned on any merger being a transaction in which the tax basis of the NHR assets was stepped up, thus resulting in taxable gain to the NHR stockholders. Following the call between Mr. Tucker and 2nd Generation, the NHR special committee, 2nd Generation and Waller Lansden held a conference call to discuss the issues raised by Mr. Tucker. Regarding the taxability of the transaction, 2nd Generation noted that the cash portion of the consideration was taxable in any event. The NHR special committee requested that 2nd Generation review the financial information and the proposed transaction in light of a fully taxable transaction structure and report back to the NHR special committee.

On October 30, 2006, Waller Lansden notified Cahill Gordon that the proposed transaction could be subject to the Maryland Business Combination Act because of the absence of an exemption in the original articles of incorporation of NHR. On October 31, 2006, representatives of Cahill Gordon, Waller Lansden and Venable met by telephone to discuss potential implications of the Maryland Business Combination Act. Waller Lansden and Cahill Gordon also discussed certain open issues regarding the merger agreement and the other transaction documents.

On November 3, 2006, the NHC special committee convened a meeting attended by its counsel during which Avondale Partners presented its preliminary analysis of the proposed transaction. The members of the NHC special committee commented on various aspects of the presentation and asked questions of the representatives of Avondale Partners with respect to each of the topics presented and discussed in considerable detail each of the matters presented, including the backup data and assumptions upon which Avondale Partner's analysis and conclusions were based. After taking into account the NHC special committee's discussions with Avondale Partners regarding the proposed transaction and based upon the NHC special committee's understanding of the terms of the proposed transaction as of the date of such meeting, and such other facts, analyses and assumptions as the NHC special committee deemed relevant, the NHC special committee expressed the view that it continued to believe that the proposed transaction would be in the best interests of NHC and its stockholders.

On November 6, 2006, the NHR special committee met by conference call with 2nd Generation and Waller Lansden regarding structural and financial issues in the proposed transaction. Having reviewed the transaction as a fully-taxable event to the NHR stockholders, representatives of 2nd Generation reported their preliminary belief that the proposal was within the range of fairness for the NHR stockholders. The NHR special committee and its advisors discussed the terms of the transaction in detail and open issues between the parties. The NHR special committee resolved that 2nd Generation should propose to the NHC special committee certain additional terms related to the

features of the NHC preferred stock.



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Pursuant to the request of the NHR special committee, 2nd Generation contacted Mr. Tucker, as representative of the NHC special committee, and on November 8, 2006 a conference call was held to discuss specific features of the NHC preferred stock, including NHC's ability to optionally redeem the NHC preferred stock and the amount of the cumulative annual dividend. That same day, representatives of Waller Lansden contacted Cahill Gordon and discussed open issues regarding the definitive agreements, including the amount of any termination fees in the event that the NHR special committee should terminate the proposed transaction following the execution of the merger agreement. Cahill Gordon expressed the view that the breakup fee should be 6% of transaction value, while Waller Lansden advocated 3%. Following this call, the NHC special committee was advised of the break up fee issue, and Avondale Partners was asked to prepare a survey of termination fees in comparable transactions, which they provided to the NHC special committee on November 9, 2006.

On November 10, 2006, the special committees of NHC and NHR, their counsel and 2nd Generation held a conference call to discuss open issues, including the cumulative annual dividend, the terms of the NHC preferred stock and the termination fee. The NHC special committee agreed to certain limitations on NHC's ability to optionally redeem the NHC preferred stock, but rejected any increase in the cumulative annual dividend. Following the call, the NHR special committee consulted with Venable regarding Maryland law regarding termination fees.

The NHR special committee, Waller Lansden and 2nd Generation met telephonically on November 13, 2006, and the NHR special committee agreed that it would request an increase in the cumulative dividend and a reduction in the termination fee. Upon receipt of the request, the NHC special committee agreed to consider it, and asked Avondale Partners to update its previous analysis based on the increase in the annual dividend from \$0.80 to \$0.85 per share. On November 14, 2006, Avondale Partners presented that analysis. After consideration of this analysis and other factors, the NHC special committee determined to reject the request to increase the dividend and communicated its decision to the NHR special committee. The NHR special committee agreed to consider its response.

On November 15, 2006, the special committees, their respective counsels and 2nd Generation again met by conference call to discuss timing of the signing of the definitive merger agreement and open issues between the parties. The NHC special committee rejected any increase in the cumulative dividend, and the parties agreed to reduce the termination fee in the amount of 3.5% of the transaction value, payable in certain circumstances in the event of a termination of a definitive merger agreement. The NHR special committee requested that the NHC special committee agree now to a fixed cash consideration amount and conversion price for the NHC preferred stock, rather than allowing those prices to continue to float on a daily basis until the signing of the merger agreement. The NHC special committee responded later that day with fixed cash consideration and conversion prices (subject to adjustment in the conversion price if the 20 trading day average price of the NHC common stock is either above a certain price or below a certain price), provided that the merger agreement was executed no later than November 30, 2006.

On November 16, 2006, Cahill Gordon and Venable held a conference call to discuss the Maryland Business Combination Act as such act related to the proposed transaction. Various potential alternatives were discussed to address the Maryland Business Combination Act requirement that, absent an exemption, a super majority vote or compliance with certain fair price provisions was required.

On November 20, 2006, Cahill Gordon, Waller Lansden and Venable held a conference call to discuss the Maryland Business Combination Act and the structure of the transaction and the effects of such structure.

On November 27, 2006, Waller Lansden, Venable and 2nd Generation met telephonically with the NHR special committee and Cahill Gordon met telephonically with the NHC special committee to update the respective special committees on the status of negotiations and discuss the Maryland Business Combination Act. Following such discussions with Cahill Gordon, on November 28, 2006, the NHC special committee reported to the NHC board of

directors at a special meeting of such directors on the status of negotiations and the discussions of the Maryland Business Combination Act.

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On November 28, 2006, the NHR special committee updated the board of directors on the status of negotiations and on efforts to structure the transaction in light of certain provisions of the Maryland Business Combination Act. The board of directors appointed Richard LaRoche, director and former general counsel of both companies, to work on behalf of the NHR board to study the transaction structure and recommend, on behalf of the NHR board of directors, a possible transaction structure that would not implicate the fair price or supermajority voting requirements of the Maryland Business Combination Act. Mr. LaRoche contacted representatives in the Baltimore office of Hogan & Hartson L.L.P. (Hogan & Hartson ) to serve as special Maryland counsel for the board of directors of NHR.

On December 4, 2006, Mr. LaRoche and John Lines, the general counsel of both NHC and NHR, contacted Waller Lansden and asked that Waller Lansden and Venable work with Hogan & Hartson regarding the structure.

Following several days of work, Hogan & Hartson proposed a transaction structure that included a consolidation of NHR with a newly formed entity as part of the transaction, and Waller Lansden, Venable and Hogan & Hartson discussed this potential solution to provide an exemption to the Maryland Business Combination Act as well as several alternative structures that Waller Lansden or Venable had developed. The firms presented a number of possible transaction structures to the NHR special committee on December 12, 2006. Among the transaction structures presented was a consolidation of NHR with a subsidiary, followed by the proposed merger, which both Hogan & Hartson and Venable were willing to opine was permissible under Maryland law and would not implicate the Maryland Business Combination Act. The NHR special committee, after considering the various alternatives decided to pursue the consolidation structure and present it to the NHC special committee via Cahill Gordon. Both the proposed consolidation and the merger would require a stockholder vote, and the NHR special committee conditioned its acceptance of the proposed structure on approval by a majority of stockholders who are not affiliates of NHC.

On December 13, 2006, Waller Lansden contacted Cahill Gordon and presented the consolidation structure and the proposed voting standard. Following Cahill Gordon's call to the NHC special committee, the NHC special committee and the NHR special committee agreed to proceed with merger negotiations and board meetings of NHC and NHR were scheduled for December 20, 2006.

On December 15, 2006, each of the NHR special committee and the NHC special committee met and agreed to recommend to their respective boards the merger price of \$24.75 per share of NHR common stock, consisting of \$9.00 cash plus \$15.75 liquidation preference of NHC preferred stock; provided the signing of a merger agreement occurs no later than December 29, 2006.

Between December 13, 2006 and December 20, 2006, counsel for each special committee finalized the definitive documents related to the merger, including the merger agreement and the schedules thereto, the voting agreement and the certificate of designations.

On December 20, 2006, the NHC special committee and the NHR special committee and the boards of directors of each company held separate special meetings. At the NHC special committee meeting, Avondale Partners presented its analysis of the proposed acquisition transaction based on the final terms negotiated by the NHC special committee and the NHR special committee. Following the presentation and subsequent discussions, Avondale Partners delivered to the NHC board of directors its oral opinion, subsequently confirmed in writing, to the effect that, as of December 20, 2006, the merger consideration was fair, from a financial point of view, to both NHC and Davis Acquisition Sub LLC. Following the delivery of such opinion by Avondale Partners the NHC special committee recommended to the board of directors of NHC that the NHC board approve the merger, the merger agreement and each of the transactions contemplated thereby.

Following the adjournment of the NHC special committee meeting, the meeting of the NHC board of directors was held at which time the NHC board heard the report of the NHC special committee in which the NHC special committee recommended that the NHC board of directors approve the merger, the merger agreement and each of the transactions contemplated thereby, including the issuance of the Preferred Stock as part of the merger consideration. After further discussions by the NHC board of directors and its advisers, the NHC board of directors approved the merger, the merger agreement and each of the transactions contemplated

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thereby, including the issuance of the Preferred Stock and the submission of the NHC Proposal to the stockholders of NHC for consideration.

At the NHR special committee meeting, 2nd Generation, made an extensive financial presentation. Among other matters reviewed in detail, 2nd Generation (i) summarized the pertinent transaction provisions, (ii) described the assumptions used and basis for the financial analysis of NHR's prospects, (iii) discussed a valuation analysis of NHR using a variety of valuation methods, and (iv) reviewed its valuation of the preferred stock to be issued to NHR stockholders. 2nd Generation presented its analysis in connection with its determination that it could render a fairness opinion with respect to the proposed transaction and delivered its opinion both orally and in writing that the proposed transaction was fair to the stockholders of NHR.

Also at the meetings, representatives of Waller Lansden discussed the terms and provisions of the merger agreement, the structure of the merger and the timing of the proposed transaction. Representatives of Venable discussed extensively with the members of the NHR special committee their duties as directors under Maryland law. Representatives of Hogan & Hartson discussed with the NHR special committee the consolidation structure and its analysis of the compliance of this structure with the Maryland Business Combination Act, and Hogan & Hartson delivered an opinion, with which Venable advised the NHR special committee that it was prepared to concur, that the consolidation, and the consolidation followed by the proposed merger complied with the Maryland Business Combination Act.

After the presentations to, and discussion among, the members of the NHR special committee, the NHR special committee unanimously agreed that the merger agreement was fair, in the best interests of NHR and its stockholders and should be unanimously recommended to the board of directors of NHR for approval.

Shortly after the NHR special committee meeting adjourned, the meeting of the NHR board of directors commenced. At this meeting, the NHR board of directors heard the report of the NHR special committee in which the NHR special committee recommended that the NHR board of directors approve the merger agreement and submit the merger agreement to the NHR stockholders for consideration, and Hogan & Hartson reviewed its Maryland law advice regarding Maryland law matters, including the compliance of the transaction with the Maryland Business Combination Act. After further discussions by the NHR board of directors and its advisers, the merger agreement was approved and the NHR board of directors recommended that it was advisable and in the best interest of NHR and its stockholders that NHR consolidate with a wholly owned subsidiary and subsequently merge with and into the Davis Acquisition Sub LLC, on substantially the terms and conditions set forth in the merger agreement and that the stockholders approve the consolidation and the merger. NHR board members W. Andrew Adams and Richard F. LaRoche, Jr. abstained from the NHR board of directors vote on the consolidation and the merger because of their membership on the board of directors of National Health Investors, Inc., another REIT affiliated with NHR and NHC.

Following the approval of the NHC and NHR boards of directors, the parties entered into the merger agreement. NHC and NHR issued a joint press release with respect to the merger on December 21, 2006.

On April 6, 2007, NHC, Davis Acquisition Sub LLC, NHC/OP, L.P. and NHR entered into Amendment and Waiver No. 1 to Agreement and Plan of Merger which, among other things, extended the termination date of the merger agreement from June 30, 2007 to August 31, 2007.

**Recommendations of the NHC Special Committee and the NHC Board of Directors**

On December 20, 2006, the NHC special committee unanimously recommended to the NHC board of directors, after giving consideration to the presentation of Avondale Partners, which was the independent financial advisor to the NHC special committee, that the merger proposal and terms of the merger agreement were advisable, fair and in the

best interest of NHC and its stockholders, and that the NHC board of directors should approve the merger, the merger agreement and each of the transactions contemplated thereby. Based on this recommendation, the fairness opinion of Avondale Partners, and other factors considered by the board of directors, the NHC board of directors approved the merger, the merger agreement and each of the transactions contemplated thereby, including the issuance of the Preferred Stock and the submission of the NHC Proposal to the NHC stockholders for consideration.

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**Fairness of the Offer and the Merger**

The NHC board of directors, NHC/OP, L.P. and Davis Acquisition Sub LLC believe that the merger is advisable and in the best interests of both NHC's and NHR's stockholders. In addition NHC's board determined that it believed that the transaction was procedurally and substantively fair to unaffiliated stockholders of NHC and NHR. During its December 20, 2006 meeting, the NHC board of directors, based on the unanimous recommendation of the NHC special committee, the fairness opinion of Avondale Partners, and a number of other factors considered by the NHC board of directors, approved, by the unanimous vote of those directors present and voting, the merger, the merger agreement and each of the transactions contemplated thereby, including the issuance of the Preferred Stock and the submission of the NHC Proposal to the NHC stockholders for consideration. One director, Mr. Andrew Adams, a director and the chairman of each of NHC and NHR, abstained from the vote.

The NHC board of directors, NHC/OP, L.P. and Davis Acquisition Sub LLC considered a number of material factors, which in the opinion of NHC board members, NHC/OP, L.P. and Davis Acquisition Sub LLC supported the NHC board of directors' determination that the merger (including the pre-merger consolidation of NHR) is substantively and procedurally fair to NHC's and NHR's stockholders.

The factors supporting a determination of procedural and substantive fairness to NHR's unaffiliated stockholders included:

the NHR board of directors received a fairness opinion from 2nd Generation that the merger consideration to be paid by Davis Acquisition Sub LLC in the merger was fair from a financial point of view, to the stockholders of NHR;

the NHR special committee was represented by independent legal counsel, Waller Lansden and independent financial advisors, 2nd Generation;

the unanimous recommendation of the NHR special committee in favor of the merger and related transactions in light of (i) the composition of the two-member non-employee NHR special committee, each of whom the NHR board of directors had previously determined were unaffiliated with NHC, (ii) the in-depth review of NHR's and NHC's business, assets, liabilities and financial condition by the NHR special committee and (iii) the protracted arms-length negotiations of the NHC special committee with the NHR special committee;

the business, financial strength and prospects of NHR as a stand-alone entity was viewed less favorably when compared to the value of the merger consideration and participation with a larger NHC entity because of NHR's history of no acquisition and limited growth;

the nature of the representations, warranties, covenants and other provisions of NHC and NHR set forth in the draft of the merger agreement and certificate of designations for the NHC preferred stock were negotiated by the NHR special committee to protect the interests of NHR and its stockholders and, therefore were viewed as supporting the fairness of the merger;

the nature of the proposed consideration consisting of a combination of cash and NHC preferred stock to be paid by NHC upon the consummation of the merger, which was considered by the NHR special committee and the NHR board of directors to be favorable to the NHR stockholders based on the financial analysis of 2nd Generation and the opportunity for stockholders to receive a substantial amount of cash per share of NHC common stock and participate through the NHC preferred stock in the future of the merger entity;

the current and historical market prices of NHR's common stock; as a result of which the merger price represented a 15.9% premium over the price of NHR common stock one day prior to the announcement of the merger and a 17.9% premium over the price of NHR common stock four weeks prior to the announcement of the merger;

based on a precedent transactions analysis, comparable companies analysis, discounted cash flow analysis, dividend discount analysis and net asset value analysis conducted by 2nd Generation on which the NHR special committee and NHR board of directors relied, the estimated going concern value of



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NHR, as a stand-alone entity, was less favorable than the proposed merger consideration. 2nd Generation used the above tests as a means of determining the estimated going concern value because these methods are generally accepted by appraisers for such purpose and in the opinion of 2nd Generation were the best evidence of going concern value of NHR in the circumstances; and

the liquidation value of NHR, the replacement cost of NHR's assets, the potential market value of NHR's assets and the benefits to NHC as an operator of long-term health care facilities, of operational control of NHR's assets;

The factors supporting a determination of procedural and substantive fairness to NHC's stockholders included:

the financial presentation of Avondale Partners to the NHC board of directors on December 20, 2006 and Avondale Partner's opinion addressed to the NHC special committee that the merger consideration to be paid by Davis Acquisition Sub LLC in the merger was fair, from a financial point of view, to both Davis Acquisition Sub LLC and NHC. We have described Avondale Partner's opinion in detail under the heading "Special Factors Opinion of NHC's Financial Advisor Avondale Partners, LLC." While not specifically addressed to the unaffiliated stockholders of NHC, the NHC board of directors considers the fairness opinion to be relevant to the determination that the consideration paid in the merger was fair to NHC's stockholders, including its unaffiliated stockholders. The NHC board of directors was not aware of and did not consider any reports, opinions or appraisals received by any other filing person in connection with its deliberations;

the unanimous recommendation of the NHC special committee in favor of the merger and related transactions in light of (i) the composition of the two-member non-employee NHC special committee, each of whom the NHC board of directors had previously determined were unaffiliated with NHR, (ii) the in-depth review of NHR's business, assets, liabilities and financial condition by the NHC special committee, (iii) the protracted arms-length negotiations of the NHC special committee with the NHR special committee and (iv) the retention by the NHC special committee of independent legal and financial advisors possessing experience with transactions similar to the merger to assist the NHC special committee;

the business, financial strength and prospects of NHC as a stand-alone entity;

the absence of firm offers for NHR from unaffiliated persons during the two years prior to the execution of the merger agreement;

the nature of the representations, warranties, covenants and other provisions of NHC and NHR set forth in the draft of the merger agreement and certificate of designations for the NHC preferred stock;

the nature of the proposed consideration consisting of a combination of cash and NHC preferred stock to be paid by NHC upon the consummation of the merger;

the expected U.S. Federal income tax consequences of the merger;

the current and historical market prices of NHR's common stock; as a result of which the merger price represented a 15.9% premium over the price of NHR common stock one day prior to the announcement of the merger and a 17.9% premium over the price of NHR common stock four weeks prior to the announcement of the merger;

the value of NHR based on a precedent transactions analysis, comparable companies analysis, discounted cash flow analysis, dividend discount analysis and net asset value analysis;

the liquidation value of NHR, the replacement cost of NHR's assets, the potential market value of NHR's assets and the benefits to NHC as an operator of long-term health care facilities, of operational control of NHR's assets;

the potential benefits of the contemplated merger with NHR, including the potential realization of (i) a larger asset and equity base, (ii) greater operating flexibility to renovate and expand facilities, (iii) an

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increase in annual recurring free cash flow resulting from the elimination of annual lease payment obligations of NHC to NHR, (iv) benefits arising from a management team focused on NHC's core business and freed of the burden of managing two public companies, (v) increased access to debt financing sources and (vi) reductions in redundant expenses relating to corporate overhead and the costs of managing a public company; and

the potential reduction in NHC's earnings per share resulting from the merger.

Because of the variety of factors considered, neither the NHC special committee nor the NHC board of directors found it practicable to assign relative weights to the specific factors considered in reaching their respective determinations. In approving the merger proposal and the terms of the merger agreement, the NHC relied on the conclusion and analysis of Avondale as to the substantive fairness of the merger.

Based primarily on the procedural safeguards resulting from the establishment and independent function of the NHC special committee and the receipt by such committee of the fairness opinion of Avondale Partners, the NHC board of directors believes that the merger is procedurally fair to NHC's unaffiliated stockholders despite the fact that (i) the terms of the merger agreement do not require the approval of a majority of the unaffiliated NHC stockholders for the consummation of the merger and (ii) no unaffiliated representative has been retained by NHC's non-employee directors to act solely on behalf of unaffiliated security holders for purposes of negotiating the terms of merger or to prepare a report concerning the fairness of the transaction. As stated above, the merger, the merger agreement and each of the transactions contemplated thereby, including the issuance of the Preferred Stock and the submission of the NHC Proposal to the NHC stockholders for consideration was approved by a majority of the non-employee members of the NHC board of directors.

**NHC's Reasons for, and Advantages of, the Merger**

The NHC board of directors' purpose in approving the merger, the merger agreement and each of the transactions contemplated thereby is to provide a larger asset and equity base for NHC, and thereby enhance NHC's future growth and prospects for long term increases in stockholder value. NHC is undertaking the merger at this time in order to capitalize on the expected resulting increase in NHC's annual recurring free cash flow. During the period following the establishment of the NHC special committee in February of 2006 until the execution of the merger agreement on December 20, 2006, the NHC board of directors considered the alternative of continuing as a stand-alone company, but did not consider any other material acquisitions or mergers. The NHC board of directors believes that the merger is advisable and in the best interests of NHC's stockholders based on the following material reasons:

the financial presentation of Avondale Partners to the NHC board of directors on December 20, 2006, and Avondale Partners' opinion addressed to the NHC special committee that the merger consideration to be paid by Davis Acquisition Sub LLC in the merger was fair, from a financial point of view, to both Davis Acquisition Sub LLC and NHC. We have described Avondale Partner's opinion in detail under the heading Special Factors Opinion of NHC's Financial Advisor Avondale Partners, LLC;

the unanimous recommendation of the NHC special committee in favor of the merger and related transactions in light of (i) the composition of the two-member non-employee NHC special committee, each of whom the NHC board of directors had previously determined were unaffiliated with NHR, (ii) the in-depth review of NHR's business, assets, liabilities and financial condition by the NHC special committee, (iii) the protracted arms-length negotiations of the NHC special committee with the NHR special committee and (iv) the retention by the NHC special committee of independent legal and financial advisors possessing experience with transactions similar to the merger to assist the NHC special committee;



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the increase in operating flexibility expected to result from the merger, which will allow NHC to renovate and expand its facilities;

the expected increase in annual recurring free cash flow resulting from the elimination of annual lease payment obligations of NHC to NHR, even after providing for the dividends on the Preferred Stock. In addition, the merger will eliminate the financial uncertainty that resulted from the periodic negotiation and renegotiation of the leasing terms of the properties that NHC leased from NHR;

the benefits arising from a management team focused on NHC's core business and freed of the burden of managing two public companies;

the elimination of the possibility that NHR could be acquired by a competitor of NHC;

the belief that the expected increase in annual recurring free cash flow and larger asset base will allow NHC to more easily access a broader range of debt financing sources and obtain borrowings on improved terms; and

the expected reduction in redundant expenses relating to corporate overhead and the costs of managing a public company.

If the merger is approved and all other conditions to the merger have been satisfied or waived, NHR will merge with and into Davis Acquisition Sub LLC, upon the terms and subject to the conditions set forth in the merger agreement. Upon effectiveness of the merger, the separate corporate existence of NHR shall cease and Davis Acquisition Sub LLC shall continue as the surviving person in the merger and a wholly-owned subsidiary of NHC/OP, L.P., which is a wholly-owned subsidiary of NHC and shall succeed to and assume all the rights and obligations of NHR. As a result, the interest of NHC in NHR's net book value will increase from approximately 3.65% to 100%. This will constitute an approximately \$107,570,000 increase in NHC's interest in NHR's net book value and will entitle NHC to all future income generated by NHR. For U.S. federal income tax purposes, NHC expects the merger to be treated as a taxable asset sale, which would thereby provide the purchaser with a step-up in the tax basis of the acquired assets. NHC expects that the receipt of cash and shares of the Preferred Stock by stockholders of NHR in exchange for their common stock of NHR pursuant to the merger should be a taxable transaction for U.S. federal income tax purposes.

**Disadvantages to NHC of the Merger**

NHC may experience a reduction in its earnings per share as a result of the merger. NHC believes, however, that this potential negative consequence will be offset by the accretive effects that the merger is expected to have on NHC's free cash flow.

**Opinion of NHC's Financial Advisor Avondale Partners, LLC**

At the December 20, 2006 meeting of the NHC special committee, Avondale Partners, LLC (Avondale Partners) rendered its oral opinion to the NHC special committee, subsequently confirmed in writing, to the effect that, as of December 20, 2006, and based upon and subject to certain matters stated therein, the merger consideration to be paid by Davis Acquisition Sub LLC in the merger was fair, from a financial point of view, to both Davis Acquisition Sub LLC and NHC.

**The full text of Avondale Partners' written opinion dated December 20, 2006 delivered to the NHC special committee, which sets forth the assumptions made, procedures followed, matters considered and limitations on the review undertaken, is attached as Annex D to this joint proxy statement/prospectus, and the written**

**opinion is incorporated herein by reference. Holders of NHC common stock are urged to read the opinion carefully and in its entirety.**

The Avondale Partners opinion was rendered at the request of the NHC special committee and for the benefit of the NHC special committee and NHC's full board of directors in their evaluation of the proposed merger.

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The NHC special committee did not impose any limitations on Avondale Partners with respect to the investigations made or procedures followed in rendering its opinion. Further, the NHC special committee did not request the advice of Avondale Partners with respect to alternatives to the merger, and Avondale Partners did not advise the NHC special committee with respect to alternatives to the merger or NHC's underlying decision to proceed with or effect the merger. The opinion addresses only the fairness, from a financial point of view, of the merger consideration to be paid by Davis Acquisition Sub LLC in the merger to both Davis Acquisition Sub LLC and NHC. It does not address the relative merits of the merger as compared to alternative transactions or strategies that may be available to NHC, nor does it address NHC's underlying decision to engage in the merger.

Avondale Partners' opinion does not constitute a recommendation to you or any of NHC's other stockholders as to how you or any other NHC stockholder should vote or act with respect to the NHC Proposal.

Avondale Partners' opinion and its related presentation were among the many factors that the NHC special committee took into consideration in making its determination to approve, and to recommend to NHC's full board of directors that the board of directors approve, the merger and the transactions contemplated thereby. Avondale Partners' opinion was also among the many factors that NHC's board of directors took into consideration in making its determination to approve, and to recommend to NHC's stockholders that they approve, the NHC Proposal. The Avondale Partners opinion should not be viewed as determinative of the views of the NHC special committee or the NHC board of directors with respect to the NHC Proposal. The merger consideration was determined through negotiations between NHC and NHR.

The following description of Avondale Partners' opinion is only a summary of the analyses and examinations that Avondale Partners deemed material to its opinion. It is not a comprehensive description of all analyses and examinations actually conducted by Avondale Partners. The preparation of a fairness opinion necessarily is not susceptible to partial analysis or summary description. Avondale Partners believes that its analyses and the summary set forth below must be considered as a whole and that selecting portions of its analyses and of the factors considered, without considering all analyses and factors, would create an incomplete view of the process underlying the analyses set forth in its presentation to the NHC special committee. In addition, Avondale Partners may have given various analyses more or less weight than other analyses, and may have deemed various assumptions more or less probable than other assumptions. The fact that any specific analysis has been referred to in the summary below is not meant to indicate that this analysis was given greater weight than any other analysis described below and should not be taken to be the view of Avondale Partners with respect to the actual value of NHR.

In performing its analyses, Avondale Partners made numerous assumptions with respect to industry performance, general business and economic conditions and other matters, many of which are beyond the control of NHC or NHR. The analyses performed by Avondale Partners are not necessarily indicative of actual values or actual future results, which may be significantly more or less favorable than those suggested by these analyses. These analyses were prepared solely as part of the analysis performed by Avondale Partners with respect to whether the merger consideration to be paid by Davis Acquisition Sub LLC in the merger is fair, from a financial point of view, to both Davis Acquisition Sub LLC and NHC, and were provided to the NHC special committee in connection with the delivery of Avondale Partners' opinion. The analyses do not purport to be appraisals or to reflect the prices at which a company might actually be sold or the prices at which any securities may trade at any time in the future. The Avondale Partners opinion does not address the number of shares of NHR common stock, if any, to be received by holders of NHR/OP, LP units in the conversion and/or redemption of such units prior to the merger.

No company or transaction used in the comparable company or comparable transaction analyses described below is identical to NHC or NHR or the merger. Accordingly, an analysis of the results of such analyses is not mathematical; rather, it involves complex considerations and judgments concerning differences in financial and operating

characteristics of the companies and other factors that could affect the public trading value of the companies to which NHC, NHR and the merger are being compared.



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***Procedures Followed***

In connection with its opinion, Avondale Partners:

reviewed certain publicly available business and financial information relating to NHC and NHR that Avondale Partners deemed to be relevant;

reviewed the merger agreement and certain exhibits and documents referenced therein;

compared NHR from a financial point of view with certain other companies in the REIT industry that Avondale Partners deemed relevant;

reviewed certain information, including financial forecasts relating to the business and prospects of NHC and NHR, furnished to Avondale Partners by management of NHC and NHR;

considered the financial terms, to the extent publicly available, of selected recent business combinations in the REIT industry that Avondale Partners deemed to be comparable, in whole or in part, to the merger;

interviewed senior management of NHC and NHR regarding each company's operating history and respective prospects;

compared the trading histories of NHC common stock and NHR common stock from December 19, 2005 to December 19, 2006 and reviewed the trading history of NHR common stock from December 19, 2004 to December 19, 2006;

reviewed publicly available premiums paid of certain other transactions Avondale Partners believed to be reasonably comparable to the merger;

reviewed the potential pro forma financial results, financial condition and capitalization of NHC after giving effect to the merger; and

performed other such analyses such as dividend discount and net asset valuation analyses and examinations as Avondale Partners deemed appropriate.

In preparing its opinion, Avondale Partners did not assume any responsibility to independently verify the information referred to above. Instead, with NHC's consent, Avondale Partners relied on the information being accurate and complete. Avondale Partners also made the following assumptions, in each case with NHC's consent, that:

the internal operating data and financial analyses and forecasts supplied to Avondale Partners were reasonably prepared on bases reflecting the best currently available estimates and judgments of NHC and NHR senior management as to NHC's and NHR's recent and likely future performance;

the merger will be consummated on the terms and subject to the conditions described in the merger agreement; and

all necessary governmental and regulatory approvals and third-party consents will be obtained on terms and conditions that will not have a material adverse effect on NHC.

In addition, for purposes of its opinion, Avondale Partners:

relied on advice of NHC counsel and considered the Company's audited financial statements as to legal and financial reporting matters with respect to NHC, the merger and the merger agreement;

did not assume responsibility for making an independent physical inspection or appraisal of any of the assets, properties or facilities of NHR; and

was not authorized to and did not solicit indications of interest from any third party with respect to the purchase of all or part of NHR.

The Avondale Partners opinion was necessarily based upon market, economic, financial and other conditions as they existed on, and could be evaluated as of, the date of its opinion. Any change in such

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conditions would require a reevaluation of the Avondale Partners opinion. Accordingly, although subsequent developments may affect its opinion, Avondale Partners has not assumed any obligation to update or revise its opinion.

***Summary of Financial and Other Analyses***

The following represents a summary of the material financial analyses performed by Avondale Partners in connection with providing its opinion to the NHC special committee. Some of the summaries of financial analyses performed by Avondale Partners include information presented in tabular format. In order to fully understand the financial analyses performed by Avondale Partners, you should read the tables together with the text of each summary. The tables alone do not constitute a complete description of the financial analyses. Considering the data set forth in the tables without considering the full narrative description of the financial analyses, including the methodologies and assumptions underlying the analyses, could create a misleading or incomplete view of the financial analyses performed by Avondale Partners.

*Historical Stock Trading Analysis.* Avondale Partners reviewed the historical stock prices and trading characteristics over the last two years of NHR common stock. The following table compares the merger price with various closing prices and averages over the last two years:

**Prices as of 12/19/2006**

|                 |          |
|-----------------|----------|
| Merger Price    | \$ 24.75 |
| 1 Week Average  | \$ 21.10 |
| 1 Month Average | \$ 21.05 |
| 3 Month Average | \$ 20.63 |
| 9 Month Average | \$ 19.30 |
| 1 Year Average  | \$ 19.34 |
| 1 Year High     | \$ 21.35 |
| 2 Year Average  | \$ 19.31 |
| 2 Year High     | \$ 21.35 |

*Volume of Shares Traded Analysis.* Avondale Partners reviewed the historical prices and historical trading activity of NHR common stock over the one-year and two-year time periods ended December 19, 2006. Avondale Partners calculated the total number of shares traded at certain share price ranges over the one year period ended December 19, 2006 beginning with \$16.75 to \$17.00 and increasing at \$0.25 increments to \$21.00 to \$21.25. Avondale Partners calculated the total number of shares traded at certain share price ranges over the two year period ended December 19, 2006 beginning with \$16.75 to \$17.00 and increasing at \$0.25 increments to \$21.00 to \$21.25. Avondale Partners observed that no shares traded above the merger price of \$24.75 per share in either the one year or two year time period ended December 19, 2006.

*Premiums Paid Analysis.* Avondale Partners reviewed the premiums paid for all REIT transactions where 100% of the target's shares were being acquired and other public transactions in the precedent acquisitions analysis for transactions with enterprise values ranging from \$100 to \$500 million for deals announced and closed between January 1, 2004 and December 15, 2006.

Avondale Partners calculated the premiums paid in these transactions over the applicable stock price of the acquired company one day, one week and four weeks prior to the announcement of the respective acquisition offer.

|              | <b>Premium One Day<br/>Prior<br/>to Announcement</b> | <b>Premium One<br/>Week<br/>Prior<br/>to Announcement</b> | <b>Premium Four Weeks<br/>Prior to<br/>Announcement</b> |
|--------------|--|---|---|
| High         | 58.0%  | 60.9%   | 66.2%   |
| Low          | (3.7)%   | (2.1)%  | (2.6)%  |
| Deal Premium | 15.9%  | 17.6%   | 17.9%   |

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Avondale Partners calculated the implied range of company share prices based on the NHC common stock price as of December 20, 2006 and the range of premiums paid for the selected time periods in the selected transactions. The range of premiums paid over the price of the acquired companies' share prices one day, one week and four weeks prior to announcement implied an equity value per share ranges of \$20.56 to \$33.74, \$20.62 to \$33.87 and \$20.45 to \$34.90, respectively, which compare to the merger price of \$24.75 per share.

*Precedent Transactions Analysis.* Based on public and other available information, Avondale Partners calculated the multiples of enterprise value (which Avondale Partners defined as equity value, plus debt, plus preferred stock, plus minority interest, less cash and cash equivalents) to last twelve months (LTM) revenues, as well as multiples of equity value to LTM funds from operations (FFO) implied in the following acquisitions of companies in the REIT industry announced since October 1, 2005:

| <b>Date Announced</b> | <b>Name of Acquiror</b>                             | <b>Name of Target</b>               |
|-----------------------|---|-------------------------------------|
| 8/21/2006             | Morgan Stanley Real Estate                          | Glenborough Realty Trust, Inc.      |
| 8/8/2006              | Revenue Properties Co Ltd                           | Sizeler Property Investors, Inc.    |
| 7/10/2006             | Kimco Realty Corp                                   | Pan Pacific Ret Property, Inc.      |
| 7/9/2006              | Centro Properties Group                             | Heritage Property Invest Trust Inc. |
| 6/5/2006              | Brookfield Properties Corp. and Blackstone Group LP | Trizec Properties Inc.              |
| 5/19/2006             | Braveheart Holdings LP                              | Boykin Lodging Co.                  |
| 5/2/2006              | Health Care Property Investors Inc                  | CNL Retirement Properties, Inc.     |
| 3/6/2006              | Blackstone Group LP                                 | CarrAmerica Realty Corp.            |
| 2/21/2006             | Blackstone Group LP                                 | MeriStar Hospitality Corp.          |
| 2/10/2006             | LBA Realty LLC                                      | Bedford Property Investors, Inc.    |
| 12/22/2005            | GE Capital Real Estate                              | Arden Realty Inc.                   |
| 12/19/2005            | Magazine Acquisition GP LLC                         | Town & Country Trust                |
| 12/7/2005             | CalEast Industrial Investors                        | CenterPoint Properties Trust        |
| 10/24/2005            | Prime Property Fund                                 | Amlri Residential Property Trust    |

The following table sets forth the multiples indicated by this analysis and the multiples implied by the proposed merger:

| <b>Enterprise Value to:</b> | <b>Proposed Transaction Multiples</b> | <b>Low</b> | <b>High</b> |
|-----------------------------|---------------------------------------|------------|-------------|
| LTM Revenues                | 13.0x                                 | 2.0x       | 14.7x       |
| LTM FFO                     | 14.5x                                 | 13.3x      | 37.8x       |

Avondale Partners also calculated the implied company share price based on the range of revenue and FFO valuation multiples based on the precedent transactions analysis. This calculation resulted in an implied equity value per share range of \$4.34 to \$64.70 which compares to the merger price of \$24.75 per share.

*Comparable Company Analysis.* Based on public filings and other publicly available information, Avondale Partners calculated the multiples of enterprise value (which Avondale Partners defined as equity value, plus debt, plus

preferred stock, plus minority interest, less cash and cash equivalents) to the LTM, estimated calendar year 2006 (CY 2006), and estimated calendar year 2007 (CY 2007) revenues, and equity value to the LTM, estimated CY 2006, and estimated CY 2007 earnings per share (EPS) and funds from operations per share for companies in the REIT industry. Avondale Partners indicated that the companies listed below have some operations similar to some of the operations of NHR, but noted that none of these companies have the same management, composition, size, or combination of businesses as NHR:

Health Care Property Investors, Inc.

Health Care REIT, Inc.

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Healthcare Realty Trust, Inc.

LTC Properties, Inc.

Medical Properties Trust

National Health Investors Inc.

Nationwide Health Properties, Inc.

Omega Healthcare Investors, Inc.

Senior Housing Properties Trust

Universal Health Realty Income Trust

Ventas Inc.

The following table sets forth the multiples indicated by this analysis:

| <b>Enterprise Value to:</b>     | <b>Proposed<br/>Transaction<br/>Multiples</b> | <b>Low</b> | <b>High</b> |
|---------------------------------|---|------------|-------------|
| LTM Revenue                     | 13.0x   | 5.4x       | 17.5x       |
| Estimated CY 2006 Revenues      | 13.3x   | 10.1x      | 15.7x       |
| Estimated CY 2007 Revenues      | 13.1x   | 8.2x       | 14.1x       |
| LTM FFO per share               | 14.5x   | 11.9x      | 18.4x       |
| Estimated CY 2006 FFO per share | 14.8x   | 13.2x      | 18.2x       |
| Estimated CY 2007 FFO per share | 14.5x   | 10.9x      | 16.8x       |
| LTM EPS                         | 20.7x   | 13.7x      | 45.2x       |
| Estimated CY 2006 EPS           | 21.2x   | 14.6x      | 39.9x       |
| Estimated CY 2007 EPS           | 20.2x   | 15.9x      | 41.6x       |

Avondale Partners also calculated the implied company share price based on the range of revenue, P/E and Price/FFO valuation multiples based on the comparable company analysis. The range of revenue, P/E and Price/FFO multiples implied equity value per share ranges of \$10.63 to \$33.14, \$16.43 to \$54.30, and \$18.58 to \$31.40, respectively, which compare to the merger price of \$24.75 per share.

*Discounted Cash Flow Analysis.* Avondale Partners performed a discounted cash flow analysis for the projected cash flows of NHR for the fiscal years ending December 31, 2007 through December 31, 2009, using projections and assumptions provided by NHR management, which projections were prepared for the purposes of these analyses. Avondale Partners used a range of discount rates (9.0% to 13.0%) and perpetuity growth rates (0.0% to 4.0%) on forecasted free cash flow for the fiscal year ending December 31, 2009 to calculate a range of implied equity values per share of NHR common stock. The following table sets forth the implied values indicated by this analysis:

(\$ in millions, except per share data)

|                          | Low      | High     |
|--------------------------|----------|----------|
| Implied Enterprise Value | \$ 162.8 | \$ 376.8 |
| Implied Equity Value     | \$ 169.9 | \$ 383.9 |
| Implied Price per Share  | \$ 15.20 | \$ 34.35 |

This analysis resulted in an implied equity value per share range of \$15.20 to \$34.35 which compares to the merger price of \$24.75 per share.

*Dividend Discount Analysis.* Avondale Partners performed a dividend discount analysis to calculate an implied stock price, using projections and assumptions provided by NHR management which projections were prepared for the purposes of these analyses. Avondale Partners used a range of discount rates (10.0% to 12.0%) and dividend growth rates (0.5% to 4.5%) based on historical dividend growth rates to calculate a



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range of implied equity values per share. The following table sets forth the implied values indicated by this analysis:

**(\$ in millions, except per share data)**

|                          | <b>Low</b> | <b>High</b> |
|--------------------------|------------|-------------|
| Implied Enterprise Value | \$ 131.9   | \$ 283.5    |
| Implied Equity Value     | \$ 139.0   | \$ 290.6    |
| Implied Price per Share  | \$ 12.43   | \$ 26.00    |

This analysis resulted in an implied equity value per share range of \$12.43 to \$26.00 which compares to the merger price of \$24.75 per share.

*Net Asset Value Analysis.* Avondale Partners performed a net asset value analysis to calculate an implied stock price. For this analysis, Avondale Partners applied a range of capitalization rates (7.0% to 13.5%) to annualized adjusted net operating income (net operating income, less capital expenditures). The resulting gross real estate values were combined with cash and cash equivalents, marketable securities, and mortgage notes and other notes receivable to arrive at total asset values. Total debt was then subtracted from such total asset values to arrive at estimated net asset values. The resulting estimated net asset values were then divided by the diluted shares outstanding to arrive at an estimated net asset values per share. In applying the range of capitalization rates, Avondale Partners took into consideration current market conditions. The following table sets forth the implied values indicated by this analysis:

**(\$ in millions, except per share data)**

|                          | <b>Low</b> | <b>High</b> |
|--------------------------|------------|-------------|
| Implied Enterprise Value | \$ 198.5   | \$ 370.3    |
| Implied Equity Value     | \$ 205.6   | \$ 377.3    |
| Implied Price per Share  | \$ 18.39   | \$ 33.76    |

This analysis resulted in an implied equity value per share range of \$18.39 to \$33.76 which compares to the merger price of \$24.75 per share.

*Pro Forma Merger Analysis.* In the course of preparing its opinion, Avondale Partners also reviewed and considered other information and data, including the potential pro forma effect of the merger on the pro forma combined company's estimated earnings per share, as well as cash flow per share (which is cash flow from operations less capital expenditures) in calendar years 2007, 2008 and 2009 after giving effect to potential cost savings and other synergies anticipated to result from the merger developed jointly by NHC and NHR and compared that data to the estimated earnings per share of NHC on a standalone basis. Such analysis indicated that, after giving effect to potential cost savings and other synergies, the merger would be dilutive to the pro forma earnings per share of NHC by (10.5%), (8.9%), and (7.4%) respectively in calendar years 2007, 2008, and 2009. Such analysis also indicated that, after giving effect to potential cost savings and other synergies, the merger would be accretive to pro forma cash flow per share of NHC by 16.2%, 14.0%, and 12.8% respectively in calendar years 2007, 2008, and 2009.

**General**

The NHC special committee selected Avondale Partners to render a fairness opinion to the NHC special committee with respect to the fairness, from a financial point of view, of the merger consideration to be paid by Davis Acquisition Sub LLC in the merger to both Davis Acquisition Sub LLC and NHC. During the selection process, the

NHC special committee met with representatives of several investment banking firms active in the healthcare and REIT industries and collected proposals from two such entities. In its search, the NHC special committee focused on (i) the reputation of each firm and its experience in the healthcare and REIT industries, (ii) the professional experience of each representative that would be assigned to work on the project and (iii) the relative costs of such services. Based on Avondale's expertise and reputation in investment banking and mergers and acquisitions, as well as in the healthcare and REIT industries, and the other considerations mentioned above, the NHC special committee selected Avondale from among the firms considered. Prior to the selection of Avondale Partners to render the fairness opinion in connection with the merger, Avondale did not have any material relationship with NHC. Avondale Partners is a nationally

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recognized investment banking firm regularly engaged in the valuation of businesses and their securities in connection with mergers and acquisitions, leveraged buyouts, negotiated underwritings, secondary distributions of listed and unlisted securities and private placements.

Avondale Partners became entitled to a fixed fee of \$200,000 upon its completion of the work necessary to render its opinion, regardless of the conclusion reached therein. No portion of Avondale Partner's fee was contingent upon consummation of the merger. Further, NHC reimbursed Avondale Partners for its reasonable out-of-pocket expenses incurred in connection with its engagement, including reasonable attorneys' fees, and agreed to indemnify Avondale Partners, its affiliates, and their respective partners, directors, officers, agents, consultants, employees and controlling persons against specific liabilities, including liabilities under applicable securities laws.

Avondale Partners was engaged to render its opinion with respect to the fairness, from a financial point of view, of the merger consideration to be paid by Davis Acquisition Sub LLC in the merger. Avondale Partners was not requested to, and did not, determine the consideration to be paid in the merger or participate in any discussion in negotiations relating to the merger. In the ordinary course of its business, Avondale Partners may trade in the equity securities of NHC or NHR for its own account and for the accounts of customers and, accordingly, may at any time hold a long or short position in these securities.

**Recommendations of the NHR Special Committee and the NHR Board of Directors; Fairness of the Offer and the Merger**

The NHR special committee and board of directors believe that the merger is advisable and in the best interests of NHR's stockholders, including its unaffiliated stockholders. On December 20, 2006, the NHR special committee to the NHR board of directors unanimously recommended to the board of directors, after giving consideration to the presentation of its legal advisors regarding Maryland law and the fairness opinion of 2nd Generation, which was the independent financial advisor to the special committee, that the merger agreement was fair, in the best interests of NHR and its stockholders and should be unanimously recommended to the board of directors of NHR for approval. Based on this recommendation, the presentation of the fairness opinion by 2nd Generation, and other factors considered by the board of directors, the NHR board of directors approved the merger agreement and recommended that it was advisable and in the best interest of NHR and its stockholders that NHR consolidate with a wholly owned subsidiary and subsequently merge with and into the Davis Acquisition Sub LLC, on substantially the terms and conditions set forth in the merger agreement and that the stockholders approve the consolidation and the merger.

The NHR special committee and board of directors considered a number of material factors, which in the opinion of NHR board members, supported the NHR special committee's and board of directors' determination that the merger (including the pre-merger consolidation of NHR) is substantively fair to NHR's stockholders, including its unaffiliated stockholders:

the financial presentation of 2nd Generation to the NHR board of directors on December 20, 2006 and 2nd Generation's opinion addressed to the NHR special committee that the merger consideration to be paid by Davis Acquisition Sub LLC in the merger was fair, from a financial point of view, to the stockholders of NHR. We have described 2nd Generation's opinion in detail under the heading "Special Factors - Opinion of NHR's Financial Advisor 2nd Generation." The NHR board of directors was not aware of and did not consider any financial reports, opinions or appraisals received by any other filing person in connection with its deliberations;

the unanimous recommendation of the NHR special committee in favor of the merger and related transactions in light of (i) the composition of the two-member non-employee NHR special committee, each of whom the NHR board of directors had previously determined were unaffiliated with NHC, (ii) the review of NHR's and NHC's business, assets, liabilities and financial condition by the NHR special committee, (iii) the protracted

arms-length negotiations of the NHR special committee with the NHC special committee and (iv) the retention by the NHR special committee of independent legal and financial advisors possessing experience with transactions similar to the merger to assist the NHR special committee;

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the business, financial strength and prospects of NHR as a stand-alone entity was viewed less favorably when compared to the value of the merger consideration and participation with a larger NHC entity because of NHR's history of no acquisitions and limited growth;

the nature of the representations, warranties, covenants and other provisions of NHC and NHR set forth in the draft of the merger agreement and certificate of designations for the NHC preferred stock were negotiated by the NHR special committee to protect the interests of NHR and its stockholders and, therefore, were viewed as supporting the fairness of the merger;

the nature of the proposed consideration consisting of a combination of cash and NHC preferred stock to be paid by NHC upon the consummation of the merger, which was considered by the NHR special committee and the NHR board of directors to be favorable to the NHR stockholders based on the financial analysis of 2nd Generation and the opportunity for stockholders to receive a substantial amount of cash per share of NHC common stock and participate through the NHC preferred stock in the future of the merger entity;

the current and historical market prices of NHR's common stock; as a result of which the merger price represented a 15.9% premium over the price of NHR common stock one day prior to the announcement of the merger and a 17.9% premium over the price of NHR common stock four weeks prior to the announcement of the merger;

based on a precedent transactions analysis, comparable companies analysis, discounted cash flow analysis, dividend discount analysis and net asset value analysis conducted by 2nd Generation on which the NHR special committee and NHR board of directors relied, the estimated going concern value of NHR, as a stand-alone entity, was less favorable than the proposed merger consideration. 2nd Generation used the above tests as a means of determining the estimated going concern value because these methods are generally accepted by appraisers for such purpose and in the opinion of 2nd Generation were the best evidence of going concern value of NHR in the circumstances; and

the potential benefits of the contemplated merger with NHC, including the potential realization of (i) a larger asset and equity base for NHC, (ii) greater operating flexibility of NHC to renovate and expand facilities, (iii) an increase in annual recurring free cash flow resulting from the elimination of annual lease payment obligations of NHC to NHR, (iv) benefits arising from a management team focused on NHC's core business and freed of the burden of managing two public companies, (v) increased access to debt financing sources and (vi) reductions in redundant expenses relating to corporate overhead and the costs of managing NHR as a public company.

The NHR special committee and board of directors considered the following factors that negatively affected the fairness determination:

the expected U.S. Federal income tax consequences of the merger, which will likely result in a taxable transaction to the NHR stockholders, and

the potential reduction in NHC's earnings per share resulting from the issuance of the NHC preferred stock in the merger;

however, the NHR special committee and board of directors did not believe such factors materially affected the fairness determination because the transaction would be accretive to NHC in terms of cash flow and the premium paid for NHR common stock would be comparable to premiums paid in other taxable transactions involving cash as

consideration.

Because of the variety of factors considered, neither the NHR special committee nor the NHR board of directors found it practicable to assign relative weights to the specific factors considered in reaching their respective determinations. The NHR special committee and board of directors expressly adopted and are relying on the analyses and conclusions of 2nd Generation as presented below.

The NHR special committee and board of directors believe that the merger is procedurally fair to NHR's unaffiliated stockholders, primarily based on the fact that (i) the terms of the merger agreement require the

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approval of a majority of the unaffiliated NHR stockholders for the consummation of the merger and (ii) 2nd Generation, as an unaffiliated representative, was retained by NHR's special committee of independent directors to act on behalf of unaffiliated security holders for purposes of assisting in the negotiation of the terms of merger or to prepare a report concerning the fairness of the transaction. As stated above, the merger, the merger agreement and each of the transactions contemplated thereby and the submission of the NHR Proposal to the NHR stockholders for consideration was approved by a majority of the non-employee members of the NHR board of directors.

The NHR special committee and board of directors did not consider the following factors to be materially relevant to its determinations set forth above, for the following reasons:

**Net Book Value** The NHR special committee and board of directors did not consider the Company's net book value, which is an accounting concept, to be material to the conclusion regarding the fairness of the merger because they believed that net book value is not a material indicator of the value of the Company as a going concern, but rather is indicative of historical cost. Because, as with NHR, real property is the primary asset of a REIT and the historical cost of such real property generally does not reflect the current value, net book value is seldom used as a measurement of value in NHR's industry.

**Liquidation Value** In the course of reaching its decision to approve the merger agreement, NHR's special committee and board of directors did not consider the liquidation value of NHR's assets. Liquidation value does not take into account existing tenant relationships and other operational efficiencies of a REIT that may not be immediately available to the purchaser or purchasers of NHR's properties and other assets in a liquidation; therefore, the NHR special committee and board of directors believed that the liquidation value would be lower than the Company's value as a viable going concern. As discussed above, the estimated going concern value of NHR was determined by 2nd Generation to be less than the proposed merger consideration. As a result, the NHR special committee and board of directors did not consider the liquidation value of the NHR assets.

**Purchase prices paid for NHR common stock over the past two years by persons filing the Schedule 13e-3 related to this transaction** There have been no such purchases known to the NHR board of directors, so it did not consider this in the course of reaching its decision to approve the merger agreement and did not consider it as relevant to a determination of fairness.

**Firm offers of which NHR or any of the filing persons are aware made by any unaffiliated person, other than the filing persons, during the past two years for a merger or consolidation involving NHR, or the sale or other transfer of all or any substantial part of the assets of NHR, or a purchase of NHR securities that would enable the holder to exercise control of the NHR** There have been no such offers known to the NHR board of directors, so it did not consider this in the course of reaching its decision to approve the merger agreement and did not consider it as relevant to a determination of fairness.

## **NHR's Reasons for, and Advantages of, the Merger**

The following outline of factors considered by the NHR board of directors is not intended to be exhaustive, but includes the material factors considered by the NHR board of directors.

1. The merger consideration represents a premium on the trading price of NHR common stock. The face value of the per share merger consideration (a cash payment of \$9.00 and a share of Preferred Stock with a liquidation preference of \$15.75) represents (1) a 17.5% premium over the average of the closing prices of NHR stock on the 20 trading days prior to the merger announcement (\$21.07), (2) a 10% increase over NHC's initial proposal and (3) a 16.3% premium over the closing price of NHR common stock on December 20, 2006, the last trading day prior to the announcement

of the merger agreement.

2. The merger will provide the stockholders of NHR with ownership in a company with a larger and more diversified asset and equity base, and with greater access to capital.



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3. The merger allows the stockholders of NHR to receive the Preferred Stock with many of the same dividend characteristics as the NHR stock, but with a greater potential for growth and appreciation.

4. Following the merger, NHC and NHR expect to achieve operational efficiencies and eliminate duplication of functions between the two companies.

**Disadvantages to NHR of the Merger**

The following disadvantages to completing the merger were considered by the NHR special committee and the board of directors of NHR:

1. The merger will constitute a taxable event for the stockholders of NHR.
2. The merger will change the character of the investment for the NHR stockholder from an investment in a REIT with stable dividends to an investment in a more volatile growth-oriented stock.
3. As a REIT, the dividends paid by NHR are taxed only at the stockholder level; however, dividends paid following the merger may be subject to taxation at both the corporate level and stockholder level.

**Opinion of NHR's Financial Advisor 2nd Generation Capital, LLC**

Pursuant to an engagement letter dated October 16, 2006, NHR retained 2nd Generation as its financial advisor in connection with the proposed merger. At the meeting of the NHR special committee on December 20, 2006, 2nd Generation rendered its oral opinion, subsequently confirmed in writing, to the NHR special committee that, as of such date and based upon and subject to the factors, limitations and assumptions set forth in its opinion, the merger consideration in the proposed merger was fair, from a financial point of view, to holders of NHR common stock.

No limitations were imposed by the NHR board of directors or the NHR special committee upon 2nd Generation that, in the opinion of 2nd Generation, unreasonably restricted its procedures or resultant opinion. 2nd Generation's opinion notes that it was not authorized to and did not solicit any expressions of interest from any other parties with respect to the sale of all or any part of NHR or any other alternative transaction.

**The accompanying full text of the written opinion of 2nd Generation, dated December 20, 2006, attached as Exhibit E to this joint proxy statement/prospectus, sets forth, among other things, the assumptions made, procedures followed, matters considered and limits on the opinion and review undertaken in connection with rendering its opinion. Holders of NHR common stock are urged to read the opinion in its entirety. 2nd Generation's opinion is addressed to the special committee of the NHR board of directors and does not constitute a recommendation to any stockholder of NHR as to how such stockholder should vote with respect to the proposed merger or any other matter. 2nd Generation's opinion does not address the underlying decision by NHR or its board of directors to engage in the proposed merger.**

In arriving at its opinion, 2nd Generation, among other things:

Reviewed a draft dated December 19, 2006 of the merger agreement;

Reviewed certain publicly available financial statements and other business and financial information of NHR, National Health Investors, Inc., and NHC;

Reviewed certain internal financial statements and other financial and operating data concerning NHR as well as estimates and financial forecasts for NHR, NHC, and the combined entity;

Discussed the past and current operations, financial conditions and prospects of NHR with senior management of NHR, National Health Investors, Inc., and NHC;

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Reviewed information and discussed with senior management of NHR, National Health Investors, Inc., and NHC information relating to certain strategic implications and financial benefits anticipated as a result of the transaction;

Reviewed certain publicly available information regarding other companies that it believed to be comparable to NHR and the stock trading data for certain of such other companies' securities;

Reviewed certain publicly available information concerning the nature and terms of certain other transactions that it considered relevant to its inquiry;

Reviewed current and historical market prices and trading volumes of NHR common stock; and

Reviewed convertible preferred stock and convertible corporate bond markets.

2nd Generation also held discussions with certain members of the managements of NHR and NHC with respect to certain aspects of the proposed merger, the past and current business operations of NHR and NHC, the financial condition and future prospects and operations of NHR and NHC, the effects of the proposed merger on the financial condition and future prospects of NHR and NHC, and certain other matters 2nd Generation believed necessary or appropriate to its inquiry. In rendering its opinion, 2nd Generation relied upon and assumed, without assuming responsibility or liability for independent verification, the accuracy and completeness of all information that was publicly available or was furnished to or discussed with 2nd Generation by NHR and NHC or otherwise reviewed by or for 2nd Generation. 2nd Generation did not conduct and was not provided with any valuation or appraisal of any assets or liabilities, and 2nd Generation did not evaluate the solvency of NHR or NHC under any state, federal or foreign laws relating to bankruptcy, insolvency or similar matters.

In relying on analyses and forecasts provided to it, including the synergies, 2nd Generation assumed that such analyses and forecasts were reasonably prepared based on assumptions reflecting the best currently available estimates and judgments by management as to the expected future results of operations and financial condition of NHR and NHC to which such analyses or forecasts related. 2nd Generation expressed no view as to such analyses or forecasts, including the synergies, or the assumptions on which they were based. 2nd Generation has also assumed that the proposed merger will have the tax consequences described in discussions with, and materials furnished to 2nd Generation by, representatives of NHR, and that the other transactions contemplated by the merger agreement will be consummated as described in the merger agreement, and that the definitive merger agreement will not differ in any material respects from the draft thereof furnished to 2nd Generation. 2nd Generation relied as to all legal matters relevant to rendering its opinion upon the advice of counsel. 2nd Generation further assumed that all material governmental, regulatory or other consents and approvals necessary for the consummation of the merger would be obtained without any waiver of any condition to the completion of the merger contained in the merger agreement.

2nd Generation's opinion is necessarily based on economic, market and other conditions as in effect on, and the information made available to 2nd Generation as of, December 19, 2006. It should be understood that subsequent developments may affect 2nd Generation's opinion and that 2nd Generation does not have any obligation to update, revise or reaffirm its opinion. 2nd Generation's opinion is limited to the fairness, from a financial point of view, to holders of NHR common stock of the merger consideration in the proposed merger, and 2nd Generation has expressed no opinion as to the fairness of the proposed merger to, or any consideration of, the holders of any other class of securities, creditors or constituencies of NHR, or as to the underlying decision by NHR to engage in the proposed merger. 2nd Generation expressed no opinion as to the price at which NHR common stock, NHC common stock, or shares of the Preferred Stock would trade at any future time.

***Summary of Financial Analyses Conducted by 2nd Generation***

In connection with rendering its opinion to the NHR special committee, 2nd Generation performed a variety of financial and comparative analyses, including those described below. The summary set forth below does not purport to be a complete description of the analyses or data presented by 2nd Generation. The preparation of a fairness opinion is a complex process and is not necessarily susceptible to partial analysis or

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summary description. 2nd Generation believes that the summary set forth below and its analyses must be considered as a whole and that selecting portions thereof, or focusing on information in tabular format, without considering all of its analyses and the narrative description of the analyses, could create an incomplete view of the processes underlying its analyses and opinion. The order of analyses described does not represent the relative importance or weight given to those analyses by 2nd Generation. In arriving at its fairness determination, 2nd Generation considered the results of all the analyses and did not attribute any particular weight to any factor or analysis considered by it; rather, 2nd Generation arrived at its opinion based on the results of all the analyses undertaken by it and assessed as a whole. 2nd Generation's analyses are not necessarily indicative of actual values or actual future results that might be achieved, which values may be higher or lower than those indicated. Moreover, 2nd Generation's analyses are not and do not purport to be appraisals or otherwise reflective of the prices at which businesses actually could be bought or sold. Except as otherwise noted, the following quantitative information, to the extent that it is based on market data, is based on market data as it existed on or before December 19, 2006 and is not necessarily indicative of current market conditions. 2nd Generation's opinion and financial analyses were only one of the many factors considered by the special committee in its evaluation of the proposed merger and should not be viewed as determinative of the views of the special committee or management with respect to the proposed merger or the merger consideration. The consideration was determined through negotiation between NHR and NHC.

The financial analysis is divided into two parts: determining the estimated value of the merger consideration and comparing that value to ranges of value produced by various valuation techniques.

*Estimated Value of the Merger Consideration:* The merger agreement calls for each NHR stockholder to receive a combination of cash and stock as follows:

\$9.00 in cash; and

\$15.75 face value of the Preferred Stock with \$0.80 annual dividend (5.09%).

Subject to conditions specified in the Preferred Stock's draft certificate of designations dated December 19, 2006, each share of Preferred Stock:

is convertible into 0.24204 shares of NHC common stock with an initial conversion price of \$65.07; and

has call protection that at assures at minimum realizable amount of \$65.07 per as-if converted share of Preferred Stock.

*Methodology:* 2nd Generation estimated the theoretical value of the Preferred Stock and added that to the \$9.00 cash component. 2nd Generation estimated the theoretical value of the Preferred Stock by evaluating its notional bond-like characteristics plus an equity option feature. 2nd Generation calculated a theoretical value for a notional bond that has the features of the Preferred Stock and then calculated a theoretical value of an option that had the equity features of NHC common stock.

*Notional Bond Value:* 2nd Generation calculated the theoretical value of a five-year callable bond with \$0.80 dividend payments and face value of \$15.75. 2nd Generation estimated the yield of this theoretical bond by examining the current yields of Ba2-rated bond issues of similar size. 2nd Generation determined that 7% is a representative market yield for a callable bond with a Ba2 credit rating. While yields for preferred stock are typically higher than yields for bonds of the same rating, the very low debt-to-equity ratio of NHC (approximately 5% NHC debt-to-equity compared to an industry average of over 90%) suggested that bonds were more appropriate comparable securities than preferred stock for the purpose of determining the discount rate. The leverage of a company is a key factor in determining the future dividend payment risk to a preferred stock holder. The claim that the security (issued to NHR

shareholders) would have on NHC cash flows (that would be used to pay future dividends) is more comparable to debt instruments of comparable companies rather than preferred stock comparables. Comparable companies with preferred stock outstanding and leverage as low as NHC were not found. It is possible that NHC may incur debt in the future that has preference to the preferred stock, which would increase the risk of the dividend payments; however, the option value of the security would most likely increase because of the potential increase in earnings that theoretically would result from an infusion of capital into the company. 2nd Generation performed an analysis of NHC's post-merger

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financial characteristics and, with input from NHR management, evaluated established debt-rating guidelines and concluded the Ba2 rating to be appropriate. The notional bond value using this yield is \$14.51. This value does not consider the likely lower stockholder tax rate on dividends compared to tax rate on interest payments.

The value to a hypothetical buyer of the call protection feature was taken into account by examining actual trading of comparable bonds with similar yields that also had a call protection features. Therefore 2nd Generation believes that the notional bond value of \$14.51 is reasonable.

*Option Value:* 2nd Generation used the Black-Scholes method to calculate the option value of the conversion feature of the Preferred Stock. This method requires the following inputs, which include assumptions 2nd Generation deems reasonable in the circumstances:

Current price: \$56.30 as of December 19, 2006

Conversion price: \$65.07 as set by the Preferred Stock's certificate of designations

Time: five years based upon expected call or conversion after that time

Interest rate: 4.56%, based upon current five-year Treasury note yields

Volatility: 39.9%, based on Bloomberg calculated annual volatility

Expected NHC dividend payments

This calculation produces an option value of \$18.40; the 0.24204 conversion rate results in a value of \$4.45 before consideration of any discounting factors. 2nd Generation concluded, however, that discounting of this \$4.45 value was appropriate for the following reasons:

Blockage discount, as a large number of share of the Preferred Stock that would potentially convert to NHC common stock at the same time relative to the average volume of NHC common stock; and

The features of the Preferred Stock are not the same as an actual option and cannot be traded as a detachable option.

For these reasons, 2nd Generation determined a 40% liquidity discount to be appropriate in the circumstances and applied that discount to the initially calculated \$4.45 option value of the Preferred Stock, arriving at an adjusted calculated option value of \$2.67 per share. A general range for a discount for the lack of marketability, or liquidity discount, is 20-40%, according to the major studies most often referred to by business valuation experts. Factors that were used to determine the value within this range include the size of the block of the security issued to NHR shareholders and potential illiquidity of the security, relative inability of security holders individually and as a class to determine or affect strategic decisions of the issuer, the holding period of the option in that the security holder must hold the option as long as the holder owns the security and inability to put the option to the company. These factors suggested a liquidity discount at the high end of the generally accepted range.

*Total Value:* 2nd Generation estimated the value of the merger consideration as a sum of the theoretical notional bond value, plus the calculated option value, and plus cash, and arrived at a total value of \$26.18. This represents a 22.6% premium over the NHR share price of \$21.35 as of December 19, 2006.

## ***Merger Consideration Fairness Analysis***

In order to determine the fairness of the merger consideration, 2nd Generation considered typical financial analysis techniques and then selected as appropriate in the circumstances the following for application:

Historical Price Analysis of NHR Common Stock

Publicly-Traded Comparable Company analysis

Dividend Discount Model analysis

Discounted Cash Flow (DCF) analysis



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Precedent Acquisition and Premiums Paid analysis

Net Asset Value analysis

*Historical Stock Trading Analysis:* 2nd Generation's analysis of the performance of NHR common stock comprised a historical analysis of their respective trading prices over one-year, two-year, and five-year time periods prior to December 19, 2006. During the one-year period, NHR common stock achieved a closing price high of \$21.35 per share and a closing price low of \$16.36 per share. During the two-year period, NHR common stock achieved a closing price high of \$21.35 per share and a closing price low of \$15.97 per share. During the five-year period, NHR common stock achieved a closing price high of \$21.35 per share and a closing price low of \$9.19 per share. 2nd Generation noted that the value of NHR common stock as calculated using the daily closing prices of over the above and other time periods were as follows:

| Period           | Period<br>Start Date | Average<br>Volume | Average<br>Close | Daily Closing Price |          |
|------------------|----------------------|-------------------|------------------|---------------------|----------|
|                  |                      |                   |                  | High                | Low      |
| Latest Month     | 11/17/06             | 3,018             | \$ 21.05         | \$ 21.35            | \$ 20.80 |
| Latest 3 Months  | 9/19/06              | 3,968             | \$ 20.60         | \$ 21.35            | \$ 19.57 |
| Latest 6 Months  | 6/19/06              | 7,919             | \$ 19.55         | \$ 21.35            | \$ 16.75 |
| Latest 12 Months | 12/19/05             | 8,988             | \$ 18.83         | \$ 21.35            | \$ 16.36 |
| Latest 2 Years   | 12/17/04             | 8,881             | \$ 18.11         | \$ 21.35            | \$ 15.97 |
| Latest 5 Years   | 12/19/01             | 9,300             | \$ 15.10         | \$ 21.35            | \$ 9.19  |
| Since Inception  | 1/5/98               | 8,761             | \$ 10.96         | \$ 21.35            | \$ 3.53  |

As of: December 19, 2006

The purpose of this historical stock trading analysis is to provide a measure of the relative market values of NHR common stock for the periods specified. 2nd Generation did observe that as of December 19, 2006, the NHR share price was at its all-time high.

2nd Generation performed a similar analysis of NHC historical prices. During the one-year period, NHC common stock achieved a closing price high of \$58.68 per share and a closing price low of \$36.29 per share. During the two-year period, NHR common stock achieved a closing price high of \$58.68 per share and a closing price low of \$29.18 per share. During the five-year period, NHR common stock achieved a closing price high of \$58.68 per share and a closing price low of \$13.66 per share. The historical high stock price for NHC of \$58.68 occurred on November 16, 2006.

2nd Generation calculated the ratio of the stock price of NHR to NHC currently, one year ago, two years ago, and five years ago:

Current: 0.3792

One year ago: 0.4921

Two years ago: 0.5277

Five years ago: 0.7005

These declining ratios from five years ago to December 19, 2006 reflect that the value of NHR continued to trend down relative to NHC.

*Precedent Transactions and Premium Paid Analysis:* 2nd Generation reviewed publicly-available information relating to selected transactions. 2nd Generation selected transactions that:

involved a United States company operating as a REIT

was announced in the preceding four years

had an announced enterprise value between \$100 million and \$1 billion

had a publicly disclosed value

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These transactions are shown below.

| <b>Date Announced</b> | <b>Date Effective</b> | <b>Target Name</b>             | <b>Acquiror Name</b>          | <b>Deal Value (\$Millions)</b> | <b>Consideration Paid</b> | <b>Deal Premium 1 Week Prior</b> | <b>Deal Premium 4 Weeks Prior</b> |
|-----------------------|-----------------------|--------------------------------|-------------------------------|--------------------------------|---------------------------|----------------------------------|-----------------------------------|
| 11/6/06 -             |                       | Columbia Equity Trust Inc      | Special Situation Pty Fund    | \$ 476.40                      | Cash Only                 | 10.02                            | 13.37                             |
| 10/23/06 -            |                       | Government Properties Trust    | Record Realty                 | 223.60                         | Cash Only                 | 13.40                            | 18.78                             |
| 9/13/06 -             |                       | Windrose Med Pty Trust         | Health Care REIT Inc          | 806.86                         | Cash & Stock              | 20.24                            | 20.72                             |
| 8/31/06 -             |                       | BNP Residential Properties Inc | Babcock & Brown Real Estate   | 703.51                         | Cash Only                 | 39.45                            | 43.37                             |
| 8/21/06               | 11/29/06              | Glenborough Realty Trust Inc   | Morgan Stanley Real Estate    | 992.56                         | Cash & Stock              | 11.44                            | 15.56                             |
| 8/8/06                | 11/10/06              | Sizeler Property Investors Inc | Revenue Properties Co Ltd     | 305.82                         | Cash Only                 | (3.70)                           | (4.73)                            |
| 8/8/06                | 12/4/06               | Saxon Capital Inc              | Morgan Stanley                | 706.16                         | Cash Only                 | 27.49                            | 21.87                             |
| 7/23/06 -             |                       | Newkirk Realty Trust Inc       | Lexington Corporate Pty Trust | 396.80                         | Stock Only                | 23.75                            | 21.90                             |
| 5/19/06               | 9/21/06               | Boykin Lodging Co              | Braveheart Holdings LP        | 195.96                         | Cash Only                 | 17.27                            | 7.00                              |
| 2/10/06               | 5/5/06                | Bedford Property Investors Inc | LBAREalty LLC                 | 435.68                         | Cash Only                 | 17.74                            | 20.13                             |
| 12/19/05              | 3/31/06               | Town & Country Trust           | Magazine Acquisition GP LLC   | 961.56                         | Cash Only                 | 32.28                            | 34.13                             |
| 10/6/05               | 1/18/06               | CRIIMI MAE Inc                 | CDP Capital Financing Inc     | 321.02                         | Cash Only                 | 15.61                            | 3.57                              |
| 6/17/05               | 9/27/05               | CRT Properties Inc             | DRA Advisers LLC              | 901.03                         | Cash Only                 | 17.15                            | 18.70                             |
| 2/17/05               | 7/1/05                | Prime Group Realty Trust       | Lightstone Group LLC          | 194.00                         | Cash Only                 | 11.20                            | 13.28                             |
| 12/19/04              | 4/20/05               | Kramont Realty Trust           | Centro Watt                   | 571.14                         | Cash Only                 | 16.57                            | 18.21                             |
| 10/22/04              | 4/1/05                |                                |                               | 613.14                         | Stock Only                | 8.90                             | 12.04                             |

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|                                       |          | Cornerstone Realty Income Tr | Colonial Properties Trust      |        |            |                |                |
|---------------------------------------|----------|------------------------------|--------------------------------|--------|------------|----------------|----------------|
| 8/24/04                               | 12/21/04 | Price Legacy Corp            | PL Retail LLC                  | 757.40 | Cash Only  | (0.16)         | 2.33           |
| 5/3/04                                | 8/4/04   | Keystone Property Trust      | Investor Group                 | 855.81 | Cash Only  | 14.20          | 0.55           |
| 4/16/04                               | 7/16/04  | Hallwood Realty Partners LP  | HRPT Properties Trust          | 433.98 | Cash Only  | 60.92          | 66.20          |
| 1/22/04                               | 4/28/04  | Great Lakes REIT Inc         | Aslan Realty Partners II LP    | 251.76 | Cash Only  | (1.94)         | (2.00)         |
| 11/20/03                              | 2/6/04   | ElderTrust Realty Group      | Ventas Inc                     | 101.64 | Cash Only  | 19.05          | 23.76          |
| 7/12/03                               | 12/3/03  | Apex Mortgage Capital Inc    | American Home Mtg Hldgs Inc    | 183.83 | Stock Only | 14.66          | 18.63          |
| 6/18/03                               | 10/1/03  | Mid-Atlantic Realty Trust    | Kimco Realty Corp              | 446.32 | Cash Only  | 6.70           | 7.40           |
| 5/8/03                                | 7/10/03  | RFS Hotel Investors Inc      | CNL Hospitality Properties Inc | 687.96 | Cash Only  | 14.99          | 26.15          |
| <b>High</b>                           |          |                              |                                |        |            | <b>60.92%</b>  | <b>66.20%</b>  |
| <b>Low</b>                            |          |                              |                                |        |            | <b>(3.70)%</b> | <b>(4.73)%</b> |
| <b>Average</b>                        |          |                              |                                |        |            | <b>16.97%</b>  | <b>17.54%</b>  |
| <b>Average excluding high and low</b> |          |                              |                                |        |            | <b>15.91%</b>  | <b>16.34%</b>  |

Source: Thomson ONE Banker

2nd Generation calculated the premium paid in each of the above transactions compared to the target price one week and four weeks prior to the announcement. The deal premiums averaged 16.34% four weeks prior to announcement. This premium applied to the December 19, 2006 NHR stock price of \$21.35 produced a value of \$24.84.

Given changes in the interest rate environment and the fundamental differences between different segments within the industry, no precedent healthcare REIT transactions were deemed by 2nd Generation to be sufficiently comparable so as to be relevant to the analysis. Two transactions yielded pertinent information for the premiums paid analysis; however, in evaluating the typical enterprise value multiples implied by these two transactions, 2nd Generation determined that the values of these multiples were not meaningful.

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*Publicly-Traded Comparable Company Analysis:* 2nd Generation compared the financial and operating performance of NHR with publicly available information of selected publicly traded companies engaged in businesses which 2nd Generation deemed similar to NHR. The companies considered were as follows:

|                                      |     |
|--------------------------------------|-----|
| Health Care Property Investors, Inc. | HCP |
| Ventas, Inc.                         | VTR |
| Health Care REIT, Inc.               | HCN |
| Nationwide Health Properties, Inc.   | NHP |
| Healthcare Realty Trust Inc.         | HR  |
| Senior Housing Properties Trust      | SHN |
| Omega Healthcare Investors, Inc.     | OHI |
| Windrose Medical Properties Trust    | WRS |
| LTC Properties, Inc.                 | LTC |
| National Health Investors, Inc.      | NHI |
| Universal Health Realty Income Trust | UHT |

These companies were selected because, among other reasons, they share similar business characteristics to NHR. However, none of the companies selected is identical or directly comparable to NHR. Accordingly, 2nd Generation made judgments and assumptions concerning differences in financial and operating characteristics of the selected companies and other factors that could affect the public trading value of the selected companies. For each of the selected companies, 2nd Generation calculated:

Closing stock prices as of December 19, 2006 divided by estimated FFO (FFO means Funds From Operations, defined as net income (loss) (computed in accordance with GAAP), excluding gains (or losses) from sales of properties, plus real estate-related depreciation and amortization and other comparable adjustments for NHR's portion of these items related to unconsolidated entities and joint ventures) for the calendar years 2006 and 2007, referred to as Price/FFO multiple .

The estimates of FFO for each of the selected companies were based on publicly available estimates of certain securities research analysts.

The following table reflects the results of the analysis:

| Company Name                         | Ticker | Price<br>12/19/2006 | 2006<br>FFO<br>est. | 2006<br>Price/FFO | 2007<br>FFO<br>est. | 2007<br>Price/FFO |
|--------------------------------------|--------|---------------------|---------------------|-------------------|---------------------|-------------------|
| Health Care Property Investors, Inc. | HCP    | \$ 35.76            | \$ 1.97             | \$ 18.2x          | \$ 2.13             | 16.8x             |
| Ventas, Inc.                         | VTR    | 40.88               | 2.41                | 17.0x             | 2.76                | 14.8x             |
| Health Care REIT, Inc.               | HCN    | 41.00               | 2.91                | 14.1x             | 3.06                | 13.4x             |
| Nationwide Health Properties, Inc.   | NHP    | 29.62               | 1.93                | 15.4x             | 2.02                | 14.7x             |
| Healthcare Realty Trust Inc.         | HR     | 37.70               | 2.19                | 17.2x             | 2.37                | 15.9x             |
| Senior Housing Properties Trust      | SNH    | 22.95               | 1.61                | 14.2x             | 1.67                | 13.7x             |
| Omega Healthcare Investors, Inc.     | OHI    | 17.07               | 1.20                | 14.2x             | 1.25                | 13.7x             |
| Windrose Medical Properties Trust    | WRS    | 18.32               | 1.18                | 15.6x             | 1.36                | 13.5x             |
| LTC Properties, Inc.                 | LTC    | 26.53               | 1.84                | 14.5x             | 1.93                | 13.7x             |

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|                                       |            |                 |                |              |                |              |
|---------------------------------------|------------|-----------------|----------------|--------------|----------------|--------------|
| National Health Investors, Inc.       | NHI        | 32.83           | na             | na           | na             | na           |
| Universal Health Realty Income Trust  | UHT        | 37.75           | 2.48           | 15.2x        | 2.55           | 14.8x        |
| <b>High</b>                           |            |                 |                | <b>18.2x</b> |                | <b>16.8x</b> |
| <b>Low</b>                            |            |                 |                | <b>14.1x</b> |                | <b>13.4x</b> |
| <b>Average</b>                        |            |                 |                | <b>15.6x</b> |                | <b>14.5x</b> |
| <b>Average excluding high and low</b> |            |                 |                | <b>15.4x</b> |                | <b>14.3x</b> |
| <b>National Health Realty</b>         | <b>NHR</b> | <b>\$ 21.35</b> | <b>\$ 1.68</b> | <b>12.7x</b> | <b>\$ 1.70</b> | <b>12.6x</b> |

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Based on the Price/FFO multiple ranges set forth in the table above, this analysis implied a range for NHR common stock of \$23.66 to \$30.54 per share for the 2006 FFO multiples and \$22.75 to \$28.58 per share for the 2007 FFO multiples. However, as the chart above illustrates, NHR historically has traded at a significant discount to the comparable companies, limiting the use of this valuation technique.

*Discounted Cash Flow Analysis:* 2nd Generation performed a discounted cash flow analysis using projections provided by NHR management for the years 2007-2009. A terminal value was calculated using the perpetuity method. 2nd Generation utilized discount rates of 9.75% to 10.75% and perpetuity growth rates of 1% to 2%. This range was determined by examining the rates of growth of NHR's projected revenue, net income, and rental revenue through the end of 2009. By the end of the projection period, net revenue growth was projected to be approximately 0.5%, net income was projected to be 2% and rental revenue growth, which is the primary long-term source of revenue of NHR, was projected to be approximately 0.8%. These growth rates suggest that long-term cash flow growth would be in the range of 1-2%. The calculations produced an implied enterprise value; cash was added to this value and long-term debt subtracted to reach an implied equity value. This number was then divided by the number of fully diluted shares to produce an implied per-share value. This value ranged from \$17.44 to \$21.29.

*Dividend Discount Model Analysis.* 2nd Generation calculated ranges of implied equity value per share for NHR common stock by performing dividend discount model analysis based on management projections for the calendar years 2006 through 2009 for NHR. The dividend discount model analysis assumed a valuation date of December 31, 2006 and did not take into effect the impact of any synergies as a result of the proposed merger.

A dividend discount model analysis is a traditional method of evaluating a stock by estimating the future dividends of a stock and taking into consideration the time value of money with respect to those future dividends by calculating the present value of the estimated future dividends of the stock. Present value refers to the current value of one or more future dividends from a stock and is obtained by discounting those future dividends or amounts by a discount rate that takes into account macro-economic assumptions and estimates of risk, the opportunity cost of capital, expected returns, the capital structure of a company and other appropriate factors. Other financial terms utilized below are terminal value, which refers to the value of all future dividends from a stock at a particular point in time.

In arriving at the estimated equity values per NHR common share, 2nd Generation calculated terminal values per NHR common share as of December 31, 2006 by applying a range of perpetual dividend growth rates of 1.0% to 2.0% and a range of discount rates of 9.75% to 10.75%. The dividend per NHR common share for each of the calendar years 2007 through 2009 and the terminal value per NHR share were then discounted to present values using a range of discount rates of 9.75% to 10.75% in order to derive a range of equity values per NHR common share. This analysis assumed the annual payment of the \$0.10 special dividend that may or not be paid in the future if NHR continues as a separate publicly-traded entity.

Based on the assumptions set forth above, this analysis implied a range for NHR common stock of \$14.67 to \$18.45 per share.

*Net Asset Value Analysis.* 2nd Generation performed a net asset value per share analysis for both NHR and NHC. In order to calculate the aggregate property value of NHR, 2nd Generation valued the properties of NHR by applying market capitalization rates to calendar year 2007 estimated, aggregated same-store NOI. Based on guidance from NHR and taking into consideration current market conditions, the perceived quality of the properties as a whole and publicly available information regarding capitalization rates, 2nd Generation applied capitalization rates of 8.5% to 9.5% to their 23 properties, including 16 licensed skilled nursing facilities, six assisted living facilities, and one independent living facility. The capitalization rates applied were determined by reviewing information regarding capitalization rates of skilled nursing facilities found in equity research reports on healthcare REIT companies and long-term care providers as well as in industry periodicals and other independent research. 2nd Generation then added

the estimated value of NHR's other assets,



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including cash, marketable securities, and mortgages receivable, and to derive estimates of NHR's aggregate net asset value, subtracted:

debt of NHR as of September 30, 2006 as reported in its public filings;

minority interest; and

other outstanding liabilities.

The minority interest is the portion of NHR/OP, L.P. that is not owned by NHR. The value of the minority interest must be deducted from the asset value of the company as a whole to arrive at the value to the NHR stockholders. The minority interest amount was determined to be \$13,418,000, as reported on the NHR Form 10-Q for the period ending September 30, 2006. 2nd Generation calculated the implied net asset value per share range by dividing the calculated aggregate net asset value by the number of shares of NHR common stock outstanding as of September 30, 2006.

Based on the assumptions set forth above, this analysis implied a range for NHR common stock of \$18.81 to \$20.99 per share.

***Miscellaneous***

As a part of its merchant banking business, 2nd Generation and its affiliates are continually engaged in the valuation of businesses and their securities in connection with mergers and acquisitions; cheap-stock analysis for initial public offerings, option plan expense, warrants, investments for passive and control purposes and valuations for estate, corporate and other purposes.

The NHR special committee selected 2nd Generation to render a fairness opinion to the NHR special committee with respect to the fairness, from a financial point of view, of the merger consideration to be paid by Davis Acquisition Sub LLC in the merger to the NHR stockholders. A prior special committee of the board of directors of NHR had engaged 2nd Generation as its financial advisor to explore strategic alternatives more than two years before its selection by the current NHR special committee. During the prior selection process, the NHR special committee met with representatives of several investment banking firms and negotiated the terms of engagement and fees with such firms. In deciding to engage 2nd Generation in the present representation, the NHR special committee focused on (i) the experience of the prior special committee with 2nd Generation (ii) the reputation of 2nd Generation and its experience in the REIT industry, (iii) the professional experience of each representative that would be assigned to work on the project (iv) the relative costs of 2nd Generation's services and (v) 2nd Generation's familiarity with NHR, NHC and certain of their affiliates. Based on those factors, the NHR special committee selected 2nd Generation and did not interview other prospective financial advisors for the present engagement. NHR engaged 2nd Generation to provide financial advisory services to the NHR special committee in connection with the merger, including, among other things, delivering its opinion. Following its engagement, 2nd Generation participated in the determination of the consideration to be paid in the merger through discussions and negotiations relating to the merger and the associated documents and transactions. Pursuant to the terms of the engagement letter, NHR paid 2nd Generation a base fee of \$175,000 plus other non-contingent consideration determined based upon a set hourly rate for time incurred, which totaled \$10,613. Total fees paid to 2nd Generation were \$185,613. While a customary portion of the fee was paid upon announcement of the merger, no portion of 2nd Generation's fee is contingent upon the completion of the merger. In addition, NHR has agreed to reimburse 2nd Generation for its reasonable expenses incurred in connection with its engagement, including the reasonable fees of its counsel. NHR has agreed to indemnify 2nd Generation for certain liabilities arising out of its engagement, including liabilities under federal securities laws.

2nd Generation has provided financial advisory services from time to time to NHR and NHC. Such past services for NHC have included acting as financial advisor in 2005 concerning the negotiation of certain healthcare facility long-term leases and related operating and management agreements with National Health Investors, Inc. for which 2nd Generation was paid a fee of \$28,750. Such past services for NHR have included acting as financial advisor in 2004 to assist in the review of certain unsolicited inquires of interest in acquiring or merging with the Company. 2nd Generation has not, nor have any of its affiliates actively traded the debt

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and equity securities of NHR or NHC for their own account or for others. 2nd Generation has not had any other material relationships during the past two years with the persons filing the Schedule 13E-3 related to this transaction.

### **Alternatives to the Merger Considered by NHC and NHR**

Each of NHC and NHR considered alternative structures during the negotiation of the merger agreement, but determined that the structure described herein best secured the interests of their respective stockholders.

The NHR board of directors considered the following alternatives to the merger: (1) continuing on as a stand-alone company, which was rejected because of the slow growth rate of NHR and because of the attractiveness of the offer from NHC, (2) merging with an unaffiliated third party in a transaction in which the NHR stockholders would retain control of the combined company, which was rejected because of the decision that such a transaction would not add value comparable to the merger with NHC and would present issues under the Maryland Business Combination Act and (3) a sale to a larger company, which was rejected because of the unsuccessful solicitation of third party interest in prior years, and the heavy concentration of NHR's leases and mortgages with NHC, which was likely to make NHR an unattractive target.

### **Effects of Completing the Merger**

If the merger is approved and all other conditions to the merger have been satisfied or waived, NHR will merge with and into Davis Acquisition Sub LLC, upon the terms and subject to the conditions set forth in the merger agreement. Upon effectiveness of the merger, the separate corporate existence of NHR shall cease and Davis Acquisition Sub LLC shall continue as the surviving person in the merger and a wholly-owned subsidiary of NHC/OP, L.P., which is a wholly-owned subsidiary of NHC, and shall succeed to and assume all the rights and obligations of NHR. NHR's Common Stock will be deregistered and NHR will cease its reporting obligations under the Securities Exchange Act.

For United States federal income tax purposes, the parties will treat the merger as if NHR had sold all of its assets (other than the cash used to fund the special dividend immediately prior to the merger) to NHC/OP, L.P. in a taxable sale in exchange for the merger consideration and the assumption of NHR's liabilities as of the effective time of the merger and then made a liquidating distribution to the stockholders of NHR in exchange for their shares of NHR common stock. The gain recognized by NHR with respect to this taxable sale is expected to be fully offset by a dividends paid deduction resulting from the deemed liquidating distribution.

### **Approval of the Merger**

#### ***NHC Proposal***

The affirmative vote of the holders of a majority of common stock outstanding and entitled to vote thereon at the NHC special meeting is required to approve the amendment to the NHC certificate of incorporation.

The affirmative vote of the holders of a majority of the outstanding common stock represented and voting is required to approve the issuance of the Preferred Stock and on each other matter to be acted on, including any postponement or adjournment of the NHC special meeting to solicit additional votes.

#### ***NHR Proposal***

Approval of the merger is conditioned on receiving:

the affirmative vote of the holders of a majority of all common stock outstanding and entitled to vote thereon at the NHR special meeting; and

the affirmative vote of the holders of a majority of the common stock outstanding and entitled to vote thereon that are not owned by a director or officer of NHR, any affiliate of NHR or NHC.

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On each other matter to be acted on at the NHR special meeting, including any postponement or adjournment of the NHR special meeting to solicit additional votes, the approval of a majority of the outstanding common stock present in person or represented by proxy at the NHR special meeting is required to approve such matter.

**Interests of NHC and NHR Management in the Merger**

Members of the NHC board of directors and members of the NHR board of directors have interests in the merger that are different from, or in addition to, or that may conflict with, the interests they share with you as stockholders of NHC or NHR, as the case may be.

As of March 1, 2007, the following members of management and/or directors of both NHC and NHR were also stockholders of both NHC and NHR:

| <b>Director/Officer</b> | <b>NHC Position</b>          | <b>NHR Position</b>       | <b>Stock Ownership in NHR</b> | <b>Stock Ownership in NHC</b> |
|-------------------------|------------------------------|---------------------------|-------------------------------|-------------------------------|
| Robert G. Adams         | President & CEO,<br>Director | President and Director    | 4.4%                          | 4.8%                          |
| Donald K. Daniel        | Senior VP & Controller       | Senior VP &<br>Controller | 1.4%                          | 1.7%                          |
| Charlotte A. Swafford   | Senior VP & Treasurer        | Senior VP &<br>Treasurer  | 1.5%                          | 1.5%                          |
| W. Andrew Adams         | Chairman and Director        | Chairman and<br>Director  | 12.8%                         | 11.3%                         |
| Dr. J. Paul Abernathy   | Director                     | Director                  | 0.1%                          | 0.1%                          |
| Ernest G. Burgess, III  | Director                     | Director                  | 1.7%                          | 1.5%                          |
| Richard F. LaRoche, Jr. | Director                     | Director                  | 3.8%                          | 3.2%                          |

As of March 1, 2007, directors and officers of NHC beneficially owned in the aggregate 4,290,158 shares of NHC common stock, representing 34.4% of the outstanding NHC common stock. As of March 1, 2007, directors and officers of NHR beneficially owned in the aggregate 2,585,943 shares of NHR common stock, representing 26.0% of the outstanding shares.

**Equity Compensation Plans**

On effectiveness of the merger, each NHR stock option will be cancelled and extinguished. For more information regarding the effect of the merger on stock options in NHR common stock, please refer to the section entitled Description of the Merger Agreement Treatment of NHR Stock Options .

**Listing of the Preferred Stock**

It is a condition to the completion of the merger that the Preferred Stock issuable to NHR stockholders pursuant to the merger agreement be approved for listing on the American Stock Exchange.

**Exchange Agent**

Prior to the time when the merger becomes effective, Davis Acquisition Sub LLC shall designate a bank or trust company reasonably acceptable to NHR to act as exchange agent for the payment of the merger consideration and special dividend described in the merger agreement.

### **Dividends and Distributions**

*NHC.* Under the merger agreement, NHC is permitted to make normal quarterly cash dividends to the holders of its common stock.

*NHR.* Under the merger agreement, NHR is permitted to make (i) the dividend, the record date for which was December 29, 2006, in the amount of \$0.4325 per share of NHR's common stock or as is otherwise equal to the dividend that NHR determines is necessary to qualify as a REIT for its taxable year ended December 31, 2006, and (ii) a special dividend payable immediately prior to the consummation of the merger in an amount equal to the dividend that NHR would have declared and paid in the ordinary course of business

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for the portion of 2007 preceding the effective time of the merger, in order to qualify as a REIT for its 2007 taxable year, if NHR had not entered into the merger agreement.

### **Material U.S. Federal Income Tax Consequences of the Merger**

Assuming that the merger is completed as currently contemplated, we expect that the receipt of cash and shares of the Preferred Stock by stockholders of NHR in exchange for their common stock of NHR pursuant to the merger should be a taxable transaction for U.S. federal income tax purposes. The specific tax consequences of the merger to stockholders of NHR will depend on their own particular situation.

**YOU SHOULD READ MATERIAL U.S. FEDERAL INCOME TAX CONSEQUENCES FOR A MORE COMPLETE DISCUSSION OF THE U.S. FEDERAL INCOME TAX CONSEQUENCES OF THE MERGER. TAX MATTERS ARE COMPLICATED AND THE TAX CONSEQUENCES OF THE MERGER TO YOU WILL DEPEND UPON THE FACTS OF YOUR PARTICULAR SITUATION. BECAUSE INDIVIDUAL CIRCUMSTANCES MAY DIFFER, WE URGE YOU TO CONSULT WITH YOUR TAX ADVISOR AS TO THE SPECIFIC TAX CONSEQUENCES OF THE MERGER TO YOU, INCLUDING THE APPLICABILITY OF U.S. FEDERAL, STATE, LOCAL, FOREIGN AND OTHER TAX LAWS**

### **Anticipated Accounting Treatment**

NHC intends to account for the merger as a purchase transaction under accounting principles generally accepted in the United States. Under the purchase method of accounting, the assets and liabilities of NHR will be recorded, as of the completion of the merger, at their respective fair values and added to those of NHC. These allocations will be based upon valuations that have not yet been finalized. The financial condition and results of operations of NHC after completion of the merger will reflect NHR's balances and results after completion of the merger but will not be restated retroactively to reflect the historical financial position or results of operations of NHR.

Following the completion of the merger, the earnings of the combined company will reflect purchase accounting adjustments, including the effect of changes in the cost bases for assets and liabilities on depreciation and amortization expense. Long-lived assets will be evaluated for impairment when events or changes in economic circumstances indicate the carrying amount of such assets may not be recoverable. The goodwill, if any, resulting from the merger, which is not subject to amortization, will be reviewed for impairment at least annually. Any future impairments or market value adjustments would reduce the asset carrying values and result in changes to earnings for the combined company.

### **Dissenters' Rights**

The stockholders of NHC will not be entitled to exercise dissenters' rights with respect to any matter to be voted upon at the NHC special meeting.

The stockholders of NHR will not be entitled to exercise dissenters' rights with respect to any matter to be voted upon at the NHR special meeting.

### **Resale of the Preferred Stock**

The Preferred Stock issued in connection with the merger will not be subject to any restrictions on transfer arising under the Securities Act, except for the Preferred Stock held by any former NHR stockholder that is, or is expected to be, an affiliate of NHC, as applicable, for purposes of Rule 145 under the Securities Act. Persons that may be deemed to be affiliates of NHC for those purposes generally include individuals or entities that control, are controlled by, or

are under common control with, NHC and include the directors of NHC. Preferred Stock issued to an affiliate generally must be sold in compliance with all of the requirements of Rule 145, or pursuant to another exemption from registration under the Securities Act. Rule 145 restricts the sale of Preferred Stock received in the merger by such affiliates of NHC and certain of the family members and related entities.



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This joint proxy statement/prospectus does not cover resales of the Preferred Stock received by any person upon completion of the merger, and no person is authorized to make any use of this joint proxy statement/prospectus in connection with any resale.

**Sources of Funds, Fees and Expenses**

The cash portion of the merger consideration, which is \$97,406,037, will be funded with Davis Acquisition Sub LLC's cash and other liquid assets. The non-cash portion of the merger consideration consists of 10,822,893 shares of the Preferred Stock, which have an aggregate liquidation preference of \$170,460,564.75

The transaction-related fees and expenses, consisting primarily of financial, legal, accounting and tax advisory fees, SEC filing fees and other related charges, will total approximately \$            million. This amount includes the following estimated fees and expenses:

| <b>Description</b>  | <b>Amount to be Paid</b> |
|---|--------------------------|
| SEC filing fee (inclusive of Schedule 13E-3 filing fee)         | \$ 8,077.08              |
| Printing, proxy solicitation and mailing expenses               |                          |
| Financial, legal, accounting and tax advisory fees and expenses |                          |
| Miscellaneous expenses  |                          |
| Total   | \$                       |

Davis Acquisition Sub LLC may borrow up to \$25.0 million from NHC's wholly owned insurance subsidiary, with which it is consolidated for financial statement purposes. Such a loan would be unsecured and at an interest rate consistent with the market for similar loans. The terms of such financing have not yet been finalized and, accordingly, the actual terms of such loan, if any, may differ from those described herein. Davis Acquisition Sub LLC may decide to proceed with the closing of the merger without obtaining such loan or additional financing.

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**RISK FACTORS**

In addition to the risks relating to the businesses of NHC, which are incorporated by reference in this joint proxy statement/prospectus from NHC's annual report on Form 10-K for the year ended December 31, 2006 and NHR's annual report on Form 10-K for the year ended December 31, 2006 and the other information included or incorporated herein, including the matters addressed in Forward-Looking Statements, you should carefully consider the following material risk factors relating to the merger in determining whether or not to vote in favor of the approval of the NHC Proposal or the NHR Proposal, as applicable.

***The value of the merger consideration that the holders of NHR common stock will receive in the merger may decline depending on the market value of the NHC common stock.***

Pursuant to the merger agreement, each outstanding share of NHR common stock will be converted into the right to receive \$9.00 in cash and one share of Preferred Stock. The prices of the NHR common stock and the NHC common stock at the closing of the merger may vary from their prices on the date of this joint proxy statement/prospectus and on the date of the respective special meetings. To the extent the market price of the NHC common stock declines, the value of the Preferred Stock that an NHR stockholder will receive as part of the merger consideration will also decrease since the Preferred Stock is convertible into NHC common stock. The market price of the NHC common stock has in the past, and may in the future, vary based on a number of factors, including general market and economic conditions and changes in its business, operations and prospects. Many of these factors are beyond the control of NHC.

***The intended benefits of the merger may not be realized, which could have a negative impact on the market price of the shares of NHC's common stock and the Preferred Stock following the completion of the merger.***

The success of the merger depends, in part, on NHC's ability to realize the anticipated benefits and cost savings from combining the businesses of NHC and NHR. No assurance can be given that the anticipated expense reductions or other operating synergies will be realized by NHC quickly following the merger or at all or that unanticipated costs will not arise as a result of the merger. If the expected savings are not realized or unexpected costs are incurred, the merger could have a significant dilutive effect on NHC's per share operating results.

***The parties may incur substantial expenses and payments if the merger does not occur.***

It is possible that the merger may not be completed. If the merger is not completed, the parties will have incurred substantial expenses. In addition, NHR may incur a termination fee of up to \$9,444,000 if the merger agreement is terminated under specified circumstances. Further, the parties also may become obligated to reimburse up to \$2,000,000 of the other parties' expenses if the merger agreement is terminated for certain reasons.

***The \$9,444,000 termination fee payable by NHR under specified circumstances may discourage third party proposals to acquire NHR that NHR stockholders may otherwise find desirable.***

The \$9,444,000 termination fee payable by NHR if the merger agreement is terminated under specified circumstances represents approximately 3.5% of the merger consideration based on the liquidation value of the Preferred Stock. This termination fee may discourage third party proposals to acquire NHR that NHR stockholders might otherwise find desirable, to the extent that a potential acquiror would not be willing to assume the termination fee.

***The financial advisors' fairness opinions will not reflect changes in circumstances between the signing of the merger agreement and the closing of the merger.***

The merger agreement does not require that the financial advisors' fairness opinions be updated as a condition to closing the merger, and neither NHC nor NHR currently intends to request that those opinions be updated. As such, the fairness opinions do not reflect any changes in the relative values of NHC or NHR.

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subsequent to the date of the merger agreement. The market price of the NHC common stock and the NHR common stock may vary significantly between the date hereof and the date of the consummation of the merger.

***The directors and executive officers of NHR have interests in the completion of the merger that may differ from or conflict with the interests of the stockholders of NHR.***

In considering the recommendation of the NHR board of directors and its special committee with respect to the merger, NHR stockholders should be aware that executive officers of NHR and members of the NHR board of directors may have interests in the transactions contemplated by the merger agreement that are different than, or in addition to, the interests of the NHR stockholders generally. The NHR board of directors and its special committee was aware of these interests and considered them, among other matters, in approving the merger agreement and making its recommendation. These interests are summarized below.

*Composition of NHC Board Following the Merger*

All of the members of the NHR board of directors (other than the members of the NHR special committee) are also directors of NHC, and will continue as directors of NHC following the merger. Mr. Robert Adams, currently the chief executive officer and president of both companies, will continue to serve as chief executive officer and president of NHC following the merger.

*Equity-Based Awards*

All of the options held by directors of NHR under the equity compensation plans maintained by NHR (less the applicable exercise price) will be exchanged for merger consideration as provided in the merger agreement, regardless of whether such options were vested prior to the consummation of the merger. See Description of the Merger Agreement Treatment of NHR Stock Options.

*Indemnification of Directors and Officers; Directors and Officers Insurance*

The merger agreement provides that Davis Acquisition Sub LLC, as the surviving entity, will indemnify and hold harmless each current and former director and officer of NHR for acts and omissions occurring before or as of the effective time of the merger to the full extent permitted by the NHR charter and bylaws prior to the consummation of the merger. The merger agreement further provides that, for a period of at least four years after the effective time of the merger, Davis Acquisition Sub LLC, as the surviving entity, will maintain NHR's current directors' and officers' liability insurance and indemnification policy with respect to events occurring before or as of the effective time of the merger and covering all current or prior directors and officers of NHR currently covered pursuant to such policy. Davis Acquisition Sub LLC, as the surviving entity, may substitute for the existing insurance substantially similar insurance so long as it is on terms no less favorable, taken as a whole. See Description of the Merger Agreement Indemnification; Directors and Officers Insurance.

For additional information about the directors and the executive officers of NHR and a summary of the NHR common stock beneficially owned by such individuals, see the annual report on Form 10-K for NHR for the year ended December 31, 2006 filed with the SEC on March 16, 2007.

***Financial forecasts and projections considered by the parties may not be realized, which may adversely affect the market price of the NHC common stock and the Preferred Stock or the NHR common stock.***

Neither NHC nor NHR generally makes, as a matter of course, public forecasts or projections as to future revenues, earnings or other financial statement data, and none of the projections relating to future financial results of NHC or

NHR prepared by management and considered by the parties to the transaction were prepared with view to public disclosure or compliance with the published guidelines of the SEC or the American Institute of Certified Public Accountants regarding projections and forecasts. These projections are inherently based on various estimates and assumptions that are subject to the judgment of those preparing them. These projections are also subject to significant economic, competitive, industry and other uncertainties

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and contingencies, all of which are difficult or impossible to predict and many of which are beyond the control of NHC or NHR. Accordingly, there can be no assurance that NHC's or NHR's financial results will not be significantly higher or lower than those set forth in such projections. Significantly lower financial results could have a material adverse effect on the market price of the NHC common stock, the Preferred Stock or the NHR common stock.

***The respective financial advisors to the NHC special committee and the NHR special committee reviewed and relied on, among other things, certain projected financial forecasts, costs savings and operational synergies, and a failure of the combined company to achieve those results could have a material adverse effect on the market price of the NHC common stock and the Preferred Stock.***

In performing their financial analyses and rendering their opinions regarding the fairness from a financial point of view of the consideration and exchange ratio in the merger, each of the respective financial advisors to the NHC special committee and the NHR special committee independently reviewed and relied on, among other things, internal financial analyses and forecasts for NHC and NHR available on the date of their respective opinions as separately provided to each financial advisor by NHC or NHR, as the case may be. Included in such internal financial analyses and forecasts were certain pro forma financial analyses and forecasts for the combined company after giving effect to the merger, including certain projected cost savings and operating synergies. Each of the respective financial advisors to the NHC special committee and the NHR special committee also independently assumed that the pro forma financial analyses and forecasts for NHC and the projected cost savings and operational synergies giving effect to the merger would be achieved within certain independently determined time frames. These pro forma financial analyses and forecasts and projected cost savings and operational synergies may not be achieved in full, at all or within projected time frames, and a failure of NHC to realize these pro forma financial analyses and forecasts and projected cost savings and operational synergies could have a material adverse effect on the earnings per share of the combined company, which could in turn have an adverse effect on the market price of the NHC common stock and the Preferred Stock.

***Most of the Preferred Stock issued in the merger will be eligible for sale immediately after the merger is completed.***

Holdings of NHR common stock other than Davis Acquisition Sub LLC, NHC/OP, L.P. or NHC will receive approximately 10,822,893 freely tradable shares of the Preferred Stock upon the consummation of the merger. These freely tradable shares of Preferred Stock will be convertible at any time into approximately 2,705,723 shares of freely tradable NHC common stock. If one or more former holders of NHR common stock sell substantial amounts of the Preferred Stock or the underlying NHC common stock into the public market following the merger, the market price of the Preferred Stock and NHC common stock could decline significantly.

***The Preferred Stock to be issued in the merger has never been publicly traded so NHC cannot predict the extent to which a market will develop for the Preferred Stock or how volatile or liquid that market will be or what the effect of its issuance will be on the market for NHC's common stock.***

There is currently no public market for the Preferred Stock, although shares of NHC's common stock, into which the Preferred Stock will be convertible, are listed on the American Stock Exchange. The market price of the Preferred Stock may fluctuate widely after the merger. The reasons for such fluctuations may include the business community's perception of the combined company's prospects and of the industries in which it operates. Differences between the combined company's actual operating results and those expected by investors and analysts and changes in analysts' recommendations or projections could also affect the price of the Preferred Stock. Other factors that could potentially cause volatility in the price for the Preferred Stock may include changes in general economic or market conditions and broad market fluctuations. NHC has agreed to use its reasonable best efforts to cause the Preferred Stock issuable in the merger to be approved for listing on the American Stock Exchange, but even if the Preferred Stock is listed on such exchange, NHC cannot guarantee that an active and liquid trading market for the Preferred Stock will develop. In

addition,

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NHC cannot predict what the effect of the issuance of the Preferred Stock will be on the market for the NHC common stock.

***NHC may incur adverse tax consequences if NHR has failed or fails to qualify as a REIT for U.S. federal income tax purposes.***

NHR believes it has qualified and will continue to qualify up to the effective time of the merger as a REIT for U.S. federal income tax purposes. However, if NHR has failed or fails to qualify as a REIT and the merger is completed, NHC generally would succeed to or incur significant tax liabilities (including the significant tax liability that would result from the deemed sale of assets by NHR pursuant to the merger). REITs are subject to a range of complex organizational and operational requirements. As a REIT, NHR generally must distribute with respect to each year at least 90% of its REIT taxable income to its stockholders. For any taxable year that NHR fails to qualify as a REIT, it will not be allowed a deduction for dividends paid to its stockholders in computing taxable income and thus would become subject to U.S. federal income tax for each such taxable year as if it were a regular taxable corporation. If NHR failed or fails to qualify as a REIT, the market price of the NHC stock may decline and NHC may need to reduce substantially the amount of distributions to its stockholders because of its increased tax liability.

***The price of NHC common stock may fluctuate significantly.***

There has been significant volatility in the market prices of securities of health care companies. We believe factors such as legislative and regulatory developments and quarterly variations in financial results could cause the market price of NHC stock to fluctuate substantially. In addition, the stock market has experienced volatility that has particularly affected the market prices for many health care service companies' securities and that often has been unrelated to the operating performance of such companies. These market fluctuations may adversely affect the price of NHC stock.

***Certain provisions in the NHC certificate of incorporation, the NHC bylaws and of Delaware law could deter, delay or prevent a third party from acquiring NHC and that could deprive you of an opportunity to obtain a takeover premium for the NHC common stock and Preferred Stock.***

NHC's certificate of incorporation, NHC's bylaws and Delaware law contain provisions that could have the effect of making it more difficult for a third party to acquire NHC, or of discouraging a third party from attempting to acquire control of NHC. See Description of NHC Capital Stock.

Together NHC's certificate of incorporation, NHC's bylaws and certain provisions of Delaware law may discourage transactions that otherwise could provide for the payment of a premium over prevailing market prices for the NHC common stock and could also limit the price that investors may be willing to pay in the future for the NHC common stock.



**Table of Contents****SELECTED HISTORICAL CONSOLIDATED FINANCIAL DATA OF NHC**

The following tables set forth selected historical consolidated financial information for NHC. The selected historical information is presented as of and for the three months ended March 31, 2007 and 2006 and for the years ended December 31, 2006, 2005, 2004, 2003 and 2002. NHC derived the historical information for the years ended December 31, 2006, 2005, 2004, 2003 and 2002 from its audited consolidated financial statements and the notes thereto. NHC derived the historical information for the three months ended March 31, 2007 and 2006 from its unaudited consolidated financial statements for those periods. In the opinion of NHC management, the unaudited consolidated financial statements incorporated by reference herein for the three months ended March 31, 2007 and 2006 have been prepared on a basis consistent with NHC's audited consolidated financial statements and include all adjustments, consisting only of normal recurring adjustments, necessary for a fair presentation of the financial position and results of operations for these periods. The operating results for the three months ended March 31, 2007 and 2006 are not necessarily indicative of the results that may be expected for the entire fiscal year of NHC or the combined company.

The selected information set forth below should be read in conjunction with NHC's consolidated financial statements and related footnotes, as well as the disclosure under the heading "Management's Discussion and Analysis of Financial Condition and Results of Operations," in NHC's annual report on Form 10-K and quarterly report on Form 10-Q, incorporated into this joint proxy statement/prospectus. The historical results of operations are not necessarily indicative of future results.

|  | <b>Three Months Ended</b>                              |             | <b>Year Ended December 31,</b> |             |             |             |             |
|--|--|-------------|--------------------------------|-------------|-------------|-------------|-------------|
|  | <b>March 31,</b>                                       |             |                                |             |             |             |             |
|  | <b>2007(b)</b>   | <b>2006</b> | <b>2006(a)</b>                 | <b>2005</b> | <b>2004</b> | <b>2003</b> | <b>2002</b> |
|  | <b>(In thousands, except share and per share data)</b> |             |                                |             |             |             |             |
| <b>Statement of Operations Data:</b>       |  |             |                                |             |             |             |             |
| Net revenues                               | 146,504  | 136,951     | \$ 562,958                     | \$ 542,381  | \$ 521,829  | \$ 472,864  | \$ 458,252  |
| Total costs and expenses                   | 135,557  | 127,976     | 508,679                        | 495,691     | 481,574     | 439,577     | 430,806     |
| Income before income taxes                 | 10,947   | 8,975       | 54,279                         | 46,690      | 40,055      | 33,287      | 27,446      |
| Income tax provision                       | 3,907  | 3,555       | 17,539                         | 18,055      | 16,083      | 13,335      | 11,009      |
| Net income                                 | 7,040  | 5,420       | 36,740                         | 28,635      | 23,972      | 19,952      | 16,437      |
| Earnings per share:                        |  |             |                                |             |             |             |             |
| Basic                                      | \$ .56   | \$ .44      | \$ 2.99                        | \$ 2.34     | \$ 2.05     | \$ 1.72     | \$ 1.43     |
| Diluted                                    | .54  | .42         | 2.85                           | 2.24        | 1.95        | 1.65        | 1.37        |
| Dividends declared per share:              |  |             |                                |             |             |             |             |
| Cash                                       | \$ 0.18  | \$ 0.15     | \$ 0.690                       | \$ 0.575    | \$ 0.500    | \$          | \$          |
| <b>Balance Sheet Data (at period end):</b> |  |             |                                |             |             |             |             |
| Total current assets                       | 298,620  | 259,201     | \$ 290,611                     | \$ 260,579  | \$ 227,734  | \$ 204,796  | \$ 164,611  |
|  | 188,677  | 159,277     | 180,866                        | 150,046     | 145,383     | 147,597     | 140,964     |

|   |         |         |         |         |         |         |         |
|---|---------|---------|---------|---------|---------|---------|---------|
| Total noncurrent assets                         |         |         |         |         |         |         |         |
| Total assets                                    | 487,297 | 418,478 | 471,477 | 410,625 | 373,117 | 352,393 | 305,575 |
| Accrued risk reserves                           | 80,058  | 74,490  | 76,471  | 70,290  | 62,354  | 43,953  | 31,632  |
| Total current liabilities                       | 167,042 | 148,091 | 168,548 | 147,191 | 128,605 | 131,809 | 114,077 |
| Long-term debt, less current portion            | 10,000  | 13,018  | 10,381  | 13,568  | 16,025  | 19,000  | 26,220  |
| Debt serviced by other parties                  |         |         |         |         | 1,494   | 1,727   | 1,952   |
| Total noncurrent liabilities                    | 32,260  | 27,021  | 21,967  | 27,571  | 30,726  | 37,859  | 40,107  |
| Minority interests in consolidated subsidiaries |         | 1,274   |         | 1,185   | 874     | 812     | 750     |
| Stockholders equity                             | 254,077 | 207,725 | 249,142 | 203,059 | 182,348 | 151,027 | 120,141 |

- (a) Effective January 1, 2006, NHC adopted Statement of Financial Accounting Standards No. 123 (Revised 2004), Share Based Payment.
- (b) Effective January 1, 2007, NHC adopted FIN 48.



|                                     |           |           |           |           |           |           |           |  |
|-------------------------------------|-----------|-----------|-----------|-----------|-----------|-----------|-----------|--|
| Total stockholders equity           |           |           |           |           |           |           |           |  |
| Common shares outstanding           | 9,951,864 | 9,939,463 | 9,951,864 | 9,939,463 | 9,699,108 | 9,590,588 | 9,570,323 |  |
| Weighted average common shares:     |           |           |           |           |           |           |           |  |
| Basic                               | 9,951,864 | 9,939,463 | 9,942,803 | 9,853,490 | 9,594,852 | 9,575,546 | 9,570,323 |  |
| Diluted                             | 9,968,645 | 9,946,538 | 9,950,022 | 9,881,484 | 9,822,823 | 9,757,238 | 9,770,730 |  |
| Common dividends declared per share | \$ 0.3325 | \$ 0.3325 | \$ 1.43   | \$ 1.43   | \$ 1.41   | \$ 1.49   | \$ 1.33   |  |

- (a) Approximately \$21,982,000 and \$30,384,000 of 10.25% notes receivable were prepaid to NHR in November 2003 and February 2004, respectively. NHR used the proceeds of the prepayments to pay down its long-term debt.

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**UNAUDITED PRO FORMA CONSOLIDATED FINANCIAL INFORMATION**

The following unaudited pro forma condensed consolidated statements of income for the three months ended March 31, 2007 and the year ended December 31, 2006, assume the business combination between NHC and NHR occurred on January 1, 2006. The unaudited pro forma condensed consolidated balance sheet as of March 31, 2007 assumes the merger had occurred on March 31, 2007.

The transactions will be accounted for under the purchase method of accounting in accordance with Statement of Financial Accounting Standards No. 141, *Business Combinations (SFAS No. 141)*. As a result, the purchase price, including related costs, will be allocated based on the estimated fair values of the assets acquired and liabilities assumed at the time of acquisition.

The allocation of the purchase price to NHR's assets, including intangible assets, and liabilities are only preliminary allocations based on estimates of fair values and will change when actual fair values are determined. Among the provisions of SFAS 141, criteria have been established for determining whether intangible assets should be recognized separately from goodwill.

The unaudited pro forma condensed financial information is presented for illustrative purposes only and is not necessarily indicative of the financial condition or results of operations of future periods or the financial condition or results of operations that actually would have been realized had the entities been a single entity during these periods. The unaudited proforma condensed financial information should be read together with the historical financial statements and related notes of NHC and NHR contained in the annual and quarterly reports and other information that each have filed with the SEC and that are incorporated by reference into this Joint Proxy Statement/Prospectus.

**Table of Contents****National HealthCare Corporation and Subsidiaries****Unaudited Pro Forma Consolidated Income Statement**

Three Months Ended March 31, 2007

*(in thousands, except share and per share amounts)*

|  | Historical |           | Pro Forma Adjustments |           | Pro Forma Consolidated |
|--|------------|-----------|-----------------------|-----------|------------------------|
|  | NHC        | NHR       | Debit                 | Credit    |                        |
| Revenues:  |            |           |                       |           |                        |
| Net patient revenue                              | \$ 133,480 | \$        |                       |           | \$ 133,480             |
| Other revenue                                    | 13,024     | 224       | \$ 125 (b)            |           | 11,697                 |
|  |            |           | 121 (d)               |           |                        |
|  |            |           | 1,305 (f)             |           |                        |
| Rental income                                    |            | 4,562     | 2,829 (a)             |           | 1,733                  |
| Mortgage interest income                         |            | 520       |                       |           | 520                    |
| Net revenue                                      | 146,504    | 5,306     | 4,380                 |           | 147,430                |
| Costs and expenses:                              |            |           |                       |           |                        |
| Salaries, wages and benefits                     | 79,174     |           |                       |           | 79,174                 |
| Other operating expenses                         | 41,828     | 525       |                       | 326 (c)   | 41,902                 |
|  |            |           |                       | 125 (b)   |                        |
| Rent   | 10,523     |           |                       | 2,829 (a) | 7,694                  |
| Depreciation and amortization                    | 3,756      | 1,341     | 79 (e)                |           | 5,176                  |
| Interest   | 276        | 138       |                       |           | 414                    |
| Total cost and expenses                          | 135,557    | 2,004     | 79                    | 3,280     | 134,360                |
| Income before income taxes and minority interest | 10,947     | 3,302     | 4,459                 | 3,280     | 13,070                 |
| Minority interest                                |            | (359)     |                       | 359 (g)   |                        |
| Income tax provision                             | 3,907      |           | 849 (i)               |           | 4,756                  |
| Net income                                       | 7,040      | 2,943     | 5,308                 | 3,639     | 8,314                  |
| Dividends to preferred stockholders              |            |           | 2,164 (h)             |           | (2,164)                |
| Net income available to common stockholders      | \$ 7,040   | \$ 2,943  | \$ 7,472              | \$ 3,639  | \$ 6,150               |
| Earnings Per Share                               |            |           |                       |           |                        |
| Basic  | \$ 0.56    | \$ 0.30   |                       |           | \$ 0.49                |
| Diluted  | \$ 0.54    | \$ 0.30   |                       |           | \$ 0.47                |
| Weighted Average Common Shares Outstanding       |            |           |                       |           |                        |
| Basic  | 12,526,231 | 9,951,864 |                       |           | 12,526,231             |
| Diluted  | 12,992,219 | 9,968,645 |                       |           | 12,992,219             |

Note: Diluted weighted average shares excludes 2,616,227 preferred stock potential common shares due to their antidilutive impact.

*See Notes to Unaudited Pro Forma Consolidated Income Statement*

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**National HealthCare Corporation and Subsidiaries**

**Notes to Unaudited Pro Forma Condensed Consolidated Income Statement**

Three Months Ended March 31, 2007

- (a) To eliminate NHR rent charged to NHC.
- (b) To eliminate NHR advisory revenue and expense.
- (c) To eliminate NHR merger related transactional expenses reflected in the historical F/S.
- (d) To eliminate dividend income of \$121,000 on 363,200 shares of NHR common stock owned by NHC.
- (e) To record additional depreciation on NHR assets after merger due to adjustment to fair value. Depreciation on newly acquired assets (consisting only of real property) is calculated assuming an average life of 30 years.
- (f) To reduce interest and investment income earned on cash, restricted cash and marketable securities due to the use of NHC's cash in the merger (\$98.4 million historically earning an average of 5.3%). The proforma adjustment assumes that NHC will borrow up to \$25.0 million from its wholly owned insurance company subsidiary. As of March 31, 2007, these funds are included in restricted cash.
- (g) To eliminate minority interest attributable to NHR by conversion of NHR/OP, L.P. partnership units into 1,215,754 shares of NHR common stock.
- (h) To record cumulative dividends payable to holders of preferred stock at \$0.80 per annum assuming 10,822,893 shares issued.
- (i) To record additional income tax due to the incremental increase in taxable income after the merger based on NHC's historical tax rate of 40%.



**Table of Contents****National HealthCare Corporation and Subsidiaries****Unaudited Pro Forma Condensed Consolidated Income Statement**

Year Ended December 31, 2006

*(in thousands, except share and per share amounts)*

|  | Historical |           | Pro Forma Adjustments |            | Pro Forma    |
|--|------------|-----------|-----------------------|------------|--------------|
|  | NHC        | NHR       | Debit                 | Credit     | Consolidated |
| Revenues:  |            |           |                       |            |              |
| Net patient revenue                              | \$ 501,705 | \$        |                       |            | \$ 501,705   |
| Other revenue                                    | 61,253     | 862       | \$ 524 (b)            |            | 55,854       |
|  |            |           | 519 (d)               |            |              |
|  |            |           | 5,218 (f)             |            |              |
| Rental income                                    |            | 17,995    | 11,382 (a)            |            | 6,613        |
| Mortgage interest income                         |            | 2,142     |                       |            | 2,142        |
| Net revenue                                      | 562,958    | 20,999    | 17,643                |            | 566,314      |
| Costs and expenses:                              |            |           |                       |            |              |
| Salaries, wages and benefits                     | 302,862    |           |                       |            | 302,862      |
| Other operating expenses                         | 157,664    | 785       |                       | 524 (b)    | 157,378      |
|  |            |           |                       | 547 (c)    |              |
| Recovery of note receivable                      | (7,309)    |           |                       |            | (7,309)      |
| Rent   | 40,310     |           |                       | 11,382 (a) | 28,928       |
| Depreciation and amortization                    | 14,172     | 5,691     | 1,574 (e)             |            | 21,437       |
| Interest   | 980        | 604       |                       |            | 1,584        |
| Total cost and expenses                          | 508,679    | 7,080     | 1,574                 | 12,453     | 504,880      |
| Income before income taxes and minority interest | 54,279     | 13,919    | 19,217                | 12,453     | 61,434       |
| Minority interest                                |            | (1,512)   |                       | 1,512 (g)  |              |
| Income tax provision                             | 17,539     |           | 2,862 (i)             |            | 20,401       |
| Net income                                       | 36,740     | 12,407    | 22,079                | 13,965     | 41,033       |
| Dividends to preferred stockholders              |            |           | 8,647 (h)             |            | (8,647)      |
| Net income available to common stockholders      | \$ 36,740  | \$ 12,407 | \$ 30,726             | \$ 13,965  | \$ 32,386    |
| Earnings Per Share                               |            |           |                       |            |              |
| Basic  | \$ 2.99    | \$ 1.25   |                       |            | \$ 2.63      |
| Diluted  | \$ 2.85    | \$ 1.25   |                       |            | \$ 2.51      |
| Weighted Average Common Shares Outstanding       |            |           |                       |            |              |
| Basic  | 12,294,730 | 9,942,803 |                       |            | 12,294,730   |
| Diluted  | 12,886,171 | 9,950,022 |                       |            | 12,886,171   |

Note: Pro forma diluted weighted average shares excludes 2,616,227 common shares issuable upon the conversion of the preferred stock due to their antidilutive impact.

*See Notes to Unaudited Pro Forma Condensed Consolidated Income Statement*

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**National HealthCare Corporation and Subsidiaries**

**Notes to Unaudited Pro Forma Condensed Consolidated Income Statement**

Year Ended December 31, 2006

- (a) To eliminate NHR rent charged to NHC.
- (b) To eliminate NHR advisory revenue and expense.
- (c) To eliminate NHR merger related transactional expenses reflected in the historical F/S.
- (d) To eliminate dividend income of \$519,000 on 363,200 shares of NHR common stock owned by NHC.
- (e) To record additional depreciation on NHR assets after merger due to adjustment to fair value. Depreciation on newly acquired assets (consisting only of real property) is calculated assuming an average life of 30 years.
- (f) To reduce interest and investment income earned on cash, restricted cash and marketable securities due to the use of NHC's cash in the merger (\$98.4 million historically earning an average of 5.3%). The pro forma adjustment assumes that NHC will borrow up to \$25.0 million from its wholly owned insurance company subsidiary. As of December 31, 2006, these funds are included in restricted cash.
- (g) To eliminate minority interest attributable to NHR by conversions of NHR/OP, LP partnership units into 1,215,754 shares of NHR common stock.
- (h) To record cumulative dividends payable to holders of preferred stock at \$0.80 per share per annum assuming 10,822,893 shares issued.
- (i) To record additional income tax due to the incremental increase in taxable income after the merger based on NHC's historical tax rate of 40%.

**Table of Contents****National HealthCare Corporation and Subsidiaries****Unaudited Pro Forma Condensed Consolidated Balance Sheet****March 31, 2007***(in thousands, except share and per share amounts)*

|  | Historical                      |                             | Pro Forma              |                    | Pro Forma Consolidated |
|--|---------------------------------|-----------------------------|------------------------|--------------------|------------------------|
|  | National HealthCare Corporation | National Health Realty Inc. | Adjustments Debit      | Adjustments Credit |                        |
| Assets:  |                                 |                             |                        |                    |                        |
| Current Assets:  |                                 |                             |                        |                    |                        |
| Cash and cash equivalents:                               | \$ 57,246                       | \$ 10,049                   | \$ 17,000(b)           | \$ 73,406(c)       | \$ 10,889              |
| Restricted cash  | 101,564                         |                             |                        | 25,000(c)          | 76,564                 |
| Marketable securities                                    | 68,401                          | 7,052                       |                        | 8,535(a)           | 49,918                 |
|  |                                 |                             |                        | 17,000(b)          |                        |
| Restricted marketable securities                         | 1,808                           |                             |                        |                    | 1,808                  |
| Accounts receivable, less allowance for doubtful amounts | 60,971                          |                             |                        |                    | 60,971                 |
| Notes and mortgages receivable                           | 189                             |                             |                        |                    | 189                    |
| Other current assets                                     | 8,441                           | 129                         |                        |                    | 8,570                  |
|  | 298,620                         | 17,230                      | 17,000                 | 123,941            | 208,909                |
| Property, Equipment & Intangibles, net                   | 127,225                         | 108,022                     | 3,045(a)<br>260,694(c) | 124,899(d)         | 374,087                |
| Other Assets:  |                                 |                             |                        |                    |                        |
| Notes and mortgages receivable                           | 20,003                          | 12,371                      | 8,172(c)               |                    | 40,546                 |
| Other  | 41,449                          | 110                         | 2,196(a)               |                    | 43,755                 |
|  | 61,452                          | 12,481                      | 10,368                 |                    | 84,301                 |
| <b>TOTAL ASSETS</b>                                      | <b>\$ 487,297</b>               | <b>\$ 137,733</b>           | <b>\$ 291,107</b>      | <b>\$ 248,840</b>  | <b>\$ 667,297</b>      |
| Liabilities and Stockholders Equity:                     |                                 |                             |                        |                    |                        |
| Current liabilities:                                     |                                 |                             |                        |                    |                        |
| Accrued risk reserves                                    | \$ 80,058                       | \$                          |                        |                    | \$ 80,058              |
| Other current liabilities                                | 86,984                          | 4,509                       |                        |                    | 91,493                 |
|  | 167,042                         | 4,509                       |                        |                    | 171,551                |
| Long-term debt, less current portion                     | 10,000                          | 8,325                       |                        |                    | 18,325                 |

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|  |            |            |                      |            |            |
|--|------------|------------|----------------------|------------|------------|
| Other noncurrent liabilities                   | 22,260     |            |                      |            | 22,260     |
| Deferred lease credit                          | 5,755      |            |                      |            | 5,755      |
| Deferred revenue                               | 28,163     |            |                      |            | 28,163     |
| Minority interest in consolidated subsidiaries |            | 13,254     | 13,254(d)            |            |            |
| Stockholders' Equity:                          |            |            |                      |            |            |
| Preferred stock                                |            |            |                      | 170,460(c) | 170,460    |
| Common stock                                   | 94,560     | 138,795    | 138,795(d)           |            | 94,560     |
| Retained earnings                              | 135,366    |            |                      |            | 135,366    |
| Cumulative net income                          |            | 92,268     | 92,268(d)            |            |            |
| Cumulative dividends                           |            | (122,986)  |                      | 122,986(d) |            |
| Unrealized gains on marketable securities      | 24,151     | 3,568      | 3,294(a)<br>3,568(d) |            | 20,857     |
|  | 320,255    | 133,224    | 251,179              | 293,446    | 495,746    |
| Total liabilities and stockholders' equity     | \$ 487,297 | \$ 137,733 | \$ 251,179           | \$ 293,446 | \$ 667,297 |

*See Notes to Unaudited Pro Forma Condensed Consolidated Balance Sheet*

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**National HealthCare Corporation and Subsidiaries**

**Notes to Unaudited Pro Forma Condensed Consolidated Balance Sheet**

March 31, 2007

- (a) To eliminate NHC's investment in 363,200 shares of NHR common stock, which shares are to be canceled upon the merger
- (b) To account for the sale of securities expected to partially fund the merger.
- (c) To record the acquisition by NHC of the property, equipment, notes and mortgage notes receivable and liabilities of NHR. Consideration given includes cash (\$9.00 for each outstanding share of the common stock of NHR) and the issuance by NHC of convertible preferred stock (\$15.75 per share of the common stock of NHR). The preferred stock is convertible into 0.24204 shares of NHC common stock. Transaction costs are estimated at \$1 million and are included in this adjustment. Such costs will be capitalized as part of the purchase price. The portion of the purchase price to be allocated to intangibles, if any, has not been finalized.
- (d) To remove NHR's historical equity and minority interest. The merger will result in NHC acquiring 100% of the NHR common stock.

**Table of Contents****COMPARATIVE SHARE DATA**

The historical per share earnings, dividends, and book value of NHC and NHR shown in the table below are derived from their audited financial statements as of and for the year ended December 31, 2006 and their unaudited financial statements for the three months ended March 31, 2007. The *pro forma* comparative per share data for NHC common stock and NHR common stock give effect to the merger using the purchase method of accounting as if the merger had been completed on January 1, 2006. The *pro forma* book value per share information was computed as if the merger had been completed on March 31, 2007 and on December 31, 2006. You should read this information in conjunction with the historical financial information of NHC and of NHR included or incorporated elsewhere in this joint proxy statement/prospectus, including NHC's and NHR's financial statements and related notes. The per share *pro forma* information assumes that (x) 10,822,893 shares of NHR common stock are converted into the right to receive cash consideration of \$9.00 per share and (y) 10,822,893 shares of Preferred Stock which are converted into NHC common stock at the exchange ratio. The *pro forma* data is not necessarily indicative of actual results had the merger occurred during the periods indicated. The *pro forma* data is not necessarily indicative of future operations of the combined entity.

|  | <b>Three Months<br/>Ended<br/>March 31,<br/>2007</b> | <b>Year Ended<br/>December 31,<br/>2006</b> |
|--|--|---|
| <b>Earnings per share: Basic</b>                                 |  |   |
| NHC historical   | \$ 0.56  | \$ 2.99                                     |
| NHR historical   | 0.30   | 1.25  |
| <i>Pro forma</i> combined  | 0.49   | 2.63  |
| Equivalent <i>pro forma</i> for one share of NHC common stock(1) | 0.12   | 0.64  |
| <b>Earnings per share: Diluted</b>                               |  |   |
| NHC historical   | \$ 0.54  | \$ 2.85                                     |
| NHR historical   | 0.30   | 1.25  |
| <i>Pro forma</i> combined  | 0.47   | 2.51  |
| Equivalent <i>pro forma</i> for one share of NHC common stock(1) | 0.11   | 0.61  |
| <b>Cash dividends declared per share</b>                         |  |   |
| NHC historical   | \$ 0.18  | \$ 0.69                                     |
| NHR historical   | 0.3325   | 1.43  |
| <i>Pro forma</i> combined common and preferred dividends(2)      | 0.38   | 1.49  |
| Equivalent <i>pro forma</i> for one share of NHC common stock(2) | 0.22   | 0.86  |
| <b>Book value per share (at period end)</b>                      |  |   |
| NHC historical   | \$ 20.28   | \$ 19.90                                    |
| NHR historical   | 11.22  | 11.29                                       |
| <i>Pro forma</i> combined  | 33.62  | 33.24                                       |
| Equivalent <i>pro forma</i> for one share of NHC common stock(1) | 27.82  | 27.50                                       |

- (1) The NHC equivalent *pro forma* information shows the effect of the merger from the perspective of an owner of NHC common stock. The NHR equivalent was calculated by using an assumed exchange ratio of 0.24204 shares of NHC common stock for each share of Preferred Stock.

- (2) Assumes no change in NHC's cash dividends per share of common stock. In addition, assumes that NHC will pay a dividend of \$0.80 per share of Preferred Stock.



**Table of Contents****NHC RATIO OF EARNINGS TO FIXED CHARGES AND PREFERRED STOCK DIVIDENDS**

The following table sets forth NHC's consolidated ratio of earnings to fixed charges and preferred stock dividends for the period indicated:

|  | <b>Three Months<br/>Ended<br/>March 31,</b> |             | <b>Year Ended December 31</b> |             |             |             |             |
|--|---|-------------|-------------------------------|-------------|-------------|-------------|-------------|
|  | <b>2007</b>                                 | <b>2006</b> | <b>2006</b>                   | <b>2005</b> | <b>2004</b> | <b>2003</b> | <b>2002</b> |
| Ratio of Earnings to Fixed Charges and Preferred Stock Dividends | 3.3x  | 3.2x        | 4.0x                          | 3.7x        | 3.4x        | 2.9x        | 2.4x        |

|  | <b>Three Months<br/>Ended<br/>March 31,</b> |  | <b>Year Ended December 31, 2006</b> |      |
|--|---|--|-------------------------------------|------|
|  | <b>2007</b>                                 |  |                                     |      |
| Pro Forma Ratio of Earnings to Fixed Charges and Preferred Stock Dividends |   |  | 4.6x                                | 5.5x |

NHC's consolidated ratio of earnings to fixed charges and preferred stock dividends was computed by dividing earnings in the applicable period by fixed charges for such period. For the purpose of these calculations, NHC's earnings consist of pre-tax income before minority interests or income from equity investees, plus fixed charges, amortization of capitalized interest, and the distributed income of equity investees, less interest capitalized. NHC's fixed charges consist of interest expensed, interest capitalized and an estimate of interest within rental expense. NHC had no outstanding preferred stock and neither declared nor paid dividends on preferred stock during the periods indicated.

**Table of Contents****NHR RATIO OF EARNINGS TO FIXED CHARGES**

The following table sets forth NHR's consolidated ratio of earnings to fixed charges for the periods indicated:

|                                    | <b>Three Months</b>   |             | <b>Year Ended</b>  |             |
|------------------------------------|-----------------------|-------------|--------------------|-------------|
|                                    | <b>Ended March 31</b> | <b>2006</b> | <b>December 31</b> | <b>2005</b> |
|                                    | <b>2007</b>           | <b>2006</b> | <b>2006</b>        | <b>2005</b> |
| Ratio of Earnings to Fixed Charges | 24.9x                 | 24.9x       | 24.3x              | 18.5x       |

NHR's consolidated ratio of earnings to fixed charges was computed by dividing earnings in the applicable period by fixed charges for such period. For the purpose of these calculations, NHR's earnings consist of pre-tax income before minority interests or income from equity investees, plus fixed charges and distributed income of equity investees. NHR's fixed charges consist of interest expensed. NHR had no outstanding preferred stock and neither declared nor paid dividends on preferred stock during the periods indicated.

**Table of Contents****MARKET PRICE AND DIVIDEND INFORMATION**

NHC common stock and NHR common stock are listed on the American Stock Exchange. The following table sets forth for the periods indicated the high and low per share sale prices of NHC's common stock and NHR's common stock, and the cash dividends declared during each period.

|  | <b>High</b> | <b>NHC<br/>Low</b> | <b>Dividend</b> | <b>High</b> | <b>NHR<br/>Low</b> | <b>Dividend</b> |
|--|-------------|--------------------|-----------------|-------------|--------------------|-----------------|
| 2005                                   |             |                    |                 |             |                    |                 |
| First Quarter                          | \$ 37.61    | \$ 30.00           | \$ 0.125        | \$ 21.00    | \$ 17.66           | \$ 0.3325       |
| Second Quarter                         | \$ 36.49    | \$ 30.51           | \$ 0.150        | \$ 20.10    | \$ 18.20           | \$ 0.3325       |
| Third Quarter                          | \$ 36.95    | \$ 33.62           | \$ 0.150        | \$ 20.23    | \$ 18.45           | \$ 0.3325       |
| Fourth Quarter                         | \$ 38.95    | \$ 33.83           | \$ 0.150        | \$ 20.98    | \$ 18.00           | \$ 0.4325       |
| 2006                                   |             |                    |                 |             |                    |                 |
| First Quarter                          | \$ 42.58    | \$ 36.50           | \$ 0.150        | \$ 20.95    | \$ 18.30           | \$ 0.3325       |
| Second Quarter                         | \$ 47.75    | \$ 38.26           | \$ 0.180        | \$ 19.99    | \$ 16.80           | \$ 0.3325       |
| Third Quarter                          | \$ 55.81    | \$ 39.22           | \$ 0.180        | \$ 20.41    | \$ 18.42           | \$ 0.3325       |
| Fourth Quarter                         | \$ 59.00    | \$ 49.84           | \$ 0.180        | \$ 25.30    | \$ 19.29           | \$ 0.4325       |
| 2007                                   |             |                    |                 |             |                    |                 |
| First Quarter (through March 31, 2007) | \$ 57.50    | \$ 50.02           | \$ 0.180        | \$ 24.26    | \$ 23.21           | \$ 0.3325       |
| Second Quarter (through June 30, 2007) | \$ 54.75    | \$ 49.82           | \$ 0.21         | \$ 24.10    | \$ 23.32           | \$ 0.333        |
| Third Quarter (through July 6, 2007)   | \$ 54.59    | \$ 52.00           |                 | \$ 23.97    | \$ 23.44           |                 |

On December 20, 2006, the last full trading day prior to the public announcement of the proposed merger, the closing price per share of NHC common stock quoted on the American Stock Exchange was \$56.10 and the closing price per share of NHR's common stock reported on the American Stock Exchange was \$21.29. On July 6, 2007, the most recent practicable date prior to the printing of this document, the closing price per share of NHC common stock reported on the American Stock Exchange was \$53.58 and the closing price per share of NHR common stock reported on the American Stock Exchange was \$23.95.

**NHR stockholders are encouraged to obtain current market quotations for NHC common stock prior to making any decision with respect to the merger. No assurance can be given concerning the market price for NHC common stock before or after the date on which the merger is consummated. The market price for NHC common stock will fluctuate between the date of this joint proxy statement/prospectus and the date on which the merger is consummated and thereafter.**

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**FORWARD-LOOKING STATEMENTS**

This joint proxy statement/prospectus contains forward-looking statements as that term is defined by the Private Securities Litigation Reform Act of 1995. These statements may be made directly in this joint proxy statement/prospectus, and they also may be incorporated by reference into this joint proxy statement/prospectus. These statements may include statements regarding the period following the completion of the merger and the transactions contemplated by the merger agreement.

All statements regarding expected operational efficiencies, costs savings and other benefits arising from the merger, the ability to execute the merger in the estimated timeframe, if at all, the anticipated value of the Preferred Stock or NHC's common stock, expected future financial position, results of operations or cash flows, continued performance improvements as a merged company, expected governance of NHC upon completion of the merger, the anticipated tax effects of the merger, the possibility that the merger agreement's termination fee may discourage competing third party proposals to acquire NHR and similar statements including, without limitations, those containing words such as anticipates, believes, estimates, expects, intends, may, plans, should and other similar expressions are forward-looking statements.

Forward-looking statements are not guarantees of future performance. They involve risks, uncertainties and assumptions. The future results and stockholder values of NHC and NHR, and of the combined company, may differ materially from those expressed in these forward-looking statements. Many of the factors that could influence or determine actual results are unpredictable and not within the control of NHC or NHR. In addition, neither NHC nor NHR intends to update these forward-looking statements after this joint proxy statement/prospectus is distributed except as required by applicable SEC laws and regulations.

Factors that may cause actual results to differ materially from those contemplated by forward-looking statements include, among others, those disclosed in the section entitled Risk Factors and in other reports filed by NHC and NHR with the SEC and incorporated by reference in this joint proxy statement/prospectus, as well as the following risks relating to the merger:

the value of the merger consideration that the holders of NHR common stock will receive in the merger may decline depending on the market value of the NHC common stock;

the failure to realize the intended benefits of the merger, which could have a negative impact on the market price of the shares of NHC's common stock and the Preferred Stock following the completion of the merger;

NHC and NHR may incur substantial expenses and payments if the merger does not occur;

the termination fee payable by NHR under specified circumstances may discourage third party proposals to acquire NHR that NHR stockholders may otherwise find desirable;

the financial advisors' fairness opinions will not reflect changes in circumstances between signing the merger agreement and the closing of the merger;

the directors and executive officers of NHR have interests in the completion of the merger that may differ from or conflict with the interests of the stockholders of NHR;

financial forecasts and projections considered by the parties may not be realized, which may adversely affect the market price of the NHC common stock and the Preferred Stock or the NHR common stock;

the respective financial advisors to the NHC special committee and the NHR special committee reviewed and relied on, among other things, certain projected financial forecasts and costs savings and operational synergies, and a failure of the combined company to achieve those results could have a material adverse effect on the market price of the NHC common stock and the Preferred Stock;

most of the Preferred Stock issued in the merger will be eligible for sale immediately after