UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, DC 20549

FORM 10-K/A

(Mark One)

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

For the fiscal year ended December 31, 2017

OR

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

Commission File Number: 001-14057

KINDRED HEALTHCARE, INC.

(Exact name of registrant as specified in its charter)

Delaware	**61-1323993**
(State or other jurisdiction of incorporation or organization)	**(I.R.S. Employer Identification Number)**
680 South Fourth Street Louisville, Kentucky	**40202**
(Address of principal executive offices)	**(Zip Code)**

(502) 596-7300

(Registrant s telephone number, including area code)

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

Title of Each Class	**Name of Each Exchange on which Registered**
Common Stock, par value $0.25 per share	**New York Stock Exchange**

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

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

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

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes No

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

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

Large accelerated filer	Accelerated filer
Non-accelerated filer	Smaller reporting company
	Emerging growth company

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act.

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

The aggregate market value of the shares of the registrant held by non-affiliates of the registrant, based on the closing price of such stock on the New York Stock Exchange on June 30, 2017, was approximately $974,300,000. For purposes of the foregoing calculation only, all directors and executive officers of the registrant have been deemed affiliates.

As of March 31, 2018, there were 91,279,221 shares of the registrant s common stock, $0.25 par value, outstanding.

Table of Contents

EXPLANATORY NOTE

This Amendment No. 1 to Form 10-K (this Amendment) amends the Annual Report on Form 10-K for the fiscal year ended December 31, 2017 originally filed on March 1, 2018 (the Original Filing) by Kindred Healthcare, Inc., a Delaware corporation (Kindred, Company, we, our, or us). We are filing this Amendment to present the informa required by Part III of Form 10-K as we will not file our definitive proxy statement within 120 days of the end of our fiscal year ended December 31, 2017.

Except as described above, no other changes have been made to the Original Filing. The Original Filing continues to speak as of the date of the Original Filing, and we have not updated the disclosures contained therein to reflect any events which occurred at a date subsequent to the filing of the Original Filing.

Table of Contents

TABLE OF CONTENTS

Table of Contents

Item 10. ***Directors, Executive Officers and Corporate Governance***
Board Meetings and Committees

During 2017, the Company s Board of Directors held 12 meetings, including eight regular meetings and four special meetings. During 2017, each director attended more than 75% of the total number of meetings held by the Board of Directors and each committee of which he or she was a member.

The Board of Directors has established an Audit Committee, an Executive Compensation Committee, a Nominating and Governance Committee, and a Quality of Care and Patient Outcomes Committee. Each committee has a written charter, which is available on the Company s website at *www.kindredhealthcare.com*. The Company s Corporate Governance Guidelines also are available on its website. Information on the Company s website is not part of the Form 10-K/A.

Audit Committee

The Audit Committee has four members consisting of Mr. Richard Goodman (Chair), Mr. Joel Ackerman, Mr. Christopher T. Hjelm, and Lynn Simon, M.D. Thomas P. Cooper, M.D. served as a member of the Audit Committee until he retired from the Board of Directors on May 24, 2017. Each member of the Audit Committee is independent and financially literate as defined under the listing standards of the New York Stock Exchange (NYSE). The Board of Directors has determined that Mr. Goodman and Mr. Ackerman are Audit Committee financial experts as defined in Item 407 of Regulation S-K promulgated under the Securities Act of 1933, as amended (the Securities Act), and the Securities Exchange Act of 1934, as amended (the Exchange Act). The Audit Committee held seven meetings during 2017. The Audit Committee assists the Board of Directors in monitoring: (1) the integrity of the Company s financial statements and the adequacy of the Company s system of internal controls, accounting policies, and financial reporting practices; (2) the independent registered public accounting firm s qualifications and independence; (3) the performance of the Company s internal audit function and of its independent registered public accounting firm; and (4) the Company s compliance with legal and regulatory requirements.

Executive Compensation Committee

The Executive Compensation Committee has four members consisting of Mr. Frederick J. Kleisner (Chair), Mr. Jonathan D. Blum, Ms. Heyward R. Donigan, and Sharad Mansukani, M.D. Each member of the Executive Compensation Committee is independent as defined under the listing standards of the NYSE, qualifies as an outside director within the meaning of Section 162(m) of the Internal Revenue Code of 1986, as amended (the Code), and qualifies as a non-employee director within the meaning of Rule 16b-3 under the Exchange Act. The Executive Compensation Committee held seven meetings during 2017. The Executive Compensation Committee assists the Board of Directors in fulfilling its responsibility to the Company s shareholders, potential shareholders, and the investment community by ensuring that the Company s key executives, officers, and Board members are compensated in accordance with the Company s overall compensation policy and executive compensation program. The Executive Compensation Committee recommends and approves compensation policies, programs, and pay levels that are necessary to support the Company s objectives and that are rational and reasonable to the value of the services rendered. The Executive Compensation Committee also reviews and discusses with management the Compensation Discussion and Analysis prepared for inclusion in this Form 10-K/A and, based upon such review, determines whether to recommend to the Board of Directors that the Compensation Discussion and Analysis be included in this Form 10-K/A. Furthermore, the Executive Compensation Committee prepared the section entitled Compensation Committee Report on page 43 of this Form 10-K/A.

The Executive Compensation Committee s processes and procedures for the consideration and determination of executive compensation, including the role of the Company s Chief Executive Officer in making recommendations to the Executive Compensation Committee and the role of its independent compensation consultant in assisting the Executive Compensation Committee in its functions, are more fully described below in the section entitled Compensation Discussion and Analysis beginning on page 4 of this Form 10-K/A.

Nominating and Governance Committee

The Nominating and Governance Committee has four members consisting of Mr. Jonathan D. Blum (Chair), Mr. Joel Ackerman, Mr. Richard Goodman, and Mr. Christopher T. Hjelm. Each member of the Nominating and Governance Committee is independent as defined under the listing standards of the NYSE. The Nominating and Governance Committee held five meetings during 2017. The Nominating and Governance Committee assists the Board of Directors by: (1) identifying individuals qualified to become members of the Board of Directors, approving the director nominees for the next annual meeting of shareholders, and approving nominees to fill vacancies on the Board of Directors; (2) recommending to the Board of Directors nominees and chair(s) for each committee; (3) leading the Board of Directors in its annual review of the Board of Directors performance; and (4) recommending to the Board of Directors the Corporate Governance Guidelines applicable to the Company. The Nominating and Governance Committee also recommends to the Board of Directors whether or not to accept the expected resignation of any director who fails to receive the required vote for re-election in any uncontested election as set forth in the Company s bylaws and Corporate Governance Guidelines.

Table of Contents

Quality of Care and Patient Outcomes Committee

The Quality of Care and Patient Outcomes Committee has six members consisting of Lynn Simon, M.D. (Chair), Mr. Paul J. Diaz, Ms. Heyward R. Donigan, Mr. Frederick J. Kleisner, Sharad Mansukani, M.D., and Ms. Phyllis R. Yale. Thomas P. Cooper, M.D. served as a member of the Quality of Care and Patient Outcomes Committee until he retired from the Board of Directors on May 24, 2017. With the exception of Mr. Diaz, all members of the Quality of Care and Patient Outcomes Committee are independent as defined under the listing standards of the NYSE. The Quality of Care and Patient Outcomes Committee held four meetings during 2017. The Quality of Care and Patient Outcomes Committee assists the Board of Directors in evaluating and monitoring the Company s: (1) programs, policies, procedures, and performance-improvement practices that support and enhance the quality of care provided by the Company; (2) compliance with applicable healthcare laws, regulations, policies, professional standards, and industry guidelines; and (3) compliance with the Company s Code of Conduct.

Director Selection and Evaluation

The Nominating and Governance Committee has generally identified director nominees based upon suggestions by directors, members of management and/or shareholders and outside search firms, and has interviewed and evaluated those persons on its own. The Company also engages outside search firms to identify and screen potential director candidates.

As set forth in its written charter, the Nominating and Governance Committee generally will seek directors who possess integrity, a high level of education and business experience, broad-based business acumen, an understanding of the Company s businesses and the healthcare industry in general, strategic thinking and a willingness to share ideas, a network of contacts and diversity of experiences, expertise, and backgrounds. While the Corporate Governance Guidelines do not prescribe diversity standards, as a matter of practice, the Nominating and Governance Committee considers diversity in the context of the Board of Directors as a whole and takes into account the personal characteristics and experience of current and prospective directors to facilitate deliberations that reflect a broad range of perspectives.

As set forth in the Company s Corporate Governance Guidelines, the Nominating and Governance Committee annually reviews with the Board of Directors the requisite skills and characteristics of new Board members, as well as the composition of the Board of Directors as a whole. This assessment includes a review of each director s independence, as well as consideration of diversity, age, tenure, skills, expertise, and experience in the context of the needs of the Board of Directors.

The Nominating and Governance Committee also conducts an annual evaluation of the Board of Directors and its committees, as well as of each individual director. This process includes the circulation of an evaluation form where specific questions are asked and comments sought. These results are then reviewed and discussed by the Nominating and Governance Committee and the Board of Directors. The Chair of the Board reviews the results with each individual director. On occasion, the Nominating and Governance Committee also engages outside consultants to assist in director evaluations.

The Nominating and Governance Committee uses the criteria and processes set forth above to evaluate potential nominees, and does not evaluate proposed nominees differently depending upon who has made the proposal. The Nominating and Governance Committee reviews current directors who may be proposed for re-election considering the factors and individual evaluation described above and their past contributions to the Board of Directors.

Code of Business Conduct and Ethics

The Company has adopted a Code of Conduct that serves as its code of ethics and applies to all of the Company s directors and employees, including the principal executive officer, principal financial officer, principal accounting officer, and certain other persons performing similar functions. The text of the Company s Code of Conduct is posted on the Company s website located at *www.kindredhealthcare.com* under the Investors section and is available in print to any requesting shareholder. Information contained on the Company s website is not part of this Form 10-K/A. In addition, the Company intends to disclose on its website: (1) the nature of any amendment to a provision of the Code of Conduct that applies to the Company s principal executive officer, principal financial officer, principal accounting officer, or certain other persons performing similar functions; and (2) the nature of any waiver, including an implied waiver, from provisions of the Code of Conduct that is granted to one of these specified individuals (which may only be made by the Board of Directors or a Board committee), the name of the person to whom the waiver was granted and the date of the waiver. Such disclosure will be made within four business days following the date of the applicable amendment or waiver.

The Code of Conduct generally prohibits the Company s directors, executive officers, and employees from engaging in activities that conflict with the interests of the Company and the residents and patients served by the Company. Situations that may give rise to a potential conflict of interest under the Code of Conduct include: (1) having a material direct or indirect financial or business interest in any entity that does business with the Company; (2) having a direct or indirect financial or business interest in any transaction between the Company and a third party; and (3) serving as a director, officer, employee, consultant, or agent of an organization that does business with the Company.

To facilitate compliance with these rules, the Code of Conduct requires that individuals report to their supervisors, or to the Board of Directors in the case of directors and executive officers, circumstances that may create or appear to create a conflict between the personal interests of the individual and the interests of the Company, regardless of the amount involved. In addition, each director and executive officer annually confirms to the Company certain information about potential related person transactions as part of the preparation of the Company s Annual Report on Form 10-K and its annual proxy statement. Director nominees and persons promoted to executive officer positions also must confirm such information. In addition, management reviews its records and makes additional inquiries of management personnel and, as appropriate, third parties and other resources for purposes of identifying related person transactions, including related person transactions involving beneficial owners of more than 5% of the Company s voting securities.

Section 16(a) Beneficial Ownership Reporting Compliance

Section 16(a) of the Exchange Act requires the Company s directors and executive officers and persons who own more than 10% of the Common Stock of the Company to file initial stock ownership reports and reports of changes in ownership with the Securities and Exchange Commission (the SEC). Based upon a review of these reports and on written representations from the Company s directors and executive officers that no other reports were required, the Company believes that the applicable Section 16(a) reporting requirements were complied with for all transactions that occurred in 2017.

Item 11. *Executive Compensation*

COMPENSATION OF DIRECTORS AND EXECUTIVE OFFICERS

COMPENSATION DISCUSSION AND ANALYSIS

Executive Summary

The Executive Compensation Committee (the Committee) has structured our compensation program and goal setting practices to (1) align the interests of our named executive officers and long-term shareholders, (2) ensure that compensation paid reflects both Company and individual named executive officer performance during the year, and (3) to attract, motivate and retain highly qualified senior executives that are critical for our success in a challenging and rapidly evolving healthcare sector.

We are one of the largest healthcare providers in the United States, operating in a highly regulated industry subject to a number of healthcare reform initiatives. At December 31, 2017, our (1) Kindred at Home division primarily provided home health, hospice, and community care services from 608 sites of service in 40 states, (2) hospital division operated 75 transitional care (TC) hospitals (certified as long-term acute care (LTAC) hospitals under the Medicare program) in 17 states, and (3) Kindred Rehabilitation Services division operated 19 inpatient rehabilitation hospitals (IRFs) and 99 hospital-based acute rehabilitation units (ARUs) (certified as IRFs), and provided rehabilitation services primarily in hospitals and long-term care settings in 45 states.

We operate highly regulated businesses and receive a substantial portion of our revenues from patients covered by the Medicare and Medicaid programs. We are therefore more susceptible to external pressures affecting our business, including the impact and uncertainty from regulations, legislation and other initiatives to reform the delivery and reimbursement of healthcare and reduce costs. Several of these reforms are very significant and could ultimately change the nature of our services, the methods of payment for our services, and the underlying regulatory environment.

During 2017, we faced several challenges, including the ongoing impact of new patient criteria for our LTAC hospitals, continued pressure on patient referrals across each of our business lines as payors look for lower-cost settings, further Medicare reimbursement risks and the planned disposition of our former nursing center division. These and other challenges negatively impacted our operating results and stock price performance and, as a result, also negatively impacted the amounts earned by our named executive officers under several components of our compensation program.

Despite these challenges, we were able to advance our strategic plan in 2017 as well as conduct an extensive process that resulted in the transaction pursuant to which we will be acquired by a consortium of three companies (TPG Capital, LLC, Welsh, Carson, Anderson & Stowe, L.P., and Humana Inc.) (the Merger).

Table of Contents

Our strategy is based upon three critical objectives: (1) optimizing our core operations; (2) extending our core operations by forging relationships with hospital systems and others in the post-acute continuum; and (3) positioning the Company for a value-based marketplace in which we develop care management capabilities and capture the financial upside we create.

This strategy requires that we focus on several key objectives:

(1) Succeeding in our core businesses by providing superior clinical outcomes, quality care and high customer service;

(2) Continued repositioning of our assets to enhance our performance by focusing on higher growth, less capital intensive businesses;

(3) Optimizing our Continue the Care® strategy to increase market share and improve care coordination and the quality of care;

(4) Developing differentiated care management capabilities supported by information technology, data analytics and the Kindred Contact Center; and

(5) Forge partnerships with leading health systems to gain market share, improve quality and increase efficiency.

Under the leadership of our executive officers, we were able to advance several strategic initiatives in 2017 to support our strategy.

Improving Quality and Clinical Outcomes We continued to make quality improvements in our home health and hospice operations, LTAC hospitals, and IRFs and outperformed national benchmarks. We also established new benchmarks to measure our patients customer service experience.

Portfolio Optimization and Strengthening the Core 2017 continued to be a difficult operating environment for post-acute providers. Nevertheless, we took several steps to improve our portfolio and strengthen our core operations. These actions reflect our focus on higher-growth and less capital-intensive businesses, such as our home health, hospice and IRF operations. These actions included:

Strategic Exit from the Skilled Nursing Facility Business. In late 2016, we announced our strategic decision to exit the skilled nursing facility business as an owner and operator. During 2017, we substantially completed the sale of our skilled nursing facility business and generated cash proceeds of approximately $664 million.

Enterprise Overhead Reduction. As part of a multi-step process, we were able to reduce annual enterprise overhead costs by approximately $92 million in 2017 without making reductions in caregivers at our sites of care.

LTAC Mitigation Strategy. We continued our multi-faceted mitigation strategy in response to LTAC patient criteria. During 2017, we implemented several strategies to mitigate over half of the revenue impact from LTAC criteria. We also continued to reduce our LTAC portfolio in certain markets to improve our overall operating results. For example, we closed six LTACs in 2017 and we announced plans to convert one LTAC into a free-standing IRF through a joint venture with a hospital partner.

Insurance Restructuring. In 2017, we restructured the funding and retention mechanisms of recent policy years of our professional liability and workers compensation insurance programs, which generated approximately $246 million in cash flows that were used to reduce our outstanding debt.

Growing IRF Portfolio. We have definitive agreements in place with joint venture partners to open seven additional IRFs, three of which we expect to open in 2018. We intend to continue expanding our IRF portfolio through joint ventures with leading health systems across the United States.

Advancing the Continue the Care Strategy In 2017, we advanced and operationalized our Continue the Care strategy by enhancing our processes to better facilitate patient placement, discharge planning and the transition of our patients among post-acute care settings and back home, which increased our Continue the Care performance rate by 10% compared to 2016.

Strengthening Care Management Capabilities During 2017, we continued to develop our capabilities to better manage episodes of care, optimize post-acute care placement, create seamless transitions between care settings, and enhance performance improvement reporting processes. A key component of these capabilities is our continued development and expansion of the Kindred Contact Center, a 24-hour telephone contact center staffed by registered nurses that we use to effectively manage patient populations by providing education, discharge planning and aftercare services.

Table of Contents

Our executive compensation programs are responsive to our performance

Total direct compensation for the named executive officers is primarily based on the following components: (1) base salary, (2) short-term cash incentives, (3) long-term cash incentives (including the 2017 Replacement Award and the 2017 LTIP Retention Component, each of which is defined below), and (4) equity-based incentive compensation. Since base salary is the only component of compensation that is fixed, we placed a significant portion of our Chief Executive Officer (91%) and other named executive officer (79%) compensation at risk during 2017. The chart below illustrates the mix of fixed versus variable compensation for our Chief Executive Officer and the other named executive officers, based upon target award levels.

2017 TARGET FIXED vs. VARIABLE COMPENSATION

2017 was a challenging year for us and our shareholders in terms of overall financial and stock price performance. Since our compensation program is designed to incentivize our named executive officers to achieve high levels of financial and stock price performance, their compensation is negatively impacted when they fail to achieve those results.

Upon the recommendation from our Chief Executive Officer, the Committee exercised its discretion to reduce the awards earned under our short-term incentive plan for 2017 by 20% to reflect our overall financial and stock price performance during 2017 and to better align interests with our shareholders.

Based on our 2017 performance on the metrics applicable to our short-term incentive plan, long-term incentive plan (excluding the 2017 LTIP Retention Component, as defined below) and performance-based restricted stock awards, as well as the 20% reduction set forth above:

Our Chief Executive Officer realized 53% of his targeted incentive compensation opportunity for 2017 under our short-term and long-term incentive plans and performance-based restricted stock awards (a shortfall of approximately $1.8 million); and

Our other named executive officers realized 57% of their targeted incentive compensation opportunity for 2017 under our short-term and long-term incentive plans and performance-based restricted stock awards (an average shortfall of approximately $460,000 per person).

Table of Contents

We have adopted best pay practices into our executive compensation program

The Committee regularly reevaluates our executive compensation program to achieve its stated objectives and to implement best pay practices as appropriate. To demonstrate this commitment, the Committee uses the following best practices in executive compensation:

What we do:	What we don t do:
Strongly emphasize performance-based compensation with 91% of Chief Executive Officer and 79% of other named executive officer compensation at risk during 2017	Allow hedging or pledging of Company stock
Strongly emphasize financial performance metrics with 57% of our Chief Executive Officer s targeted incentive compensation opportunity for 2017 based on financial performance metrics	Allow change in control tax gross ups
Use a leading independent compensation consultant that provides no other services to the Company to advise on executive compensation program design, pay levels and best practices	Allow backdating or repricing of options without shareholder approval
Target total direct compensation at approximately the 50th percentile of our peers	Approve change in control agreements that provide for payments above a minimum threshold without shareholder approval
Include recoupment provisions or clawbacks in our cash and equity compensation plans	Encourage unreasonable risk taking with our executive compensation program
Maintain significant stock ownership and retention policies (net shares must be held one year following a vesting or exercise date)	
Use change in control agreements and equity plans with double trigger severance/equity acceleration requirements	
Focus a significant portion of short-term incentive plan awards on strategic and operational performance goals that promote long-term value	
Use performance-based restricted stock awards as a material component of total direct compensation	
Welcome engagement with shareholders to evaluate and critique our executive compensation program	

When appropriate, use our negative discretion to reduce earned awards to better align interests with our shareholders, as we did this year by reducing our short-term incentive plan payments by 20%

We have adopted best governance practices to benefit our shareholders

The Committee, with the assistance of its independent compensation consultant, Frederic W. Cook & Co. (F.W. Cook), as well as the Company, stay attuned to recent trends in compensation and governance practices. In recent years, we have:

- Formally separated the offices of Chair of the Board and Chief Executive Officer, and further required, whenever possible, that the Chair be an independent director;
- Adopted Proxy Access (shareholders that own at least 3% of our Common Stock over a three-year period may nominate up to 20% of the Board and include such nominees in our proxy materials); and
- Achieved the highest governance rating on the Institutional Shareholder Services (ISS) QualityScore rating system for all of 2017.

Our Executive Compensation Process

The Committee is comprised entirely of independent directors who meet regularly to review and oversee the Company s executive compensation program. The Committee reviews all components of, and makes all decisions regarding, the compensation of the named executive officers. The Committee also engages a leading independent compensation consultant to advise it on several aspects of our executive compensation program.

Table of Contents

Our Chief Executive Officer (Benjamin A. Breier) and Chief Administrative and People Officer (Stephen R. Cunanan) participate frequently in meetings of the Committee to provide evaluations related to the performance of our other executive officers and discuss the roles and responsibilities of such executive officers. In addition, Committee members frequently interact directly with our executive officers and receive input from other independent Board members, thereby gaining an appreciation of the roles and levels of responsibility of the executive officers, as well as their performance. The Chief Executive Officer makes non-binding recommendations for the Committee s consideration regarding executive compensation, including base salary, incentive targets, performance measures, equity compensation and any special awards for our executive officers. The Committee also regularly holds executive sessions not attended by any members of management. The Committee discusses Mr. Breier s compensation with him and then makes decisions with respect to Mr. Breier s compensation without him present. The named executive officers other than the Chief Executive Officer and Chief Administrative and People Officer do not make recommendations on compensation or otherwise significantly participate in the Committee s compensation decision-making process.

Internal Pay Equity

Compensation opportunities for the named executive officers reflect their positions, responsibilities and tenure in a given position and are generally similar for executives who have comparable levels of responsibility (although actual compensation delivered may differ depending on relative performance). The Chief Executive Officer has generally been the most highly compensated executive due to his ultimate responsibility for the strategic direction and performance of the Company, the unique nature and scope of his leadership and the competitive marketplace for attracting and retaining a talented chief executive officer.

Evaluation of Compensation Policies and Practices as They Relate to Risk Management

The Committee believes that the performance measures it selects appropriately reward performance without encouraging unnecessary or excessive risk taking on the part of our employees. The Committee encourages our employees to balance short-term objectives with long-term operational and clinical performance and financial stability by conditioning performance-based pay on the achievement of various financial, quality, strategic and operational goals which are aligned with our key success factors and operational goals and objectives. In addition, the goals are often tied to facility, district, regional, divisional and/or enterprise performance with no single goal comprising a significant portion of the overall total target. We also have in place various controls such as internal audit functions, a compliance hotline and quality controls to further support the Committee s conclusions on its risk assessment.

Engaging with our shareholders

We have directly engaged several of our largest shareholders in the past few years to solicit feedback on our executive compensation program and governance practices.

In 2015, following a coordinated outreach campaign to our shareholders, including contacting our 25 largest shareholders (which held more than 70% of our Common Stock), (1) we adopted a Proxy Access bylaw permitting shareholders who have owned at least 3% of Common Stock for a three-year period to nominate directors constituting up to 20% of the Board and to include such nominees in our proxy materials, and (2) we amended our Corporate Governance Guidelines to require shareholder approval or ratification of amended or future change in control severance agreements that provide for payments in excess of 2.99 times base salary and target bonus under our short-term incentive plan.

At the 2016 annual meeting of shareholders, we received an 84% favorable vote on our non-binding proposal to approve the compensation for our named executive officers. This result was lower than our prior three-year average of a 94% favorable vote, and was primarily driven by an against vote issued by one of our largest shareholders. Following the annual meeting, our Chair of the Board and Chief Executive Officer met with representatives of this shareholder to learn and discuss the shareholder s concerns. In response, the Committee reviewed our executive compensation plans and practices, and asked F.W. Cook to identify potential modifications against practices within our peer group and general industry. Following further analysis, F.W. Cook confirmed that our overall executive compensation program is appropriately structured and generally consistent with our peer group. Following its detailed review of the potential modifications and F.W. Cook s analysis, the Committee elected in March 2017 to broaden the payout ranges applicable to the Consolidated Adjusted EBIT metric (as defined below) under our short-term incentive plan and the Consolidated Adjusted EBITDAR metric (also as defined below) applicable to our long-term cash incentive plan and performance-based restricted stock awards. These changes require larger changes in performance before higher award percentages are attained, making payouts above the targeted amount more challenging to achieve. At the 2017 annual meeting of shareholders, the non-binding advisory proposal to approve the compensation paid to our named executive officers received a greater than 93% favorable vote, which we believe was a result of our engagement efforts and the resulting executive compensation program refinements.

We welcome shareholder feedback on our executive compensation program and governance practices, and encourage shareholders to contact us to express their views.

Table of Contents

Use of Compensation Consultants

The Committee s charter provides that it has the sole authority to select, evaluate, retain and dismiss an independent compensation consultant. During 2017, the Committee retained F.W. Cook as its independent compensation consultant to review our executive compensation program, including base salaries, and short-term and long-term incentive compensation. Prior to engaging F.W. Cook, the Committee assessed the independence of F.W. Cook pursuant to NYSE rules and concluded that no conflict of interest exists that would prevent F.W. Cook from being an independent compensation consultant to the Committee. F.W. Cook has never served the Company in any capacity except as an independent compensation consultant to the Committee.

In 2017, F.W. Cook s review of our executive compensation program included:

- Reviewing our senior executive compensation plans;
- Benchmarking the total direct compensation levels for the executive officers, including salaries and targeted short-term and long-term incentive opportunities;
- Evaluating key executive compensation program practices among our peers, including short-term and long-term performance metrics, the prevalence of executive retirement programs, severance programs and perquisites, stock ownership guidelines, incentive compensation targets and award levels, and equity compensation usage;
- Review of our peer group based upon objective metrics;
- Comparing the actual compensation paid to our Chief Executive Officer to the amounts targeted by the Committee;
- Evaluating potential changes to our employee and director equity plans;
- Advising the Committee on recent regulatory, governance, and market-based executive compensation trends and developments; and
- Advised the Committee regarding the basis and structure of the LTIP Retention Awards (as defined below).

Based on its review of our executive compensation plans, practices and performance targets during 2017, F.W. Cook indicated that:

The majority of our named executive officers base salaries are positioned slightly below the 50th percentile of our peers, with target cash compensation generally positioned between the 25th percentile and the median of our peers;

Targeted total direct compensation was at or below the 50th percentile of our peers for each of our named executive officers other than our Chief Administrative and Chief People Officer and slightly above the 50th percentile for our Chief Administrative and Chief People Officer;

Our use of financial, strategic and operational objectives under our incentive plans continues to be consistent with the practice of our peers;

Our use of restricted stock and performance stock as part of our long-term incentive program is consistent with typical peer companies, but the additional use of performance cash is atypical (though we believe it is appropriate given our capital structure) and results in a heavier weighting of performance-based awards than our peers;

Our retirement and deferral programs are consistent with those provided by peer companies;

Our perquisite program is limited and generally more conservative than our peers but consistent with broader market practices;

Severance benefits for our executive officers are generally consistent with our peer group;

Our stock ownership guidelines for executive officers are standard among peers and the broader market;

Our three year equity plan share usage was high relative to our peers (primarily due to a depressed stock price for the 2016 grants);

Our aggregate grant date fair value ranks around the 25th percentile and potential equity plan dilution ranks in the bottom quartile of our peers; and

Granting additional performance-based LTIP awards was an appropriate retentive tool to promote executive continuity and engagement while the Company navigates a significantly challenging period.

Table of Contents

Peer Group

Consistent with the Committee s goal of providing competitive compensation, the Committee benchmarks our executive officer compensation against the executive officer compensation at a selected group of peer companies that the Committee believes compete with us for executive officers and reflects the size, scope and diverse nature of our businesses and the healthcare industry.

There are very few publicly traded companies that operate within our primary businesses of home health and hospice, TC hospitals, IRFs, and rehabilitation services, and none that operate with the same breadth and scope within each of these businesses. As such, our peer group primarily consists of healthcare companies that approximate our size, scale and complexity. We operate in several segments of post-acute care and provide healthcare services in more than 2,500 locations in 45 states. It is also useful to note that many of the companies in the peer group are not subject to the same Medicare and Medicaid reimbursement risks as we are, which can make comparisons difficult. The peer group is periodically reviewed and updated by the Committee based upon organic changes in the peer companies and upon recommendations from its independent compensation consultant. In developing the peer group, the Committee considers a variety of selection criteria such as: (1) inclusion of U.S.-based public companies in the Global Industry Classification Standard sub-industry codes for health care facilities and health care services, (2) inclusion of companies with revenues approximating one-third to three times our revenues, and (3) exclusion of companies with market capitalization greater than $40 billion. Following a detailed review with F.W. Cook, the Committee elected not to make any changes to the Company s peer group for 2017.

The Committee and its independent compensation consultant also review companies that do not meet the aforementioned criteria but are otherwise used by proxy advisory firms (such as ISS) in creating a peer group used solely by such firms for comparative analysis. Following a detailed review and upon recommendation of its independent compensation consultant, the Committee elected not to include any additional peer companies used by such proxy advisory firms because such companies (1) did not meet the above-referenced criteria, (2) were healthcare distributors or managed care companies and not healthcare service providers, and (3) thus were not subject to the same business and reimbursement risks as we were.

For each company in the peer group, the Committee reviews data including base salary, annual cash incentive compensation, long-term incentive compensation and total annual direct compensation of such company s named executive officers. The following companies comprised our peer group for compensation benchmarking purposes during 2017:

Brookdale Senior Living, Inc.	Lifepoint Hospitals, Inc.
Community Health Systems, Inc.	MEDNAX, Inc.
DaVita Inc.	Quest Diagnostics, Inc.
Envision Healthcare Holdings, Inc.	Select Medical, Inc.
Genesis Healthcare, Inc.	Team Health Holdings, Inc.
Encompass Health Corp.	Tenet Healthcare Corporation
Laboratory Corp. of America Holdings	Universal Health Services, Inc.

Table of Contents

The following chart compares us and our peer group on several of the selection criteria used by the Committee.

Company	Symbol	Revenues (1) ($ in millions)		Enterprise value (1)(2) ($ in millions)		Market capitalization (1) ($ in millions)		Number of employees (1)	
Tenet Healthcare	THC	$ 19,630	DVA	$ 25,602	LH	$ 14,064	CYH	137,000
Community Health Systems	CYH	$ 19,233	LH	$ 21,776	DVA	$ 13,670	THC	134,630
Davita	DVA	$ 14,347	CYH	$ 19,977	UHS	$ 12,000	KND	102,000
Universal Health Services	UHS	$ 9,424	THC	$ 18,436	DGX	$ 11,765	GEN	88,700
Laboratory Corp. of America Holdings	LH	$ 9,192	DGX	$ 16,973	MD	$ 6,096	BKD	82,000
Quest Diagnostics	DGX	$ 7,503	UHS	$ 16,308	EVHC	$ 4,168	UHS	74,600
Kindred Healthcare	KND	$ 7,226	BKD	$ 12,533	EHC	$ 3,642	DVA	60,400
Envision Healthcare	EVHC	$ 6,088	MD	$ 7,736	BKD	$ 3,244	LH	50,000
Lifepoint Health	LPNT	$ 5,853	EVHC	$ 7,493	LPNT	$ 2,450	EVHC	49,463
Genesis Healthcare	GEN	$ 5,656	EHC	$ 7,212	TMH	$ 2,415	DGX	44,000
Brookdale Senior Living	BKD	$ 4,262	KND	$ 7,082	THC	$ 2,255	SEM	41,000
Select Medical	SEM	$ 4,178	GEN	$ 6,652	SEM	$ 1,775	LPNT	40,000
Team Health	TMH	$ 4,137	SEM	$ 6,144	CYH	$ 1,311	EHC	34,700
Encompass	EHC	$ 3,432	LPNT	$ 5,515	KND	$ 871	TMH	18,800
MEDNAX	MD	$ 2,988	TMH	$ 4,922	GEN	$ 240	MD	11,885
75th percentile		$ 9,366		$ 18,070		$ 10,348		80,150
Median		$ 5,971		$ 10,135		$ 3,443		49,732
25th percentile		$ 4,199		$ 6,792		$ 2,295		40,250
Percentile rank		60%		29%		5%		87%

(1) These amounts represent information as of September 30, 2016 as prepared by F.W. Cook and reviewed by the Committee in selecting the peer group.
(2) Enterprise value equals the market capitalization plus total debt minus cash and cash equivalents with an adjustment for the latest fiscal year rental expense capitalized at eight times.

Components of Executive Compensation

Our executive compensation program generally uses the following components to structure the total direct compensation for the named executive officers: base salary; short-term cash incentives; long-term cash incentives; and equity-based incentive compensation. In addition, from time to time the Committee considers the grant of special one-time awards which enable it to reward executive officers in special circumstances or provide mechanisms to retain executive officers. Each of these components is discussed in more detail below.

Table of Contents

As illustrated in the chart below, we utilize a variety of incentive compensation plans and performance measures to link named executive officer compensation to our short-term and long-term performance in meaningful ways. These financial, quality, strategic and operational goals encourage the named executive officers to strive for appropriate financial results related to our operating budget and key financial measures, while maintaining an appropriate focus on the quality and customer service objectives that are critical to ensuring patient satisfaction and regulatory compliance and achieving favorable short-term and long-term financial results.

SUMMARY OF KEY COMPONENTS OF EXECUTIVE COMPENSATION

Component	Performance Period	Vesting /Payout Timing	2017 Performance Metrics	Target Incentive Opportunity for 2017 (% of Salary) CEO	Other NEOs
Short-Term Incentive Plan (Cash)	One year	Paid in full in the year following the end of the performance period	Consolidated Adjusted EBIT, Adjusted EBITM, growth, efficiency, quality, customer satisfaction, employee turnover, and capital goals	125%	80% - 60%
Long-Term Incentive Plan (Cash) (1)	Each tranche based upon performance during one year (with a three year total shareholder return modifier)	Paid in full one year following the end of the three-year award period	Consolidated Adjusted EBITDAR, Consolidated Adjusted Free Cash Flows, and relative total shareholder return	75%	60% - 50%
Performance-Based Restricted Stock Units	Each tranche based upon performance during one year	Vest pro rata over three years	Consolidated Adjusted EBITDAR and Consolidated Adjusted Free Cash Flows	(2)	(2)
Service-Based Restricted Stock	n/a	Vest pro rata over three years	n/a	(2)	(2)

(1) For 2017, the Committee also made retention awards under the LTIP. See LTIP Retention Awards below.
(2) Awards vary based upon peer analysis, our performance and the named executive officer s individual performance as discussed in more detail below.

Base Salary

The base salary for each named executive officer is determined annually by the Committee following a review of each individual executive officer s performance, changes in the executive officer s position or responsibility, relevant comparisons to peer group data, an assessment of our overall or division performance, and a consideration of general market salary increases for all employees. The Committee generally attempts to establish base salaries at or approximately the 50th percentile of our peer group because it believes that a significant portion of total compensation should be subject to the attainment of performance goals. Since awards under our cash incentive plans are calculated as a percentage of base salary, the Committee also considers how changes in base salary may impact the total direct compensation opportunity for the named executive officers. In 2017, base salary was 11% of Mr. Breier s targeted total annual direct compensation and approximately 23% of the targeted total annual direct compensation for the other named executive officers.

Table of Contents

In February 2017, the Committee conducted its annual review of base salaries for the named executive officers. The Committee recognized that the base salaries were at or slightly below the 50th percentile for each of the named executive officers other than Messrs. Wallace and Causby, which were each slightly above the 50th percentile.

The following chart reflects the changes in base salary for the following named executive officers from 2016 to 2017:

	2016	2017
Mr. Breier, President and Chief Executive Officer	$ 1,050,000	$ 1,100,000
Mr. Farber, Executive Vice President, Chief Financial Officer	$ 606,000	$ 650,000
Mr. Wallace, Executive Vice President and Chief Operating Officer	$ 707,000	$ 715,000
Mr. Causby, Executive Vice President and President, Kindred at Home	$ 575,000	$ 600,000
Mr. Cunanan, Chief Administrative and Chief People Officer	$ 404,000	$ 435,000

In 2017, the Committee increased Mr. Breier s base salary to reflect his continuing strong performance in leading our strategic and operational efforts and to move his base salary to the median of the peer group based on data provided by F.W. Cook. The Committee increased Mr. Causby s base salary to reflect his continuing leadership of our Kindred at Home division and to move his total direct compensation closer to the median of the peer group based on data provided by F.W. Cook. The Committee increased Mr. Farber s and Mr. Cunanan s base salaries in response to a continued high level of performance. The Committee also increased Mr. Wallace s base salary by 1% over the previous year, consistent with how base salaries were treated across the Company during 2017.

Cash Incentives

Under our executive compensation program, a significant portion of total cash compensation for the named executive officers is subject to the attainment of objective financial, quality, strategic and operational goals. We use two cash incentive plans: an annual short-term incentive plan and a long-term incentive plan (LTIP). All named executive officers participated in both of these plans for 2017.

Short-Term Incentive Plan

Under the short-term incentive plan, the Committee establishes company-wide and divisional annual financial and quality goals, as well as specific strategic and operational goals for our named executive officers. In establishing annual performance goals, the Committee considers the appropriate relative weighting of financial, quality, strategic and operational goals on an annual basis and seeks to appropriately reward performance without encouraging unnecessary or excessive risk taking on the part of our employees.

Target Award Levels Annual cash bonuses under the short-term incentive plan are determined as a percentage of the named executive officer s base salary. The following chart reflects the target award levels for each named executive officer as a percentage of his base salary for 2017. The target award levels for each of the named executive officers were unchanged from 2016.

	2017 Target Award Level
Mr. Breier	125%
Mr. Farber	80%
Mr. Wallace	80%
Mr. Causby	60%
Mr. Cunanan	60%

Use of Financial, Quality, Strategic and Operational Goals For 2017, the financial goals for the named executive officers were based upon our operating budget approved by the Board of Directors and other financial metrics that support the achievement of our 2017 operating budget. We believe that certain of these financial goals are measures generally used by investors to value our Common Stock and are therefore appropriate goals to motivate executive performance. The quality goals were based upon key quality metrics across our operating divisions and new initiatives to enhance quality of care and customer service. The quality goals are objective measures and are established with a view to be challenging but achievable with solid operational focus on our businesses. The Committee believes that maintaining or improving the quality of our services is critical to our core services and reputation, as well as attaining our financial results. The Committee also used divisional financial and quality goals for Mr. Causby given his primary responsibility for the operations of our Kindred at Home division. The strategic and operational goals used for 2017 include measurable goals that are related to our strategic plan and are more specifically described below.

Weighting of Goals The following charts reflect the relative weighting of the consolidated financial and quality goals, strategic and operational goals, and divisional financial and quality goals (to the extent applicable) for 2017 assuming target performance. At the beginning of the performance period, the Committee may adjust the weighting between goals depending on our needs or strategic imperatives and the named executive officer s areas of responsibility.

Table of Contents

	Weighting of Target Award			
	Consolidated Financial and Quality Goals (see page 15)	Strategic and Operational Goals (see pages 16 and 17)	Divisional Financial and Quality Goals (see page 16)	Total Target Percentage
Mr. Breier	60%	40%		100%
Mr. Farber	70%	30%		100%
Mr. Wallace	70%	30%		100%
Mr. Causby	20%	20%	60%	100%
Mr. Cunanan	60%	40%		100%

Threshold Goals The Committee established minimum consolidated and divisional financial performance thresholds that must be achieved in order for the financial and quality components of the short-term incentive awards to become payable, thereby ensuring sufficient financial performance by us to support the cash incentives. As such, the consolidated or divisional financial and quality components of the 2017 short-term incentive awards are forfeited in the following circumstances:

- for each of the named executive officers, if we failed to satisfy 90% of the targeted Consolidated Adjusted EBITDAR (as defined below) goal of approximately $765.2 million[1]; or

- for Mr. Causby, if the Kindred at Home division failed to satisfy 90% of the targeted consolidated adjusted earnings before interest, income taxes, depreciation, amortization, rent and management fee (KAH Adjusted EBITDARM) goal of approximately $388.9 million[2].

These two threshold goals were achieved in 2017.

(1) Our performance goals include the non-GAAP financial measure earnings before interest, investment income, income taxes, depreciation, amortization, and total rent from continuing operations (EBITDAR), as adjusted for certain items as described below (Consolidated Adjusted EBITDAR). We believe that income (loss) from continuing operations is the most comparable GAAP measure to Consolidated Adjusted EBITDAR. Our 2017 performance goals and the actual comparative results for purposes of the 2017 calculation of Consolidated Adjusted EBITDAR exclude the 2017 Adjustments (as defined below).

(2) Our performance goals include the non-GAAP financial measure KAH Adjusted EBITDARM. We believe that income (loss) from continuing operations is the most comparable GAAP measure to KAH Adjusted EBITDARM. Income (loss) from continuing operations is reported on a consolidated (rather than a segment) basis in our Annual Report on Form 10-K filed with the SEC on February 28, 2018 (the 2017 Audited Financials). The actual performance achieved towards the KAH Adjusted EBITDARM performance goal is based upon earnings before interest, income taxes, depreciation, amortization, total rent and management fee (EBITDARM) from continuing operations for the Kindred at Home segment. Our 2017 performance goals and the actual comparative results for purposes of the 2017 calculation of KAH Adjusted EBITDARM exclude the 2017 Adjustments (as defined below) but include the impact of non-controlling interests.

Table of Contents

Financial and Quality Goal Performance The following chart sets forth the minimum, target and maximum consolidated and divisional financial and quality goals under the short-term incentive plan for 2017, as well as the relative weight of each specific goal and the actual level achieved. Actual results between these goals are interpolated on a straight-line basis.

Short-Term Incentive Plan

Consolidated Financial and Quality Goals

(applicable for All Named Executive Officers)

	2017 Incentive Goals							% of
	Minimum		Target		Maximum		Actual	Target
		% of		% of		% of	Performance	Bonus
	Goal	Bonus	Goal	Bonus	Goal	Bonus	Achieved	Achieved
Consolidated Adjusted EBIT ($ millions) (1)	$ 342.6	15.0%	$ 380.7	30.0%	$ 418.8	95.0%	$ 354.5	19.68%
Accounts receivable days outstanding 1 Q	66.3	1.0%	63.0	2.5%	60.0	3.75%	61.8	3.0%
Accounts receivable days outstanding 2 Q	64.2	1.0%	61.0	2.5%	58.1	3.75%	61.2	2.41%
Accounts receivable days outstanding 3 Q	63.2	1.0%	60.0	2.5%	57.1	3.75%	66.2	0.0%
Accounts receivable days outstanding 4 Q	64.2	1.0%	61.0	2.5%	58.1	3.75%	66.2	0.0%
Consolidated revenues ($ millions)	$ 6,364	4.0%	$ 6,698.9	10.0%	$ 7,033.8	15.0%	$ 6,541.1	7.17%
Cost reductions ($ millions)	$ 70.0	8.0%	$ 85.0	20.0%	$ 100.0	30.0%	$ 92.0	24.67%
Hospital division clinical quality mix	2.19	2.0%	2.08	5.0%	1.98	7.5%	1.78	7.5%
Nursing center division health deficiency index	1.05	2.0%	1.0	5.0%	0.95	7.5%	1.01	4.43%
Rehabilitation customer satisfaction	4.17	2.0%	4.39	5.0%	4.61	7.5%	4.48	6.02%
Kindred at Home patient equality	85.5%	2.0%	90.0%	5.0%	94.5%	7.5%	95.7%	7.5%
Aggregate employee turnover	24.3%	2.0%	23.1%	5.0%	22.0%	7.5%	22.4%	6.59%
Voluntary officer turnover	5.26%	2.0%	5.0%	5.0%	4.76%	7.5%	13.2%	0.0%

Total	43.0%	100.0%	200.0%	89.0%

Table of Contents

Short-Term Incentive Plan

Kindred at Home Division Financial and Quality Goals

(applicable for Mr. Causby)

	2017 Incentive Goals							
	Minimum		Target		Maximum		Actual	% of Target
	Goal	% of Bonus	Goal	% of Bonus	Goal	% of Bonus	Performance Achieved	Bonus Achieved
Kindred at Home Division Adjusted EBITM ($ millions) (2)	$ 327.1	15.0%	$ 363.4	30.0%	$ 399.7	95.0%	$ 343.1	21.6%
Accounts receivable days outstanding 1 Q	60.0	1.5%	57.0	3.75%	54.3	5.625%	54.2	5.625%
Accounts receivable days outstanding 2 Q	53.5	1.5%	50.8	3.75%	48.4	5.625%	52.3	2.4%
Accounts receivable days outstanding 3 Q	52.4	1.5%	49.8	3.75%	47.4	5.625%	52.5	0.0%
Accounts receivable days outstanding 4 Q	51.2	1.5%	48.6	3.75%	46.3	5.625%	51.2	1.5%
Total net revenues ($ millions)	$ 2,475.5	6.0%	$ 2,605.8	15.0%	$ 2,736.1	22.5%	$ 2,544.7	9.6%
Star rating patient quality	85.5%	2.0%	90.0%	5.0%	94.5%	7.5%	94.5%	7.5%
Star rating patient experience	85.5%	2.0%	90.0%	5.0%	94.5%	7.5%	96.8%	7.5%
Hospice audit compliance	90.3%	4.0%	95.0%	10.0%	99.8%	15.0%	97.0%	12.0%
Total gross margin %	45.7%	2.0%	48.1%	5.0%	50.5%	7.5%	47.5%	3.8%
Total operating expense as % of revenue	32.7%	2.0%	31.1%	5.0%	29.6%	7.5%	31.0%	5.0%
Employee turnover	26.3%	4.0%	25.0%	10.0%	23.8%	15.0%	24.2%	14.0%
Total		43.0%		100.0%		200.0%		90.5%

(1) Our performance goals include the non-GAAP financial measure earnings before interest, investment income and income taxes (EBIT) from continuing operations, as adjusted for certain items as described below (Consolidated

Adjusted EBIT). We believe that income (loss) from continuing operations is the most comparable GAAP measure to Consolidated Adjusted EBIT. Consolidated Adjusted EBIT for the year ended December 31, 2017 is calculated by excluding from EBIT the following items: (1) items separately disclosed in our earnings release as non-core; (2) operating results of acquisitions that are not included in the original budget; (3) operating results of closures or divestitures after disposal date that are not included in the original budget; (4) unplanned or unbudgeted employee relations/severance costs; (5) asset impairment charges; (6) impact of accounting policy changes; (7) business interruption losses associated with Hurricanes Harvey and Irma; and (8) operating results of skilled nursing facilities for periods after qualifying as discontinued operations under GAAP (the 2017 Adjustments).

(2) Our performance goals include the non-GAAP financial measure earnings before interest, investment income, income taxes and management fee (EBITM) from continuing operations, as adjusted for certain items as described below (Adjusted EBITM). We believe that income (loss) from continuing operations is the most comparable GAAP measure to Adjusted EBITM. Income (loss) from continuing operations is reported on a consolidated (rather than a segment) basis in the 2017 Audited Financials. The actual performance achieved towards the divisional 2017 EBITM performance goals is based upon segment EBITM from continuing operations. Our 2017 performance goals and the actual comparative results for purposes of the 2017 calculation of Adjusted EBITM excludes the 2017 Adjustments but includes the impact of non-controlling interests.

Strategic and Operational Goal Performance As noted previously, a significant portion of the named executive officer s short-term incentive award is based on the achievement of strategic and operational goals. The target award allocation varies among the named executive officers and also provides for the potential to earn up to 200% of the target award for maximum performance. The strategic and operational portion of the 2017 short-term incentive award was structured as follows:

we must achieve at least a pre-established and objective Consolidated Adjusted EBITDAR (as defined below) threshold goal of approximately $765.2 million (the Threshold Goal), which was achieved in 2017;

since the Threshold Goal for 2017 was achieved, the named executive officers are eligible for the maximum strategic and operational award potential of 200% of their individual target. If the Threshold Goal had not been achieved, then the corresponding strategic and operational portion of the award is zero; and

the Committee exercises its negative discretion to adjust the maximum award downward for any individual, depending on the achievement of the specified strategic and operational goals identified below.

16

Table of Contents

The Committee established the following strategic and operational goals for 2017:

- continue to develop our quality and service culture, including compliance with our corporate integrity agreements and enterprise-wide quality goals;
- achieve cost containment and Continue the Care performance goals;
- execute on the disposition of our skilled nursing facility assets;
- mitigate 75% of the revenue impact of LTAC patient criteria;
- advance care management capabilities and network development initiatives to support integrated care and new payment models; and
- continue our talent and human resources development efforts, including expanding diversity representation and retaining key officers.

The Committee evaluated the performance of the named executive officers across all of the relevant strategic and operational goals within the context of our overall performance and noted the following:

- we completed an enterprise-wide dashboard for quality measures, including benchmarks for key quality measures;
- we successfully exited a corporate integrity agreement and continue to meet applicable performance metrics under a remaining corporate integrity agreement;
- we improved our Continue the Care performance and achieved significant overhead savings;
- we mitigated a substantial portion of the revenue impact under new LTAC patient criteria but below the targeted goal;
- we substantially completed the skilled nursing facility divestitures during 2017;
- we executed two gain share risk-based payment arrangements in 2017;

we made significant progress towards building a care management platform product offering and information technology capabilities; and

we achieved diversity hiring and promotion initiatives and conducting extensive talent reviews for all executive committee members, senior executives and market leaders.

Short-Term Incentive Payouts; Reductions to Earned Awards

Based on the actual performance achieved and the Committee s evaluation of the named executive officers performance under our financial, quality, strategic and operational goals, the named executive officers earned aggregate short-term incentive bonuses for 2017 as set forth below under the column Total Award Earned. Upon the recommendation from our Chief Executive Officer, the Committee exercised its discretion to reduce the awards earned under our short-term incentive plan for 2017 by 20% to reflect our overall financial and stock price performance during 2017 and to better align interests with our shareholders.

	Percent Earned									
	Consolidated Financial/ Quality (a)	**Strategic and Operational (b)**	**Divisional Financial/ Quality (c)**	**Total (a + b+c)**		**Potential Target Bonus**	**Base Salary**	**Total Award Earned**	**Less Discretionary Reduction**	**Actual Payout**
Mr. Breier	53.4%	46.6%		100%	x					