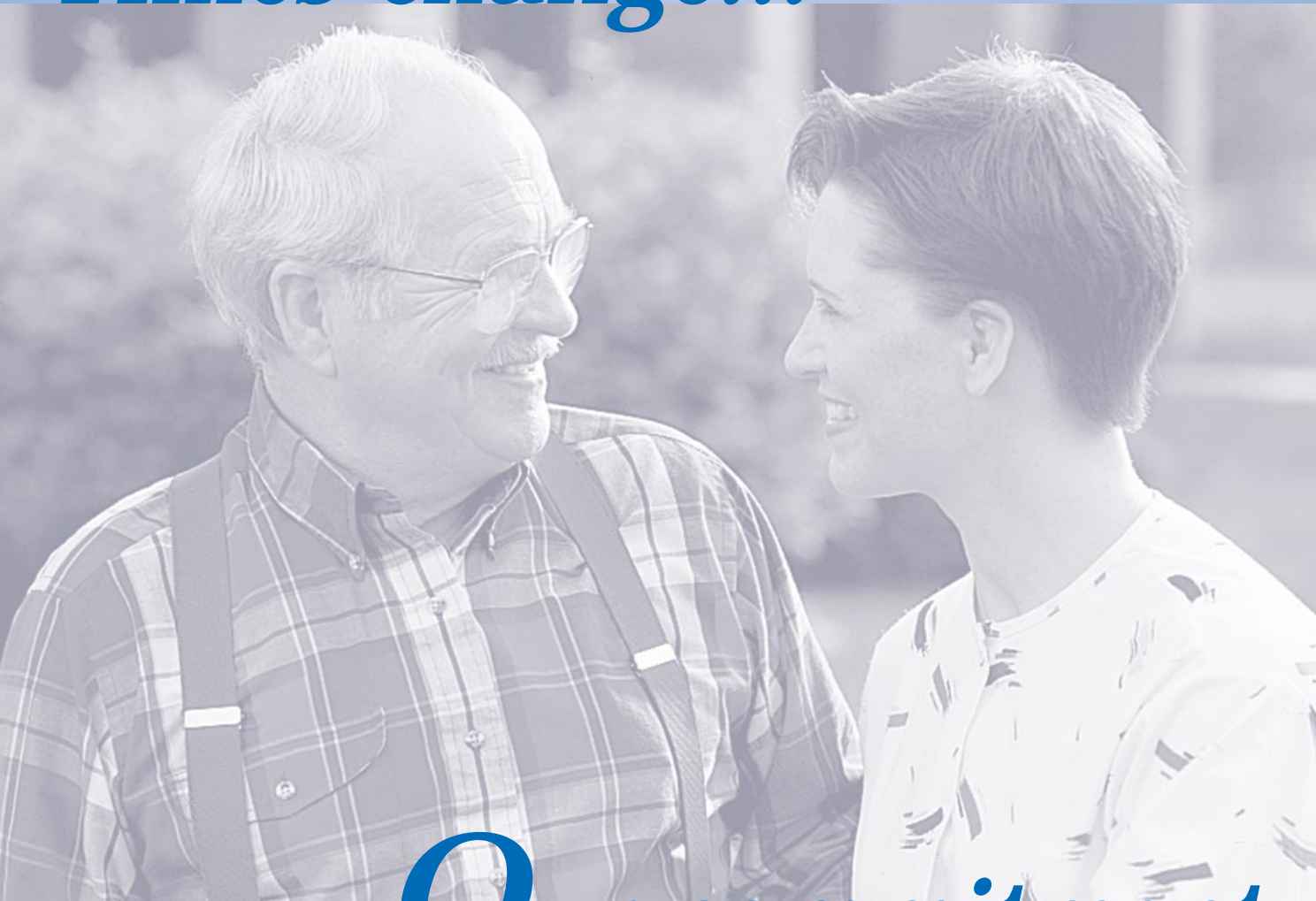


EXTENDICARE

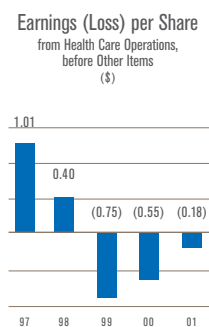
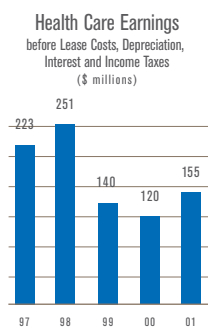
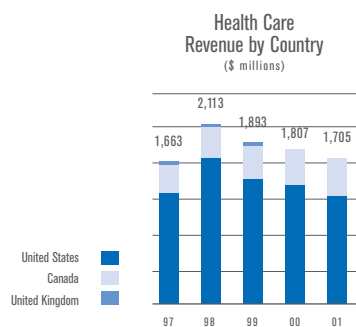
*Times change...*



*Our commitment  
does not.*

**2001 Annual Report**

# Financial Highlights



(thousands of dollars unless otherwise noted)

	2001	2000	1999
Revenue	1,704,511	1,807,406	1,892,687
Earnings before lease costs, depreciation, interest and income taxes	155,359	119,998	139,842
Loss from health care before undernoted	(11,678)	(39,747)	(55,163)
Loss from asset disposal and other items, net of tax	(35,466)	(27,358)	(127,357)
Loss from health care	(47,144)	(67,105)	(182,520)
Share of earnings of Crown Life	10,738	7,827	22,818
Loss	(36,406)	(59,278)	(159,702)
Earnings (loss) per share			
Health care operations before undernoted and after preferred share dividends	(0.18)	(0.55)	(0.75)
Loss from asset disposal and other items	(0.49)	(0.36)	(1.69)
Share of earnings of Crown Life	0.15	0.10	0.30
Basic and diluted loss per share	(0.52)	(0.81)	(2.14)
Cash provided by operations, before changes in working capital	60,002	73,132	94,138
Cash flow per share	0.83	0.98	1.25
Property and equipment capital expenditures	45,377	46,292	50,268
Total assets	1,740,246	1,735,752	1,834,123
Shareholders' equity	350,696	381,437	435,933
Book value per share	4.61	4.90	5.53
Number of Subordinate and Multiple Voting Shares purchased for cancellation	1,969,500	1,284,100	1,197,800

## Contents

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# Core Values

Rapidly changing political and social dynamics are transforming long-term care across North America. • As we position our business to turn challenge to opportunity, some things will not change. • Our **commitment** to our clients, our employees, and our shareholders, remains the same today as it was yesterday. And it is the same today as it will be tomorrow. • We owe them unwavering **dedication** to the core values that have been the foundation of our Company for more than 30 years and that will continue to drive its success. • Success means providing **quality care** to each person who entrusts us with his or her personal health and dignity. We endeavor to make each day an affirmation of life. Providing quality service to clients is our highest priority. • Success means **energizing employees** to live our vision of excellence. Good people are our greatest strength. That is why we strive to create enjoyable and rewarding work environments. • Success means achieving **profitable growth** over the long term to create value for our shareholders. We are committed to communicating effectively with them. • So we're not interested in stopping the tide of change. We plan to ride its crest. Performance – for all our stakeholders – is the key to our success.

That's because times change, but our commitment does not.

## Testimonials

**commitment** “Our family is spread throughout the United States and we visit intermittently. My siblings have all remarked to me that Dad is...very content in your care...His privacy is respected. He remarks how he loves the food. He’s becoming more social. He is treated with professionalism and kindness. Always...As a result, I can honestly report that Dad hasn’t looked and felt this good in many years.”

Barbara A. Klein (daughter of George Klein), North Carolina, January 2, 2002

**dedication** “My Mother suffered from a massive stroke which left her totally unable to care for her own needs...the nursing staff and aides were exceptional in providing for privacy, minimizing the hard reality of a feeding tube, and expressing concern and maintaining her comfort...You are very lucky, actually I was the lucky one, to have a staff who do take great pride in the services they provide and the care they give... You can be sure that if I have future need of health and rehab facilities, yours will be the only one I will ever use.”

Cheryl Stewart (daughter of Mildred Schnitzer), Washington, November 28, 2001

**quality care** “From the first day [my Sister] was admitted, I have been so very impressed with the level of care and attention she has received...To begin with, she was treated by the staff with dignity and interest and not simply ‘passed into the system’. She was made to feel at home and her concerns were listened to and dealt with. The time that was spent with her that morning was not just a pro forma procedure but has continued on a daily basis and is how she has been treated ever since.”

Doug White (brother of Margaret White), Ontario, January 30, 2001

**energizing employees** “In the end you can have the nicest surroundings but if the staff does not care then those feelings get translated to the residents. I am happy to say it is my firm belief that your staff does care about the residents and I believe that in business, everything starts with the right attitude from the top. So my sincere thanks...for doing all the right things.”

Rick Field (son of Harold Field), Ontario, June 14, 2001

## Message to Shareholders



**Mel Rhineland**  
President and  
Chief Executive Officer

### Fellow Shareholders:

When I assumed Extencicare's leadership last year, I told you the core values that have made our Company a respected long-term care leader in North America for more than 30 years will not change.

That remains our fundamental commitment.

The most successful companies will be those that consistently deliver on the promise of quality care to residents. This not only means satisfying physical, social, emotional and intellectual needs but listening carefully to ensure that we do things right. It is why we pursue many ways of delivering and measuring services – like resident and family advisory councils, education sessions and community programs, customer surveys and response lines, and voluntary accreditation of facilities.

Budget constraints are posing risks to health care funding. This reality, combined with proliferating regulations, creates challenges for long-term care providers. Yet we remain dedicated to providing the same high levels of service.

Companies that thrive in a changing environment will be adept at addressing challenges. That is why we have raised the bar for the individuals we recruit. Outstanding people have joined us, as we made key changes at our regional and corporate offices, and we expect to further strengthen our organization in 2002.

Leadership is critical to differentiating winners from losers – distinguishing those who will accomplish their goals from those who will not. Resilient leadership ensures that core values are understood, believed, supported and implemented across the organization.

At the same time, we have many long-term, front-line employees whose hard work and skill too often goes unacknowledged in our communities. Their dedication and commitment to service delivery at the bedside are our Company's foundation.

Finally, the most successful companies will be those that resolutely build value for their shareholders – companies that both communicate coherent strategies and carry them out.



**Mark Durishan**

Vice-President, Finance, and  
Chief Financial Officer

**Philip Small**

Senior Vice-President,  
Strategic Planning and Investor Relations

**Richard Bertrand**

Senior Vice-President, Development

**The most successful companies will be those that consistently deliver on the promise of quality care to residents...and remain committed to building shareholder value.**

We are confident that this approach was instrumental in enabling us to exceed our 2001 forecast. As anticipated, the second half of the year was stronger than the first and Extendicare was profitable in the fourth quarter, with both our U.S. and Canadian operations contributing positively to earnings.

We will continue to improve our results by disposing of assets that impede growth or create undue risk exposure, and by obtaining better performance from our other facilities. However, our disposition program is largely completed. We exited Florida at year-end 2000 and the Texas nursing home market on October 1, 2001. Getting out of these markets represented a huge step toward reducing our resident care liability exposure.

Our strategies for improving U.S. payor mix are beginning to pay off. U.S. Medicare census rose in the 2001 fourth quarter compared to both the third quarter of the year and the fourth quarter of 2000. Medicare patient days increased by just over 6% in 2001 and, in the second half of the year, Medicare census levels were up more than 8% from the same period in 2000.

Census development is key to the financial success of our U.S. company, Extendicare Health Services, Inc. (EHSI).

In our view, these initiatives reflect a turning point in our performance. The fourth and final year of the Prospective Payment System (PPS) phase-in began January 1, 2002, resulting in reduced Medicare funding. While we must continue to refine our ability to work effectively under this system, we believe that higher census levels are attainable and we have made increasing census a top priority.

Although the assisted living market was soft throughout 2001, an industry-wide construction slowdown enhanced the prospects of filling existing units and we expect this to increase future occupancy levels. Assisted living accounted for 3% of our revenue last year.

U.S. employee turnover levels remain a problem for our industry but improved at EHSI in 2001. We continued our efforts to attract people who enjoy the challenge of providing care.

In Canada, Extendicare is the second largest operator of long-term care facilities and, through our ParaMed Home Health Care division, the largest private home care provider.

## Message to Shareholders

The first five openings of new Extendicare (Canada) Inc. (ECI) nursing homes in more than a decade proceeded smoothly and demonstrated our ability to meet our growth objectives on time and on budget. An additional ECI nursing home will open in 2002 and five more in 2003.

ECI's success in winning awards to own or manage new nursing home beds, under a multi-year Ontario government program, was among the highest of any operator in the Province.

ParaMed is the market leader in Canadian home health care delivery, both in quality and pricing. Home care represented 10% of Extendicare's 2001 revenue. Margins and profitability were up but volumes were down because of budget constraints by the Ontario Community Care Access Centres that contract for the services. We believe volumes will stabilize by the end of 2002.

In Canada, our goals in 2002 involve: constructing and opening new homes and maximizing their occupancy; maintaining high occupancy levels in existing facilities; growing our group purchasing, management and consulting operations; and enhancing ParaMed's leadership.

Health systems across North America are in a complex state of tension that cries out for solutions. Our approach is to be a thinking partner of the various jurisdictions in which we do business – to solve problems and influence best practices. We do this by taking a leadership role in trade associations and through direct relationships with political and regulatory authorities.

In the United States, we will continue to press for higher levels of state Medicaid funding, which is currently inadequate to meet care requirements. A further uncertainty is whether temporary Medicare increases will be extended beyond September 30, 2002. Industry efforts are underway to obtain an extension but a decision is unlikely until much closer to the sunset date.

Our objectives include diversifying within the long-term care continuum in North America. While nursing homes are our core business and accounted for 83% of our revenue in 2001, associated opportunities – management and consulting services; group purchasing of food, supplies and capital equipment for our own and other long-term care companies; Canadian home health care; ProStep rehabilitative clinics and Virtual Care Provider information technology services – have a growing impact on our profitability.

Remember, we have a steadfast commitment to quality care for every resident. But we are managing differently in a changing environment. This means ensuring that our U.S. and Canadian companies exchange knowledge and share services, creating synergies that minimize costs and maximize efficiencies.

Overall, we see great potential for growth. Long-term care providers serve the fastest growing segments of the population.

## Message to Shareholders

So while times are changing, we are convinced that Extencicare can turn these changes into opportunities. Government restrictions on supply, coupled with an aging population, are causing overall declines in availability of long-term care beds. Meanwhile, average acute care hospital stays have shortened, while advances in medical technology allow certain treatments outside hospital settings. Consequently, more patients require the kind of complex care offered by our U.S. nursing homes at much lower costs than in traditional acute care and rehabilitation hospitals.

Extencicare has competitive strengths that are crucial to future success. We own rather than lease 91% of the facilities that we operate, excluding those we manage, which gives us great flexibility.

In addition, we geographically cluster facilities to offer wide-ranging care and services and improve operating efficiencies. We primarily target smaller urban areas where we maintain a strong reputation as a locally-oriented provider closely linked to the community.

While many challenges remain, our plan calls for 2002 to be profitable from ongoing operations, assuming temporary U.S. Medicare funding increases continue beyond September 2002.

Our faith in the value of our Company is underscored by our purchase and cancellation of nearly 4.5 million Subordinate and Multiple Voting Shares at an average price of \$3.89 since 1999.

Thanks are due to everyone who contributed to Extencicare's improved results in 2001. In particular, thanks to our Board of Directors, whose guidance was crucial to the Company's accomplishments. And I especially want to express my appreciation to Extencicare's clients, employees and shareholders. Your confidence empowers our Company's growth in a changing environment – and drives our commitment to the unchanging values of which we all can be proud.



### **Mel Rhineland**

President and  
Chief Executive Officer

## United States Operations

Extendicare's improved U.S. performance in 2001 confirmed that we have made the right decisions in restructuring our asset portfolio and refocusing our growth plans, as our U.S. operating company, Extendicare Health Services, Inc. (EHSI), returned to profitability in the fourth quarter. This is a key development for the Company as a whole, since revenue from U.S. operations accounted for 73% of Extendicare's total business last year.

We continually review the performance of our assets. During the last three years we have improved the financial results of a number of facilities while determining that others no longer meet our criteria for financial or operational performance. As a consequence, EHSI ceased all Florida operations at year-end 2000 and those of its Texas nursing homes at the start of the 2001 fourth quarter.

Florida and Texas have been excessively litigious for long-term care companies. By exiting the Florida market, we eliminated our liability for incidents there subsequent to December 31, 2000. The Texas transaction had the same effect for events in that State after September 30, 2001.

The final phase-in of the Medicare Prospective Payment System (PPS) took effect on January 1, 2002. However, industry concerns with respect to Medicare are primarily focused on whether certain temporary funding increases will continue beyond September 2002. Vigorous lobbying is underway to obtain an extension, which is integral to our goal of achieving sustained profitability for EHSI.

Entering 2001, EHSI was awarded a second consecutive national contract with the Veteran's Administration (VA), which puts our Company on a provider list for veterans seeking nursing home placements over the next three years. EHSI is particularly pleased with this achievement because of the high performance levels required to attain a VA contract.

An increasing percentage of our census is coming from Medicare admissions, which underscores the strong relationships we have established with hospitals, discharge planners and physicians. In fact, over 90% of our admissions are Medicare patients. Since Medicare services produce higher margins, we will continue to target our marketing to increase Medicare referrals.

We will intensify our marketing efforts to improve census for both skilled nursing and assisted living facilities. In addition, we are examining opportunities to develop specialized programs, such as dementia units, based on local market needs.

The long-term care industry continues to experience a shortage of qualified personnel. Consequently, we are taking a disciplined approach to recruitment and retention of personnel, while working hard to reduce our use of agency staff. Since 1999, we have granted stock options to more than 300 facility-level employees annually, in recognition of their fundamental contribution to the Company's performance. EHSI's overall turnover rates improved moderately in 2001.

Reducing the use of high cost agency staff is a key to lowering labour and training expenses. Moreover, the use of our own staff represents continuity in resident relationships that enhances efficiency and quality of care.

## United States Operations

New senior operating personnel – all of them originally trained as nurses – led three of EHSI's five operating regions in 2001. The skills and experience that these individuals bring to our leadership mix have excellent benefits in terms of our ability to attract staff and reinforce a caring perspective across our operations.

We have good reason to be proud of our quality of care. Our skilled nursing facilities are surveyed annually for compliance with federal and state regulations, and for the fourth consecutive year we achieved improved results.

We intend to increase the level of diversification within our long-term care business in the United States by expanding our information technology services company, Virtual Care Provider, Inc. (VCP); our rehabilitative therapy organization, Progressive Step Rehabilitation Services (ProStep); our group purchasing business, UHF Purchasing Group (UPG); and our management and consulting services companies, Partners Health Group and Fiscal Services Group.

On January 1, 2001, all employees of EHSI's information technology group were transferred to the newly created VCP. The company targets small to medium sized health care organizations, hosting their application software, in addition to meeting EHSI's information technology needs. VCP won contracts to service approximately 300 facilities during its first year of operation and anticipates adding substantial new business in 2002.

We offer outpatient therapy services in five states through 22 freestanding clinics operated by ProStep, a division of EHSI. These clinics serve individuals requiring physical, occupational and speech-language therapy.

Rehabilitative therapy is also available in our nursing homes on an inpatient and outpatient basis. ProStep provides management oversight of the delivery of rehabilitation services within EHSI facilities and we believe there are opportunities to increase efficiencies that would lead to higher revenues.

UPG provides purchasing services for over 2,500 skilled nursing facilities in 32 states, including those owned and managed by EHSI. In addition, UPG administers separate food purchasing programs for two major long-term care groups with more than 700 long-term care facilities. The purchasing group offers substantial cost reductions to its members through contractual volume-based arrangements with supply vendors.

We established Partners Health Group and Fiscal Services Group to market our growing management and consulting business in the United States. At the start of 2001, our customers accounted for more than 3,300 beds in 33 facilities. During the year we added 400 beds under management contracts and nearly 2,500 beds under consulting service arrangements. Consulting and management services generate high margins through the sale of excess capacity.

In all, our U.S. assets constitute a business portfolio that serves as a strong base for future growth.

## Canadian Operations

Extendicare (Canada) Inc. (ECI) achieved strong operating results in 2001 and expanded its presence in Ontario with the opening of five new facilities.

Nursing homes were constructed and commissioned in Lakefield, Lindsay, Windsor, Brampton and Cobourg, with capacity for 533 long-term care beds and 76 assisted living units. Moreover, we'll open a new 160-bed Ontario home in Hamilton in 2002, and five more in 2003 – in Mississauga, Port Hope, Tecumseh, Toronto and Halton Hills – with capacity for 718 long-term care beds.

One of the keys to the success of our development program is the cost-effective use of prototypical processes and designs – an approach that distinguishes us from many of our competitors and enables us to expedite our projects.

Architects prepared two basic designs – one for our small, rural facilities and the other for large, urban homes – enabling us to tailor our plans readily for specific locations while obtaining bulk purchasing and other advantages. Quality interior finishings and homelike comforts were emphasized.

Nursing home occupancy stood at 98% in 2001, unchanged from the previous year-end. We have targeted three nursing homes for major renovation in 2002 to ensure that we maintain our market leadership in more competitive jurisdictions.

All ECI facilities were in full compliance with regulatory requirements. We continue to strive to exceed externally mandated standards. All of our facilities have attained voluntary national third party certificates of accreditation from a non-profit council of senior, independent health care professionals.

Our home health care business, ParaMed, enhanced its market leadership in quality service and pricing. In the 2001 second half, all home health care providers in Ontario experienced volume declines resulting from budgetary restraints at the local agencies that contract their services. However, ParaMed – the country's largest private home health care company – increased its margins and profitability year-over-year while providing 6.9 million hours of service.

While funding issues remain to be resolved, ECI is expanding existing product lines and developing new ones to reflect growing demand for home care. In 2001, ParaMed began offering both nursing services in support of clinical drug trials and nursing-based assessment services for the automobile insurance industry.

We are focusing on a wide range of health care partnership opportunities, involving public, private and not-for-profit organizations, as well as management, consulting and group purchasing contracts. At West Park Hospital in Toronto, we were involved in developing a new 200-bed long-term care centre completed early in 2002, which we now manage.

In 2003, we will complete the development of and begin managing a 128-bed facility in Oakville for the Halton Health Sciences Centre, as well as a 160-bed facility for the District of Muskoka. In addition, we are developing and managing a new 128-bed facility for the Toronto Rehabilitation Institute, scheduled to open in 2004.

We continue to strengthen our management team and enjoy a strong and stable workforce in Canada, with low turnover levels.

## Our Care Focus



Residents and their families participate in developing care plans.



Spacious internal courtyards enable safe and pleasant outdoor recreation.

## EXTENDICARE

### Long-term Care Facilities

Extendicare, through its subsidiaries, is one of the largest operators of long-term care facilities in North America. Extendicare (Canada) Inc. (ECI) and Extendicare Health Services, Inc. (EHSI) operated 217 nursing facilities in the United States and Canada, with capacity for over 24,000 residents, at year-end 2001.

The Company's nursing facilities are designed for people who cannot be cared for at home or in assisted living facilities, due to frailty or other physical limitations. Residents require support and assistance with activities of daily living and continuing care. In addition, programs and services are provided to those with behavioural needs.

The U.S. nursing facilities also provide skilled nursing and rehabilitative therapy to support patients recovering from acute illness or injury. Specialized resources are aimed at optimizing treatment outcomes and efficiently using health care benefits.

### Assisted Living and Retirement Facilities

Assisted living offers an environment in which people receive support for activities of daily living, such as personal care, reminders to take medications, and housekeeping. Staff is available 24 hours a day to enable seniors to maintain active and independent lifestyles.

Retirement communities provide residents with comfortable suites, housekeeping services, meals, activities, security, transportation and special amenities. Residents are typically very active and live independently.

At year-end 2001, Extendicare, through its subsidiaries, operated 1,912 units in U.S. assisted living communities and 175 units in Canadian retirement communities, as well as a newly opened 38-unit assisted living wing.

### Management and Consulting Services

In Canada and the United States, Extendicare applies its expertise in long-term care by providing management and consulting services to other organizations, including government, not-for-profit and private-sector operators seeking to improve their levels of care and enhance operating efficiencies. Extendicare offers full management or selected consulting services in a variety of areas, including nursing, dietary, cost reimbursement, information technology, asset management, regulatory compliance and accounting services. In addition, operators can access Extendicare's expertise in all phases of planning, development and management of new facilities.



Residents can host private gatherings in warm and relaxing settings.



New facility design emphasizes quality finishings and personal comfort.

### Group Purchasing Services

With their large scale North American operations, ECI and EHSI can offer measurable cost savings to their own facilities and those of other providers through group purchasing of a wide range of operational supplies, furnishings, and capital equipment. Services are available through UHF Purchasing Group in the United States and LTC Group Purchasing in Canada. LTC Group Purchasing members can also obtain support in organizing nutritional care and dining services, through menu planning, costing and nutritional analysis programs.



### Home Care

ParaMed Home Health Care has served Canadians since 1974. As the country's largest private-sector home care provider, ParaMed offers a range of services. Staff members are skilled in providing all levels of nursing care, home support, occupational and speech-language therapy and physiotherapy. With approximately seven million hours of service provided in 2001, ParaMed's excellent reputation has earned it contracts with government home care programs, social service agencies and insurance companies.



### Rehabilitative Therapy Clinics

Progressive Step Rehabilitation Services (ProStep) operates 22 rehabilitative therapy clinics in the United States, including 10 in Wisconsin, nine in Pennsylvania, and one each in Ohio, Texas and Illinois. Patient populations range from pediatrics to geriatrics. ProStep services outpatients requiring physical, occupational and speech-language therapy, pulmonary rehabilitation and nursing services in Medicare certified outpatient settings.



### Application Service Provider

Virtual Care Provider (VCP) provides application and hardware support to EHSI's own facilities, in addition to acting as an application service provider to other operators in the long-term care and health care industries. VCP deploys, hosts and manages access to packaged software applications from a centrally managed facility on a subscription basis. With contracts to service approximately 300 facilities in 2001, its first year of operation, VCP aims to be regarded by its target market as the specialist information technology organization of choice, offering the means of reducing customers' in-house technology resource requirements in an increasingly complex health care environment.



# Facility Location and Resident Capacity

	Nursing Centres		Assisted Living and Retirement Centres		Hospitals/Units		Total	
	Number of Facilities	Resident Capacity	Number of Facilities	Resident Capacity	Number of Facilities	Resident Capacity	Number of Facilities	Resident Capacity
<i>at December 31, 2001</i>								
<b>By State/Province</b>								
<b>United States</b>								
Pennsylvania	27	3,145	8	298	–	–	35	3,443
Massachusetts	5	606	–	–	–	–	5	606
Delaware	1	120	–	–	–	–	1	120
-----								
Ohio	30	3,194	3	165	–	–	33	3,359
West Virginia	1	120	–	–	–	–	1	120
-----								
Wisconsin	24	2,203	10	443	–	–	34	2,646
Minnesota	10	1,250	1	60	–	–	11	1,310
-----								
Indiana	17	1,827	3	133	–	–	20	1,960
Kentucky	18	1,511	1	39	–	–	19	1,550
-----								
Washington	15	1,479	8	381	–	–	23	1,860
Oregon	3	194	2	102	–	–	5	296
Idaho	2	178	–	–	–	–	2	178
-----								
Louisiana	3	567	–	–	–	–	3	567
Arkansas	1	96	3	181	–	–	4	277
Texas	–	–	2	110	–	–	2	110
-----								
<b>Total United States</b>	<b>157</b>	<b>16,490</b>	<b>41</b>	<b>1,912</b>	<b>–</b>	<b>–</b>	<b>198</b>	<b>18,402</b>
-----								
<b>Canada</b>								
Ontario	37	5,188	2	213	1	120	40	5,521
Alberta	15	1,229	–	–	–	–	15	1,229
Saskatchewan	5	654	–	–	–	–	5	654
Manitoba	2	458	–	–	–	–	2	458
British Columbia	1	75	–	–	–	–	1	75
-----								
<b>Total Canada</b>	<b>60</b>	<b>7,604</b>	<b>2</b>	<b>213</b>	<b>1</b>	<b>120</b>	<b>63</b>	<b>7,937</b>
-----								
<b>TOTAL</b>	<b>217</b>	<b>24,094</b>	<b>43</b>	<b>2,125</b>	<b>1</b>	<b>120</b>	<b>261</b>	<b>26,339</b>
-----								
<b>By Type of Ownership</b>								
<b>United States</b>								
Owned	122	12,282	35	1,691	–	–	157	13,973
Leased	17	1,882	1	65	–	–	18	1,947
Managed	18	2,326	5	156	–	–	23	2,482
-----								
<b>Total United States</b>	<b>157</b>	<b>16,490</b>	<b>41</b>	<b>1,912</b>	<b>–</b>	<b>–</b>	<b>198</b>	<b>18,402</b>
-----								
<b>Canada</b>								
Owned	50	6,716	1	111	–	–	51	6,827
Leased	2	129	–	–	–	–	2	129
Managed	8	759	1	102	1	120	10	981
-----								
<b>Total Canada</b>	<b>60</b>	<b>7,604</b>	<b>2</b>	<b>213</b>	<b>1</b>	<b>120</b>	<b>63</b>	<b>7,937</b>
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<b>TOTAL</b>	<b>217</b>	<b>24,094</b>	<b>43</b>	<b>2,125</b>	<b>1</b>	<b>120</b>	<b>261</b>	<b>26,339</b>
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## Forward-looking Information

Information provided by the Company from time to time, including this annual report, contains or may contain forward-looking statements concerning the Company's operations, economic performance and financial condition, including the Company's business strategy. Forward-looking statements can be identified because they generally contain the words "anticipate", "believe", "estimate", "expect", "objective", "project", or a similar expression.

Forward-looking statements reflect management's beliefs and assumptions and are based on information currently available to the Company. They are not guarantees of future performance and involve known and unknown risks, uncertainties and other factors that may cause actual results, performance or achievements of the Company to differ materially from those expressed or implied in the statements. In addition to the assumptions and other factors referred to specifically in connection with these statements, such factors are identified in the Company's public filings with Canadian and United States securities regulators and include, but are not limited to, the following: changes in the health care industry in general and the long-term care industry in particular because of political and economic influences; changes in regulations governing the industry and the Company's compliance with such regulations; changes in government funding levels for health care services; liabilities and other claims asserted against the Company; the Company's ability to attract and retain qualified personnel; the availability and terms of capital to fund the Company's capital expenditures; changes in competition; and demographic changes.

Given these risks and uncertainties, readers are cautioned not to place undue reliance on the Company's forward-looking statements.

## Management's Discussion and Analysis

The consolidated financial results include those of Extencare Inc. and its subsidiaries. Unless the context indicates otherwise, a reference to "Extencare" or the "Company" means Extencare Inc. and its subsidiaries. The Extencare Inc. legal entity is not itself a provider of services or products.

In the United States, the Company's wholly owned subsidiary, Extencare Health Services, Inc. and its subsidiaries (EHSI), operate long-term care facilities and assisted living facilities in 15 states. EHSI provides inpatient routine nursing care and medical specialty services on an inpatient and outpatient basis.

In Canada, the Company's wholly owned subsidiary, Extencare (Canada) Inc. and its subsidiaries (ECI), operate nursing and retirement centres in five provinces, and also manage an acute care hospital unit in Ontario. ECI is a major provider of home health care in three provinces through its ParaMed Home Health Care division.

At December 31, 2001, Extencare, through its subsidiaries, operated 261 facilities with capacity for 26,339 residents (December 31, 2000: 274 facilities, with capacity for 27,052 residents). Page 13 details the facilities and resident capacity by area. The Company has a significant presence (more than 10% of total facilities) in three states – Pennsylvania, Wisconsin and Ohio – as well as in the Province of Ontario, Canada. Nursing and assisted living facilities are located in groups within geographic proximity of each other, thereby allowing for regional development

of ancillary businesses, cost-effective management control and reduced travel costs. The Company's average occupancy levels for 2001, 2000, and 1999 were 90.0%, 89.9%, and 88.2%, respectively.

### Significant Events in 2001 and 2000 Construction

As a result of new beds awarded in 1998 by the Government of Ontario, ECI undertook to develop eight new facilities with capacity for 1,101 residents, of which 905 represent new long-term care beds awarded, 120 represent beds to be transferred from existing ECI facilities, and 76 represent assisted living units. Five of these new facilities (capacity for 609 residents) have been completed, four of which opened during 2001, and the fifth at the end of January 2002. Two of these newly opened facilities include 38-unit assisted living wings. The remaining three projects are due to open in 2002 and 2003. These eight projects are estimated to cost \$125.4 million, of which \$83.9 million had been capitalized at the end of 2001. In an agreement finalized in February 2001, ECI obtained from Borealis Long-Term Care Facilities Inc., a wholly owned subsidiary of the Ontario Municipal Employees Retirement System, financing of \$125.4 million to build the new facilities. ECI will operate the facilities for Borealis during the 25-year capital lease arrangement at a financing cost of approximately 8.0%.

## Management's Discussion and Analysis

The Ontario Government will fund a portion of the construction costs over a 20-year period. Approximately \$74.4 million will be received by ECI related to the 905 new long-term care beds and certain redeveloped existing ECI beds. As each facility opens, a receivable will be recorded and offset against the cost of construction, based on applying a discount rate equivalent to the yield on a 20-year Ontario Government bond. As at December 31, 2001, the balance of such notes related to the four facilities opened in 2001 was \$18.1 million with discount rates in the range of 6.2% to 6.5%.

During 2001, ECI was awarded 256 additional long-term beds, and is in the process of finalizing plans for the development and financing of two facilities for completion after 2002. In addition, ECI intends to develop a new 130-bed facility, pending approval for the transfer of 96 new long-term care beds awarded to the Halton Health Services Centre. The other 34 beds would be transferred from existing ECI facilities.

### Other

On February 22, 2001, the Board of Directors of Crown Life Insurance Company declared a cash dividend of \$20.30 per common share, payable March 15, 2001, resulting in a cash payment to Extencicare of \$22.6 million on its 34.8% common equity investment. In December 2001, Crown Life redeemed all of its 3,652,599 outstanding preferred shares for \$25.00 per share. During 2000, Crown Life completed the acquisition for cancellation of its common shares not held by its two principal shareholders, being Extencicare and HARO Financial Company. This transaction resulted in the increase in Extencicare's common equity interest in Crown Life to 34.8% from 32.3%.

During 2001, under the terms of normal course issuer bids, the Company purchased and cancelled 1,744,900 Subordinate Voting Shares and 224,600 Multiple Voting Shares at a cost of \$9.8 million. During 2000, the Company purchased and cancelled 1,284,100 Subordinate Voting Shares at a cost of \$2.8 million.

The current bid, filed in November 2001, is for the purchase and cancellation of up to 4,000,000 Subordinate Voting Shares, 640,000 Multiple Voting

Shares and 38,200 Class II Preferred Shares, Series 1. As at February 21, 2002, cumulative purchases for cancellation of 40,900 Subordinate Voting Shares and 30,700 Multiple Voting Shares have been made under the current bid, which expires November 26, 2002.

### Loss from Dispositions

A number of significant factors affected the Company during the past few years. These included changes in legislation, changes in the insurance marketplace and the implementation of the new Medicare Prospective Payment System. In response, management identified assets that were either underperforming or not strategic to its operations. This resulted in a number of dispositions and the sale or lease of all of EHSI's nursing home operations in the states of Florida and Texas. The ceasing of nursing home operations in Florida and Texas will limit the Company's future exposure to litigation claims, which have been prevalent in these states. Proceeds from the sale of assets have been used primarily to reduce long-term debt, thereby improving the Company's leverage and lowering interest costs.

### 2001 Dispositions

EHSI effectively ceased nursing operations in Texas by leasing and subleasing 17 nursing homes (1,421 beds) to Senior Health Properties – Texas, Inc. On October 1, 2001 Senior Health started operating the 17 nursing homes through five-year leases on four facilities owned by EHSI, as well as 13 subleases. Senior Health will operate the subleased facilities for their remaining lease terms, one of which expired on October 31, 2001, and the other 12 leases expire in February 2012. The owner of the property whose lease expired on October 31, 2001 subsequently assumed operation of the facility. Senior Health has the right of first refusal to purchase the four EHSI owned facilities.

In April 2001, Tandem Health Care, Inc. exercised its option to purchase from EHSI two leased Florida facilities for gross proceeds of \$17.5 million (US\$11.4 million consisting of: cash of US\$7.0 million; US\$2.5 million of 8.5% five-year notes; and US\$1.9 million of 9% cumulative dividend preferred shares, retractable in five years). The carrying value of the two facilities disposed of was \$14.1 million (US\$9.2 million). As the

## Management's Discussion and Analysis

buyer has purchase options on further leased facilities, the gain on sale has been deferred until the balance of the transactions are completed or the options expire. The net cash proceeds of the transaction were \$10.6 million (US\$6.9 million), of which \$6.2 million (US\$4.0 million) was applied to EHSI term bank debt.

In December 2001, ECI sold its investment in Accident Injury Management Clinics Inc. (AIM), a rehabilitative therapy business operating in Ontario, resulting in a gain of \$1.1 million. Proceeds of \$3.5 million from the sale consisted of cash of \$2.2 million and notes receivable of \$1.3 million.

### 2000 Dispositions

In 2000, EHSI was successful in selling or leasing its remaining 32 facilities (3,427 beds) in the State of Florida through a series of transactions. EHSI sold two Florida nursing homes in separate transactions in July and December. In September, EHSI entered into an agreement involving 15 Florida properties in which EHSI retains an interest, which is described in note 4 to the financial statements. This particular transaction, while not accounted for as a sale, resulted in initial net cash proceeds of \$43.8 million. In December, the remaining 15 Florida facilities were leased through two separate transactions with operators that have options to purchase. In addition, EHSI sold in May and June, two formerly closed facilities. The transactions, accounted for as sales, generated net proceeds of

\$13.5 million on \$18.4 million of net assets sold, resulting in a loss of \$4.9 million. EHSI applied the net after-tax proceeds of \$49.2 million (US\$33.1 million) from the above transactions to reduce EHSI's term bank debt.

### Other Items

The Company is required to record a provision for asset impairment when indicators of impairment are present and the undiscounted cash flows do not appear to be sufficient to recover the assets' carrying amounts. Accordingly, the Company recorded in 2001 and 2000 provisions of \$2.6 million and \$31.6 million, respectively, related to the impairment of assets.

The Company also recorded charges of \$20.3 million during 2001 and \$3.6 million in 2000 for the closure of facilities and provisions for previously ceased operations in the United States.

In addition, the Company recorded a \$27.0 million provision for adverse development of prior years' general and professional liability costs (resident care liability costs) related to ceased Florida operations.

### United States Revenue Payor Mix

The majority of the Company's operations are in the United States, where 73% of revenue was earned in 2001 (76% in 2000). In the United States, EHSI receives payment for its services and products from various federal (Medicare) and state (Medicaid) medical

### Components of Loss (Gain) from Dispositions and Other Items

(\$ millions)	2001		2000	
	Net Proceeds	Net Book Value	(Gain) Loss	Loss
Loss (gain) from dispositions				
United States nursing facilities	17.3	17.3	—	4.9
Canada rehabilitative therapy services	3.4	2.3	(1.1)	—
	<u>20.7</u>	<u>19.6</u>	<u>(1.1)</u>	<u>4.9</u>
Provision for impairment of assets			2.6	31.6
Provision for adverse development of general and professional liability costs			27.0	—
Provision for closure and disposal of United States facilities			20.3	3.6
Other			1.3	2.6
			<u>50.1</u>	<u>42.7</u>

## Management's Discussion and Analysis

assistance programs, as well as from private payors. The private-pay classification includes payments from individuals, commercial insurers, health maintenance organizations, preferred provider organizations and other charge-based payment sources, including Blue Cross associations and the Veteran's Administration.

Funds received by EHSI's nursing home operations under the Medicare and Medicaid programs are subject to audit with respect to the proper application of various payment formulas. Such audits can result in retroactive adjustments to revenue. In addition, ongoing efforts by third-party payors to contain health care costs by limiting reimbursement rates, increasing case management reviews and negotiating reduced contract pricing could affect EHSI's future revenue and profitability.

The following table sets forth EHSI's percentage of total revenue from private pay, Medicare and Medicaid sources:

<i>(percent)</i>	2001	2000	1999
Private pay	25	25	28
Medicare	24	24	22
Medicaid	51	51	50

The Balanced Budget Act of 1997 (the "Balanced Budget Act"), signed into law on August 5, 1997, made numerous changes to the Medicare and Medicaid programs, which affected long-term care providers. With respect to the Medicare program, the law established a Prospective Payment System (PPS) for skilled nursing facility services. Under PPS, long-term care providers are reimbursed for Medicare Part A services based on federally established per diem rates for 44 categories of care. The categories of care are associated with patients' medical complexities and needs. Patients are categorized using the Resource Utilization Groupings III (RUGs) system. The payment category dictates the amount that the provider will receive to care for the patient on a daily basis. The legislation became effective for cost report periods commencing July 1, 1998. For EHSI, this new system became effective for three facilities during 1998. The remainder of EHSI's facilities became PPS-funded as of January 1, 1999.

The PPS rate was essentially phased-in over a three-year period using a blended rate comprised of a federal and facility-specific rate. The facility-specific

rate took into account a facility's 1995 costs. The federal component was based on a national federal rate, and during the phase-in period, represented 25% of the total PPS rate in the first year, 50% in the second, and 75% in the third, before becoming a full 100% federal rate in the final year and thereafter. Facilities that began operating subsequent to 1995 were subject to 100% of the federal rate starting in year one.

In addition, the Balanced Budget Act repealed the federal payment standard known as the Boren Amendment, which required state Medicaid programs to pay rates that were reasonable and adequate to meet costs incurred by efficiently and economically operated nursing facilities. As a result, states now have considerable flexibility in establishing payment rates for Medicaid services provided.

In November 1999, Congress and the President reached agreement on a package of Medicare program revisions for approximately US\$2.7 billion in Medicare funding for skilled nursing providers over the next three fiscal years, thereby restoring some of the funding that had been eliminated or excluded by the Balanced Budget Act. The Balanced Budget Refinement Act 1999 (BBRA) made numerous revisions to Medicare Part A and Part B, which included, among other things:

- (i) the option for nursing facilities operating under a phased-in PPS rate of moving to the full federal rate, effective January 1, 2000;
- (ii) a temporary 20% increase in the revenue value for the federal component for 15 RUGs categories identified as having high intensity, non-therapy ancillary services, from April 1, 2000 through September 30, 2000, pending a refinement of the overall RUGs categories; however, the refinement was not subsequently provided, and the 20% increase was extended;
- (iii) a 4% increase in the federal component for all of the RUGs for each of the periods October 1, 2000 through September 30, 2001, and October 1, 2001 through September 30, 2002; and
- (iv) a two-year moratorium effective January 1, 2000 on the US\$1,500 cap on speech and physical therapy and the US\$1,500 cap on occupational therapy, which had a favourable impact on the Company's Part B Medicare revenue.

## Management's Discussion and Analysis

In December 2000, Congress and the President approved an additional US\$35.0 billion Medicare and Medicaid provider relief package through the Benefits Improvement and Protection Act of 2000 (BIPA). Approximately US\$2.0 billion of this was expected to benefit nursing home providers. The BIPA revisions included, among other things:

- (i) a 16.66% increase in the nursing component of the RUGs rate for the period April 1, 2001 through September 30, 2002, and a requirement that the Comptroller General complete a study of nursing staff ratios by August 1, 2002;
- (ii) a redistribution of the 20% Part A enhancement implemented for three RUGs categories across all 14 rehabilitation RUGs categories, effective April 1, 2001, increasing them by 6.7%, and an extension of the 20% add-on for all other RUGs categories, pending a refinement of the overall RUGs categories;
- (iii) a modification to the skilled nursing facility PPS inflation adjustment to remove the negative 1% factor for the 2001 year and establish a minus 0.5% factor for years 2002 and 2003;
- (iv) the continuation through 2002 of the moratorium on therapy caps; and
- (v) the elimination of Medicare Part B consolidated billing, except for therapy services.

Following the enactment of the BBRA and BIPA, EHSI identified additional facilities that would benefit from the full federal rate. During 2000, EHSI had 35 facilities operating under the full federal rate, and during 2001, EHSI had 38 facilities at the full federal rate. Starting January 1, 2002, all nursing facilities are on the full federal rate.

The incremental Medicare relief packages received from BBRA and BIPA provide a total of US\$2.7 billion in temporary Medicare funding enhancements to the long-term care industry. These funding enhancements fall into two categories being: (i) "Legislative Add-ons", which included the 16.66% nursing add-on to the nursing component of the RUGs rate and the 4% base adjustment; and (ii) "CMS RUGs Refinements", which involved the initial 20% add-on for 15 RUGs categories, and subsequent redistribution of the 20% add-on

from three RUGs categories to 14 Rehab categories at 6.7%. The Legislative Add-ons are scheduled to sunset on September 30, 2002. Currently, no legislation has been introduced by Congress, nor have recommendations been made by the Centers for Medicare and Medicaid Services (CMS), to continue this funding. The CMS RUGs Refinements continue until such time as CMS refines the RUGs categories. The Company estimates that the average per diem effect of the Legislative Add-ons and CMS RUGs Refinements is US\$31.00 and US\$25.00, respectively; representing incremental annual Medicare funding to EHSI of approximately US\$16.0 million and US\$13.0 million, respectively. A decision to discontinue all or part of the enhancements could have a significant impact on the Company.

### Results of Operations

The table on the following page presents the Company's quarterly financial results as reported, in addition to supplemental information to assist the reader in better understanding the quarterly trend in results and the discussion of year-over-year comparisons that follows. The Company has presented both EBITDAR and health care results before certain items. The Company reports on the face of its consolidated income statement a loss from asset impairment, disposals and other items of \$50.1 million during 2001 and \$42.7 million during 2000. On an after-tax basis, these items represented a loss of \$35.5 million (\$0.49 loss per share) and \$27.4 million (\$0.36 loss per share), respectively. In addition, during both 2001 and 2000, significant items of a non-recurring nature were reported in revenue and operating expense, which affected the quarterly trend in results. During 2001, such items related to a provision in the third quarter for prior years' resident care liability costs of \$11.5 million, or \$7.9 million on an after-tax basis (\$0.11 loss per share). During 2000, such items related to a \$17.8 million recovery of a Medicare settlement, reported as revenue in the fourth quarter, and a \$13.2 million provision for potential punitive damages in the third quarter. The net \$4.6 million impact on earnings was an improvement of \$3.0 million after-tax, or \$0.04 per share.

## Management's Discussion and Analysis

### Quarterly Financial and Supplemental Information

(unaudited) (thousands of dollars except per share amounts)

	1st	2nd	3rd	4th	Total
<b>Year ended December 31, 2001<sup>(1)</sup></b>					
Revenue	408,730	431,129	432,730	431,922	1,704,511
EBITDAR <sup>(2)</sup> before undernoted	32,432	42,779	41,882	49,764	166,857
Provision for resident care liability costs related to prior years included in operating expense	–	–	(11,498)	–	(11,498)
EBITDAR	32,432	42,779	30,384	49,764	155,359
Earnings (loss) from health care before undernoted	(6,216)	(184)	(732)	3,365	(3,767)
Provision for resident care liability costs related to prior years recorded in EBITDAR, net of tax	–	–	(7,911)	–	(7,911)
Loss from asset disposal and other items, net of tax	(1,399)	(6,493)	(27,574)	–	(35,466)
Earnings (loss) from health care	(7,615)	(6,677)	(36,217)	3,365	(47,144)
Share of earnings of Crown Life	2,277	2,561	2,405	3,495	10,738
Earnings (loss)	(5,338)	(4,116)	(33,812)	6,860	(36,406)
Earnings (loss) per share					
Health care operations before undernoted	(0.09)	(0.01)	(0.01)	0.04	(0.07)
Provision for resident care liability costs related to prior years recorded in EBITDAR	–	–	(0.11)	–	(0.11)
Loss from asset disposal and other items	(0.02)	(0.09)	(0.38)	–	(0.49)
Share of earnings of Crown Life	0.03	0.04	0.03	0.05	0.15
Basic and diluted loss per share	(0.08)	(0.06)	(0.47)	0.09	(0.52)
<b>Year ended December 31, 2000<sup>(1)</sup></b>					
Revenue	437,899	450,698	450,361	468,448	1,807,406
EBITDAR before undernoted	24,742	33,929	30,294	26,488	115,453
Adjustment for special items:					
Medicare settlement recovery, included in revenue	–	–	–	17,794	17,794
Provision for potential punitive damages	–	–	(13,249)	–	(13,249)
EBITDAR	24,742	33,929	17,045	44,282	119,998
Loss from health care before undernoted	(14,036)	(7,429)	(8,377)	(12,859)	(42,701)
Special items as noted above, net of tax	–	–	(8,612)	11,566	2,954
Gain (loss) from asset disposal and other items, net of tax	–	(1,660)	245	(25,943)	(27,358)
Loss from health care	(14,036)	(9,089)	(16,744)	(27,236)	(67,105)
Share of earnings of Crown Life	2,132	2,240	2,243	1,212	7,827
Loss	(11,904)	(6,849)	(14,501)	(26,024)	(59,278)
Earnings (loss) per share					
Health care operations before undernoted	(0.19)	(0.11)	(0.11)	(0.18)	(0.59)
Special items as noted above	–	–	(0.12)	0.16	0.04
Loss from asset disposals and other items	–	(0.02)	–	(0.34)	(0.36)
Share of earnings of Crown Life	0.03	0.03	0.03	0.01	0.10
Basic and diluted loss per share	(0.16)	(0.10)	(0.20)	(0.35)	(0.81)

<sup>(1)</sup> Quarterly results have been restated for the reclassification of certain items between operating expense and lease costs.

<sup>(2)</sup> EBITDAR represents earnings before lease costs, depreciation, interest and income taxes.

## Management's Discussion and Analysis

### Fiscal Year 2001 Compared with 2000

Extendicare's loss in 2001 was \$36.4 million (\$0.52 loss per share) compared to \$59.3 million (\$0.81 loss per share) in the prior year. Health care operations reflected a significant improvement as a result of the ceasing of operations in Florida and Texas. Prior to the share of earnings of Crown Life, and the after-tax impact of special charges as noted above, health care operations realized a loss of \$3.8 million (\$0.07 loss per share) in 2001 compared to a loss of \$42.7 million (\$0.59 loss per share) in 2000.

### Revenue

Revenue for 2001 declined by \$102.9 million compared to 2000.

Revenue from U.S. nursing and assisted living operations declined \$158.5 million. Ceased operations reduced nursing and assisted living revenue by \$230.2 million, while revenue from same-facility operations (those operated throughout 2001 and 2000) improved by \$71.7 million. Improvements in same-facility revenue resulted from several factors. These included higher rates and improved Medicare census, partially offset by a \$17.8 million Medicare settlement recovery received in the fourth quarter of 2000 and one less day in 2001. In addition, the change in the U.S. foreign exchange rate on translation of United States operations added \$48.4 million to the year-over-year variance.

The average annual exchange rate used to translate the results of the United States operations to Canadian dollars was: 1.5484 for 2001; 1.4852 for 2000; and 1.4858 for 1999.

Medicare census improved to 11.4% of total nursing census in 2001, compared to 10.7% in 2000, notwithstanding a decline in overall nursing census on a same-facility basis. Excluding ceased operations, Medicare patient days in 2001 increased 6.2% to 520,900 from 490,700 in 2000. The average percentage occupancy, based on U.S. nursing and assisted living facilities in operation throughout 2001 and 2000, was 87.2% and 87.4%, respectively.

The Company's average daily Medicare and Medicaid rates on a same-facility basis increased to US\$334 and US\$121, respectively, compared to US\$316 and US\$115, respectively, in 2000. For the

U.S. operations, the Company's overall average daily Medicare Part A rate rose to US\$312 in 2001 compared to US\$304 in 2000.

Canadian nursing centre operations reported an increase in revenue of \$12.9 million. This improvement was primarily due to funding changes to support greater care and staffing needs (pass-through funding), as well as rate increases. Also, the Company realized additional revenue of \$3.5 million in Ontario related to the opening of four new facilities during the year.

Home health revenue in Canada combined the operations of ParaMed's home health care services and AIM's rehabilitative therapy services. In December 2001, the Company disposed of its investment in AIM, which contributed \$5.1 million of revenue in 2001 compared to \$3.0 million in 2000. Revenue from home health care operations increased by \$8.4 million as a result of higher rates and mix of services provided. ParaMed's hours of service declined year-over-year by 1.4% to 6.9 million in 2001. ParaMed's operations saw a decline in service hours in the latter half of 2001, with 3.2 million hours provided versus 3.7 million hours in the first half of the year. This decline was due to budget constraints among the Ontario agencies that contract for such services. In 2002, management anticipates home care hours will stabilize and return to their previous levels when budget constraints subside and other growth opportunities are explored.

Other revenue of \$50.9 million increased \$31.9 million. Revenue from the Company's wholly owned captive insurance companies rose by \$10.4 million. Revenue from new contracts for operating leases, management services and consulting services accounted for \$17.1 million of the year-over-year increase. Virtual Care Provider, the Company's new information technology business, earned \$3.5 million in revenue on external contracts. The remaining improvement related to group purchasing services and other minor miscellaneous items.

### Operating and Administrative Costs

Operating and administrative costs declined \$138.3 million, or 8.2%, as a result of ceased operations, partially offset by increased costs. The Company's resident care liability costs (both premiums and accruals for potential claims) charged to operating expense of

## Management's Discussion and Analysis

\$46.6 million declined year-over-year by \$61.4 million, primarily as a result of ceasing operations in Florida at the end of 2000, and Texas in the fourth quarter of 2001. There was a further \$198.8 million decline in operating and administrative costs as a result of ceased operations.

Operating and administrative costs from ongoing operations, excluding resident care liability costs, rose approximately \$121.9 million of which \$46.3 million was attributable to the change in the U.S. foreign exchange rate on translation of United States operations. Wage-related expenses increased year-over-year by approximately \$59.5 million, primarily due to wage pressures realized in both the U.S. and Canadian markets, pass-through funding increases, and an additional \$2.3 million in wage related costs due to the opening of new facilities in Ontario during 2001. Remaining operating and administrative costs rose \$16.1 million, due to a combination of business activities and inflationary increases.

### Earnings before Lease Costs, Depreciation, Interest and Income Taxes (EBITDAR)

The Company reported EBITDAR of \$155.4 million (9.1% of revenue) for 2001 compared to \$120.0 million (6.6% of revenue) in 2000, an improvement of \$35.4 million or 29.5%.

EBITDAR from U.S. operations improved by \$29.5 million, and represented 9.2% of revenue in 2001, compared to 6.2% in 2000. Ceased operations, in conjunction with lower resident care liability costs, partially offset by the non-recurring Medicare settlement recovery, resulted in a year-over-year improvement in EBITDAR of \$13.4 million. EBITDAR from ongoing operations rose by \$16.1 million due to improved revenue rates, census mix, and growth in management and consulting contracts, partially offset by increased operating costs.

EBITDAR from Canadian operations rose by \$5.9 million, and represented 8.8% of revenue compared to 8.0% in the prior year. The Company experienced improvements in both nursing centre and home health operations.

### Lease Costs, Depreciation and Amortization

Lease costs, depreciation and amortization charges of \$99.7 million decreased \$2.8 million over 2000, primarily as a result of ceased operations.

### Interest

Interest costs declined \$13.2 million in 2001 to \$65.2 million, as a result of lower debt levels and interest rates, partially offset by additional interest costs in Canadian operations due to financing of the new Ontario facilities.

### Income Taxes

Income taxes for 2001 represented a recovery of \$12.7 million compared with a recovery of \$36.9 million in 2000. The effective benefit of the pre-tax loss was less in 2001 than in 2000 due to a shift in income between taxable and non-taxable entities, and as a result of not tax benefiting operating losses in the Company's captive insurance company. The Company reported a shift between current and future income taxes in the fourth quarter of 2001 due to a Canadian tax reassessment related to deferred revenue. As a result, previously benefited operating losses have been utilized and future income tax on the deferred revenue timing difference has been recorded.

### Share of Earnings of Crown Life

The Company's share of Crown Life earnings for 2001 was \$10.7 million compared to \$7.8 million in 2000. The improvement reflected the profitability of Crown Life's remaining insurance operations and related investment activities.

### Fiscal Year 2000 Compared with 1999

The Company incurred a loss for the year of \$59.3 million (\$0.81 loss per share) compared to \$159.7 million (\$2.14 loss per share) in 1999. Results for both 2000 and 1999 included charges for certain non-recurring items. Those for 2000, as outlined in the Quarterly and Supplemental Financial Information on page 19, represented a pre-tax loss of \$38.2 million. For 1999, in addition to the \$183.9 million pre-tax loss from asset impairment, disposals and other items, the Company recorded a \$39.5 million provision for Medicare

## Management's Discussion and Analysis

settlements. On an after-tax basis these special items resulted in a loss of \$24.4 million in 2000 and \$150.7 million in 1999. Prior to the share of earnings of Crown Life, and the after-tax impact of the noted special charges, health care operations realized a loss of \$42.7 million (\$0.59 loss per share) in 2000 compared to a loss of \$31.8 million (\$0.44 loss per share in 1999). The decline in health care results during 2000 reflected the significant increase in resident care liability costs due to adverse claims experience, particularly in the State of Florida.

### Revenue

Revenue for 2000 declined by \$85.3 million compared to 1999.

Revenue from U.S. nursing and assisted living facilities declined \$18.0 million. Dispositions, net of new facilities, contributed \$126.7 million to the year-over-year decline. Revenues from facilities operated throughout both 2000 and 1999 (same-facility) rose by \$108.7 million due to: (i) a \$39.5 million non-recurring provision recorded in 1999 related to disputed Medicare settlements; (ii) a favourable \$17.8 million revenue item in 2000 related to the recovery of a portion of the 1999 Medicare settlement provision; (iii) \$5.3 million related to a favourable ruling for the billing of blood glucose claims from the period October 1, 1997 through December 31, 2000 and (iv) an improvement of \$46.1 million (4.6% increase) in remaining same-facility operations due to improved census and increased Medicaid rates, partially offset by lower Medicare rates.

The Company's overall average daily Medicaid rate increased to US\$112 in 2000 compared to US\$106 in 1999, and the percent of Medicaid-related revenue to total revenues improved slightly to 51% in 2000 from 50% in 1999. In 2000, the overall average daily rate for Medicare Part A services was approximately US\$304 compared to US\$323 in 1999. The percentage of Medicare patients in nursing operations increased to 10.9% in 2000 from 10.7% in 1999. The percent of Medicare-related revenue to total revenues increased to 24% in 2000 from 22% in 1999.

The average percentage occupancy, based on U.S. nursing and assisted living facilities in operation throughout 2000 and 1999, was 87.2% and 85.7%, respectively.

Canadian nursing centre operations realized a revenue increase of \$5.9 million. During 1999, the Company received a payment of \$8.1 million from the Ontario government in respect of retroactive pay equity funding for the years 1994 to 1998. Therefore, excluding this item, revenue in 2000 increased \$14.0 million over the prior year. This improvement was primarily due to funding changes to support greater care and staffing needs, as well as rate increases. In particular, effective April 1, 2000, the Ontario government increased the funding for preferred accommodation, improving revenue by \$2.2 million. Funding improvements were also realized in Saskatchewan and Manitoba, including one-time retroactive payments of \$1.5 million. Also, the Company realized higher revenue of \$2.7 million in Ontario, reflecting a full year of operations of interim nursing beds.

Medical supplies and outpatient therapy revenue in the United States decreased \$49.6 million due to the disposal of operations.

Home health revenue in Canada combined the operations of ParaMed's home health care services and AIM's rehabilitative therapy services. Revenue from these services in 2000 increased \$11.0 million or 7.3%. During 2000, the Company received payment from the Ontario government in respect of retroactive pay equity funding for prior years of \$3.6 million, compared to \$5.6 million received in 1999. Excluding this item, revenue rose \$13.0 million in 2000. This increase was due to both higher rates and volume of services provided. ParaMed increased its home care hours of service to 7.0 million compared with 6.6 million in 1999.

Other revenue of \$18.9 million increased \$1.3 million from 1999, and was primarily from group purchasing services and income from investments held for self-insured liabilities.

### Operating and Administrative Costs

Operating and administrative costs declined \$65.6 million, or 3.8%, as a result of asset disposals, partially offset by increased costs. The Company's resident care liability costs of \$108.0 million, including a \$13.2 million provision for punitive damages, increased year-over-year by \$60.9 million, as a result of higher retention levels and increased adverse claims

## Management's Discussion and Analysis

experience. Operating and administrative costs declined approximately \$176.0 million as a result of disposals, net of new facilities, prior to any allocation of resident care liability costs.

Operating and administrative costs from same-facility operations, excluding resident care liability costs, rose approximately \$49.5 million. Wage-related expenses increased year-over-year by approximately \$57.0 million, primarily due to wage pressures realized in both the U.S. and Canadian markets, pass-through funding increases, and in part due to increased home health business volumes. Remaining operating and administrative costs declined due to cost reductions in the U.S. operations, partially offset by higher costs in the Canadian nursing and home health care operations due to increased volumes of business.

### Earnings before Lease Costs, Depreciation, Interest and Income Taxes (EBITDAR)

EBITDAR of \$120.0 million represented a 14.2% decrease from 1999. These earnings as a percent of revenue were 6.6% compared with 7.4% in the prior year.

EBITDAR from United States operations declined by \$15.9 million to \$85.7 million from \$101.6 million in 1999, and represented 6.2% of revenue compared to 7.0% in 1999. The decline reflected asset disposals, partially offset by higher operating costs. The impact of the Medicare settlement provision and recovery, increased resident care liability costs, and provision for punitive damages, produced a \$3.6 million year-over-year reduction in EBITDAR. Disposals, net of new facilities, resulted in a \$32.4 million drop in EBITDAR, which was partially offset by a \$20.1 million improvement in same-facility operations. Same-facility operations improved due to higher Medicaid rates, occupancy, and census mix, partially offset by increased wage costs.

EBITDAR from Canadian operations rose to \$34.3 million from \$32.3 million in 1999 and represented 8.0% of revenue compared to 7.8% in the prior year. While revenue improved, the majority of this increase was offset by higher operating costs as most funding increases are accompanied by government-mandated

changes in resident care or staffing needs. The Company did, however, experience improvements in both nursing and home health care operations.

The Company disposed of its U.K. operations in 1999, which contributed \$6.0 million to EBITDAR in that year.

### Lease Costs, Depreciation and Amortization

Lease costs, depreciation and amortization charges of \$102.5 million decreased \$13.4 million over 1999, primarily as a result of disposed operations.

### Interest

Interest costs decreased \$13.4 million in 2000 to \$78.5 million, mainly as a result of lower debt levels, partially offset by an increase in floating rates. The Company has used cash proceeds from asset disposals to reduce debt levels over and above the regular repayments.

### Start-up Costs

The Company absorbed in income start-up costs associated with newly constructed facilities of approximately \$1.5 million in 2000 compared with \$6.2 million in 1999. There were no new facilities constructed during 2000.

### Income Taxes

Income taxes for 2000 represented a recovery of \$36.9 million compared with \$69.2 million in 1999. The effective benefit of the pre-tax loss was less in 2000 than in 1999, as a result of the recovery of prior year's taxes, resulting from the disposal of assets in a share transaction during 1999.

### Share of Earnings of Crown Life

The Company's share of Crown Life earnings for 2000 was \$7.8 million compared with \$22.8 million in 1999. In the fourth quarter of 1999, Crown Life finalized the gain on sale of its transaction with Canada Life, resulting in a \$47.9 million gain to shareholders, of which \$15.1 million was Extendicare's share. The remaining increase in earnings for 2000 primarily reflected the profitability of Crown Life's remaining insurance operations and related investment activities.

## Management's Discussion and Analysis

### Liquidity and Capital Resources

Long-term debt, including the portion due within one year, declined to \$811.5 million at December 31, 2001 from \$824.3 million at the beginning of the year. The \$12.8 million net reduction in long-term debt consisted of: an \$80.5 million reduction in the U.S. revolver loan balance; a \$24.3 million repayment of term debt; and a \$29.4 million investment in EHSI bonds; partially offset by an \$83.9 million increase in Canadian capital lease obligations, and a \$37.5 million increase in the 2001 year-end balance due to the change in the exchange rate on translation of U.S. operations. The closing rates used to translate U.S. operations were 1.5928 at December 31, 2001, and 1.4995 at December 31, 2000.

The cash flow statement reflects an issue of long-term debt of \$29.9 million, which represents a portion of the \$83.9 million in Canadian capital lease obligations recognized in 2001. The arrangement with Borealis was finalized in February 2001. The \$29.9 million represents those expenditures already incurred directly by ECI prior to the receipt of the funds from Borealis. Subsequent to the finalization of the capital lease agreement, the costs of the projects are paid directly by Borealis.

After taking into account interest rate swap agreements, the weighted average interest rate of all long-term debt at December 31, 2001 was approximately 7.3%. In addition, after considering swap agreements in place to fix certain floating rate debt, 81.0% of the long-term debt was effectively at fixed rates.

At December 31, 2001 the Company had cash and cash equivalents of \$25.5 million, compared with \$9.0 million at December 31, 2000. The increase in cash on hand was primarily due to the receipt during 2001 of financing for the Ontario construction projects, of which \$23.2 million had been expended directly by ECI prior to 2001.

Cash flow generated from operations prior to working capital changes was \$60.0 million, \$73.1 million, and \$94.1 million for the years ended December 31, 2001, 2000, and 1999, respectively. In March 2001, the Company received a \$22.6 million dividend from Crown Life. However, cash from operations declined over the

past three years due to reduced cash flow from ceased operations and an increase in claim payments for self-insured liabilities.

The net change in operating working capital (excluding cash and borrowings included in current liabilities) reflected a source of cash of \$76.4 million in 2001, and a use of cash in each of 2000 and 1999 of \$25.5 million and \$54.8 million, respectively. For 2001, the source of cash from working capital changes related to a tax refund of \$34.5 million on U.S. operating losses, and a reduction in accounts receivable due to improved collections efforts and ceased operations. The 2000 and 1999 uses of cash as a result of working capital changes, reflected reduced accounts payable in excess of the decline in accounts receivable, primarily as a result of asset disposals. Also, during 2000 the Company recovered its 1999 taxes recoverable balance through a tax refund of \$69.4 million, of which \$42.6 million related to asset sales.

Cash used for investing activities was \$33.5 million in 2001, compared to a source of cash of \$50.8 million in 2000 and \$47.5 million in 1999. Proceeds of \$12.2 million were realized on asset transactions in 2001, compared to \$54.5 million and \$132.0 million in 2000 and 1999, respectively. Property and equipment capital expenditures reflected on the cash flow statement were \$45.4 million in 2001, \$46.3 million in 2000 and \$50.3 million in 1999. Expenditures related to the growth of the business – such as construction of facilities and bed additions – were approximately \$9.8 million, \$22.0 million, and \$15.0 million, respectively. The expenditures during 2001 and 2000 related primarily to the construction of new Ontario facilities. Not reflected on the cash flow statement is \$54.0 million of construction costs paid directly by Borealis under the capital lease. Growth expenditures during 1999 related to the completion of new facilities constructed in the U.S. and the start of development of the new Ontario projects. Maintenance capital expenditures, which represent required periodic capital improvements and routine replacement of capital items, were \$35.6 million, \$24.3 million and \$35.3 million, respectively, for the past three years. During 2001, maintenance capital expenditures increased due to additional renovation projects to existing facilities. The

## Management's Discussion and Analysis

decline in maintenance capital expenditures during 2000 related to non-recurring renovation projects and the disposal of facilities.

Cash used in financing activities was \$86.6 million in 2001, \$116.6 million in 2000, and \$80.2 million in 1999, primarily reflecting the Company's change in long-term debt.

At the end of 2001, the Company's accrual for self-insured liabilities was \$204.2 million compared to \$182.0 million at the beginning of the year. The current year's provision, net of claim payments, increased the accrual by \$10.3 million, with the remaining increase due to the change in the year-end exchange rate on translation of U.S. operations. The Company self-insures certain risks related to general and professional liability, auto liability, health benefits, and employers' liability. The accrual for self-insured liabilities includes estimates of the costs of both reported claims and claims incurred but not yet reported. As of January 1, 2001, EHSI no longer operates nursing and assisted living facilities in the State of Florida, and as of October 1, 2001, EHSI ceased nursing home operations in the State of Texas. Consequently, EHSI has reduced its level of exposure to future litigation in these states. However, as a result of an increase in the frequency and severity of claims, the Company recorded a provision to increase its accrual for resident care liability costs by \$38.5 million in the third quarter of 2001, of which \$33.8 million was attributable to potential claims for incidents occurring in Florida and Texas prior to EHSI's ceasing of nursing home operations in these states. This additional accrual was based upon an independent actuarial review. Management believes the Company has provided sufficient reserves at the end of December 2001 for estimated costs of self-insured liabilities.

The Company invests funds to support the accrual for self-insured liabilities. These funds, reported in other assets, totalled \$45.5 million at the end of 2001, compared to \$68.2 million at the end of 2000. In addition, the Company's captive insurance company, Laurier Indemnity Company, Ltd., held an intercompany investment in EHSI bonds. This investment had a face value of \$24.5 million (US\$15.4 million) and a carrying value of \$21.3 million (US\$13.4 million) at the end of 2001. Most of the risks that the Company self-insures are long-term in nature and accordingly, claim payments

for any particular policy year occur over a long period of time. The Company believes that it has sufficient cash resources to meet its estimated current claims payment obligations.

The Company obtains third-party reinsurance for its self-insured liabilities. Beginning in 2000, due to the adverse litigious environment experienced by the long-term care industry, the Company's reinsurance premiums and per claim risk retention for general and professional liability risks increased significantly.

The Company's long-term debt, including current maturities, as a percent of total long-term debt and capital, was 69.8% at December 31, 2001 compared to 68.4% at the beginning of the year. While the Company continued to reduce its leverage in 2001, shareholders' equity also declined, due to losses incurred and the purchase for cancellation of share capital.

During 2002, capital expenditures of approximately \$110.0 million are planned, of which approximately \$50.0 million will relate to the new Ontario facilities. In conjunction with the construction of new facilities, renovations related to existing facilities in both the U.S. and Canadian operations are planned.

The current level of cash flow, available bank credit facilities and long-term capital lease financing are sufficient to support ongoing operations and capital expenditures, service debt obligations and pay preferred share dividends. At year-end, EHSI had US\$74.3 million available under its revolver loan, and the Canadian operations had \$4.2 million available under its operating bank line.

EHSI is in compliance with the financial covenants of its credit facility as of December 31, 2001. The financial covenants under this credit facility continue to become more stringent over the term of the facility. While management has a strategy to remain in compliance, there can be no assurance that EHSI will meet future covenant requirements. EHSI's available bank lines can be affected by its ability to remain in compliance, or if not, would depend upon management's ability to amend the covenants or refinance the debt.

### Recently Issued Accounting Standards

On July 20, 2001, the Canadian Institute of Chartered Accountants issued new Handbook Sections 1581, "Business Combinations", and 3062, "Goodwill and

## Management's Discussion and Analysis

Other Intangible Assets". Section 1581 requires that all business combinations initiated after June 30, 2001 be accounted for under a single method – the purchase method. Use of the pooling-of-interests method is no longer permitted. Section 3062 requires that goodwill and other intangible assets with an indefinite life be tested for impairment on an annual basis and no longer be amortized. The Company adopted the provisions of Section 1581 as of July 2001. The Company is required to adopt Section 3062 no later than its fiscal year beginning January 1, 2002. The Company will be required to reassess the useful lives and residual values of goodwill and intangible assets acquired, with such valuation to take place on a transitional basis during the first year of adoption. Any impairment loss will be measured as of the date of adoption and recognized as an adjustment to opening retained earnings at January 1, 2002.

As at December 31, 2001, the Company had unamortized goodwill of \$115.2 million, which will be subject to the transition provisions of Section 3062. Amortization expense related to goodwill was \$4.0 million, and \$3.4 million for 2001 and 2000, respectively. Based on current market conditions, which could change in the future, management expects that these impairment tests will not have a material impact on the Company's consolidated financial position or results from operations.

In November 2001, the CICA amended Handbook Section 1650, "Foreign Currency Translation" and issued Accounting Guideline 13 (AcG 13), "Hedging Relationships". The revision to Section 1650 eliminates the deferral and amortization of foreign currency translation differences resulting from the translation of long-term monetary assets and liabilities denominated in foreign currencies. All such translation differences will be charged directly to income. Section 1650 took effect as of January 1, 2002 and requires a retroactive restatement. The Company did not have any such amount deferred on its balance sheet at December 31, 2001 or 2000.

AcG 13 establishes new criteria for hedge accounting and will apply to all hedging relationships in effect on or after January 1, 2003. Currently, the only hedging

relationships the Company has are its interest rate swaps, which fix the rates on certain floating debt. These swaps would continue to qualify as hedges under the new criteria. On January 1, 2003 the Company will re-assess all hedging relationships existing at that time to determine whether the criteria are met or not and will apply the new guidance on a prospective basis.

In December 2001, Handbook Section 3870, "Stock-based Compensation and Other Stock-based Payments" was issued. Section 3870 establishes standards for the recognition, measurement, and disclosure of stock-based compensation and other stock-based payments made in exchange for goods and services provided by employees and non-employees. It applies to transactions in which shares of common stock, stock options, or other equity instruments are granted or liabilities incurred based on the price of common stock or other equity instruments.

Section 3870 sets out a fair value based method of accounting that is required for certain, but not all, stock-based transactions. Section 3870 must be applied to: all stock-based payments to non-employees, and to employee awards that are direct awards of stock, that call for settlement in cash or other assets, or are stock appreciation rights that call for settlement by the issuance of equity instruments. However, the new standard permits the Company to continue its existing policy that no compensation cost is recorded on the grant of stock options to employees. Consideration paid by employees on the exercise of stock options is recorded as share capital.

Section 3870, however, does require additional disclosures for options granted to employees, including disclosure of pro forma earnings and pro forma earnings per share as if the fair value based accounting method had been used to account for employee stock options.

Other than stock options granted, for which the Company will adopt the additional disclosure requirements, the Company has not entered into any such transactions that would result in a change to opening balances upon retroactive application of Section 3870 as at January 1, 2002.

## Management's Responsibility for Financial Statements

The accompanying consolidated financial statements of Extencicare Inc. and other financial information contained in this annual report are the responsibility of management. The consolidated financial statements have been prepared in conformity with Canadian generally accepted accounting principles, using management's best estimates and judgments, where appropriate. In the opinion of management, these consolidated financial statements reflect fairly the financial position, results of operations and cash flows of the Company within reasonable limits of materiality. The financial information contained elsewhere in this annual report has been reviewed to ensure consistency with that in the consolidated financial statements.

A system of internal accounting and administrative controls is maintained by management to provide reasonable assurance that assets are safeguarded against loss from unauthorized use or disposition and that financial records are properly maintained to provide accurate and reliable financial statements.

The Extencicare Board of Directors is responsible for ensuring that management fulfills its responsibilities for financial reporting and internal controls. The Board carries out this responsibility principally through its independent Audit Committee comprised of unrelated and outside directors. The Audit Committee meets regularly during the year to review significant accounting and auditing matters with management and the independent auditors and to review the interim and annual consolidated financial statements of the Company.

The consolidated financial statements have been audited by KPMG LLP, Chartered Accountants, which has full and unrestricted access to the Audit Committee. KPMG's report on the consolidated financial statements follows.



**Mel Rhineland**  
President and  
Chief Executive Officer



**Mark W. Durishan**  
Vice-President, Finance,  
and Chief Financial Officer

February 21, 2002

## Auditors' Report

### To the Shareholders of Extencicare Inc.

We have audited the consolidated balance sheets of Extencicare Inc. as at December 31, 2001 and 2000 and the consolidated statements of loss, shareholders' equity and cash flows for each of the years in the three-year period ended December 31, 2001. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

We conducted our audits in accordance with Canadian generally accepted auditing standards. Those standards require that we plan and perform an audit to obtain reasonable assurance whether the consolidated financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall consolidated financial statement presentation.

In our opinion, these consolidated financial statements present fairly, in all material respects, the financial position of the Company as at December 31, 2001 and 2000 and the results of its operations and cash flows for each of the years in the three-year period ended December 31, 2001 in accordance with Canadian generally accepted accounting principles.



Toronto, Canada  
February 21, 2002

**KPMG LLP**  
Chartered Accountants

## Consolidated Balance Sheets

(thousands of dollars) December 31

### Assets

#### Current assets

Cash and short-term investments	26,491	10,181
Accounts receivable	194,412	222,477
Income taxes recoverable	8,352	34,550
Future income tax assets (note 10)	17,987	15,346
Inventories, supplies and prepaid expenses	15,227	15,745

#### Property and equipment (note 3)

#### Goodwill

#### Other assets (note 4)

	262,469	298,299
	968,202	920,231
	115,196	112,775
	258,435	257,040

#### Investment in Crown Life Insurance Company (note 5)

	1,604,302	1,588,345
	135,944	147,407

	1,740,246	1,735,752
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### Liabilities and Shareholders' Equity

#### Current liabilities

Bank overdraft	942	1,147
Accounts payable and accrued liabilities	276,828	247,719
Current maturities of long-term debt (note 7)	23,128	21,876

#### Accrual for self-insured liabilities (note 6)

#### Long-term debt (note 7)

#### Deposits under divestiture agreement (note 4)

#### Future income tax liabilities (note 10)

#### Minority interests

	300,898	270,742
	204,221	182,026
	788,354	802,426
	47,784	44,985
	48,293	53,549
	–	587

#### Shareholders' equity

	1,389,550	1,354,315
	350,696	381,437

	1,740,246	1,735,752
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### Approved by the Board



**David J. Hennigar**

Chairman



**Mel Rhinelander**

President and  
Chief Executive Officer

## Consolidated Statements of Loss

*(thousands of dollars except per share amounts) Years ended December 31*

	2001	2000	1999
<b>Revenue</b> <i>(note 9)</i>			
Nursing and assisted living centres			
United States	1,187,547	1,346,033	1,364,084
Canada	279,559	266,671	260,723
United Kingdom	–	–	35,985
Outpatient therapy and medical supplies – United States	14,733	14,430	63,989
Home health – Canada	171,809	161,323	150,280
Other	50,863	18,949	17,626
	<b>1,704,511</b>	<b>1,807,406</b>	<b>1,892,687</b>
<b>Operating and administrative costs</b>	<b>1,549,152</b>	<b>1,687,408</b>	<b>1,752,845</b>
<b>Earnings before undernoted</b>	<b>155,359</b>	<b>119,998</b>	<b>139,842</b>
Lease costs	28,202	27,529	29,095
Depreciation and amortization	71,547	75,002	86,880
Interest, net	65,248	78,484	91,888
Loss from asset impairment, disposals and other items <i>(note 2)</i>	50,082	42,747	183,889
<b>Loss before income taxes</b>	<b>(59,720)</b>	<b>(103,764)</b>	<b>(251,910)</b>
<b>Income taxes</b> <i>(note 10)</i>			
Current (recovery)	8,270	(20,625)	(58,414)
Future (reduction)	(20,929)	(16,291)	(10,805)
	<b>(12,659)</b>	<b>(36,916)</b>	<b>(69,219)</b>
Loss from health care before minority interests	(47,061)	(66,848)	(182,691)
Minority interests	83	257	(171)
<b>Loss from health care</b>	<b>(47,144)</b>	<b>(67,105)</b>	<b>(182,520)</b>
<b>Share of earnings of Crown Life</b> <i>(note 5)</i>	<b>10,738</b>	<b>7,827</b>	<b>22,818</b>
<b>Loss for the year</b>	<b>(36,406)</b>	<b>(59,278)</b>	<b>(159,702)</b>
<b>Basic and diluted loss per share</b> <i>(note 11)</i>	<b>(0.52)</b>	<b>(0.81)</b>	<b>(2.14)</b>

## Consolidated Statements of Cash Flows

(thousands of dollars) Years ended December 31

### Cash provided by operations

	2001	2000	1999
Loss	(36,406)	(59,278)	(159,702)
Adjustments for:			
Depreciation and amortization	71,547	75,002	86,880
Provision for self-insured liabilities	69,335	71,252	85,341
Payments for self-insured liabilities	(59,079)	(30,637)	(20,174)
Provision for punitive damages	–	13,249	–
Future income taxes (note 10)	(20,929)	(16,291)	(10,805)
Dividends received, net of undistributed share of earnings of Crown Life	11,874	(7,827)	(22,818)
Loss from asset impairment, disposals and other items, net of current taxes (note 2)	23,130	42,747	93,780
Reserve (recovery) for settlements with third parties	–	(17,794)	39,546
Other	530	2,709	2,090
	60,002	73,132	94,138
Net change in operating working capital, excluding cash			
Accounts receivable	40,703	7,825	14,455
Inventories, supplies and prepaid expenses	958	2,593	1,068
Accounts payable and accrued liabilities	(5,472)	(41,967)	(48,092)
Income taxes	40,215	6,066	(22,284)
	136,406	47,649	39,285

### Cash provided by (used in) investment activities

Property and equipment	(45,377)	(46,292)	(50,268)
Net cash proceeds from divestiture agreement (note 4)	–	43,774	–
Net cash proceeds from dispositions (note 2)	12,236	10,677	132,002
Income taxes recovered (paid) related to dispositions	–	42,584	(37,790)
Other assets	(371)	71	3,586
	(33,512)	50,814	47,530

### Cash provided by (used in) financing activities

Issue of long-term debt	29,851	–	65,886
Repayment of long-term debt	(104,799)	(115,501)	(128,119)
Purchase of subsidiary public debt	(24,852)	(6,735)	–
Decrease (increase) in investments held for self-insured liabilities	27,989	13,161	(8,865)
Purchase of shares for cancellation	(10,283)	(4,036)	(5,932)
Financing costs	(2,301)	(2,894)	(3,102)
Other	(2,167)	(592)	(89)
	(86,562)	(116,597)	(80,221)

### Foreign exchange gain (loss) on cash held in foreign currency

	183	(62)	(283)
<b>Increase (decrease) in cash and cash equivalents</b>	<b>16,515</b>	<b>(18,196)</b>	<b>6,311</b>
Cash and cash equivalents at beginning of year	9,034	27,230	20,919
<b>Cash and cash equivalents at end of year</b>	<b>25,549</b>	<b>9,034</b>	<b>27,230</b>

## Consolidated Statements of Shareholders' Equity

(thousands of dollars for amounts) Years ended December 31

	2001		2000		1999	
	Number	Amount	Number	Amount	Number	Amount
<b>Share Capital</b> (note 8)						
Class I Preferred Shares						
Cumulative Redeemable, Series 2						
Issued and outstanding at beginning of year	173,705	4,343	226,005	5,650	290,705	7,268
Purchased pursuant to obligation	(19,300)	(483)	(52,300)	(1,307)	(64,700)	(1,618)
Issued and outstanding at end of year	154,405	3,860	173,705	4,343	226,005	5,650
Adjustable Dividend, Series 3						
Issued and outstanding at beginning of year	165,243	4,131	165,243	4,131	165,243	4,131
Converted to Series 4	(71,933)	(1,798)	-	-	-	-
Issued and outstanding at end of year	93,310	2,333	165,243	4,131	165,243	4,131
Adjustable Dividend, Series 4						
Issued and outstanding at beginning of year	169,307	4,233	169,307	4,233	169,307	4,233
Issued on conversion of Series 3	71,933	1,798	-	-	-	-
Issued and outstanding at end of year	241,240	6,031	169,307	4,233	169,307	4,233
Class II Preferred Shares, Series 1	382,979	6,319	382,979	6,319	382,979	6,319
Class I and II Preferred Shares issued and outstanding at end of year	18,543		19,026		20,333	
Subordinate Voting Shares						
Issued and outstanding at beginning of year	60,063,923	282,275	61,348,023	288,311	62,532,182	293,889
Purchased pursuant to issuer bid	(1,744,900)	(8,201)	(1,284,100)	(6,036)	(1,197,800)	(5,612)
Issued on conversion of Multiple Voting Shares	203,488	506	-	-	13,641	34
Issued pursuant to options	22,000	92	-	-	-	-
Issued and outstanding at end of year	58,544,511	274,672	60,063,923	282,275	61,348,023	288,311
Multiple Voting Shares						
Issued and outstanding at beginning of year	13,204,005	32,855	13,204,005	32,855	13,217,646	32,889
Purchased pursuant to issuer bid	(224,600)	(559)	-	-	-	-
Converted to Subordinate Voting Shares	(203,488)	(506)	-	-	(13,641)	(34)
Issued and outstanding at end of year	12,775,917	31,790	13,204,005	32,855	13,204,005	32,855
<b>Share Capital</b>	325,005		334,156		341,499	
<b>Retained earnings (deficit)</b>						
Balance at beginning of year		(5,661)		55,644		215,232
Loss for the year		(36,406)		(59,278)		(159,702)
Transfer of contributed surplus (note 8)		21		3,303		1,298
Purchase of shares in excess of book (note 8)		(1,062)		-		-
Retroactive adjustments for new accounting requirements (notes 10, 15)		-		(4,085)		-
Preferred share dividends		(1,000)		(1,245)		(1,184)
Balance at end of year		(44,108)		(5,661)		55,644
<b>Foreign currency translation adjustment account</b>						
		69,799		52,942		38,790
		350,696		381,437		435,933

# Notes to the Consolidated Financial Statements

Years ended December 31, 2001, 2000 and 1999

## 1. Summary of Significant Accounting Policies

### (A) Basis of Presentation

The consolidated financial statements have been prepared in accordance with Canadian generally accepted accounting principles and include the accounts of Extendicare Inc. and its subsidiaries ("Extendicare" or the "Company"). Health care operations are conducted through wholly owned subsidiaries Extendicare Health Services, Inc. (EHSI) in the United States, and Extendicare (Canada) Inc. (ECI) in Canada, and prior to its disposal in December 1999, Extendicare (UK) Limited in the United Kingdom, and their subsidiaries.

The equity method is used to account for the Company's 34.8% ownership interest in Crown Life Insurance Company (Crown Life).

Certain reclassifications have been made to the 2000 and 1999 financial statements to conform to the 2001 presentation.

### (B) Use of Estimates

The preparation of financial statements in conformity with Canadian generally accepted accounting principles requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. The more subjective of such estimates are Medicare cost reimbursement, accrual for self-insured liabilities, impairment of capital assets and goodwill, and valuation allowances for future tax assets. The recorded amounts for such items are based on management's best information and judgment, and accordingly, actual results could differ from those estimates.

### (C) Foreign Currency Translation

Foreign operations and foreign currency denominated items are translated to Canadian dollars.

Revenues and expenses of self-sustaining foreign operations are translated at average rates of exchange in effect during the period. Assets and liabilities are translated at the exchange rates in effect at the balance sheet date. Unrealized exchange gains or losses arising on translation are deferred and included in shareholders' equity in the foreign currency translation adjustment account.

Other assets and liabilities denominated in foreign currencies are translated at the exchange rates in effect at the balance sheet date. Translation gains and losses are reflected in earnings in the period in which they arise except for gains and losses relating to non-current monetary items. Translation gains and losses related to these items are deferred and amortized on a straight-line basis over the remaining life of the respective item.

### (D) Cash and Cash Equivalents

Cash and cash equivalents include unrestricted cash and short-term investments less bank overdraft. Short-term investments, comprised of money market instruments, have a short maturity of 90 days or less from their date of purchase and are stated at cost, which approximates net realizable value.

### (E) Property and Equipment

Property and equipment is stated at cost less accumulated depreciation and amortization. Provisions for depreciation and amortization are computed by the straight-line method at rates based on the following estimated life expectancies:

- Buildings – 20 to 40 years;
- Building improvements – 5 to 30 years;
- Furniture and equipment – varying periods not exceeding 15 years;
- Land improvements – 10 to 25 years;
- Leasehold improvements – the shorter of the useful life of the improvements or the initial term of the lease; and, in certain cases, the initial term of the lease plus one renewal period, not to exceed 25 years.

Leased nursing home assets held under option agreements are stated at cost less accumulated depreciation. Provisions for depreciation are computed as outlined above.

## Notes to the Consolidated Financial Statements

### (F) Deferred Charges

Costs associated with obtaining financing are deferred and amortized over the life of the related debt. The costs of acquiring leasehold rights are deferred and amortized over the term of the lease including renewal options. Deferred charges are stated at cost less accumulated amortization and are included in other assets in the consolidated balance sheets.

### (G) Goodwill

Goodwill represents the cost of acquired net assets in excess of their fair market values. Amortization is computed using the straight-line method over periods not exceeding 40 years. On an ongoing basis, management reviews the valuation and amortization of goodwill, taking into consideration any events and circumstances that might have impaired the value. Goodwill is carried in the balance sheet at cost less accumulated amortization of \$20,537,000 (2000 – \$16,106,000).

### (H) Impairment of Capital Assets and Goodwill

The Company periodically assesses the recoverability of capital assets and goodwill when there are indications of potential impairment. In performing this analysis, management considers such factors as current results, trends and future prospects, in addition to other economic and regulatory factors. The amount of any impairment is determined as the excess of the asset's net carrying value over its estimated net recoverable amount, as determined by its estimated future cash flows or current market value, as appropriate.

### (I) Accrual and Investments Held for Self-insured Liabilities

The Company self-insures certain risks related to general and professional liability, auto liability, health benefits, employers' liability and workers' compensation. The accrual for self-insured liabilities includes estimates of the costs of both reported claims and claims incurred but not reported and is based on estimates of loss based on assumptions made by management, including consideration of actuarial projections.

The Company invests funds to support the accrual for self-insured liabilities. These funds are investment grade, are carried at amortized cost approximating market value and are classified in other assets as investments held for self-insured liabilities.

### (J) Revenue

In the United States, nursing centre revenue results from the payment for services and products from various federal and state medical assistance programs as well as private-pay residents. Revenues are recorded in the period in which services and products are provided at established rates less contractual adjustments. Contractual adjustments include differences between established billing rates and amounts estimated by management as reimbursable under various reimbursement formulas or contracts in effect. Differences between final settlements and amounts recorded in previous years are reported as adjustments to revenues in the period such settlements are determined.

In Canada, the fees charged by ECI for its nursing centres and home care services are regulated by provincial authorities. Provincial programs fund a substantial portion of these fees.

In the United Kingdom, a substantial portion of the Company's fees was funded by government agencies, either directly to the Company or through government assistance to residents. The fees paid by government agencies were based on care requirements and financial means assessments for each resident.

### (K) Income Taxes

The Company follows the liability method of tax allocation, which is based on differences between financial reporting and tax bases of assets and liabilities. Future income tax liabilities or assets are calculated using tax rates anticipated to apply in the periods that the temporary differences are expected to reverse. The income tax rates used to measure income tax assets and liabilities are those rates enacted or substantially enacted at the balance sheet date. Realization of the future tax assets is dependent on the availability of taxable income of similar character.

## Notes to the Consolidated Financial Statements

### (L) Employee Future Benefits

The costs of the Company's defined benefit pension plans, post-retirement health, life insurance and other post-employment benefits are accrued as earned, based on actuarial valuations. The Company's pension fund assets are valued at market values and the excess net actuarial gain or loss in excess of 10% of the greater of the benefit obligations and the market value of plan assets is amortized over the average remaining service periods of active employees. Employee future benefit obligations are measured using market interest rates for high quality debt instruments.

### (M) Stock-based Compensation Plan

The Company has a stock-based compensation plan, which is described in note 8. No compensation expense is recognized for this plan when stock options are issued to employees. Any consideration paid by employees on exercise of stock options is credited to share capital.

## 2. Loss (Gain) from Asset Impairment, Disposals and Other Items

The following summarizes the components of the loss (gain) from asset impairment, disposals and other items.

(thousands of dollars)

	2001			2000	1999
	Proceeds Net of Selling Costs	Net Book Value	Loss (Gain)	Loss	Loss
Loss (gain) from dispositions					
United States nursing and outpatient facilities	17,327	17,327	-	4,858	51,914
United States home health operations	-	-	-	-	2,305
United Kingdom operations	-	-	-	-	15,348
Canada rehabilitation therapy services	3,400	2,336	(1,064)	-	-
	<u>20,727</u>	<u>19,663</u>	<u>(1,064)</u>	4,858	69,567
Provision for impairment of assets					
United States			2,592	31,595	58,479
Canada			-	-	859
Provision for closure and loss on disposals of United States facilities			20,315	3,614	5,234
Provision for adverse development of general and professional liability costs			26,952	-	48,253
Provision for severance costs					
United States			-	1,641	1,082
Canada			-	-	415
Other			1,287	1,039	-
			<u>50,082</u>	<u>42,747</u>	<u>183,889</u>

## Notes to the Consolidated Financial Statements

The following reconciles the loss (gain) from asset impairment, disposals and other items to that reported in the cash flow statements. The provision for general and professional liability costs is removed as it is already reflected in the provision for self-insured liabilities line, as an item not involving cash.

<i>(thousands of dollars)</i>	2001	2000	1999
Reconciliation of loss (gain) to cash flow statements			
Loss (gain) from asset impairment, disposals and other items	50,082	42,747	183,889
Provision for general and professional liability costs	(26,952)	–	(48,253)
Current taxes related to dispositions	–	–	(41,856)
	<b>23,130</b>	42,747	93,780
Reconciliation of cash proceeds from dispositions			
Proceeds, net of selling costs	20,290	13,516	144,986
Cash held in escrow	–	(1,418)	(7,211)
Notes receivable	(5,133)	(1,421)	(5,773)
Preferred shares	(2,921)	–	–
	<b>12,236</b>	10,677	132,002

### 2001

During the year, the Company made provisions totalling \$20,315,000 related to ceased operations. These were comprised of a provision of \$3,002,000 (US\$1,953,000) related to the closure and or sale of three nursing properties, a loss of \$2,814,000 (US\$1,829,000) related to the transfer of the Texas nursing operations, and \$14,499,000 (US\$9,426,000) in provisions for previously ceased operations, primarily for the Florida nursing homes.

The Company also recorded charges of \$1,287,000 related to interest on past years' tax re-assessments and a write-off of deferred financing costs from the early payment of debt.

On December 7, 2001, ECI sold its investment in Accident Injury Management Clinics Inc. (AIM), a rehabilitative therapy business, resulting in a pre-tax gain of \$1,064,000. Gross proceeds of \$3,500,000 from the sale consisted of cash of \$2,200,000 and notes receivable of \$1,300,000.

At the end of September, EHSI ceased operating its nursing homes in Texas, consisting of 17 facilities (1,421 beds), through lease agreements with a third-party operator that has an option to purchase the properties. In addition to the loss described above on transfer of the assets, a provision of \$2,592,000 (US\$1,685,000) was recorded for impairment of the remaining Texas properties, related to leasehold rights and leasehold improvements.

In September, based upon an independent actuarial review, the Company recorded an additional provision of \$26,952,000 for resident care liability costs related to the Company's ceased Florida operations for years prior to 2001.

In April, ESHI disposed of two leased facilities in Florida to Tandem Health Care, Inc. (Tandem), which had operated the facilities since December 31, 2000 under lease agreements with purchase options. Gross proceeds of \$17,494,000 (US\$11,402,000, comprised of cash proceeds of US\$7,000,000, notes receivable of US\$2,498,000 and preferred shares of US\$1,904,000) were received, resulting in a \$3,254,000 pre-tax gain that was deferred until the balance of the purchase options held by Tandem on the remaining leased facilities are completed or the options expire.

### 2000

During December 2000, EHSI disposed of one nursing facility (120 beds) in Florida for proceeds of \$5,246,000 (US\$3,446,000, comprised of cash proceeds of US\$2,571,000, including escrow funds of US\$932,000, and a note receivable net of applicable discounts of US\$875,000). The sale resulted in a pre-tax loss of \$3,875,000.

## Notes to the Consolidated Financial Statements

During the third quarter of 2000, EHSI disposed of one nursing facility (119 beds) in Florida for \$4,151,000 (US\$2,809,000), resulting in a pre-tax gain of \$1,389,000.

During the second quarter of 2000, EHSI disposed of two nursing centres, which previously had been closed, for gross proceeds of \$3,959,000 (US\$2,656,000). Together, the sales resulted in pre-tax losses of \$2,268,000. During the first quarter of 2000, EHSI disposed of seven outpatient therapy facilities for gross proceeds of \$309,000, resulting in a pre-tax loss of \$104,000.

During the fourth quarter of 2000, the Company recorded a provision of \$31,595,000 (US\$20,753,000) related to the impairment of capital assets. The provision included the write-down to the net realizable value of certain assets that were subject to a purchase transaction (see below). Also during 2000, the Company determined that certain other United States assets located outside of Florida were impaired and, accordingly, recorded a provision of \$7,358,000.

In December, EHSI leased nine nursing centres in Florida (1,033 beds) to Tandem for an 18-month term. In April 2001, Tandem exercised its right to acquire two of the facilities. Tandem has options to purchase the remaining facilities at any time during the term of the lease for up to US\$37,000,000, less related costs and other credits that may exist at the time the options are exercised. In 2002, if Tandem holds the remaining leases to term, EHSI will receive rental fees of US\$3,500,00 and incur associated costs in respect of the leases of approximately US\$2,000,000. The provision for impairment of assets recorded in 2000, included \$24,237,000 related to the nine leased facilities, as the option price was less than the net book value of the assets.

The Company recorded a provision of \$3,614,000 primarily related to the closure of two nursing facilities and one assisted living facility in the United States. Severance costs recorded of \$1,641,000 were related to the divestiture of Florida operations.

### 1999

On December 30, 1999, EHSI divested six of its Florida facilities in a share transaction, for gross proceeds of \$58,454,000 (US\$40,500,000, comprised of cash proceeds of US\$36,500,000, and an interest bearing note of US\$4,000,000). The sale resulted in a pre-tax loss of \$52,678,000, and included the reduction of goodwill of \$41,463,000. The share sale resulted in a recovery of prior year income taxes of \$41,856,000. Also during 1999, EHSI sold three nursing facilities in the United States for gross proceeds of \$13,461,000 (US\$9,100,000), resulting in a pre-tax gain of \$764,000.

On November 30, 1999, the Company divested the home health business of EHSI for gross proceeds of \$18,765,000 (US\$12,700,000), resulting in a pre-tax loss of \$2,305,000. Goodwill related to the operations sold was reduced by \$7,943,000.

On December 7, 1999, the Company divested its United Kingdom operations for gross proceeds of \$62,956,000 (£26,300,000), resulting in a pre-tax and after-tax loss of \$15,348,000.

During the fourth quarter of 1999, the Company recorded a provision of \$58,479,000 related to asset impairment (goodwill – \$37,320,000; property and equipment – \$19,801,000; and deferred charges – \$1,358,000).

During 1999, the Company wrote down \$859,000 of the goodwill related to its investment in AIM, as a result of management's assessment of the fair value of the operations. The remaining \$680,000 in goodwill was being amortized over five years up to the disposition of the Company's investment in AIM.

The Company recorded a provision of \$5,234,000 related to the closure of four United States nursing facilities, and a provision of \$1,497,000 for severance costs related to certain staff reductions in the United States and Canada.

During the fourth quarter of 1999, the Company recorded a provision for adverse development of general and professional liability costs related to prior years of \$48,253,000.

In total, during 1999 the Company recorded a pre-tax loss of \$183,889,000 resulting from: the sale of nine nursing facilities, the sale of home health operations, and the closure of four nursing facilities in the United States; the sale of the United Kingdom operations; the write-down of assets; the provision for adverse development of general and professional liability costs; and the provision for severance costs. Total income tax expense related to these items was \$56,532,000.

## Notes to the Consolidated Financial Statements

### 3. Property and Equipment

*(thousands of dollars)*

	2001	2000
Land	92,133	88,601
Buildings	1,085,722	1,005,940
Furniture and equipment	175,738	174,328
Leasehold improvements	20,932	29,331
Construction in progress	29,366	28,148
	<b>1,403,891</b>	<b>1,326,348</b>
Accumulated depreciation and amortization	435,689	406,117
	<b>968,202</b>	<b>920,231</b>

The above includes \$66,029,000 (2000 – \$490,000) of net assets under capital leases of which \$65,526,000 relates to construction of eight new facilities, net of \$18,229,000 of government funding and \$152,000 of depreciation booked in 2001.

Based on new beds awarded in 1998 by the Government of Ontario, ECI undertook to construct eight new facilities at an estimated cost of \$125,400,000. In an agreement finalized in February 2001, ECI obtained from Borealis Long-Term Care Facilities Inc. (Borealis), a wholly owned subsidiary of the Ontario Municipal Employees Retirement System, financing of \$125,400,000 to build the new facilities. ECI will operate the facilities for Borealis during the 25-year capital lease arrangement at a financing cost of approximately 8.0%. Borealis funded \$83,907,000 in construction costs during 2001, which ECI capitalized as property and equipment, offset by a capital lease obligation. ECI incurred \$29,851,000 of the construction costs prior to the finalization of the February agreement. Accordingly, this portion of the funding was reported on the statement of cash flows as an issue of long-term debt. Construction costs subsequently incurred were paid directly by Borealis. The minimum rental schedule for capital leases includes anticipated capital expenditures of \$41,493,000 required to complete the facilities, as well as related financing costs, as agreed to with Borealis (note 13).

The Ontario Government is funding a portion of the construction costs over a 20-year period, with approximately \$74,400,000 to be received by ECI related to the new beds and certain redevelopment of existing beds. As each facility opens, a receivable from the government will be recorded and will offset the cost of construction, based upon applying a discount rate equivalent to the yield on a 20-year Ontario Government bond. During 2001, \$18,229,000 of amounts receivable included in other assets, discounted at rates ranging from 6.2% to 6.5%, was treated as a reduction of property and equipment related to the four facilities that were opened in 2001 (note 4).

Effective October 1, 2001, EHSI leased and or subleased 17 facilities in the State of Texas. Four facilities owned by EHSI were leased for five years and 13 facilities were subleased. One lease expired at the end of October 2001, and the remainder will expire February 2012.

At the end of December 2000, EHSI leased under two separate lease arrangements, 15 facilities located in the State of Florida. One lease arrangement (nine facilities) is for an 18-month period and the other (six facilities) has a 60-month term. The terms of the agreements provide the lessee with the option to purchase the facilities. The leases are treated as operating leases. The net book value at December 31, 2001 of the assets under these agreements was \$70,537,000 (2000 – \$67,836,000).

Interest is capitalized in connection with the construction of facilities and is amortized over the estimated useful life of the facilities. Interest capitalized in 2001, 2000 and 1999 was \$4,761,000, \$849,000 and \$751,000, respectively.

## Notes to the Consolidated Financial Statements

### 4. Other Assets

(thousands of dollars)

	2001	2000
Investments held for self-insured liabilities	45,465	68,199
Assets held under divestiture agreement (details below)	61,820	62,326
Notes, mortgages and amounts receivable	52,588	27,986
Other long-term receivables, less allowance of \$24,559 (2000 – \$23,120)	57,990	55,804
Deferred charges	19,075	20,582
Other investments	12,792	12,042
Leasehold rights	8,705	10,101
	<b>258,435</b>	<b>257,040</b>
Assets held under divestiture agreement:		
Land	4,911	4,623
Building	88,445	83,297
Furniture and equipment	15,665	17,151
	<b>109,021</b>	<b>105,071</b>
Accumulated depreciation and amortization	47,201	42,745
	<b>61,820</b>	<b>62,326</b>

The Company invests funds to support the accrual for self-insured liabilities. At the end of December 2001, these funds totalled \$66,773,000. Of this amount \$45,465,000 was reported in other assets, as compared to \$68,199,000 at the beginning of the year. At December 31, 2001, the Company's captive insurance company, Laurier Indemnity Company, Ltd., had an investment in EHSI Senior Subordinated Notes with a face value of \$24,529,000 (US\$15,400,000) and a carrying value of \$21,308,000 (US\$13,378,000). Accounting rules require that this intercompany investment be eliminated on consolidation, and therefore it is reflected as a reduction in long-term debt.

As of December 2001, EHSI is pursuing settlement of a number of outstanding Medicare and Medicaid receivables, with the long-term portion included in other assets. For two specific Medicare issues totalling \$35,201,000 (US\$22,100,000), agreement has been reached with the fiscal intermediary, that should resolution not be made in early 2002, the matters will be reviewed through a mediator between the fiscal intermediary and EHSI prior to either party proceeding to the Provider Reimbursement Review Board (PRRB). The two issues involve the allocation of overhead costs and a staffing cost issue.

In September 2000, EHSI reached an agreement with Greystone Tribeca Acquisition L.L.C. (Greystone), involving the disposal of 11 nursing centres and four assisted living centres. Gross proceeds were cash of \$44,985,000 (US\$30,000,000) and contingent consideration in the form of a series of notes, which have an aggregate potential value of up to US\$30,000,000 plus interest. The Greystone notes have a maximum term of 3.5 years, and may be retired at any time by Greystone through the subsequent sale or refinancing of the facilities. As of December 31, 2001, Greystone had not sold or refinanced any of the nursing properties. During the term of the notes, EHSI retains the right of first refusal and an option to repurchase the facilities. Accordingly, the contingent notes have not been reported on the balance sheet, and while EHSI no longer operates these facilities, they will remain on EHSI's balance sheet as assets held under divestiture agreement, as required by generally accepted accounting principles, until final consideration for each facility is determined and a corresponding gain or loss is recorded. The balance is net of depreciation of \$5,178,000 from the date of the agreement.

**5. Investment in Crown Life Insurance Company**

Extendicare holds a 34.8% (1,113,690 shares) common equity interest in Crown Life. In March 2001, Extendicare received dividends of \$22,608,000 (\$20.30 per common share), which had been declared by the Board of Directors of Crown Life on February 22, 2001.

In December 2000, Crown Life completed its acquisition of the common shares not held by its two principal shareholders, HARO Financial Company and Extendicare.

On January 1, 1999, Crown Life sold or indemnity reinsured substantially all of its insurance business to The Canada Life Assurance Company (Canada Life). The final settlement of the transaction was subject to the final determination of policy liabilities in accordance with the sale agreements. Thus, the resulting shareholders' gain on sale of \$47,934,000 was reported in the Crown Life financial results for the fourth quarter of 1999. Extendicare's share of this gain was \$15,146,000. The comprehensive agreement among Crown Life and its principal shareholders and Canada Life provides that at a later date Canada Life may either acquire substantially all of the balance of Crown Life's insurance business, or at the election of Canada Life or Crown Life's principal shareholders, make an offer for all of the common shares of Crown Life.

On January 12, 1999, Crown Life redeemed at par \$149,500,000 principal amount of convertible subordinated debentures that had been retracted by its principal shareholder, HARO Financial Company.

Crown Life is a defendant in a number of lawsuits that were commenced in prior years involving the sale, allegedly on a "vanishing premium" basis, of participating whole life insurance policies. Many life insurers are defendants in similar lawsuits brought by purchasers of such policies. Crown Life will vigorously contest all lawsuits. It is not possible to predict the ultimate outcome of the outstanding litigation, or to estimate additional costs that may result.

Crown Life has voided certain reinsurance contracts and continues to investigate the validity of the claims arising from other reinsurance contracts. It is not possible to estimate the ultimate costs, if any, that may result.

**6. Self-insured Liabilities and Measurement Uncertainty**

The accrual for self-insured liabilities is based on management's best estimate of the ultimate cost to settle claims. Management regularly evaluates the appropriateness of the carrying value of this liability. Of the risks for which the Company self-insures, general and professional liability claims are the most volatile and significant.

Management's estimate of the accrual for general and professional liability costs is significantly influenced by assumptions, which are limited by the uncertainty of predictions concerning future events, and assessments regarding expectations of several factors. Such factors include, but are not limited to: the frequency and severity of claims, which can differ materially by jurisdiction in which the Company operates; coverage limits of third-party reinsurance; the effectiveness of the claims management process; and uncertainty regarding the outcome of litigation.

The Company has experienced adverse claims development. Consequently, as of January 1, 2000 the Company's per claim retained risk increased significantly for resident care liability cost, mainly due to the level of risks associated with the Florida and Texas operations. In 2001, EHSI no longer operated nursing and assisted living facilities in the State of Florida and as of October 1, 2001 ceased nursing operations in the State of Texas, thereby reducing the level of exposure to future litigation in these litigious states. However, as a result of an increase in the frequency and severity of claims, the Company recorded a provision to increase its accrual for resident care liability costs in the third quarter of 2001. This additional accrual was based upon an independent actuarial review and was largely attributable to potential claims for Florida and Texas. Changes in the Company's level of retained risk, and other significant assumptions that underlie management's estimates of self-insured liabilities, could have a material effect on the future carrying value of the self-insured liabilities as well as the Company's operating results and liquidity.

The Company invests funds to support the accrual for self-insured liabilities. General and professional liability and workers' compensation risks are long-term in nature and accordingly, claim payments for any one policy year occur over a period of up to 10 years. The Company believes that it has sufficient cash resources to meet its estimated current claims payment obligations.

## Notes to the Consolidated Financial Statements

### 7. Long-term Debt

(thousands of dollars)

#### Payable in Canadian Dollars

Mortgages, 5.81% to 9.81%, maturing through to 2013

Obligations under capital leases (note 3)

#### Payable in United States Dollars

Bank term loans, at rates varying with prime and/or LIBOR,  
maturing through to 2004

Senior Subordinated Notes at 9.35%, due 2007

Mortgages and Industrial Development Bonds

6.25% to 13.61%, maturing through to 2010

At varying rates, due 2015

Notes payable, 3.00% to 10.00%, maturing through to 2008

Obligations under capital leases

Less due within one year and included in current liabilities

	2001	2000
	158,331	161,153
	83,810	–
	217,276	298,050
	274,121	286,553
	12,731	12,530
	57,232	56,374
	7,884	9,531
	97	111
	811,482	824,302
	23,128	21,876
	788,354	802,426

The weighted average interest rate of all long-term debt at December 31, 2001 was approximately 7.3% (2000 – 8.8%). After taking into account swaps to fix certain floating rate debt, 81% of the Company's total long-term debt at December 31, 2001 was subject to fixed rates.

Interest paid in 2001, 2000 and 1999 was \$66,391,000, \$78,984,000 and \$88,950,000, respectively.

EHSI entered into a syndicated bank credit agreement (the "Credit Facility") dated November 26, 1997, which provided EHSI with senior secured credit facilities of up to US\$600,000,000. The Credit Facility consisted of three term loans, each in the amount of US\$200,000,000, as follows: a six-year revolving credit facility (the "Revolving Credit Facility"); a six-year term loan (the "Tranche A Term Loan"); and a seven-year term loan (the "Tranche B Term Loan"). Borrowings under the Credit Facility are secured by the outstanding common shares and various assets of EHSI and each of its existing and future domestic subsidiaries. As a result of the decline in financial results, amendments to EHSI's Credit Facility in the second quarter of 1999 included revisions to the financial covenants, increased interest rates and asset securitization. The Credit Facility was further amended in the first quarter of 2000 for the 1999 general provision for Medicare settlements and non-cash provisions for general and professional liability costs.

On December 2, 1997, EHSI issued US\$200,000,000 9.35% Senior Subordinated Notes due 2007 (the "Subordinated Notes"). The Subordinated Notes are unsecured senior subordinated obligations of EHSI subordinated in right of payment to all existing and future senior indebtedness of EHSI, which includes all borrowings under the Credit Facility as well as all indebtedness not refinanced by the Credit Facility. At December 31, 2001, \$44,439,000 (US\$27,900,000) of the Senior Subordinated Notes was held by Extendicare and had been deducted from long-term debt.

The Revolving Credit Facility matures on December 31, 2003, at which time all outstanding borrowings are due. As part of the amendments to the Credit Facility, EHSI waived its right to US\$25,000,000 of the Revolving Credit Facility. The unused portion of the Revolving Credit Facility at December 31, 2001, was US\$74,300,000 (net of letters of credit of US\$37,700,000 and the US\$25,000,000 unavailable portion), which is available for working capital and general corporate purposes. The Tranche A Term Loan matures on December 31, 2003 with annual repayments of US\$6,576,000 in 2002 and US\$6,105,000 in 2003, payable in quarterly instalments. The Tranche B Term Loan matures on December 31, 2004 with annual repayments, payable in quarterly instalments, of US\$983,000 in 2002 and US\$629,000 in 2003, with the balance of US\$59,118,000 due in 2004.

## Notes to the Consolidated Financial Statements

Borrowings under the Credit Facility bear interest at EHSI's option at rates equal to the prime rate or LIBOR, plus applicable margins, depending upon leverage ratios of EHSI. Applicable margins at December 31, 2001, under the Revolving Credit Facility and the Tranche A Term Loan, were 1.50% for prime rate loans and 2.25% for LIBOR-based borrowings. The applicable margin at December 31, 2001, under the Tranche B Term Loan, was 2.25% for prime rate borrowings and 3.00% for LIBOR-based borrowings.

EHSI is party to two interest rate swap agreements to reduce the impact of changes in interest rates on certain of its floating rate long-term debt with two banks. The swaps effectively change the interest rates on US\$75,000,000 of LIBOR-based borrowings under the Credit Facility to fixed rates ranging from 5.53% to 5.74% (average of 5.67%), plus the applicable margins. One swap agreement, with notional amount of US\$50,000,000, matures on February 27, 2002 and the remaining agreement matures on February 27, 2003. EHSI may be exposed to credit loss in the event of non-performance by the banks under the swap agreements but does not anticipate such non-performance.

The Credit Facility contains a number of covenants, such as: restrictions on the payment of dividends by EHSI; redemption of EHSI's common stock and change of control, as defined, of EHSI; as well as financial covenants, including fixed charge coverage, debt leverage, and net worth ratios. EHSI is required to make mandatory prepayments of principal upon the occurrence of certain events, such as certain asset sales and certain issuances of securities. EHSI is permitted to make voluntary prepayments at any time. Such prepayments may, under certain conditions, reduce the amounts available to be borrowed under the Credit Facility.

EHSI is in compliance with the financial covenants of its credit facility as of December 31, 2001. The financial covenants under this credit facility continue to become more stringent over the term of the facility. While management has a strategy to remain in compliance, there can be no assurance that EHSI will meet future covenant requirements. EHSI's available bank lines can be affected by its ability to remain in compliance, or if not, would depend upon management's ability to amend the covenants or refinance the debt.

In Canada, the Company has a \$40,000,000 operating line, of which \$35,755,000 has been utilized by a standby letter of credit, primarily to secure pension obligations.

Principal payments on long-term debt due within the next five fiscal years, exclusive of those obligations under capital leases, after giving effect to renewal privileges, are as follows:

	<i>(thousands of dollars)</i>
2002	22,327
2003	115,782
2004	99,260
2005	5,455
2006	5,746

### 8. Share Capital

The authorized capital of the Company consists of an unlimited number of:

Class I preferred shares, issuable in series; Class II preferred shares, issuable in series; Subordinate Voting Shares; and Multiple Voting Shares, convertible on the basis of one Subordinate Voting Share for each Multiple Voting Share. All preferred shares are redeemable at \$25.00 per share at the option of the Company.

The Cumulative Redeemable Preferred Shares, Series 2 are entitled to receive quarterly cumulative preferential cash dividends in an amount determined by applying \$25.00 to one-quarter of 71% of the average Canadian prime rate of interest for the quarter ended immediately before the relevant dividend payment date.

The Adjustable Dividend Preferred Shares, Series 3 are entitled to receive quarterly cumulative preferential cash dividends in an amount determined by applying \$25.00 to one-quarter of 72% of an interest rate to be determined every five years by reference to yields on selected Government of Canada bonds (which rate has been set at 3.96% for the period commencing February 16, 2001, and ending February 15, 2006). The Series 3 Preferred Shares are convertible into Adjustable Dividend Preferred Shares, Series 4 on a share-for-share basis on February 16, 2006, and on each fifth anniversary thereof.

## Notes to the Consolidated Financial Statements

The Adjustable Dividend Preferred Shares, Series 4 are entitled to receive quarterly cumulative preferential cash dividends in an amount determined by applying \$25.00 to one-quarter of 72% of the average Canadian prime rate of interest for the quarter ended immediately before the relevant dividend payment date. The Series 4 Preferred Shares are convertible into Series 3 Preferred Shares on a share-for-share basis on February 16, 2006, and on each fifth anniversary thereof.

The Class II Preferred Shares, Series 1 are entitled to receive monthly cumulative cash dividends in an amount determined by applying \$25.00 to one-twelfth of the defined Annual Dividend Rate applicable to that calendar month. The Annual Dividend Rate for a calendar month is calculated with reference to the Canadian prime rate of interest and the defined Calculated Trading Price of the Class II Preferred Shares, Series 1.

The holders of Subordinate Voting Shares are entitled to one vote for each share held at any meeting of shareholders of the Company. The Subordinate Voting Shares entitle the holders thereof to quarterly preferential dividends cumulative within each financial year, aggregating 2.5 cents per share in each financial quarter, after which each Multiple Voting Share and Subordinate Voting Share participates equally in all further dividends.

The holders of Multiple Voting Shares are entitled to 10 votes for each share held at any meeting of shareholders.

The Company's accumulated contributed surplus during 2001 of \$21,000 (2000 – \$3,303,000; 1999 – \$1,298,000) arising on the purchase for cancellation of shares, was transferred to retained earnings. During 2001, shares purchased for cancellation in excess of their original cost resulted in a direct charge to retained earnings of \$1,062,000.

The Company, in each of 2001, 2000 and 1999, filed a Normal Course Issuer Bid for the purchase and cancellation of Subordinate Voting Shares. During 2001, the Company purchased and cancelled 1,744,900 Subordinate Voting Shares at a cost of \$8,237,000 (2000 – 1,284,100 shares at a cost of \$2,807,000). Of the shares purchased and cancelled during 2001, 35,900 shares were purchased under the current Subordinate Voting Share Bid at a cost of \$199,000. The current Subordinate Voting Share Bid, which commenced November 27, 2001, will terminate on the earlier of November 26, 2002 and the date on which a total of 4,000,000 shares have been purchased and cancelled by the Company pursuant to the Bid. In addition, the Company filed a Normal Course Issuer Bid for the purchase and cancellation of 375,000 Multiple Voting Shares, which began on May 1, 2001 and terminated on November 26, 2001. A new Bid was filed, which commenced on November 27, 2001 and will terminate on the earlier of November 26, 2002 and the date on which a total of 640,000 Multiple Voting Shares and 38,200 Class II Preferred Shares, Series 1, have been purchased and cancelled by the Company pursuant to the Bid. During 2001, the Company purchased and cancelled 224,600 Multiple Voting Shares at a cost of \$1,571,000. Of the shares purchased and cancelled during 2001, 19,800 shares were purchased under the current Bid at a cost of \$108,000.

The Company's Stock Option Plan (the "Plan") provides for the granting, from time to time, at the discretion of the Board of Directors, to certain directors, officers and employees of the Extencicare group of companies, of options to purchase Subordinate Voting Shares of the Company for cash. The Plan provides that the exercise price of any option granted shall not be less than the closing price (or, if there is no closing price, the simple average of the bid and ask price) of the Subordinate Voting Shares as quoted on The Toronto Stock Exchange on the trading day prior to the date of grant. It also permits options to be exercised for a period not to exceed either five or 10 years from the date of grant, as determined by the Board of Directors at the time the option is granted. The options vest equally over the first four years and the Plan contains provisions for appropriate adjustments in the event of a corporate reorganization.

A total of 4,776,350 Subordinate Voting Shares have been reserved under stock option plans of which a total of 2,342,875 Subordinate Voting Shares have been granted. These options have exercise prices ranging from \$2.37 to \$22.05, and expire between February 2002 and September 2006.

## Notes to the Consolidated Financial Statements

Stock option transactions during 2001 and 2000 were as follows:

	2001		2000	
	Shares	Weighted- average Exercise Price (\$)	Shares	Weighted- average Exercise Price (\$)
Outstanding at beginning of year	1,933,000	7.80	1,879,250	11.84
Granted	754,000	4.05	796,500	2.61
Exercised	(22,000)	4.15	-	-
Cancelled	(322,125)	6.30	(742,750)	12.44
Outstanding at end of year	2,342,875	6.84	1,933,000	7.80
Options exercisable at year-end	902,875	11.68	560,250	14.62

The following table summarizes information about stock options outstanding at December 31, 2001:

Range of Exercise Price (\$)	Options Outstanding			Options Exercisable	
	Number	Weighted- average Remaining Contractual Life	Weighted- average Exercise Price (\$)	Number	Weighted- average Exercise Price (\$)
2.37 to 4.35	1,391,875	3.4 years	3.30	287,375	3.37
4.70 to 7.01	474,000	3.1	5.37	145,000	5.52
15.60 to 22.05	477,000	0.3	18.62	470,500	18.66
	2,342,875			902,875	

### 9. Revenue

The Company derived approximately 75%, 75% and 72% of its United States revenue in 2001, 2000 and 1999, respectively, from services provided under various federal (Medicare) and state (Medicaid) medical assistance programs. The Medicare program pays each participating facility a prospectively set rate for each resident, which is based on the resident's acuity. Most Medicaid programs fund participating facilities using a case-mix based system, paying prospectively set rates. Prior to 1999, Medicare was a cost based reimbursement program.

In the normal course of business, EHSI has ongoing discussions with its fiscal intermediaries regarding the treatment of various items related to prior years' cost reports. Normally items are resolved during the audit process and no provision is required. Differences of opinion regarding cost reporting methods between EHSI and its fiscal intermediaries can be settled through a formal appeal process. Should this occur, a general provision for Medicare receivables may be recorded for disagreements that result in EHSI filing an appeal with the PRRB of the Centers for Medicare and Medicaid Services (CMS), formerly named the Health Care Financing Administration.

In 1999, a fiscal intermediary notified EHSI of several adjustments for services rendered from 1995 through 1998 and EHSI filed a formal appeal to the PRRB and was in the process of filing others. Based upon this situation, a general provision of \$39,546,000 (US\$27,400,000) was recorded during 1999 as a reduction in revenue.

## Notes to the Consolidated Financial Statements

In 2000, the PRRB heard EHSI's first appeal involving the reimbursement of workers' compensation costs and issued a decision that supported EHSI's position. The CMS administrator confirmed the PRRB's decision, which resulted in a favourable settlement of \$18,465,000, including a recovery of the general provision of \$15,272,000. In addition, EHSI reached a settlement with a fiscal intermediary regarding another cost reporting issue, which resulted in revenue of \$3,495,000, including a recovery of \$2,522,000 of the general provision. In total, a recovery of \$17,794,000 was recorded in 2000 relating to the general provision recorded in 1999.

Other adjustments related to prior years' estimated settlement amounts, including Medicare waiver requests set out above, increased revenue in 1999 by \$2,762,000.

For each participating facility, differences between revenue to be derived under third-party payor programs and amounts received as payments from such programs are reflected as accounts receivable when revenue is greater than payments received and as accrued liabilities when payments have exceeded revenue that the Company ultimately expects to be realized. Accounts receivable at December 31, 2001 and 2000, which are expected to be substantially collected within one year, include estimated settlements from third-party payors of \$18,800,000 and \$23,400,000, respectively.

### 10. Income Taxes

The provision (recovery) for income taxes is comprised as follows:

<i>(thousands of dollars)</i>	2001	2000	1999
Loss from health care before income taxes	(59,720)	(103,764)	(251,910)
Income taxes at statutory Canadian rate of 42.12% (2000 – 43.95%; 1999 – 44.62%)	(25,154)	(45,609)	(112,402)
Income tax effect relating to the following items:			
Non-deductible goodwill and accounting provisions	1,223	924	14,520
Tax rate variance of foreign subsidiaries	6,241	6,891	49,545
Benefit of operating and capital loss utilization	(224)	–	(42,200)
Capital losses not benefited	–	–	14,738
Non-taxable income	(224)	(531)	(695)
Other items	5,479	1,409	7,275
	(12,659)	(36,916)	(69,219)

Cash taxes recovered during 2001 and 2000 were \$31,945,000 and \$69,275,000, respectively and cash taxes paid in 1999 were \$43,517,000.

The Company adopted, on a retroactive basis, the new requirements of the Canadian Institute of Chartered Accountants (CICA) effective January 1, 2000, with respect to accounting for income taxes. The Company did not restate prior periods and therefore, at January 1, 2000, shareholders' equity included a cumulative charge to opening retained earnings of \$1,250,000.

At December 31, 2001, the Company had net operating loss carryforwards available for U.S. state income tax financial reporting purposes of \$152,600,000, which expire in years 2002 through 2021. The Company also had net operating loss carryforwards available for U.S. federal income tax financial reporting purposes of \$33,800,000, which expire in 2021. In addition, the Company had \$1,044,000 net operating loss carryforwards available for Canadian income tax purposes, which expire in years 2003 through 2008. To the extent the realization of these losses is uncertain, they have been offset by a valuation allowance.

There are capital losses available for income tax purposes amounting to \$62,979,000 (2000 – \$64,679,000) that can be carried forward indefinitely to apply against future capital gains. The future tax benefit of these capital losses of \$10,902,000 (2000 – \$11,590,000) has been fully offset in the valuation allowance for future tax assets.

## Notes to the Consolidated Financial Statements

The valuation allowance for future tax assets as of December 31, 2001 and 2000 was \$37,754,000 and \$33,908,000, respectively. The net change in the total valuation allowance for the 2001 year was an increase of \$3,846,000. In assessing the realizability of future tax assets, management considers whether it is more likely than not that some portion or all of the future tax assets will not be realized. The ultimate realization of future tax assets is dependent upon the generation of future taxable income during the periods in which those temporary differences become deductible. Management considers the scheduled reversal of future tax liabilities, projected future taxable income and tax planning strategies in making this assessment. Management believes it is more likely than not the Company will realize the benefits of these deductible differences, net of the valuation allowances.

Future income taxes are provided for temporary differences. The significant components of future income tax assets and liabilities are as follows:

<i>(thousands of dollars)</i>	2001	2000
Future income tax assets		
Self-insurance reserves	40,184	40,850
Investment in Crown Life	11,088	13,764
Employee benefit accruals	14,466	13,086
Accounts receivable reserves	11,855	12,272
Net capital loss carryforwards	10,902	11,590
Deferred revenue	5,044	-
Goodwill	3,220	3,879
Operating loss carryforwards	22,356	10,402
Operating reserves	6,285	3,273
Other	11,398	8,061
	136,798	117,177
Valuation allowance	37,754	33,908
	99,044	83,269
Future income tax liabilities		
Property and equipment	107,850	100,273
Leasehold rights	3,580	4,061
Other	17,920	17,138
	129,350	121,472
Future income tax liabilities, net	30,306	38,203
Less current portion of future income tax assets, net	17,987	15,346
Long-term future income tax liabilities, net	48,293	53,549

## Notes to the Consolidated Financial Statements

### 11. Loss per Share

Effective January 1, 2001, the Company adopted, on a retroactive basis, the revised CICA accounting standard for determining earnings per share. The treasury stock method is now used in the computation of diluted earnings per share, whereas previously, the Company used the "if converted" method. Earnings per share is calculated by dividing net earnings after preferred share dividends for the year by the weighted average number of combined Subordinate Voting Shares and Multiple Voting Shares outstanding during the year. Diluted earnings per share, using the treasury stock method, assumes outstanding stock options are exercised at the beginning of the year and common shares are purchased at the average market price during the year from funds derived on the exercise of these outstanding options.

The following table reconciles the numerator and denominator of the basic and diluted loss per share computation:

<i>(thousands of dollars except per share amounts)</i>	2001	2000	1999
Numerator for basic and diluted loss per share:			
Loss for the year	(36,406)	(59,278)	(159,702)
Dividends on preferred shares	(1,028)	(1,243)	(1,199)
	(37,434)	(60,521)	(160,901)
Denominator for basic and diluted loss per share:			
Weighted average number of Subordinate Voting Shares and Multiple Voting Shares	71,928,589	74,332,251	75,068,896
Basic and diluted loss per share	(0.52)	(0.81)	(2.14)

### 12. Segmented Information

During 2001, Extencicare had two reportable operating segments: United States operations and Canadian operations. Prior to December 6, 1999, the Company had a third operating segment in the United Kingdom. The Company's operations are managed independently of each other because of their geographic areas and regulatory environments. Each operation retains its own management team and is responsible for compiling its own financial information.

The Company, through its subsidiaries, operates long-term care facilities in the United States and Canada. Also offered in the United States are medical specialty services, such as subacute care and rehabilitative therapy services, while home health care services are provided in Canada.

Substantial portions of the Company's revenues are funded by various federal, state, provincial and local government programs. The funding programs from which Extencicare receives 10% or more of its revenues are: the United States federal Medicare program, representing revenues of \$283,747,000, \$335,495,000 and \$293,878,000 in 2001, 2000 and 1999, respectively; and the Ontario provincial government, representing revenues of \$229,618,000, \$273,585,000 and \$206,553,000 in 2001, 2000 and 1999, respectively.

## Notes to the Consolidated Financial Statements

The significant accounting policies of the reportable operating segments are the same as those described in note 1. Information about the Company's segments and a reconciliation of segment profit to net income are as follows:

*(thousands of dollars)*

	2001		
	United States	Canada	Total
Revenue			
Nursing and assisted living centres	1,187,547	279,559	1,467,106
Outpatient therapy	14,733	–	14,733
Home health	–	171,809	171,809
Other	47,508	3,355	50,863
	<u>1,249,788</u>	<u>454,723</u>	<u>1,704,511</u>
Earnings before undernoted	115,137	40,222	155,359
Lease costs	23,474	4,728	28,202
Depreciation and amortization	64,197	7,350	71,547
Interest expense	55,216	15,129	70,345
Interest revenue	(3,631)	(1,466)	(5,097)
Intersegment interest expense (revenue)	976	(976)	–
Loss from asset impairment, disposals and other items	50,082	–	50,082
	<u>(75,177)</u>	<u>15,457</u>	<u>(59,720)</u>
Earnings (loss) before income taxes			
Income taxes			
Current	1,798	6,472	8,270
Future (reduction)	(21,245)	316	(20,929)
	<u>(55,730)</u>	<u>8,669</u>	<u>(47,061)</u>
Net earnings (loss) from health care before minority interests			
Minority interests	–	83	83
	<u>(55,730)</u>	<u>8,586</u>	<u>(47,144)</u>
Net earnings (loss) from health care			
Share of earnings of Crown Life			10,738
			<u>(36,406)</u>
Loss			
Cash used in property and equipment	26,355	19,022	45,377
Balance sheet			
Property and equipment	764,321	203,881	968,202
Goodwill	114,884	312	115,196
Leasehold rights	8,705	–	8,705
	<u>1,324,399</u>	<u>279,903</u>	<u>1,604,302</u>
Assets before undernoted			
Investment in Crown Life			135,944
			<u>1,740,246</u>
Total consolidated assets			

## Notes to the Consolidated Financial Statements

(thousands of dollars)

	2000		
	United States	Canada	Total
Revenue			
Nursing and assisted living centres	1,346,033	266,671	1,612,704
Outpatient therapy	14,430	–	14,430
Home health	–	161,323	161,323
Other	16,660	2,289	18,949
	<u>1,377,123</u>	<u>430,283</u>	<u>1,807,406</u>
Earnings before undernoted	85,688	34,310	119,998
Lease costs	23,272	4,257	27,529
Depreciation and amortization	68,071	6,931	75,002
Interest expense	68,516	13,903	82,419
Interest revenue	(1,993)	(1,942)	(3,935)
Intersegment interest expense (revenue)	406	(406)	–
Loss from asset impairment, disposals and other items	42,747	–	42,747
	<u>(115,331)</u>	<u>11,567</u>	<u>(103,764)</u>
Earnings (loss) before income taxes			
Income taxes			
Current (recovery)	(21,435)	810	(20,625)
Future (reduction)	(19,934)	3,643	(16,291)
	<u>(73,962)</u>	<u>7,114</u>	<u>(66,848)</u>
Net earnings (loss) from health care before minority interests	(73,962)	7,114	(66,848)
Minority interests	37	220	257
	<u>(73,999)</u>	<u>6,894</u>	<u>(67,105)</u>
Net earnings (loss) from health care			
Share of earnings of Crown Life			7,827
			<u>(59,278)</u>
Loss			
Cash used in property and equipment	19,436	26,856	46,292
Balance sheet			
Property and equipment	763,578	156,653	920,231
Goodwill	111,824	951	112,775
Leasehold rights	10,101	–	10,101
	<u>1,385,451</u>	<u>202,894</u>	<u>1,588,345</u>
Assets before undernoted			
Investment in Crown Life			147,407
			<u>1,735,752</u>
Total consolidated assets			

## Notes to the Consolidated Financial Statements

(thousands of dollars)

1999

	United States	Canada	United Kingdom	Total
Revenue				
Nursing and assisted living centres	1,364,084	260,723	35,985	1,660,792
Medical supplies and outpatient therapy				
Therapy	14,720	-	-	14,720
Medical supplies and services	49,269	-	-	49,269
Home health	-	150,280	-	150,280
Other	15,828	1,798	-	17,626
	<u>1,443,901</u>	<u>412,801</u>	<u>35,985</u>	<u>1,892,687</u>
Earnings before undernoted	101,538	32,341	5,963	139,842
Lease costs	24,621	4,195	279	29,095
Depreciation and amortization	77,640	6,524	2,716	86,880
Interest expense	77,327	14,813	2,071	94,211
Interest revenue	(1,655)	(622)	(46)	(2,323)
Intersegment interest expense (revenue)	-	(1,206)	1,206	-
Loss from asset impairment, disposals and other items	167,267	1,274	15,348	183,889
Earnings (loss) before income taxes	(243,662)	7,363	(15,611)	(251,910)
Income taxes				
Current (recovery)	(58,527)	113	-	(58,414)
Deferred (reduction)	(13,773)	2,968	-	(10,805)
Net earnings (loss) from health care before minority interests	(171,362)	4,282	(15,611)	(182,691)
Minority interests	(236)	65	-	(171)
Net earnings (loss) from health care	(171,126)	4,217	(15,611)	(182,520)
Share of earnings of Crown Life				<u>22,818</u>
Loss				<u>(159,702)</u>
Cash used in property and equipment	33,748	15,184	1,336	50,268
Balance sheet				
Property and equipment	882,061	135,321	-	1,017,382
Goodwill	113,784	1,156	-	114,940
Leasehold rights	11,989	-	-	11,989
Assets before undernoted	1,494,747	203,053	-	1,697,800
Investment in Crown Life				<u>136,323</u>
Total consolidated assets				<u>1,834,123</u>

## Notes to the Consolidated Financial Statements

### 13. Other Commitments

At December 31, 2001, the Company was committed under non-cancellable leases requiring future minimum rentals as follows:

<i>(thousands of dollars)</i>	Capital Leases	Operating Leases	Total
2002	7,669	21,461	29,130
2003	11,644	16,534	28,178
2004	11,644	15,689	27,333
2005	11,635	15,317	26,952
2006	11,616	11,062	22,678
Thereafter	235,589	52,894	288,483
Total minimum payments	289,797	132,957	422,754
Less amount representing interest	164,463		
Obligations under capital leases	125,334		

At December 31, 2001, EHSI had capital expenditure purchase commitments outstanding of approximately \$8,600,000 (US\$5,400,000).

During 2000, EHSI exercised its right to purchase seven nursing facilities in the United States that it had operated under a lease agreement. EHSI continues to lease and operate the facilities in good faith and has held ongoing negotiations with the landlord to conclude issues involved in completing the transaction. Negotiations to date have not resolved all issues to complete the transaction and may require arbitration to conclude. The Company believes it has complied fully with the terms of the option and believes that settlement of outstanding issues can be resolved. There are, however, no assurances that the transaction will be completed, and as of December 31, 2001, the Company had \$6,690,000 in leaseholds and equipment relating to these facilities.

### 14. Contingent Liabilities

The Company and its consolidated subsidiaries are defendants in actions brought against them from time to time in connection with their operations. It is not possible to predict the ultimate outcome of the various proceedings at this time or to estimate additional costs that may result.

In December 2000, EHSI leased six nursing facilities (585 beds) to Senior Health Properties – South Inc. (Senior Health) for a 60-month term. Under the terms of the transaction, Senior Health has an option to purchase the properties for US\$10,700,000. EHSI will earn rental income based upon the net operating cash flow of the properties, which cannot exceed on average US\$2,000,000 per annum, and has entered into a specific-services consulting agreement over the term of the lease with Senior Health. Under the terms of the transaction, EHSI has retained a commitment to fund any cash flow deficiencies for one of the six properties, which EHSI anticipates would not exceed US\$300,000 per annum. All operations and assets, other than the land, building and equipment, were transferred to the lessees at the commencement of the leases at no cost to the lessees.

## Notes to the Consolidated Financial Statements

### 15. Employee Future Benefits

Retirement compensation arrangements, including defined benefit plans, are maintained with certain employee groups. Information about the Company's defined benefit pension plans follows:

*(thousands of dollars)*

	2001	2000
Accrued benefit obligations		
Balance at beginning of year	22,742	22,180
Current service cost	572	523
Benefits paid	(1,589)	(1,307)
Interest costs	1,706	1,525
Actuarial losses (gains)	1,653	(179)
Balance at end of year	25,084	22,742
Plan assets		
Fair value at beginning of year	6,288	5,675
Employer contributions	1,124	1,088
Actual return on plan assets	(430)	832
Benefits paid	(1,589)	(1,307)
Fair value at end of year	5,393	6,288
Funded status – plan deficit	19,691	16,454
Unamortized actuarial loss	(2,117)	565
Unrecognized net experience gains (losses)	(281)	(400)
Accrued benefit liability	17,293	16,619
Net benefit plan expense		
Current period service costs	572	523
Interest cost	1,706	1,525
Expected return on plan assets	(480)	(446)
Net benefit plan expense	1,798	1,602
Significant assumptions used		
Discount rate	7%	7%
Expected long term rate of return on plan assets	8%	8%
Rate of compensation increase	5%	5%
Average remaining service period of active employees	10 years	11 years

The Company maintains defined contribution retirement 401(K) savings plans in its United States operations, which are made available to substantially all of the Company's United States employees. EHSI pays a matching contribution of 17% to 25% of every qualifying dollar contributed by plan participants, net of any forfeitures. The Company incurred expenses related to the 401(K) savings plans of \$2,013,000, \$2,036,000 and \$1,547,000 in 2001, 2000 and 1999, respectively.

The Company adopted effective January 1, 2000, on a retroactive basis, the new requirements of the CICA with respect to accounting for employee future benefits. The Company did not restate prior periods and therefore, at January 1, 2000, shareholders' equity included a cumulative charge to opening retained earnings of \$2,835,000, net of income taxes of \$2,101,000.

## Notes to the Consolidated Financial Statements

### 16. Financial Instruments

With the exception of the following, the fair values of financial instruments approximate their recorded values.

(thousands of dollars)

	2001		2000	
	Carrying Amount	Fair Value	Carrying Amount	Fair Value
Accounts receivable, less allowance	248,798	246,828	277,312	273,478
Notes, mortgages and amounts receivable, including current portion	56,192	56,567	28,955	28,955
Other investments	12,792	9,445	12,042	7,788
Investments held for self-insured liabilities	45,465	46,507	68,199	69,605
Long-term debt, including current portion	811,482	833,421	824,302	867,695
Interest rate swaps	–	2,235	–	487

Accounts receivable, including other long-term receivables, are recorded at the net realizable value expected to be received from government assistance programs, other third-party payors or individual patients. The carrying values of accounts receivable approximate fair values due to their short maturities, with the exception of certain settlement receivables from third-party payors that are anticipated to be collected beyond one year. The fair value of these settlement receivables is estimated based on discounted cash flows at current borrowing rates.

Notes and mortgages receivable primarily consist of debt service and capital expenditure trust funds, and notes due from government agencies. The fair values for these instruments are based on the amount of future cash flows associated with each instrument, discounted using current applicable rates for similar instruments of comparable maturity and credit quality.

Receivables from government agencies represent the only concentrated group of credit risks for the Company. Management does not believe that there are any credit risks associated with these government agencies other than possible funding delays. Receivables other than from government agencies consist of receivables from various payors and do not represent any concentrated credit risks to the Company. Furthermore, management continually monitors and adjusts its allowances associated with these receivables.

Other investments consist of investments in stock and warrants, the fair values of which are based on quoted market prices.

The fair values for investments held for self-insured liabilities are based on quoted market prices. These investments are subject to insurance regulatory requirements. At year-end, the investment portfolio was comprised of investment-grade United States dollar-denominated corporate and government securities. The securities within the investments held for self-insured liabilities are all considered to be available for sale.

The Company has determined that it is not reasonable or meaningful to calculate a fair value for the accrual for self-insured liabilities.

The fair values for long-term debt are based on the amount of future cash flows associated with each instrument discounted using current applicable rates for similar instruments of comparable maturity and credit quality.

The fair values of interest rate swaps are based on the quoted market prices as provided by the financial institutions that are counter party to the swaps.

## Financial and Statistical Information

*(unaudited) (thousands of dollars unless otherwise noted)*

	2001	2000	1999	1998	1997
<b>Financial Position</b>					
Property and equipment	968,202	920,231	1,017,382	1,292,369	1,175,784
Health care assets	1,604,302	1,588,345	1,697,800	2,089,207	2,106,341
Investment in Crown Life, equity basis	135,944	147,407	136,323	132,631	125,435
Long-term debt	788,354	802,426	891,955	1,004,261	1,173,420
Shareholders' equity	350,696	381,437	435,933	656,853	553,493
<b>Financial Results</b>					
Revenue					
Nursing and assisted living centres					
United States	1,187,547	1,346,033	1,364,084	1,470,539	1,105,075
Canada	279,559	266,671	260,723	240,782	231,194
United Kingdom	-	-	35,985	38,412	31,762
Outpatient therapy and medical supplies – United States					
	14,733	14,430	63,989	209,308	156,879
Home health – Canada					
	171,809	161,323	150,280	134,984	122,941
Other					
	50,863	18,949	17,626	18,843	14,664
	<b>1,704,511</b>	<b>1,807,406</b>	<b>1,892,687</b>	<b>2,112,868</b>	<b>1,662,515</b>
Earnings (loss)					
Health care					
Earnings before lease costs, depreciation, interest and income taxes					
	155,359	119,998	139,842	251,403	222,911
Net earnings (loss) from health care					
	(47,144)	(67,105)	(182,520)	61,812	64,478
Share of earnings of Crown Life					
	10,738	7,827	22,818	3,520	8,893
Net earnings (loss)					
	(36,406)	(59,278)	(159,702)	65,332	73,371
Earnings (loss) per share from operations					
Health care operations before undernoted and after preferred share dividends					
	(0.18)	(0.55)	(0.75)	0.40	1.01
Loss (gain) from asset disposal and other items					
	(0.49)	(0.36)	(1.69)	0.40	(0.17)
Share of earnings of Crown Life					
	0.15	0.10	0.30	0.05	0.12
	<b>(0.52)</b>	<b>(0.81)</b>	<b>(2.14)</b>	<b>0.85</b>	<b>0.96</b>
<b>Other Information</b>					
Number of facilities (period end)					
United States	198	212	237	246	232
Canada	63	62	60	60	62
United Kingdom	-	-	-	16	16
	<b>261</b>	<b>274</b>	<b>297</b>	<b>322</b>	<b>310</b>
Operational resident capacity (period end)					
United States	18,402	19,420	22,055	23,536	22,459
Canada	7,937	7,632	7,527	7,828	8,289
United Kingdom	-	-	-	1,062	1,041
	<b>26,339</b>	<b>27,052</b>	<b>29,582</b>	<b>32,426</b>	<b>31,789</b>
Average occupancy (percentage)					
U.S. payor source as a percentage of total U.S. revenue					
Private	25	25	28	28	23
Medicare	24	24	22	29	33
Medicaid	51	51	50	43	44
Canadian home health care hours of service					
	6,868,000	6,967,000	6,562,000	6,303,000	5,920,000
Number of employees (period end)					
	36,700	38,800	41,000	44,100	41,100
Number of shares outstanding (period end)					
Subordinate Voting Shares	58,544,511	60,063,923	61,348,023	62,532,182	62,001,532
Multiple Voting Shares	12,775,917	13,204,005	13,204,005	13,217,646	13,656,546

## Board of Directors

### David J. Hennigar <sup>(CG)</sup>

#### Chairman

Mr. Hennigar is Chairman of Annapolis Group Inc. and of High Liner Foods Inc., as well as Chairman and founder of Acadian Securities Inc. He serves as a director of Crown Life Insurance Company and Scotia Investments Limited, as well as of several other private and public companies. Mr. Hennigar has been on the Extencicare Board since 1980; he resides in Bedford, Nova Scotia. Age 62.

### H. Michael Burns <sup>(CG) (IS)</sup>

#### Deputy Chairman

Mr. Burns is President of Kingfield Investments Limited and a director of several private and public companies, including Algoma Central Corp., Landmark Global Financial Corp., and InSystems Technologies Inc. Mr. Burns is Chancellor of Renison College, at the University of Waterloo. He has been on the Extencicare Board since 1978, and resides in Maple, Ontario. Age 64.

### Frederick B. Ladly <sup>(CG) (HR) (QS)</sup>

#### Deputy Chairman

Mr. Ladly is Vice-Chairman of Crown Life Insurance Company and a director of High Liner Foods Inc., Knudsen Engineering Limited, UBS Bank (Canada) and UBS Trust (Canada). He has been on the Extencicare Board since 1986. Mr. Ladly resides in the Township of Bathurst, Ontario. Age 71.

### Mel Rhinelander

#### President and Chief Executive Officer

Mr. Rhinelander was appointed Chief Executive Officer of Extencicare Inc. in August 2000, following his appointment as President in August 1999. He joined the Company in 1977 and has served in a number of senior positions. Mr. Rhinelander was elected to the Extencicare Board on May 2, 2000, and he resides in Milwaukee, Wisconsin. Age 51.

### Derek H. L. Buntain <sup>(HR) (IS)</sup>

Mr. Buntain is President of The Dundee Bank, a private bank offering banking services to international clients. He serves as a director of a number of public companies, including Dundee Precious Metals Inc., Eurogas Corporation and Cencotech Inc. Mr. Buntain joined the Extencicare Board in 1995, and he resides in Grand Cayman, Cayman Islands. Age 61.

### Sir Graham Day <sup>(CG) (HR)</sup>

Sir Graham is Chairman of Hydro One Inc. and Sobeys Inc., and Counsel to the Atlantic Canada law firm of Stewart McKelvey Stirling Scales. He serves as a director of a number of public and private companies, including The Bank of Nova Scotia and Empire Company Limited, and is a Fellow of the Institute of Corporate Directors. Sir Graham holds the Herbert S. Lamb Chair in Business Education in Dalhousie's Graduate School of Business Administration. He has been on the Board since 1989, and resides in Hantsport, Nova Scotia. Age 68.

### George S. Dembroski <sup>(A) (IS)</sup>

Mr. Dembroski serves as a director of Cameco Corporation, Electrohome Limited, Héroux-Devtek Inc., Middlefield Bancorp Limited, Murphy Oil Corporation, and other private companies. Mr. Dembroski joined the Extencicare Board in 1995, and resides in Toronto, Ontario. Age 67.

### David M. Dunlap <sup>(A) (HR) (QS)</sup>

Mr. Dunlap is Chairman of G.F. Thompson Co. Ltd., a manufacturing company, as well as of Burnley Manufacturing Inc. He is Vice-President of Canadian Mining and Finance Co. Ltd. Mr. Dunlap has been on the Board since 1980, and resides in the Township of King, Ontario. Age 63.

## Board of Directors

### **George A. Fierheller** <sup>(A) (IS)</sup>

Mr. Fierheller is President of Four Halls Inc., a private investment and consulting firm, and Chairman of The Greater Toronto Marketing Alliance. He serves as a director of GBC North America Growth Fund Inc., Rogers AT&T Wireless, and Sierra Systems Inc. Mr. Fierheller is a Member of the Order of Canada and Past President of the Toronto Board of Trade. He has been on the Extendicare Board since 1981, and resides in Toronto, Ontario. Age 68.

### **Dr. Seth B. Goldsmith** <sup>(CG) (QS)</sup>

Dr. Goldsmith is Professor of Health Policy and Management at the University of Massachusetts at Amherst. He is former Chief Executive Officer of the Miami Jewish Home & Hospital for the Aged, and has served as a consultant to numerous organizations including the World Health Organization, Geneva, Switzerland, and the U.S. Army. Dr. Goldsmith has been on the Board since 1995, and he resides in Hollywood, Florida. Age 60.

### **Michael J. L. Kirby** <sup>(CG) (HR) (QS)</sup>

Mr. Kirby is a member of The Senate of Canada. He serves as a director of The Bank of Nova Scotia, Goldfarb Corporation, Maxxcom Inc., Indigo Books & Music Inc., CPI Plastics Group Ltd. and ARS Networks Inc. Mr. Kirby has been on the Extendicare Board since 1987, and he resides in Nepean, Ontario. Age 60.

### **Alvin G. Libin** <sup>(A)</sup>

Mr. Libin is President and Chief Executive Officer of Balmon Holdings Ltd., a management services and investment company. He is Chairman of the Alberta Ingenuity Fund, is a director and one of the owners of the Calgary Flames of the National Hockey League, and serves as a director of several corporate and community boards. Mr. Libin is an Officer of the Order of Canada, and has been on the Extendicare Board since 1984. He resides in Calgary, Alberta. Age 70.

### **J. Thomas MacQuarrie, Q.C.** <sup>(A) (HR)</sup>

Mr. MacQuarrie is a senior partner in the Atlantic Canada law firm of Stewart McKelvey Stirling Scales. He serves as a director of Minas Basin Pulp & Power Co. Ltd. and High Liner Foods Inc., as well as of a number of other public and private corporations. Mr. MacQuarrie has been on the Extendicare Board since 1980. He resides in Halifax, Nova Scotia. Age 64.

- A** Audit Committee
- CG** Corporate Governance and Nominating Committee
- HR** Human Resources Committee
- IS** Information Systems Committee
- QS** Quality/Standards Committee

## Honorary Directors

### **Marsh A. Cooper**

President, M.A. Cooper Consultants Inc.

### **John J. Jodrey**

Chairman, Scotia Investments Limited

### **Derril G. McLeod, Q.C.**

Senior Counsel, Pedersen, Norman, McLeod & Todd

## **Corporate Governance**

The Toronto Stock Exchange (TSE) requires each listed company to disclose on an annual basis its approach to corporate governance with reference to guidelines published by the TSE (the “TSE Guidelines”). The Company’s corporate governance policy is outlined below.

### **Mandate of the Board**

The mandate of the Board includes:

- adopting a strategic planning process for the Company;
- approving objectives for the Company and the overall operating and financial plans to achieve them;
- evaluating the performance of the Company and its senior management;
- identifying and ensuring management of the principal risks of the Company’s business;
- responsibility for the integrity of the Company’s internal control and management information systems;
- selecting the Chief Executive Officer and approving the selection of other senior executives; and
- monitoring the Company’s communications with shareholders, other stakeholders and the general public.

The Board believes that management is responsible for the development of long-term corporate strategy, while the role of the Board is to review, question and validate, and ultimately to approve the strategies proposed by management. In addition to those matters that must by law be approved by the Board, management is required to seek Board approval for significant acquisitions, divestitures and capital expenditures. Other matters of strategic importance to the Company or that impact significantly on the operations of the Company are brought to the Board’s attention for its input, consideration and approval.

The Board’s expectation is that management will seek to maximize shareholder value in a manner that is consistent with good corporate citizenship, including fair treatment of the Company’s employees and the provision of quality service to the public.

### **Composition of the Board**

One of the TSE Guidelines recommends that the majority of a company’s board members be “unrelated”. An “unrelated” director is a director who is independent of management and is free from any interest and any business or other relationship that could, or could reasonably be perceived to, materially interfere with the director’s ability to act with a view to the best interests of the company, other than interests and relationships arising from shareholding.

The Board has considered the relevant definitions in the TSE Guidelines and other factors and has determined that of the Company’s 13 directors, 10 are unrelated directors. Although Messrs. Hennigar and Burns are “outside” directors, in that they are not considered to be members of management, they and Mr. Rhineland, by virtue of his position with the Company,

are clearly not unrelated directors and accordingly are related directors. In addition to the Board being comprised of a majority of unrelated directors, each Board committee is comprised of a majority of unrelated directors, and the role of the Chairman and Chief Executive Officer are separate.

The TSE Guidelines also recommend that, in circumstances where a company has a “significant shareholder” (i.e. a shareholder with the ability to exercise the majority of the votes for the election of the directors), the board of directors should include a number of directors who do not have interests in or relationships with either the company or the significant shareholder and who fairly reflect the investment in the company by shareholders other than the significant shareholder.

Mr. Burns and Mr. Hennigar, respectively representing the interests of Kingfield Investments Limited and Scotia Investments Limited, could be considered significant shareholders, given their agreement to act in concert. However, the 10 directors of the Company who are unrelated directors are also independent of Messrs. Burns and Hennigar, with the result that the investment in the Company by its other shareholders is fairly reflected in the composition of the Board.

The Board has determined that 13 directors is an appropriate number at the current time, given the Company’s structure and needs, as this permits the Board to be large enough for a diversity of experience and opinion, yet small enough to allow for efficient operation and decision making.

### Board Committees

The Company currently has an Audit Committee, a Corporate Governance and Nominating Committee, a Human Resources Committee, an Information Systems Committee and a Quality/Standards Committee. Set out below is a description of each committee, its mandate and its activities.

#### Audit Committee

The Audit Committee reviews the quarterly and annual financial statements of the Company, and makes recommendations to the Board with respect to these statements. It also makes recommendations to the Board regarding the appointment of independent auditors and their remuneration, and reviews any proposed changes in accounting practice or policies. The Committee reviews the nature, scope and results of the external audit and, with the auditors and management, the adequacy of the Company’s internal accounting control procedures and systems. The Committee meets with the external auditors independently of management at least once a year. It also reviews material for public disclosure.

The Audit Committee is composed of five directors, all of whom are unrelated directors. The Committee met four times during the financial year ended December 31, 2001.

## Corporate Governance

### Corporate Governance and Nominating Committee

The Corporate Governance and Nominating Committee makes recommendations as to the size and composition of the Board; reviews qualifications of potential candidates for election to the Board; recommends the slate of nominees for presentation to the annual shareholders' meeting; makes recommendations with respect to the membership of committees; and assesses the performance of the Board and its members. This Committee is responsible for planning succession to the position of Chief Executive Officer. The Committee also oversees issues of corporate governance as they apply to the Company and recommends amendments to the Company's corporate governance procedures where appropriate. Any director who wishes to engage outside advisors with respect to the affairs of the Company, at the expense of the Company, is required to review such matter with this Committee.

The Corporate Governance and Nominating Committee is composed of six directors, including four unrelated directors and two who are considered related directors, although they are outside directors. The Committee met once during the financial year ended December 31, 2001.

### Human Resources Committee

The Human Resources Committee reviews and approves the compensation of senior management with a view to ensuring that the level of compensation reflects performance. The Committee also reviews the performance of the Chief Executive Officer on an annual basis. The Committee is responsible for monitoring the development of senior management.

The Human Resources Committee also is responsible for reviewing and recommending directors' compensation. It reviews external surveys to compare the compensation paid by the Company with compensation paid to directors in other organizations.

The Human Resources Committee is composed of six directors, all of whom are unrelated directors. The Committee met four times during the financial year ended December 31, 2001.

### Information Systems Committee

The Information Systems Committee reviews information systems business plans and assesses new developments and initiatives being discussed across the business units with a view to enhancing business efficiency or competitive advantage. The Committee monitors the decision-making process regarding systems development and ensures that contingency plans are in place in the event of system breakdowns or malfunctions.

The Information Systems Committee is comprised of four directors, including three unrelated directors and one who is considered a related director, although he is an outside director. The Committee was established in 1998 in light of the significance of the Year 2000 Issue, as well as other major projects then being undertaken. During 2001 the Committee did not meet, as the Company's Year 2000 preparations were successful and the information systems projects in progress were sufficiently minor to be monitored by the Board as a whole during its regular meetings.

### Quality/Standards Committee

The Quality/Standards Committee's mandate is to monitor management's responsibilities with respect to service delivery practices and the achievement of certain quality service benchmarks. The Committee's responsibilities include ensuring that the Company and its operations have in place quality assurance processes that meet or exceed best practices; auditing the quality assurance programs of the Company and its operations against best practices and reporting outcomes to the Board not less than annually; and monitoring and providing advice with respect to strategies and approaches in dealing with government regulatory agencies.

The Quality/Standards Committee is composed of four directors, all of whom are unrelated directors. The Committee met four times during the financial year ended December 31, 2001.

### Directors' Orientation Program

The orientation of new directors consists of a presentation regarding their general responsibilities as directors, as well as being provided with an overview of current issues and business strategies by an executive of each of the main operating divisions. Board meetings held at regional locations in Canada and the United States are combined with tours of the Company's facilities so that the directors can gain a greater insight into the Company's business operations.

### Shareholder Relations

The Company holds scheduled quarterly telephone conference calls with investors and analysts. Shareholder questions and concerns are handled by the offices of the Chief Executive Officer and Chief Financial Officer. Corporate information is posted on the Extencare website at [www.extencare.com](http://www.extencare.com).

## Officers

### Extendicare Inc.

3000 Steeles Avenue East,  
Markham, Ontario  
Canada L3R 9W2  
Tel: (905) 470-4000  
Fax: (905) 470-5588

#### David J. Hennigar

Chairman

#### H. Michael Burns

Deputy Chairman

#### Frederick B. Ladly

Deputy Chairman

#### Mel Rhinelander

President and  
Chief Executive Officer

#### Mark W. Durishan

Vice-President, Finance, and  
Chief Financial Officer

#### Philip W. Small

Senior Vice-President,  
Strategic Planning and  
Investor Relations

#### Len G. Koroneos

Vice-President and Treasurer

#### Jillian E. Fountain

Corporate Secretary

### Extendicare Health Services, Inc.

111 West Michigan Street,  
Milwaukee, Wisconsin  
United States 53203-2903  
Tel: (414) 908-8000  
(800) 395-5000  
Fax: (414) 908-8059

#### Mel Rhinelander

Chairman and  
Chief Executive Officer

#### John G. McLaughlin

President and  
Chief Operating Officer

#### Mark W. Durishan

Vice-President,  
Chief Financial Officer,  
and Treasurer

#### Richard L. Bertrand

Senior Vice-President,  
Development

#### Philip W. Small

Senior Vice-President,  
Strategic Planning and  
Investor Relations

#### Roch Carter

Vice-President,  
General Counsel and  
Assistant Secretary

#### Douglas J. Harris

Vice-President and Controller

#### L. William Wagner

Vice-President

#### Jillian E. Fountain

Corporate Secretary

### Extendicare (Canada) Inc.

3000 Steeles Avenue East,  
Markham, Ontario  
Canada L3R 9W2  
Tel: (905) 470-4000  
Fax: (905) 470-5588

#### Mel Rhinelander

Chairman and  
Chief Executive Officer

#### Shelly L. Jamieson

President

#### Mark W. Durishan

Vice-President, Finance, and  
Chief Financial Officer

#### Philip W. Small

Senior Vice-President,  
Strategic Planning and  
Investor Relations

#### Elaine E. Everson

Vice-President and Controller

#### Stephen R. Haas

Vice-President,  
ParaMed Home Health Care

#### Paul Rushforth

Vice-President,  
Western Operations

#### Christina L. McKey

Vice-President,  
Human Resources

#### R. Gordon Spear

Vice-President,  
Administration

#### Jillian E. Fountain

Corporate Secretary

## Shareholder Information

### Extendicare Inc.

3000 Steeles Avenue East,  
Markham, Ontario L3R 9W2  
Tel: (905) 470-4000  
Fax: (905) 470-5588  
www.extendicare.com  
e-mail: wsmith@extendicare.com

### Shareholder Inquiries

Jillian Fountain  
Corporate Secretary  
Tel: (905) 470-5534

### Investor Relations

Wendy Smith, Tel: (905) 470-5584

### Transfer Agent

Computershare  
Tel: (800) 663-9097  
www.computershare.com

### Annual Meeting

Shareholders are invited to attend the Annual Meeting of Extendicare Inc. on Thursday, May 9, 2002 at 11:00 a.m. at the Glenn Gould Studio, Canadian Broadcasting Centre, 250 Front Street West, Toronto, Ontario, Canada.

### AIF and Form 40F

A copy of the Company's Annual Information Form and Form 40F filed with the securities commissions will be sent to any shareholder upon request to the Company's Corporate Secretary.

### Stock Exchange Listings

The Toronto Stock Exchange  
New York Stock Exchange (EXE.A only)

### Share Information

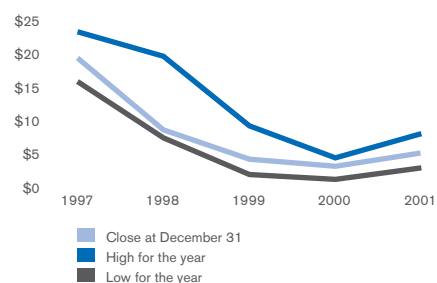
Shares	Stock Symbols	Shares Outstanding <sup>(1)</sup>	Year-end Closing Market Price on the TSE		
			2001	2000	1999
Multiple Voting	EXE	12,775,917	\$ 5.27	\$ 3.50	\$ 4.50
Subordinate Voting	EXE.A	58,544,511	5.25	3.40	4.35
Class I Preferred					
Series 2	EXE.PR.B	154,405	24.00	24.00	18.50
Series 3	EXE.PR.C	93,310	23.55	14.50	18.00
Series 4	EXE.PR.D	241,240	21.00	21.00	21.00
Class II Preferred					
Series 1	EXE.PR.E	382,979	16.06	17.00	15.00

<sup>(1)</sup> Outstanding as at December 31, 2001

### Quarterly Price Ranges of Subordinate Voting Shares (EXE.A) on the TSE

	1st	2nd	3rd	4th
2001: High	\$4.45	\$6.85	\$8.25	\$7.58
Low	3.25	4.13	5.55	4.87
2000: High	4.59	2.75	3.80	3.40
Low	1.68	1.45	1.65	2.05

### Trading Price of Subordinate Voting Shares (EXE.A) on the TSE



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