

**ADCARE HEALTH SYSTEMS, INC. AND SUBSIDIARIES**  
**CONSOLIDATED BALANCE SHEET**

	September 30, 2009 (Unaudited)	December 31, 2008
<u>ASSETS</u>		
Current Assets:		
Cash	\$ 2,031,370	\$ 1,266,315
Accounts receivable:		
Long-term care resident receivables, net	2,019,183	2,008,847
Management, consulting and development receivables, net	114,433	258,811
Advances and receivables from affiliates	37,638	17,635
Prepaid expenses and other	434,965	478,534
Total current assets	4,637,589	4,030,142
Restricted cash	1,107,646	1,155,596
Property and equipment, net	16,447,215	16,772,660
License, net	1,189,307	1,189,307
Goodwill	2,679,482	2,679,482
Other assets	916,687	1,012,340
Total assets	\$ 26,977,926	\$ 26,839,527
<u>LIABILITIES AND STOCKHOLDERS' EQUITY</u>		
Current Liabilities:		
Current portion of notes payable and other debt	\$ 663,078	\$ 713,323
Current portion of notes payable to stockholder	9,432	9,432
Accounts payable	722,606	1,009,002
Accrued expenses	2,863,475	2,838,407
Total current liabilities	4,258,591	4,570,164
Notes payable and other debt, net of current portion	16,498,924	16,974,788
Notes payable to stockholder, net of current portion	28,748	34,626
Other liabilities	570,690	299,314
Income tax payable	201,932	170,007
Total liabilities	21,558,885	22,048,899
Stockholders' equity:		
Preferred stock, no par value; 500,000 shares authorized; no shares issued or outstanding	-	-
Common stock and additional paid-in capital, no par value; 14,500,000 shares authorized; 3,786,129 shares issued and outstanding	14,933,652	14,766,967
Accumulated deficit	(9,802,600)	(10,245,532)
Total stockholders' equity	5,131,052	4,521,435
Noncontrolling interest in subsidiaries	287,989	269,193
Total equity	5,419,041	4,790,628
Total liabilities and stockholders' equity	\$ 26,977,926	\$ 26,839,527

See notes to consolidated financial statements

**ADCARE HEALTH SYSTEMS, INC. AND SUBSIDIARIES**  
**CONSOLIDATED STATEMENTS OF OPERATIONS**  
(Unaudited)

	Three-Months Ended September 30,		Nine-Months Ended September 30,	
	2009	2008	2009	2008
Revenues:				
Patient care revenues	\$ 6,434,186	\$ 5,731,938	\$18,513,767	\$16,874,113
Management, consulting and development fee revenue	475,313	453,822	1,393,748	1,320,725
Total revenue	<u>6,909,499</u>	<u>6,185,760</u>	<u>19,907,515</u>	<u>18,194,838</u>
Expenses:				
Payroll and related payroll costs	3,929,280	4,162,908	11,376,737	11,447,782
Other operating expenses	2,250,032	2,086,919	6,418,118	6,223,303
Depreciation and amortization	231,773	222,500	682,959	655,519
Total expenses	<u>6,411,085</u>	<u>6,472,327</u>	<u>18,477,814</u>	<u>18,326,604</u>
Income (Loss) from Operations	<u>498,414</u>	<u>(286,567)</u>	<u>1,429,701</u>	<u>(131,766)</u>
Other Income (Expense):				
Interest income	520	6,381	2,926	20,609
Interest expense, others	(292,364)	(352,931)	(886,311)	(972,641)
Interest expense, related parties	(489)	(14,598)	(1,717)	(43,044)
Other expense	(1,622)	-	(50,946)	-
	<u>(293,955)</u>	<u>(361,148)</u>	<u>(936,048)</u>	<u>(995,076)</u>
Gain on Acquisition	<u>-</u>	<u>-</u>	<u>-</u>	<u>413,954</u>
Income (Loss) Before Income Taxes	204,459	(647,715)	493,653	(712,888)
Income Tax Expense	(10,641)	(10,641)	(31,925)	(31,925)
Net Income (Loss)	<u>193,818</u>	<u>(658,356)</u>	<u>461,728</u>	<u>(744,813)</u>
Net (Income) Loss Attributable to Noncontrolling Interests	6,199	(6,093)	(18,796)	(35,782)
Net Income (Loss) Attributable to AdCare Health Systems	<u>\$ 200,017</u>	<u>\$ (664,449)</u>	<u>\$ 442,932</u>	<u>\$ (780,595)</u>
Net Income (Loss) Per Share, Basic:	<u>\$ 0.05</u>	<u>\$ (0.18)</u>	<u>\$ 0.12</u>	<u>\$ (0.21)</u>
Net Income (Loss) Per Share, Diluted:	<u>\$ 0.05</u>	<u>\$ (0.18)</u>	<u>\$ 0.12</u>	<u>\$ (0.21)</u>
Weighted Average Common Shares Outstanding,				
Basic	<u>3,786,129</u>	<u>3,786,129</u>	<u>3,786,129</u>	<u>3,786,129</u>
Diluted	<u>3,998,789</u>	<u>3,786,129</u>	<u>3,998,789</u>	<u>3,786,129</u>

See notes to consolidated financial statements.

**ADCARE HEALTH SYSTEMS, INC. AND SUBSIDIARIES**  
**CONSOLIDATED STATEMENTS OF CASH FLOWS**  
(Unaudited)

	Nine-Months Ended September 30, 2009	2008
Cash flows from operating activities:		
Net income (loss) inclusive of noncontrolling interest	\$ 461,728	\$ (744,813)
Adjustments to reconcile net income (loss) to net cash provided by operating activities:		
Depreciation and amortization	682,959	655,519
Warrants issued for services	40,486	75,462
Stock option compensation expense	120,776	243,948
Note receivable forgiveness exchanged for rent	-	9,000
Gain on acquisition	-	(413,954)
Changes in certain assets and liabilities:		
Accounts receivable	114,039	321,298
Prepaid expenses and other	3,830	(24,680)
Other assets	95,653	(121,132)
Accounts payable and accrued expenses	(261,328)	208,151
Income tax liability	31,925	31,925
Other liabilities	271,377	(88,317)
Net cash provided by operating activities	1,561,445	152,407
Cash flows from investing activities:		
Distribution to noncontrolling interest	-	(50,000)
Proceeds from the sale of assets, net of associated costs	892	2,500
Increase in restricted cash	47,950	77,639
Restricted cash received upon acquisition of assets	-	19,813
Assets transferred to noncontrolling interest upon acquisition	-	(6,651)
Purchase of property plant and equipment	(343,245)	(286,689)
Net cash used in investing activities	(294,403)	(243,388)
Cash flows from financing activities:		
Proceeds from notes payable	-	2,287,127
Stock issuance	30,000	-
Repayment of notes payable to stockholder	(5,878)	(760,000)
Prepaid financing costs	-	159,130
Repayment of notes payable	(526,109)	(560,587)
Net cash (used in) provided by financing activities	(501,987)	1,125,670
Net Increase in Cash	765,055	1,034,689
Cash, Beginning	1,266,315	926,625
Cash, Ending	\$ 2,031,370	\$ 1,961,314
Supplemental Disclosure of Cash Flow Information:		
Cash paid during the year for interest	\$ 876,987	\$ 855,030
Supplemental Disclosure of Non-Cash Activities:		
Rent in exchange of note receivable repayment	\$ -	\$ 9,000
Acquisition of assets in exchange for note forgiveness	\$ -	\$ 2,740,584

See notes to consolidated financial statements.