CC – Palo Alto, Inc.

Form 7-1 Explanation for Increase in Monthly Service Fees

Each monthly service fee increase is based on projected expenses, prior year expenses and economic indicators. As with most businesses, we are faced with rising costs in several areas. One significant area is rising salaries and benefits costs. Pressure in the labor markets and rising health care costs (coupled with the impact of federal regulation) continue to lead to rising salaries and benefits costs which outpace normal inflation. Additionally, property, workers compensation, and professional liability insurance costs continue to rise. Food cost, utilities expense, and property taxes are other significant considerations within the overall expense base that drive monthly service fee increases. Each of these factors is evaluated in detail and we utilize the best information we have available at the time the increases are finalized. The data used to calculate the increase consists primarily of compensation analyses on the local market, health insurance consultant reports, forward looking data on commodities pricing, discussions with utility companies, and discussion with non-health insurance consultants. We also analyze repair and maintenance needs annually based on the life cycle of our systems and specific needs. To maintain the high level of quality and services expected of our brand, the following increases were implemented:

IL	4.5%
AL	4.5%
SNF	4.5%