

HESKA CORP
Form 10-K
March 25, 2015

UNITED STATES

SECURITIES AND EXCHANGE
COMMISSION

Washington, D.C. 20549

FORM 10-K

(Mark One)

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

For the fiscal year ended
December 31, 2014

OR

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

For the transition period
from _____ to

Commission file number: 0-22427

HESKA CORPORATION

(Exact name of registrant as specified in
its charter)

Delaware 77-0192527
(State or other
jurisdiction of
incorporation or
organization) (I.R.S. Employer
Identification
Number)

3760 Rocky Mountain
Avenue 80538

Loveland, Colorado
(Address of principal
executive offices) (Zip Code)

Registrant's telephone number, including
area code: (970) 493-7272

Securities registered
pursuant to Section 12(b)

of the Act: The Nasdaq
Stock Market

Public Common Stock, LLC
\$.01 par value

(Title of Class) (Name of Each
Exchange on
Which
Registered)

Securities registered
pursuant to Section 12(g)
of the Act: None

Indicate by check mark if the registrant is
a well-known seasoned issuer, as defined
in Rule 405 of the Securities Act.

Yes No

Indicate by check mark if the registrant is
not required to file reports pursuant to
Section 13 or 15(d) of the Act.

Yes No

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

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

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

Indicate by check mark whether the
registrant is a large accelerated filer, an
accelerated filer, a non-accelerated filer or
a smaller reporting company. See the

definitions of "large accelerated filer,"
"accelerated filer" and "smaller reporting
company" in Rule 12b-2 of the Exchange
Act.

Large accelerated filer

Accelerated filer

Non-accelerated filer (Do not check if a small reporting company) Smaller Reporting Company

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Act).

Yes No

The aggregate market value of voting common stock held by non-affiliates of the Registrant was approximately \$58,865,366 as of June 30, 2014 based upon the closing price on the Nasdaq Capital Market reported for such date. This calculation does not reflect a determination that certain persons are affiliates of the Registrant for any other purpose.

6,482,753 shares of the Registrant's Public Common Stock, \$.01 par value, were outstanding at March 24, 2015.

DOCUMENTS INCORPORATED BY REFERENCE

Items 10, 11, 12, 13 and 14 of Part III incorporate by reference information from the Registrant's Proxy Statement to be filed with the Securities and Exchange Commission in connection with the solicitation of proxies for the Registrant's 2014 Annual Meeting of Stockholders.

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HESKA, ALLERCEPT, HEMATRUE, SOLO STEP, THYROMED, VET/OX and VITALPATH are registered trademarks of Heska Corporation. TRI-HEART is a registered trademark of Intervet Inc., d/b/a Merck Animal Health, formerly known as Schering-Plough Animal Health Corporation ("Merck Animal Health"), which is a unit of Merck & Co., Inc., in the United States and is a registered trademark of Heska Corporation in other countries. DRI-CHEM is a registered trademark of FUJIFILM Corporation. This Form 10-K also refers to trademarks and trade names of other organizations.

Statement Regarding Forward Looking Statements

This Form 10-K contains forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended (the "Exchange Act"). For this purpose, any statements contained herein that are not statements of current or historical fact may be deemed to be forward-looking statements. Without limiting the foregoing, words such as "anticipates," "expects," "intends," "plans," "believes," "seeks," "estimates," variations of such words and similar expressions are intended to identify such forward-looking statements. These statements are not guarantees of future performance and are subject to certain risks, uncertainties and assumptions that are difficult to predict. Therefore, actual results could differ materially from those expressed or forecasted in any such forward-looking statements as a result of certain factors, including those set forth in "Risk Factors," "Management's Discussion and Analysis of Financial Condition and Results of Operations," "Business" and elsewhere in this Form 10-K. Readers are cautioned not to place undue reliance on these forward-looking statements.

Although we believe that expectations reflected in the forward-looking statements are reasonable, we cannot guarantee future results, levels of activity, performance or achievements. We expressly disclaim any obligation or undertaking to release publicly any updates or revisions to any forward-looking statements contained herein to reflect any change in our expectations with regard thereto or any change in events, conditions or circumstances on which any such statement is based. These forward-looking statements apply only as of the date of this Form 10-K or for statements incorporated by reference from our 2015 definitive proxy statement on Schedule 14A, as of the date of the Schedule 14A.

Internet Site

Our Internet address is www.heska.com. Because we believe it provides useful information in a cost-effective manner to interested investors, via a link on our website our annual report on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K, and amendments to those reports filed or furnished pursuant to Section 13(a) or 15(d) of the Exchange Act are publicly available free of charge and we believe are available as soon as reasonably practical after we electronically file such material with, or furnish it to, the Securities Exchange Commission (the "SEC"). Information contained on our website is not a part of this annual report on Form 10-K.

PART I

Item 1. Business.

We develop, manufacture, market, sell and support veterinary products. Our core focus is on the canine and feline companion animal health markets where we strive to provide high value products.

Our business is composed of two reportable segments, Core Companion Animal Health and Other Vaccines, Pharmaceuticals and Products. The Core Companion Animal Health segment ("CCA") includes, primarily for canine and feline use, blood testing instruments and supplies, digital imaging products, software and services, and single use products and services such as heartworm diagnostic tests, heartworm preventive products, allergy immunotherapy products and allergy testing. These products are sold directly to veterinarians by us as well as through distribution relationships. The Other Vaccines, Pharmaceuticals and Products segment ("OVP") includes private label vaccine and pharmaceutical production, primarily for cattle but also for other animals including small mammals. All OVP products are sold by third parties under third party labels. Please refer to Note 10 of our audited consolidated financial statements filed herewith for financial information about each of our segments.

Our principal executive offices are located at 3760 Rocky Mountain Avenue, Loveland, Colorado 80538, our telephone number is (970) 493-7272 and our internet address is www.heska.com. We originally incorporated in California in 1988, and we subsequently incorporated in Delaware in 1997.

Background

We were founded as Paravax, Inc. in 1988 and conducted research on vaccines to prevent infections by parasites. We changed our name to Heska Corporation in 1995, completed our initial public offering in 1997 and continued to be a research and development-focused company, devoting substantial resources to the research and development of innovative products for the companion animal health market. In 2001 and 2002, we took steps to lower our expense base, largely in internal research and development. We subsequently continued to concentrate our efforts on operating improvements, such as enhancing the effectiveness of our sales and marketing efforts and pursuing cost efficiencies, as well as seeking new product opportunities with third parties. We acquired a 54.6% interest in Cuattro Veterinary USA, LLC in February 2013 (the "Acquisition"), which marked our entry into the veterinary imaging market. In June 2013, we sold certain non-core assets useful for the production of both bovine and feline vaccines to Elanco Animal Health ("Elanco"), a division of Eli Lilly and Company.

Core Companion Animal Health Segment

We presently sell a variety of companion animal health products and services, among the most significant of which are the following:

Veterinary Blood Testing and Other Non-Imaging Instruments

We offer a line of veterinary blood testing and other instruments, some of which are described below. We also market and sell consumable supplies for these instruments. Our line of veterinary instruments includes the following:

Blood Chemistry. The Element DC_v Veterinary Chemistry Analyzer (the "Element DC") is an easy-to-use, robust system that uses dry slide technology for blood chemistry and electrolyte analysis and has the ability to run 22 tests at a time with a single blood sample. Test slides are available as both pre-packaged panels as well as individual slides. The Element DC is faster and has an enhanced user interface compared to the instrument it replaced, the DRI-CHEM 4000 Veterinary Chemistry Analyzer (the "DRI-CHEM 4000"). The DRI-CHEM 7000 Veterinary Chemistry Analyzer (the "DRI-CHEM 7000") is a complementary chemistry offering, co-branded with FUJIFILM Corporation ("FUJIFILM"), with higher throughput, multiple patient staging and a "STAT" feature which provides emergency sample flexibility in critical cases. The Element DC, DRI-CHEM 7000 and DRI-CHEM 4000 all utilize the same test slides. We are supplied with the Element DC, the DRI-CHEM 7000 and affiliated test slides and supplies under a contractual agreement with FUJIFILM.

Hematology. The Element HT₅ Hematology Analyzer (the "HT5") is a true 5-part hematology analyzer which uses laser, impedance and colorimetric technologies to measure key parameters such as white blood cell count, red blood cell count, platelet count and hemoglobin levels in animals. The HT5 can generate results in less than a minute with 15 µL of sample. We began to ship HT5 units in January 2015. We are supplied with the HT5 and affiliated reagents and supplies under a contractual agreement with Shenzhen Mindray Bio-Medical Electronics Co., Ltd. ("Mindray"). The HEMATTRUE Veterinary Hematology Analyzer (the "HEMATTRUE") is an easy-to-use and reliable 3-part hematology blood analyzer that we continue to offer to our customers. In addition, we continue to service and support a previous hematology instrument, the HESKA CBC-DIFF Veterinary Hematology System (the "CBC"). We are supplied new

HEMATRUE instruments and affiliated reagents and supplies for the HEMATRUE and the CBC under a contractual agreement with Boule Medical AB ("Boule").

Blood Gases and Electrolytes. The Element POC™ Blood Gas & Electrolyte Analyzer ("EPOC") is a handheld, wireless analyzer which delivers rapid blood gas, electrolyte, metabolite, and basic blood chemistry testing. EPOC features test cards with room temperature storage which can offer results with less than 100 µL of sample as well as WiFi and Bluetooth connectivity. We began to ship EPOC units to customers in October 2013. EPOC and affiliated consumables and supplies are supplied to us under a contractual agreement with Alere North America, LLC, a unit of Alere Inc.

IV Pumps. The VET/IV 2.2 infusion pump is a compact, affordable IV pump that allows veterinarians to easily provide regulated infusion of fluids, drugs or nutritional products for their patients.

Veterinary Imaging Instruments and Services

On February 24, 2013, we acquired a 54.6% interest in Cuattro Veterinary USA, LLC, which was subsequently renamed Heska Imaging US, LLC ("Heska Imaging") and operates only in the United States. This transaction marked our entry into the veterinary imaging market. Heska Imaging's offerings in this area include:

Digital Radiography Solutions. Our digital radiography solutions are marketed and sold under the "Cuattro" brand name. We sell hardware including digital radiography detectors, acquisition workstation equipment, positioning aides such as tunnels and tables, viewing computers and other accessories along with embedded software and support, data hosting and other services. The CloudDR™ solution combines flat panel digital radiography with web-based image storage. The Cloudbank™ archive is an automatic, secure, web-based image storage solution designed to interface with the software we sell. ViewCloud™ is a PACS (Picture Archival and Communications System) for Cloudbank for web or local viewing, reporting, planning and email sharing of studies on internet devices, including personal computers, Mac desktop and portable systems, tablet devices, iPad™ devices and smartphones. SupportCloud™ is a support package including call center voice and remote diagnostics, recovery and other services, such as the provision of warranty-related loaner units, to support CloudDR, Cloudbank and ViewCloud.

We also sell mobile digital radiography products, primarily for equine use. The Uno 4™ is a full powered, seamlessly integrated, portable digital radiography generator with an embedded detector and touchscreen computer based upon a patented design of Cuattro, LLC. The Slate 5™ series features an Automatic Exposure Detection technology detector for use with an existing generator and which communicates wirelessly with a mobile, case-based direct sunlight readable display, including multi-touch software and the ability to natively link to Digital Imaging and Communication in Medicine, or DICOM, servers of all types as well as Cloudbank. Slate 5™ comes in a 20" model and a 12" model, both of which are handheld, touchscreen tablets with embedded wireless communication, battery-powered and line-powered capabilities, and image acquisition and communication functions.

Cuattro, LLC provides us with the hardware, software and support, data hosting and other services for our digital radiography solutions under exclusive contractual arrangements in the United States.

Ultrasound Systems. Our ultrasound products, including affiliated probes and peripherals, are provided to us under an exclusive agreement with Esaote USA ("Esaote"). We sell several different ultrasound products with varying features and corresponding price points, all under Esaote's trade names or logos. These offerings include the MyLab family of high performance systems and probes, for use in abdominal, cardiac and small parts applications in companion animal and equine patients as well as other species. The ultrasound products we sell generally seamlessly integrate with our Cloudbank and ViewCloud offerings discussed above for image storing and viewing.

Point-of-Care Heartworm Diagnostic Tests

Heartworm infections of dogs and cats are caused by the parasite *Dirofilaria immitis*. This parasitic worm is transmitted in larval form to dogs and cats through the bite of an infected mosquito. Larvae develop into adult worms that live in the pulmonary arteries and heart of the host, where they can cause serious cardiovascular, pulmonary, liver and kidney disease. Our canine and feline heartworm diagnostic tests use monoclonal antibodies or a recombinant heartworm antigen, respectively, to detect heartworm antigens or antibodies circulating in the blood of an infected animal.

We currently market and sell heartworm diagnostic tests for both dogs and cats. SOLO STEP CH for dogs and SOLO STEP FH for cats are available in point-of-care, single use formats that can be used by veterinarians on site. We also offer SOLO STEP CH Batch Test Strips, a rapid and simple point-of-care antigen detection test for dogs that allows veterinarians in larger practices to run multiple samples at the same time. We obtain SOLO STEP CH, SOLO STEP FH and SOLO STEP Batch Test Strips under a contractual agreement with Quidel Corporation ("Quidel").

Heartworm Preventive Products

We have an agreement with Merck Animal Health, a unit of Merck & Co., Inc., granting Merck Animal Health the exclusive distribution and marketing rights for our canine heartworm prevention product, TRI-HEART Plus Chewable Tablets, ultimately sold to or through veterinarians in the United States and Canada. TRI-HEART Plus Chewable Tablets (ivermectin/pyrantel) are indicated for use as a monthly preventive treatment of canine heartworm infection and for treatment and control of ascarid and hookworm infections. We manufacture TRI-HEART Plus Chewable Tablets at our Des Moines, Iowa production facility.

Allergy Products and Services

Allergy is common in companion animals, and it has been estimated to affect approximately 10% to 15% of dogs. Clinical symptoms of allergy are variable, but are often manifested as persistent and serious skin disease in dogs and cats. Clinical management of allergic disease is problematic, as there are a large number of allergens that may give rise to these conditions. Although skin testing is often regarded as the most accurate diagnostic procedure, such tests can be painful, subjective and inconvenient. The effectiveness of the immunotherapy that is prescribed to treat allergic disease is inherently limited by inaccuracies in the diagnostic process.

Our ALLERCEPT Definitive Allergen Panels provide the most accurate determination of which we are aware of the specific allergens to which an animal, such as a dog, cat or horse, is reacting. The panels use a highly specific recombinant version of the natural IgE receptor to test the serum of potentially allergic animals for IgE directed against a panel of known allergens. A typical test panel consists primarily of various pollen, grass, mold, insect and mite allergens. The test results serve as the basis for prescription ALLERCEPT Therapy Shots and ALLERCEPT Therapy Drops. We operate veterinary laboratories in Loveland, Colorado and Fribourg, Switzerland which both offer blood testing using our ALLERCEPT Definitive Allergen Panels.

We sell kits to conduct blood testing using our ALLERCEPT Definitive Allergen Panels to third-party veterinary diagnostic laboratories outside of the United States. We also sell products to screen for the presence of allergen-specific IgE to these customers – we sell kits to conduct preliminary blood testing using products based on our ALLERCEPT Definitive Allergen Panels as well as a similar test requiring less technical sophistication, our E-SCREEN Test. Animals testing positive for allergen-specific IgE using these screening tests are candidates for further evaluation using our ALLERCEPT Definitive Allergen Panels.

Veterinarians who use our ALLERCEPT Definitive Allergen Panels often purchase our ALLERCEPT Therapy Shots or ALLERCEPT Therapy Drops for those animals with positive test results. These prescription immunotherapy treatment sets are formulated specifically for each allergic animal and contain only the allergens to which the animal has significant levels of IgE antibodies. The prescription formulations are administered in a series of injections, with doses increasing over several months, to ameliorate the allergic condition of the animal. Immunotherapy is generally continued for an extended time. Immunotherapy delivered by injection is referred to as subcutaneous immunotherapy. We offer canine, feline and equine subcutaneous immunotherapy treatment products. We have licensed intellectual property for a proprietary, sublingual (administered under the tongue) therapy treatment for pets suffering with allergies – now known as ALLERCEPT Therapy Drops. We believe our ALLERCEPT Therapy Drops offer a convenient alternative to subcutaneous injection, thereby enhancing the likelihood of pet owner compliance.

Other Core Companion Animal Health Single Use Products. We also sell other products in our Core Companion Animal Health segment. For example, we sell E.R.D. Reagent Packs used to detect microalbuminuria, the most sensitive indicator of renal damage, to VCA Antech, Inc. for use in its veterinary diagnostic laboratories.

Other Vaccines, Pharmaceuticals and Products Segment

We developed a line of bovine vaccines that are licensed by the United States Department of Agriculture ("USDA"). Historically, the largest distributor of these vaccines was Agri Laboratories, Ltd. ("AgriLabs"), who sold these vaccines primarily under the Titanium[®] and MasterGuard[®] brands. In November 2013, AgriLabs assigned the long-term agreement with us related to these vaccines to, and the agreement was assumed by, Eli Lilly and Company ("Eli Lilly") acting through Elanco.

We manufacture biological and pharmaceutical products for a number of other animal health companies. We manufacture products for animals other than cattle including horses and small mammals. Our offerings range from providing complete turnkey services which include research, licensing, production, labeling and packaging of products to providing any one of these services as needed by our customers as well as validation support and distribution services.

Marketing, Sales and Customer Support

We estimate that there are approximately 53,000 veterinarians in the United States whose practices are devoted principally to small animal medicine. These veterinarians practice in approximately 24,000 clinics in the United States. In 2014, our products were sold to approximately 13,000 such clinics in the United States. Veterinarians may obtain our products directly from us or indirectly through others. All our Core Companion Animal Health products ultimately are sold primarily to or through veterinarians. In many cases, veterinarians will markup their costs to the end user. The acceptance of our products by veterinarians is critical to our success.

We currently market our Core Companion Animal Health products in the United States to veterinarians through an outside field organization, a telephone sales force, independent third-party distributors, as well as through trade shows and print advertising and through other distribution relationships,

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such as Merck Animal Health in the case of our heartworm preventive. Our outside field organization currently consists of 36 individuals in various parts of the United States. Our inside sales force consists of 18 persons currently.

We have a staff dedicated to customer and product support in our Core Companion Animal Health segment including veterinarians, technical support specialists and service technicians. Individuals from our product development group may also be used as a resource in responding to certain product inquiries.

Internationally, we market our Core Companion Animal Health products to veterinarians primarily through third-party veterinary diagnostic laboratories, independent third-party distributors and Novartis Agro K.K., Tokyo ("Novartis Japan"). These entities typically provide customer support. Novartis Japan exclusively markets and distributes SOLO STEP CH in Japan.

All OVP products are marketed and sold by third parties under third-party labels.

We grant third parties rights to our intellectual property as well as our products, with our compensation often taking the form of royalties and/or milestone payments.

Manufacturing

The majority of our revenue is from proprietary products manufactured by third parties. Third parties manufacture our veterinary instruments, including affiliated consumables and supplies, as well as other products including key components of our heartworm point-of-care diagnostic tests. Our chemistry instruments and affiliated supplies are manufactured under contract with FUJIFILM. Our hematology instruments and affiliated supplies are manufactured under contracts with Mindray and Boule. Our blood gas and electrolyte analyzers and affiliated supplies are supplied under a contract with Alere North America, LLC. Our digital radiography products are supplied under contract with Cuattro, LLC, which typically buys its hardware products and components from third parties. Our ultrasound products are supplied under a contract with Esaote USA. Key components of our heartworm point-of-care diagnostic tests are manufactured under a contract with Quidel. We manufacture and supply Quidel with certain critical raw materials and perform the final packaging operations for these products. Our facility in Des Moines, Iowa is a USDA, Food and Drug Administration ("FDA"), and Drug Enforcement Agency ("DEA") licensed biological and pharmaceutical manufacturing facility. This facility currently has the capacity to manufacture more than 50 million doses of vaccine each year. We expect that we will, for the foreseeable future, manufacture most or all of our pharmaceutical and biological products at this facility, as well as most or all of our recombinant proteins and other proprietary reagents for our diagnostic tests. We currently manufacture our canine heartworm prevention product, our allergy treatment products and all our OVP segment products at this facility. Our OVP segment's customers purchase products in both finished and bulk format, and we perform all phases of manufacturing, including growth of the active bacterial and viral agents, sterile filling, lyophilization and packaging at this facility. We manufacture our various allergy products at our Des Moines facility, our Loveland facility and our Fribourg facility. We believe the raw materials for products we manufacture are available from more than one source.

Product Development

We are committed to providing innovative products to address health needs of companion animals. We may obtain such products from external sources, external collaboration or internal research and development.

We are committed to identifying external product opportunities and creating business and technical collaborations that lead to high value veterinary products. We believe that our active participation in scientific networks and our reputation for investing in research enhances our ability to acquire external

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product opportunities. We have collaborated, and intend to continue to do so, with a number of companies and universities. Examples of such collaborations include:

- Quidel for the development of SOLO STEP CH Cassettes, SOLO STEP CH Batch Test Strips and SOLO STEP FH Cassettes;
- Boule for the development of veterinary applications for the HEMATRUE Veterinary Hematology Analyzer and associated reagents; and
- FUJIFILM for the development of veterinary applications for the Element DC Veterinary Chemistry Analyzer and associated slides and supplies.

Internal research and development is managed on a case-by-case basis. We employ individuals with microbiology, immunology, genetics, biochemistry, molecular biology, parasitology as well as veterinary expertise and will form multidisciplinary product-associated teams as appropriate. We incurred expenses of \$1.0 million, \$1.5 million and \$1.4 million in the years ended December 31, 2012, 2013 and 2014, respectively, in support of our research and development activities.

Intellectual Property

We believe that patents, trademarks, copyrights and other proprietary rights are important to our business. We also rely upon trade secrets, know-how, continuing technological innovations and licensing opportunities to develop and maintain our competitive position. The proprietary technologies of our OVP segment are primarily protected through trade secret protection of, for example, our manufacturing processes in this area.

We actively seek patent protection both in the United States and abroad. Our issued and pending patent portfolios primarily relate to heartworm control, flea control, allergy, infectious disease vaccines, diagnostic and detection tests, immunomodulators, instrumentation, nutrition, pain control and vaccine delivery technologies. As of December 31, 2014, we owned, co-owned or had rights to 162 issued U.S. patents expiring at various dates from January 2015 to May 2028 and had no pending U.S. patent applications. Our corresponding foreign patent portfolio as of December 31, 2014 included 139 issued patents and 1 pending application in various foreign countries expiring at various dates from October 2015 to March 2026.

We also have obtained exclusive and non-exclusive licenses for numerous other patents held by academic institutions and for profit companies.

Seasonality

In 2013 and 2014, our fourth quarter results were significantly stronger than those for any other quarter. We expect this trend to continue in the future, primarily as this is our understanding of the historical results at Heska Imaging and other digital imaging businesses.

Government Regulation

Although the majority of our revenue is from the sale of unregulated items, many of our products or products that we may develop are, or may be, subject to extensive regulation by governmental authorities in the United States, including the USDA and the FDA, and by similar agencies in other countries. These regulations govern, among other things, the development, testing, manufacturing, labeling, storage, pre-market approval, advertising, promotion, sale and distribution of our products. Satisfaction of these requirements can take several years to achieve and the time needed to satisfy them may vary substantially,

based on the type, complexity and novelty of the product. Any product that we develop must receive all relevant regulatory approval or clearances, if required, before it may be marketed in a particular country. The following summarizes the major U.S. government agencies that regulate animal health products:

USDA. Vaccines and certain single use, point-of-care diagnostics are considered veterinary biologics and are therefore regulated by the Center for Veterinary Biologics, or CVB, of the USDA. Industry data indicate that it takes approximately four years and in excess of \$1.0 million to license a conventional vaccine for animals from basic research through licensing. In contrast to vaccines, single use, point-of-care diagnostics can typically be licensed by the USDA in about two years, at considerably less cost. However, vaccines or diagnostics that use innovative materials, such as those resulting from recombinant DNA technology, usually require additional time to license. The USDA licensing process involves the submission of several data packages. These packages include information on how the product will be manufactured, information on the efficacy and safety of the product in laboratory and target animal studies and information on performance of the product in field conditions.

FDA. Pharmaceutical products, which typically include synthetic compounds, are approved and monitored by the Center for Veterinary Medicine of the FDA. Under the Federal Food, Drug and Cosmetic Act, the same statutory standard for FDA approval applies to both human and animal drugs: demonstrated safety, efficacy and compliance with FDA manufacturing standards. However, unlike human drugs, neither preclinical studies nor a sequential phase system of studies are required. Rather, for animal drugs, studies for safety and efficacy may be conducted immediately in the species for which the drug is intended. Thus, there is no required phased evaluation of drug performance, and the Center for Veterinary Medicine will review data at appropriate times in the drug development process. The process can be costly and time consuming, requiring up to \$100 million and seven to ten years to sell an animal drug in the market. In addition, the time and cost for developing companion animal drugs may be significantly less than for drugs for livestock animals, which generally have enhanced standards designed to ensure safety in the food chain.

EPA. Products that are applied topically to animals or to premises to control external parasites are regulated by the Environmental Protection Agency, or EPA.

After we have received regulatory licensing or approval for our products, numerous regulatory requirements typically apply. Among the conditions for certain regulatory approvals is the requirement that our manufacturing facilities or those of our third-party manufacturers conform to current Good Manufacturing Practices or other manufacturing regulations, which include requirements relating to quality control and quality assurance as well as maintenance of records and documentation. The USDA, FDA and foreign regulatory authorities strictly enforce manufacturing regulatory requirements through periodic inspections and/or reports.

A number of our animal health products are not regulated. For example, certain products such as our ALLERCEPT panels are not regulated by either the USDA or FDA. Similarly, none of our veterinary instruments requires regulatory approval to be marketed and sold in the United States.

We have pursued regulatory approval outside the United States based on market demographics of foreign countries. For marketing outside the United States, we are subject to foreign regulatory requirements governing regulatory licensing and approval for many of our products. Licensing and approval by comparable regulatory authorities of foreign countries must be obtained before we can market products in those countries. Product licensing approval processes and requirements vary from country to country and the time required for such approvals may differ substantially from that required in the United States. We cannot be certain that approval of any of our products in one country will result in approvals in any other country.

To date, we or our distributors have sought regulatory approval for certain of our products in Canada, which is governed by the Canadian Center for Veterinary Biologics, or CCVB; in Japan, which is governed by the Japanese Ministry of Agriculture, Forestry and Fisheries, or MAFF; in Australia, which is governed by the Australian Department of Agriculture, Fisheries and Forestry, or ADAFF; in South Africa, which is governed by the Republic of South Africa Department of Agriculture, or RSADA; and in certain other countries requiring such approval.

Core Companion Animal Health products previously discussed which have received regulatory approval in the United States and/or elsewhere are summarized below.

Products	Country	Regulated	Agency Status
ALLERCEPT Allergy Treatment Sets	United States	Yes	USDA Licensed
	United States	Yes	USDA Licensed
	EU	No-in most countries	
SOLO STEP CH	Canada	Yes	CCVB Licensed
	Japan	Yes	MAFF Licensed
	Australia United States	Yes Yes	ADAFF Licensed USDA Licensed
SOLO STEP CH Batch Test Strips	Canada	Yes	CCVB Licensed
	United States	Yes	USDA Licensed
SOLO STEP FH	Canada	Yes	CCVB Licensed
	Australia	Yes	ADAFF Licensed
	United States	Yes	FDA Licensed
TRI-HEART Plus Heartworm Preventive	Japan	Yes	MAFF Licensed
	South Korea	Yes	NVRQSLicensed

Competition

Our market is intensely competitive. Our competitors include independent animal health companies and major pharmaceutical companies that have animal health divisions. We also compete with independent, third-party distributors, including distributors who sell products under their own private labels. In the point-of-care diagnostic testing market, our major competitors include IDEXX Laboratories, Inc. ("IDEXX"), Abaxis, Inc. ("Abaxis") and Synbiotics Corporation ("Synbiotics"), a unit of Zoetis Inc. ("Zoetis"). The products manufactured by our OVP segment for sale by third parties compete with similar products offered by a number of other companies, some of which have substantially greater financial, technical, research and other resources than us and may have more established marketing, sales, distribution and service organizations than our OVP segment's customers. Companies with a significant presence in the animal health market such as Bayer AG, CEVA Sante Animale, Eli Lilly, Merck & Co., Inc. ("Merck"), sanofi-aventis, Ve toquinol S.A., Virbac S.A. and Zoetis may be marketing or developing products that compete with our products or would compete with them if successfully developed. These and other

competitors and potential competitors may have substantially greater financial, technical, research and other resources and larger, more established marketing, sales, distribution and service organizations than we do. Our competitors may offer broader product lines and have greater name recognition than we do.

Environmental Regulation

In connection with our product development activities and manufacturing of our biological, pharmaceutical and diagnostic and detection products, we are subject to federal, state and local laws, rules, regulations and policies governing the use, generation, manufacture, storage, handling and disposal of certain materials, biological specimens and wastes. Although we believe that we have complied with these laws, regulations and policies in all material respects and have not been required to take any significant action to correct any noncompliance, we may be required to incur significant costs to comply with environmental and health and safety regulations in the future. Although we believe that our safety procedures for handling and

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disposing of such materials comply with the standards prescribed by state and federal regulations, the risk of accidental contamination or injury from these materials cannot be eliminated. In the event of such an accident, we could be held liable for any damages that result and any such liability could exceed our resources.

Employees

As of December 31, 2014, we and our subsidiaries employed 301 people, of whom 128 were focused in production and technical and logistical services, including instrumentation service, 116 in sales, marketing and customer support, 51 in general and administrative services, such as finance, and 6 in product development. We believe that our ability to attract and retain skilled personnel is critical to our success. None of our employees is covered by a collective bargaining agreement, and we believe our employee relations are good.

Where You Can Find Additional Information

You may review a copy of this annual report on Form 10-K, including exhibits and any schedule filed therewith, and obtain copies of such materials at prescribed rates, at the Securities and Exchange Commission's Public Reference Room in Room 1580, 100 F Street, NE, Washington, D.C. 20549-0102. You may obtain information on the operation of the Public Reference Room by calling the Securities and Exchange Commission at 1-800-SEC-0330. The Securities and Exchange Commission maintains a website (<http://www.sec.gov>) that contains reports, proxy and information statements and other information regarding registrants, such as Heska Corporation, that file electronically with the Securities and Exchange Commission.

Executive Officers of the Registrant

Our executive officers and their ages as of March 25, 2015 are as follows:

Name	Age	Position
Kevin S. Wilson	43	Chief Executive Officer and President
Robert B. Grieve, Ph.D.	63	Executive Chair of the Board
Jason A. Napolitano	46	Executive Vice President, Chief Financial Officer and Secretary
Michael J. McGinley, Ph.D.	54	President, Biologicals & Pharmaceuticals
Steven M. Eyl	49	Executive Vice President, Commercial Operations
Nancy Wisnewski, Ph.D.	52	Executive Vice President, Product Development and Customer Support
Steven M. Asakowicz	49	Executive Vice President, Companion Animal Health Sales
Rodney A. Lippincott	41	Executive Vice President, Companion Animal Health Sales

Kevin S. Wilson was appointed President and Chief Executive Officer effective March 31, 2014. He previously served as our President and Chief Operating Officer from February 2013. Mr. Wilson became a member of our Board of Directors in May 2014. Mr. Wilson is a founder, member and officer of Cuattro, LLC. Since 2008, he has been involved in developing technologies for radiographic imaging with Cuattro, LLC and as a founder of Cuattro Software, LLC, Cuattro Medical, LLC and Cuattro Veterinary, LLC. Mr. Wilson served on the board of various private, non-profit, and educational organizations from 2005 to 2011. He was a founder of Sound Technologies, Inc., a diagnostic imaging company, in 1996. After Sound Technologies, Inc. was sold to VCA Antech, Inc. in 2004, Mr. Wilson served as Chief Strategy Officer for VCA Antech, Inc. until 2006. Mr. Wilson attended Saddleback College.

Robert B. Grieve, Ph.D., one of our founders, currently serves as Executive Chair of the Board. Dr. Grieve was named Executive Chair effective March 31, 2014, having previously served as Chief Executive Officer from January 1999. He was named Chairman of the Board effective May 2000 having previously served as Vice Chairman from March 1992. Dr. Grieve also served as Chief Scientific Officer from December 1994 to January 1999 and Vice President, Research and Development, from March 1992 to December 1994. He has been a member of our Board of Directors since 1990. He holds a Ph.D. degree from the University of Florida and M.S. and B.S. degrees from the University of Wyoming.

Jason A. Napolitano was appointed Executive Vice President and Chief Financial Officer in May 2002. He was appointed our Secretary in February 2009, having previously served as our Secretary from May 2002 to December 2006. Prior to joining us formally, he was a financial consultant. From 1990 to 2001, Mr. Napolitano held various positions at Credit Suisse First Boston, an investment bank, including Vice President in health care investment banking and Director in mergers and acquisitions. He holds a B.S. degree from Yale University.

Michael J. McGinley, Ph.D. was appointed President, Biologicals & Pharmaceuticals in February 2013. He previously served as President and Chief Operating Officer from January 2009 to February 2013, Vice President, Global Operations from April through December 2008, Vice President, Operations and Technical Affairs and General Manager, Heska Des Moines from January 2002 to April 2008 and in other positions beginning in June 1997. Prior to joining the Company, Dr. McGinley held positions with Bayer Animal Health and Fort Dodge Laboratories. He holds Ph.D. and M.S. degrees in Immunobiology from Iowa State University and successfully completed the Advanced Management Program at the Harvard Business School in 2008.

Steven M. Eyl has served as our Executive Vice President, Commercial Operations since May 2013. Mr. Eyl was a principal of Eyl Business Services, a consulting firm, from January 2012 to May 2013. He was President of Sound Technologies, Inc. ("Sound") from 2000 to 2011, including after Sound's acquisition by VCA Antech, Inc. in 2004. Mr. Eyl has an extensive background in medical technology sales. He is a graduate of Indiana University.

Nancy Wisnewski, Ph.D. was appointed Executive Vice President, Product Development and Customer Support in April 2011. She served as Vice President, Product Development and Technical Customer Service from December 2006 to April 2011. From January 2006 to November 2006, Dr. Wisnewski was Vice President, Research and Development. Dr. Wisnewski held various positions in Heska's Research and Development organization between 1993 and 2005. She holds a Ph.D. in Parasitology/Biochemistry from the University of Notre Dame and a B.S. in Biology from Lafayette College.

Steven M. Asakowicz was appointed Executive Vice President, Companion Animal Health Sales in February 2013. From July 2011 to February 2013, he was employed by Cuattro, LLC as Vice President, Sales – US Veterinary and sold exclusively on behalf of Cuattro Veterinary USA, LLC. Mr. Asakowicz previously worked as Sales Director for Sound Technologies, Inc. ("Sound") from November 2002 to June 2011, including after Sound was acquired by VCA Antech, Inc. in 2004. Prior to entering the animal health market, Mr. Asakowicz spent 3.5 years employed by Smith Micro Software, Inc. as a Sales Manager and spent 7.5 years employed by AirTouch Cellular and PacTel Cellular (currently Verizon Wireless) as a Corporate Account Executive. Mr. Asakowicz holds a B.A. degree from San Diego State University.

Rodney A. Lippincott was appointed Executive Vice President, Companion Animal Health Sales in February 2013. From July 2011 to February 2013, he was employed by Cuattro, LLC as Vice President, Sales – US Veterinary and sold

exclusively on behalf of Cuattro Veterinary USA, LLC. Mr. Lippincott held various positions including Sales Director for Sound Technologies, Inc., a unit of VCA Antech, Inc., from September 2007 to June 2011. Prior to entering the animal health market, Mr. Lippincott spent 13.5 years employed by Smith Micro Software, Inc. and held positions including US and International Sales Manager

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and Director of Marketing. Mr. Lippincott attended Saddleback College and completed the Executive Education Marketing Management Program at Stanford University, Graduate School of Business.

Item 1A. Risk Factors

Our future operating results may vary substantially from period to period due to a number of factors, many of which are beyond our control. The following discussion highlights some of these factors and the possible impact of these factors on future results of operations. The risks and uncertainties described below are not the only ones we face. Additional risks or uncertainties not presently known to us or that we deem to be currently immaterial also may impair our business operations. If any of the following factors actually occur, our business, financial condition or results of operations could be harmed. In that case, the price of our Public Common Stock could decline and you could experience losses on your investment.

Our February 2013 acquisition of a 54.6% majority interest in Cuatro Veterinary USA, LLC, which has been renamed Heska Imaging US, LLC, could be detrimental to the interests of our shareholders due to related puts, calls or other provisions, or for other reasons.

Under the Amended and Restated Operating Agreement of Heska Imaging US, LLC (the "Operating Agreement"), should Heska Imaging meet certain performance criteria, the unit holders of the 45.4% of Heska Imaging we do not own (the "Imaging Minority") has been granted a put option to sell us some or all of the Imaging Minority's position in Heska Imaging following the audit of our financial statements for 2015, 2016 and 2017. Based on Heska Imaging's current ownership position, this put option could require us to deliver either up to \$17.0 million following calendar year 2015, \$17.0 million following calendar year 2016 or \$36.9 million following calendar year 2017 - as well as 25% of Heska Imaging's cash (any applicable payment in aggregate to be defined as the "Put Payment") to acquire the outstanding minority interest in Heska Imaging. While we have the right to deliver up to 55% of the consideration in our Public Common Stock under certain circumstances, such stock is to be valued based on 90% of market value (the "Delivery Stock Value") and is limited to approximately 650 thousand shares in any case. If the Delivery Stock Value is less than the market value of our Public Common Stock at the time of the Acquisition, we do not have the right to deliver any Public Common Stock as consideration. Cash required under any Put Payment could put a significant strain on our financial position or require us to raise additional capital. There is no guarantee that additional capital will be available in such a circumstance on reasonable terms, if at all. We may be unable to obtain debt financing, the public markets may be unreceptive to equity financing and we may not be able to obtain financing from other alternative sources, such as private equity. Any debt financing, if available, may include restrictive covenants and high interest rates and any equity financing would likely be dilutive to stockholders in this scenario. If additional funds are required and are not available, it would likely have a material adverse effect on our business, financial condition and our ability to continue as a going concern.

Under the Operating Agreement, should Heska Imaging meet certain performance criteria, and the Imaging Minority fail to exercise an applicable put to sell us all of the Imaging Minority's position in Heska Imaging following the audit of our financial statements for 2015, 2016 and 2017, we would have a call option to purchase all, but not less than all, of the Imaging Minority's position in Heska Imaging. Based on Heska Imaging's current ownership position, exercising this call option could require us to deliver up to \$19.6 million following calendar year 2015, \$19.6 million

following calendar year 2016 or \$42.4 million following calendar year 2017 - as well as 25% of Heska Imaging's cash (any applicable payment in aggregate to be defined as the "Call Payment") to acquire the outstanding minority interest in Heska Imaging. While we have the right to deliver up to 55% of the consideration in our Public Common Stock under certain circumstances, such stock is to be valued based on 90% of market value (the "Delivery Stock Value") and is limited to approximately 650 thousand shares in any case. If the Delivery Stock Value is less than the market value of our stock at the time of the Acquisition, we do not have the right to deliver any Public Common

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Stock as consideration. If we believe it is desirable to exercise any one of these calls, cash required under the Call Payment could put a significant strain on our financial position or require us to raise additional capital. There is no guarantee that additional capital will be available in such a circumstance on reasonable terms, if at all. If we believe it is desirable to exercise any such call, determine we are unable to economically finance the Call Payment and do not exercise the call as a result, we could be subject to a more expensive Put Payment less than a year in the future. In this circumstance, unless there is a significant change in our financial position or market conditions, such a Put Payment could have a material adverse effect on our business, financial condition and our ability to continue as a going concern.

Under and as defined in the Operating Agreement, should we undergo a change in control prior to the end of 2017, the Imaging Minority will be entitled to sell their Heska Imaging units to us for cash at the highest call value they otherwise could have obtained (the "Change in Control Payment"). This will be \$42.4 million until at least the end of 2015 and could be as high as \$42.4 million beyond 2015 if Heska Imaging meets certain minimum performance criteria. The Change in Control Payment may materially decrease the interest of third parties in acquiring the Company or a majority of the Company's shares, which could otherwise have occurred at a significant premium to the Company's then current market price for the benefit of some or all of our shareholders. This could make some investors less likely to buy and hold our stock.

Under the terms of the Operating Agreement, Heska Imaging will be managed by a three-person board of managers, two of which are to be appointed by Heska Corporation and one of which is to be appointed by Kevin S. Wilson, a founder of Heska Imaging who has also been Heska Corporation's Chief Executive Officer and President since March 31, 2014. The current board of managers consists of Robert B. Grieve, Ph.D., Heska Corporation's Executive Chair, Mr. Wilson and Jason A. Napolitano, Heska Corporation's Executive Vice President, Chief Financial Officer and Secretary. Until the earlier of (1) our acquiring 100% of the units of Heska Imaging pursuant to the puts and/or calls discussed above or (2) the sixth anniversary of the Acquisition, Heska Imaging may only take the following actions, among others, by unanimous consent of the board of managers: (i) issue securities, (ii) incur, guarantee, prepay, refinance, renew, modify or extend debt, (iii) enter into material contracts, (iv) hire or terminate an officer or amend the terms of their employment, (v) make a distribution other than a tax or liquidation distribution, (vi) enter into a material acquisition or disposition arrangement or a merger, (vii) lease or acquire an interest in real property, (viii) convert or reorganize Heska Imaging, or (ix) amend its certificate of formation or the Heska Imaging Agreement. This unanimous consent provision may hinder our ability to optimize the value of its investment in Heska Imaging in certain circumstances.

Mr. Wilson's employment agreement with us acknowledges that Mr. Wilson has business interests in Cuattro, LLC, Cuattro Software, LLC, Cuattro Medical, LLC and Cuattro Veterinary, LLC which may require a portion of his time, resources and attention in his working hours. If Mr. Wilson is distracted by these or other business interests, he may not contribute as much as he otherwise would have to enhancing our business, to the detriment of our shareholder value. Mr. Wilson is the spouse of Shawna M. Wilson ("Mrs. Wilson"). Mr. Wilson, Mrs. Wilson and trusts for their children and family own a majority interest in Cuattro Veterinary, LLC and Cuattro Medical, LLC. In addition, including shares held by Mrs. Wilson and by trusts for the benefit of Mr. and Mrs. Wilson's children and family, Mr. Wilson also owns a 100% interest in Cuattro, LLC, the largest supplier to Heska Imaging. Cuattro, LLC owns a 100% interest in Cuattro Software, LLC. While the terms of both the Amended and Restated Master License Agreement and the Supply Agreement between Heska Imaging and Cuattro, LLC were negotiated at arm's length as part of the Acquisition, Mr. Wilson has an interest in these agreements and any time and resources devoted to

monitoring and overseeing this relationship may prevent us from deploying such time and resources on more productive matters.

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Since January 1, 2014, Cuattro, LLC charged Heska Imaging \$10.5 million, primarily related to digital imaging products, for which there is an underlying supply contract with minimum purchase obligations, software and services as well as other operating expenses provided for under a license agreement and a supply agreement, respectively; Heska Corporation charged Heska Imaging \$3.9 million, primarily related to sales and other administrative expenses; Heska Corporation net charged Cuattro, LLC \$219 thousand, primarily related to facility usage and other services.

At December 31, 2014, Heska Imaging had a \$1.5 million note receivable, including accrued interest, from Cuattro Veterinary, LLC, which is due on March 15, 2016; Heska Imaging had accounts receivable from Cuattro Software, LLC of \$871 thousand; Heska Corporation had accounts receivable from Heska Imaging of \$6.1 million, including accrued interest; Heska Corporation had net accounts receivable from Cuattro, LLC of \$21 thousand; Heska Imaging had net accounts payable from Cuattro, LLC of \$252 thousand. All monies owed accrue interest at the same interest rate Heska Corporation pays under its credit and security agreement with Wells Fargo once past due with the exception of the note receivable, which accrues at this rate to its maturity date.

Mrs. Wilson, Clint Roth, DVM, Mr. Asakowicz, Mr. Lippincott, Mr. Wilson and Cuattro, LLC own approximately 29.75%, 8.39%, 4.09%, 3.07%, 0.05% and 0.05% of Heska Imaging, respectively, each are a member of Heska Imaging, and each have an interest in the puts and calls discussed above. If Mr. Wilson, Mr. Asakowicz or Mr. Lippincott is distracted by these holdings or interests, they may not contribute as much as they otherwise would have to enhancing our business, to the detriment of our shareholder value. While the Operating Agreement was negotiated at arm's length as part of the Acquisition, and requires that none of the members shall cause Heska Imaging to operate its business in any manner other than the ordinary course of business, any time and resources devoted to monitoring and overseeing this relationship may prevent us from deploying such time and resources on more productive matters.

In addition, like any acquisition, if Heska Imaging significantly underperforms our financial expectations, it may serve to diminish rather than enhance shareholder value. Heska Imaging generated an operating loss of approximately \$2.1 million in the year ended December 31, 2014.

The loss of significant customers who, for example, are historically large purchasers or who are considered leaders in their field could damage our business and financial results.

Revenue from Merck entities, including Merck Animal Health, represented approximately 12% of our consolidated revenue for the twelve months ended December 31, 2014, and 13% for the twelve months ended December 31, 2013. Revenue from Elanco represented approximately 11% of our consolidated revenue for the twelve months ended December 31, 2014. No other single customer accounted for more than 10% of our consolidated revenue for the twelve months ended December 31, 2014, December 31, 2013 or December 31, 2012. Merck entities accounted for approximately 11% of our consolidated accounts receivable at December 31, 2014 and 12% of our consolidated accounts receivable at December 31, 2013. No other single customer accounted for more than 10% of our consolidated accounts receivable at December 31, 2014 or December 31, 2013.

The loss of significant customers who, for example, are historically large purchasers or who are considered leaders in their field could damage our business and financial results.

We have historically not consistently generated positive cash flow from operations, may need additional capital and any required capital may not be available on reasonable terms or at all.

If our actual performance deviates from our operating plan, we may be required to raise additional capital in the future. If necessary, we expect to raise these additional funds by borrowing under our revolving line of credit, the increased sale of customer leases, the sale of equity securities or the issuance of new term

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debt secured by the same assets as the term loans which we fully repaid in 2010. There is no guarantee that additional capital will be available from these sources on reasonable terms, if at all, and certain of these sources may require approval by existing lenders. Funds we expect to be available under our existing revolving line of credit may not be available and other lenders could refuse to provide us with additional debt financing. Financial institutions and other potentially interested parties may not be interested in purchasing our customer leases on economic terms, or at all. The public markets may be unreceptive to equity financings and we may not be able to obtain additional private equity or debt financing. Any equity financing would likely be dilutive to stockholders and additional debt financing, if available, may include restrictive covenants and increased interest rates that would limit our currently planned operations and strategies. We believe the credit markets are particularly restrictive and it may be more difficult to obtain funding versus recent history. Furthermore, even if additional capital is available, it may not be of the magnitude required to meet our needs under these or other scenarios. If additional funds are required and are not available, it would likely have a material adverse effect on our business, financial condition and our ability to continue as a going concern.

If the third parties to whom we granted substantial marketing rights for certain of our existing products or future products under development are not successful in marketing those products, then our sales and financial position may suffer.

Our agreements with our corporate marketing partners generally contain no or small minimum purchase requirements in order for them to maintain their exclusive marketing rights. We are party to an agreement with Merck Animal Health, which grants Merck Animal Health exclusive distribution and marketing rights for our canine heartworm preventive product, TRI-HEART Plus Chewable Tablets, ultimately sold to or through veterinarians in the United States and Canada. Novartis Agro K.K., Tokyo ("Novartis Japan