

PETMED EXPRESS INC  
Form 10-K  
May 28, 2013

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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION  
Washington, D.C. 20549  
FORM 10-K

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

For the fiscal year ended March 31, 2013

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 000-28827

\_\_\_\_\_  
PETMED EXPRESS, INC.  
(Exact name of registrant as specified in its charter)

FLORIDA  
(State or other jurisdiction of  
incorporation or organization)

65-0680967  
(IRS Employer  
Identification No.)

1441 S.W. 29th Avenue, Pompano Beach, Florida 33069  
(Address of principal executive offices) (Zip Code)

Registrant's telephone number, including area code: (954) 979-5995

Securities registered under Section 12(b) of the Act:

Title of each class	Name of each exchange on which registered
COMMON STOCK, \$.001 PAR VALUE	The NASDAQ Stock Market LLC (NASDAQ Global Select Market)

Securities registered under Section 12(g) of the Act:

NONE

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

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

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

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate website, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§ 229.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes  No

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this 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 definition of "accelerated filer", "large accelerated filer", and "smaller reporting company" in Rule 12b-2 of the Exchange Act. (check one):

Large accelerated filer	<input type="radio"/>	Accelerated filer	<input checked="" type="radio"/>
Non-accelerated filer	<input type="radio"/>	Smaller reporting company	<input type="radio"/>

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

The aggregate market value of the registrant's common stock held by non-affiliates of the registrant as of September 30, 2012, the last business day of the registrant's most recently completed second fiscal quarter, was \$192.6 million based on the closing sales price of the registrant's Common Stock on that date, as reported on the NASDAQ Global Select Market.

The number of shares of the registrant's Common Stock outstanding as of May 28, 2013 was 20,108,773.

DOCUMENTS INCORPORATED BY REFERENCE

Information to be set forth in our Proxy Statement relating to our 2013 Annual Meeting of Stockholders to be held on July 26, 2013 is incorporated by reference in Items 10, 11, 12, 13, and 14 of Part III of this report.

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PETMED EXPRESS, INC.

2013 Annual Report on Form 10-K

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## PART I

### CAUTIONARY STATEMENT REGARDING FORWARD-LOOKING INFORMATION

Certain information in this Annual Report on Form 10-K includes forward-looking statements within the meaning of Section 27A of the Securities Act of 1933 and Section 21E of the Securities Exchange Act of 1934. You can identify these forward-looking statements by the words “believes,” “intends,” “expects,” “may,” “will,” “should,” “plan,” “projects,” “contemplates,” “intends,” “budgets,” “predicts,” “estimates,” “anticipates,” or similar expressions. These statements are based on our beliefs, as well as assumptions we have used based upon information currently available to us. Because these statements reflect our current views concerning future events, these statements involve risks, uncertainties and assumptions. Actual future results may differ significantly from the results discussed in the forward-looking statements. A reader, whether investing in our common stock or not, should not place undue reliance on these forward-looking statements, which apply only as of the date of this Annual Report.

When used in this Annual Report on Form 10-K, “PetMed Express,” “1-800-PetMeds,” “PetMeds,” “PetMed,” “PetMeds.com,” “PetMed Express.com,” “the Company,” “we,” “our,” and “us” refer to PetMed Express, Inc. and our wholly-owned subsidiaries.

### ITEM 1. BUSINESS

#### General

PetMed Express, Inc. and subsidiaries, d/b/a 1-800-PetMeds, is a leading nationwide pet pharmacy. The Company markets prescription and non-prescription pet medications, and other health products for dogs and cats, direct to the consumer. The Company offers consumers an attractive alternative for obtaining pet medications in terms of convenience, price, and speed of delivery.

The Company markets its products through national television, online, and direct mail/print advertising campaigns, which aim to increase the recognition of the “1-800-PetMeds” brand name, and “PetMeds” family of trademarks, increase traffic on its website at [www.1800petmeds.com](http://www.1800petmeds.com), acquire new customers, and maximize repeat purchases. Our fiscal year end is March 31, our executive offices are located at 1441 S.W. 29th Avenue, Pompano Beach, Florida 33069, and our telephone number is (954) 979-5995.

#### Our Products

We offer a broad selection of products for dogs and cats. Our current product line contains approximately 3000 SKUS of the most popular pet medications, health products, and supplies. These products include a majority of the well-known brands of medication, such as Frontline Plus®, K9 Advantix® II, Advantage® II, Heartgard Plus®, Sentinel®, Revolution®, and Rimadyl®. Generally, our prices are competitive with the prices for medications charged by veterinarians and retailers. In March 2010, the Company started offering for sale additional pet supplies on our website, which are drop shipped to our customers by third parties. These pet supplies include: food, beds, crates, stairs, strollers, and other popular pet supplies.

We research new products, and regularly select new products or the latest generation of existing products to become part of our product selection. In addition, we also refine our current products to respond to changing consumer-purchasing habits. Our website is designed to give us the flexibility to change featured products or promotions. Our product line provides customers with a wide variety of selections across the most popular health categories for dogs and cats. Our current products include:

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Non-Prescription Medications (OTC) and supplies: Flea and tick control products, bone and joint care products, vitamins, treats, nutritional supplements, hygiene products, and supplies.

Prescription Medications (Rx): Heartworm preventatives, arthritis, thyroid, diabetes, pain medications, antibiotics, and other specialty medications, as well as generic substitutes.

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## Sales

The following table provides a breakdown of the percentage of our total sales by each category during the indicated periods:

	Year Ended March					
	2013		31, 2012		2011	
Non-prescription medications and supplies	59	%	59	%	61	%
Prescription medications	40	%	40	%	38	%
Shipping and handling charges and other	1	%	1	%	1	%
Total	100	%	100	%	100	%

We offer our products through three main sales channels: Internet through our website, telephone contact center through our toll-free number, and direct mail/print through 1-800-PetMeds catalogs, brochures, and postcards. We have designed our catalogs and website to provide a convenient, cost-effective, and informative shopping experience that encourages consumers to purchase products important for a pet's health and quality of life. We believe that these multiple channels allow us to increase the visibility of our brand name and provide our customers with increased shopping flexibility and excellent service.

## Internet

We seek to combine our product selection and pet health information with the shopping ease of the Internet to deliver a convenient and personalized shopping experience. Our website offers health and nutritional product selections for dogs and cats, and relevant editorial and easily obtainable or retrievable resource information. From our home page, customers can search our website for products and access resources on a variety of information on dogs and cats. Customers can shop at our website by category, product line, individual product, or symptom. We attracted approximately 22.7 million visitors to our website during fiscal 2013, approximately 10% of those visitors placed an order, and our website generated approximately 77% of our total sales for the same time period. On our website pet owners have access to health information covering pets' behavior and illnesses, and natural and pharmaceutical remedies specifically for a pet's problems. The pet education content on our main website is periodically updated with the latest research for pet owners.

## Telephone Contact Center

Our customer care representatives receive and process inbound and outbound customer calls, facilitate our live web chat, and process customer e-mails. Our telephone system is equipped with certain features including pop-up screens and call blending capabilities that give us the ability to efficiently utilize our customer care representatives' time, providing excellent customer care, service, and support. Our customer care representatives receive a base salary and are rewarded with commissions for sales, and bonuses and other awards for achieving certain quality goals.

## Direct Mail/Print

The 1-800-PetMeds catalog is a full-color catalog that features our most popular products. The catalog is produced by a combination of in-house writers, production artists, and independent contractors. We mail catalogs, brochures, and postcards in response to requests generated from our advertising and as part of direct mail campaigns to our customers.

## Our Customers

Approximately 2.7 million customers have purchased from us within the last two years. We attracted approximately 630,000 and 722,000 new customers in fiscal 2013 and 2012, respectively. Our customers are located throughout the United States, with approximately 50% of customers residing in California, Florida, New York, Texas, Pennsylvania, Virginia, North Carolina, and New Jersey. Our primary focus has been on retail customers and the average purchase was approximately \$73 for fiscal 2013 compared to \$76 for fiscal 2012.

## Marketing

The goal of our marketing strategy is to build brand recognition, increase customer traffic, add new customers, build strong customer loyalty, maximize reorders, and develop incremental revenue opportunities. We have an integrated marketing campaign that includes television advertising, online marketing, direct mail/print and e-mail.

### Television Advertising

Our television advertising is designed to build brand equity, create brand awareness, and generate initial purchases of products via the telephone and the Internet. We have used :30 and :15 second television commercials to attract new customer orders. Our television commercials typically focus on our ability to rapidly deliver to customers the same medications offered by veterinarians, but at reduced prices. We generally purchase advertising on national cable channels to target our key demographic group – women, ages 30 to 65. We believe that television advertising is particularly effective and instrumental in building brand awareness.

### Online Marketing

We supplement our traditional advertising with online advertising and marketing efforts. We make our brand available to Internet consumers by purchasing targeted keywords and achieving prominent placement on the top search engines and search engine networks, including Google, Bing™, and Yahoo®. We utilize Internet display and video advertisements, social media, and comparison shopping, and we are also members of the LinkShare Network, which is an affiliate program with merchant clients and affiliate websites.

### Direct Mail/Print and E-mail

We use direct mail/print and e-mail to acquire new customers and to remind our existing customers to reorder.

## Operations

### Order Processing

Our website allows customers to easily browse and purchase all of our products online. Our website is designed to be fast, secure, and easy to use with order and shipping confirmations, and with online order tracking capabilities. We provide our customers with toll-free telephone access to our customer care representatives. Our call center generally operates from 8:00 AM to 11:00 PM, Monday through Thursday, 8:00 AM to 9:00 PM on Friday, 9:00 AM to 6:00 PM on Saturday, and 10:00 AM to 5:00 PM on Sunday, Eastern Time. The process of customers purchasing products from 1-800-PetMeds consists of a few simple steps. A customer first places a call to our toll-free telephone number or visits our website. The following information is needed to process prescription orders: pet information, prescription information, and the veterinarian's name and phone number. This information is entered into our computer system. Then our pharmacists and pharmacy technicians verify all prescriptions. The order process system checks for the verification for prescription medication orders and a valid payment method for all orders. An invoice is generated and printed in our fulfillment center, where items are picked, and then shipped via United States Postal Service, Federal Express, or UPS. Our customers enjoy the convenience of rapid home delivery, with approximately 80% of all orders being shipped within 24 hours of ordering.

### Customer Care and Support

We believe that a high level of customer care and support is critical in retaining and expanding our customer base. Customer care representatives participate in ongoing training programs under the supervision of our training



managers. These training sessions include a variety of topics such as product knowledge, computer usage, customer service tips, and the relationship between our Company and veterinarians. Our customer care representatives respond to customers' e-mails, calls, and live chats that are related to products, order status, prices, and shipping. We believe our customer care representatives are a valuable source of feedback regarding customer satisfaction.

## Warehousing and Shipping

We inventory our products and fill most customer orders from our corporate headquarters in Pompano Beach, Florida. We have an in-house fulfillment and distribution operation, which is used to manage the entire supply chain, beginning with the placement of the order, continuing through order processing, and then fulfilling and shipping of the product to the customer. We offer a variety of shipping options, including next day delivery. We ship to anywhere in the United States served by the United States Postal Service, Federal Express, or UPS. Priority orders are expedited in our fulfillment process. Our goal is to ship the products the same day that the order is received. For prescription medications, our goal is to ship the product immediately after the prescription has been authorized by the customer's veterinarian.

## Purchasing

We purchase our products from a variety of sources, including certain manufacturers, domestic distributors, and wholesalers. There were five suppliers from whom we purchased approximately 50% of all products in fiscal 2013. We purchase the majority of our health and nutritional supplements directly from manufacturers. We believe having strong relationships with product manufacturers will ensure the availability of an adequate volume of products ordered by our customers, and will enable us to provide more and better product information. Historically, substantially all the major manufacturers of prescription and non-prescription medications have declined to sell these products to direct marketing companies, such as our Company. (See Risk Factors.) Part of our growth strategy includes developing direct relationships with the leading pharmaceutical manufacturers of the more popular prescription and non-prescription medications.

## Technology

We utilize integrated technologies in our call centers, e-commerce, order entry, and inventory control/fulfillment operations. Our systems are custom configured by the Company to optimize our computer telephone integration and mail-order processing. The systems are designed to maintain a large database of specialized information and process a large volume of orders efficiently and effectively. Our systems provide our customer care representatives, and our customers on our website, with real time product availability information and updated customer information to enhance our customer care. We also have an integrated direct connection for processing credit cards to ensure that a valid credit card number and authorization have been received at the same time our customer care representatives are on the phone with the customer or when a customer submits an order on our website. Our information systems provide our customer care representatives with records of all prior contact with a customer, including the customer's address, phone number, e-mail address, prescription information, order history, payment history, and notes.

## Competition

The pet medications market is competitive and highly fragmented. Our competitors consist of veterinarians, and online and traditional retailers. We believe that the following are the principal competitive factors in our market:

Product selection and availability, including the availability of prescription and non-prescription medications;  
Brand recognition;  
Reliability and speed of delivery;  
Personalized service and convenience;  
Price; and  
Quality of website content.

We compete with veterinarians for the sale of prescription and non-prescription pet medications and other health products. Many pet owners may prefer the convenience of purchasing their pet medications or other health products at the time of a veterinarian visit. In order to effectively compete with veterinarians, we must continue to educate pet owners about the service, convenience, and savings offered by our Company.

According to the American Pet Products Manufacturers Association, pet spending in the United States increased 4.7% to \$53.3 billion in 2012. Pet supplies and medications represented \$12.6 billion, or 24% of the total spending on pets in the United States. The pet medication market that we participate in is estimated to be approximately \$4.0 billion, with veterinarians having the majority of the market share. The dog and cat population is approximately 165 million, with approximately 62% of all households having a pet.

We believe that the following are the main competitive strengths that differentiate 1-800-PetMeds from the competition:

Channel leader, in an estimated \$4.0 billion industry;  
“1-800-PetMeds” brand name;

Licensed pharmacy to conduct business in 50 states, and awarded Vet-VIPPSCM (Veterinary-Verified Internet Pharmacy Practice Site) accreditation by the National Association of Boards of Pharmacy®;

Exceptional customer care and support

### Intellectual Property

We conduct our business under the trade name “1-800-PetMeds” and use a family of names all containing the term “PetMeds” or “PetMed” in some form. We believe this trade name, which is also our toll-free telephone number, and the “PetMeds” family of trademarks, have added significant value and are an important factor in the marketing of our products. We have also obtained the right to use and control the Internet addresses [www.1800petmeds.com](http://www.1800petmeds.com), [www.1888petmeds.com](http://www.1888petmeds.com), [www.petmedexpress.com](http://www.petmedexpress.com), [www.petmed.com](http://www.petmed.com), and [www.petmeds.com](http://www.petmeds.com). We do not expect to lose the ability to use the Internet addresses; however, there can be no assurance in this regard and the loss of these addresses may have a material adverse effect on our financial position and results of operations. We are the exclusive owners of United States Trademark Registrations for “PetMed Express and Design®,” “1888PetMeds and Design®,” “1-800-PetMeds and Design®,” “1-800-PetMeds®,” and “PetMeds®.”

### Government Regulation

Dispensing prescription medications is governed at the state level by the Boards of Pharmacy, or similar regulatory agencies, of each state where prescription medications are dispensed. We are subject to regulation by the State of Florida and are licensed as a community pharmacy by the Florida Board of Pharmacy. Our current license is valid until February 28, 2015, and prior to that date a renewal application will be submitted to the Board of Pharmacy. Our pharmacy practice is also licensed and/or regulated by 49 other state pharmacy boards and, with respect to our products, by other regulatory authorities including, but not necessarily limited to, the United States Food and Drug Administration (“FDA”) and the United States Environmental Protection Agency. As a licensed pharmacy in the State of Florida, we are subject to the Florida Pharmacy Act and regulations promulgated thereunder. To the extent that we are unable to maintain our license as a community pharmacy with the Florida Board of Pharmacy, or if we do not maintain the licenses granted by other state pharmacy boards, or if we become subject to actions by the FDA, or other enforcement regulators, our distribution of prescription medications to pet owners could cease, which could have a material adverse effect on our financial condition and results of operations.

### Employees

We currently have 206 full time employees, including: 126 in customer care and marketing; 33 in fulfillment and purchasing; 36 in our pharmacy; 3 in information technology; 3 in administrative positions; and 5 in management. None of our employees are represented by a labor union, or governed by any collective bargaining agreements. We consider relations with our employees to be satisfactory.

Available Information

We file annual, quarterly, and current reports, proxy statements, and other information with the Securities and Exchange Commission (“SEC”). Our SEC filings, including our annual reports on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K, and any amendments to those reports filed or furnished pursuant to the Exchange Act are available free of charge over the Internet on our website at [www.1800petmeds.com](http://www.1800petmeds.com) or at the SEC’s web site at [www.sec.gov](http://www.sec.gov). Our SEC filings will be available through our website as soon as reasonably practicable after we have electronically filed or furnished them to the SEC. Information contained on our website is not incorporated by reference into this annual report on Form 10-K.

## ITEM 1A. RISK FACTORS

You should carefully consider the risks and uncertainties described below, and all the other information included in this Annual Report on Form 10-K before you decide to invest in our common stock. Any of the following risks could materially adversely affect our business, financial condition, or operating results and could result in a loss of your investment.

We may inadvertently fail to comply with various state regulations covering the dispensing of prescription pet medications which may subject us to reprimands, sanctions, probations, fines, suspensions, or the loss of one or more of our pharmacy licenses.

The sale and delivery of prescription pet medications is generally governed by state laws and state regulations. Since our pharmacy is located in the State of Florida, the Company is governed by the laws and regulations of the State of Florida. Each prescription pet medication sale we make is likely also to be covered by the laws of the state where the customer is located. The laws and regulations relating to the sale and delivery of prescription pet medications vary from state to state, but generally require that prescription pet medications be dispensed with the authorization from a prescribing veterinarian. To the extent that we are unable to maintain our license as a community pharmacy with the Florida Board of Pharmacy, or if we do not maintain the licenses granted by other state boards, or if we become subject to actions by the FDA, or other enforcement regulators, our dispensing of prescription medications to pet owners could cease, which could have a material adverse effect on our operations.

The Company is a party to routine litigation and administrative complaints incidental to its business. Management does not believe that the resolution of any or all of such routine litigation and administrative complaints is likely to have a material adverse effect on the Company's financial condition or results of operations. While we make every effort to fully comply with all applicable state rules, laws, and regulations, from time to time we have been the subject of administrative complaints regarding the authorization of prescriptions prior to shipment. We cannot assure you that we will not continue to be the subject of administrative complaints in the future. We cannot guarantee you that we will not be subject to reprimands, sanctions, probations, or fines, or that one or more of our pharmacy licenses will not be suspended or revoked. If we were unable to maintain our license as a community pharmacy in the State of Florida, or if we are not granted licensure in a state that begins to require licensure, or if one or more of the licenses granted by other state boards should be suspended or revoked, our ability to continue to sell prescription medications and to continue our business as it is presently conducted could be in jeopardy.

We currently purchase a portion of our prescription and non-prescription medications from third party distributors and we are not an authorized distributor of these products. We do not have any guaranteed supply of medications at any pre-established prices.

The majority of our sales were attributable to sales of prescription and non-prescription medications. Historically, substantially all the major pharmaceutical manufacturers have declined to sell prescription and non-prescription pet medications directly to us. In order to assure a supply of these products, we purchase medications from various secondary sources, including a variety of domestic distributors. Our business strategy includes seeking to establish direct purchasing arrangements with major pet pharmaceutical manufacturing companies. If we are not successful in achieving this goal, we will continue to rely upon secondary sources.

We cannot guarantee that if we continue to purchase prescription and non-prescription pet medications from secondary sources that we will be able to purchase an adequate supply to meet our customers' demands, or that we will be able to purchase these products at competitive prices. As these products represent a significant portion of our sales, our failure to fill customer orders for these products could adversely impact our sales. If we are forced to pay higher prices for these products to ensure an adequate supply, we cannot guarantee that we will be able to pass along to our

customers any increases in the prices we pay for these medications. This inability to pass along increased prices could materially adversely affect our financial condition and results of operations.

Our failure to properly manage our inventory may result in excessive inventory carrying costs, or inadequate supply of products, which could materially adversely affect our financial condition and results of operations.

Our current product line contains approximately 3,000 SKUs. A significant portion of our sales is attributable to products representing approximately 100 SKUs, including the most popular flea and tick, and heartworm preventative brands. We need to properly manage our inventory to provide an adequate supply of these products and avoid excessive inventory of the products representing the balance of the SKUs. We generally place orders for products with our suppliers based upon our internal estimates of the amounts of inventory we will need to fill future orders. These estimates may be significantly different from the actual orders we receive.

In the event that subsequent orders fall short of original estimates, we may be left with excess inventory. Significant excess inventory could result in price discounts and increased inventory carrying costs. Similarly, if we fail to have an adequate supply of some SKUs, we may lose sales opportunities. We cannot guarantee that we will maintain appropriate inventory levels. Any failure on our part to maintain appropriate inventory levels may have a material adverse effect on our financial condition and results of operations.

Resistance from veterinarians to authorize prescriptions, or attempts/efforts on their part to discourage pet owners to purchase from internet mail-order pharmacies could cause our sales to decrease and could materially adversely affect our financial condition and results of operations.

Since we began our operations some veterinarians have resisted providing our customers with a copy of their pet's prescription or authorizing the prescription to our pharmacy staff, thereby effectively preventing us from filling such prescriptions under state law. We have also been informed by customers and consumers that veterinarians have tried to discourage pet owners from purchasing from internet mail-order pharmacies. Sales of prescription medications represented approximately 40% of our sales for the fiscal year. Although veterinarians in some states are required by law to provide a pet owner with a prescription if medically appropriate, if the number of veterinarians who refuse to authorize prescriptions should increase, or if veterinarians are successful in discouraging pet owners from purchasing from internet mail-order pharmacies, our sales could decrease and our financial condition and results of operations may be materially adversely affected.

Significant portions of our sales are made to residents of eight states. If we should lose our pharmacy license in one or more of these states, our financial condition and results of operations would be materially adversely affected.