

VCA ANTECH INC
Form 10-K405
March 29, 2002

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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 December 31, 2001

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

Commission file number 1-16783

VCA ANTECH, INC.

(Exact name of registrant as specified in its charter)

Delaware	95-4097995
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

**12401 West Olympic Boulevard
Los Angeles, California 90064-1022**
(Address of principal executive offices and zip code)

(310) 571-6500
(Registrant's telephone number, including area code)

Securities registered pursuant to Section 12(b) of the Act:

None

Securities registered pursuant to Section 12(g) of the Act:

Common stock, \$0.001 par value

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 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.

At March 25, 2001, there were outstanding 36,736,081 shares of the Common Stock of the registrant and the aggregate market value of the shares held on that date by non-affiliates of the registrant, based on the closing price (\$13.45 per share) of the Registrant's Common Stock on the Nasdaq Stock Market's National Market, was \$245.1 million. For purposes of this computation, it has been assumed that the shares beneficially held by directors and officers of registrant were held by affiliates; this assumption is not to be deemed to be an admission by these persons that

they are affiliates of registrant.

DOCUMENTS INCORPORATED BY REFERENCE

Portions of Registrant's proxy statement relating to its 2002 annual meeting of stockholders are incorporated by reference in Part III of this annual report.

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PART I

ITEM 1. BUSINESS

General

We are VCA Antech, Inc. (VCA), a leading animal health care services company and operate the largest networks of veterinary diagnostic laboratories and free-standing, full-service animal hospitals in the United States. Our network of veterinary diagnostic laboratories provides sophisticated testing and consulting services to the veterinarian comparable to that provided by the human diagnostic laboratory to the physician. Veterinarians use these services in the detection, diagnosis, evaluation, monitoring, treatment and prevention of diseases and other conditions affecting animals. With a nationwide veterinary laboratory network serving all 50 states, we provide diagnostic testing for an estimated 13,000 animal hospitals, a customer base over twice the size of our next largest competitor. Our network of animal hospitals offers a full range of general medical and surgical services for companion animals, as well as specialized treatments including advanced diagnostic services, internal medicine, oncology, ophthalmology, dermatology and cardiology. In addition, we provide pharmaceutical products and perform a variety of pet wellness programs including routine vaccinations, health examinations, diagnostic testing, spaying, neutering and dental care. The more than 750 veterinarians supporting our 214 animal hospitals had over 3 million patient visits in 2001.

Industry Overview

The U.S. population of companion animals has reached approximately 188 million, including about 141 million dogs and cats. The most recent industry data show that over \$11 billion was spent on animal health care services in 1996, with an annual growth rate of over 9.5% from 1991 through 1996 for spending on dogs and cats. The ownership of pets is widespread, with over 62% of U.S. households owning at least one pet, including companion and other animals. Pet ownership is highest among households with children under 18 and empty-nesters whose pets have become their new children. We believe the pet population and the number of pet-owning households should continue to grow.

Among this expanding number of pet owners is a growing awareness of pet health and wellness, including the benefits of preventive care and specialized services. As technology continues to migrate from the human healthcare sector into the practice of veterinary medicine, more sophisticated treatments and diagnostic tests are becoming available to treat companion animals. These new and increasingly complex procedures, diagnostic tests and pharmaceuticals are gaining wider acceptance as pet owners are exposed to these previously unconsidered treatment programs through literature and marketing programs sponsored by large pharmaceutical and pet nutrition companies. We believe this is evidenced by an industry survey revealing that 70% of pet owners view their animals as important members of the family and are willing to pay for more veterinary services to promote the good health and extend the life of their pet.

Even as treatments available in veterinary medicine become more complex, prices for veterinary services typically remain a low percentage of a pet-owner's income, facilitating payment at the time of service. Unlike the human health care industry, providers of veterinary services are not dependent on third-party payors in order to collect fees. As a consequence, providers of veterinary services do not have the problems of extended payment collection cycles or pricing pressures from third party-payors faced by human health care providers. Outsourced laboratory testing is a wholesale business that collects payments directly from animal hospitals, generally on terms requiring payment within 30 days of the date the charge is invoiced. Fees for animal hospital services are due at the time of the service. For example, over 95% of our animal hospital services are paid for in cash or by credit card at that time. In addition, over the past three fiscal years, our bad debt expense has averaged only 1% of total revenue.

The practice of veterinary medicine is subject to seasonal fluctuation. In particular, demand for veterinary services is significantly higher during the warmer months because pets spend a greater amount of time outdoors, where they are more likely to be injured and are more susceptible to disease and parasites. In addition, use of veterinary services may be affected by levels of infestation of fleas, heartworms and ticks and the number of daylight hours.

Diagnostic Laboratories. Laboratory tests are used by veterinarians to diagnose, monitor and treat illnesses and conditions in animals through the detection of substances in urine, tissue, fecal and blood samples and other specimens. As is the case with the physician treating a human patient, laboratory diagnostic testing is becoming a routine diagnostic tool used by the veterinarian.

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Veterinary laboratory tests are performed primarily at free-standing veterinary diagnostic laboratories, universities or animal hospitals using on-site diagnostic equipment. For particular types of tests, on-site diagnostic equipment can provide more timely results than outside laboratories, but this in-house testing requires the animal hospital or veterinarian to purchase the equipment, maintain and calibrate the equipment periodically to avoid testing errors, and employ trained personnel to operate it. Conversely, veterinary diagnostic laboratories can provide a wider range of tests than generally are available on-site at most animal hospitals and do not require any up-front investment on the part of the animal hospital or veterinarian. Also, leading veterinary diagnostic laboratories employ highly trained individuals who specialize in the detection and diagnosis of diseases and thus are a valuable resource for the veterinarian.

Within the outsourcing market, our laboratories specialize in the veterinary market and offer a broad spectrum of standard and customized tests, convenient sample pick-up times, rapid test reporting and access to professional consulting services provided by trained specialists. Providing the customer with this level of service at competitive prices requires high throughput volumes due to the operating leverage associated with the laboratory business. As a result, larger laboratories likely maintain a competitive advantage relative to smaller laboratories.

We believe that the outsourced laboratory testing market is one of the fastest growing segments of the animal health care services industry, and expect continued growth as a result of:

the increased focus on wellness and monitoring programs in veterinary medicine, which is increasing the overall number of tests being performed;

the emphasis in veterinary education on diagnostic tests and the trend toward specialization in veterinary medicine, which are causing veterinarians to increasingly rely on tests for more accurate diagnoses;

the continued technological developments in veterinary medicine, which are increasing the breadth of tests offered; and

the trend toward outsourcing tests because of the relative low cost, the high accuracy rates and the diagnostic support provided by specialists employed by the laboratory.

Animal Hospitals. Animal health care services are provided predominately by the veterinarian practicing as a sole practitioner, or as part of a larger animal medical group or hospital. Veterinarians diagnose and treat animal illnesses and injuries, perform surgeries, provide routine medical exams and prescribe medication. Some veterinarians specialize by type of medicine, such as orthopedics, dentistry, ophthalmology or dermatology. Others focus on a particular type of animal. The principal factors in a pet owner's decision as to which veterinarian to use include convenient location, recommendation of friends, reasonable fees, convenient hours and quality of care.

The U.S. market for veterinary services is highly fragmented, with more than 35,000 veterinarians practicing at over 18,000 companion animal hospitals. Although most animal hospitals are single site, sole practitioner facilities, we believe veterinarians are increasingly gravitating toward animal hospitals that provide state-of-the-art facilities, treatments, methods and pharmaceuticals to enhance the services they can provide their clients.

Well-capitalized animal hospital operators have the opportunity to supplement their internal growth with selective acquisitions. We believe the extremely fragmented animal hospital industry is consolidating due to:

the purchasing, marketing and administrative cost advantages that can be realized by a large, multiple location, multi-practitioner veterinary provider;

the cost of financing equipment purchases and upgrading technology necessary for a successful practice;

the desire of veterinarians to focus on practicing veterinary medicine, rather than spending large portions of their time at work performing the administrative tasks necessary to operate an animal hospital;

the choice of some owners of animal hospitals to diversify their investment portfolio by selling all or a portion of their investment in the animal hospital; and

the appeal to many veterinarians of the benefits and work scheduling flexibility that are not typically available to a sole practitioner or single-site provider.

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Business Strategy

Our business strategy is to continue to expand our market leadership in animal health care services through our diagnostic laboratories and animal hospitals. Key elements of our strategy include:

Capitalizing on our Leading Market Position to Generate Revenue Growth. Our leading market position in each of our business segments positions us to capitalize on favorable growth trends in the animal health care services industry. In our laboratories, we seek to generate revenue growth by taking advantage of the growing number of outsourced diagnostic tests and by increasing our market share. We continually educate veterinarians on new and existing technologies and test offerings available to diagnose medical conditions. Further, we leverage the knowledge of our specialists by providing veterinarians with extensive customer support in promoting and understanding these diagnostic tests. In our animal hospitals, we seek to generate revenue growth by capitalizing on the growing emphasis on pet health and wellness. For example, in 2000, we implemented a senior wellness program. This program bundles tests and animal hospital services, seeking to promote recurring visits and to increase the average amount spent per visit.

Leveraging Established Infrastructure to Improve Margins. We intend to leverage our established laboratory and animal hospital infrastructure to continue to increase our operating margins. Due to our established networks and the fixed cost nature of our business model, we are able to realize high margins on incremental revenues from both laboratory and animal hospital customers. For example, given that our nationwide transportation network servicing our laboratory customers is a relatively fixed cost, we are able to achieve significantly higher margins on most incremental tests ordered by the same customer when picked up by our couriers at the same time. We estimate that in most cases, we realize an operating and EBITDA margin between 60% and 75% on these incremental tests.

Utilizing Enterprise-Wide Systems to Improve Operating Efficiencies. We recently completed the migration of all animal hospital operations to an enterprise-wide management information system. We believe that this common system will enable us to more effectively manage the key operating metrics that drive our business. With the aid of this system, we seek to standardize pricing, expand the services our veterinarians provide, capture unbilled service, increase volume and implement targeted marketing programs.

Pursue Selected Acquisitions. Although we have substantially completed our laboratory infrastructure, we may make selective, strategic laboratory acquisitions. Additionally, the fragmentation of the animal hospital industry provides us with significant expansion opportunities in our animal hospital segment. Depending on the attractiveness of the candidates and the strategic fit with our existing operations, we intend to acquire approximately 15 to 25 animal hospitals per year primarily using internally generated cash.

Diagnostic Laboratories

We operate the only full-service, veterinary diagnostic laboratory network serving all 50 states. We have a client base over two times that of our largest competitor. In 2001, we performed approximately 18.3 million tests and handled roughly 6.9 million requisitions in our state-of-the-art, automated diagnostic laboratories. Our laboratory network services a diverse customer base of over 13,000 animal hospitals, and non-affiliated animal hospitals generated approximately 95% of our laboratory revenue in 2001.

Services. Our diagnostic spectrum includes over 300 different tests in the areas of chemistry, pathology, serology, endocrinology, hematology, and microbiology, as well as tests specific to particular diseases. We do not conduct experiments on animals and are not engaged in animal research.

Although modified to address the particular requirements of the species tested, the tests performed in our veterinary laboratories are similar to those performed in human clinical laboratories and utilize similar laboratory equipment and technologies. The growing concern for animal health, combined with the movement of veterinary medicine toward increasing specialization, should spur the migration of additional areas of human testing into the veterinary field. For example, we now provide cancer testing for household pets whereas several years ago, these tests were not available.

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Given the recent advancements in veterinary medical technology and the increased breadth and depth of knowledge required for the practice of veterinary medicine, many veterinarians solicit the knowledge and experience of our 91 specialists to interpret test results, consult on the diagnosis of illnesses and suggest treatment programs. This resource includes veterinarians, chemists, and other scientists with expertise in pathology, internal medicine, oncology, cardiology, dermatology, neurology and endocrinology. This depth of experience and expertise enables our specialists to suggest additional testing or provide diagnostic advice that assists the veterinarian in developing an appropriate treatment plan.

Together with our specialist support, we believe the quality of our service further distinguishes our laboratory services. We maintain quality assurance programs to ensure that specimens are collected and transported properly, that tests are performed accurately and that client, patient and test information is reported and billed correctly. Our quality assurance programs include quality control testing of specimens of known concentration or reactivity to ensure accuracy and precision, routine checks and preventive maintenance of laboratory testing equipment, and personnel standards ensuring that only qualified personnel perform testing. As a result, we believe that our accuracy rate is over 99%.

We operate 16 full-service laboratories. Our laboratory network includes:

primary hubs that are open 24 hours per day and offer a full testing menu;

secondary laboratories, that service large metropolitan areas, are open 24 hours per day and offer a wide testing menu; and

ten STAT laboratories that service other locations with demand sufficient to warrant nearby laboratory facilities and are open primarily during daytime hours.

We connect our laboratories to our customers with what we believe is the industry's largest transportation network, which picks up an average of 20,000 to 25,000 requisitions daily through an extensive network of drivers and independent couriers. In 2001, we derived approximately 69% of our laboratory revenue from major metropolitan areas, where we offer twice-a-day pick-up service and same-day results. In addition, in these areas, we generally offer to report results within three hours of pick-up. Outside of these areas, we typically provide test results to veterinarians before 8:00 a.m. the following day.

Veterinarian customers located outside the areas covered by our transportation network are serviced using our Test Express service. Users of the Test Express service send patient specimens by Federal Express to our laboratory just outside of Memphis, the proximity of which to the Federal Express primary sorting facility permits speedy and cost-efficient testing.

Sales, Marketing and Customer Service. We employ over 40 full-time sales and field service representatives who market laboratory services and maintain relationships with existing customers. The sales force is commissioned-based and organized along geographic regions. We support our sales efforts by strengthening our industry-leading team of specialists, developing marketing literature, attending trade shows, participating in trade associations and providing educational services to veterinarians. In addition, we employ over 80 customer service representatives who respond to customer inquiries, provide test results and, when appropriate, introduce the customer to other services offered by the laboratory.

Given the high margins we enjoy on many of our incremental tests, our sales force is compensated primarily on its success in maximizing the amount of business from existing customers as well as adding new customers.

Personnel. We employ a staff of approximately 1,000 full-time-equivalent employees in our laboratory network. We employ on average 306 employees at each of our primary laboratories. At a typical secondary laboratory, we employ on average 89 employees and at our typical STAT laboratory we employ on average 18 employees. We employ some of our specialists and enter into consulting arrangements with others. Our laboratory network consists of an eastern and western division and we employ a vice president to manage each region. We employ a manager at each of our laboratories and supervisors for each department within the laboratories.

Table of Contents**Animal Hospitals**

At December 31, 2001, we operated 214 animal hospitals in 33 states that were supported by over 750 veterinarians. Our nationwide network of free-standing, full-service animal hospitals has facilities located in the following states:

California	44
New York*	21
Florida	17
Illinois	16
Michigan	12
Pennsylvania	11
New Jersey*	9
Texas*	9
Maryland	8
Indiana	7
Massachusetts	7
Virginia	6
Nevada	5
Ohio*	5
Alaska	4
Colorado	4
Delaware	4
Connecticut	3
New Mexico	3
Arizona	2
Minnesota*	2
Nebraska*	2
North Carolina*	2
Utah	2
Alabama*	1
Georgia	1
Hawaii	1
Louisiana*	1
Missouri	1
South Carolina	1
Washington*	1
West Virginia*	1
Wisconsin	1

* States where we manage animal hospitals owned by veterinary medical groups.

We seek to provide quality medical care in clean, attractive facilities that are open on average between 10 and 15 hours per day, six to seven days per week. Our typical animal hospital:

is located in a 4,000 to 6,000 square foot, free-standing facility in an attractive location;

has annual revenue between \$1.0 million and \$2.0 million;

is supported by three to five veterinarians; and

has an operating history of over ten years.

In addition to general medical and surgical services, we offer specialized treatments for companion animals, including advanced diagnostic services, internal medicine, oncology, ophthalmology, dermatology and cardiology. We also provide pharmaceutical products for use in the delivery of treatments by our veterinarians and pet owners. Many of our animal hospitals offer additional services, including grooming, bathing and boarding. We also sell specialty pet products at our hospitals, including pet food, vitamins, therapeutic shampoos and conditioners, flea collars and sprays, and other accessory products.

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As part of the growth strategy of our hospital business, we intend to continue our disciplined acquisition strategy by identifying high quality practices that may have value to be unlocked through the services and scale we can provide. We contemplate the acquisition of 15 to 25 animal hospitals per year. Our typical candidate mirrors the profile of our existing hospital base. Acquisitions will be used to both expand in existing markets and enter new geographical areas. We intend primarily to use cash in our acquisitions, but we may use debt or stock to the extent we deem appropriate. By undertaking prudent acquisitions, we are able to grow our hospital business without diluting the local market for veterinary services.

Personnel. Our animal hospitals generally employ a staff of between 10 to 30 full-time equivalent employees, depending upon the facility's size and customer base. The staff includes administrative and technical support personnel, three to five veterinarians, an office manager who supervises the day-to-day activities of the facility, and a small office staff. We employ a relatively small corporate staff to provide centralized administrative services to all of our animal hospitals.

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We actively recruit highly qualified veterinarians and technicians and are committed to supporting continuing education for our professional staff. We operate post-graduate teaching programs for veterinarians at eight of our facilities, which train approximately 40 veterinarians each year. We believe that these programs enhance our reputation in the veterinary profession and further our ability to continue to recruit the most talented veterinarians.

We seek to establish an environment that supports the veterinarian in the delivery of quality medicine and fosters professional growth through increased patient flow and a diverse case mix, continuing education, state-of-the-art equipment and access to specialists. We believe our hospitals offer attractive employment opportunities to veterinarians because of this professional environment, competitive compensation programs, management opportunities, employee benefits not generally available to a sole practitioner, scheduling flexibility to accommodate personal lifestyles and the ability to relocate to different regions of the country. Further, we permit some of our veterinarians to participate with us in the ownership and operation of selected animal hospitals. In these circumstances, the veterinarian purchases an equity position in our animal hospital and is our partner in its operation. As of December 31, 2001, we operated 23 hospitals under a partnership structure. Typically, the salary of the veterinarian partner is based on a percentage of the revenue of the animal hospital that is generated by the veterinarian. The operating income of the partnership that is distributed to the veterinarian partner is based on the veterinarian partner's percentage interest in the partnership, which is typically between 10% and 25%.

We have established a Medical Advisory Board to support our operations. The Medical Advisory Board's function, under the direction of our Chief Medical Officer, is to recommend medical standards for our network of animal hospitals. The committee is comprised of leading veterinarians representing both the different geographic regions in which we operate and the medical specialties practiced by our veterinarians. Currently, four members of the Medical Advisory Board are faculty members at leading veterinary colleges in the United States. These members serve as medical consultants to us.

Marketing. Our marketing efforts are primarily directed towards our existing clients through customer education efforts. We inform and educate our clients about pet wellness and quality care through mailings of the Healthy Pet Magazine, a magazine focused on pet care and wellness published by an affiliate of ours, targeted demographic mailings regarding specific pet health issues and collateral health material available at each animal hospital. With these internal marketing programs, we seek to leverage our existing customer base by increasing the number of visits of existing clients and intensity of the services used during each visit. Further, reminder notices are used to increase awareness of the advantages of regular, comprehensive veterinary medical care, including preventive care such as vaccinations, dental screening and geriatric care.

We also enter into referral arrangements with local pet shops and humane societies to increase our client base. In addition, we seek to obtain referrals from veterinarians by promoting our specialized diagnostic and treatment capabilities to veterinarians and veterinary practices that cannot offer their clients these services.

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Ownership Limitations. Some states have laws that prohibit business corporations from providing veterinary services through the direct employment of veterinarians. At December 31, 2001, we operated 54 animal hospitals in 11 states with these types of ownership restrictions. In these states, instead of owning an animal hospital, we provide management services to veterinary medical groups. We do not consolidate the operating results of these hospitals for financial statement purposes. We provide our management services pursuant to long-term management agreements with the veterinary medical groups, ranging from 10 to 40 years, with non-binding renewal options where allowable. Pursuant to the management agreements, the veterinary medical groups are each solely responsible for all aspects of the practice of veterinary medicine, as defined by their respective state. We are responsible for providing the following services:

- availability of all facilities and equipment;
- day-to-day financial and administrative supervision and management;
- maintenance of patient records;
- recruitment of veterinarians and animal hospital staff;
- marketing; and
- malpractice and general insurance.

As compensation for these services, we receive management fees, which are included in animal hospital revenue.

Systems

We maintain a nationwide management information system to support our veterinary laboratories. In 2000, we completed the migration of our animal hospital operations onto an enterprise-wide management information network. All of our financial and customer records and laboratory results are stored in computer databases, most of which may be accessed by our management. Substantially all of our animal hospitals utilize consistent patient accounting/point-of-sale software, and we are able to track the performance of hospitals on a per service, per veterinarian basis. Laboratory technicians and specialists are able to electronically access test results from remote testing sites, enabling our specialists from varying fields of veterinary medicine to assist in the interpretation of test results and help structure potential treatment programs. We expect that this operational visibility will lead to increases in laboratory, veterinarian and hospital productivity.

We are continuing to upgrade and integrate our management information systems. The upgrade of the laboratory system will enable us to communicate diagnostic test results to veterinarian customers online and via electronic mail, a service that we believe will provide additional tools for veterinarians in their practice and will help to solidify our relationship with these clients. The upgrade of the animal hospital system will allow us to track performance data on a per customer basis. We expect this upgrade and integration to be substantially complete in early 2002.

Competition

The companion animal health care services industry is highly competitive and subject to continual change in the manner in which services are delivered and providers are selected. We believe that the primary factors influencing a customer's selection of an animal hospital are convenient location, recommendation of friends, reasonable fees, quality of care and convenient hours. Our primary competitors for our animal hospitals in most markets are individual practitioners or small, regional multi-clinic practices. In addition, some national companies in the pet care industry, including the operators of super-stores, are developing multi-regional networks of animal hospitals in markets that include our animal hospitals. Among veterinary diagnostic laboratories, we believe that quality, price, specialist support and the time required to report results are the major competitive factors. Although there are many individual clinical laboratories that provide a broad range of diagnostic testing services in the same markets serviced by us, few outsourced laboratory companies compete on a national level. Our client base is twice that of our primary competitor in the laboratory business. In addition to competing with dedicated veterinary laboratories, we face competition from several providers of on-site diagnostic equipment that allow veterinarians to perform their own laboratory tests.

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Government Regulation

The laws of many states prohibit business corporations from providing, or holding themselves out as providers of, veterinary medical care. These laws vary from state to state and are enforced by the courts and by regulatory authorities with broad discretion. We operate 54 hospitals in 11 states with these laws. Although we seek to structure our operations to comply with veterinary medicine laws of each state in which we operate, given the varying and uncertain interpretations of these laws, we may not be in compliance with restrictions on the corporate practice of veterinary medicine in all states. A determination that we are in violation of applicable restrictions on the practice of veterinary medicine in any state in which we operate could have a material adverse effect on us, particularly if we were unable to restructure our operations to comply with the requirements of that state.

In addition, all of the states in which we operate impose various registration requirements. To fulfill these requirements, we have registered each of our facilities with appropriate governmental agencies and, where required, have appointed a licensed veterinarian to act on behalf of each facility. All veterinary doctors practicing in our clinics are required to maintain valid state licenses to practice.

Acquisitions may be subject to pre-merger or post-merger review by governmental authorities for antitrust and other legal compliance. Adverse regulatory action could negatively affect our operations through the assessment of fines or penalties against us or the possible requirement of divestiture of one or more of our operations.

Employees

At December 31, 2001, we had approximately 3,480 full-time-equivalent employees, including approximately 623 licensed veterinarians. None of our employees are a party to a collective bargaining agreement with the exception of our courier drivers in the State of New York. These employees are subject to a collective bargaining agreement expiring on July 10, 2003 with the Teamsters Local Union 813. We believe our employee relations to be good.

ITEM 2. PROPERTIES

Our corporate headquarters and principal executive offices are located in West Los Angeles, California, in approximately 30,000 square feet of leased space. As of March 15, 2002, we maintain leased and owned facilities at 231 other locations that house our animal hospitals and laboratories. We own 63 facilities and the remainder are leased. We believe that our real property facilities are adequate for our current needs.

ITEM 3. LEGAL PROCEEDINGS

The Ohio Attorney General's office filed a lawsuit on December 14, 1998, in the Franklin County Court of Common Pleas in the State of Ohio in which the state alleged that our management of a veterinary medical group licensed to practice veterinary medicine in that state violates the Ohio statute prohibiting business corporations from providing, or holding themselves out as providers of, veterinary medical care. On March 20, 2001, the trial court in the case entered summary judgment in favor of the State of Ohio and issued an order enjoining us from operating in the State of Ohio in a manner that is in violation of the state statute. In response, we have restructured our operations in the State of Ohio in a manner that we believe conforms to the state law and the court's order. The Attorney General of the State of Ohio informed us that it disagrees with our position that we are in compliance with the court's order. In June 2001, we appeared at a status conference before the trial court at which time the court directed the parties to meet together to attempt to settle this matter. Consistent with the trial court's directive, we engaged in discussions with the Attorney General's office in the State of Ohio. The parties appeared at an additional status conference in February 2002. The parties were not able to reach a settlement prior to the February status conference. At that status conference, the court ordered the parties to participate in a court-supervised settlement conference that was scheduled for March 19, 2002. The court postponed the settlement conference and has not yet scheduled a new date. Our five animal hospitals in the State of Ohio have a book value of \$6.1 million as of December 31, 2001. If we were required to discontinue our operations in the State of Ohio, we may not be able to dispose of the hospital assets for their book value. The animal hospitals located in the State of Ohio generated revenue and operating income of \$2.1 million and \$409,000, respectively, in the year ended December 31, 2001 and \$2.2 million and \$513,000, respectively, in the year ended December 31, 2000.

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On November 30, 2001, two majority stockholders of a company that merged with Zoasis.com, Inc. in June 2000 filed a civil complaint against us, Zoasis.com, Inc. and Robert Antin. In the merger, the two stockholders received a less than 10% interest in Zoasis.com, Inc. At the same time, we acquired a less than 20% interest in Zoasis.com, Inc. for an investment of \$5.0 million. Robert Antin, our Chief Executive Officer, President and Chairman of the Board, is the majority stockholder of Zoasis.com, Inc. and serves on its board of directors. The complaint alleges securities fraud under California law, common law fraud, negligent misrepresentation, and declaratory judgment arising from the plaintiffs' investment in Zoasis. On December 31, 2001, we filed a demurrer to the Complaint. On February 25, 2002, the plaintiffs filed an opposition to our demurrer and on March 1, 2002, we filed our Reply to plaintiff's opposition. On March 7, 2002, our demurrer was denied. On March 22, 2002, we filed an answer to plaintiff's complaint denying all allegations in the complaint, and we filed a counter claim alleging breach of contract and claim and delivery. We have responded to plaintiff's initial discovery request and the preparation of our initial discovery request is in process.

We are a party to various other legal proceedings that arise in the ordinary course of our business. Although we cannot determine the ultimate disposition of these proceedings, we do not believe that adverse determinations in any or all of these proceedings would have a material adverse effect upon our financial condition, liquidity or results of operations.

ITEM 4. SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS

On November 19, 2001, stockholders holding a majority of the outstanding shares of our common stock, series A redeemable preferred stock and series B redeemable preferred stock, voting separately, voted by written consent to adopt and approve our Amended and Restated Certificate of Incorporation.

PART II**ITEM 5. MARKET FOR REGISTRANT'S EQUITY AND RELATED STOCKHOLDER MATTERS**

Since November 27, 2001, our common stock has traded on the Nasdaq Stock Market's National Market under the symbol WOOF. From September 20, 2000 through November 26, 2001, our common stock was not publicly traded. From March 19, 1993 through September 20, 2000, our common stock was traded on the Nasdaq Stock Market's National Market under the symbol VCAI. The following table sets forth the range of high and low bid information per share for our common stock as quoted on the Nasdaq Stock Market's National Market for the periods indicated. All stock prices have been restated to reflect a fifteen-for-one stock split.

	<u>High</u>	<u>Low</u>
Fiscal 2000 by Quarter		
First	\$ 0.96	\$0.68
Second	0.93	0.83
Third (through September 19, 2000)	0.99	0.90
Fiscal 2001 by Quarter		
Fourth (commencing November 21, 2001)	12.45	8.83

At March 25, 2001, the closing price of the common stock on the Nasdaq Stock Market was \$13.45.

At March 25, 2001, there were approximately 107 holders of record of the Company's common stock.

Dividends

We have not paid cash dividends on our common stock, and we do not anticipate paying cash dividends in the foreseeable future. In addition, our credit facility and the indentures governing our outstanding senior and senior subordinated notes place limitations on our ability to pay dividends or make other distributions in respect of our common stock. Any future determination as to the payment of dividends on our common stock will be restricted by these limitations, will be at the discretion of our board of directors and will depend on our results of operations, financial

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condition, capital requirements and other factors deemed relevant by the board of directors, including the General Corporation Law of the State of Delaware, which provides that dividends are only payable out of surplus or current net profits.

Use of Proceeds from IPO

As a result of the initial public offering and the underwriters' exercise of its over-allotment, we issued 17,370,000 shares of common stock and received net proceeds of approximately \$161.5 million. Concurrent with our initial public offering, we issued \$170.0 million of 9.875% senior subordinated notes due 2009. We applied the net proceeds from our initial public offering and the sale of the notes, plus \$6.3 million of cash on hand, as follows:

redeemed all of the outstanding series A and series B redeemable preferred stock for \$173.8 million;

repaid \$100.0 million of bank debt;

repaid \$59.1 million in principal of the 15.5% senior notes due 2010, at a redemption price of 110%, plus accrued and unpaid interest; and

repaid \$5.0 million in principal of the 13.5% senior subordinated notes due 2010, at a redemption price of 110%, plus accrued and unpaid interest.

Equity Compensation Plan

The following table summarizes information about the securities and exercise price of securities available and outstanding as of December 31, 2001. For a description of these plans, please see Note 10 Stock-Based Compensation Plans in our consolidated financial statements.

Plan Category	Shares Acquired Upon Exercise of Outstanding Options	Weighted Average Exercise Price	Number of Shares Remaining Available for Future Issuance of Options
2001 Stock Incentive Plan, not approved by our stockholders			2,000,000
1996 Stock Incentive Plan, approved by our stockholders	633,795	\$ 1.00	

Lock-Up Agreements

In connection with our initial public offering, our directors, officers and other security holders executed lock-up agreements covering an aggregate of 21,366,081 shares of our common stock. The lock-up agreements prohibit the holders of these shares to sell, dispose of, loan, pledge or grant any rights to any of these shares without the prior written consent of Credit Suisse First Boston Corporation. These lock-up agreements expire May 20, 2002.

Recent Sales of Unregistered Securities

In February 1999, we granted to Robert Antin, Arthur Antin, Neil Tauber, Tomas Fuller, Dawn Olsen and other employees restricted stock bonus awards to purchase an aggregate of 1,428,435 shares of common stock. These stock bonus awards have all been exercised. These shares were issued in reliance on the exemption from registration provided by Section 4(2) of the Securities Act.

In January 2000, we granted to Robert Antin, Arthur Antin, Neil Tauber, Tomas Fuller, Dawn Olsen and other employees restricted stock bonus awards to purchase an aggregate of 4,785,645 shares of common stock. These stock bonus awards have all been exercised. These shares were issued in reliance on the exemption from registration provided by Section 4(2) of the Securities Act.

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As part of our recapitalization, on September 20, 2000 we made the following sales of unregistered securities:

Issued and sold 17,524,335 shares of our common stock at a per share purchase price of \$1.00 for an aggregate purchase price of \$17,524,335 to the following: Robert Antin, 1,906,380 shares; Arthur Antin, 400,005 shares; Neil Tauber, 49,995 shares; Tomas Fuller, 200,010 shares; certain entities controlled by Leonard Green & Partners, 14,336,112 shares; and certain of our employees, some of whom are accredited and some of whom are unaccredited, 631,833 shares. These securities were issued in reliance on the exemption from registration provided by Regulation D, Rule 506, of the Securities Act.

Issued and sold 2,998,408 shares of 14% series A senior redeemable exchangeable cumulative preferred stock at a per share purchase price of \$25.00 for an aggregate purchase price of approximately \$75,000,000 to the following: Green Equity Investors III, L.P. and affiliated investment funds, 2,826,000 shares; GS Mezzanine Partners II, L.P. and affiliated investment funds, 122,123 shares; TCW Leveraged Income Trust, L.P. and affiliated investment funds, 35,918 shares; and The Northwestern Mutual Life Insurance Company, 14,367 shares. These securities were issued in reliance on the exemption from registration provided by Regulation D, Rule 506, of the Securities Act.

Issued and sold 2,970,822 shares of 12% series B junior redeemable cumulative preferred stock at a per share purchase price of \$25.00 for an aggregate purchase price of approximately \$74,300,000 to the following: Green Equity Investors III, L.P. and affiliated investment funds, 2,800,000 shares; GS Mezzanine Partners II, L.P. and affiliated investment funds, 121,000 shares; TCW Leveraged Income Trust, L.P. and affiliated investment funds, 35,588 shares; and The Northwestern Mutual Life Insurance Company, 14,234 shares. These securities were issued in reliance on the exemption from registration provided by Regulation D, Rule 506, of the Securities Act.

Sold \$100.0 million in senior notes due 2010 pursuant to an indenture of the same date with Chase Manhattan Bank and Trust Company, National Association, as trustee, to the following: GS Mezzanine Partners II, L.P. and affiliated investment funds, \$70,834,000; TCW Leveraged Income Trust, L.P. and affiliated funds, \$20,833,000; and The Northwestern Mutual Life Insurance Company, \$8,333,000. In connection with the sale of the senior notes, VCA Antech issued warrants to purchase up to 1,149,990 shares of common stock to the following investors: GS Mezzanine Partners II, L.P. and affiliated investment funds, 814,575 warrants; TCW Leveraged Income Trust, L.P. and affiliated funds, 239,580 warrants; and The Northwestern Mutual Life Insurance Company, 95,835 warrants. The warrants allow the holders to purchase the common shares at a price of \$0.0007 on or before the closing of an initial public offering of our common stock. These securities were issued in reliance on the exemption from registration provided by Regulation D, Rule 506, of the Securities Act.

Sold \$20.0 million in senior subordinated notes due 2010 pursuant to an indenture of the same date with Chase Manhattan Bank and Trust Company, National Association, as trustee, to the following: GS Mezzanine Partners II, L.P. and affiliated investment funds, \$14,166,000; TCW Leveraged Income Trust, L.P. and affiliated funds, \$4,167,000; and The Northwestern Mutual Life Insurance Company, \$1,667,000. These securities were issued in reliance on the exemption from registration provided by Section 4(2) of the Securities Act.

On November 27, 2001, and concurrent with our initial public offering, we sold \$170.0 million in senior subordinated notes due 2009 pursuant to an indenture of the same date with Chase Manhattan Bank and Trust Company, National Association, as trustee, to the Goldman, Sachs & Co. These securities were issued in reliance on the exemption from registration provided by Regulation D, Rule 506, of the Securities Act.

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The selected historical consolidated financial data as of and for the years ended December 31, 2001, 2000, 1999, 1998, and 1997 have been derived from our audited financial statements. You should read the selected financial data presented below together with Management's Discussion and Analysis of Financial Condition and Results of Operations and our consolidated financial statements and related notes. Our audited consolidated financial statements as of December 31, 2001 and 2000 and for each of the three years in the period ended December 31, 2001 are included in this Annual Report on Form 10-K.

	Year Ended December 31,				
	2001	2000	1999	1998	1997
	(in thousands, except per share amounts)				
Statements of Operations Data:					
Laboratory revenue	\$ 134,711	\$ 119,300	\$ 103,282	\$ 89,896	\$ 68,997
Animal hospital revenue	272,113	240,624	217,988	191,888	165,848
Other revenue (1)	2,000	925	5,100	5,100	5,764
Intercompany	(7,462)	(6,162)	(5,810)	(5,845)	(4,696)
	<u>401,362</u>	<u>354,687</u>	<u>320,560</u>	<u>281,039</u>	<u>235,913</u>
Total revenue					
Direct costs	283,226	254,890	232,493	209,380	178,630
Selling, general and administrative	38,633	27,446	23,622	19,693	17,676
Depreciation and amortization	25,166	18,878	16,463	13,132	11,199
Agreement termination costs	17,552				
Recapitalization costs		34,268			
Year 2000 remediation expense			2,839		
Other non-cash operating items	9,079		(1,873)		
	<u>27,706</u>	<u>19,205</u>	<u>47,016</u>	<u>38,834</u>	<u>28,408</u>
Operating income					
Net interest expense	42,918	19,892	9,449	8,832	7,411
Other expense, net	168	1,800			
	<u>(15,380)</u>	<u>(2,487)</u>	<u>37,567</u>	<u>30,002</u>	<u>20,997</u>
Income (loss) before minority interest, provision for income taxes and extraordinary item					
Minority interest in income of subsidiaries	1,439	1,066	850	780	424
Provision for income taxes	445	2,199	14,360	12,954	9,347
Extraordinary loss on early extinguishment of debt (net of taxes)	10,159	2,659			
Increase in carrying amount of redeemable preferred stock	19,151	5,391			
	<u>\$ (46,574)</u>	<u>\$ (13,802)</u>	<u>\$ 22,357</u>	<u>\$ 16,268</u>	<u>\$ 11,226</u>
Net income (loss) available to common stockholders					
Basic earnings (loss) per share	\$ (2.39)	\$ (0.06)	\$ 0.07	\$ 0.05	\$ 0.04
Diluted earnings (loss) per share					