

VCA ANTECH INC  
Form 10-K  
March 01, 2013

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, 2012

or

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

Commission file number 001-16783

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  
(Address of principal executive offices)

90064-1022  
(Zip code)

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

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

Title of Each Class

Common Stock, par value \$0.001 per share

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 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 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 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.

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Large accelerated filer       Accelerated filer       Non-accelerated filer       Smaller reporting company   
(Do not check if a smaller reporting company)

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 voting common equity held by non-affiliates as of June 30, 2012, was approximately \$1.9 billion, computed by reference to the price of \$21.98 per share, the price at which the common equity was last sold on such date as reported on the NASDAQ Global Select Market. For purposes of this computation, it is assumed that the shares beneficially held by directors and officers of the registrant would be deemed to be stock held by affiliates. Non-affiliated common stock outstanding at June 30, 2012 was 84,455,024 shares. Total common stock outstanding at February 25, 2013 was 88,382,010 shares.

**DOCUMENTS INCORPORATED BY REFERENCE**

Parts of the definitive Proxy Statement to be delivered to stockholders in connection with the 2012 Annual Meeting of Stockholders are incorporated by reference into Items 10, 11, 12, 13 and 14 hereof.

VCA Antech, Inc. and Subsidiaries  
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## PART I

### ITEM 1. BUSINESS

#### Company Overview

We are a leading national animal healthcare company operating in the United States and Canada. We provide veterinary services and diagnostic testing to support veterinary care, we sell diagnostic imaging equipment and other medical technology products and related services to the veterinary market and we provide various communication, marketing solutions and other services to the veterinary community.

Our animal hospitals offer 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 health examinations, diagnostic testing, routine vaccinations, spaying, neutering and dental care. Our network of animal hospitals is supported by more than 3,000 veterinarians and had approximately 7.4 million patient visits in 2012. Our network of veterinary diagnostic laboratories provides sophisticated testing and consulting services used by veterinarians in the detection, diagnosis, evaluation, monitoring, treatment and prevention of diseases and other conditions affecting animals. Our network of veterinary diagnostic laboratories provides diagnostic testing for over 16,000 clients, which includes standard animal hospitals, large animal practices, universities and other government organizations. Our medical technology business sells digital radiography and ultrasound imaging equipment, provides education and training on the use of that equipment, and provides consulting and mobile imaging services. Our Vetstreet business, provides services to veterinary practices, pharmaceutical manufacturers, and the pet owning community. Our services to veterinary practices include subscriptions to our Pro Pet Portals. The Pro Pet Portal provides an online platform for the veterinarian to offer secure individualized portals for pet owners as well as practice websites that are branded to the individual veterinary clinic. We also sell appointment reminder notices that are sent to pet owners on behalf of their clinics. Our services to manufacturers predominately involve targeted marketing programs to animal hospitals whom are subscribers to our Pro Pet Portal.

Our principal executive offices are located at 12401 West Olympic Boulevard, Los Angeles, California. We can be contacted at (310) 571-6500.

#### Company History

Our company was formed in 1986 as a Delaware corporation and has since established a position in the animal healthcare industry through both internal growth and by acquisitions. By our twentieth anniversary in 2006 we operated a total of 379 animal hospitals, 33 laboratories, and a supplier of digital radiography and ultrasound imaging equipment. Subsequent to 2006, our company continued to grow by adding, additional laboratories, independent animal hospitals, animal hospital chains and other ancillary businesses, the following of which were noteworthy:

On June 1, 2007, we acquired Healthy Pet Corp. (“Healthy Pet”), which operated 44 animal hospitals and a small laboratory, which primarily serviced its own animal hospitals, as of the acquisition date. This acquisition allowed us to expand our animal hospital operations, particularly in Massachusetts, Connecticut, Virginia and Georgia.

On July 1, 2009, we acquired Eklin Medical Systems, Inc. (“Eklin”), a leading seller of digital radiography, ultrasound and practice management software systems in the veterinary market. We combined the operations of Eklin with our Sound Technologies, Inc (“STI”) business unit and the resulting combined company is the largest supplier of diagnostic imaging equipment and other medical technology products tailored specifically for the veterinary market.

On July 1 2010, we acquired Pet DRx Corporation (“Pet DRx”), which operated 23 animal hospitals as of the acquisition date. This acquisition allowed us to expand our animal hospital operations in California.

On July 11, 2011, we acquired BrightHeart Veterinary Centers (“BrightHeart”) which operated nine animal hospitals, eight of which focus on the delivery of specialty and emergency medicine. The acquisition will increase our level of market recognition in areas where we have an existing market presence.

On August 9, 2011, we acquired Vetstreet, Inc., formerly known as MediMedia Animal Health, LLC (“Vetstreet”), the nation’s largest provider of online communications, professional education and marketing solutions to the veterinary

community. The acquisition of Vetstreet expands the breadth of our product offerings to the veterinary community and is expected to provide long-term synergies to our existing businesses.

On January 31, 2012 we expanded our operations into Canada with an increased investment in Associate Veterinary Clinics (1984) Limited ("AVC"), which operates 44 hospitals in three Canadian provinces.

## Industry Overview

According to American Pet Products Association, Inc.'s ("APPA") 2011-2012 APPA National Pet Owners Survey, the United States population of companion animals is approximately 189 million, including about 165 million dogs and cats. APPA estimates that over \$30 billion was spent in the United States on pets in 2012 for veterinary care, supplies, medicine and boarding and grooming. The survey indicated that the ownership of pets is widespread with approximately 73 million, or 62%, of U.S. households owning at least one pet, including companion and other animals. Specifically, 46 million households owned at least one dog and 39 million households owned at least one cat. We believe that among pet owners there 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, diagnostic tests and equipment are becoming available to treat companion animals. These new and increasingly complex procedures, diagnostic tests, including laboratory testing and advanced imaging, and pharmaceuticals are gaining wider acceptance as pet owners are exposed to these previously unconsidered treatment programs through their exposure with this technology in human healthcare, and through literature and marketing programs sponsored by large pharmaceutical and pet nutrition companies. 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 healthcare industry, providers of veterinary services are not dependent on third-party payers in order to collect fees. As such, providers of veterinary services typically do not have the problems of extended payment collection cycles or pricing pressures from third-party payers faced by human healthcare providers. Outsourced laboratory testing and diagnostic equipment sales are wholesale businesses that collect payments directly from animal hospitals under standard industry payment terms. Fees for services provided in our animal hospitals are due at the time of service. In 2012, over 99% of our animal hospital services were paid at the time of service. In addition, over the past three fiscal years our bad debt expense has averaged less than 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.

## Animal Hospital Industry

Animal healthcare is provided predominately by the veterinarian practicing as a sole practitioner, or as part of a larger group practice 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 and hours, personal recommendations, reasonable fees and quality of care.

According to the American Veterinary Medical Association, the U.S. market for veterinary services is highly fragmented with more than 52,000 veterinarians practicing at the end of 2012. We have estimated that there are over 22,000 companion animal hospitals operating at the end of 2012. Although most animal hospitals are single-site, sole-practitioner facilities, we believe veterinarians are gravitating toward larger, multi-doctor 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 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;
- the purchasing, marketing and administrative cost advantages that can be realized by a large, multiple location, multi-doctor 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 performing the administrative tasks necessary to operate an animal hospital; and

the appeal to many veterinarians of the benefits and flexible work schedule that is not typically available to a sole practitioner or single-site provider.

#### Diagnostic Laboratory Industry

Veterinarians use laboratory tests to diagnose and monitor illnesses and conditions 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,

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laboratory diagnostic testing is becoming a routine diagnostic tool used by the veterinarian.

Veterinary laboratory tests are performed primarily at veterinary diagnostic laboratories, universities or at animal hospitals using on-site diagnostic equipment. For certain 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 or lease the equipment, maintain and calibrate the equipment periodically to avoid testing errors, employ trained personnel to operate it and purchase testing supplies. 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. Leading veterinary diagnostic laboratories also employ highly trained individuals who specialize in the detection and diagnosis of diseases and thus are a valuable resource for the veterinarian.

Our laboratories offer a broad spectrum of standard and customized tests to the veterinary market, 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 are likely to have a competitive advantage relative to smaller laboratories.

We believe that the outsourced laboratory testing market is an integral segment of the animal healthcare industry as a result of:

- 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 continued focus on wellness, early detection and monitoring programs in veterinary medicine.

#### Business Strategy

Our business strategy is to continue expanding our market leadership in animal healthcare through our Animal Hospital, Laboratory, Medical Technology and Vetstreet operating segments. Key elements to our strategy include: Capitalizing on our Leading Market Position to Generate Revenue Growth. Our leading market position in the animal hospital, veterinary laboratory and the online communications markets position us to capitalize on favorable growth trends in the animal healthcare industry. In our animal hospitals, we seek to generate revenue growth by capitalizing on the growing emphasis on pet health and wellness. In our laboratories, we seek to generate revenue growth by taking advantage of the growing number of outsourced diagnostic tests, the opportunities to expand the testing that we provide and by increasing our market share. We continually educate veterinarians on new and existing technologies and tests available to diagnose medical conditions. Further, we leverage the knowledge of our specialists by providing veterinarians with extensive client support in utilizing and understanding these diagnostic tests. Our Medical Technology business seeks to leverage our strengths in the broader veterinary markets by introducing technologies, products and services to the veterinary market. We seek to generate revenue growth by increasing our market share and educating veterinarians on new and existing technologies. In our Vetstreet business, we seek to generate revenue growth by capitalizing on the growing usage of online media to both aid pet owners in diagnosing illnesses and to purchase necessary medications and other pet related products.

Leveraging Established Infrastructure to Improve Margins. We intend to leverage our established Animal Hospital and Laboratory infrastructure 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 revenue from Animal Hospital and Laboratory 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.

Utilizing Enterprise-Wide Information Systems to Improve Operating Efficiencies. Our Laboratory and the majority of our Animal Hospital operations utilize enterprise-wide management information systems. We believe that these common systems enable us to more effectively manage the key operating metrics that drive our business. With the aid of these systems, we seek to standardize pricing, expand the services we provide and increase volume through targeted marketing programs.



Pursuing Selected Acquisitions. The fragmentation of the animal hospital industry provides us with significant expansion opportunities in our Animal Hospital segment. Depending upon the attractiveness of the candidates and the strategic fit with our existing operations, we intend to acquire independent animal hospitals each year with aggregate annual revenue of approximately \$50 million to \$85 million. Our overall acquisition strategy involves the identification of high-quality practices where we can create additional value through the services and scale we can provide. Our typical candidate mirrors the profile of our existing animal hospital base. These acquisitions will be used to both expand

existing markets and to enter into new geographic areas. In addition, we also evaluate the acquisition of animal hospital chains, laboratories or related businesses if favorable opportunities are presented. We intend primarily to use cash in our acquisitions but, depending on the timing and amount of our acquisitions, we may use stock or debt.

#### Business Segments

We report our results of operations through two reportable segments: Animal Hospital and Laboratory. Our Vetstreet and Medical Technology operating segments did not meet the materiality requirements to be presented as separate reportable segments. Accordingly, they are grouped into an “All Other” category.

Information regarding revenue and operating income, attributable to each of our reportable segments, is included in the Segment Results section within Management’s Discussion and Analysis of Financial Condition and Results of Operations, and within Note 15, Lines of Business, of our Notes to Consolidated Financial Statements, which are incorporated herein by reference.

#### Animal Hospital

At December 31, 2012, we operated 609 animal hospitals serving 41 states and three Canadian provinces. Our Animal Hospital revenue accounted for 78%, 77% and 76% of total consolidated revenue in 2012, 2011 and 2010, respectively.

#### Services

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 animal hospitals, including pet food, vitamins, therapeutic shampoos and conditioners, flea collars and sprays, and other accessory products.

#### Animal Hospital Network

We seek to provide quality care in clean, attractive facilities that are generally open between 10 to 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, freestanding facility in an attractive location;
- has annual revenue between \$1 million and \$3 million;
- is supported by three to five veterinarians; and
- has an operating history of over 10 years.

As of December 31, 2012, our network of freestanding, full-service animal hospitals had facilities located in the following states and three Canadian provinces:

California	110	Nevada	7
Texas*	48	Minnesota*	6
Washington*	33	New Mexico	6
Florida	30	Hawaii	6
New York*	30	Alaska	5
Massachusetts	27	Delaware	4
Pennsylvania	25	New Hampshire*	4
Illinois	19	Wisconsin	4
Virginia	19	South Carolina	4
Georgia	18	Missouri	3
Colorado	18	Nebraska*	3
Connecticut	16	Rhode Island*	3
Arizona	14	Louisiana*	2
New Jersey*	13	Vermont	2
Indiana	12	Kansas*	2
Ohio	12	Tennessee	2
Oregon*	12	Kentucky	1
Maryland	12	Alabama*	1
Michigan*	11	Utah	1
Oklahoma	8	West Virginia*	1
North Carolina*	8		
Alberta, Canada*	21		
British Columbia, Canada*	9		
Ontario, Canada*	17		

States and Canadian provinces with laws, rules and regulations which require that veterinary medical practices be owned by licensed veterinarians and that corporations which are not owned by licensed veterinarians refrain from providing, or holding themselves out as providers of, veterinary medical care. In these states/provinces we provide management and other administrative services to veterinary practices rather than owning such practices or providing such care.

#### Marketing

We direct our marketing efforts toward increasing the number of annual visits from existing clients through customer education efforts and toward attracting new clients to our network of hospitals through online and offline initiatives. We inform and educate our clients about pet wellness and quality care through mailings of HealthyPet Magazine, which focuses on pet care and wellness. We also market through targeted demographic mailings regarding specific pet health issues and collateral health material made available at each animal hospital. With these internal marketing programs, we seek to leverage our existing customer base by increasing the number and intensity of the services received during each visit. We send reminder notices to increase awareness of the advantages of regular, comprehensive veterinary medical care, including preventive care such as early disease detection exams, vaccinations, dental screening and geriatric care. We also have expanded our online capabilities both internally and through our acquisition of Vetstreet. Our internal efforts involve offering increased convenience for our clients to book appointments or find detailed health related materials on our hospital websites. We also enter into referral arrangements with local pet shops, humane societies and veterinarians to increase our client base. 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. Through our acquisition and integration of Vetstreet, we will be able to provide more robust health and wellness information to the pet owning community that we expect

will attract additional clients to both VCA and non-VCA hospitals.

Personnel

Our animal hospitals generally employ a staff of between 20 and 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, and a hospital manager who supervises the day-to-day activities of the facility.

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We actively recruit qualified veterinarians and technicians and are committed to supporting continuing education for our professional staff. We operate post-graduate teaching programs for veterinarians at 27 of our facilities, which train approximately 161 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 animal hospitals offer attractive employment opportunities to veterinarians because of our professional environment, competitive compensation, management opportunities, employee benefits not generally available to a sole practitioner, flexible work schedules that accommodate personal lifestyles and the ability to relocate to different regions of the country.

We have established a medical advisory board to support our operations. Our advisory board, under the direction of our Chief Medical Officer, recommends medical standards for our network of animal hospitals and is comprised of veterinarians recognized for their outstanding knowledge and reputations in the veterinary field. Our advisory board members represent both the different geographic regions in which we operate and the medical specialties practiced by our veterinarians; and three members are faculty members at highly-ranked veterinary colleges. Additionally, our regional medical directors, a group of highly experienced veterinarians, are also closely involved in the development and implementation of our medical programs.

#### Laboratory

We operate a full-service, veterinary diagnostic laboratory network serving all 50 states and certain areas in Canada. Our Laboratory revenue accounted for 16%, 18% and 20% of total consolidated revenue in 2012, 2011 and 2010, respectively. We service a diverse customer base of over 16,000 clients including animal hospitals we operate, which accounted for 16%, 14% and 12% of total Laboratory revenue in 2012, 2011 and 2010, respectively.

#### Services

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

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. We believe that the growing concern for animal health, combined with the movement of veterinary medicine toward increasing specialization, may result in the migration of additional areas of human testing into the veterinary field.

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 specialists to interpret test results to aid in the diagnosis of illnesses and to suggest possible treatment alternatives. Our diagnostic experts include veterinarians, chemists and other scientists with expertise in pathology, internal medicine, oncology, cardiology, dermatology, neurology and endocrinology. Because of our specialists involvement, we believe the quality of our service further distinguishes our laboratory services as a premiere service provider.

#### Laboratory Network

At December 31, 2012, we operated 55 veterinary diagnostic laboratories. Our laboratory network includes:

- primary hubs that are open 24 hours per day and offer a full-testing menu;
- secondary laboratories that are open 24 hours per day and offer a wide-testing menu servicing large metropolitan areas; and
- short-term assessment and treatment (“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, picking up requisitions daily through an extensive network of drivers and independent couriers. Customers outside our transportation network use FedEx to send specimens to our laboratory just outside of Memphis, Tennessee, which permits rapid and cost-efficient testing because of the proximity to the primary sorting facility of FedEx.

In 2012, we derived approximately 85% 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 day following pick-up.

#### Sales, Marketing and Client Service

Our full-time sales and field-service representatives market laboratory services and maintain relationships with existing customers. Our sales force is compensated via salary plus commission 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. Our client-service representatives respond to customer inquiries, provide test results and, when appropriate, introduce the customer to other services offered by the laboratory.

#### Personnel

Each of our primary and secondary laboratory locations includes a manager, supervisors for each department and personnel for laboratory testing. In addition, we employ or contract with specialists to interpret test results to assist veterinarians in the diagnosis of illnesses and to suggest possible treatment alternatives.

We actively recruit qualified personnel and are committed to supporting continuing education for our professional staff. We have internal training programs for routine testing procedures to improve the skill level of our technicians and to improve the overall capacity of our existing staff. We sponsor various internship and certain other educational programs. These programs serve to build awareness of our company with students, who may seek employment with our company following graduation.

#### Systems

We use an enterprise-wide management information system to support our Animal Hospital operations. We decide whether or not to place newly acquired animal hospitals on this network based on a cost-benefit analysis. In addition, a majority of our animal hospitals utilize consistent patient accounting/point-of-sale software and we are able to track performance of hospitals on a per-service, per-veterinarian and per-client basis.

We use an enterprise-wide management information system to support our veterinary laboratories. All of our financial data, customer records and laboratory results are stored in computer databases. Laboratory technicians and specialists are able to electronically access test results from remote testing sites. Our software gathers data in a data warehouse enabling us to provide expedient results via fax or through our Internet online resulting system.

#### Competition

The companion animal healthcare 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 and hours, personal recommendations, reasonable fees and quality of care. 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 networks of animal hospitals in markets that include our animal hospitals. We also compete with sellers of pet-related products and diagnostic services delivered via the Internet. As we progress in our integration of Vetstreet we expect to position ourselves and other independent animal hospitals to better compete in the online market.

Among veterinary diagnostic laboratories, we believe that quality, price, specialist support and the time required to deliver results are the major competitive factors. There are many clinical laboratories that provide a broad range of diagnostic testing services in the same markets serviced by us, and we also face competition from several providers of on-site diagnostic equipment that allows veterinarians to perform various testing. Our principal competitor in most geographic locations in the United States is IDEXX Laboratories.

Our Vetstreet business operates in the online communication, professional education and marketing business within the animal healthcare industry. We believe that the primary factors influencing a customer's selection of a company which provides services such as Vetstreet to be price, breadth of product offering and ease of integration with existing systems. The competitive landscape in this business changed during the latter part of 2012. Specifically, four competitors launched product offerings similar to Vetstreet's. We consider three of the four to be direct competitors. Vetstreet's main competition in this space is IDEXX, Demand Force, and ePet Health.





### Government Regulation

Certain states and provinces have laws, rules and regulations which require that veterinary medical practices be either wholly-owned or majority-owned by licensed veterinarians and that corporations which are not wholly-owned or majority-owned by licensed veterinarians refrain from providing, or holding themselves out as providers of, veterinary medical care. In these states and provinces, we provide management and other administrative services to veterinary practices rather than owning such practices or providing such care. We provide management and other administrative services to veterinary practices located in these states and provinces.

At December 31, 2012, we provided management and administrative services to 177 animal hospitals in 15 states, and 47 animal hospitals in three Canadian provinces, under a variety of ownership structures and/or management agreements with these veterinary practices. We consolidate these veterinary practices for financial reporting purposes. Although we have structured our operations to comply with our understanding of the veterinary medicine laws of each state and province in which we operate, interpretive legal precedent and regulatory guidance varies by jurisdiction and is often sparse and not fully developed. A determination that we are in violation of applicable restrictions on the practice of veterinary medicine in any jurisdiction in which we operate could have a material adverse effect on our operations, particularly if we were unable to restructure our operations to comply with the requirements of that jurisdiction.

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 veterinarians practicing in our animal hospitals are required to maintain valid state licenses to practice.

Our acquisitions may be subject to pre-merger or post-merger review by governmental authorities for anti-trust 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, 2012 we employed or managed on behalf of the professional corporations to which we provide services approximately 10,500 full-time-equivalent employees. At that date, none of these employees were a party to a collective bargaining agreement.

### Availability of Our Reports Filed with the Securities and Exchange Commission ("SEC")

We maintain a website with the address <http://investor.vcaantech.com>. We are not including the information contained on our website as a part of, or incorporating it by reference into, this annual report on Form 10-K. We make available free of charge through our website our annual reports on Form 10-K, quarterly reports on Form 10-Q and current reports on Form 8-K, and amendments to these reports, as soon as reasonably practicable after we electronically file that material with, or furnish that material to, the SEC.

The SEC maintains an Internet site that contains reports, proxy and information statements, and other information regarding issuers that file electronically with the SEC. Copies of our reports filed electronically with the SEC may be accessed on the SEC's website [www.sec.gov](http://www.sec.gov). The public may also read and copy any materials filed with the SEC at the SEC's Public Reference Room at 100 F Street NE, Washington, DC 20549. Information on the operation of the Public Reference Room may be obtained by calling the SEC at (800) SEC-0330.

## ITEM 1A. RISK FACTORS

Various sections of this annual report contain forward-looking statements, all of which are based on current expectations and could be affected by the uncertainties and risk factors described below and throughout this annual report. Our actual results may differ materially from these forward-looking statements.

Changes in the demand for our products and services could negatively affect our operating results.

The frequency of visits to our animal hospitals has declined and may continue to decline. We believe that the frequency of visits is impacted by consumer spending habits, which are affected by a number of factors, including among other things, prevailing economic conditions, levels of employment, salaries and wage rates, consumer confidence and consumer perception of economic conditions. Over the past several years these factors have caused consumer spending to deteriorate significantly and they may cause levels of spending to remain depressed for the

foreseeable future. Changes in consumer spending habits may cause pet owners to elect to skip or defer visits to veterinary hospitals, affect their willingness to approve certain diagnostic tests, comply with a treatment plan, forgo expensive treatment options, or defer treatment for their pets altogether. Additionally, the frequency of visits to our animal hospitals and the number of diagnostic tests performed by our laboratories, may be negatively impacted as a result of preventative care and better pet nutrition. Demand for vaccinations will be impacted in the future as protocols for vaccinations change. Our veterinarians establish their own vaccine protocols. Some of our

veterinarians have changed their protocols and others may change their protocols in light of recent and/or future literature. The demand for our products and services may also decline as a result of the eradication or substantial declines in the prevalence of certain diseases. Also, many pet-related products traditionally sold at animal hospitals have become more widely available in retail stores and other channels of distribution, including the Internet, resulting in a decline in demand for these products at our animal hospitals. All of the foregoing may result in a decrease in sales of our products and services, which could have a material adverse effect on our business, financial position, results of operations, and cash flows.

The significant competition in the companion animal healthcare industry could result in a decrease in our prices, an increase in our acquisition costs, a loss of market share and could materially affect our revenue and profitability. The companion animal healthcare industry is highly competitive with few barriers to entry. To compete successfully, we may be required to reduce prices, increase our acquisition and operating costs or take other measures that could have an adverse effect on our financial condition, results of operations, margins and cash flow. In addition, if we are unable to compete successfully, we may lose market share.

A significant component of our annual growth strategy includes the acquisition of independent animal hospitals. The competition for animal hospital acquisitions from small national and regional multi-clinic companies may cause us to increase the amount we pay to acquire additional animal hospitals and may result in fewer acquisitions than anticipated by our growth strategy. If we are unable to acquire a requisite number of animal hospitals annually or if our acquisition costs increase, we may be unable to effectively implement our growth strategy and realize anticipated economies of scale.

Some national companies in the pet care industry, including the operators of super-stores, are developing networks of animal hospitals in markets that include our animal hospitals; this may cause us to reduce prices to remain competitive. Reducing prices may have an adverse effect on our Animal Hospital revenue, alternatively not reducing prices may cause us to lose market share.

We compete with clinical laboratory companies in the same markets we service. These companies have acquired additional laboratories in the markets in which we operate and may continue their expansion, and aggressively “bundle” their products and services to compete with us. Increased competition may adversely affect our Laboratory revenue and margins. Several other national companies develop and sell on-site diagnostic equipment that allows veterinarians to perform their own laboratory tests. Growth of the on-site diagnostic testing market may have an adverse effect on our Laboratory revenue.

Our medical technology business is a leader in the market for medical imaging equipment in the animal healthcare industry. Our primary competitors are companies that are much larger than us and have substantially greater capital, manufacturing, marketing and research and development resources than we do, including companies such as Siemens Medical Systems, Philips Medical Systems and Canon Medical Systems. The success of our medical technology business, in part, is due to its focus on the veterinary market, which allows it to differentiate its products and services to meet the unique needs of this market. If this market receives more focused attention from these larger competitors, we may find it difficult to compete and as a result our revenues and operating margins from this business could decline.

If we are unable to effectively execute our growth strategy, we may not achieve our desired economies of scale and our profitability may decline.

Our success depends in part on our ability to increase our revenue and operating income through a balanced program of organic growth initiatives and selective acquisitions of established animal hospitals, laboratories and related businesses. If we cannot implement or effectively execute on this strategy, our results of operations will be adversely affected. Even if we effectively implement our growth strategy, we may not achieve the economies of scale that we have experienced in the past or that we anticipate occurring in the future. We experienced a decline in same-store revenue growth in our animal hospitals for ten consecutive quarters, which ended during 2011, when we experienced an increase in same-store revenue growth in our third and fourth quarters. Our Laboratory growth has also been affected and became negative during certain quarters of the three year period ending December 31, 2012. Our Animal Hospital same-store revenue, adjusted for differences in business days, has fluctuated between a decline of 3.2% and growth of 1.2% for 2008 through 2012. Our Laboratory internal revenue growth, adjusted for differences in billing

days, has fluctuated between 0% and 3.6% over the same years. Our internal growth may continue to fluctuate and may be below our historical rates. Any reduction in the rate of our internal growth may cause our revenue and operating income to decrease. Investors should not assume that our historical growth rates are reliable indicators of results in future periods.

Due to the fixed cost nature of our business, fluctuations in our revenue could adversely affect our gross profit, operating income and margins.

A substantial portion of our expense, particularly rent and personnel costs, are fixed and are based in part on expectations of revenue. We may be unable to reduce spending in a timely manner to compensate for any significant fluctuations in our revenue. Accordingly, shortfalls in revenue may adversely affect our gross profit, operating income and margins.

We may experience difficulties hiring skilled veterinarians due to shortages that could disrupt our business. From time to time we experience shortages of skilled veterinarians in some regional markets in which we operate animal hospitals which may require us to enhance wages and benefits to recruit and retain enough qualified veterinarians to adequately staff our animal hospitals. If our labor costs increase, we may not be able to raise our rates for our products and services to offset these increased costs. Our failure to recruit and retain qualified veterinarians, or to control our labor costs, could have a material adverse effect on our business, financial position, results of operations, and cash flows.

Any failure in our information technology systems, disruption in our transportation network or failure to receive supplies could significantly increase testing turn-around time, reduce our production capacity and otherwise disrupt our operations.

Our Laboratory operations depend on the continued and uninterrupted performance of our information technology systems and transportation network, including overnight delivery services provided by FedEx. Sustained system failures or interruption in our transportation network could disrupt our ability to process laboratory requisitions, perform testing, provide test results in a timely manner and/or bill the appropriate party. We could lose customers and revenue as a result of a system or transportation network failure. In addition, any change in government regulation related to transportation samples or specimens could also have an impact on our business.

Our computer systems are vulnerable to damage or interruption from a variety of sources, including telecommunications failures, electricity brownouts or blackouts, malicious human acts and natural disasters. Moreover, despite network security measures, some of our servers are potentially vulnerable to digital break-ins, computer viruses and similar disruptive problems. Despite the precautions we have taken, unanticipated problems affecting our systems could cause interruptions in our information technology systems. Our insurance policies may not adequately compensate us for any losses that may occur due to any failures in our systems.

Our Laboratory operations depend on a limited number of employees to upgrade and maintain its customized computer systems. If we were to lose the services of some or all of these employees, it may be time-consuming for new employees to become familiar with our systems, and we may experience disruptions in service during these periods.

Our operations depend, in some cases, on the ability of single source suppliers or a limited number of suppliers, to deliver products and supplies on a timely basis. Some of these suppliers are smaller companies with limited capital resources and some of the products that we purchase from these suppliers are proprietary, and, therefore, cannot be readily or easily replaced by alternative suppliers. We have in the past experienced, and may in the future experience, shortages of or difficulties in acquiring products and/or supplies in the quantities and of the quality needed. Shortages in the availability of products and/or supplies for an extended period of time will disrupt our ability to deliver products and provide services in a timely manner, could result in the loss of customers, and could have a material adverse impact on our results of operations.

Difficulties integrating new acquisitions may impose increased costs, loss of customers and a decline in operating margins and profitability and other risks that we may not anticipate.

Our success depends in part on our ability to timely and cost-effectively acquire, and integrate into our business, additional animal hospitals, laboratories and related businesses. In 2012, we acquired 79 animal hospitals, including 44 with the acquisition of AVC, one laboratory and ThinkPets. In 2011, we acquired 27 animal hospitals, including nine with the acquisition of BrightHeart, one laboratory and Vetstreet. In 2010, we acquired 50 animal hospitals, including 23 with the acquisition of Pet DRx. We expect to continue our animal hospital acquisition program and, if presented with favorable opportunities, we may acquire animal hospital chains, laboratories or related businesses. Our expansion into new territories and new business segments creates the risk that we will be unsuccessful in the integration of the acquired businesses that are new to our operations. Any difficulties in the integration process could result in increased expense, loss of customers and a decline in operating margins and profitability. In some cases, we have experienced delays and increased costs in integrating acquired businesses, particularly where we acquire a large number of animal hospitals in a single region at or about the same time. We also could experience delays in converting the systems of acquired businesses into our systems, which could result in increased staff and payroll expense to collect our results as well as delays in reporting our results, both for a particular region and on a

consolidated basis. Further, the legal and business environment prevalent in new territories and with respect to new businesses may pose risks that we do not anticipate and adversely impact our ability to integrate newly acquired operations. In addition, our field management may spend a greater amount of time integrating these new businesses and less time managing our existing businesses. During these periods, there may be less attention directed to marketing efforts or staffing issues, which could affect our revenue and expense. For all of these reasons, our historical success in integrating acquired businesses is not a reliable indicator of our ability to do so in the future. The carrying value of our goodwill and other intangible assets could be subject to an impairment write-down. At December 31, 2012, our consolidated balance sheet reflected \$1.3 billion of goodwill and \$94.8 million of other intangible assets, constituting a substantial portion of our total assets of \$2.1 billion at that date. We expect that the aggregate amount of goodwill and other intangible assets on our consolidated balance sheet will increase as a result of future acquisitions.

We continually evaluate whether events or circumstances have occurred that suggest that the fair value of our other intangible assets or each of our reporting units are below their respective carrying values. The determination that the fair value of our intangible assets or one of our reporting units is less than its carrying value would result in an impairment write-down. The impairment write-down would be reflected as expense and could have a material adverse effect on our results of operations during the period in which we recognize the expense.

Our estimated fair values are calculated in accordance with generally accepted accounting principles related to fair value and utilize valuation methods consisting primarily of discounted cash flow techniques, and market comparables, where applicable. These valuation methods involve the use of significant assumptions and estimates such as forecasted growth rates, valuation multiples, the weighted-average cost of capital, and risk premiums, which are based upon the best available market information and are consistent with our long-term strategic plans. We provide no assurance that forecasted growth rates, valuation multiples, and discount rates will not deteriorate or that we will not incur additional impairment charges. We will continue to analyze changes to these assumptions in future periods. We require a significant amount of cash to service our debt and expand our business as planned.

We have, and will continue to have, a substantial amount of debt. Our substantial amount of debt requires us to dedicate a significant portion of our cash flow from operations to service interest and principal payments on our debt, thereby reducing the funds available for use for working capital, capital expenditures, acquisitions and general corporate purposes.

Our failure to satisfy covenants in our debt instruments will cause a default under those instruments.

In addition to imposing restrictions on our business and operations, our debt instruments include a number of covenants relating to financial ratios and tests. Our ability to comply with these covenants may be affected by events beyond our control, including prevailing economic, financial and industry conditions. The breach of any of these covenants would result in a default under these instruments. An event of default would permit our lenders and other debtholders to declare all amounts borrowed from them to be due and payable, together with accrued and unpaid interest. If we are unable to repay debt to our senior lenders, these lenders and other debtholders could proceed against our assets.

Our debt instruments may adversely affect our ability to run our business.

Our substantial amount of debt, as well as the guarantees of our subsidiaries and the security interests in our assets and those of our subsidiaries, could impair our ability to operate our business effectively and may limit our ability to take advantage of business opportunities. For example, our senior credit facility may:

- limit our ability to borrow additional funds or to obtain other financing in the future for working capital, capital expenditures, acquisitions, investments and general corporate purposes;
- limit our ability to dispose of our assets, create liens on our assets or to extend credit;
  - make us more vulnerable to economic downturns and reduce our flexibility in responding to changing business and economic conditions;
- limit our flexibility in planning for, or reacting to, changes in our business or industry;
- place us at a competitive disadvantage to our competitors with less debt; and
- restrict our ability to pay dividends, repurchase or redeem our capital stock or debt, or merge or consolidate with another entity.

The terms of our senior credit facility allow us, under specified conditions, to incur further indebtedness, which would heighten the foregoing risks. If compliance with our debt obligations materially hinders our ability to operate our business and adapt to changing industry conditions, we may lose market share, our revenue may decline and our operating results may suffer.

Any failure by the manufacturers of our medical imaging equipment, failure in our ability to develop functional and cost-effective software for our products, or any product malfunctions could result in a decline in customer purchases and a reduction in our revenue and profitability.

We do not develop or manufacture the medical imaging equipment that we distribute, except for the software component of our digital radiography machines. Our business in large part is dependent upon distribution agreements with the manufacturers of the equipment, the ability of those manufacturers to produce desirable equipment and to keep pace with advances in technology, our ability to develop cost-effective, functional, and user-friendly software for

the digital radiography machines, and the overall rate of new development within the industry. If the distribution agreements terminate or are not renewed, if the manufacturers breach their covenants under these agreements, if the equipment manufactured by these manufacturers or our software becomes less competitive or if there is a general decrease in the rate of new development within the industry, demand for our products and services would decrease.



Manufacturing flaws, component failures, design defects, or inadequate disclosure of product-related information could result in an unsafe condition or injury. These problems could result in product liability claims and lawsuits alleging that our products have resulted or could result in an unsafe condition or injury. In addition, an adverse event involving one of our products could result in reduced market acceptance and demand for all of our products, and could harm our reputation and our ability to market our products in the future. Any of the foregoing problems could disrupt our business and have a material adverse effect on our business, results of operations, financial condition and cash flows.

Our use of self-insurance, self-insured retention and high-deductible insurance programs to cover certain claims for losses suffered and costs or expenses incurred could negatively impact our business upon the occurrence of an uninsured and/or significant event.

We self-insure and use high retention or high-deductible insurance programs with regard to property risks, general, professional and employment practice liabilities, health benefits, and workers' compensation. In the event that the frequency of losses we experience increases unexpectedly, the aggregate of those losses could materially increase our liability and adversely affect our cash flows and results of operations. In addition, we have made certain judgments as to the limits on our existing insurance coverage that we believe are in line with industry standards, as well as in light of economic and availability considerations. If we experience losses above these limits it could materially adversely affect our financial and business condition.

If we fail to comply with governmental regulations applicable to our business, various governmental agencies may impose fines, institute litigation or preclude us from operating in certain states.

Certain states and provinces have laws, rules and regulations which require that veterinary medical practices be owned by licensed veterinarians and that corporations which are not owned by licensed veterinarians refrain from providing, or holding themselves out as providers of, veterinary medical care. At December 31, 2012, we provided management and administrative services to 177 animal hospitals in 15 states and 47 animal hospital in three Canadian provinces, under management agreements with these veterinary practices, including 48 practices in Texas, 33 in Washington, and 30 in New York. We may experience difficulty in expanding our operations into other states or provinces with similar laws, rules and regulations. Although we have structured our operations to comply with our understanding of the veterinary medicine laws of each state and province in which we operate, interpretive legal precedent and regulatory guidance varies by jurisdiction and is often sparse and not fully developed. A determination that we are in violation of applicable restrictions on the practice of veterinary medicine in any jurisdiction in which we operate, could have a material adverse effect on us, particularly if we are unable to restructure our operations to comply with the requirements of that jurisdiction.

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 veterinarians practicing in our animal hospitals are required to maintain valid state licenses to practice.

Fluctuations in foreign currency exchange rates could adversely affect our operating results.

We are exposed to foreign currency fluctuation risk in Canada as we recently expanded our animal hospital operations and now operate 47 animal hospitals in three provinces, and operate four laboratories, that create market risk associated with changes in the value of the Canadian dollar. Currency exchange rates fluctuate on a daily basis as a result of a number of factors and cannot easily be predicted. To date, we have not hedged against foreign currency fluctuations; however, we may pursue hedging alternatives in the future. Our business, financial condition, operating results and cash flows therefore could be materially adversely affected by fluctuations in the exchange rate between the Canadian dollar and the U.S. dollar.

Our international operations may result in additional market risks, which may harm our business.

We operate over 40 animal hospitals and four laboratories in Canada as of December 31, 2012. As these operations grow, they may require greater management and financial resources. Internal operations require the integration of personnel with varying cultural and business backgrounds and an understanding of the relevant differences in the cultural, legal and regulatory environments. Our results may be increasingly affected by the risks of our international operations, including:

- Fluctuations in currency exchange rates;
- Changes in internal staffing and employment issues,
- Failure to understand the local culture and market, and
- The burden of complying with foreign laws, including tax laws and financial accounting standards.

Changes in regulations or user concerns regarding privacy and protection of user data could adversely affect our business.

Vetstreet offers e-commerce services to veterinary practices through the Pro Pet Portal, and engages in e-commerce through the Vetstreet.com website. Federal, state and international laws and regulations may govern the collection, use, retention, sharing and security of data that we receive from customers, visitors to the websites of our customers, and others. In addition, we have and post on our website our own privacy policy concerning the collection, use and disclosure of user data. Any failure, or perceived failure, by us to comply with our posted privacy policies or with any privacy-related laws, government regulations or directives, or industry self-regulatory principles could result in damage to our reputation, or proceedings or actions against us by governmental entities or otherwise, which could potentially have an adverse effect on our business.

**ITEM 1B. UNRESOLVED STAFF COMMENTS**

None.

**ITEM 2. PROPERTIES**

Our corporate headquarters and principal executive offices are located in Los Angeles, California, in approximately 50,000 square feet of leased space. At February 25, 2013, we leased or owned facilities at 715 other locations that house our animal hospitals, laboratories, our medical technology business, and our Vetstreet business. We own 147 facilities and the remainder are leased. We believe that our real property facilities are adequate for our current needs.

**ITEM 3. LEGAL PROCEEDINGS**

We are subject to legal proceedings and claims arising in the ordinary course of business. In the opinion of management, the ultimate disposition of these matters will not have a material adverse effect on our results of operations, financial condition or cash flows.

**ITEM 4. MINE SAFETY DISCLOSURES**

Not applicable.

## PART II

## ITEM 5. MARKET FOR REGISTRANT'S COMMON EQUITY, RELATED STOCKHOLDER MATTERS AND ISSUER PURCHASES OF EQUITY SECURITIES

Our common stock trades on the NASDAQ Global Select Market under the symbol "WOOF." The following table sets forth the range of high and low sales prices per share for our common stock as quoted on the NASDAQ Global Select Market for the periods indicated.

	High	Low
Fiscal 2012 by Quarter		
Fourth	\$21.44	\$18.42
Third	\$23.21	\$17.56
Second	\$26.00	\$20.04
First	\$23.41	\$19.22
Fiscal 2011 by Quarter		
Fourth	\$21.55	\$14.73
Third	\$22.09	\$15.00
Second	\$25.57	\$19.05
First	\$26.29	\$22.44

At February 25, 2013, there were 291 holders of record of our common stock.

The following graph sets forth the percentage change in cumulative total stockholder return on our common stock from December 31, 2007 to December 31, 2012. These periods are compared with the cumulative returns of the NASDAQ Stock Market (U.S. Companies) Index and the Russell 2000 Index. The comparison assumes \$100 was invested on December 31, 2007 in our common stock and in each of the foregoing indices. The stock price performance on the following graph is not necessarily indicative of future stock price performance.

\*\$100 invested on 12/31/07 in stock or index, including reinvestment of dividends. Fiscal year ending December 31.

	12/07	12/08	12/09	12/10	12/11	12/12
VCA Antech, Inc.	100.00	44.95	56.34	52.66	44.65	47.59
NASDAQ Composite	100.00	59.03	82.25	97.32	98.63	110.78
Russell 2000	100.00	66.21	84.20	106.82	102.36	119.09

#### 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 senior credit facility places limitations on our ability to pay cash dividends in respect of our common stock. Specifically, our senior credit facility dated August 16, 2011 prohibits us from declaring, ordering, paying, or setting apart any sum for any dividends or other distributions on account of any shares of any class of stock, other than dividends payable solely in shares of stock to holders of such class of 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 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.

#### Transactions in Our Equity Securities

For the period covered by this report, we have not engaged in any transactions involving the sale of our unregistered equity securities that were not disclosed in a quarterly report on Form 10-Q or a current report on Form 8-K. We have not engaged in any sales of registered securities for which the use of proceeds is required to be disclosed. This table provides certain information with respect to our purchases of shares of our common stock during the year ended December 31, 2012:

Period	Total Number of Shares Purchased <sup>(1)</sup>	Average Price Paid Per Share	Total Number of Shares Purchased as Part of Publicly Announced Plan	Approximate Dollar Value of Shares That May Yet Be Purchased Under the Plan
March 1, 2012 to March 31, 2012	27,477	\$22.61	—	\$—
May 1, 2012 to May 31, 2012	29,202	\$23.79	—	\$—
June 1, 2012 to June 30, 2012	106,701	\$20.53	—	\$—
August 1, 2012 to August 31, 2012	3,332	\$18.63	—	\$—
September 1, 2012 to September 30, 2012	18,347	\$20.19	—	\$—
November 1, 2012 to November 30, 2012	218,395	\$19.67	—	\$—
	403,454	\$20.90	—	\$—

<sup>(1)</sup> This column reflects the surrender to us of shares of common stock to satisfy minimum statutory tax withholding obligations in connection with the vesting of restricted stock and stock option awards issued to employees.

## ITEM 6. SELECTED FINANCIAL DATA

The following table provides our selected consolidated financial data as of and for each of the years in the five-year period ended December 31, 2012. The income statement and cash flow data and the other data for each of the three years ended December 31, 2012, and the balance sheet data as of December 31, 2012 and 2011 has been derived from our financial statements included elsewhere in this Form 10-K. The other periods presented were derived from our financial statements that are not included in this Form 10-K.

The selected financial data presented below is not necessarily indicative of results of future operations and should be read in conjunction with the Management's Discussion and Analysis of Financial Condition and Results of Operations section and our consolidated financial statements and related notes included elsewhere in this 10-K.

	December 31,				
	2012	2011	2010	2009	2008
	(in thousands, except per share amounts)				
Income Statement Data:					
Animal Hospital revenue <sup>(1)</sup>	\$1,331,314	\$1,150,120	\$1,052,462	\$994,215	\$959,395
Laboratory revenue	327,801	316,797	310,654	310,057	306,891
All Other revenue <sup>(2)</sup>	112,960	80,430	64,013	48,557	49,238
Intercompany revenue	(72,433 )	(61,986 )	(45,661 )	(38,322 )	(38,054 )
Total revenue	1,699,642	1,485,361	1,381,468	1,314,507	1,277,470
Direct costs	1,324,668	1,146,904	1,050,304	973,275	934,996
Gross profit	374,974	338,457	331,164	341,232	342,474
Selling, general and administrative expense <sup>(3)</sup>	157,155	121,112	123,541	95,669	90,564
Impairment of goodwill and other long-lived assets <sup>(4)</sup>	123,573	21,310	—	—	—
Net loss on sale of assets	1,310	382	374	4,035	234
Operating income <sup>(4)</sup>	92,936	195,653	207,249	241,528	251,676
Interest expense, net	16,552	16,884	13,630	21,466	28,559
Debt retirement costs	—	2,764	2,131	—	—
Business combination adjustment gain	(5,719 )	—	—	—	—
Other (income) expense	(488 )	118	(772 )	(104 )	(212 )
Income before provision for income taxes	82,591	175,887	192,260	220,166	223,329
Provision for income taxes <sup>(4)(5)</sup>	31,875	76,027	78,102	84,580	86,219
Net income	50,716	99,860	114,158	135,586	137,110
Net income attributable to noncontrolling interests	5,165	4,455	3,915	4,158	4,126
Net income attributable to VCA Antech, Inc	\$45,551	\$95,405	\$110,243	\$131,428	\$132,984
Basic earnings per share	\$0.52	\$1.10	\$1.28	\$1.54	\$1.57
Diluted earnings per share	\$0.51	\$1.09	\$1.27	\$1.53	\$1.55
Weighted-average shares outstanding for basic earnings per share	87,681	86,606	86,049	85,077	84,455
Weighted-average shares outstanding for diluted earnings per share	88,671	87,394	87,051	86,097	85,700

	December 31,					
	2012	2011	2010	2009	2008	
	(in thousands, except percentages)					
<b>Other Financial Data:</b>						
Consolidated gross margin	22.1	% 22.8	% 24.0	% 26.0	% 26.8	%
Animal Hospital gross margin	14.2	% 15.6	% 16.4	% 18.5	% 19.2	%
Laboratory gross margin	46.3	% 45.4	% 45.8	% 46.3	% 46.6	%
All Other gross margin	34.3	% 26.1	% 30.1	% 32.6	% 35.6	%
Consolidated operating margin <sup>(1)(4)</sup>	5.5	% 13.2	% 15.1	% 18.4	% 19.7	%
Animal Hospital operating margin	11.7	% 13.5	% 14.1	% 16.3	% 16.9	%
Laboratory operating margin	37.3	% 36.6	% 37.3	% 38.9	% 39.9	%
All Other operating margin <sup>(2)(4)</sup>	(108.2)	)% (24.2	)% 7.3	% 6.1	% 10.8	%
<b>Cash Flow Data:</b>						
Net cash provided by operating activities	\$237,253	\$191,051	\$168,073	\$183,471	\$197,308	
Net cash used in investing activities	\$(219,258 )	\$(271,310 )	\$(150,174 )	\$(130,760 )	\$(210,713 )	
Net cash (used in) provided by financing activities	\$(13,514 )	\$47,004	\$(66,142 )	\$3,467	\$(8,400 )	
Capital expenditures	\$(76,807 )	\$(63,485 )	\$(61,951 )	\$(50,801 )	\$(55,045 )	
<b>Balance Sheet Data (at period end):</b>						
Cash and cash equivalents	\$68,435	\$63,651	\$97,126	\$145,181	\$88,959	
Goodwill	\$1,291,231	\$1,237,607	\$1,092,480	\$985,674	\$922,057	
Total assets	\$2,091,580	\$1,995,368	\$1,766,422	\$1,627,404	\$1,449,038	
Long-term debt	\$630,643	\$618,853	\$527,036	\$545,055	\$552,631	
Total VCA Antech, Inc. stockholders' equity	\$1,183,503	\$1,107,878	\$998,924	\$875,047	\$710,989	

On January 31, 2012, we increased our investment in Associate Veterinary Clinics (1981) LTD ("AVC"),

<sup>(1)</sup> becoming the sole non-veterinary shareholder. Accordingly, we now consolidate their results into our own. At the time of the additional investment, AVC operated 44 animal hospitals.

On July 11, 2011, we acquired BrightHeart Veterinary Centers ("BrightHeart"), which operated nine animal hospitals as of the acquisition date.

On July 1, 2010, we acquired Pet DRx Corporation, which operated 23 animal hospitals as of the acquisition date.

On July 1, 2009, we acquired Eklin, a supplier of digital radiography equipment to the veterinary industry.

<sup>(2)</sup> On February 1, 2012, we acquired ThinkPet's, Inc. ("ThinkPets"), which was merged into our existing Vetstreet business. ThinkPets was previously a competitor of Vetstreet.

On August 9, 2011, we acquired Vetstreet, a provider of online communications, professional education and marketing solutions to the veterinary community.

On July 1, 2009, we acquired Eklin, a supplier of digital radiography equipment to the veterinary industry.

In 2010, our SG&A, operating income and operating margin were unfavorably impacted by a \$14.5 million accrual <sup>(3)</sup> related to consulting and Supplemental Executive Retirement Program ("SERP") amounts to be paid in accordance with consulting and SERP agreements entered into on June 30, 2010.

In 2012, our operating income and operating margin were unfavorably impacted by a \$123.6 million non-cash impairment charge. The charge was primarily attributable to impairment of our goodwill and intangible assets,

<sup>(4)</sup> related to our Vetstreet business, included in our All Other segments category. Our operating income was also impacted by a \$3.1 million out-of-period adjustment to depreciation expense related to our acquired capital leases.

These charges impacted our 2012 consolidated operating margin by 7.5%.

In 2011, our operating income and operating margin was unfavorably impacted by a \$21.3 million non-cash goodwill impairment charge, related to our medical technology business. The charge impacted our 2011 operating margin by



1.4%.

<sup>(5)</sup> The 2012 provision for income taxes was impacted by the tax effect of the impairment charge, mentioned above. The 2010 provision for income taxes includes the recognition of \$5.4 million, or \$3.5 million net of tax, related to

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additional state tax payments required as a result of a tax settlement reached.

#### ITEM 7. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

The following discussion should be read in conjunction with our consolidated financial statements provided under Part II, Item 8 of this annual report on Form 10-K. We have included herein statements that constitute forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995. We generally identify forward-looking statements in this report using words like "believe," "intend," "seek," "expect," "estimate," "may," "plan," "sl plan," "project," "contemplate," "anticipate," "predict," "potential," "continue," or similar expressions. You may find some of statements below and elsewhere in this report. These forward-looking statements are not historical facts and are inherently uncertain and outside of our control. Any or all of our forward-looking statements in this report may turn out to be wrong. They can be affected by inaccurate assumptions we might make or by known or unknown risks and uncertainties. Many factors mentioned in our discussion in this report will be important in determining future results. Consequently, no forward-looking statement can be guaranteed. Actual future results may vary materially. Factors that may result in these forward-looking statements in being different than reflected in this report are described throughout this annual report and particularly in "Risk Factors" Part I, Item 1A of this annual report on Form 10-K.

The forward-looking information set forth in this annual report on Form 10-K is as of March 1, 2013, and we undertake no duty to update this information. Shareholders and prospective investors can find information filed with the SEC after March 1, 2013, at our website at <http://investor.vcaantech.com> or at the SEC's website at [www.sec.gov](http://www.sec.gov).

##### Overview

We are a leading North American animal healthcare company. We provide veterinary services and diagnostic testing services to support veterinary care and we sell diagnostic imaging equipment and other medical technology products and related services to veterinarians. We also provide both online and printed communications, education and information, and analytical based marketing solutions to the veterinary community.

Our reportable segments are as follows:

Our Animal Hospital segment operates the largest network of freestanding, full-service animal hospitals in the nation. Our animal hospitals offer a full range of general medical and surgical services for companion animals. We treat diseases and injuries, offer pharmaceutical and retail products and perform a variety of pet wellness programs, including health examinations, diagnostic testing, routine vaccinations, spaying, neutering and dental care. At December 31, 2012, our animal hospital network consisted of 609 animal hospitals in 41 states and three Canadian provinces.

Our Laboratory segment operates the largest network of veterinary diagnostic laboratories in the nation. Our laboratories provide sophisticated testing and consulting services used by veterinarians in the detection, diagnosis, evaluation, monitoring, treatment and prevention of diseases and other conditions affecting animals. At December 31, 2012, our laboratory network consisted of 55 laboratories serving all 50 states and certain areas in Canada.

Our "All Other" category includes the results of our Medical Technologies and Vetstreet operating segments. Each of these segments did not meet the materiality thresholds to be reported individually.

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 flea infestation, heartworms and ticks, and the number of daylight hours.

##### Executive Overview

The slow economic recovery continues to have an adverse impact on our organic revenue growth and our profitability. Consumer spending habits, including spending for pet healthcare, are affected by, among other things, prevailing economic conditions, levels of employment, salaries and wage rates, consumer confidence and consumer perception of economic conditions. These factors continue to impact consumer spending and may continue to cause levels of spending to remain depressed for the foreseeable future. Additionally, these factors may cause pet owners to elect to defer expensive treatment options or to forgo treatment for their pets altogether. During 2010, continuing through 2012, we experienced a decline in the number of visits to our animal hospitals and the number of orders placed.

During 2012, we saw gradual improvement in our Animal Hospital same-store revenue and number of visits as well as

improvement in our Laboratory internal revenue growth, requisitions, and related gross profit margin. Our consolidated gross profit margin however, still declined due to deleveraging as a result of increased labor costs in our Animal Hospital segment and lower gross profit margins on our acquired businesses.

We believe that our ability to maintain or increase margins in 2013 will be dependent on organic revenue growth rates.

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We plan to continue our growth strategy of acquiring individual animal hospitals and maintain our strong emphasis on expense management. However, our ability to return to our historical margins will be dependent on increases in same-store revenue growth in our animal hospitals and successful integration of our acquired businesses.

#### Financing Transaction

On January 25, 2012 we amended our Amended and Restated Credit and Guaranty Agreement, dated as of August 16, 2011. The amendment replenishes the aggregate amount of uncommitted incremental facilities available under our senior credit facility to a maximum of \$100 million, after giving effect to the funding of \$50 million of new term loan commitments on January 24, 2012, which were drawn in connection with the additional investment made in Associate Veterinary Clinics (1981) LTD ("AVC"), detailed below.

#### Goodwill and Other Intangible Asset Impairments

Following our October 31, 2012 annual impairment test, we recorded a goodwill and other intangible assets impairment charge in our Vetstreet reporting unit of \$122.4 million, \$78.5 million net of tax or \$0.89 per diluted share. We significantly lowered our revised forecasted cash flows for the Vetstreet reporting unit primarily as a result of continued operational delays in part due to our upgrading and migration of Vetstreet's information technology systems from their former parent MediMedia, to their own Corporate data center, and less than anticipated financial performance for fiscal 2012, including with respect to revenue and operating cash flow. Our revised forecasted cash flows were also lowered related to a change in Vetstreet's overall business strategy and to reflect the impact of increased competition. These cumulative changes to our financial projections reduced the estimated fair value of the reporting unit, its goodwill and other long-lived assets below its carrying value at October 31, 2012.

#### Acquisitions

Our annual growth strategy includes the acquisition of independent animal hospitals. In addition, we also evaluate the acquisition of animal hospital chains, laboratories or related businesses if favorable opportunities are presented. In 2012, we acquired 35 independent animal hospitals with annual revenue of \$83.5 million and increased our investment in a chain of 44 animal hospitals with annual revenue of \$93.8 million. The following table summarizes the changes in the number of facilities operated by our Animal Hospital and Laboratory segments:

	For the Years Ended		
	December 31,		
	2012	2011	2010
Animal hospitals:			
Beginning of period	541	528	489
Acquisitions, excluding AVC in 2012, BrightHeart in 2011 and Pet DRx in 2010 <sup>(1)</sup>	35	18	27
AVC	44	—	—
BrightHeart	—	9	—
Pet DRx	—	—	23
New facilities	1	—	—
Acquisitions relocated into our existing animal hospitals	(6	) (3	) (2
Sold, closed or merged	(6	) (11	) (9
End of period	609	541	528
Laboratories:			
Beginning of period	53	50	47
Acquisitions	1	1	—
New facilities	2	2	4
Closed or merged	(1	) —	(1
End of period	55	53	50

(1) We increased our investment in AVC on January 31, 2012, BrightHeart Veterinary Centers ("BrightHeart") was acquired on July 11, 2011 and Pet DRx Corporation ("Pet DRx") was acquired on July 1, 2010.

Pet DRx Acquisition

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On July 1, 2010, we acquired a 70.4% interest in Pet DRx, a provider of veterinary primary care and specialized services to companion animals. Pet DRx operated 23 animal hospitals in California at the time of its acquisition. The acquisition has expanded our presence in the California market. We acquired the remaining interest in Pet DRx on November 1, 2010. The aggregate purchase price for both steps was \$41.3 million. Our consolidated financial statements reflect the operating results of Pet DRx since July 1, 2010.

#### BrightHeart Acquisition

On July 11, 2011, we acquired 100% of the membership interests of BrightHeart for approximately \$50 million in cash. BrightHeart operates nine animal hospitals, eight of which focus on the delivery of specialty and emergency medicine. The acquisition has increased our level of market recognition in areas where we have an existing market presence. At the time of the acquisition BrightHeart had annualized revenue of approximately \$53.4 million. Our consolidated financial statements reflect the operating results of BrightHeart since July 11, 2011.

Vetstreet, Inc., formerly known as MediMedia Animal Health, LLC (“Vetstreet”)

On August 9, 2011, we acquired Vetstreet, a provider of online communications, professional education and marketing solutions to the veterinary community. The acquisition of Vetstreet expanded the breadth of our product offerings to the veterinary community and is expected to provide long-term synergies to our existing businesses. We acquired Vetstreet for \$146.4 million, net of cash acquired. At the time of the acquisition Vetstreet had annualized revenue of approximately \$23.0 million. Our consolidated financial statements reflect the operating results of Vetstreet since August 9, 2011.

#### AVC Investment

On January 31, 2012, we increased our investment in AVC by approximately CDN \$81 million (approximately US \$81 million) becoming the sole non-veterinarian shareholder of AVC. At the time of the additional investment, AVC operated 44 animal hospitals in three Canadian provinces, offering services ranging from primary care, to specialty referral services and 24-hour emergency care. This investment and planned additional investments in AVC will facilitate our continued expansion in the Canadian market. At the time of the investment, AVC had annualized revenue of approximately CDN \$95 million (approximately US \$95 million). Our consolidated financial statements reflect the operating results of AVC since January 31, 2012.

#### ThinkPets

On February 1, 2012, we acquired 100% interest in ThinkPets for \$21 million, payable by delivery of 473,389 shares of VCA common stock and \$10.5 million in cash. We merged the business of ThinkPets with Vetstreet, which we expect will improve the products and services it offers to clients of both companies. Our consolidated financial statements reflect the operating results of ThinkPets since February 1, 2012.

#### Critical Accounting Policies and Estimates

We believe that the application of the following accounting policies, which are important to our financial position and results of operations, require significant judgments and estimates on the part of management. For a summary of all our accounting policies, including the accounting policies discussed below, see Note 2, Summary of Significant Accounting Policies, in our consolidated financial statements of this annual report on Form 10-K.

#### Revenue

Generally, we recognize revenue when persuasive evidence of a sales arrangement exists, delivery of goods has occurred or services have been rendered, the sales price or fee is fixed or determinable and collectability is reasonably assured.

We also generate revenue from the sale of digital radiography and ultrasound imaging equipment. We also generate revenue from: (i) licensing software; (ii) providing technical support and product updates on a when-and-if available basis related to our software, otherwise known as maintenance; (iii) providing professional services related to our equipment and software, including installations, on-site training, education services and extended warranty programs; and (iv) providing mobile imaging services. We frequently sell equipment and license our software in multiple element arrangements in which the customer may choose a combination of our products and services.

The accounting for the sale of equipment and the sale of software licenses and related items is substantially governed by the requirements of the Financial Accounting Standards Board (“FASB”) general revenue recognition rules. The

determination of the amount of software license, maintenance and professional service revenue to be recognized in each accounting period requires us to exercise judgment and use estimates. In determining whether or not to recognize revenue, we evaluate each of these criteria:

Evidence of an arrangement: We consider a non-cancelable agreement signed by the customer and us to be evidence

of an arrangement.

**Delivery:** We consider delivery to have occurred when the ultrasound imaging equipment is delivered. We consider delivery to have occurred when the digital radiography imaging equipment, including software, is delivered or accepted by the customer if installation is required. We consider delivery to have occurred with respect to professional services when those services are provided or on a straight-line basis over the service contract term, based on the nature of the service or the terms of the contract.

**Fixed or determinable fee:** We assess whether fees are fixed or determinable at the time of sale and recognize revenue if all other revenue recognition requirements are met. We generally consider payments that are due within six months to be fixed or determinable based upon our successful collection history. We only consider fees to be fixed or determinable if they are not subject to refund or adjustment.

**Collection is deemed reasonably assured:** We conduct a credit review for all significant transactions at the time of the arrangement to determine the credit worthiness of the customer. Collection is deemed reasonably assured if we expect that the customer will be able to pay amounts under the arrangement as payments become due. If we determine that collection is not reasonably assured, we defer the revenue and recognize the revenue upon cash collection.

#### Digital Radiography Imaging Equipment

We sell our digital radiography imaging equipment with multiple elements, including hardware, software licenses and/or services. Tangible products containing software components and nonsoftware components that function together to deliver the tangible product's essential functionality are accounted for under the FASB's accounting guidance pertaining to multiple-deliverable revenue arrangements.

Under the guidance sales arrangement consideration is allocated at the inception of the arrangement to all deliverables using the relative selling price method, whereby any discount in the arrangement is allocated proportionally to each deliverable on the basis of each deliverable's selling price. The selling price for each deliverable is based on vendor-specific objective evidence ("VSOE") if available, third-party evidence ("TPE") if VSOE is not available, or estimated selling price ("ESP") if neither VSOE nor TPE is available. For elements where VSOE is available, VSOE of fair value is based on the price for those products and services when sold separately by us or the price established by management with the relevant authority. TPE of selling price is the price of our, or any of our competitor's, largely interchangeable products or services in stand-alone sales to similarly situated customers. We do not currently have VSOE for our DR imaging equipment as units are not sold on a stand-alone basis without the related support packages. As this is also true for our competitors, TPE of selling price is also unavailable. We therefore use the ESP to allocate the arrangement consideration related to our DR imaging equipment.

We recognize revenue when the services are provided or at the time of delivery or installation and customer acceptance. Generally, at the time of delivery and installation of equipment the only undelivered item is the post-contract customer support ("PCS"). This obligation is contractually defined in both terms of scope and period. For the PCS, we recognize the revenue for these services on a straight-line basis over the period of support and we expense the costs of these services as they are incurred.

#### Ultrasound Imaging Equipment

We sell our ultrasound imaging equipment on a stand-alone basis and with multiple elements, including hardware, software, licenses and/or services. We account for the sale of ultrasound imaging equipment on a stand-alone basis under the requirements of the FASB's general revenue recognition rules and recognize revenue upon delivery. We allocate revenue for the sale of ultrasound imaging equipment with related computer hardware and software pursuant to the requirements of the FASB's Revenue Recognition — Multiple-Element Arrangements guidance.

#### Digital Radiography and Ultrasound Imaging Equipment Sold Together

In certain transactions we sell our ultrasound imaging equipment and related services together with our digital radiography imaging equipment and related services. In these transactions, each element is allocated revenue pursuant to the FASB's Revenue Recognition — Multiple-Element Arrangements guidance.

#### Other Services

We recognize revenue on mobile imaging, consulting and education services at the time the services have been rendered. We also generate revenue from extended service agreements related to our digital radiography imaging and ultrasound imaging equipment. These extended service agreements include technical support, product updates for



software on a when and if available basis and extended warranty coverage. The revenue for these extended service agreements is recognized on a straight-line basis over the term of the agreement. In certain transactions we sell bundled services to pharmaceutical companies, which primarily include pet portal subscriptions and several different forms of advertising. These items are accounted for in accordance with the FASB's accounting guidance pertaining to multiple element arrangements as discussed above. However,

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we do not generally have VSOE or TPE for any of these types of transactions, accordingly we allocate the arrangement consideration to each deliverable based upon ESP.

#### Valuation of Goodwill and Other Intangible Assets

##### Goodwill

We allocate a significant portion of the purchase price for our acquired businesses to goodwill. Our goodwill represents the excess of the cost of an acquired entity over the net of the amounts assigned to identifiable assets acquired and liabilities assumed. The total amount of our goodwill at December 31, 2012 was \$1.3 billion, consisting of \$1.2 billion for our Animal Hospital reporting unit, \$96.9 million for our Laboratory reporting unit, \$8.2 million for our Medical Technology reporting unit, and \$8.8 million for our Vetstreet reporting unit.

We test our goodwill for impairment annually, or sooner if circumstances indicate impairment may exist, in accordance with goodwill guidance. We adopted the end of October as our annual impairment testing date, which allows us time to accurately complete our impairment testing process in order to incorporate the results in our annual financial statements and timely file those statements with the Securities and Exchange Commission (“SEC”) in accordance with our accelerated filing requirements. Following our October 31, 2012 goodwill impairment testing, we determined that goodwill related to our Vetstreet reporting unit was impaired. Accordingly, we recorded a \$122.4 million goodwill and long-lived asset impairment charge for the fiscal year ended December 31, 2012. As a result of the October 31, 2011 goodwill impairment testing, we determined that the goodwill related to our Medical Technology reporting unit was impaired. Accordingly, we recorded a \$21.3 million goodwill impairment charge for the fiscal year ended December 31, 2011. There was no impairment charge resulting from the October 31, 2010 impairment tests. No events have occurred subsequent to the 2012 testing date which would indicate any further impairment may have occurred in any of our reporting units.

The recognition and measurement of a goodwill impairment loss involves either a qualitative assessment of the fair value of each reporting unit or a more detailed two-step process. We have not presently elected to rely on a qualitative assessment, accordingly we measure our goodwill for impairment based upon the following two-step process:

First we identify potential impairment by comparing the estimated fair value of our reporting units with the carrying value of our reporting units, with carrying value defined as the reporting unit’s net assets, including goodwill. If the estimated fair value of our reporting units is greater than our carrying value, there is no impairment and the second step is not needed.

If we identify a potential impairment in the first step, we then measure the amount of impairment. The amount of the impairment is determined by allocating the estimated fair value of the reporting unit as determined in step one to the reporting unit’s net assets based on fair value as would be done in an acquisition. In this hypothetical purchase price allocation, the residual estimated fair value after allocation to the reporting units’ identifiable net assets is the implied current fair value of goodwill. If the implied current fair value of goodwill is less than the carrying amount of goodwill, goodwill is considered impaired and written down to the implied current fair value with a corresponding charge to earnings. However, if the implied current fair value of goodwill is greater than the carrying amount of goodwill, goodwill is not considered impaired and is not adjusted to the implied current fair value. Determining the fair value of the net assets of our reporting units under this step requires significant estimates.

Our estimated fair values are calculated in accordance with generally accepted accounting principles related to fair value and utilize generally accepted valuation techniques consisting primarily of discounted cash flow techniques and market comparables, where applicable. These valuation methods involve the use of significant assumptions and estimates such as forecasted growth rates, valuation multiples, the weighted-average cost of capital, and risk premiums, which are based upon the best available market information and are consistent with our long-term strategic plans.

In 2011, we recorded an impairment charge in our Medical Technology reporting unit reflecting changes in our estimate of forecasted cash flows. This reporting unit’s remaining goodwill is \$8.2 million.

In 2012, we recorded an impairment charge in our Vetstreet reporting unit reflecting changes in our estimate of forecasted cash flows related to continued operational delays in part due to our upgrading and migration of Vetstreet's information technology systems from their former parent MediMedia, to their own Corporate data center, less than anticipated financial results for the 2012 fiscal year, the negative impact of increasing competition and a related

overall change in business strategy to better compete in the marketplace. The Vetstreet reporting unit's remaining goodwill is \$8.8 million. Our Animal Hospital and Medical Technology reporting units which have \$1.2 billion and \$8.2 million of goodwill, respectively, exceeded their respective carrying values by 13% and 17%, respectively, while our Laboratory reporting unit exceeded its carrying value by a more substantial margin.

Negative changes in the undiscounted cash flows related to variables such as revenue growth rates, margins, or the discount rate could result in a decrease in the estimated fair value of our reporting units and could ultimately result in a substantial goodwill impairment charge. The performance of our reporting units, and in turn the risk of goodwill impairment, is subject to a number of risks and uncertainties, some of which are outside of our control.

#### Other Intangible Assets

In addition to goodwill, we acquire other identifiable intangible assets in our acquisitions, including but not limited to covenants-not-to-compete, client lists, lease related assets and customer relationships. We value these identifiable intangible assets at estimated fair value. Our estimated fair values are based on generally accepted valuation techniques such as market comparables, discounted cash flow techniques or costs to replace. These valuation methods involve the use of significant assumptions such as the timing and amount of future cash flows, risks, appropriate discount rates, and the useful lives of intangible assets.

Subsequent to acquisition, we test our identifiable intangible assets for impairment as part of a broader test for impairment of long-lived assets under the FASB's accounting guidance whenever events or changes in circumstances indicate that the carrying value may not be recoverable. The recognition and measurement of an impairment loss under the FASB's accounting guidance also involves a two-step process:

First we identify potential impairment by estimating the aggregate projected undiscounted future cash flows associated with an asset or asset group and compare that amount with the carrying value of those assets. If the aggregate projected cash flow is greater than our carrying amount, there is no impairment and the second step is not needed.

If the estimated aggregate projected undiscounted future cash flows associated with an asset or asset group is less than the carrying value, we then write the assets or asset group down to the estimated fair value with a corresponding charge to earnings. If the estimated fair value is greater than carrying value, there is no adjustment. We may be required to make significant estimates in determining the fair value of some of our assets or asset groups.

In conjunction with our year-end review, we recorded long-lived intangible asset impairment of \$22.9 million related to the aforementioned Vetstreet business. The intangibles consisted of technology, customer relationships, trademarks and certain other contracts.

#### Capitalized Software Costs

We capitalize certain software costs in accordance with FASB's guidance on internal-use software. In accordance with the capitalization criteria of the accounting guidance, we capitalize external direct costs of materials and services consumed in developing and obtaining internal-use computer software and the payroll-related costs of employees who devote time directly to the internal use computer software project during the application development stage.

Management's judgment is required in determining the point at which various projects enter the stages at which costs may be capitalized, in assessing the ongoing value of the capitalized costs, and in determining the estimated useful lives over which the costs are amortized. We typically estimate a useful life of three years for our internal-use software.

#### Income Taxes

We account for income taxes under the FASB's accounting guidance for income taxes. We record deferred tax liabilities and deferred tax assets, which represent taxes to be settled or recovered in the future. We adjust our deferred tax assets and deferred tax liabilities to reflect changes in tax rates or other statutory tax provisions. Changes in tax rates or other statutory provisions are recognized in the period the enactment occurs.

We make judgments in assessing our ability to realize future benefits from our deferred tax assets, which includes operating loss carryforwards. We believe that our earnings during the periods when the temporary differences become deductible will be sufficient to realize the related future tax benefits. Should we determine that we would not be able to realize all or a portion of our deferred tax assets, an adjustment would be made to the carrying amount through a valuation allowance.

Also, our net deductible temporary differences and tax carryforwards are recorded using the enacted tax rates expected to apply to taxable income in the periods in which the deferred tax liability or asset is expected to be settled or realized. At December 31, 2012, we have a net deferred tax liability of \$53.3 million. Should the expected applicable tax rates change in the future, an adjustment to the net deferred tax liability would be credited or charged, as appropriate, to income in the period such determination was made. For example, an increase of 1.0% in our income tax rate would cause us to increase our net deferred tax liability balance by \$1.3 million with a corresponding charge to earnings.

We also assess differences between our tax bases, which are more likely than not to be realized, and the as-filed tax bases of certain assets and liabilities. We account for unrecognized tax benefits in accordance with the FASB's accounting guidance on income taxes, which prescribe a minimum probability threshold that a tax position must meet before a financial statement benefit is recognized. The minimum threshold is defined as a tax position that is more likely than not to be sustained upon examination by the applicable taxing authority, including resolution of any related appeals or litigation, based solely on the technical merits of the position. The tax benefit to be recognized is measured as the largest amount of benefit that is greater than 50% likely of being realized upon ultimate settlement. We did not have any unrecognized tax benefits on December 31, 2012.

Self-Insured Liabilities

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We self-insure and use high retention or high-deductible insurance programs for certain losses related to workers' compensation and employee health claims. Our self-insured liabilities contain uncertainties because we are required to make assumptions and to apply judgment to estimate the ultimate cost to settle reported claims and claims incurred but not reported as of the balance sheet date. We have not made any material changes in the reserving methodology used to establish our self-insured liabilities during the past three years.

#### Workers' Compensation Insurance

A portion of our workers' compensation insurance policies are self-insured high retention annual policies that begin on October 1st. The policies cover specific annual periods and are normally open for no longer than seven years after the period allowing claims for incidents occurring during the covered period to be submitted after the end of the policy year.

Under our workers' compensation insurance policies, we are responsible for the first \$250,000 in claim liability per individual occurrence and we are also subject to an aggregate limit. We use an internal review process to estimate claim liability based on actual and expected claims incurred and the estimated ultimate cost to settle the claims.

Periodically, we review our assumptions and valuations to determine the adequacy of our self-insured liabilities.

#### Health Insurance

With the exception of California employees enrolled in HMO plans, we are effectively self-insuring our employee health care benefit by retaining claims liability risk up to \$200,000 per incident and an aggregate claim limit based on the number of employees enrolled in the plan per month. We estimate our liability for the uninsured portion of employee health care obligations that have been incurred but not reported based on our claims experience, the number of employees enrolled in the program and the average time from when a claim is incurred to the time it is paid. In addition, we perform an analysis of our potential liability for open claims.

Consolidated Results of Operations

The following table sets forth components of our income statements expressed as a percentage of revenue:

	For the Years Ended December 31,			
	2012	2011	2010	
Revenue:				
Animal Hospital	78.4	% 77.4	% 76.2	%
Laboratory	19.3	21.3	22.5	
All Other	6.6	5.5	4.6	
Intercompany	(4.3 )	(4.2 )	(3.3 )	)
Total revenue	100.0	100.0	100.0	
Direct costs	77.9	77.2	76.0	
Gross profit	22.1	22.8	24.0	
Selling, general and administrative expense	9.2	8.2	8.9	
Impairment of goodwill and other long-lived assets	7.3	1.4	—	
Net loss on sale of assets	0.1	—	—	
Operating income	5.5	13.2	15.1	
Interest expense, net	1.0	1.2	1.0	
Debt retirement costs	—	0.2	0.2	
Business combination adjustment gain	(0.4 )	—	—	
Other income	—	—	(0.1 )	)
Income before provision for income taxes	4.9	11.8	14.0	
Provision for income taxes	1.9	5.1	5.7	
Net income	3.0	6.7	8.3	
Net income attributable to noncontrolling interests	0.3	0.3	0.3	
Net income attributable to VCA Antech, Inc	2.7	% 6.4	% 8.0	%

Revenue

The following table summarizes our revenue (in thousands, except percentages):

	For the Years Ended December 31,									
	2012		2011		2010		% Change			
	\$	% of Total	\$	% of Total	\$	% of Total	2012	2011		
Animal Hospital	\$ 1,331,314	78.4	% \$ 1,150,120	77.4	% \$ 1,052,462	76.2	% 15.8	% 9.3	%	
Laboratory	327,801	19.3	% 316,797	21.3	% 310,654	22.5	% 3.5	% 2.0	%	
All Other	112,960	6.6	% 80,430	5.5	% 64,013	4.6	% 40.4	% 25.6	%	
Intercompany	(72,433 )	(4.3 )	)% (61,986 )	(4.2 )	)% (45,661 )	(3.3 )	)% 16.9	% 35.8	%	
Total revenue	\$ 1,699,642	100.0	% \$ 1,485,361	100.0	% \$ 1,381,468	100.0	% 14.4	% 7.5	%	

Consolidated revenue increased \$214.3 million in 2012, as compared to 2011. The increase in revenue was primarily attributable to acquisitions including animal hospitals in the United States and Canada, Vetstreet and ThinkPets.

Excluding acquisitions, revenue increased \$15.1 million due to organic revenue increase from both our Animal Hospital and Laboratory segments. Our Animal Hospital same-store revenue increased 1.2% in 2012. Our Laboratory internal revenue growth was 3.6% in 2012.

Consolidated revenue increased \$103.9 million in 2011, as compared to 2010. The increase in revenue was primarily attributable to acquisitions including animal hospitals and Vetstreet. Excluding acquisitions, revenue decreased \$12.2 million due to a decrease in Animal Hospital same-store revenue, partially offset by an increase in internal growth in our Laboratory revenue. Our Animal Hospital same-store revenue declined 0.7% in 2011. Our Laboratory internal revenue growth was 2.0% in 2011.





## Gross Profit

The following table summarizes our gross profit and our gross profit as a percentage of applicable revenue, or gross margin (in thousands, except percentages):

	For the Years Ended December 31,									
	2012		2011		2010		% Change			
	\$	Gross Margin	\$	Gross Margin	\$	Gross Margin	2012	2011		
Animal Hospital	\$189,111	14.2 %	\$179,810	15.6 %	\$172,390	16.4 %	5.2 %	4.3 %		
Laboratory	151,761	46.3 %	143,790	45.4 %	142,196	45.8 %	5.5 %	1.1 %		
All Other	38,707	34.3 %	20,971	26.1 %	19,277	30.1 %	84.6 %	8.8 %		
Intercompany	(4,605 )		(6,114 )		(2,699 )					
Total gross profit	\$374,974	22.1 %	\$338,457	22.8 %	\$331,164	24.0 %	10.8 %	2.2 %		

Consolidated gross profit increased \$36.5 million in 2012, as compared to 2011. The increase was primarily due to \$31.5 million gross profit from the acquisitions of AVC, Vetstreet and ThinkPets. Excluding the impact of acquisitions, the remaining increase in gross profit is attributable to organic revenue growth at our Laboratory and Vetstreet segments, partially offset by a decrease in gross profit from our same-store animal hospitals.

Consolidated gross profit increased \$7.3 million in 2011, as compared to 2010. The increase was primarily due to gross profit from our acquisitions and to a lesser extent internal revenue growth at our Laboratory segment, partially offset by a decrease in gross profit from our same-store animal hospitals, due to decreased same-store revenue.

## Segment Results

## Animal Hospital Segment

The following table summarizes revenue and gross profit for the Animal Hospital segment (in thousands, except percentages):

	For the Years Ended December 31,						% Change	
	2012	2011	2010	2012	2011			
Revenue	\$1,331,314	\$1,150,120	\$1,052,462	15.8 %	9.3 %			
Gross profit	\$189,111	\$179,810	\$172,390	5.2 %	4.3 %			
Gross margin	14.2 %	15.6 %	16.4 %					

Animal Hospital revenue increased \$181.2 million in 2012, as compared to 2011 and \$97.7 million in 2011, as compared to 2010. The components of the increases are summarized in the following table (in thousands, except percentages and average price per order):

	2012 Comparative Analysis			2011 Comparative Analysis		
	For the Years Ended December 31,					
	2012	2011	% Change	2011	2010	% Change
Animal Hospital Revenue:						
Same-store facility:						
Orders <sup>(1)(2)</sup>	6,747	6,867	(1.7 %)	6,176	6,427	(3.9 %)
Average revenue per order <sup>(3)</sup>	\$165.43	\$160.56	3.0 %	\$159.52	\$154.42	3.3 %
Same-store revenue <sup>(1)</sup>	\$1,116,153	\$1,102,535	1.2 %	\$985,200	\$992,418	(0.7 %)
AVC	96,377	—		—	—	
Net acquired revenue <sup>(4)</sup>	118,784	47,585		164,920	60,044	
Total	\$1,331,314	\$1,150,120	15.8 %	\$1,150,120	\$1,052,462	9.3 %

(1)

Same-store revenue and orders were calculated using Animal Hospital revenue, which are adjusted to exclude the revenue for newly acquired animal hospitals that we did not own as of the beginning of the comparable period in the prior year. Same-store revenue also includes revenue generated by customers referred from our relocated or combined animal hospitals, including those merged upon acquisition.

<sup>(2)</sup> The change in orders may not calculate exactly due to rounding.

- (3) Computed by dividing same-store revenue by same-store orders. The average revenue per order may not calculate exactly due to rounding.

Net acquired revenue represents the revenue from those animal hospitals acquired (other than AVC), net of revenue from those animal hospitals sold or closed on or after the beginning of the comparable period, which was

- (4) January 1, 2011 for the 2012 Comparative Analysis and January 1, 2010 for the 2011 Comparative Analysis.

Fluctuations in net acquired revenue occur based on the volume, size and timing of acquisitions and dispositions during the periods from this date through the end of the applicable period.

Contributing to the decline in our volume of same-store orders is the continued negative impact of the current economic environment and the wide competing availability of many pet-related products traditionally sold in our animal hospitals, in retail stores, and other distribution channels such as the Internet.

Our business strategy is to place a greater emphasis on comprehensive wellness visits and advanced medical procedures, which typically generate higher priced orders. The migration of lower priced orders from our animal hospitals to other distribution channels mentioned above and our emphasis on comprehensive wellness visits has, over the past several years, resulted in a decrease in lower priced orders and an increase in higher priced orders.

However, for both the years ended December 31, 2012 and 2011 this trend did not continue, as we experienced a decrease in the number of both lower and higher priced orders, which we believe is primarily a consequence of current economic conditions in the United States, and the impact of changes in our overall business environment on the mix of tests performed.

Price increases contributed to the increase in the average revenue per order. Prices at each of our hospitals are reviewed regularly and adjustments are made based on market considerations, demographics and our costs. These adjustments historically approximated 3% to 6% on most services at the majority of our animal hospitals and are typically implemented in February of each year; however, price increases in 2012 generally ranged between 3% and 4%.

Animal Hospital gross profit is calculated as Animal Hospital revenue less Animal Hospital direct costs. Animal Hospital direct costs comprise all costs of services and products at the animal hospitals, including, but not limited to, salaries of veterinarians, technicians and all other animal hospital-based personnel, facilities rent, occupancy costs, supply costs, depreciation and amortization, certain marketing and promotional expenses and costs of goods sold associated with the retail sales of pet food and pet supplies.

Our Animal Hospital gross margin in 2012, 2011 and 2010 was 14.2%, 15.6% and 16.4%, respectively. In 2012 the gross margin declined as a result of lower same-store margins as a result of increased labor costs and to a lesser extent lower gross margins from our acquired hospitals. In 2011 the gross margin declined as a result of a decline in our same-store revenue and to a lesser extent lower gross margins from our acquired hospitals.

Our Animal Hospital same-store gross margin in 2012, 2011 and 2010 was 14.8%, 15.8% and 17.1%, respectively. The 2012 decrease, as compared to 2011, was primarily attributable to deleveraging as a result of increased labor costs and the 2011 decrease, as compared to 2010, was primarily due to deleveraging as a result of the aforementioned decline in same-store revenue.

Over the last several years we have acquired a significant number of animal hospitals. Many of these newly acquired animal hospitals had lower gross margins at the time of acquisition than those previously operated by us. We have improved these lower gross margins, in the aggregate, subsequent to the acquisition by improving animal hospital revenue, reducing costs and/or increasing operating leverage.

#### Laboratory Segment

The following table summarizes revenue and gross profit for our Laboratory segment (in thousands, except percentages):

	For the Years Ended December 31,			% Change		
	2012	2011	2010	2012	2011	
Revenue	\$327,801	\$316,797	\$310,654	3.5	% 2.0	%
Gross profit	\$151,761	\$143,790	\$142,196	5.5	% 1.1	%
Gross margin	46.3	% 45.4	% 45.8	%		

Laboratory revenue increased \$11.0 million in 2012, as compared to 2011 and \$6.1 million in 2011, as compared to 2010. The components of the increase in Laboratory revenue are detailed below (in thousands, except percentages and average price per requisition):

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	2012 Comparative Analysis For the Years Ended December 31,			2011 Comparative Analysis				
	2012	2011	% Change	2011 <sup>(5)</sup>	2010 <sup>(5)</sup>	% Change		
Laboratory Revenue:								
Internal growth:								
Number of requisitions <sup>(1)</sup>	12,605	12,378	1.8	% 12,396	12,391	—	%	
Average revenue per requisition <sup>(2)</sup>	\$25.99	\$25.55	1.7	% \$25.55	\$25.07	1.9	%	
Total internal revenue <sup>(1)</sup>	\$327,609	\$316,280	3.6	% \$316,715	\$310,654	2.0	%	
Billing day adjustment <sup>(4)</sup>	—	517		—	—			
Acquired revenue <sup>(3)</sup>	192	—		82	—			
Total	\$327,801	\$316,797	3.5	% \$316,797	\$310,654	2.0	%	

Internal revenue and requisitions were calculated using Laboratory operating results, which are (1) adjusted to exclude the operating results of acquired laboratories for the comparable periods that we did not own them in the prior year and (2) adjusted for the impact resulting from any differences in the number of billing days in comparable periods.

(2) Computed by dividing internal revenue by the number of requisitions.

(3) Acquired revenue in both the 2012 and 2011 Comparative Analyses represents the revenue of the laboratories acquired in each of those respective years.

(4) The 2011 billing day adjustment reflects the impact of one less billing day in 2012, as compared to 2011.

(5) Prior-year amounts have been adjusted to conform to the current year presentation. The changes were not material. Laboratory revenue in 2012 increased, as compared to 2011, due to an increase in internal revenue growth attributable to an increase in number of requisitions and average revenue per requisition.

Historically, requisitions have been driven by an ongoing trend in veterinary medicine to focus on the importance of laboratory diagnostic testing in the diagnosis, early detection and treatment of diseases, and the migration of certain tests to outside laboratories that have historically been performed in animal hospitals. While these factors have resulted in significant increases in requisitions in the past, the economic downturn, slow economic recovery and the effects of increased competition continued to negatively impact requisitions in 2012.

We derive our laboratory revenue from services provided to over 16,000 independently owned animal hospitals. Shifts in the purchasing habits of any individual animal hospital or small group of animal hospitals is not material to our laboratory revenues. Other companies are developing networks of animal hospitals and shifts in the purchasing habits of these networks have the potential of a greater impact on our laboratory revenues.

The average revenue per requisition increased slightly in 2012 due to price increases in both February 2012 and February 2011. The overall increase was partially offset by various factors including changes in the mix, lower-priced tests historically performed at the animal hospitals and a decrease in higher-priced tests as a result of the current economic environment.

Laboratory gross profit is calculated as Laboratory revenue less Laboratory direct costs. Laboratory direct costs comprise all costs of laboratory services, including but not limited to, salaries of veterinarians, specialists, technicians and other laboratory-based personnel, transportation and delivery costs, facilities rent, occupancy costs, depreciation and amortization and supply costs.

Our Laboratory gross margin increased in 2012, as compared to 2011 due to operating leverage from increased revenue. The decrease in Laboratory gross margin in 2011 compared to 2010, was primarily due to the decline in the rate of our revenue growth relative to increasing transportation costs.

#### Intercompany Revenue

Laboratory revenue in 2012, 2011 and 2010 included intercompany revenue of \$52.4 million, \$44.3 million and \$37.0 million, respectively, that was generated by providing laboratory services to our animal hospitals. All Other revenue in 2012, 2011 and 2010 included intercompany revenue of \$20.0 million, \$17.7 million and \$8.6 million, respectively, generated by providing products and services to our animal hospitals and laboratories. For purposes of reviewing the

operating performance of our operating segments, all intercompany transactions are generally accounted for as if the transactions were with an independent third party at current market prices. For financial reporting purposes, intercompany transactions are eliminated as part of our consolidation.

## Selling, General and Administrative Expense

The following table summarizes our selling, general and administrative (“SG&A”) expense and our expense as a percentage of applicable revenue (in thousands, except percentages):

	For the Years Ended December 31,									
	2012		2011		2010		% Change			
	\$	% of Revenue	\$	% of Revenue	\$	% of Revenue	2012	2011		
Animal Hospital	\$30,826	2.3 %	\$24,342	2.1 %	\$23,539	2.2 %	26.6 %	3.4 %		%
Laboratory	29,660	9.0 %	27,864	8.8 %	26,243	8.4 %	6.4 %	6.2 %		%
All Other	37,879	33.5 %	19,136	23.8 %	14,507	22.7 %	97.9 %	31.9 %		%
Corporate	58,790	3.5 %	49,770	3.4 %	59,252	4.3 %	18.1 %	(16.0) %		%
Total SG&A	\$157,155	9.2 %	\$121,112	8.2 %	\$123,541	8.9 %	29.8 %	(2.0) %		%

Consolidated SG&A expense increased \$36.0 million in 2012, as compared to 2011 and decreased \$2.4 million in 2011, as compared to 2010.

The increases in consolidated SG&A in 2012, as compared to 2011, included approximately \$17.5 million from the acquisition of AVC, Vetstreet and ThinkPets. Excluding the impact of these acquisitions, consolidated SG&A increased by \$18.5 million. The remaining increase was primarily due to increases in corporate costs of which \$3.5 million was related to corporate share-based compensation expense, as well as, increases in compensation-related expenses in the Animal Hospital and Laboratory segments.

The decreased SG&A in 2011, as compared to 2010, was due to: decreased SG&A at Corporate primarily due to the 2010 accrual of consulting and Supplemental Executive Retirement Program (“SERP”) expenses; offset by increases in share-based compensation and increased SG&A in other operating segments primarily due to growth in those segments as a result of acquisitions.

## Operating Income

The following table summarizes our operating income (in thousands, except percentages):

	For the Years Ended December 31,									
	2012		2011		2010		% Change			
	\$	% of Revenue	\$	% of Revenue	\$	% of Revenue	2012	2011		
Animal Hospital	\$156,356	11.7 %	\$155,141	13.5 %	\$148,578	14.1 %	0.8 %	4.4 %		%
Laboratory	122,115	37.3 %	115,905	36.6 %	115,931	37.3 %	5.4 %	— %		%
All Other	(122,246 )	(108.2) %	(19,502 )	(24.2) %	4,699	7.3 %	526.8 %	(515.0) %		%
Corporate	(58,684 )		(49,777 )		(59,260 )		17.9 %	(16.0) %		%
Eliminations	(4,605 )		(6,114 )		(2,699 )		(24.7) %	126.5 %		%
Total operating income	\$92,936	5.5 %	\$195,653	13.2 %	\$207,249	15.1 %	(52.5) %	(5.6) %		%

Consolidated operating income decreased by \$102.7 million in 2012, as compared to 2011 and decreased \$11.6 million in 2011, as compared to 2010.

Excluding the impact of the current year \$123.6 million impairment charge, primarily related to our Vetstreet business, the prior year \$21.3 million non-cash goodwill impairment charge recorded in our medical technology business and the current year \$3.1 million depreciation expense adjustment, consolidated operating income increased by \$2.6 million. The remaining increase in consolidated operating income in 2012, as compared to 2011, was primarily attributable to acquisitions in the period and increased operating income in our laboratory business, partially offset by a decrease in the same-store animal hospital gross profit and increased corporate SG&A, mentioned above. The decrease in our consolidated operating income in 2011, as compared to 2010, was due to the non-cash goodwill impairment charge recorded in our medical technology business. The decrease was partially offset by a decrease in our overall SG&A and the increase in gross profit.





## Interest Expense, Net

The following table summarizes our interest expense, net of interest income (in thousands):

	For the Years Ended December 31,		
	2012	2011	2010
Interest expense:			
Senior term notes	\$12,394	\$12,239	\$10,672
Interest rate swap agreements	—	—	382
Capital leases and other	3,348	3,801	2,515
Amortization of debt costs	1,278	1,445	862
	17,020	17,485	14,431
Interest income	(468	) (601	) (801
Total interest expense, net of interest income	\$16,552	\$16,884	\$13,630

The decrease in net interest expense in 2012, as compared to 2011, was primarily attributable to a decrease in mandatorily redeemable partnership interest, interest accrued on executive retirement liabilities, and amortized debt costs written off in the prior year related to the refinancing of our senior term debt notes on August 16, 2011. The change in interest for senior term notes was relatively flat. While we experienced a decline in year-over-year weighted average interest rates, this effect was offset by an increase in the weighted average balance related to additional borrowing completed in association with the purchase of AVC. See Note 7, Long-Term Obligations, in our consolidated financial statements of this annual report on Form 10-K for a more detailed discussion, including applicable interest rates on our debt, which was amended in August 2011.

The increase in net interest expense in 2011, as compared to 2010, was primarily attributable to an increase in the average debt balance due to the amendment of our existing credit and guaranty facility to provide for a \$100 million increase in our senior term notes and the related increase in debt amortization costs due to the capitalization of additional debt amendment fees.

## Provision for Income Taxes

The effective tax rate for 2012, 2011 and 2010 was 41.2%, 44.3% and 41.5%, respectively.

The effective tax rate for 2012 was positively impacted by a nondeductible charge related to goodwill impairment offset by (i) a non-taxable gain of \$5.7 million related to the increase in value of our historic noncontrolling interest in AVC realized upon the acquisition of the remaining equity interest and (ii) lower tax rates in Canada. The effective rate for 2011 was impacted by a nondeductible charge related to goodwill impairment. The effective tax rate for 2010 was impacted by a tax expense of \$3.5 million, related to the settlement of taxes on 2004 through 2007 taxable income.

## Net Income Attributable to Noncontrolling Interests

Net income attributable to noncontrolling interests represents our partners' proportionate share of income generated by those subsidiaries that we do not wholly-own.

## Inflation

Historically, our operations have not been materially affected by inflation. We cannot assure that our operations will not be affected by inflation in the future.

## Related Party Transactions

## ThinkPets Inc. (formerly known as Zoasis Corporation)

On February 1, 2012, we acquired all of the outstanding capital stock of ThinkPets, Inc. for \$21.0 million, payable by delivery of 473,389 shares of VCA common stock and \$10.5 million in cash. The number of shares of VCA common stock were determined based on the daily volume weighted average closing sales price of the VCA common stock for the 10 consecutive trading days ending on the trading day immediately preceding the acquisition. At the time of the acquisition, Bob Antin, our CEO and Chairman of the Board, owned 54% of the common stock of ThinkPets, and served as a director of ThinkPets, and Art Antin, our Chief Operating Officer, owned 8% of the common stock of ThinkPets. In accordance with its charter, our Audit Committee is responsible for reviewing and approving all related-party transactions. Both the Audit Committee and our Board of Directors unanimously approved the

acquisition. Due to the related party nature of the acquisition, Bob Antin recused himself from all Board meetings wherein the acquisition was discussed and did not vote in connection with the acquisition.

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#### Related Party Vendors

Frank Reddick joined our company as a director in February 2002 and is a partner in the law firm of Akin Gump Strauss Hauer & Feld, LLP (“Akin”). Akin provided legal services to us during 2012, 2011 and 2010. The amount paid by our company to Akin for these legal services was approximately \$551,000, \$1.6 million and \$2.3 million in 2012, 2011 and 2010, respectively.

#### Liquidity and Capital Resources

##### Introduction

We generate cash primarily from (i) payments made by customers for our veterinary services, (ii) payments from animal hospitals and other clients for our laboratory services, (iii) proceeds received from the sale of our imaging equipment and other related services and (iv) payments received from participating hospitals for Vetstreet subscriptions and reminder notices. Our business historically has experienced strong liquidity, as fees for services provided in our animal hospitals are due at the time of service and fees for laboratory services are collected under standard industry terms. Our cash disbursements are primarily for payments related to the compensation of our employees, supplies and inventory purchases for our operating segments, occupancy and other administrative costs, interest expense, payments on long-term borrowings, capital expenditures and acquisitions. Cash outflows fluctuate with the amount and timing of the settlement of these transactions.

We manage our cash, investments and capital structure so we are able to meet the short-term and long-term obligations of our business while maintaining financial flexibility and liquidity. We forecast, analyze and monitor our cash flows to enable investment and financing within the overall constraints of our financial strategy.

At December 31, 2012, our consolidated cash and cash equivalents totaled \$68.4 million, representing an increase of \$4.8 million as compared to the prior year. Cash flows generated from operating activities totaled \$237.3 million in 2012, representing an increase of \$46.2 million as compared to the prior year. We spent \$219.3 million on acquisitions, investments and capital expenditures during the year.

We have historically funded our working capital requirements, capital expenditures and investment in individual acquisitions primarily from internally-generated cash flows and we expect to do so in the future. During the first quarter of the 2012 fiscal year, we amended our Amended and Restated Credit & Guaranty Agreement dated as of August 16, 2011. The First Amendment replenished the aggregate amount of New Term Loan Commitments available under the Credit Agreement to a maximum of \$100 million, after giving effect to the funding of \$50 million of New Term Loan Commitments on January 24, 2012, which were drawn in connection with the additional investment made in AVC. As of December 31, 2012, we have access to an unused \$125 million revolving credit facility, which expires August 2016, allowing us to maintain further operating and financial flexibility.

Historically, we have been able to access the capital markets to fund acquisitions that could not be funded out of internally generated cash flows. The availability of financing in the form of debt or equity is influenced by many factors including our profitability, operating cash flows, debt levels, debt ratings, contractual restrictions, and market conditions. Although in the past we have been able to obtain financing for material transactions on terms we believe to be reasonable, there is a possibility that we may not be able to obtain financing on favorable terms in the future.

##### Future Cash Flows

##### Short-term

Other than our acquisitions of animal hospital chains, we historically have funded our working capital requirements, capital expenditures and investments in animal hospital acquisitions from internally-generated cash flow. We anticipate that our cash on hand and net cash provided by operations and available funds under our revolving credit agreement and incremental facilities will be sufficient to meet our anticipated cash requirements for more than the next 12 months. If we consummate additional significant acquisitions during this period, we may seek additional debt or equity financing.

In 2013, we expect to spend \$50 million to \$85 million for the acquisition of independent animal hospitals. The ultimate number of acquisitions is largely dependent upon the attractiveness of the candidates and the strategic fit with our existing operations. In addition, we expect to spend approximately \$90 million in 2013 for both property and

equipment additions and other capital expenditures primarily to maintain our existing facilities.

Long-term

Our long-term liquidity needs, other than those related to the day-to-day operations of our business, including commitments for operating leases, generally are comprised of scheduled principal and interest payments for our outstanding long-term indebtedness, capital expenditures related to the expansion of our business and acquisitions in accordance with our

growth strategy. The scheduled payments on our long-term obligations are included in our contractual obligations table below.

We are unable to project with certainty whether our long-term cash flow from operations will be sufficient to repay our long-term debt when it comes due. If this cash flow is insufficient, we expect that we will need to refinance such indebtedness, amend its terms to extend maturity dates, or issue common stock on our company. Our management cannot make any assurances that such refinancing or amendments, if necessary, will be available on attractive terms, if at all.

#### Debt Related Covenants

Our senior credit facility contains certain financial covenants pertaining to fixed charge coverage and leverage ratios. In addition, our senior credit facility has restrictions pertaining to capital expenditures, acquisitions and the payment of cash dividends. As of December 31, 2012, we were in compliance with these covenants, including the two covenant ratios, the fixed charge coverage ratio and the leverage ratio.

At December 31, 2012, we had a fixed charge coverage ratio of 1.60 to 1.00, which was in compliance with the required ratio of no less than 1.20 to 1.00. The senior credit facility defines the fixed charge coverage ratio as that ratio that is calculated on a last 12-month basis by dividing pro forma earnings before interest, taxes, depreciation and amortization, as defined by the senior credit facility (“pro forma earnings”), by fixed charges. Fixed charges are defined as cash interest expense, scheduled principal payments on debt obligations, capital expenditures, and provision for income taxes. Pro forma earnings include 12 months of operating results for businesses acquired during the period. At December 31, 2012, we had a leverage ratio of 2.03 to 1.00, which was in compliance with the required ratio of no more than 3.00 to 1.00. The senior credit facility defines the leverage ratio as that ratio which is calculated as total debt divided by pro forma earnings.

#### Historical Cash Flows

The following table summarizes our cash flows (in thousands):

	For the Years Ended December 31,		
	2012	2011	2010
Cash provided by (used in):			
Operating activities	\$237,253	\$191,051	\$168,073
Investing activities	(219,258 )	(271,310 )	(150,174 )
Financing activities	(13,514 )	47,004	(66,142 )
Effect of currency exchange rate charges on cash and cash equivalents	303	(220 )	188
Increase (decrease) in cash and cash equivalents	4,784	(33,475 )	(48,055 )
Cash and cash equivalents at beginning of year	63,651	97,126	145,181
Cash and cash equivalents at end of year	\$68,435	\$63,651	\$97,126

#### Cash Flows from Operating Activities

Net cash provided by operating activities increased \$46.2 million in 2012, as compared to 2011. Operating cash flow for the year ended December 31, 2012 included \$50.7 million of net income and net non-cash expenses of \$180.3 million, partially offset by net cash provided as a result of changes in operating assets and liabilities of \$6.2 million. The changes in operating assets and liabilities included a \$7.2 million increase in accrued payroll and related liabilities, a \$3.6 million increase in accounts payable and accrued liabilities, a \$4.1 million decrease in prepaid income taxes and a \$1.6 million decrease in accounts receivable, partially offset by a \$10.3 million increase in inventory, prepaid expenses and other assets. The increases in accrued payroll and related liabilities and accounts payable and accrued liabilities were primarily due to the acquisition of AVC and timing of payment obligations. The decrease in prepaid income taxes was due to the payment of estimated taxes owed from the prior year. The decrease in accounts receivable was primarily related to the timing of deposits-in-transit on our credit card receivables, there was one more day available for deposit for December 31, 2012, as compared to December 31, 2011. In addition, we had improved collection efforts at our Medical Technology business. The increase in inventory, prepaid expense and other assets was primarily due to an increase in lease receivables as a result of executing additional contracts.

Net cash provided by operating activities increased \$23.0 million in 2011, as compared to 2010. Cash provided by operating activities of \$191.1 million for the year ended December 31, 2011 consisted of \$99.9 million of net income and net non-cash expenses of \$117.6 million, partially offset by net cash used as a result of changes in operating assets and liabilities of \$26.4 million. The changes in operating assets and liabilities included a \$14.1 million increase in trade accounts receivable, a \$12.3 million increase in inventory, prepaid expense and other assets and a \$5.4 million decrease in accounts payable and other accrued liabilities, partially offset by a \$4.6 million increase in accrued payroll and related liabilities. The increase in accounts receivable was primarily due to an increase in net revenues from our acquired animal hospitals and other businesses. The

increase in inventory, prepaid expense and other assets was primarily due to the build-up of inventory, increases due to new products and an increase in lease receivables as a result of executing additional contracts. The decrease in accounts payable and other accrued liabilities and the increase in accrued payroll and related liabilities were all a result of timing of payment obligations.

#### Cash Flows from Investing Activities

The table below presents the components of the changes in investing cash flows (in thousands):

	For the Years Ended December 31,			Variance	
	2012	2011	2010	2012	2011
Investing Cash Flows:					
Acquisition of independent animal hospitals and laboratories	\$(78,629 )	\$(34,243 )	\$(68,624 )	\$(44,386 )	\$34,381
Acquisition of AVC	(48,819 )	—	—	(48,819 )	—
Acquisition of ThinkPets	(7,468 )	—	—	(7,468 )	—
Acquisition of BrightHeart	—	(23,490 )	—	23,490	(23,490 )
Acquisition of Pet DRx	—	—	(7,670 )	—	7,670
Acquisition of Vetstreet	—	(146,420 )	—	146,420	(146,420 )
Other	—				