

**UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION  
Washington, D.C. 20549**

**FORM 10-K**

(Mark One)

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

For the fiscal year ended December 31, 2014

OR

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

For the transition period from \_\_\_\_\_ to \_\_\_\_\_

**Commission file number: 0-22427**

**HESKA CORPORATION**

(Exact name of registrant as specified in its charter)

**Delaware**  
(State or other jurisdiction of  
incorporation or organization)

**3760 Rocky Mountain Avenue  
Loveland, Colorado**  
(Address of principal executive offices)

**77-0192527**  
(I.R.S. Employer  
Identification Number)

**80538**  
(Zip Code)

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

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

**Public Common Stock, \$.01 par value**  
(Title of Class)

**The Nasdaq Stock Market LLC**  
(Name of Each Exchange on Which Registered)

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

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

Yes  No

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

Yes  No

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

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

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

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer or a smaller reporting company. See the definitions of "large accelerated filer," "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act.

Large accelerated filer

Accelerated filer

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

Smaller Reporting Company

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

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

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

**DOCUMENTS INCORPORATED BY REFERENCE**

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

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

## Statement Regarding Forward Looking Statements

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

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

### Internet Site

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

## PART I

### Item 1. Business.

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

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

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

## **Background**

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

## **Core Companion Animal Health Segment**

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

### ***Veterinary Blood Testing and Other Non-Imaging Instruments***

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

- *Blood Chemistry.* The Element DC™ Veterinary Chemistry Analyzer (the "Element DC") is an easy-to-use, robust system that uses dry slide technology for blood chemistry and electrolyte analysis and has the ability to run 22 tests at a time with a single blood sample. Test slides are available as both pre-packaged panels as well as individual slides. The Element DC is faster and has an enhanced user interface compared to the instrument it replaced, the DRI-CHEM 4000 Veterinary Chemistry Analyzer (the "DRI-CHEM 4000"). The DRI-CHEM 7000 Veterinary Chemistry Analyzer (the "DRI-CHEM 7000") is a complementary chemistry offering, co-branded with FUJIFILM Corporation ("FUJIFILM"), with higher throughput, multiple patient staging and a "STAT" feature which provides emergency sample flexibility in critical cases. The Element DC, DRI-CHEM 7000 and DRI-CHEM 4000 all utilize the same test slides. We are supplied with the Element DC, the DRI-CHEM 7000 and affiliated test slides and supplies under a contractual agreement with FUJIFILM.
- *Hematology.* The Element HT™5 Hematology Analyzer (the "HT5") is a true 5-part hematology analyzer which uses laser, impedance and colorimetric technologies to measure key parameters such as white blood cell count, red blood cell count, platelet count and hemoglobin levels in animals. The HT5 can generate results in less than a minute with 15 µL of sample. We began to ship HT5 units in January 2015. We are supplied with the HT5 and affiliated reagents and supplies under a contractual agreement with Shenzhen Mindray Bio-Medical Electronics Co., Ltd. ("Mindray"). The HEMATTRUE Veterinary Hematology Analyzer (the "HEMATTRUE") is an easy-to-use and reliable 3-part hematology blood analyzer that we continue to offer to our customers. In addition, we continue to service and support a previous hematology instrument, the HESKA CBC-DIFF Veterinary Hematology System (the "CBC"). We are supplied new

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

- *Blood Gases and Electrolytes.* The Element POC™ Blood Gas & Electrolyte Analyzer ("EPOC") is a handheld, wireless analyzer which delivers rapid blood gas, electrolyte, metabolite, and basic blood chemistry testing. EPOC features test cards with room temperature storage which can offer results with less than 100 µL of sample as well as WiFi and Bluetooth connectivity. We began to ship EPOC units to customers in October 2013. EPOC and affiliated consumables and supplies are supplied to us under a contractual agreement with Alere North America, LLC, a unit of Alere Inc.
- *IV Pumps.* The VET/IV 2.2 infusion pump is a compact, affordable IV pump that allows veterinarians to easily provide regulated infusion of fluids, drugs or nutritional products for their patients.

### ***Veterinary Imaging Instruments and Services***

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

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

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

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

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

### ***Point-of-Care Heartworm Diagnostic Tests***

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

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

### ***Heartworm Preventive Products***

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

### ***Allergy Products and Services***

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

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

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

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

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

#### **Other Vaccines, Pharmaceuticals and Products Segment**

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

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

#### **Marketing, Sales and Customer Support**

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

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

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

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

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

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

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

### **Manufacturing**

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

### **Product Development**

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

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



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

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

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

### **Intellectual Property**

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

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

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

### **Seasonality**

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

### **Government Regulation**

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

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

- *USDA.* Vaccines and certain single use, point-of-care diagnostics are considered veterinary biologics and are therefore regulated by the Center for Veterinary Biologics, or CVB, of the USDA. Industry data indicate that it takes approximately four years and in excess of \$1.0 million to license a conventional vaccine for animals from basic research through licensing. In contrast to vaccines, single use, point-of-care diagnostics can typically be licensed by the USDA in about two years, at considerably less cost. However, vaccines or diagnostics that use innovative materials, such as those resulting from recombinant DNA technology, usually require additional time to license. The USDA licensing process involves the submission of several data packages. These packages include information on how the product will be manufactured, information on the efficacy and safety of the product in laboratory and target animal studies and information on performance of the product in field conditions.
- *FDA.* Pharmaceutical products, which typically include synthetic compounds, are approved and monitored by the Center for Veterinary Medicine of the FDA. Under the Federal Food, Drug and Cosmetic Act, the same statutory standard for FDA approval applies to both human and animal drugs: demonstrated safety, efficacy and compliance with FDA manufacturing standards. However, unlike human drugs, neither preclinical studies nor a sequential phase system of studies are required. Rather, for animal drugs, studies for safety and efficacy may be conducted immediately in the species for which the drug is intended. Thus, there is no required phased evaluation of drug performance, and the Center for Veterinary Medicine will review data at appropriate times in the drug development process. The process can be costly and time consuming, requiring up to \$100 million and seven to ten years to sell an animal drug in the market. In addition, the time and cost for developing companion animal drugs may be significantly less than for drugs for livestock animals, which generally have enhanced standards designed to ensure safety in the food chain.
- *EPA.* Products that are applied topically to animals or to premises to control external parasites are regulated by the Environmental Protection Agency, or EPA.

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

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

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

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

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

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

### Competition

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

### Environmental Regulation

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

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

## Employees

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

## Where You Can Find Additional Information

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

## Executive Officers of the Registrant

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

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

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

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

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

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

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

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

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

*Rodney A. Lippincott* was appointed Executive Vice President, Companion Animal Health Sales in February 2013. From July 2011 to February 2013, he was employed by Cuattro, LLC as Vice President, Sales – US Veterinary and sold exclusively on behalf of Cuattro Veterinary USA, LLC. Mr. Lippincott held various positions including Sales Director for Sound Technologies, Inc., a unit of VCA Antech, Inc., from September 2007 to June 2011. Prior to entering the animal health market, Mr. Lippincott spent 13.5 years employed by Smith Micro Software, Inc. and held positions including US and International Sales Manager

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

#### **Item 1A. Risk Factors**

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

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

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

Under the Operating Agreement, should Heska Imaging meet certain performance criteria, and the Imaging Minority fail to exercise an applicable put to sell us all of the Imaging Minority's position in Heska Imaging following the audit of our financial statements for 2015, 2016 and 2017, we would have a call option to purchase all, but not less than all, of the Imaging Minority's position in Heska Imaging. Based on Heska Imaging's current ownership position, exercising this call option could require us to deliver up to \$19.6 million following calendar year 2015, \$19.6 million following calendar year 2016 or \$42.4 million following calendar year 2017 - as well as 25% of Heska Imaging's cash (any applicable payment in aggregate to be defined as the "Call Payment") to acquire the outstanding minority interest in Heska Imaging. While we have the right to deliver up to 55% of the consideration in our Public Common Stock under certain circumstances, such stock is to be valued based on 90% of market value (the "Delivery Stock Value") and is limited to approximately 650 thousand shares in any case. If the Delivery Stock Value is less than the market value of our stock at the time of the Acquisition, we do not have the right to deliver any Public Common

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

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

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

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

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

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

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

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

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

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

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

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

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



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

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

Our agreements with our corporate marketing partners generally contain no or small minimum purchase requirements in order for them to maintain their exclusive marketing rights. We are party to an agreement with Merck Animal Health, which grants Merck Animal Health exclusive distribution and marketing rights for our canine heartworm preventive product, TRI-HEART Plus Chewable Tablets, ultimately sold to or through veterinarians in the United States and Canada. Novartis Agro K.K., Tokyo ("Novartis Japan") markets and distributes our SOLO STEP CH heartworm test in Japan under an exclusive arrangement. AgriLabs had the non-exclusive right to sell certain of our produced bovine vaccines in the United States, Africa and Mexico and has historically generated the majority of our sales of those vaccines in those territories under an agreement which was assigned to and assumed by Eli Lilly acting through Elanco in November 2013. One or more of these marketing partners may not devote sufficient resources to marketing our products and our sales and financial position could suffer significantly as a result. Revenue from Merck entities, including Merck Animal Health, represented 12% of our 2014 revenue. Revenue from Elanco represented 11% of our 2014 revenue. If Merck Animal Health personnel fail to market, sell and support our heartworm preventive sufficiently or if Elanco personnel fail to market, sell and support the bovine vaccines we produce and sell to Elanco, our sales could decline significantly. Furthermore, there may be nothing to prevent these partners from pursuing alternative technologies or products that may compete with our products in current or future agreements, including as part of mergers, acquisitions or divestitures. For example, we believe a unit of Merck has obtained FDA approval for a canine heartworm preventive product with additional claims compared with our TRI-HEART Plus Chewable Tablets, which we believe is not currently being marketed actively. Should Merck decide to emphasize sales and marketing efforts of this product rather than our TRI-HEART Plus Chewable Tablets or cancel our agreement regarding canine heartworm preventive distribution and marketing, our sales could decline significantly. In the future, third-party marketing assistance may not be available on reasonable terms, if at all. If any of these events occur, we may not be able to maintain our current market share or commercialize certain of our products and our sales will decline accordingly.

***We may be unable to market and sell our products successfully.***

We may not develop and maintain marketing and/or sales capabilities successfully, and we may not be able to make arrangements with third parties to perform these activities on satisfactory terms. If our marketing and sales strategy is unsuccessful, our ability to sell our products will be negatively impacted and our revenues will decrease. This could result in the loss of distribution rights for products or failure to gain access to new products and could cause damage to our reputation and adversely affect our business and future prospects.

The market for companion animal healthcare products is highly fragmented. Because our CCA proprietary products are generally available only to veterinarians or by prescription and our medical instruments require technical training to operate, we ultimately sell all our CCA products primarily to or through veterinarians. The acceptance of our products by veterinarians is critical to our success. Changes in our ability to obtain or maintain such acceptance or changes in veterinary medical practice could significantly decrease our anticipated sales. As the vast majority of cash flow to veterinarians ultimately is funded by pet owners without private insurance or government support, our business may be more susceptible to severe economic downturns than other health care businesses which rely less on individual consumers.

We recently have entered into agreements with independent third party distributors, including Butler Animal Health Supply, LLC d/b/a Henry Schein Animal Health ("Henry Schein"), which we expect to market and sell our products to a greater degree than in the recent past. Our agreement with Henry Schein prohibits us from selling our chemistry blood testing products and our hematology blood testing products to an independent third party distributor other than Henry Schein. Independent third-party distributors may be effective in increasing sales of our products to veterinarians, although we would expect a corresponding lower gross margin as such distributors typically buy products from us at a discount to end user prices. It is possible new or existing independent third-party distributors could cannibalize our direct sales efforts and lower our total gross margin. For us to be effective when working with an independent third-party distributor, the distributor must agree to market and/or sell our products and we must provide proper economic incentives to the distributor as well as contend effectively for the time, energy and focus of the employees of such distributor given other products the distributor may be carrying, potentially including those of our competitors. If we fail to be effective with new or existing independent third-party distributors, our financial performance may suffer.

***We depend on key personnel for our future success. If we lose our key personnel or are unable to attract and retain additional personnel, we may be unable to achieve our goals.***

Our future success is substantially dependent on the efforts of our senior management and other key personnel, including our Chief Executive Officer, Kevin Wilson. The loss of the services of members of our senior management or other key personnel may significantly delay or prevent the achievement of our business objectives. Although we have an employment agreement with many of these individuals, all are at-will employees, which means that either the employee or Heska may terminate employment at any time without prior notice. If we lose the services of, or fail to recruit, key personnel, the growth of our business could be substantially impaired. We do not maintain key person life insurance for any of our senior management or key personnel.

***We rely substantially on third-party suppliers. The loss of products or delays in product availability from one or more third-party suppliers could substantially harm our business.***

To be successful, we must contract for the supply of, or manufacture ourselves, current and future products of appropriate quantity, quality and cost. Such products must be available on a timely basis and be in compliance with any regulatory requirements. Similarly, we must provide ourselves, or contract for the supply of certain services. Such services must be provided in a timely and appropriate manner. Failure to do any of the above could substantially harm our business.

We rely on third-party suppliers to manufacture those products we do not manufacture ourselves and to provide services we do not provide ourselves. Proprietary products provided by these suppliers represent a majority of our revenue. We currently rely on these suppliers for our blood testing instruments and consumable supplies for these instruments, for our imaging products and related software and services, for key components of our point-of-care diagnostic tests as well as for the manufacture of other products.

The loss of access to products from one or more suppliers could have a significant, negative impact on our business. Major suppliers who sell us proprietary products who are responsible for more than 5% of our 2014 revenue for the twelve months ended December 31, 2014 are Boule Medical AB, Cuatro, LLC, and FUJIFILM Corporation. None of these suppliers sold us products which were responsible for more than 25% of our 2014 revenue, although products purchased from one of these suppliers was responsible for more than 20% of our 2014 revenue and products purchased from another was responsible for more than 10% of our 2014 revenue. We often purchase products from our suppliers under agreements that are of limited duration or potentially can be terminated on an annual basis. In the case of our blood testing instruments and our digital radiography solutions we are typically entitled to non-exclusive access to consumable supplies, or ongoing non-exclusive access to products and services to meet the needs of an existing customer base, respectively, for a defined period upon expiration of exclusive rights, which could subject us to competitive pressures in the period of non-exclusive access. Although we believe we will be able to maintain supply of our major product and service offerings in the near future, there can be no assurance that our suppliers will meet their obligations under any agreements we may have in place with them or that we will be able to compel them to do so. Risks of relying on suppliers include:

- *Inability to meet minimum obligations.* Current agreements, or agreements we may negotiate in the future, may commit us to certain minimum purchase or other spending obligations. It is possible we will not be able to create the market demand to meet such obligations, which could create a drain on our financial resources and liquidity. Some such agreements may require minimum purchases and/or sales to maintain product rights and we may be significantly harmed if we are unable to meet such requirements and lose product rights.
- *Loss of exclusivity.* In the case of our blood testing instruments, if we are entitled to non-exclusive access to consumable supplies for a defined period upon expiration of exclusive rights, we may face increased competition from a third party with similar non-exclusive access or our former supplier, which could cause us to lose customers and/or significantly decrease our margins and could significantly affect our financial results. In addition, current agreements, or agreements we may negotiate in the future, with suppliers may require us to meet minimum annual sales levels to maintain our position as the exclusive distributor of these products. We may not meet these minimum sales levels and maintain exclusivity over the distribution and sale of these products. If we are not the exclusive distributor of these products, competition may increase significantly, reducing our revenues and/or decreasing our margins.
- *Changes in economics.* An underlying change in the economics with a supplier, such as a large price increase or new requirement of large minimum purchase amounts, could have a significant, adverse effect on our business, particularly if we are unable to identify and implement an alternative source of supply in a timely manner.
- *The loss of product rights upon expiration or termination of an existing agreement.* Unless we are able to find an alternate supply of a similar product, we would not be able to continue to offer our customers the same breadth of products and our sales and operating results would likely suffer. In the case of an instrument supplier, we could also potentially suffer the loss of sales of consumable supplies, which would be significant in cases where we have built a significant installed base, further harming our sales prospects and opportunities. Even if we were able to find an alternate supply for a product to which we lost rights, we would likely face increased competition from the product whose rights we lost being marketed by a third party or the former supplier and it may take us additional time and expense to gain the necessary approvals and launch an alternative product.
- *High switching costs.* In our blood testing instrument products we could face significant competition and lose all or some of the consumable revenues from the installed base of those instruments if we were to switch to a competitive instrument. If we need to change to other commercial manufacturing contractors for certain of our regulated products, additional regulatory

licenses or approvals generally must be obtained for these contractors prior to our use. This would require new testing and compliance inspections prior to sale, thus resulting in potential delays. Any new manufacturer would have to be educated in, or develop, substantially equivalent processes necessary for the production of our products. We likely would have to train our sales force, distribution network employees and customer support organization on the new product and spend significant funds marketing the new product to our customer base.

- *The involuntary or voluntary discontinuation of a product line.* Unless we are able to find an alternate supply of a similar product in this or similar circumstances with any product, we would not be able to continue to offer our customers the same breadth of products and our sales would likely suffer. Even if we are able to identify an alternate supply, it may take us additional time and expense to gain the necessary approvals and launch an alternative product, especially if the product is discontinued unexpectedly.
- *Inconsistent or inadequate quality control.* We may not be able to control or adequately monitor the quality of products we receive from our suppliers. Poor quality items could damage our reputation with our customers.
- *Limited capacity or ability to scale capacity.* If market demand for our products increases suddenly, our current suppliers might not be able to fulfill our commercial needs, which would require us to seek new manufacturing arrangements and may result in substantial delays in meeting market demand. If we consistently generate more demand for a product than a given supplier is capable of handling, it could lead to large backorders and potentially lost sales to competitive products that are readily available. This could require us to seek or fund new sources of supply, which may be difficult to find or may require terms that are less advantageous if available at all.
- *Regulatory risk.* Our manufacturing facility and those of some of our third-party suppliers are subject to ongoing periodic unannounced inspection by regulatory authorities, including the FDA, USDA and other federal, state and foreign agencies for compliance with strictly enforced Good Manufacturing Practices, regulations and similar foreign standards. We do not have control over our suppliers' compliance with these regulations and standards. Regulatory violations could potentially lead to interruptions in supply that could cause us to lose sales to readily available competitive products.
- *Developmental delays.* We may experience delays in the scale-up quantities needed for product development that could delay regulatory submissions and commercialization of our products in development, causing us to miss key opportunities.
- *Limited intellectual property rights.* We typically do not have intellectual property rights, or may have to share intellectual property rights, to the products supplied by third parties and any improvements to the manufacturing processes or new manufacturing processes for these products.

Potential problems with suppliers such as those discussed above could substantially decrease sales, lead to higher costs and/or damage our reputation with our customers due to factors such as poor quality goods or delays in order fulfillment, resulting in our being unable to sell our products effectively and substantially harming our business.

***We operate in a highly competitive industry, which could render our products obsolete or substantially limit the volume of products that we sell. This would limit our ability to compete and maintain sustained profitability.***

The market in which we compete is intensely competitive. Our competitors include independent animal health companies and major pharmaceutical companies that have animal health divisions. We also compete with independent, third-party distributors, including distributors who sell products under their own

private labels. In the point-of-care diagnostic testing market, our major competitors include IDEXX, Abaxis, and Synbiotics, a unit of Zoetis. The products manufactured by our OVP segment for sale by third parties compete with similar products offered by a number of other companies, some of which have substantially greater financial, technical, research and other resources than us and may have more established marketing, sales, distribution and service organizations than those of our OVP segment's customers. Competitors may have facilities with similar capabilities to our OVP segment, which they may operate and sell at a lower unit price to customers than our OVP segment does, which could cause us to lose customers. Companies with a significant presence in the companion animal health market, such as Bayer AG, CEVA Santé Animale, Eli Lilly, Merck, Sanofi, Vétoquinol S.A., Virbac S.A. and Zoetis may be marketing or developing products that compete with our products or would compete with them if developed. These and other competitors and potential competitors may have substantially greater financial, technical, research and other resources and larger, more established marketing, sales and service organizations than we do. Our competitors may offer broader product lines and have greater name recognition than we do. For example, if Zoetis devotes its significant commercial and financial resources to growing Synbiotics' market share, our sales could suffer significantly. Our competitors may also develop or market technologies or products that are more effective or commercially attractive than our current or future products or that would render our technologies and products obsolete. Further, additional competition could come from new entrants to the animal health care market. Moreover, we may not have the financial resources, technical expertise or marketing, sales or support capabilities to compete successfully. One of our competitors, Abaxis, recently announced agreements with units of VCA Inc. ("VCA") for the long-term supply of blood chemistry testing products to VCA-owned veterinary clinics and for the co-marketing of Abaxis' blood chemistry testing products with VCA's veterinary diagnostic laboratory offering, which may serve to intensify competition and lower our margins as well as limit our prospects to sell blood chemistry testing products to VCA-owned veterinary clinics.

If we fail to compete successfully, our ability to achieve sustained profitability will be limited and sustained profitability, or profitability at all, may not be possible.

***Obtaining and maintaining regulatory approvals in order to market our products may be costly and delay the marketing and sales of our products. Failure to meet all regulatory requirements could cause significant losses from affected inventory and the loss of market share.***

Many of the products we develop, market or manufacture may subject us to extensive regulation by one or more of the USDA, the FDA, the EPA and foreign and other regulatory authorities. These regulations govern, among other things, the development, testing, manufacturing, labeling, storage, pre-market approval, advertising, promotion and sale of some of our products. Satisfaction of these requirements can take several years and time needed to satisfy them may vary substantially, based on the type, complexity and novelty of the product. The decision by a regulatory authority to regulate a currently non-regulated product or product area could significantly impact our revenue and have a corresponding adverse impact on our financial performance and position while we attempt to comply with the new regulation, if such compliance is possible at all. The effect of government regulation may be to delay or to prevent marketing of our products for a considerable period of time and to impose costly procedures upon our activities. We have experienced in the past, and may experience in the future, difficulties that could delay or prevent us from obtaining the regulatory approval or license necessary to introduce or market our products. Such delays in approval may cause us to forego a significant portion of a new product's sales in its first year due to seasonality and advanced booking periods associated with certain products. Regulatory approval of our products may also impose limitations on the indicated or intended uses for which our products may be marketed. Difficulties in making established products to all regulatory specifications may lead to significant losses related to affected inventory as well as market share. Among the conditions for certain regulatory approvals is the requirement that our facilities and/or the facilities of our third-party manufacturers conform to current Good Manufacturing Practices and other requirements. If any regulatory authority determines that our manufacturing facilities or those of our third-party manufacturers do not conform to appropriate manufacturing requirements, we or the manufacturers of our products may be subject to sanctions, including,

but not limited to, warning letters, manufacturing suspensions, product recalls or seizures, injunctions, refusal to permit products to be imported into or exported out of the United States, refusals of regulatory authorities to grant approval or to allow us to enter into government supply contracts, withdrawals of previously approved marketing applications, civil fines and criminal prosecutions. Furthermore, third parties may perceive procedures required to obtain regulatory approval objectionable and may attempt to disrupt or otherwise damage our business as a result. In addition, certain of our agreements may require us to pay penalties if we are unable to supply products, including for failure to maintain regulatory approvals. Any of these events, alone or in unison, could damage our business.

***Our stock price has historically experienced high volatility, and could do so in the future, including experiencing a material price decline resulting from a large sale in a short period of time. In addition, our Public Common Stock has certain transfer restrictions which could reduce trading liquidity from what it otherwise would have been and have other undesired effects.***

According to the latest available filings with the SEC of which we are aware and excluding our executive officers, we have one shareholder who controls more than 5% of our shares outstanding. This shareholder holds approximately 5.5% of our shares outstanding according to the latest available filings with the SEC of which we are aware. Should this shareholder or another relatively large shareholder decide to sell a large number of shares in a short period of time, it could lead to an excess supply of our shares available for sale and correspondingly result in a significant decline in our stock price. For example, we had a shareholder who held over 16% of our shares outstanding as of September 30, 2011 sell all of its holdings in our stock on or before December 7, 2011 – and we believe this contributed to a corresponding decline in our stock price during this period.

The securities markets have experienced significant price and volume fluctuations and the market prices of securities of many microcap and small cap companies have in the past been, and can in the future be expected to be, especially volatile. During the twelve months ended December 31, 2014, our closing stock price has ranged from a low of \$8.63 to a high of \$18.13. Fluctuations in the trading price or liquidity of our Public Common Stock may adversely affect our ability to raise capital through future equity financings. Factors that may have a significant impact on the market price and marketability of our Public Common Stock include:

- stock sales by large stockholders or by insiders;
- changes in the outlook for our business;
- our quarterly operating results, including as compared to expected revenue or earnings and in comparison to historical results;
- termination, cancellation or expiration of our third-party supplier relationships;
- announcements of technological innovations or new products by our competitors or by us;
- litigation;
- regulatory developments, including delays in product introductions;
- developments or disputes concerning patents or proprietary rights;
- availability of our revolving line of credit and compliance with debt covenants;
- releases of reports by securities analysts;
- economic and other external factors; and
- general market conditions.

In the past, following periods of volatility in the market price of a company's securities, securities class action litigation has often been instituted. If a securities class action suit is filed against us, it is likely we would incur substantial legal fees and our management's attention and resources would be diverted from operating our business in order to respond to the litigation.

On May 4, 2010, our shareholders approved an amendment (the "Amendment") to our Restated Certificate of Incorporation. The Amendment places restrictions on the transfer of our stock that could adversely affect our ability to use our domestic Federal Net Operating Loss carryforward ("NOL"). In particular, the Amendment prevents the transfer of shares without the approval of our Board of Directors if, as a consequence, an individual, entity or groups of individuals or entities would become a 5-percent holder under Section 382 of the Internal Revenue Code of 1986, as amended, and the related Treasury regulations, and also prevents any existing 5-percent holder from increasing his or her ownership position in the Company without the approval of our Board of Directors. Any transfer of shares in violation of the Amendment (a "Transfer Violation") shall be void *ab initio* under the our Restated Certificate of Incorporation, as amended (our "Certificate of Incorporation") and our Board of Directors has procedures under our Certificate of Incorporation to remedy a Transfer Violation including requiring the shares causing such Transfer Violation to be sold and any profit resulting from such sale to be transferred to a charitable entity chosen by the Company's Board of Directors in specified circumstances. The Amendment could have an adverse impact on the value and trading liquidity of our stock if certain buyers who would otherwise have bid on or purchased our stock, including buyers who may not be comfortable owning stock with transfer restrictions, do not bid on or purchase our stock as a result of the Amendment. In addition, because some corporate takeovers occur through the acquirer's purchase, in the public market or otherwise, of sufficient shares to give it control of a company, any provision that restricts the transfer of shares can have the effect of preventing a takeover. The Amendment could discourage or otherwise prevent accumulations of substantial blocks of shares in which our stockholders might receive a substantial premium above market value and might tend to insulate management and the Board of Directors against the possibility of removal to a greater degree than had the Amendment not passed.

***Our future revenues depend on successful product development, commercialization and/or market acceptance, any of which can be slower than we expect or may not occur.***

The product development and regulatory approval process for many of our potential products is extensive and may take substantially longer than we anticipate. Research projects may fail. New products that we may be developing for the veterinary marketplace may not perform consistently within our expectations. Because we have limited resources to devote to product development and commercialization, any delay in the development of one product or reallocation of resources to product development efforts that prove unsuccessful may delay or jeopardize the development of other product candidates. If we fail to successfully develop new products and bring them to market in a timely manner, our ability to generate additional revenue will decrease.

Even if we are successful in the development of a product or obtain rights to a product from a third-party supplier, we may experience delays or shortfalls in commercialization and/or market acceptance of the product. For example, veterinarians may be slow to adopt a product or there may be delays in producing large volumes of a product. The former is particularly likely where there is no comparable product available or historical precedent for such a product. The ultimate adoption of a new product by veterinarians, the rate of such adoption and the extent veterinarians choose to integrate such a product into their practice are all important factors in the economic success of one of our new products and are factors that we do not control to a large extent. If our products do not achieve a significant level of market acceptance, demand for our products will not develop as expected and our revenues will be lower than we anticipate. For example, our VitalPath Blood Gas and Electrolyte Analyzer generated significantly less revenue than we anticipated following its launch in May 2010 as placements of this product with customers did not occur as we expected.

***We may face costly legal disputes, including related to our intellectual property or technology or that of our suppliers or collaborators.***

We may face legal disputes related to our business. For example, on March 12, 2015, a complaint was filed against us in the United States District Court Northern District of Illinois alleging our violation of the federal Telephone Consumer Protection Act of 1991, as amended by the Junk Fax Prevention Act of 2005, as a class action. Even if meritless, these disputes may require significant expenditures on our part and could entail a significant distraction to members of our management team or other key employees. We may have to use legal means to collect payment for goods shipped to third parties. A legal dispute leading to an unfavorable ruling or settlement could have significant material adverse consequences on our business.

We may become subject to patent infringement claims and litigation in the United States or other countries or interference proceedings conducted in the United States Patent and Trademark Office, or USPTO, to determine the priority of inventions. The defense and prosecution of intellectual property suits, USPTO interference proceedings and related legal and administrative proceedings are likely to be costly, time-consuming and distracting. As is typical in our industry, from time to time we and our collaborators and suppliers have received, and may in the future receive, notices from third parties claiming infringement and invitations to take licenses under third-party patents. Any legal action against us or our collaborators or suppliers may require us or our collaborators or suppliers to obtain one or more licenses in order to market or manufacture effected products or services. However, we or our collaborators or suppliers may not be able to obtain licenses for technology patented by others on commercially reasonable terms, or at all, may not be able to develop alternative approaches if unable to obtain licenses or current and future licenses may not be adequate, any of which could substantially harm our business.

We may also need to pursue litigation to enforce any patents issued to us or our collaborative partners, to protect trade secrets or know-how owned by us or our collaborative partners, or to determine the enforceability, scope and validity of the proprietary rights of others. Any litigation or interference proceedings will likely result in substantial expense to us and significant diversion of the efforts of our technical and management personnel. Any adverse determination in litigation or interference proceedings could subject us to significant liabilities to third parties. Further, as a result of litigation or other proceedings, we may be required to seek licenses from third parties which may not be available on commercially reasonable terms, if at all.

***We often depend on third parties for products we intend to introduce in the future. If our current relationships and collaborations are not successful, we may not be able to introduce the products we intend to introduce in the future.***

We are often dependent on third parties and collaborative partners to successfully and timely perform research and development activities to successfully develop new products. For example, we jointly developed point-of-care diagnostic products with Quidel Corporation. In other cases, we have discussed Heska marketing in the veterinary market an instrument being developed by a third party for use in the human health care market. In the future, one or more of these third parties or collaborative partners may not complete research and development activities in a timely fashion, or at all. Even if these third parties are successful in their research and development activities, we may not be able to come to an economic agreement with them. If these third parties or collaborative partners fail to complete research and development activities, fail to complete them in a timely fashion, or if we are unable to negotiate economic agreements with such third parties or collaborative partners, our ability to introduce new products will be impacted negatively and our revenues may decline. For example, we have experienced significant delays compared to our expectations in our development of products in collaboration with Rapid Diagnostek, Inc.



***We may not be able to continue to achieve sustained profitability or increase profitability on a quarterly or annual basis.***

Prior to 2005, we incurred net losses on an annual basis since our inception in 1988 and, as of December 31, 2014, we had an accumulated deficit of \$169.5 million. We have achieved only four quarters with income before income taxes greater than \$1.5 million. Accordingly, relatively small differences in our performance metrics may cause us to generate an operating or net loss in future periods. Our ability to continue to be profitable in future periods will depend, in part, on our ability to increase sales in our CCA segment, including maintaining and growing our installed base of instruments and related consumables, to maintain or increase gross margins and to limit the increase in our operating expenses to a reasonable level as well as avoid or effectively manage any unanticipated issues. We may not be able to generate, sustain or increase profitability on a quarterly or annual basis. If we cannot achieve or sustain profitability for an extended period, we may not be able to fund our expected cash needs, including the repayment of debt as it comes due, or continue our operations.

***Interpretation of existing legislation, regulations and rules, including financial accounting standards, or implementation of future legislation, regulations and rules could cause our costs to increase or could harm us in other ways.***

We prepare our financial statements in conformance with United States generally accepted accounting principles, or GAAP. These accounting principles are established by and are subject to interpretation by the SEC, the Financial Accounting Standards Board ("FASB") and others who interpret and create accounting policies. A change in those policies can have a significant effect on our reported results and may affect our reporting of transactions completed before a change is made effective. Such changes may adversely affect our reported financial results, the way we conduct our business or have a negative impact on us if we fail to track such changes. For example, we have found FASB's recent decision to codify the accounting standards has made it more difficult to research complex accounting matters, increasing the risk we will fail to account consistent with FASB rules in the future.

If our regulators and/or auditors adopt or interpret more stringent standards than we anticipate, we could experience unanticipated changes in our reported financial statements, including but not limited to restatements, which could adversely affect our business due to litigation and investor confidence in our financial statements. In addition, changes in the underlying circumstances to which we apply given accounting standards and principles may affect our results of operations and have a negative impact on us. For example, we review goodwill recognized on our consolidated balance sheets at least annually and if we were to conclude there was an impairment of goodwill, we would reduce the corresponding goodwill to its estimated fair value and recognize a corresponding expense in our statement of operations. This impairment and corresponding expense could be as large as the total amount of goodwill recognized on our consolidated balance sheets, which was \$21.2 million at December 31, 2014. There can be no assurance that future goodwill impairments will not occur if projected financial results are not met, or otherwise.

The Sarbanes-Oxley Act of 2002 ("Sarbanes-Oxley") has increased our required administrative actions and expenses as a public company since its enactment. The general and administrative costs of complying with Sarbanes-Oxley will depend on how it is interpreted over time. Of particular concern are the level of standards for internal control evaluation and reporting adopted under Section 404 of Sarbanes-Oxley. If our regulators and/or auditors adopt or interpret more stringent standards than we anticipate, we and/or our auditors may be unable to conclude that our internal controls over financial reporting are designed and operating effectively, which could adversely affect investor confidence in our financial statements and cause our stock price to decline. Even if we and our auditors are able to conclude that our internal controls over financial reporting are designed and operating effectively in such a circumstance, our general and administrative costs are likely to increase. In addition, if our stock market value is at or above a certain level

on June 30, 2015, we will be required to have our independent registered public accountant conduct an audit of our internal controls, which would increase our general and administrative costs.

Similarly, we are required to comply with the SEC's mandate to provide interactive data using the eXtensible Business Reporting Language as an exhibit to certain SEC filings. Compliance with this mandate has required a significant time investment, which has and may in the future preclude some of our employees from spending time on more productive matters. In addition, actions by other entities, such as enhanced rules to maintain our listing on the Nasdaq Capital Market, could also increase our general and administrative costs or have other adverse effects on us, as could further legislative, regulatory or rule-making action or more stringent interpretations of existing legislation, regulations and rules.

***Many of our expenses are fixed and if factors beyond our control cause our revenue to fluctuate, this fluctuation could cause greater than expected losses, cash flow and liquidity shortfalls.***

We believe that our future operating results will fluctuate on a quarterly basis due to a variety of factors which are generally beyond our control, including:

- supply of products from third-party suppliers or termination, cancelation or expiration of such relationships;
- competition and pricing pressures from competitive products;
- the introduction of new products or services by our competitors or by us;
- large customers failing to purchase at historical levels;
- fundamental shifts in market demand;
- manufacturing delays;
- shipment problems;
- information technology problems, which may prevent us from conducting our business effectively, or at all, and may also raise our costs;
- regulatory and other delays in product development;
- product recalls or other issues which may raise our costs;
- changes in our reputation and/or market acceptance of our current or new products; and
- changes in the mix of products sold.

We have high operating expenses, including those related to personnel. Many of these expenses are fixed in the short term and may increase over the course of the coming year. If any of the factors listed above cause our revenues to decline, our operating results could be substantially harmed.

***If we are unable to maintain various financial and other covenants required by our credit facility agreement we will be unable to borrow any funds under the agreement and fund our operations.***

Under our credit and security agreement with Wells Fargo, we are required to comply with various covenants, both financial and non-financial, in order to borrow under the agreement. The availability of borrowings under this agreement is expected to be important to continue to fund our operations. Beginning January 1, 2015 a key financial covenant is based on a fixed charge coverage ratio, as defined in the credit and security agreement with Wells Fargo. Although we believe we will be able to maintain compliance with all these covenants and any covenants we may negotiate in the future, there can be no assurance thereof. We have not always been able to maintain compliance with all covenants under our credit and security agreement with Wells Fargo. Although Wells Fargo has granted us a waiver of non-compliance in each case, there can be no assurance we will be able to obtain similar waivers or other modifications if needed in the future on economic terms, if at all. Failure to comply with any of the covenants, representations or warranties, or failure to modify them to allow future compliance, could result in our being in default and could cause all outstanding borrowings under our credit and security agreement to become immediately due and payable, or

impact our ability to borrow under the agreement. In addition, Wells Fargo has discretion in setting the advance rates which we may borrow against eligible assets. We may need to rely on available borrowings under the credit and security agreement to fund our operations in the future. If we are unable to borrow funds under this agreement, we will need to raise additional capital from other sources to continue our operations, which capital may not be available on acceptable terms, or at all.

***Our Public Common Stock is listed on the Nasdaq Capital Market and we may not be able to maintain that listing, which may make it more difficult for you to sell your shares. In addition, we have less than 300 record holders, which would allow us to terminate voluntarily the registration of our common stock with the SEC and after which we would no longer be eligible to maintain the listing of our Public Common Stock on the Nasdaq Capital Market.***

Our Public Common Stock is listed on the Nasdaq Capital Market. The Nasdaq has several quantitative and qualitative requirements companies must comply with to maintain this listing, including a \$1.00 minimum bid price. We completed a 1-for-10 reverse stock split effective December 30, 2010 in order to resolve an ongoing minimum bid price deficiency. While we believe we are currently in compliance with all Nasdaq requirements, there can be no assurance we will continue to meet Nasdaq listing requirements including the minimum bid price, that Nasdaq will interpret these requirements in the same manner we do if we believe we meet the requirements, or that Nasdaq will not change such requirements or add new requirements to include requirements we do not meet in the future. If we are delisted from the Nasdaq Capital Market, our Public Common Stock may be considered a penny stock under the regulations of the SEC and would therefore be subject to rules that impose additional sales practice requirements on broker-dealers who sell our securities. The additional burdens imposed upon broker-dealers may discourage broker-dealers from effecting transactions in our Public Common Stock, which could severely limit market liquidity of the Public Common Stock and any stockholder's ability to sell our securities in the secondary market. This lack of liquidity would also likely make it more difficult for us to raise capital in the future.

We have less than 300 record holders as of our latest information, a fact which would make us eligible to terminate voluntarily the registration of our common stock with the SEC and therefore suspend our reporting obligations with the SEC under the Exchange Act and become a non-reporting company. If we were to cease reporting with the SEC, we would no longer be eligible to maintain the listing of our common stock on the Nasdaq Capital Market, which we would expect to materially adversely affect the liquidity and market price for our common stock.

***We may face product returns and product liability litigation in excess of, or not covered by, our insurance coverage or indemnities and/or warranties from our suppliers. If we become subject to product liability claims resulting from defects in our products, we may fail to achieve market acceptance of our products and our sales could substantially decline.***

The testing, manufacturing and marketing of our current products as well as those currently under development entail an inherent risk of product liability claims and associated adverse publicity. Following the introduction of a product, adverse side effects may be discovered. Adverse publicity regarding such effects could affect sales of our other products for an indeterminate time period. To date, we have not experienced any material product liability claims, but any claim arising in the future could substantially harm our business. Potential product liability claims may exceed the amount of our insurance coverage or may be excluded from coverage under the terms of the policy. We may not be able to continue to obtain adequate insurance at a reasonable cost, if at all. In the event that we are held liable for a claim against which we are not indemnified or for damages exceeding the \$10 million limit of our insurance coverage or which results in significant adverse publicity against us, we may lose revenue, be required to make substantial payments which could exceed our financial capacity and/or lose or fail to achieve market acceptance.

*We may be held liable for the release of hazardous materials, which could result in extensive remediation costs or otherwise harm our business.*

Certain of our products and development programs produced at our Des Moines, Iowa facility involve the controlled use of hazardous and bio hazardous materials, including chemicals and infectious disease agents. Although we believe that our safety procedures for handling and disposing of such materials comply with the standards prescribed by applicable local, state and federal regulations, we cannot eliminate the risk of accidental contamination or injury from these materials. In the event of such an accident, we could be held liable for any fines, penalties, remediation costs or other damages that result. Our liability for the release of hazardous materials could exceed our resources, which could lead to a shutdown of our operations, significant remediation costs and potential legal liability. In addition, we may incur substantial costs to comply with environmental regulations if we choose to expand our manufacturing capacity.

**Item 1B. Unresolved Staff Comments.**

Not applicable.

**Item 2 Properties.**

Our principal administrative and research and development activities are located in Loveland, Colorado. We currently lease approximately 60,000 square feet at a facility in Loveland, Colorado under an agreement which expires in 2023. Our principal production facility located in Des Moines, Iowa, consists of 168,000 square feet of buildings on 34 acres of land, which we own. We also own a 175-acre farm used principally for testing products, located in Carlisle, Iowa. Our European facility in Fribourg, Switzerland has approximately 6,000 square feet leased under an agreement which expires in 2017.

**Item 3 Legal Proceedings.**

From time to time, we may be involved in litigation related to claims arising out of our operations. At December 31, 2014, we were not a party to any legal proceedings that are expected, individually or in the aggregate, to have a material adverse effect on our business, financial condition or operating results.

**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.**

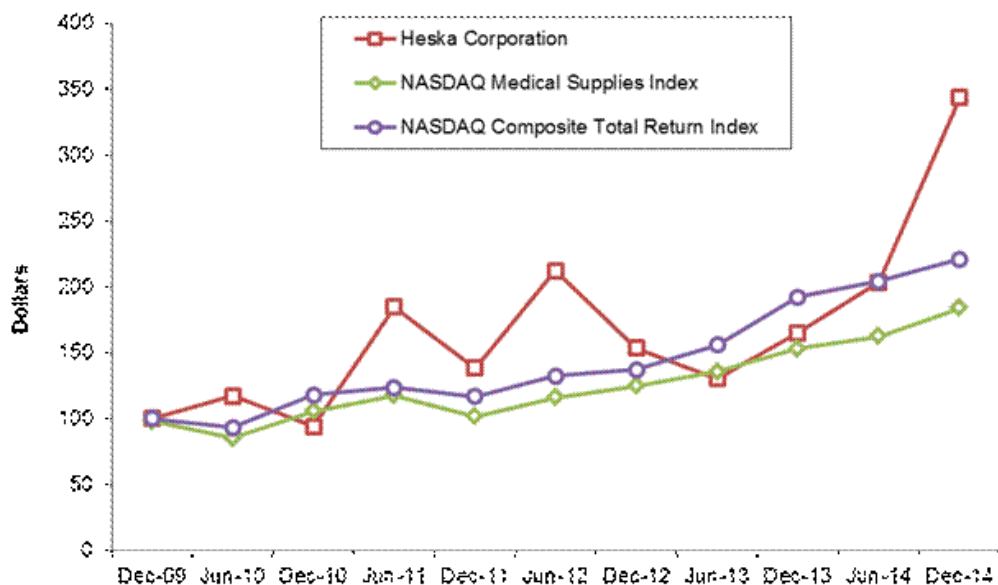
Our Public Common Stock is quoted on the Nasdaq Capital Market under the symbol "HSKA." The following table sets forth the high and low sales prices for our Public Common Stock as reported by the Nasdaq Capital Market for the periods indicated below:

	High	Low
<b>2013</b>		
First Quarter	9.37	7.70
Second Quarter	9.33	6.62
Third Quarter	6.98	5.16
Fourth Quarter	8.93	5.50
<b>2014</b>		
First Quarter	11.43	8.19
Second Quarter	12.74	10.27
Third Quarter	14.58	10.60
Fourth Quarter	18.63	11.89
<b>2015</b>		
First Quarter (through March 24)	26.68	15.58

As of February 27, 2015, there were approximately 252 record holders of our Public Common Stock, including approximately 95 participant accounts of Cede & Co.'s position held with our registrar, and approximately 3,700 beneficial stockholders. While we paid \$1.6 million in dividends in 2012, we do not anticipate any dividend payments in the foreseeable future.

### STOCK PRICE PERFORMANCE GRAPH

The following graph provides a comparison over the five-year period ended December 31, 2014 of the cumulative total shareholder return from a \$100 investment in the Company's common stock with the NASDAQ Medical Supplies Index and the NASDAQ Composite Total Return.



**Item 6 Selected Financial Data.**

The following consolidated statement of operations and consolidated balance sheets data have been derived from our consolidated financial statements. The information set forth below is not necessarily indicative of the results of future operations and should be read in conjunction with "Management's Discussion and Analysis of Financial Condition and Results of Operations" and the Consolidated Financial Statements and related Notes included as Items 7 and 8 in this Form 10-K. We completed a 1-for-10 reverse stock split effective December 30, 2010. Except as otherwise indicated, all related amounts reported below have been retroactively adjusted for the effect of this reverse stock split.

Year Ended December 31,

	2010	2011	2012	2013	2014
(in thousands, except per share amounts)					
<b>Consolidated Statement of Operations Data:</b>					
Revenue:					
Core companion animal health	\$ 55,655	\$ 57,481	\$ 61,502	\$ 66,404	\$ 72,354
Other vaccines, pharmaceuticals and products	9,796	12,584	11,303	11,935	17,483
Total revenue, net	<u>65,451</u>	<u>70,065</u>	<u>72,805</u>	<u>78,339</u>	<u>89,837</u>
Cost of revenue	<u>40,659</u>	<u>40,878</u>	<u>41,704</u>	<u>47,707</u>	<u>54,122</u>
Gross Profit	<u>24,792</u>	<u>29,187</u>	<u>31,101</u>	<u>30,632</u>	<u>35,715</u>
Operating expenses:					
Selling and marketing	14,726	15,167	18,339	19,428	19,159
Research and development	1,597	1,650	958	1,500	1,414
General and administrative	8,111	9,121	9,646	11,134	12,231
Total operating expenses	<u>24,434</u>	<u>25,938</u>	<u>28,943</u>	<u>32,062</u>	<u>32,804</u>
Operating income (loss)	358	3,249	2,158	(1,430)	2,911
Interest and other (income) expense, net	<u>289</u>	<u>(117)</u>	<u>135</u>	<u>(37)</u>	<u>(39)</u>
Income (loss) before income taxes	69	3,366	2,023	(1,393)	2,950
Income tax expense:					
Current income tax expense	61	165	214	183	47
Deferred income tax expense (benefit)	<u>(10)</u>	<u>1,056</u>	<u>606</u>	<u>(637)</u>	<u>1,304</u>
Total income tax expense (benefit)	<u>51</u>	<u>1,221</u>	<u>820</u>	<u>(454)</u>	<u>1,351</u>
Net income (loss)	<u>\$ 18</u>	<u>\$ 2,145</u>	<u>\$ 1,203</u>	<u>\$ (939)</u>	<u>\$ 1,599</u>
Net income (loss) attributable to non-controlling interest	—	—	—	257	(1,004)
Net income (loss) attributable to Heska Corporation	<u>18</u>	<u>2,145</u>	<u>1,203</u>	<u>(1,196)</u>	<u>2,603</u>
Basic net income (loss) per share attributable to Heska Corporation	<u>\$ 0.00</u>	<u>\$ 0.41</u>	<u>\$ 0.23</u>	<u>\$ (0.21)</u>	<u>\$ 0.44</u>
Diluted net income (loss) per share attributable to Heska Corporation	<u>\$ 0.00</u>	<u>\$ 0.40</u>	<u>\$ 0.22</u>	<u>\$ (0.21)</u>	<u>\$ 0.41</u>
Dividends declared per share	<u>\$ —</u>	<u>\$ —</u>	<u>\$ 0.30</u>	<u>\$ —</u>	<u>\$ —</u>
<b>Consolidated Balance Sheet Data:</b>					
Cash and cash equivalents	\$ 5,492	\$ 6,332	\$ 5,784	\$ 6,016	\$ 5,855
Total current assets	27,279	28,891	32,955	33,911	34,400
Note receivable – related party	—	—	—	1,407	1,466
Total assets	63,048	61,894	66,826	93,553	96,844
Line of credit	3,079	—	2,552	4,798	48
Other short-term borrowings, including current portion of long-term debt					
	—	—	—	132	141
Total current liabilities	12,660	9,289	14,389	17,706	15,052
Long-term debt, excluding current portion	—	—	—	369	227
Non-controlling interest	—	—	—	13,659	15,679
Public Common Stock subject to redemption	—	—	—	3,405	—
Total stockholders' equity	45,798	48,439	48,862	47,116	53,132

## **Item 7 Management's Discussion and Analysis of Financial Condition and Results of Operations.**

The following discussion and analysis of our financial condition and results of operations should be read in conjunction with "Selected Consolidated Financial Data" and the Consolidated Financial Statements and related Notes included in Items 6 and 8 of this Form 10-K. This discussion contains forward-looking statements that involve risks and uncertainties. Such statements, which include statements concerning future revenue sources and concentration, gross profit margins, selling and marketing expenses, research and development expenses, general and administrative expenses, capital resources, additional financings or borrowings and additional losses, are subject to risks and uncertainties, including, but not limited to, those discussed below and elsewhere in this Form 10-K, particularly in Item 1A "Risk Factors," that could cause actual results to differ materially from those projected. The forward-looking statements set forth in this Form 10-K are as of the close of business on March 24, 2015, and we undertake no duty and do not intend to update this information.

### **Overview**

We develop, manufacture, market, sell and support veterinary products. Our business is comprised of two reportable segments, Core Companion Animal Health ("CCA"), which represented 81% of our revenue for the twelve months ended December 31, 2014 (which we define as "LTM") and Other Vaccines, Pharmaceuticals and Products ("OVP"), which represented 19% of LTM revenue.

The CCA segment includes, primarily for canine and feline use, blood testing instruments and supplies, digital imaging products, software and services, and single use products and services such as heartworm diagnostic tests, heartworm preventive products, allergy immunotherapy products and allergy testing.

Blood testing and other non-imaging instruments and supplies represented approximately 36% of our LTM revenue. Many products in this area involve placing an instrument in the field and generating future revenue from consumables, including items such as supplies and service, as that instrument is used. Approximately 31% of our LTM revenue resulted from the sale of such consumables to an installed base of instruments and approximately 5% of our LTM revenue was from hardware revenue. A loss of, or disruption in, the supply of consumables we are selling to an installed base of instruments could substantially harm our business. All of our blood testing and other non-imaging instruments and supplies are supplied by third parties, who typically own the product rights and supply the product to us under marketing and/or distribution agreements. In many cases, we have collaborated with a third party to adapt a human instrument for veterinary use. Major products in this area include our chemistry instruments, our hematology instruments and our blood gas instruments and their affiliated operating consumables. Revenue from products in these three areas, including revenues from consumables, represented approximately 32% of our LTM revenue.

Imaging hardware, software and services represented approximately 15% of LTM revenue. Digital radiography is the largest product offering in this area, which also includes ultrasound instruments. Digital radiography solutions typically consist of a combination of hardware and software placed with a customer, often combined with an ongoing service and support contract. Our experience has been that most of the economic benefit is generated at the time of sale in this area, in contrast to the blood testing category discussed above where ongoing consumable revenue is often a larger component of economic value as a given blood testing instrument is used.



Other CCA revenue, including single use diagnostic and other tests, pharmaceuticals and biologicals as well as research and development, licensing and royalty revenue, represented approximately 29% of our LTM revenue. Since items in this area are often single use by their nature, our typical aim is to build customer satisfaction and loyalty for each product, generate repeat annual sales from existing customers and expand our customer base in the future. Products in this area are both supplied by third parties and provided by us. Major products and services in this area include our heartworm diagnostic tests, our heartworm preventives, our allergy test kits, our allergy immunotherapy and our allergy testing. Combined revenue from heartworm-related products and allergy-related products represented 27% of our LTM revenue.

We consider the CCA segment to be our core business and devote most of our management time and other resources to improving the prospects for this segment. Maintaining a continuing, reliable and economic supply of products we currently obtain from third parties is critical to our success in this area. Virtually all of our sales and marketing expenses occur in the CCA segment. The majority of our research and development spending is dedicated to this segment as well.

All our CCA products are ultimately sold primarily to or through veterinarians. In many cases, veterinarians will mark up their costs to the end user. The acceptance of our products by veterinarians is critical to our success. CCA products are sold directly to end users by us as well as through distribution relationships, such as our corporate agreement with Merck Animal Health, the sale of kits to conduct blood testing to third-party veterinary diagnostic laboratories and independent third-party distributors. Revenue from direct sales and distribution relationships represented approximately 73% and 27%, respectively, of CCA LTM revenue.

We intend to sustain profitability over the long term through a combination of revenue growth, gross margin improvement and expense control. Accordingly, we closely monitor revenue growth trends in our CCA segment. LTM revenue in this segment increased 8% as compared to pro forma revenue for the twelve months ended December 31, 2013 assuming we had consolidated Heska Imaging for the entire period.

The OVP segment includes our 168,000 square foot USDA- and FDA-licensed production facility in Des Moines, Iowa. We view this facility as an asset which could allow us to control our cost of goods on any pharmaceuticals and vaccines that we may commercialize in the future. We have increased integration of this facility with our operations elsewhere. For example, virtually all our U.S. inventory, excluding Heska Imaging, is now stored at this facility and related fulfillment logistics are managed there. CCA segment products manufactured at this facility are transferred at cost and are not recorded as revenue for our OVP segment. We view OVP reported revenue as revenue primarily to cover the overhead costs of the facility and to generate incremental cash flow to fund our CCA segment.

Our OVP segment includes private label vaccine and pharmaceutical production, primarily for cattle but also for other animals such as small mammals. All OVP products are sold by third parties under third-party labels.

We have an agreement for the production of certain bovine vaccines which was assigned by a previous distributor, Agri Laboratories, Ltd., ("AgriLabs") to, and assumed by, Eli Lilly and Company ("Eli Lilly") acting through its Elanco Animal Health division ("Elanco") in November 2013. AgriLabs previously conducted the marketing and sale of certain of these vaccines, which AgriLabs sold primarily under the Titanium® and MasterGuard® brands, under this agreement. This agreement has historically generated a significant portion of our OVP segment's revenue. Our OVP segment also produces vaccines and pharmaceuticals for other third parties.

## Critical Accounting Policies and Estimates

Our discussion and analysis of our financial condition and results of operations is based upon the consolidated financial statements, which have been prepared in accordance with U.S. generally accepted accounting principles ("GAAP"). The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities as of the date of the financial statements, and the reported amounts of revenue and expense during the periods. These estimates are based on historical experience and various other assumptions that we believe to be reasonable under the circumstances. We have identified those critical accounting policies used in reporting our financial position and results of operations based upon a consideration of those accounting policies that involve the most complex or subjective decisions or assessment. We consider the following to be our critical policies.

### Revenue Recognition

We generate our revenue through the sale of products, as well as through licensing of technology product rights, royalties and sponsored research and development. Our policy is to recognize revenue when the applicable revenue recognition criteria have been met, which generally include the following:

- Persuasive evidence of an arrangement exists;
- Delivery has occurred or services rendered;
- Price is fixed or determinable; and
- Collectability is reasonably assured.

Revenue from the sale of products is recognized after both the goods are shipped to the customer and acceptance has been received, if required, with an appropriate provision for estimated returns and allowances. We do not permit general returns of products sold. Certain of our products have expiration dates. Our policy is to exchange certain outdated, expired product with the same product. We record an accrual for the estimated cost of replacing the expired product expected to be returned in the future, based on our historical experience, adjusted for any known factors that reasonably could be expected to change historical patterns, such as regulatory actions which allow us to extend the shelf lives of our products. Revenue from both direct sales to veterinarians and sales to independent third-party distributors are generally recognized when goods are shipped. Our products are shipped complete and ready to use by the customer. The terms of the customer arrangements generally pass title and risk of ownership to the customer at the time of shipment. Certain customer arrangements provide for acceptance provisions. Revenue for these arrangements is not recognized until the acceptance has been received or the acceptance period has lapsed. We reduce our revenue by the estimated cost of any rebates, allowances or similar programs, which are used as promotional programs.

Recording revenue from the sale of products involves the use of estimates and management judgment. We must make a determination at the time of sale whether the customer has the ability to make payments in accordance with arrangements. While we do utilize past payment history, and, to the extent available for new customers, public credit information in making our assessment, the determination of whether collectability is reasonably assured is ultimately a judgment decision that must be made by management. We must also make estimates regarding our future obligation relating to returns, rebates, allowances and similar other programs.

License revenue under arrangements to sell or license product rights or technology rights is recognized as obligations under the agreement are satisfied, which generally occurs over a period of time. Generally, licensing revenue is deferred and recognized over the estimated life of the

related agreements, products, patents or technology. Nonrefundable licensing fees, marketing rights and milestone payments received under contractual arrangements are deferred and recognized over the remaining contractual term using the straight-line method.

Recording revenue from license arrangements involves the use of estimates. The primary estimate made by management is determining the useful life of the related agreement, product, patent or technology. We evaluate all of our licensing arrangements by estimating the useful life of either the product or the technology, the length of the agreement or the legal patent life and defer the revenue for recognition over the appropriate period.

We may enter into arrangements that include multiple elements. Such arrangements may include the licensing of technology and manufacturing of product. In these situations we must determine whether the various elements meet the criteria to be accounted for as separate elements. If the elements cannot be separated, revenue is recognized once revenue recognition criteria for the entire arrangement have been met or over the period that the Company's obligations to the customer are fulfilled, as appropriate. If the elements are determined to be separable, the revenue is allocated to the separate elements based on relative fair value and recognized separately for each element when the applicable revenue recognition criteria have been met. In accounting for these multiple element arrangements, we must make determinations about whether elements can be accounted for separately and make estimates regarding their relative fair values.

#### **Allowance for Doubtful Accounts**

We maintain an allowance for doubtful accounts receivable based on client-specific allowances, as well as a general allowance. Specific allowances are maintained for clients which are determined to have a high degree of collectability risk based on such factors, among others, as: (i) the aging of the accounts receivable balance; (ii) the client's past payment history; (iii) a deterioration in the client's financial condition, evidenced by weak financial condition and/or continued poor operating results, reduced credit ratings, and/or a bankruptcy filing. In addition to the specific allowance, the Company maintains a general allowance for credit risk in its accounts receivable which is not covered by a specific allowance. The general allowance is established based on such factors, among others, as: (i) the total balance of the outstanding accounts receivable, including considerations of the aging categories of those accounts receivable; (ii) past history of uncollectable accounts receivable write-offs; and (iii) the overall creditworthiness of the client base. A considerable amount of judgment is required in assessing the realizability of accounts receivable. Should any of the factors considered in determining the adequacy of the overall allowance change, an adjustment to the provision for doubtful accounts receivable may be necessary.

#### **Inventories**

Inventories are stated at the lower of cost or market, cost being determined on the first-in, first-out method. Inventories are written down if the estimated net realizable value of an inventory item is less than its recorded value. We review the carrying cost of our inventories by product each quarter to determine the adequacy of our reserves for excess/obsolescence inventory. In accounting for inventories we must make estimates regarding the estimated net realizable value of our inventory. This estimate is based, in part, on our forecasts of future sales and shelf life of product.

### **Deferred Tax Assets – Valuation Allowance**

Our deferred tax assets, such as a domestic Net Operating Loss ("NOL"), are reduced by an offsetting valuation allowance based on judgmental assessment of available evidence if we are unable to conclude that it is more likely than not that some or all of the related deferred tax assets will be realized. If we are able to conclude it is more likely than not that we will realize a future benefit from a deferred tax asset, we will reduce the related valuation allowance by an amount equal to the estimated quantity of income taxes we would pay in cash if we were not to utilize the deferred tax asset in the future. The first time this occurs in a given jurisdiction, it will result in a net deferred tax asset on our consolidated balance sheets and an income tax benefit of equal magnitude in our statement of operations in the period we make the determination. In future periods, we will then recognize as income tax expense the estimated quantity of income taxes we would have paid in cash had we not utilized the related deferred tax asset. The corresponding journal entry will be a reduction of our deferred tax asset. If there is a change regarding our tax position in the future, we will make a corresponding adjustment to the related valuation allowance.

## Results of Operations

The following table summarizes our results of operations for the three most recent fiscal years:

	Year Ended December 31,		
	2012	2013	2014
	(in thousands except per share amounts)		
<b>Consolidated Statement of Income Data:</b>			
Revenue:			
Core companion animal health	\$ 61,502	\$ 66,404	\$ 72,354
Other vaccines, pharmaceuticals and products	11,303	11,935	17,483
Total revenue, net	72,805	78,339	89,837
Cost of revenue	41,704	47,707	54,122
Gross profit	31,101	30,632	35,715
Operating expenses:			
Selling and marketing	18,339	19,428	19,159
Research and development	958	1,500	1,414
General and administrative	9,646	11,134	12,231
Total operating expenses	28,943	32,062	32,804
Operating income (loss)	2,158	(1,430)	2,911
Interest and other (income) expense, net	135	(37)	(39)
Income (loss) before income taxes	2,023	(1,393)	2,950
Income tax expense (benefit):			
Current income tax expense	214	183	47
Deferred income tax expense (benefit)	606	(637)	1,304
Total income tax expense (benefit)	820	(454)	1,351
Net income (loss)	\$ 1,203	\$ (939)	\$ 1,599
Net income (loss) attributable to non-controlling interest	\$ —	\$ 257	\$ (1,004)
Net income (loss) attributable to Heska Corporation	\$ 1,203	\$ (1,196)	\$ 2,603
Basic net income (loss) per share attributable to Heska Corporation			
	\$ 0.23	\$ (0.21)	\$ 0.44
Diluted net income (loss) per share attributable to Heska Corporation			
	\$ 0.22	\$ (0.21)	\$ 0.41
Weighted average outstanding shares used to compute basic net income (loss) per share attributable to Heska Corporation			
	5,326	5,755	5,951
Weighted average outstanding shares used to compute diluted net income (loss) per share attributable to Heska Corporation			
	5,489	5,755	6,409

### Revenue

Total revenue increased 15% to \$89.8 million in 2014 compared to \$78.3 million in 2013. Total revenue increased 8% to \$78.3 million in 2013 compared to \$72.8 million in 2012.

CCA segment revenue increased 9% to \$72.4 million in 2014, including \$13.6 million in revenue from Heska Imaging, compared to \$66.4 million in 2013. Increased sales of our instrument consumables, somewhat offset by lower sales of our heartworm diagnostic tests, were a key factor in the improvement. CCA segment revenue increased 8% to \$66.4 million in 2013 compared to \$61.5 million in 2012. The largest factor in the increase was \$12.7 million in revenue from Heska Imaging, which represents the revenue from sales after our acquisition of Heska Imaging on February 24, 2013. We also generated greater revenue from sales of our heartworm preventive to Merck Animal Health. These were somewhat offset by lower revenue from domestic sales of our heartworm diagnostic tests, our chemistry instruments, our hematology instruments, our instrument consumables and our international allergy business.

OVP segment revenue increased 47% to \$17.5 million in 2014 compared to \$11.9 million in 2013. The largest factor in the increase was greater revenue from the contract Elanco Animal Health assumed from Agrilabs in 2013. OVP segment revenue increased 6% to \$11.9 million in 2013 compared to \$11.3 million in 2012. Increased revenue from sponsored research and development activities was the largest factor in the increase.

### ***Cost of Revenue***

2014 Cost of revenue was \$54.1 million, an increase of 13% compared to \$47.7 million in 2013. Gross profit increased 17% to \$35.7 million in 2014 from \$30.6 million in 2013. 2014 gross profit included \$3.6 million in gross profit from Heska Imaging. Gross Margin, i.e. gross profit divided by total revenue, increased to 39.8% in 2014 from 39.1% in 2013. In June 2013, we recognized a reserve (the "Roche Reserve") related to an agreement (the "Roche Agreement") with Roche related to our blood gas analyzers under which we would be relieved of any minimum purchase obligations other than the Roche Agreement and Roche would be obligated to supply us with consumables and spare parts for a shortened period of time. The Roche Reserve was \$1.1 million, as follows: \$600 thousand recognized in cost of revenue related to required purchase of new instruments under the Roche Agreement, \$168 thousand recognized in cost of revenue related to instruments already in inventory and accelerated depreciation on service units, \$13 thousand recognized in sales and marketing expenses related to accelerated depreciation on demonstration units, \$99 thousand recognized in research and development expenses related to the purchase of research and development equipment required under the Roche Agreement we would not have otherwise purchased and \$243 thousand recognized in general and administrative expenses related to other anticipated costs related to the Roche Agreement. In addition, in June 2013 we recognized a \$453 thousand reserve (the "SpotChem Reserve") related to consumable and accessory inventory which we did not expect to sell. A shift in product mix to relatively lower margin product areas as well as the impact of the Roche Reserve and the SpotChem Reserve, were factors in the decline in Gross Margin for the twelve months ended December 31, 2013 as compared to the prior year period. The Roche Reserve and the Spot Chem reserve, along with product mix, were factors in the improved year-over-year Gross Margin. These factors were somewhat offset by a higher relative revenue contribution from our OVP segment, which tends to operate at lower Gross Margin than our consolidated Gross Margin, and lower Gross Margin recognized from Heska Imaging.

2013 Cost of revenue was \$47.7 million, an increase of 14% compared to \$41.7 million in 2012. Gross profit decreased 2% to \$30.6 million in 2013 from \$31.1 million in 2012. Gross Margin, i.e. gross profit divided by total revenue, decreased to 39.1% in 2013 from 42.7% in 2012. A shift in product mix to relatively lower margin product areas as well as the impact of the Roche Reserve and the Spot Chem Reserve, were factors in the decline in Gross Margin in 2013 as compared to 2012.

### ***Operating Expenses***

Selling and marketing expenses were \$19.2 million in 2014, including \$4.5 million recognized from Heska Imaging. This represents a 1% decline compared to \$19.4 million in selling and marketing expenses in 2013. Lower promotional and advertising expenses was a key factor in the change. Selling and marketing expenses increased by 6% to \$19.4 million in 2013 compared to \$18.3 million in 2012. Heska Imaging sales and marketing expense of \$3.3 million recognized in 2013 but not 2012, was the largest factor in the change. This was somewhat offset by lower spending on travel and compensation for members of our sales force and lower marketing expenses related to advertising and other third party services.

Research and development expenses were \$1.4 million in 2014, including \$273 thousand in expense recognized from Heska Imaging, a decrease of \$85 thousand as compared to \$1.5 million in 2013. Research and development expenses were \$1.5 million in 2013, including \$175 thousand in expense recognized from Heska Imaging, an increase of \$542 thousand as compared to \$958 thousand in 2012. In addition to expense recognized from Heska Imaging, which did not occur in 2012, factors in the change in both cases include a

reserve in 2013 for equipment that had been previously used in a project that was discontinued in 2013 and expenses related to the Roche Reserve, neither of which occurred in 2012 or 2014.

General and administrative expenses were \$12.2 million, including approximately \$913 thousand in expense recognized from Heska Imaging, in 2014, an increase of 10% as compared to \$11.1 million in 2013. Increased non-cash compensation expense related to new employment agreements for our Chief Executive Officer and our Executive Chair which were signed in March 2014, were key factors in the change. General and administrative expenses were \$11.1 million and included approximately \$1.0 million in expense recognized from Heska Imaging in 2013, a 15% increase as compared to \$9.6 million in 2012. In addition to expenses from and related to the acquisition of Heska Imaging, severance expenses related to the termination of certain employees and expenses related to the Roche Reserve were key factors in the increase.

#### ***Interest and Other Expense, Net***

Interest and other expense, net, was income of \$39 thousand in 2014, as compared to income of \$37 thousand in 2013 and an expense of \$135 thousand in 2012. This line item can be broken into two components: net interest expense or income and net foreign currency gains and losses. Net interest was expense of \$16 thousand in 2014, as compared to income of \$53 thousand in 2013 and an expense of \$22 thousand in 2012. We recognized net interest income related to Heska Imaging in 2013 and 2014, primarily related to income on an interest-bearing note from Cuattro Veterinary, LLC, which did not occur in 2012, although the net interest income related to Heska Imaging was lower in 2014 as compared to 2013 due to higher interest expense from increased average interest-bearing balances owed by Heska Imaging. Net foreign currency gain was \$55 thousand in 2014, as compared to net foreign currency losses of \$16 thousand in 2013 and \$113 thousand in 2012.

#### ***Income Tax Expense (Benefit)***

In 2014, we had total income tax expense of \$1.4 million, including \$1.3 million in domestic deferred income tax expense, a non-cash item, and \$47 thousand in current income tax expense. In 2013, we had total income tax benefit of \$454 thousand, including \$637 thousand in domestic deferred income tax benefit, a non-cash item, and \$183 thousand in current income tax expense. In 2012, we had total income tax expense of \$820 thousand, including \$606 thousand in domestic deferred income tax expense, and \$214 thousand in current income tax expense. We had a deferred income tax benefit in 2013 as we had a loss before income taxes in 2013. We generated domestic taxable income in 2013 due to the impact of upfront payments received in 2013, which is why we had domestic current tax expense despite a loss before income taxes and a deferred tax benefit. We had both current tax expense and deferred tax expense in 2012 and 2014 as we generated income before income taxes and utilized deferred tax assets, including our NOL, in both periods.

#### ***Net Income (Loss)***

Our 2014 net income was \$1.6 million as compared to net loss of \$939 thousand in 2013 and net income of \$1.2 million in 2012. Increased revenue and Gross Margin, somewhat offset by higher operating expenses, were factors in the improvement from 2013 to 2014. Increased operating expenses and lower Gross Margin, somewhat offset by higher revenue, were the most important factors in the decline from 2012 to 2013.

### ***Net Income (Loss) attributable to Heska Corporation***

Net income attributable to Heska Corporation was \$2.6 million in 2014, as compared to a net loss attributable to Heska Corporation of \$1.2 million in 2013 and net income attributable to Heska Corporation of \$1.2 million in 2012. The difference between this line item and "Net Income (Loss)" above is the net income or loss attributable to the minority interest in Heska Imaging, which was a net loss of \$1.0 million in 2014 and net income of \$257 thousand in 2013. There was no corresponding entry for 2012 as Heska Imaging was not consolidated into our financial statements until February 24, 2013.

### **Liquidity, Capital Resources and Financial Condition**

We have incurred net cumulative negative cash flow from operations since our inception in 1988. For the year ended December 31, 2014, we had net income of \$1.6 million. In 2014, net cash provided from operations was \$5.8 million. At December 31, 2014, we had \$5.9 million of cash and cash equivalents, working capital of \$19.3 million and \$48 thousand outstanding borrowings under our revolving line of credit, discussed below.

Net cash provided from operating activities was \$5.8 million in 2014 as compared to cash used by operating activities of \$1.4 million in 2013, a change of approximately \$7.2 million. Key factors in the change were a \$4.5 million improvement in cash provided by net income and deferred tax expense, a \$4.1 million improvement in cash provided by accounts payable, accrued liabilities and other current liability accounts primarily related to payment timing, a \$1.5 million increase in non-cash stock-based compensation which was primarily related to restricted stock grants to our Chief Executive Officer and our Executive Chair in 2014 and \$1.2 million in increased depreciation and amortization for which a factor was increased depreciation and amortization recognized from Heska Imaging rental assets. Greater cash provided from these key factors in 2014 as compared to 2013 were somewhat offset by \$3.9 million in greater cash used in inventory in 2014, some of which related to inventory transferred to property, plant and equipment as rental units. Net cash flows from operating activities used cash of \$1.4 million in 2013 as compared to \$369 thousand in 2012, a change of approximately \$1.0 million. A key factor in the change was a \$3.4 million change in cash used in moving from net income in 2012 to a net loss in 2013, including the impact on deferred tax expense or benefit. We had higher levels of accounts receivable, accounts payable, accrued liabilities and other current assets at year end 2012 than we did at year end 2013, which had corresponding cash flow effects; we experienced \$4.2 million greater cash usage due to accounts payable, accrued liabilities and other short term liabilities in 2013 as compared to 2012; we also experienced \$3.8 million greater cash generated from accounts receivable and other current assets in 2013 as compared to 2012. We were provided \$2.4 million greater cash from deferred revenue, other long-term liabilities and other long-term assets, primarily related to upfront payments received in 2013 as compared to 2012. Depreciation and amortization provided \$798 thousand more cash in 2013 as opposed to 2012, with the increase primarily related to depreciation and amortization from Heska Imaging.

Net cash flows from investing activities used cash of \$2.3 million in 2014 as compared to cash provided of \$71 thousand in 2013 and using cash of \$1.5 million in 2012. The major factor in the change in 2014 from 2013 and 2013 from 2012 was \$5.0 million in proceeds from disposition of property, including non-core vaccine-related intellectual property, which occurred in June 2013, which was somewhat offset by the incremental \$3.0 million investment in Heska Imaging in February 2013. Purchases of property and equipment increased \$407 thousand in 2014 as compared to 2013. Purchases related to loaner and demonstration equipment for Heska Imaging, somewhat offset by lower spending related to our OVP segment and capitalized software costs, was a factor in the change. Purchases of property and equipment also increased \$421 thousand in 2013 as compared to 2012. The largest factor in the change was capitalized software costs related to a new customer relationship management system.



Net cash flows from financing activities used cash of \$3.5 million in 2014, provided cash of \$1.5 million in 2013 and provided cash of \$1.3 million in 2012. In 2014, we used cash by repaying \$4.8 million under our revolving line of credit and \$178 thousand in other debt. This was somewhat offset by \$1.4 million in cash provided by the issuance of common stock under our Employee Stock Purchase Plan and upon option exercises, net of Heska Imaging distributions to the Imaging Minority which include payments required by a state tax authority. Cash provided by the issuance of common stock was greater in 2014 than in 2013 or 2012 due to increased cash from option exercises. In 2013, we borrowed \$2.2 million under our line of credit and received \$323 thousand in proceeds from the issuance of common stock under our Employee Stock Purchase Plan and upon option exercises, which were cash inflows, but we repaid \$1.0 million in other debt which was a cash outflow. The increased line of credit borrowing was largely necessary to fund the other debt repayments as well as cash used in our operating activities. In 2012, we borrowed \$2.6 million under our line of credit and received \$390 thousand in proceeds from the issuance of common stock under our Employee Stock Purchase Plan and upon option exercises, somewhat offset by funds paid to participating shareholders in our odd lot tender offer for shareholders with 99 shares or less. These cash flows were somewhat offset by \$1.6 million in dividends we paid. In 2012, we essentially borrowed under our line of credit to finance dividends paid to shareholders, our capital expenditures and cash used in our operating activities.

At December 31, 2014, Heska Corporation had accounts receivable from Heska Imaging of \$6.1 million, including accrued interest, which eliminates upon consolidation of our financial statements. These monies accrue interest at the same interest rate as Heska Corporation pays under its asset-based revolving line of credit with Wells Fargo once past due.

At December 31, 2014, we, including the balance sheets of our consolidated subsidiaries, had an account receivable from Cuattro Software, LLC of \$871 thousand, net accounts receivable from Cuattro, LLC of \$21 thousand and net accounts payable to Cuattro, LLC of \$252 thousand. These items are listed on our consolidated balance sheets as "Due from - related parties" and "Due to - related party" as Kevin S. Wilson, our Chief Executive Officer and President, Mrs. Wilson and trusts for their children and family hold a 100% interest in Cuattro, LLC and Cuattro, LLC owns a 100% interest in Cuattro Software, LLC. All monies owed are to accrue interest at the same interest rate the Company pays under its credit and security agreement with Wells Fargo once past due.

At December 31, 2014, we had a \$1.5 million Note receivable, including accrued interest, from Cuattro Veterinary, LLC. The note accrues interest at the same interest rate as the Company pays under its asset-based revolving line of credit with Wells Fargo and is due on March 15, 2016. Cuattro Veterinary, LLC sells the same digital radiography solutions outside the United States that Heska Imaging sells in the United States. The note is listed on our consolidated balance sheets as "Note receivable - related party" as Kevin S. Wilson, Mrs. Wilson and trusts for their children and family hold a majority interest in Cuattro Veterinary, LLC. This note was held by Heska Imaging at the time of our acquisition of a majority interest in Heska Imaging on February 24, 2013.

At December 31, 2014, we had a \$15.0 million asset-based revolving line of credit with Wells Fargo which has a maturity date of December 31, 2015 as part of our credit and security agreement with Wells Fargo. At December 31, 2014, we had \$48 thousand of borrowings outstanding on this line of credit. Our ability to borrow under this line of credit varies based upon available cash, eligible accounts receivable and eligible inventory. On December 31, 2014, any interest on borrowings due was to be charged at a stated rate of three month LIBOR plus 3.75% and payable monthly. We expect the stated rate will decline to LIBOR plus 2.75% as of April 1, 2015 based on the terms of the credit and security agreement and our 2014 financial performance. We are required to comply with various financial and non-financial covenants, and we have made various representations and warranties under our agreement with Wells Fargo. Among the financial covenants through December 31, 2014 were requirements for minimum capital monthly, minimum net income quarterly and capital expenditures monthly. As of January 1, 2015 a key financial covenant is based

on a fixed charge coverage ratio, as defined in our agreement with Wells Fargo. Failure to comply with any of the covenants, representations or warranties could result in our being in default on the loan and could cause all outstanding amounts payable to Wells Fargo to become immediately due and payable or impact our ability to borrow under the agreement. We were in compliance with all financial covenants as of December 31, 2014. We failed to comply with the net income covenant as of June 30, 2013, for which we obtained a waiver and subsequently negotiated new covenants as well as an extension of our asset-based revolving line of credit with Wells Fargo to December 31, 2015. At December 31, 2014, our available borrowing capacity based upon eligible accounts receivable and eligible inventory under our revolving line of credit was approximately \$8.8 million.

At December 31, 2014, we had other borrowings outstanding totaling \$368 thousand, all of which were obligations of a Heska Imaging loan from De Lage Landen Financial Services, Inc. ("DLL"). The note bears an interest rate of 6% and is due in equal monthly payments, including principal and interest, of \$13 thousand through June 2017. The note may be prepaid prior to maturity, but is subject to a surcharge in such a circumstance. \$141 thousand of principal associated with this note is listed as short term on our consolidated balance sheets as it is due within a year.

At December 31, 2014, our consolidated balance sheets included \$15.7 million in non-controlling interest. This represents the value of the aggregate position in Heska Imaging of the Imaging Minority. At the time of the Acquisition, we estimated a weighted average valuation for this position and began accreting to this value over a three year period from the date of the Acquisition using a weighted average cost of capital of 18.65%. The cost of capital assumption was provided to us by a third party with expertise in estimating such items. We evaluate the value of this position every reporting period and in 2014 decided to adjust our accretion to a weighted average accretion based on various potential outcomes and our estimate of the likelihood of such outcomes, which had the effect of lowering the accretion from what it otherwise would have been. The accretion is to be recorded as a credit where this line item has increased compared to the prior reporting period, with the corresponding debit to directly reduce additional paid-in-capital as we have an accumulated deficit. If the value of non-controlling interest were to decrease compared to the prior reporting period, we anticipate non-controlling interest would be adjusted with a debit to non-controlling interest and a corresponding credit to additional paid-in-capital.

At December 31, 2013, our consolidated balance sheets included \$3.4 million in Public Common Stock subject to redemption. This represented the shares of stock we issued to acquire our position in Heska Imaging, which may have been used to meet the purchase obligation if a Cuattro 12-month Call Option or a Cuattro 18-month Call Option had been exercised under the Operating Agreement. The Cuattro 12-month Call Option expired in February 2014 and the Imaging Minority waived the Cuattro 18-month Call Option in May 2014, and, accordingly, these shares are no longer reported as "Public Common Stock subject to redemption" following the waiver. The corresponding credit at the time of waiver increased our additional paid-in capital.

Our financial plan for 2015 indicates that our available cash and cash equivalents, together with cash from operations and borrowings expected to be available under our revolving line of credit, will be sufficient to fund our operations through 2015 and into 2016. However, our actual results may differ from this plan, and we may be required to consider alternative strategies. We may be required to raise additional capital in the future. If necessary, we expect to raise these additional funds through the increased sale of customer leases, the sale of equity securities or the issuance of new term debt secured by the same assets as the term loans which were fully repaid in 2010. There is no guarantee that additional capital will be available from these sources on acceptable terms, if at all, and certain of these sources may require approval by existing lenders. See "Risk Factors" in Item 1A of this Form 10-K for a discussion of some of the factors that affect our capital raising alternatives.

Under the Operating Agreement, should Heska Imaging meet certain performance criteria, the Imaging Minority has been granted a put option to sell us some or all of the Imaging Minority's remaining 45.4% position in Heska Imaging following the audit of our financial statements in 2015, 2016 and 2017.

Furthermore, should Heska Imaging meet certain performance criteria, and the Imaging Minority fail to exercise an applicable put to sell us all of the Imaging Minority's position in Heska Imaging following the audit of our financial statements in 2015, 2016 and 2017, we would have a call option to purchase all, but not less than all, of the Imaging Minority's position in Heska Imaging. While we intend to meet any related cash payment obligations with funds provided by our ongoing operations and assets, likely supplemented by debt financing and potentially with equity financing, there can be no assurance our results will unfold according to our expectations. These potential cash payment obligations are an important consideration for us in our cash management decisions.

We believe it is likely that Heska Imaging will meet the required performance criteria for its 2015 lowest strike put, but not its 2015 highest strike put, in 2015. In this case, the Imaging Minority would be granted a put following our 2015 audit which could require us to deliver up to \$13.6 million, as well as 25% of Heska Imaging's cash, to purchase the 45.4% of Heska Imaging we do not own. In such a case, while we have the right to deliver up to 55% of the consideration in our Public Common Stock under certain circumstances, such stock is to be valued based on 90% of market value (the "Delivery Stock Value") and is limited to approximately 650 thousand shares in any case. If the Delivery Stock Value is less than the market value of our stock at the time of the Acquisition, we do not have the right to deliver any Public Common Stock as consideration. Assuming we deliver the full 55% of the consideration in our Public Common Stock, we could still have an obligation to pay approximately \$6.1 million in cash as well as 25% of Heska Imaging's cash to the Imaging Minority in this circumstance.

We would consider acquisitions if we felt they were consistent with our strategic direction. We paid \$1.6 million in dividends in 2012, and while we may consider paying dividends again in the long term, we do not anticipate the payment of any further dividends for the foreseeable future. We conducted an odd lot tender offer in 2012 which could have led to the repurchase of approximately \$400 thousand of our stock if all eligible holders had chosen to participate, and while we may consider stock repurchase alternatives in an opportunistic manner or in the long term, we do not anticipate any stock repurchase programs in the foreseeable future.

A summary of our contractual obligations at December 31, 2014 is shown below:

Payments Due by Period (in thousands)					
	Total	Less Than 1 Year	1-3 Years	4-5 Years	After 5 Years
<b>Contractual Obligations</b>					
Long-term debt	\$ 368	\$ 141	\$ 227	\$ —	\$ —
Interest payments on debt	129	118	11	—	—
Line of credit	48	48	—	—	—
Unconditional purchase obligations	4,322	4,322	—	—	—
Operating leases	14,081	1,861	3,259	3,017	5,944
Purchase of non-controlling interest	6,214	—	6,214	—	—
Total contractual cash obligations	<u>\$ 25,162</u>	<u>\$ 6,490</u>	<u>\$ 9,711</u>	<u>\$ 3,017</u>	<u>\$ 5,944</u>

In addition to those agreements considered above where our contractual obligation is fixed, we are party to commercial agreements which may require us to make milestone payments under certain circumstances. Any milestone obligations which we believe are likely to be triggered but are not yet paid are included in "Unconditional Purchase Obligations" in the table above. We do not believe other potential milestone obligations, some of which we consider to be of remote likelihood of ever being triggered, will have a material impact on our liquidity, capital resources or financial condition in the foreseeable future.

The line item entitled "Purchase of non-controlling interest" indicates our obligations to purchase the non-controlling interest in Heska Imaging under a series of performance-based puts. We believe it is likely that Heska Imaging will meet the required performance criteria for its 2015 lowest strike put, but not its 2015 highest strike put, in 2015 and that we will be able to deliver 55% of the consideration required by the put in our Public Common Stock. The table above assumes this is the case, assumes that Heska Imaging's performance merits the maximum payout under this put, estimates Heska Imaging year end 2015 cash based on year end 2014 and assumes the Imaging Minority exercises this option in full. In such a circumstance, we would pay \$6.2 million in cash in 2016 following our 2015 audit. As discussed above, if our stock declines such that Delivery Stock Value is less than the market value of our stock at the time of Acquisition, we would not be able to deliver our Public Common Stock as consideration upon the exercise of any put by the Imaging Minority and we would have to deliver the full consideration to acquire the minority interest in cash. Furthermore, we are limited to a maximum of approximately 650 thousand shares as consideration upon the exercise of any put by the Imaging Minority, which in certain circumstances could require us to deliver more than 45% of the consideration required by a put in cash. The maximum Put Payment, excluding a change-in-control, by year is 25% of Heska Imaging's cash plus an amount as follows: \$17.0 million in 2016 following the 2015 audit, \$17.0 million in 2017 following the 2016 audit and \$36.9 million in 2018 following the 2017 audit. In addition, the Change in Control Payment is \$42.4 million in cash until at least the end of 2015.

### **Net Operating Loss Carryforwards**

As of December 31, 2014, we had a net domestic operating loss carryforward, or NOL, of approximately \$108.4 million, a domestic alternative minimum tax credit carryforward of approximately \$308 thousand and a domestic research and development tax credit carryforward of approximately \$472 thousand for federal tax purposes. Our federal NOL is expected to expire as follows if unused: \$102.5 million in 2018 through 2022, \$5.5 million in 2024 and 2025 and \$385 thousand in 2027. The NOL and tax credit carryforwards are subject to alternative minimum tax limitations and to examination by the tax authorities. In addition, we had a "change of ownership" as defined under the provisions of Section 382 of the Internal Revenue Code of 1986, as amended (an "Ownership Change"). We believe the latest Ownership Change occurred at the time of our initial public offering in July 1997.

### **Recent Accounting Pronouncements**

In May 2014, the Financial Accounting Standards Board issued Accounting Standards Update ("ASU") 2014-09, "Revenue from Contracts with Customers", which provides guidance for revenue recognition that supersedes existing revenue recognition guidance (but does not apply to nor supersede accounting guidance for lease contracts). The ASU is to be effective for reporting periods beginning after December 15, 2016, and is anticipated to be applied retrospectively to each prior reporting period presented or retrospectively with the cumulative effect of initially applying the ASU recognized at the date of initial application. The Company has not evaluated the impact of the adoption of this ASU on the Company's consolidated results.

In August 2014, the Financial Accounting Standards Board issued ASU No. 2014-15, "Presentation of Financial Statements – Going Concern: Disclosures about an Entity's Ability to Continue as a Going Concern." The new standard requires management to perform interim and annual assessments of an entity's ability to continue as a going concern within one year of the date the financial statements are issued as well as

certain disclosures if conditions or events raise substantial doubt about the entity's ability to continue as a going concern. The new guidance is effective for annual periods ending after December 15, 2016, and interim periods thereafter. The Company has not evaluated the impact of the adoption of this ASU on the Company's consolidated results.

Management has evaluated recent accounting pronouncements other than ASU No. 2014-09 and ASU No. 2014-15 and determined none would have a material impact on the Company's financial statements.

#### **Item 7A. Quantitative and Qualitative Disclosures about Market Risk.**

Market risk represents the risk of loss that may impact the financial position, results of operations or cash flows due to adverse changes in financial and commodity market prices and rates. We are exposed to market risk in the areas of changes in United States and foreign interest rates and changes in foreign currency exchange rates as measured against the United States dollar. These exposures are directly related to our normal operating and funding activities.

##### **Interest Rate Risk**

At December 31, 2014, there was approximately \$48 thousand outstanding on our line of credit with Wells Fargo. We also had approximately \$5.9 million of cash and cash equivalents at December 31, 2014, the majority of which was invested in liquid interest bearing accounts. We had no interest rate hedge transactions in place on December 31, 2014. We completed an interest rate risk sensitivity analysis based on the above and an assumed one-percentage point increase/decrease in interest rates. If market rates increase/decrease by one percentage point, we would experience a decrease/increase in annual net interest expense of approximately \$58 thousand based on our outstanding balances as of December 31, 2014.

##### **Foreign Currency Risk**

Our investment in foreign assets consists primarily of our investment in our Swiss subsidiary. Foreign currency risk may impact our results of operations. In cases where we purchase inventory in one currency and sell corresponding products in another, our gross margin percentage is typically at risk based on foreign currency exchange rates. In addition, in cases where we may be generating operating income in foreign currencies, the magnitude of such operating income when translated into U.S. dollars will be at risk based on foreign currency exchange rates. Our agreements with suppliers and customers vary significantly in regard to the existence and extent of currency adjustment and other currency risk sharing provisions. We had no foreign currency hedge transactions in place on December 31, 2014.

We have a wholly-owned subsidiary in Switzerland which uses the Swiss Franc as its functional currency. We purchase inventory in foreign currencies, primarily Euros, and sell corresponding products in U.S. dollars. We also sell products in foreign currencies, primarily Euros and Japanese Yen, where our inventory costs are largely in U.S. dollars. Based on our 2014 results of operations, currency holdings and currency-related prepaid accounts, accounts receivable and accounts payable (all of which, including currency holdings, we will refer to as "Currency Accounts") as of December 31, 2014 and the functional currency of the accounting entity where such Currency Accounts are held, the expected impact on our consolidated statements of operations, if foreign currency exchange rates were to strengthen/weaken by 25% against the dollar, would be a resulting gain/loss in operating income of approximately \$254 thousand and a currency loss/gain of \$69 thousand, if all other currencies were to strengthen/weaken by 25% against the Swiss Franc, would be a resulting loss/gain in operating income of approximately \$93 thousand and a currency gain/loss of \$352 thousand, and if all other currencies were to strengthen/weaken by 25% against the Euro, would be a resulting loss/gain in operating income of approximately \$306 thousand and a currency loss/gain of \$276 thousand.

**Item 8. Financial Statements and Supplementary Data.**

**HESKA CORPORATION**

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## REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the Board of Directors and Stockholders  
Heska Corporation  
Loveland, Colorado

We have audited the accompanying consolidated balance sheets of Heska Corporation and subsidiaries (the "Company") as of December 31, 2013 and 2014, and the related consolidated statements of operations, stockholders' equity, comprehensive income (loss), and cash flows for each of the years in the three-year period ended December 31, 2014. Our audits also included financial statement Schedule II appearing under Item 15(a)(2) of this Form 10-K. These consolidated financial statements and financial statement schedule are the responsibility of the Company's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. The Company is not required to have, nor were we engaged to perform, an audit of its internal control over financial reporting. Our audit included consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Heska Corporation and subsidiaries as of December 31, 2013 and 2014, and the results of their operations and their cash flows for each of the years in the three-year period ended December 31, 2014, in conformity with accounting principles generally accepted in the United States of America. Also, in our opinion, the related financial statement schedule, when considered in relation to the basic financial statements taken as a whole, presents fairly, in all material respects, the information set forth therein.

/s/ EKS&H LLLP

March 25, 2015  
Boulder, Colorado

**HESKA CORPORATION AND SUBSIDIARIES**  
**CONSOLIDATED BALANCE SHEETS**  
(dollars in thousands, except per share amounts)

	December 31,	
	2013	2014
<b>ASSETS</b>		
Current Assets:		
Cash and cash equivalents	\$ 6,016	\$ 5,855
Accounts receivable, net of allowance for doubtful accounts of \$209 and \$216, respectively	11,409	11,919
Due from – related parties	1,200	892
Inventories, net	11,687	12,658
Deferred tax asset, current	2,156	1,489
Other current assets	1,443	1,587
Total current assets	<u>33,911</u>	<u>34,400</u>
Property and equipment, net	9,928	13,410
Note receivable – related party	1,407	1,466
Goodwill and other intangibles	21,571	21,205
Deferred tax asset, net of current portion	26,358	25,721
Other long-term assets	378	642
Total assets	<u>\$ 93,553</u>	<u>\$ 96,844</u>
<b>LIABILITIES AND STOCKHOLDERS' EQUITY</b>		
Current liabilities:		
Accounts payable	\$ 4,448	\$ 4,897
Due to – related party	—	252
Accrued liabilities	4,420	5,130
Current portion of deferred revenue	3,908	4,584
Line of credit	4,798	48
Other short-term borrowings, including current portion of long-term note payable	132	141
Total current liabilities	<u>17,706</u>	<u>15,052</u>
Long-term note payable, net of current portion	369	227
Deferred revenue, net of current portion, and other	11,298	12,754
Total liabilities	<u>29,373</u>	<u>28,033</u>
Commitments and contingencies		
Non-Controlling Interest	13,659	15,679
Public Common Stock subject to redemption	3,405	—
Stockholders' equity:		
Preferred stock, \$.01 par value, 2,500,000 shares authorized, none issued or outstanding	—	—
Common stock, \$.01 par value, 7,500,000 shares authorized, none issued or outstanding	—	—
Public common stock, \$.01 par value, 7,500,000 shares authorized, 5,845,931 and 6,342,205 shares issued and outstanding, respectively	58	63
Additional paid-in capital	217,588	222,297
Accumulated other comprehensive income	580	283
Accumulated deficit	(171,110)	(169,511)
Total stockholders' equity	<u>47,116</u>	<u>53,132</u>
Total liability and stockholders' equity	<u>\$ 93,553</u>	<u>\$ 96,844</u>

See accompanying notes to consolidated financial statements.



**HESKA CORPORATION AND SUBSIDIARIES**  
**CONSOLIDATED STATEMENTS OF OPERATIONS**  
(in thousands, except per share amounts)

	Year Ended December 31,		
	2012	2013	2014
<b>Revenue:</b>			
Core companion animal health	\$ 61,502	\$ 66,404	\$ 72,354
Other vaccines, pharmaceuticals and products	11,303	11,935	17,483
Total revenue, net	<u>72,805</u>	<u>78,339</u>	<u>89,837</u>
Cost of revenue	<u>41,704</u>	<u>47,707</u>	<u>54,122</u>
Gross profit	<u>31,101</u>	<u>30,632</u>	<u>35,715</u>
<b>Operating expenses:</b>			
Selling and marketing	18,339	19,428	19,159
Research and development	958	1,500	1,414
General and administrative	9,646	11,134	12,231
Total operating expenses	<u>28,943</u>	<u>32,062</u>	<u>32,804</u>
Operating income (loss)	<u>2,158</u>	<u>(1,430)</u>	<u>2,911</u>
Interest and other (income) expense, net	135	(37)	(39)
Income (loss) before income taxes	<u>2,023</u>	<u>(1,393)</u>	<u>2,950</u>
<b>Income tax expense:</b>			
Current income tax expense	214	183	47
Deferred income tax expense (benefit)	606	(637)	1,304
Total income tax expense (benefit)	<u>820</u>	<u>(454)</u>	<u>1,351</u>
Net income (loss)	<u>\$ 1,203</u>	<u>\$ (939)</u>	<u>\$ 1,599</u>
Net income (loss) attributable to non-controlling interest	—	257	(1,004)
Net income (loss) attributable to Heska Corporation	<u>1,203</u>	<u>(1,196)</u>	<u>2,603</u>
<b>Basic net income (loss) per share attributable to Heska Corporation</b>			
	<u>\$ 0.23</u>	<u>\$ (0.21)</u>	<u>\$ 0.44</u>
<b>Diluted net income (loss) per share attributable to Heska Corporation</b>			
	<u>\$ 0.22</u>	<u>\$ (0.21)</u>	<u>\$ 0.41</u>
<b>Weighted average outstanding shares used to compute basic net income (loss) per share attributable to Heska Corporation</b>			
	<u>5,326</u>	<u>5,755</u>	<u>5,951</u>
<b>Weighted average outstanding shares used to compute diluted net income (loss) per share attributable to Heska Corporation</b>			
	<u>5,489</u>	<u>5,755</u>	<u>6,409</u>

See accompanying notes to consolidated financial statements.

**HESKA CORPORATION AND SUBSIDIARIES**  
**CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME (LOSS)**  
(in thousands)

	Year Ended December 31,		
	2012	2013	2014
Net income (loss)	\$ 1,203	\$ (939)	\$ 1,599
Other comprehensive income (expense):			
Minimum pension liability	(20)	182	—
Unrealized gain (loss) on available for sale investments	—	30	3
Foreign currency translation	74	72	(300)
Comprehensive income (loss)	<u>\$ 1,257</u>	<u>\$ (655)</u>	<u>\$ 1,302</u>
Comprehensive income (loss) attributable to non-controlling interest	<u>\$ —</u>	<u>\$ 257</u>	<u>\$ (1,004)</u>
Comprehensive income (loss) attributable to Heska Corporation	<u>\$ 1,257</u>	<u>\$ (912)</u>	<u>\$ 2,306</u>

See accompanying notes to consolidated financial statements.

**HESKA CORPORATION AND SUBSIDIARIES**  
**CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY**  
(in thousands)

	Common Stock		Additional Paid-in Capital	Accumulated Other Comprehensive Income (Loss)	Accumulated Deficit	Total Stockholders' Equity
	Shares	Amount				
Balances, January 1, 2012	5,250	52	217,778	242	(169,633)	48,439
Net income (loss)	—	—	—	—	1,203	1,203
Issuance of common stock related to options, ESPP and other	—	—	—	—	—	—
Recognition of stock based compensation	122	2	388	—	—	390
Dividends paid	—	—	378	—	—	378
Minimum pension liability adjustments	—	—	—	(20)	(1,602)	(1,602)
Foreign currency translation adjustments	—	—	—	74	—	(20)
Balances, December 31, 2012	5,372	54	218,544	296	(170,032)	48,862
Net income (loss)	—	—	—	—	(939)	(939)
Issuance of common stock related to options, ESPP and other	—	—	—	—	—	—
Recognition of stock based compensation	55	—	323	—	—	323
Stock issued for Heska Imaging	—	—	423	—	—	423
Stock issued for Heska Imaging Mark to Market	419	4	3,571	—	—	3,575
Accretion of non-controlling interest	—	—	(3,405)	—	—	(3,405)
Accrued distribution for Heska Imaging minority	—	—	(1,868)	—	—	(1,868)
Minimum pension liability adjustments	—	—	—	182	(139)	(139)
Unrealized gain on available for sale investments	—	—	—	30	—	30
Foreign currency translation adjustments	—	—	—	72	—	72
Balances, December 31, 2013	5,846	58	217,588	580	(171,110)	47,116
Net income (loss)	—	—	—	—	1,599	1,599
Issuance of common stock related to options, ESPP and other	—	—	—	—	—	—
Recognition of stock based compensation	496	5	1,443	—	—	1,448
Stock issued for Heska Imaging Mark to Market	—	—	1,881	—	—	1,881
Accretion of non-controlling interest	—	—	3,405	—	—	3,405
Accrued distribution for Heska Imaging minority	—	—	(2,020)	—	—	(2,020)
Minimum pension liability adjustments	—	—	—	—	—	—
Unrealized gain on available for sale investments	—	—	—	3	—	3
Foreign currency translation adjustments	—	—	—	(300)	—	(300)
Balances, December 31, 2014	6,342	\$ 63	\$ 222,297	\$ 283	\$ (169,511)	\$ 53,132

See accompanying notes to consolidated financial statements.

**HESKA CORPORATION AND SUBSIDIARIES**  
**CONSOLIDATED STATEMENTS OF CASH FLOWS**  
(in thousands)

	Year Ended December 31,		
	2012	2013	2014
<b>CASH FLOWS PROVIDED BY (USED IN) OPERATING ACTIVITIES:</b>			
Net income (loss)	\$ 1,203	\$ (939)	\$ 1,599
Adjustments to reconcile net income (loss) to cash provided by (used in) operating activities:			
Depreciation and amortization	1,699	2,497	3,712
Deferred tax (benefit) expense	606	(637)	1,304
Stock based compensation	378	423	1,881
Unrealized (gain) loss on foreign currency translation	46	20	(81)
Changes in operating assets and liabilities:			
Accounts receivable	(3,099)	(159)	(510)
Inventories	(1,405)	(1,687)	(5,592)
Other current assets	(1,551)	(642)	(73)
Accounts payable	1,298	(2,276)	900
Accrued liabilities and other	741	(130)	814
Other non-current assets	—	(179)	(263)
Deferred revenue and other	(285)	2,312	2,091
Net cash provided by (used in) operating activities	<u>(369)</u>	<u>(1,397)</u>	<u>5,782</u>
<b>CASH FLOWS PROVIDED BY (USED IN) INVESTING ACTIVITIES:</b>			
Investment in subsidiary	—	(3,019)	—
Purchases of property and equipment	(1,509)	(1,930)	(2,337)
Proceeds from disposition of property and equipment	—	5,020	6
Net cash provided by (used in) investing activities	<u>(1,509)</u>	<u>71</u>	<u>(2,331)</u>
<b>CASH FLOWS PROVIDED BY (USED IN) FINANCING ACTIVITIES:</b>			
Proceeds from issuance of common stock, net of distributions	390	323	1,430
Proceeds from (repayments of) line of credit borrowings, net	2,552	2,246	(4,751)
Proceeds from (repayments of) other debt	—	(1,025)	(178)
Dividends paid to stockholders	(1,602)	—	—
Net cash provided by (used in) financing activities	<u>1,340</u>	<u>1,544</u>	<u>(3,499)</u>
EFFECT OF EXCHANGE RATE CHANGES ON CASH	(10)	14	(114)
INCREASE IN CASH AND CASH EQUIVALENTS	(548)	232	(162)
CASH AND CASH EQUIVALENTS, BEGINNING OF YEAR	6,332	5,784	6,016
CASH AND CASH EQUIVALENTS, END OF YEAR	<u>\$ 5,784</u>	<u>\$ 6,016</u>	<u>\$ 5,855</u>
<b>SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION:</b>			
Cash paid for interest	\$ 77	\$ 78	\$ 92
Cash paid for income taxes	\$ 153	\$ 84	\$ 272
Non-cash transfer of inventory to property and equipment and other long-term assets	\$ 1,327	\$ 3,950	\$ 4,598
Prepaid applied to acquisition of Heska Imaging	\$ —	\$ 1,000	\$ —

See accompanying notes to consolidated financial statements.

**HESKA CORPORATION AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**1. ORGANIZATION AND BUSINESS**

Heska Corporation ("Heska" or the "Company") develops, manufactures, markets, sells and supports veterinary products. Heska's core focus is on the canine and feline companion animal health markets.

**2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**

*Basis of Presentation*

The accompanying consolidated financial statements include the accounts of the Company, its wholly-owned subsidiaries and its majority-owned subsidiaries since their respective dates of acquisitions. All material intercompany transactions and balances have been eliminated in consolidation. Where the Company's ownership of a subsidiary is less than 100%, the non-controlling interest is reported on the Company's consolidated balance sheets. The non-controlling interest in the Company's consolidated net income is reported as "Net income (loss) attributable to non-controlling interest" on the Company's consolidated statements of operations.

*Use of Estimates*

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates. Significant estimates are required when establishing the allowance for doubtful accounts and the provision for excess/obsolete inventory, in determining the period over which the Company's obligations are fulfilled under agreements to license product rights and/or technology rights, evaluating long-lived and intangible assets for impairment, determining the allocation of purchase price under purchase accounting, estimating the expense associated with the granting of stock options and in determining the need for, and the amount of, a valuation allowance on deferred tax assets.

*Trade Accounts Receivable*

Trade accounts receivable are recorded at the invoiced amount. The allowance for doubtful accounts is the Company's best estimate of the amount of probable credit losses in the Company's existing accounts receivable. The Company determines the allowance based on historical write-off experience. The Company reviews its allowance for doubtful accounts monthly. Past due balances over 90 days and over a specified amount are reviewed individually for collectability. Account balances are charged against the allowance after all means of collection have been exhausted and the potential for recovery is considered remote. The Company does not have any off-balance-sheet credit exposure related to its customers.

*Concentration of Credit Risk*

Financial instruments that potentially subject the Company to a concentration of credit risk consist of cash and cash equivalents and accounts receivable. The Company maintains the majority of its cash and cash equivalents with financial institutions that management believes are creditworthy in the form of demand deposits. The Company has no significant off-balance-sheet concentrations of credit risk such as foreign exchange contracts, options contracts or other foreign currency hedging arrangements. Its accounts receivable balances are due primarily from domestic veterinary clinics and individual veterinarians, and both domestic and international corporations.

**HESKA CORPORATION AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - (Continued)**

*Cash and Cash Equivalents*

Cash and cash equivalents are stated at cost, which approximates market, and include short-term, highly liquid investments with original maturities of less than three months. The Company valued its Euro and Japanese Yen cash accounts at the spot market foreign exchange rate as of each balance sheet date, with changes due to foreign exchange fluctuations recorded in current earnings. The Company held 321,411 and 652,110 Euros at December 31, 2013 and 2014, respectively. The Company held 1,252,220 and 1,252,221 Yen at December 31, 2013 and 2014, respectively. The Company held 209,486 and 166,832 Swiss Francs at December 31, 2013 and 2014, respectively. The Company held 0 and 22,761 Canadian Dollars at December 31, 2013 and 2014, respectively. The majority of the Company's cash and cash equivalents are held at U.S.-based or Swiss-based financial institutions in accounts not insured by governmental entities.

*Fair Value of Financial Instruments*

The Company's financial instruments consist of cash and cash equivalents, short-term trade receivables and payables and the Company's revolving line of credit. The carrying values of cash and cash equivalents and short-term trade receivables and payables approximate fair value. The fair value of the Company's line of credit balance is estimated based on current rates available for similar debt with similar maturities and collateral, and at December 31, 2013 and 2014, approximates the carrying value due primarily to the floating rate of interest on such debt instruments.

*Inventories*

Inventories are stated at the lower of cost or market using the first-in, first-out method. Inventory manufactured by the Company includes the cost of material, labor and overhead. If the cost of inventories exceeds estimated fair value, provisions are made to reduce the carrying value to estimated fair value.

Inventories, net consist of the following (in thousands):

	<b>December 31,</b>	
	<b>2013</b>	<b>2014</b>
Raw materials	\$ 5,787	\$ 6,298
Work in process	2,920	2,966
Finished goods	4,784	4,949
Allowance for excess or obsolete inventory	(1,804)	(1,555)
	<u>\$ 11,687</u>	<u>\$ 12,658</u>

*Property and Equipment*

Property and equipment are recorded at cost and depreciated on a straight-line basis over the estimated useful lives of the related assets. Leasehold improvements are amortized over the applicable lease period or their estimated useful lives, whichever is shorter. Maintenance and repairs are charged to expense when incurred, and major renewals and improvements are capitalized.

**HESKA CORPORATION AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - (Continued)**

Property and equipment consist of the following (in thousands):

	Estimated Useful Life	December 31,	
		2013	2014
Land	N/A	\$ 377	\$ 377
Building	10 to 20 years	2,868	2,868
Machinery and equipment	3 to 15 years	36,107	30,655
Leasehold and building improvements	7 to 15 years	5,838	5,871
Construction in progress		753	185
		45,943	39,956
Less accumulated depreciation and amortization		(36,015)	(26,546)
		<u>\$ 9,928</u>	<u>\$ 13,410</u>

The Company has utilized marketing programs whereby its instruments in inventory may be placed in a customer's location on a rental basis. The cost of these instruments is transferred to machinery and equipment or other long-term assets and depreciated, typically over a five to seven year period depending on the circumstance under which the instrument is placed with the customer. During 2012, 2013 and 2014, total costs transferred from inventory were approximately \$1.3 million, \$3.9 million and \$4.6 million, respectively.

The Company has sold certain customer rental contracts and underlying assets to a third party under the agreement that once the customer has met the customer obligations under the contract, ownership of the assets underlying the contract would be returned to the Company. The Company enters a debit to cash and a corresponding credit to deferred revenue at the time of these sales. These sales provided \$1.1 million and \$1.8 million of cash which was reported in the "deferred revenue and other" line item of the Company's consolidated statements of cash flows in 2013 and 2014, respectively, all related to the Company's 54.6%-owned subsidiary, Heska Imaging US, LLC. As the Company anticipates it will regain ownership of the assets underlying these sales, it reports these assets as part of property and equipment and depreciates these assets per its depreciation policies. The Company had \$1.3 million of net property and equipment and \$3.0 million of net property and equipment related to these transactions as December 31, 2013 and December 31, 2014, respectively, all related to the Company's 54.6%-owned subsidiary, Heska Imaging US, LLC.

Depreciation and amortization expense for property and equipment was \$1.7 million, \$2.5 million and \$3.7 million for the years ended December 31, 2012, 2013 and 2014, respectively.

*Capitalized Software*

The Company capitalizes third-party software costs, where appropriate, and reports such capitalized costs, net of accumulated amortization, on the "property and equipment" line of its consolidated balance sheets. The Company had \$791 thousand and \$587 thousand of such capitalized costs, net of accumulated amortization, on the "property and equipment" line of its consolidated balance sheets as of December 31, 2013 and December 31, 2014, respectively. Capitalized software costs in a given year are reported on the "purchases of property and equipment" line item of the Company's consolidated statements of cash flows. The Company had \$11 thousand, \$809 thousand and \$31 thousand of capitalized software costs reported on the "purchases of property and equipment" line item of its consolidated statements of cash flows for the years ended December 31, 2012, 2013 and 2014, respectively.

**HESKA CORPORATION AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS- (Continued)**

*Realizability of Long-Lived Assets*

The Company continually evaluates whether events and circumstances have occurred that indicate the remaining estimated useful life of long-lived assets may warrant revision, or that the remaining balance of these assets may not be recoverable. When deemed necessary, the Company completes this evaluation by comparing the carrying amount of the assets with the estimated undiscounted future cash flows associated with them. If such evaluations indicate that the future undiscounted cash flows of amortizable long-lived assets are not sufficient to recover the carrying value of such assets, the assets are adjusted to their estimated fair values.

*Goodwill*

Goodwill is subject to an annual assessment for impairment or sooner if there is an indication of impairment. Impairment is indicated when the carrying amount of the related reporting unit is greater than its estimated fair value.

The Company's recorded goodwill relates to the February 2013 acquisition of a majority interest in Cuatro Veterinary USA, LLC, which was subsequently renamed Heska Imaging US, LLC and the 1997 acquisition of Heska AG, the Company's Swiss subsidiary. This goodwill is reviewed at least annually for impairment. This impairment assessment is completed at the reporting unit level. The Company completed its annual analysis of the Company's Swiss subsidiary estimating that the fair value of the reporting unit exceeds the carrying value of the reporting unit including goodwill at December 15, 2014 and determined there was no indicated impairment. The key inputs to the estimated fair value included estimates of future profitability for the reporting unit as well as discount rate and operating income terminal multiple. The Company also determined there is no indication of impairment for goodwill related to the acquisition of Cuatro Veterinary USA, LLC at December 15, 2014. The key inputs to the estimated fair value included estimates of future profitability for the reporting unit as well as discount rate and operating income terminal multiple. At December 31, 2013 and 2014, goodwill was approximately \$21.0 million and \$21.0 million, respectively, and was included in the assets of the Core Companion Animal Health segment. There can be no assurance that future goodwill impairments will not occur if projected financial results are not met, or otherwise.

*Revenue Recognition*

The Company generates its revenues through sale of products and services, licensing and sale of product and technology rights, and research and development services. Revenue is accounted for in accordance with the guidelines provided by SEC Codification of Staff Accounting Bulletins, Topic 13: Revenue Recognition. The Company's policy is to recognize revenue when the applicable revenue recognition criteria have been met, which generally include the following:

- Persuasive evidence of an arrangement exists;
- Delivery has occurred or services rendered;
- Price is fixed or determinable; and
- Collectability is reasonably assured.



**HESKA CORPORATION AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - (Continued)**

Revenue from the sale of products is generally recognized after both the goods are shipped to the customer and acceptance has been received, if required, with an appropriate provision for estimated returns and other allowances. The terms of the customer arrangements generally pass title and risk of ownership to the customer at the time of shipment. Certain customer arrangements provide for acceptance provisions. Revenue for these arrangements is not recognized until the acceptance has been received or the acceptance period has lapsed. The Company maintains an allowance for sales returns based upon its customer policies and historical experience. Shipping and handling costs charged to customers are included as revenue, and the related costs are recorded as a component of cost of products sold.

In addition to its direct sales force, the Company utilizes distributors to sell its products. Distributors purchase goods from the Company, take title to those goods and resell them to their customers in the distributors' territory.

Upfront payments received by the Company under arrangements for product, patent or technology rights in which the Company retains an interest in the underlying product, patent or technology are initially deferred, and revenue is subsequently recognized over the estimated life of the agreement, product, patent or technology. Similarly, upfront payments received by the Company under agreements where the Company is obligated to maintain a product or technology sold to a third party and/or transfer know-how or technology to a third party are initially deferred and revenue is subsequently recognized over the estimated life of the agreement. Milestone payments related to an improvement in a product in which the Company retains an interest in the product are initially deferred and recognized over the estimated life of the agreement or product. The Company received upfront and milestone payments totaling \$0.0, \$7.0 million and \$3.0 million in 2012, 2013 and 2014, respectively. Revenue from royalties is recognized as the Company is informed of sales on which it is entitled to royalties.

For multiple-element arrangements that are not subject to a higher level of authoritative literature, the Company follows the authoritative guidance for accounting for revenue arrangements with multiple deliverables in determining the separate units of accounting. For those arrangements subject to appropriate separation criteria, the Company must determine whether the various elements meet the criteria to be accounted for as separate elements. If the elements cannot be separated, revenue is recognized once revenue recognition criteria for the entire arrangement have been met or over the period that the Company's obligations to the customer are fulfilled, as appropriate. If the elements are determined to be separable, the revenue is allocated to the separate elements based on relative fair value and recognized separately for each element when the applicable revenue recognition criteria have been met. In accounting for these multiple element arrangements, the Company must make determinations about whether elements can be accounted for separately and make estimates regarding their relative fair values.

*Cost of Products Sold*

Royalties payable in connection with certain licensing agreements (see Note 9) are reflected in cost of products sold as incurred.

**HESKA CORPORATION AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - (Continued)**

*Stock-Based Compensation*

During the years ended December 31, 2012, 2013 and 2014, the Company's operating income and income before income taxes were reduced by \$378 thousand, \$423 thousand and \$1.9 million, respectively, and net income was reduced by \$219 thousand, \$380 thousand and \$1.2 million, respectively, for compensation related to stock options issued and shares issued under our employee stock purchase plan. Basic and diluted earnings per share were reduced by \$0.04 and \$0.04 in 2012, \$0.07 and \$0.07 in 2013 and \$0.20 and \$0.19 in 2014, respectively. For all years presented, there was no material impact on cash flow from operations. Cash flow from financing activities was increased by approximately \$386 thousand, \$312 thousand and \$1.4 million in the years ended December 31, 2012, 2013 and 2014. At December 31, 2014, the Company had two stock-based compensation plans. See Note 7 for a description of these plans and additional disclosures regarding the plans.

*Advertising Costs*

The Company expenses advertising costs as incurred. Advertising expenses were \$701 thousand, \$386 thousand and \$111 thousand for the years ended December 31, 2012, 2013 and 2014, respectively.

*Income Taxes*

The Company records a current provision for income taxes based on estimated amounts payable or refundable on tax returns filed or to be filed each year. Deferred tax assets and liabilities are recognized for the future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases and operating loss and tax credit carryforwards. Deferred tax assets and liabilities are measured using enacted tax rates, in each tax jurisdiction, expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. The effect on deferred tax assets and liabilities of a change in tax rates is recognized in operations in the period that includes the enactment date. The overall change in deferred tax assets and liabilities for the period measures the deferred tax expense or benefit for the period. Deferred tax assets are reduced by a valuation allowance based on a judgmental assessment of available evidence if the Company is unable to conclude that it is more likely than not that some or all of the deferred tax assets will be realized.

*Basic and Diluted Net Income (Loss) Per Share*

Basic net income (loss) per common share is computed using the weighted average number of common shares outstanding during the period. Diluted net income (loss) per share is computed using the sum of the weighted average number of shares of common stock outstanding, and, if not anti-dilutive, the effect of outstanding common stock equivalents (such as stock options and warrants) determined using the treasury stock method.

For the twelve months ended December 31, 2012 and 2014, the Company reported net income attributable to Heska Corporation and therefore, dilutive common stock equivalent securities, as computed using the treasury method (but excluding options to purchase fractional shares resulting from the Company's December 2010 1-for-10 reverse stock split), were added to basic weighted average shares outstanding for the period to derive the weighted average shares for diluted earnings per share calculation. Common stock equivalent securities other than options to purchase fractional shares that were anti-dilutive for the twelve months ended December 31, 2012 and 2014, and therefore excluded, were outstanding options to purchase 643,094 and 367,225 shares of common stock, respectively. These securities are anti-dilutive primarily due to exercise prices greater than the average trading price of the Company's common stock during the twelve months ended December 31, 2012 and 2014.

**HESKA CORPORATION AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - (Continued)**

For the twelve months ended December 31, 2013, the Company reported a net loss attributable to Heska Corporation and therefore all common stock equivalent securities would be anti-dilutive and were not included in the diluted earnings per share calculation for the period. Common stock equivalent securities other than options to purchase fractional shares that were anti-dilutive for the twelve months ended December 31, 2013, and therefore excluded, were outstanding options to purchase 1,321,232 shares of common stock.

*Comprehensive Income (Loss)*

Comprehensive income (loss) includes net income adjusted for the results of certain stockholders' equity changes. Such changes include foreign currency items and minimum pension liability adjustments. At December 31, 2012, Accumulated Other Comprehensive Income (Loss) consists of \$912 thousand gain for cumulative translation adjustments, \$629 thousand loss for unrealized pension liability and \$13 thousand of unrealized gain on available for sale investments. At December 31, 2013, Accumulated Other Comprehensive Income (Loss) consists of \$984 thousand gain for cumulative translation adjustments, \$447 thousand loss for unrealized pension liability and \$43 thousand of unrealized gain on available for sale investments. At December 31, 2014, Accumulated Other Comprehensive Income (Loss) consists of \$683 thousand gain for cumulative translation adjustments, \$447 thousand loss for unrealized pension liability and \$47 thousand of unrealized gain on available for sale investments.

*Foreign Currency Translation*

The functional currency of the Company's Swiss subsidiary is the Swiss Franc. Assets and liabilities of the Company's Swiss subsidiary are translated using the exchange rate in effect at the balance sheet date. Revenue and expense accounts and cash flows are translated using an average of exchange rates in effect during the period. Cumulative translation gains and losses are shown in the consolidated balance sheets as a separate component of stockholders' equity. Exchange gains and losses arising from transactions denominated in foreign currencies (i.e., transaction gains and losses) are recognized as a component of other income (expense) in current operations, as are exchange gains and losses on intercompany transactions expected to be settled in the near term.

*Recent Accounting Pronouncements*

In May 2014, the Financial Accounting Standards Board issued Accounting Standards Update ("ASU") No. 2014-09, "Revenue from Contracts with Customers", which provides guidance for revenue recognition that supersedes existing revenue recognition guidance (but does not apply to nor supersede accounting guidance for lease contracts). The ASU is to be effective for reporting periods beginning after December 15, 2016, and is anticipated to be applied retrospectively to each prior reporting period presented or retrospectively with the cumulative effect of initially applying the ASU recognized at the date of initial application. The Company has not evaluated the impact of the adoption of this ASU on the Company's consolidated results.

In August 2014, the Financial Accounting Standards Board issued ASU No. 2014-15, "Presentation of Financial Statements - Going Concern: Disclosures about an Entity's Ability to Continue as a Going Concern." The new standard requires management to perform interim and annual assessments of an entity's ability to continue as a going concern within one year of the date the financial statements are issued as well as certain disclosures if conditions or events raise substantial doubt about the entity's ability to continue as a going concern. The new guidance is effective for annual periods ending after December 15, 2016, and interim periods thereafter. The Company has not evaluated the impact of the adoption of this ASU on the Company's consolidated results.

**HESKA CORPORATION AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - (Continued)**

**3. ACQUISITION AND RELATED PARTY ITEMS**

On February 24, 2013, the Company acquired a 54.6% interest in Cuatro Veterinary USA, LLC ("Cuatro Vet USA") for approximately \$7.6 million in cash and stock, including more than \$4 million in cash (the "Acquisition"). Immediately following and as a result of the transaction, former Cuatro Vet USA unit holders owned approximately 7.2% of the Company's Public Common Stock. The remaining minority position (45.4%) in Cuatro Vet USA is subject to purchase by Heska under performance-based puts and calls following calendar year 2015, 2016 and 2017. Should Heska undergo a change in control, as defined, prior to the end of 2017, Cuatro Vet USA minority unit holders will be entitled to sell their Cuatro Vet USA units to Heska at the highest call value they could have otherwise obtained.

The Company accounted for the acquisition pursuant to ASC No. 805, "Business Combinations." Accordingly, it recorded assets acquired, liabilities assumed and non-controlling interests at their estimated fair values. The intangible assets and non-controlling interest were valued based on a report from an independent third party. The following summarizes the aggregate consideration paid by the Company and the allocation of the purchase price (in thousands):

<b>Consideration</b>			
Cash		\$	4,073
Stock			3,571
Total		\$	<u>7,644</u>
Inventories		\$	1,466
Notes from Cuatro Veterinary, LLC, due March 15, 2016			1,360
Other tangible assets			1,278
Intangible assets			688
Goodwill			19,994
Notes payable and other borrowings			(1,527)
Accounts payable			(1,424)
Other assumed liabilities			(2,399)
Total Net Assets Acquired		\$	19,436
Non-controlling interest			(11,792)
Total		\$	<u>7,644</u>

Intangible assets and their amortization periods are as follows:

Trade name	Useful Life (in years)	Fair Value
	2.75	\$ 688
		<u>\$ 688</u>

**HESKA CORPORATION AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - (Continued)**

The Company believes goodwill is a function of several factors. Cuattro Vet USA had assembled a workforce highly knowledgeable in the veterinary imaging area. These individuals had acquired the training necessary to identify opportunities for the Cuattro Vet USA to sell products, including training related to which components from existing systems could be utilized within the Cuattro Vet USA's solution to minimize the out-of-pocket cost to the customer. Cuattro Vet USA had demonstrated an ability to combine disparate assets including but not limited to digital radiography detectors, positioning aides such as tunnels and tables, viewing computers and other accessories along with embedded software and support, data hosting and other services to provide customers with a simple, efficient and convenient experience in utilizing advanced data imaging technology far in excess of what a typical customer could have created individually with similar but separately purchased assets and services. The Company anticipated bundling and cross promotion programs, including potentially in one customer contract, could enhance the revenue of both the Company and Cuattro Vet USA following the Acquisition. The ability of Cuattro Vet USA to generate estimated future cash flows due to these factors supports the goodwill calculated at the closing of the Acquisition and the current carrying value of the goodwill on the Company's consolidated balance sheets. The Company estimates it had approximately \$6.9 million in tax deductible goodwill from the Acquisition at the closing of the Acquisition.

Cuattro Vet USA was subsequently renamed Heska Imaging US, LLC ("Heska Imaging") and markets, sells and supports digital radiography and ultrasound products along with embedded software and support, data hosting and other services.

Shawna M. Wilson, Clint Roth, DVM, Steven M. Asakowicz, Rodney A. Lippincott, Kevin S. Wilson and Cuattro, LLC own approximately 29.75%, 8.39%, 4.09%, 3.07%, 0.05% and 0.05% of Heska Imaging, respectively. Kevin S. Wilson is the Chief Executive Officer and President of the Company and the spouse of Shawna M. Wilson. Steven M. Asakowicz serves as Executive Vice President, Companion Animal Health Sales for the Company. Rodney A. Lippincott serves as Executive Vice President, Companion Animal Health Sales for the Company. Mr. Wilson, Mrs. Wilson and trusts for their children and family own a 100% interest in Cuattro, LLC. Cuattro, LLC owns a 100% interest in Cuattro Software, LLC. Mr. Wilson, Mrs. Wilson and trusts for their children and family own a majority interest in Cuattro Veterinary, LLC and Cuattro Medical, LLC.

In 2013, following the Acquisition closing, Cuattro, LLC charged Heska Imaging \$6.8 million, primarily related to digital imaging products, for which there is an underlying supply contract with minimum purchase obligations, software and services as well as other operating expenses; Heska Corporation charged Heska Imaging \$2.2 million, primarily related to sales expenses; Heska Corporation net charged Cuattro, LLC \$140 thousand, primarily related to facility usage and other services. In 2014, Cuattro, LLC charged Heska Imaging \$10.5 million, primarily related to digital imaging products, for which there is an underlying supply contract with minimum purchase obligations, software and services as well as other operating expenses; Heska Corporation charged Heska Imaging \$3.9 million, primarily related to sales expenses; Heska Corporation net charged Cuattro, LLC \$219 thousand, primarily related to facility usage and other services.

At December 31, 2014, Heska Imaging had a \$1.5 million note receivable, including accrued interest, from Cuattro Veterinary, LLC, which is due on March 15, 2016 and which is listed as "Note receivable - related party" on the Company's consolidated balance sheets; Heska Imaging had accounts receivable from Cuattro Software, LLC of \$871 thousand, which is included in "Due from - related parties" on the Company's consolidated balance sheets; Heska Corporation had net accounts receivable from Cuattro, LLC of \$21 thousand which is included in "Due from - related parties" on the Company's consolidated balance sheets; Heska Imaging had net accounts payable to Cuattro, LLC of \$252 thousand which is included in "Due to - related party" on the Company's consolidated balance sheets; Heska Corporation had accounts receivable from Heska Imaging of \$6.1 million, including accrued interest, which

**HESKA CORPORATION AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - (Continued)**

eliminated in consolidation of the Company's financial statements; all monies owed accrue interest at the same interest rate Heska Corporation pays under its credit and security agreement with Wells Fargo Bank, National Association ("Wells Fargo") once past due with the exception of the note receivable, which accrues at this rate to its maturity date.

The aggregate position in Heska Imaging of the unit holders who hold the 45.4% of Heska Imaging that Heska Corporation does not own (the "Put Value") is being accreted to its estimated redemption value in accordance with Heska Imaging's Operating Agreement. Since the Operating Agreement contains certain put rights that are out of the control of the Company, authoritative guidance requires the non-controlling interest, which includes the estimated value of such put rights, to be displayed outside of the equity section of the consolidated balance sheets. The adjustment to increase or decrease the Put Value to its expected redemption value and to estimate any distributions required under Heska Imaging's Operating Agreement to the unit holders who hold the 45.4% of Heska Imaging that Heska Corporation does not own (the "Imaging Minority") each reporting period is recorded to stockholders' equity in accordance with United States Generally Accepted Accounting Principles.

The following is a reconciliation of the non-controlling interest balance (in thousands):

Beginning at December 31, 2013	\$	13,659
Accretion of Put Value		2,020
Balance at December 31, 2014	\$	15,679

In addition, Heska Imaging made a distribution of approximately \$2 thousand during the twelve months ended December 31, 2014, approximately \$1 thousand of which was to the Imaging Minority and which has been recorded on the "Proceeds from issuance of common stock, net of distributions" line item of the Company's consolidated statements of cash flows.

Cuatro Vet USA generated net revenue of \$26.4 million and net loss of \$1.6 million, inclusive of net loss of \$747 thousand attributable to non-controlling interest, for the period from February 24, 2013 to December 31, 2014. The following unaudited pro forma financial information presents the combined results of the Company and Cuatro Vet USA, in thousands, as if the Acquisition had closed on January 1, 2012.

	Year Ended December 31,	
	2013	2014
Revenue, net	\$ 79,239	\$ 89,837
Net income (loss) attributable to Heska Corporation	(1,948)	2,603
Basic earnings (loss) per share attributable to Heska Corporation	\$ (0.34)	\$ 0.44
Diluted earnings (loss) per share attributable to Heska Corporation	(0.34)	0.41

**4. CREDIT FACILITY AND LONG-TERM DEBT**

The Company has a credit and security agreement with Wells Fargo which expires December 31, 2015. The agreement includes a \$15.0 million asset-based revolving line of credit with a stated interest rate at December 31, 2014 of LIBOR plus 3.75% (4.125%). The Company anticipates the stated interest rate will decline to LIBOR plus 2.75% as of April 1, 2015 based on the terms of credit and security agreement and the Company's 2014 financial performance. There is an annual minimum interest charge of \$100 thousand under the agreement. Amounts due under the credit facility are secured by a first security interest in essentially all of the Company's assets excluding assets securing the term debt referenced below, which is an obligation of Heska Imaging and which was outstanding when the Company acquired a majority interest in Heska Imaging. Under the agreement, the Company is required to comply with certain covenants, both

**HESKA CORPORATION AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - (Continued)**

financial and non-financial. Among the financial covenants through December 31, 2014 are requirements for minimum capital monthly, minimum net income quarterly and capital expenditures monthly. Beginning January 1, 2015 a key financial covenant is based on a fixed charge coverage ratio, as defined in the credit and security agreement with Wells Fargo. The amount available for borrowings under the line of credit varies based upon available cash, eligible accounts receivable and eligible inventory. As of December 31, 2014, there was \$48 thousand of borrowings outstanding and there was approximately \$8.8 million available capacity for borrowings under the line of credit agreement.

Long-term debt consists of the following (dollars in thousands):

	December 31,	
	2013	2014
Term loan with a financial entity, secured by demo equipment, due in monthly installments beginning July 2012 with the balance paid in full in June 2017 and a stated interest rate of 6.0%.	\$ 501	\$ 368
Less current portion of long-term debt	132	141
Long-term debt, net of current portion	<u>\$ 369</u>	<u>\$ 227</u>

Maturities of long-term debt as of December 31, 2014 were as follows (in thousands):

<u>Year Ending December 31,</u>	
2015	\$ 141
2016	149
2017	78
	<u>\$ 368</u>

**5. SUPPLEMENTAL DISCLOSURE OF INTEREST AND OTHER EXPENSE (INCOME) INFORMATION**

	Year Ended December 31,		
	2012	2013	2014
	(in thousands)		
Interest and other expense (income):			
Interest income	\$ (95)	\$ (127)	\$ (190)
Interest expense	117	74	206
Other, net	113	16	(55)
	<u>\$ 135</u>	<u>\$ (37)</u>	<u>\$ (39)</u>

**6. INCOME TAXES**

As of December 31, 2014, the Company had a domestic net operating loss carryforward ("NOL"), of approximately \$108.4 million, a domestic alternative minimum tax credit of approximately \$307 thousand and a domestic research and development tax credit carryforward of approximately \$472 thousand for federal tax purposes. The Company's federal NOL is expected to expire as follows if unused: \$102.5 million in 2018 through 2022, \$5.5 million in 2024 and 2025 and \$385 thousand in 2027. The NOL and tax credit carryforwards are subject to alternative minimum tax limitations and to examination by the tax authorities. In addition, the Company had a "change of ownership" as defined under the provisions of Section 382 of the Internal Revenue Code of 1986, as amended (an "Ownership Change").

**HESKA CORPORATION AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - (Continued)**

The Company does not believe this Ownership Change will place a significant restriction on its ability to utilize its NOL in the future. The Company has established a valuation allowance against those NOL's for which it is estimated to be more likely than not that they will expire unutilized.

The Company is subject to income taxes in the U.S. federal jurisdiction, and various foreign, state and local jurisdictions. Tax regulations within each jurisdiction are subject to the interpretation of the related tax laws and regulations and require significant judgment to apply. In the United States, the tax years 2011 – 2013 remain open to examination by the federal Internal Revenue Service and the tax years 2010 – 2013 remain open for various state taxing authorities.

The components of income (loss) before income taxes were as follows (in thousands):

	<b>Year Ended December 31,</b>		
	<b>2012</b>	<b>2013</b>	<b>2014</b>
Domestic	\$ 1,869	\$ (1,508)	\$ 2,837
Foreign	154	115	113
	<u>\$ 2,023</u>	<u>\$ (1,393)</u>	<u>\$ 2,950</u>

Temporary differences that give rise to the components of deferred tax assets are as follows (in thousands):

	<b>December 31,</b>	
	<b>2013</b>	<b>2014</b>
<b>Current deferred tax assets:</b>		
Inventory	\$ 692	\$ 643
Accrued compensation	131	124
Net operating loss carryforwards – domestic	1,589	1,198
Stock and Stock Options	443	57
Other	695	601
	<u>3,550</u>	<u>2,623</u>
Valuation allowance	(1,394)	(1,134)
Total current deferred tax assets	<u>\$ 2,156</u>	<u>\$ 1,489</u>
<b>Noncurrent deferred tax assets:</b>		
Research and development tax credit	\$ 598	\$ 472
Alternative minimum tax credit	297	308
Deferred revenue	3,978	4,396
Property and equipment	2,006	1,777
Net operating loss carryforwards – domestic	36,445	39,079
Other	60	(732)
	<u>43,384</u>	<u>45,300</u>
Valuation allowance	(17,026)	(19,579)
Total noncurrent deferred tax assets	<u>\$ 26,358</u>	<u>\$ 25,721</u>



**HESKA CORPORATION AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - (Continued)**

The components of the income tax expense (benefit) are as follows (in thousands):

	Year Ended December 31,		
	2012	2013	2014
Current income tax expense (benefit):			
Federal	\$ 41	\$ 95	\$ 11
State	140	62	7
Foreign	33	26	29
Total current expense (benefit)	<u>214</u>	<u>183</u>	<u>47</u>
Deferred income tax expense (benefit):			
Federal	560	(583)	1,181
State	46	(54)	123
Foreign	—	—	—
Total deferred expense (benefit)	<u>606</u>	<u>(637)</u>	<u>1,304</u>
Total income tax expense (benefit)	<u>\$ 820</u>	<u>\$ (454)</u>	<u>\$ 1,351</u>

The Company's income tax expense (benefit) relating to income (loss) for the periods presented differs from the amounts that would result from applying the federal statutory rate to that income (loss) as follows:

	Year Ended December 31,		
	2012	2013	2014
Statutory federal tax rate	34 %	34 %	34 %
State income taxes, net of federal benefit	4 %	3 %	5 %
Non-controlling interest in Heska Imaging US, LLC	—	6 %	12 %
Other permanent differences	6 %	(10) %	(3) %
Change in tax rate	(1) %	— %	2 %
Foreign rate difference	(1) %	(1) %	0 %
Change in valuation allowance	(638) %	(13) %	78 %
Other	637 %	13 %	(82) %
Effective income tax rate	<u>41 %</u>	<u>33 %</u>	<u>46 %</u>

ASC 740 provides detailed guidance for the financial statement recognition, measurement and disclosure of uncertain tax positions recognized in the financial statements. Tax positions must meet a "more-likely-than-not" recognition threshold before a benefit is recognized in the financial statements. As of December 31, 2014, the Company has not recorded a liability for uncertain tax positions. The Company would recognize interest and penalties related to uncertain tax positions in income tax (benefit)/expense. No interest and penalties related to uncertain tax positions were accrued at December 31, 2014.

## 7. CAPITAL STOCK

### Stock Option Plans

The Company has two stock option plans which authorize granting of stock options and stock purchase rights to employees, officers, directors and consultants of the Company to purchase shares of common stock. In 1997, the board of directors adopted the 1997 Stock Incentive Plan (the "1997 Plan") and terminated two prior option plans. All shares that remained available for grant under the terminated plans were incorporated into the 1997 Plan, including shares subsequently cancelled under prior plans. In May 2012, the stockholders approved an amendment to the 1997 Plan allowing for an increase of 250,000 shares and an annual increase through 2016 based on the number of non-employee directors serving as of the Company's Annual Meeting of Stockholders, subject to a maximum of 45,000 shares per year. In May 2003, the stockholders approved a new plan, the 2003 Equity Incentive Plan, which allows for the granting

**HESKA CORPORATION AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - (Continued)**

of options for up to 239,050 shares of the Company's common stock. The number of shares reserved for issuance under both plans as of December 31, 2014 was 212,026.

The stock options granted by the board of directors may be either incentive stock options ("ISOs") or non-qualified stock options ("NQs"). The exercise price for options under all of the plans may be no less than 100% of the fair value of the underlying common stock for ISOs or 85% of fair value for NQs. Options granted will expire no later than the tenth anniversary subsequent to the date of grant or three months following termination of employment, except in cases of death or disability, in which case the options will remain exercisable for up to twelve months. Under the terms of the 1997 Plan, in the event the Company is sold or merged, outstanding options will either be assumed by the surviving corporation or vest immediately.

There are four key inputs to the Black-Scholes model which the Company uses to estimate fair value for options which it issues: expected term, expected volatility, risk-free interest rate and expected dividends, all of which require the Company to make estimates. The Company's estimates for these inputs may not be indicative of actual future performance and changes to any of these inputs can have a material impact on the resulting estimated fair value calculated for the option. The Company's expected term input was estimated based on the Company's historical experience for time from option grant to option exercise for all employees in 2012, 2013 and 2014; the Company treated all employees in one grouping in all three years. The Company's expected volatility input was estimated based on the Company's historical stock price volatility in 2012, 2013 and 2014. The Company's risk-free interest rate input was determined based on the U.S. Treasury yield curve at the time of option issuance in 2012, 2013 and 2014. The Company's expected dividends input were 4.3% in 2012, zero in 2013 and zero in 2014. Weighted average assumptions used in 2012, 2013 and 2014 for each of these four key inputs are listed in the following table:

	2012	2013	2014
Risk-free interest rate	0.38%	0.75%	1.21%
Expected lives	3.0 years	3.4 years	3.4 years
Expected volatility	57%	46%	43%
Expected dividend yield	4.3%	0%	0%

A summary of the Company's stock option plans, excluding options to purchase fractional shares resulting from the Company's December 2010 1-for-10 reverse stock split, is as follows:

	Year Ended December 31,					
	2012		2013		2014	
	Options	Weighted Average Exercise Price	Options	Weighted Average Exercise Price	Options	Weighted Average Exercise Price
Outstanding at beginning of period	1,448,675	\$ 10.425	1,245,161	\$ 11.054	1,321,232	\$ 10.386
Granted at Market	137,950	\$ 9.534	275,654	\$ 7.532	134,800	\$ 16.398
Cancelled	(118,330)	\$ 11.373	(166,286)	\$ 11.437	(218,926)	\$ 17.786
Exercised	(223,134)	\$ 5.863	(33,297)	\$ 6.488	(162,855)	\$ 7.234
Outstanding at end of period	1,245,161	\$ 11.054	1,321,232	\$ 10.386	1,074,251	\$ 10.110
Exercisable at end of period	971,029	\$ 12.129	939,458	\$ 11.556	729,175	\$ 9.800

**HESKA CORPORATION AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - (Continued)**

The total estimated fair value of stock options granted during the years ended December 31, 2012, 2013 and 2014 were computed to be approximately \$402 thousand, \$701 thousand and \$712 thousand, respectively. The amounts are amortized ratably over the vesting periods of the options. The weighted average estimated fair value of options granted during the years ended December 31, 2012, 2013 and 2014 was computed to be approximately \$2.92, \$2.54 and \$5.28, respectively. The total intrinsic value of options exercised during the years ended December 31, 2012, 2013 and 2014 was \$1.1 million, \$42 thousand and \$737 thousand, respectively. The cash proceeds from options exercised during the years ended December 31, 2012, 2013 and 2014 was \$263 thousand, \$161 thousand and \$1.2 million.

The following table summarizes information about stock options outstanding and exercisable at December 31, 2014, excluding outstanding options to purchase an aggregate of 37.4 fractional shares resulting from the Company's December 2010 1-for-10 reverse stock split with a weighted average remaining contractual life of 0.89 years, a weighted average exercise price of \$10.55 and exercise prices ranging from \$4.40 to \$22.50. The Company intends to issue whole shares only from option exercises.

Exercise Prices	Options Outstanding			Options Exercisable	
	Number of Options Outstanding at December 31, 2014	Weighted Average Remaining Contractual Life in Years	Weighted Average Exercise Price	Number of Options Exercisable at December 31, 2014	Weighted Average Exercise Price
\$ 2.70 - \$ 7.29	246,696	5.92	\$ 5.631	220,240	\$ 5.498
\$ 7.30 - \$ 8.34	231,546	8.67	\$ 7.490	84,020	\$ 7.669
\$ 8.35 - \$ 9.73	214,800	5.06	\$ 8.647	150,408	\$ 8.685
\$ 9.74 - \$15.80	186,682	3.41	\$ 12.481	178,480	\$ 12.440
\$15.81 - \$22.50	194,527	6.33	\$ 18.250	96,027	\$ 18.374
\$ 2.70 - \$22.50	<u>1,074,251</u>	5.98	\$ 10.110	<u>729,175</u>	\$ 9.800

As of December 31, 2014, there was \$1.2 million of total unrecognized compensation expense related to outstanding stock options. That cost is expected to be recognized over a weighted-average period of 2.0 years with all cost to be recognized by the end of December 2018, assuming all options vest according to the vesting schedules in place at December 31, 2014. As of December 31, 2014, the aggregate intrinsic value of outstanding options was \$8.7 million and the aggregate intrinsic value of exercisable options was \$6.1 million.

*Employee Stock Purchase Plan (the "ESPP")*

Under the 1997 Employee Stock Purchase Plan, the Company is authorized to issue up to 375,000 shares of common stock to its employees, of which 374,169 had been issued as of December 31, 2014. Employees of the Company who are expected to work at least 20 hours per week and five months per year are eligible to participate. Under the terms of the plan, employees can choose to have up to 10% of their annual base earnings withheld to purchase the Company's common stock. During the period from January 1, 2012 to June 30, 2013, the Company's ESPP had a five-year offering period and six-month accumulation periods ending on each June 30 and December 31. The purchase price of stock on June 30 and December 31 was 85% of the fair market value at purchase.

**HESKA CORPORATION AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - (Continued)**

Beginning on July 1, 2013, the Company's ESPP had a 27-month offering period and three-month accumulation periods ending on each March 31, June 30, September 30 and December 31. The purchase price of stock on March 31, June 30, September 30 and December 31 was the lesser of (1) 85% of the fair market value at the time of purchase and (2) the greater of (i) 95% of the fair market value at the beginning of the applicable offering period or (ii) 65% of the fair market value at the time of purchase. In addition, participating employees may purchase shares under the ESPP at the beginning of an applicable offering period for a purchase price of stock equal to 95% of the fair market value at such time or at 5 pm on a day other than March 31, June 30, September 30 and December 31 during the applicable offering period for a purchase price of stock equal to 95% of the fair market value at purchase.

Since July 1, 2013, the Company has estimated the fair values of stock purchase rights granted under the ESPP using the Black-Scholes pricing model and the following weighted average assumptions:

	<u>2013</u>	<u>2014</u>
Risk-free interest rate	0.21%	0.23%
Expected lives	1.3 years	1.3 years
Expected volatility	34%	34%
Expected dividend yield	0%	0%

For the years ended December 31, 2012, 2013 and 2014, the weighted-average fair value of the purchase rights granted was \$1.45, \$1.28 and \$2.61 per share, respectively.

*Restricted Stock Issuance*

On March 26, 2014, the Company issued 63,572 shares to Robert B. Grieve, Ph.D., who is currently the Company's Executive Chair, pursuant to an employment agreement between Dr. Grieve and the Company effective as of March 26, 2014 (the "Grieve Employment Agreement"). The shares were issued in five tranches and are subject to time-based vesting and other provisions outlined in the Grieve Employment Agreement. All shares are to vest in full as of April 30, 2017.

On March 26, 2014, the Company issued 110,000 shares to Mr. Wilson pursuant to an employment agreement between Mr. Wilson and the Company effective as of March 26, 2014 (the "Wilson Employment Agreement"). The shares were issued in four equal tranches and are subject to time-based vesting and other provisions outlined in the Wilson Employment Agreement. The first tranche vested on September 26, 2014, and each of the three remaining tranches is to vest on the succeeding March 26 until all shares are vested in full as of March 26, 2017. On May 6, 2014, the Company issued an additional 130,000 shares to Mr. Wilson following a vote of approval on the issuance by the Company's stockholders. The shares were issued in ten equal tranches, five of which were subject to vesting based on the achievement of certain stock price targets as defined and further described in the Wilson Employment Agreement and five of which were subject to vesting based on certain "Adjusted EBITDA" targets as defined and further described in the Wilson Employment Agreement. All shares subject to vesting based on "Adjusted EBITDA" vested based on the Company's 2014 performance and one of five tranches based on the achievement of certain stock price targets had vested as of December 31, 2014.

**HESKA CORPORATION AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - (Continued)**

*Restrictions on the transfer of Company stock*

The Company's Restated Certificate of Incorporation, as amended (the "Certificate of Incorporation"), places restrictions (the "Transfer Restrictions") on the transfer of the Company's stock that could adversely affect the Company's ability to utilize its domestic Federal Net Operating Loss Position. In particular, the Transfer Restrictions prevent the transfer of shares without the approval of the Company's Board of Directors if, as a consequence of such transfer, an individual, entity or groups of individuals or entities would become a 5-percent holder under Section 382 of the Internal Revenue Code of 1986, as amended, and the related Treasury regulations, and also prevents any existing 5-percent holder from increasing his or her ownership position in the Company without the approval of the Company's Board of Directors. Any transfer of shares in violation of the Transfer Restrictions (a "Transfer Violation") shall be void *ab initio* under the Certificate of Incorporation, and the Company's Board of Directors has procedures under the Certificate of Incorporation to remedy a Transfer Violation including requiring the shares causing such Transfer Violation to be sold and any profit resulting from such sale to be transferred to a charitable entity chosen by the Company's Board of Directors in specified circumstances.

**8. MAJOR CUSTOMERS**

One customer represented approximately 12% of the Company's 2014 revenue and 13% of the Company's 2013 revenue and another customer represented approximately 11% of the Company's 2014 revenue. One customer represented approximately 11% of the Company's accounts receivable at December 31, 2014 and 12% of the Company's accounts receivable at December 31, 2013 and another entity represented 16% of the Company's accounts receivable at December 31, 2013. No other customers represented 10% or more of revenue for 2012, 2013 or 2014 nor 10% or more of accounts receivable at December 31, 2013 or December 31, 2014.

**9. COMMITMENTS AND CONTINGENCIES**

The Company holds certain rights to market and manufacture all products developed or created under certain research, development and licensing agreements with various entities. In connection with such agreements, the Company has agreed to pay the entities royalties on net product sales. In the years ended December 31, 2012, 2013 and 2014, royalties of \$503 thousand, \$391 thousand and \$388 thousand became payable under these agreements, respectively.

The Company has contracts with suppliers for unconditional annual minimum inventory purchases and milestone obligations to third parties the Company believes are likely to be triggered currently totaling approximately \$4.3 million for fiscal 2015.

The Company has entered into operating leases for its office and research facilities and certain equipment with future minimum payments as of December 31, 2014 as follows (in thousands):

<u>Year Ending December 31,</u>		
2015	\$	1,861
2016		1,642
2017		1,617
2018		1,513
2019		1,504
Thereafter		5,944
	<u>\$</u>	<u>14,081</u>

**HESKA CORPORATION AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - (Continued)**

The Company had rent expense of \$1.8 million, \$1.8 million and \$1.9 million in 2012, 2013 and 2014, respectively.

From time to time, the Company may be involved in litigation relating to claims arising out of its operations. At December 31, 2014, the Company was not a party to any legal proceedings that were expected, individually or in the aggregate, to have a material adverse effect on our business, financial condition or operating results.

The Company's current terms and conditions of sale include a limited warranty that its products and services will conform to published specifications at the time of shipment and a more extensive warranty related to certain of its products. The Company also sells a renewal warranty for certain of its products. The typical remedy for breach of warranty is to correct or replace any defective product, and if not possible or practical, the Company will accept the return of the defective product and refund the amount paid. Historically, the Company has incurred minimal warranty costs. The Company's warranty reserve on December 31, 2014 was \$449 thousand.

**10. SEGMENT REPORTING**

The Company is comprised of two reportable segments, Core Companion Animal Health ("CCA") and Other Vaccines, Pharmaceuticals and Products ("OVP"). The Core Companion Animal Health segment includes diagnostic instruments and supplies, as well as single use diagnostic and other tests, pharmaceuticals and vaccines, primarily for canine and feline use. The CCA segment also includes digital radiography and ultrasound products along with embedded software and support, data hosting and other services from Heska Imaging after February 24, 2013. These products are sold directly by the Company as well as through independent third-party distributors and through other distribution relationships. CCA segment products manufactured at the Des Moines, Iowa production facility included in the OVP segment's assets are transferred at cost and are not recorded as revenue for the OVP segment. The Other Vaccines, Pharmaceuticals and Products segment includes private label vaccine and pharmaceutical production, primarily for cattle, but also for other animals including small mammals. All OVP products are sold by third parties under third-party labels.

Summarized financial information concerning the Company's reportable segments is shown in the following table (in thousands):

**HESKA CORPORATION AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - (Continued)**

	<b>Core Companion Animal Health</b>	<b>Other Vaccines, Pharmaceuticals and Products</b>	<b>Total</b>
<b>2012:</b>			
Total revenue	\$ 61,502	\$ 11,303	\$ 72,805
Operating income (loss)	1,160	998	2,158
Interest expense	91	26	117
Total assets	55,071	11,755	66,826
Net assets	39,726	9,136	48,862
Capital expenditures	634	875	1,509
Depreciation and amortization	862	837	1,699

	<b>Core Companion Animal Health</b>	<b>Other Vaccines, Pharmaceuticals and Products</b>	<b>Total</b>
<b>2013:</b>			
Total revenue	\$ 66,404	\$ 11,935	\$ 78,339
Operating income (loss)	(2,295)	865	(1,430)
Interest expense	45	29	74
Total assets	81,041	12,512	93,553
Net assets	37,732	9,384	47,116
Capital expenditures	512	1,418	1,930
Depreciation and amortization	1,691	806	2,497

	<b>Core Companion Animal Health</b>	<b>Other Vaccines, Pharmaceuticals and Products</b>	<b>Total</b>
<b>2014:</b>			
Total revenue	\$ 72,354	\$ 17,483	\$ 89,837
Operating income (loss)	1,198	1,713	2,911
Interest expense	153	53	206
Total assets	85,361	11,483	96,844
Net assets	44,520	8,612	53,132
Capital expenditures	1,864	473	2,337
Depreciation and amortization	2,954	758	3,712

Total revenue by principal geographic area was as follows (in thousands):

	<b>For the Years Ended December 31,</b>		
	<b>2012</b>	<b>2013</b>	<b>2014</b>
United States	\$ 64,552	\$ 71,713	\$ 83,584
Europe	2,996	2,738	2,264
Other International	5,257	3,888	3,989
Total	\$ 72,805	\$ 78,339	\$ 89,837

**HESKA CORPORATION AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - (Continued)**

Total assets by principal geographic areas were as follows (in thousands):

	For the Years Ended December 31,		
	2012	2013	2014
United States	\$ 63,980	\$ 90,572	\$ 93,977
Europe	2,846	2,981	2,867
Other International	—	—	—
<b>Total</b>	<b>\$ 66,826</b>	<b>\$ 93,553</b>	<b>\$ 96,844</b>

**11. QUARTERLY FINANCIAL INFORMATION (unaudited)**

The following summarizes selected quarterly financial information for each of the two years in the periods ended December 31, 2013 and 2014 (amounts in thousands, except per share data).

	Q1	Q2	Q3	Q4	Total
<b>2013:</b>					
Total revenue	\$ 18,979	\$ 18,261	\$ 17,595	\$ 23,504	\$ 78,339
Gross profit	7,802	5,020	7,406	10,404	30,632
Operating income (loss)	(682)	(3,578)	75	2,755	(1,430)
Net income (loss)	(352)	(2,467)	(18)	1,898	(939)
Net income (loss) attributable to Heska Corporation	(386)	(2,228)	241	1,177	(1,196)
Basic net income (loss) per share attributable to Heska Corporation	(0.07)	(0.38)	0.04	0.20	(0.21)
Diluted net income (loss) per share attributable to Heska Corporation	(0.07)	(0.38)	0.04	0.20	(0.21)
<b>2014:</b>					
Total revenue	\$ 20,793	\$ 22,916	\$ 21,805	\$ 24,323	\$ 89,837
Gross profit	8,279	9,077	8,317	10,042	35,715
Operating income (loss)	(101)	917	341	1,754	2,911
Net income (loss)	(273)	778	15	1,079	1,599
Net income (loss) attributable to Heska Corporation	192	1,069	513	829	2,603
Basic net income (loss) per share attributable to Heska Corporation	0.03	0.18	0.09	0.14	0.44
Diluted net income (loss) per share attributable to Heska Corporation	0.03	0.17	0.08	0.12	0.41



**Item 9. Changes in and Disagreements with Accountants on Accounting and Financial Disclosure.**

None.

**Item 9A. Controls and Procedures.**

***Evaluation of Disclosure Controls and Procedures.***

Our management, with the participation of our chief executive officer and our chief financial officer, evaluated the effectiveness of our disclosure controls and procedures, as defined by Rule 13a-15 of the Exchange Act, as of December 31, 2014. Based on this evaluation, our chief executive officer and chief financial officer have concluded that our disclosure controls and procedures are effective to provide reasonable assurance that information we are required to disclose in reports that we file or submit under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in the SEC's rules and forms and that such information is accumulated and communicated to our management, including our chief executive officer and chief financial officer, as appropriate, to allow timely decisions regarding disclosure.

***Management's Report on Internal Control Over Financial Reporting.***

Our management is responsible for establishing and maintaining adequate internal control over financial reporting as defined in Rules 13a-15(f) and 15d-15(f) under the Exchange Act. Under the supervision and with the participation of our management, including our chief executive officer and chief financial officer, the Company conducted an evaluation of the effectiveness of its internal control over financial reporting based on criteria outlined in the 1992 COSO Internal Control over Financial Reporting – Guidance for Smaller Public Companies, a supplemental implementation guide issued in 2007 which modified criteria established in the framework in Internal Control—Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission. Based on this evaluation, the Company's management has concluded that the Company's internal control over financial reporting was effective as of December 31, 2014.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risks that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate. Accordingly, even an effective system of internal control will provide only reasonable assurance that the objectives of the internal control system are met.

This annual report does not include an attestation report of our independent registered public accounting firm regarding internal control over financial reporting. Management's report was not subject to attestation by our independent registered public accounting firm pursuant to rules of the Securities and Exchange Commission that permit us to provide only management's report in this annual report.

***Changes in Internal Control over Financial Reporting.***

There has been no change in our internal control over financial reporting during the fourth fiscal quarter covered by this Form 10-K that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

**Item 9B. Other Information.**

None.

**PART III**

Certain information required by Part III is incorporated by reference to our definitive Proxy Statement filed with the Securities and Exchange Commission in connection with the solicitation of proxies for our 2014 Annual Meeting of Stockholders.

**Item 10. Directors, Executive Officers and Corporate Governance.**

**Executive Officers**

The information required by this item with respect to executive officers is incorporated by reference to Item 1 of this report and can be found under the caption "Executive Officers of the Registrant."

**Directors**

The information required by this section with respect to our directors will be incorporated by reference to the information in the sections entitled "Election of Directors" and "Section 16(a) Beneficial Ownership Reporting Compliance" in the Proxy Statement.

**Code of Ethics**

Our Board of Directors has adopted a code of ethics for our senior executive and financial officers (including our principal executive officer, principal financial officer and principal accounting officer). The code of ethics is available on our website at [www.heska.com](http://www.heska.com). We intend to disclose any amendments to or waivers from the code of ethics at that location.

**Audit Committee**

The information required by this section with respect to our Audit Committee will be incorporated by reference to the information in the section entitled "Board Structure and Committees" in the Proxy Statement.

**Section 16(a) Beneficial Ownership Reporting Compliance**

The information required by this item is incorporated by reference to the information in the section entitled "Section 16(a) Beneficial Ownership Reporting Compliance" in the Proxy Statement.

**Item 11. Executive Compensation.**

The information required by this section will be incorporated by reference to the information in the sections entitled "Director Compensation," "Executive Compensation," "Compensation Committee Report" and "Compensation Committee Interlocks and Insider Participation" in the Proxy Statement.

**Item 12. Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters.**

The other information required by this section will be incorporated by reference to the information in the section entitled "Common Stock Ownership of Certain Beneficial Owners and Management" in the Proxy Statement.

## Equity Compensation Plan Information

The following table sets forth information about our common stock that may be issued upon exercise of options and rights under all of our equity compensation plans as of December 31, 2014, including the 1988 Stock Option Plan, the 1997 Stock Incentive Plan, the 2003 Stock Incentive Plan and the 1997 Employee Stock Purchase Plan. Our stockholders have approved all of these plans.

Plan Category	(a) Number of Securities to be Issued Upon Exercise of Outstanding Options and Rights (1)	(b) Weighted-Average Exercise Price of Outstanding Options and Rights (1)	(c) Number of Securities Remaining Available for Future Issuance Under Equity Compensation Plans (excluding securities reflected in column (a))
Equity Compensation Plans Approved by Stockholders	1,074,251	\$10.11	212,026
Equity Compensation Plans Not Approved by Stockholders	None	None	None
Total	1,074,251	\$10.11	212,026

(1) Excluding outstanding options to purchase an aggregate of 37.4 fractional shares resulting from our December 2010 reverse stock split.

### Item 13. Certain Relationships and Related Transactions and Director Independence.

The information required by this section will be incorporated by reference to the information in the sections entitled "Board Structures and Committees" and "Significant Relationships and Transactions with Directors, Officers or Principal Stockholders" in the Proxy Statement.

### Item 14. Principal Accountant Fees and Services.

The information required by this section will be incorporated by reference to the information in the section entitled "Auditor Fees and Services" in the Proxy Statement.

The information required by Part III to the extent not set forth herein, will be incorporated herein by reference to our definitive Proxy Statement for the 2015 Annual Meeting of Stockholders.

**PART IV**

**Item 15. Exhibits and Financial Statement Schedules.**

(a) The following documents are filed as a part of this Form 10-K.

**(1) Financial Statements:**

Reference is made to the Index to Consolidated Financial Statements under Item 8 in Part II of this Form 10-K.

**(2) Financial Statement Schedules:**

Schedule II – Valuation and Qualifying Accounts.

**SCHEDULE II**

**HESKA CORPORATION AND SUBSIDIARIES  
VALUATION AND QUALIFYING ACCOUNTS**  
(amounts in thousands)

	<b>Balance at Beginning of Year</b>	<b>Additions charged to Costs and Expenses</b>	<b>Other Additions</b>	<b>Deductions</b>	<b>Balance At End of Year</b>
<b>Allowance for doubtful accounts</b>					
Year ended:					
December 31, 2012	\$ 174	\$ 76	—	\$ (95) (a)	\$ 155
December 31, 2013	\$ 155	\$ 98	—	\$ (44) (a)	\$ 209
December 31, 2014	\$ 209	\$ 143	—	\$ (136) (a)	\$ 216

(a) Write-offs of uncollectible accounts.

**(3) Exhibits:**

The exhibits listed below are required by Item 601 of Regulation S-K. Each management contract or compensatory plan or arrangement required to be filed as an exhibit to this Form 10-K has been identified.

<b>Exhibit Number</b>	<b>Notes</b>	<b>Description of Document</b>
3(i)	(16)	Restated Certificate of Incorporation of the Registrant.
3(ii)	(16)	Certificate of Amendment to Restated Certificate of Incorporation of Registrant.
3(iii)	(16)	Certificate of Amendment to the Restated Certificate of Incorporation, as amended, of Registrant.
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21.1		Subsidiaries of the Company.
23.1		Consent of EKS&H LLLP, Independent Registered Public Accounting Firm.
24.1		Power of Attorney (See Signature Page of this Form 10-K).
31.1		Certification of Chief Executive Officer Pursuant to Rule 13a-14(a) and Rule 15d-14(a) of the Securities Exchange Act, as amended.
31.2		Certification of Chief Executive Officer and Chief Financial Officer Pursuant to 18 U.S.C. 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
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101.INS		XBRL Instance Document.
101.SCH		XBRL Taxonomy Extension Schema Document.
101.CAL		XBRL Taxonomy Extension Calculation Linkbase Document.
101.DEF		XBRL Taxonomy Extension Definition Linkbase Document.
101.PRE		XBRL Taxonomy Extension Presentation Linkbase Document.
101.LAB		XBRL Taxonomy Extension Label Linkbase Document.



Notes

- \* Indicates management contract or compensatory plan or arrangement.
- + Portions of the exhibit have been omitted pursuant to a request for confidential treatment.
- \*\* Furnished herewith but not filed.
- (1) Filed with the Registrant's Form 10-Q for the quarter ended September 30, 1997.
- (2) Filed with the Registrant's Form 10-K for the year ended December 31, 2001.
- (3) Filed with the Registrant's Form 10-Q for the quarter ended September 30, 2002.
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- (16) Filed with the Registrant's Form 10-K for the year ended December 31, 2012.
- (17) Filed with the Registrant's Form 10-Q for the quarter ended March 31, 2013.
- (18) Filed with the Registrant's Form 10-Q for the quarter ended June 30, 2013.
- (19) Filed with the Registrant's Form 8-K/A on August 29, 2013.
- (20) Filed with the Registrant's Form 10-Q for the quarter ended September 30, 2013.
- (21) Filed with the Registrant's Form 10-K for the year ended December 31, 2013.
- (22) Filed with the Registrant's Form 10-Q for the quarter ended March 31, 2014.
- (23) Filed with the Registrants' Form 10-Q for the quarter ended June 30, 2014.
- (24) Filed with the Registrants' Form 10-Q for the quarter ended September 30, 2014.

## SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the Registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized, on March 25, 2015.

### HESKA CORPORATION

By: /s/ KEVIN S. WILSON  
Kevin S. Wilson  
Chief Executive Officer and President

## POWER OF ATTORNEY

KNOW ALL PERSONS BY THESE PRESENTS, that each person whose signature appears below constitutes and appoints Robert B. Grieve, Ph.D., Jason A. Napolitano and Nancy Wisnewski, Ph.D., and each of them, his or her true and lawful attorneys-in-fact, each with full power of substitution, for him or her in any and all capacities, to sign any amendments to this report on Form 10-K and to file the same, with exhibits thereto and other documents in connection therewith, with the Securities and Exchange Commission, hereby ratifying and confirming all that each of said attorneys-in-fact or their substitute or substitutes may do or cause to be done by virtue hereof.

Pursuant to the requirements of the Securities and Exchange Act of 1934, this report has been signed below by the following persons on behalf of the Registrant and in the capacities and on the dates indicated:

<u>Signature</u>	<u>Title</u>	<u>Date</u>
<u>/s/ KEVIN S. WILSON</u> Kevin S. Wilson	Chief Executive Officer, President and Director	March 25, 2015
<u>/s/ JASON A. NAPOLITANO</u> Jason A. Napolitano	Executive Vice President, Chief Financial Officer and Secretary (Principal Financial Officer and Principal Accounting Officer)	March 25, 2015
<u>/s/ ROBERT B. GRIEVE</u> Robert B. Grieve, Ph.D.	Executive Chair	March 25, 2015
<u>/s/ SHARON L. RILEY</u> Sharon L. Riley	Lead Director	March 25, 2015
<u>/s/ WILLIAM A. AYLESWORTH</u> William A. Aylesworth	Director	March 25, 2015
<u>/s/ G. IRWIN GORDON</u> G. Irwin Gordon	Director	March 25, 2015
<u>/s/ BONNIE J. TROWBRIDGE</u> Bonnie J. Trowbridge	Director	March 25, 2015
<u>/s/ DAVID E. SVEEN</u> David E. Sveen, Ph.D.	Director	March 25, 2015
<u>/s/ CAROL A. WRENN</u> Carol A. Wrenn	Director	March 25, 2015

## Exhibit Index

### (3) Exhibits:

The exhibits listed below are required by Item 601 of Regulation S-K. Each management contract or compensatory plan or arrangement required to be filed as an exhibit to this Form 10-K has been identified.

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31.1		Certification of Chief Executive Officer Pursuant to Rule 13a-14(a) and Rule 15d-14(a) of the Securities Exchange Act, as amended.
31.2		Certification of Chief Financial Officer Pursuant to Rule 13a-14(a) and Rule 15d-14(a) of the Securities Exchange Act, as amended.
32.2**		Certification of Chief Executive Officer and Chief Financial Officer Pursuant to 18 U.S.C. 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
101.INS		XBRL Instance Document.
101.SCH		XBRL Taxonomy Extension Schema Document.
101.CAL		XBRL Taxonomy Extension Calculation Linkbase Document.
101.DEF		XBRL Taxonomy Extension Definition Linkbase Document.
101.PRE		XBRL Taxonomy Extension Presentation Linkbase Document.
101.LAB		XBRL Taxonomy Extension Label Linkbase Document.

Notes

- \* Indicates management contract or compensatory plan or arrangement.
- + Portions of the exhibit have been omitted pursuant to a request for confidential treatment.
- \*\* Furnished herewith but not filed.
- (1) Filed with the Registrant's Form 10-Q for the quarter ended September 30, 1997.
- (2) Filed with the Registrant's Form 10-K for the year ended December 31, 2001.
- (3) Filed with the Registrant's Form 10-Q for the quarter ended September 30, 2002.
- (4) Filed with the Registrant's Form 10-K for the year ended December 31, 2002.
- (5) Filed with the Registrant's Form 10-Q for the quarter ended September 30, 2004.
- (6) Filed with the Registrant's Form 10-K for the year ended December 31, 2004.
- (7) Filed with the Registrant's Form 10-Q for the quarter ended June 30, 2005.
- (8) Filed with the Registrant's Form 10-K for the year ended December 31, 2006.
- (9) Filed with the Registrant's Form 10-K for the year ended December 31, 2007.
- (10) Filed with the Registrant's Form 10-Q for the quarter ended September 30, 2008.
- (11) Filed with the Registrant's Form 10-K for the year ended December 31, 2008.
- (12) Filed with the Registrant's Form 10-K for the year ended December 31, 2010.
- (13) Filed with the Registrant's Form 10-Q for the quarter ended June 30, 2011.
- (14) Filed with the Registrant's Form 10-Q for the quarter ended September 30, 2011.
- (15) Filed with the Registrant's Form 10-K for the year ended December 31, 2011.
- (16) Filed with the Registrant's Form 10-K for the year ended December 31, 2012.
- (17) Filed with the Registrant's Form 10-Q for the quarter ended March 31, 2013.
- (18) Filed with the Registrant's Form 10-Q for the quarter ended June 30, 2013.
- (19) Filed with the Registrant's Form 8-K/A on August 29, 2013.
- (20) Filed with the Registrant's Form 10-Q for the quarter ended September 30, 2013.
- (21) Filed with the Registrant's Form 10-K for the year ended December 31, 2013.
- (22) Filed with the Registrant's Form 10-Q for the quarter ended March 31, 2014.
- (23) Filed with the Registrants' Form 10-Q for the quarter ended June 30, 2014.
- (24) Filed with the Registrants' Form 10-Q for the quarter ended September 30, 2014.

**HESKA CORPORATION**  
**1997 STOCK INCENTIVE PLAN**  
**(AS AMENDED MARCH 6, 2007 AND MAY 5, 2009,**  
**AMENDED AND RESTATED ON FEBRUARY 22, 2012,**  
**FURTHER AMENDED ON MARCH 25, 2014**  
**AND FURTHER AMENDED AND RESTATED ON MAY 6, 2014)**

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**HESKA CORPORATION  
1997 STOCK INCENTIVE PLAN**

**(AS AMENDED MARCH 6, 2007 AND MAY 5, 2009  
AND AMENDED AND RESTATED ON FEBRUARY 22, 2012,  
FURTHER AMENDED ON MARCH 25, 2014  
AND FURTHER AMENDED AND RESTATED ON MAY 6, 2014)**

**ARTICLE 1.  
INTRODUCTION**

The Plan was adopted by the Board effective March 15, 1997, and was subsequently amended on each of March 6, 2007 and May 5, 2009. In connection with completion of the Company's 1-for-10 Reverse Stock Split on December 30, 2010, pursuant to Article 9 the Compensation Committee of the Board approved adjustments to the Plan to reduce by a factor of ten the number of Options and Restricted Shares, and related underlying Common Shares, available for issuance under the Plan. On February 22, 2012, the Board approved, subject to stockholder approval, further amendments to the Plan to increase the aggregate number of Common Shares available for issuance under the Plan. On March 25, 2014, the Board approved, subject to stockholder approval, further amendments to the Plan to increase the aggregate number of Common Shares available for issuance under the Plan, and adding provisions permitting the Committee to make Awards under the Plan that will meet the performance-based compensation exception to Code Section 162(m).

The purpose of the Plan is to promote the long-term success of the Company and the creation of stockholder value by (a) encouraging Employees, Outside Directors and Consultants to focus on critical long-range objectives, (b) encouraging the attraction and retention of Employees, Outside Directors and Consultants with exceptional qualifications and (c) linking Employees, Outside Directors and Consultants directly to stockholder interests through increased stock ownership. The Plan seeks to achieve this purpose by providing for Awards in the form of Restricted Shares or Options (which may constitute incentive stock options or nonstatutory stock options).

The Plan shall be governed by, and construed in accordance with, the laws of the State of Colorado (except its choice-of-law provisions).

**ARTICLE 2.  
ADMINISTRATION.**

2.1 **COMMITTEE COMPOSITION.** The Plan shall be administered by the Committee. The Committee shall consist exclusively of two or more directors of the Company, who shall be appointed by the Board. In addition, the composition of the Committee shall satisfy:

- (a) Such requirements as the Securities and Exchange Commission may establish for administrators acting under plans intended to qualify for exemption under Rule 16b-3 (or its successor) under the Exchange Act; and
- (b) Such requirements as the Internal Revenue Service may establish for outside directors acting under plans intended to qualify for exemption under section 162(m)(4)(C) of the Code.

The Board may also appoint one or more separate committees of the Board, each composed of one or more directors of the Company who need not satisfy the foregoing requirements,

who may administer the Plan with respect to Employees and Consultants who are not considered officers or directors of the Company under section 16 of the Exchange Act, may grant Awards under the Plan to such Employees and Consultants and may determine all terms of such Awards.

- 2.2 **COMMITTEE RESPONSIBILITIES.** The Committee shall (a) select the Employees, Outside Directors and Consultants who are to receive Awards under the Plan, (b) determine the type, number, vesting requirements and other features and conditions of such Awards, (c) interpret the Plan and (d) make all other decisions relating to the operation of the Plan. The Committee may adopt such rules or guidelines as it deems appropriate to implement the Plan. The Committee's determinations under the Plan shall be final and binding on all persons.

### **ARTICLE 3. SHARES AVAILABLE FOR GRANTS.**

- 3.1 **BASIC LIMITATION.** Common Shares issued pursuant to the Plan may be authorized but unissued shares or treasury shares. Prior to December 30, 2010, the effective date of the Reverse Stock Split, the aggregate number of Options and Restricted Shares awarded under the Plan were not to exceed: (a) 1,350,000; plus (b) the aggregate number of Common Shares remaining available for grants under the Predecessor Plans on March 15, 1997; plus (c) the additional Common Shares described in Sections 3.2(a) and 3.3; less (d) 250,000. From and after the effective date of the Reverse Stock Split, the aggregate number of Options and Restricted Shares available for award under the Plan were reduced (pursuant to Article 9) by a factor of ten as follows: (a) 135,000; plus (b) 10% of the aggregate number of Common Shares that remained available for grants under the Predecessor Plans on March 15, 1997; plus (c) the additional Common Shares described in Sections 3.2(b) and 3.3 plus 10% of the additional Common Shares described in Section 3.2(a); less (d) 25,000. Subject to stockholder approval, from and after the effective date of this amended and restated Plan, the aggregate number of Options and Restricted Shares that may be awarded under the Plan shall be increased by 250,000. No additional grants have been or are permitted to be made under the Predecessor Plans after March 15, 1997. The limitation of this Section 3.1 shall be further subject to adjustment pursuant to Article 9.

3.2 **ANNUAL INCREASE IN SHARES.**

- (a) As of January 1 of each year, commencing with the year 1998 and continuing through January 1, 2007, the aggregate number of Options and Restricted Shares that may be awarded under the Plan shall be increased by a number of Common Shares equal to the lesser of (i) 5% of the total number of Common Shares outstanding as of the next preceding December 31 or (ii) 1,500,000. After the annual increase on January 1, 2007, there shall be no further annual increases under the Plan pursuant to this Section 3.2(a) unless and until stockholder approval of such increase has been obtained.
- (b) Subject to stockholder approval, as of the Company's Annual meeting of stockholders of each given year, commencing with the Company's Annual meeting of stockholders in 2012 and continuing through the Company's Annual meeting of stockholders in 2016, the aggregate number of Options and Restricted Shares that may be awarded under the Plan shall be increased by a number of Common Shares

equal to the lesser of (A) 45,000 and (B) the product of 5,000 multiplied by the number of non-employee directors serving on the Board as of the Company's Annual meeting of stockholders in the particular year of determination. After the annual increase as of the Company's Annual meeting of stockholders in 2016, there shall be no further annual increases under the Plan pursuant to this Section 3.2(b) unless and until stockholder approval of such increase has been obtained.

3.3 **ADDITIONAL SHARES.** If Options granted under this Plan or under the Predecessor Plans are forfeited or terminate for any other reason before being exercised, then the corresponding Common Shares shall become available for the grant of Options and Restricted Shares under this Plan. If Restricted Shares are forfeited, then the corresponding Common Shares shall again become available for the grant of NQOs and Restricted Shares under the Plan. The aggregate number of Common Shares that may be issued under the Plan upon the exercise of ISOs shall not be increased when Restricted Shares are forfeited.

3.4 **ONE TIME INCREASE.** As of May 6, 2014, the aggregate number of Options and Restricted Shares that may be awarded under the Plan is increased by 130,000 Common Shares. Following their initial grant, such Common Shares will not again be available for grant under this Plan to the extent they are forfeited under the terms of the corresponding Options and/or Restricted Shares.

#### **ARTICLE 4. ELIGIBILITY.**

4.1 **NONSTATUTORY STOCK OPTIONS AND RESTRICTED SHARES.** Only Employees, Outside Directors and Consultants shall be eligible for the grant of NQOs and Restricted Shares.

4.2 **INCENTIVE STOCK OPTIONS.** Only Employees who are common-law employees of the Company, a Parent or a Subsidiary shall be eligible for the grant of ISOs. In addition, an Employee who owns more than 10% of the total combined voting power of all classes of outstanding stock of the Company or any of its Parents or Subsidiaries shall not be eligible for the grant of an ISO unless the requirements set forth in section 422(c)(6) of the Code are satisfied.

#### **ARTICLE 5. OPTIONS.**

5.1 **STOCK OPTION AGREEMENT.** Each grant of an Option under the Plan shall be evidenced by a Stock Option Agreement between the Optionee and the Company. Such Option shall be subject to all applicable terms of the Plan and may be subject to any other terms that are not inconsistent with the Plan. The Stock Option Agreement shall specify whether the Option is an ISO or an NQO. The provisions of the various Stock Option Agreements entered into under the Plan need not be identical. Options may be granted in consideration of a cash payment or in consideration of a reduction in the Optionee's other compensation. A Stock Option Agreement may provide that a new Option will be granted automatically to the Optionee when he or she exercises a prior Option and pays the Exercise Price in the form described in Section 6.2.

5.2 **NUMBER OF SHARES.** Each Stock Option Agreement shall specify the number of Common Shares subject to the Option and shall provide for the adjustment of such number in

accordance with Article 9. Options granted to any Optionee in a single fiscal year of the Company shall not cover more than 50,000 Common Shares, except that Options granted to a new Employee in the fiscal year of the Company in which his or her service as an Employee first commences shall not cover more than 100,000 Common Shares. The limitations set forth in the preceding sentence shall be subject to adjustment in accordance with Article 9.

- 5.3 **EXERCISE PRICE.** Each Stock Option Agreement shall specify the Exercise Price; provided that the Exercise Price under an ISO shall in no event be less than 100% of the Fair Market Value of a Common Share on the date of grant and the Exercise Price under an NQO shall in no event be less than 85% of the Fair Market Value of a Common Share on the date of grant. In the case of an NQO, a Stock Option Agreement may specify an Exercise Price that varies in accordance with a predetermined formula while the NQO is outstanding.
- 5.4 **EXERCISABILITY AND TERM.** Each Stock Option Agreement shall specify the date when all or any installment of the Option is to become exercisable. The Stock Option Agreement shall also specify the term of the Option; provided that the term of an ISO shall in no event exceed 10 years from the date of grant. A Stock Option Agreement may provide for accelerated exercisability in the event of the Optionee's death, disability or retirement or other events and may provide for expiration prior to the end of its term in the event of the termination of the Optionee's service. NQOs may also be awarded in combination with Restricted Shares, and such an Award may provide that the NQOs will not be exercisable unless the related Restricted Shares are forfeited.
- 5.5 **EFFECT OF CHANGE IN CONTROL.** The Committee may determine, at the time of granting an Option or thereafter, that such Option shall become exercisable as to all or part of the Common Shares subject to such Option in the event that a Change in Control occurs with respect to the Company, subject to the following limitations:
- (a) In the case of an ISO, the acceleration of exercisability shall not occur without the Optionee's written consent.
  - (b) If the Company and the other party to the transaction constituting a Change in Control agree that such transaction is to be treated as a "pooling of interests" for financial reporting purposes, and if such transaction in fact is so treated, then the acceleration of exercisability shall not occur to the extent that the surviving entity's independent public accountants determine in good faith that such acceleration would preclude the use of "pooling of interests" accounting.
- 5.6 **MODIFICATION OR ASSUMPTION OF OPTIONS.** Within the limitations of the Plan, the Committee may modify, extend or assume outstanding options or may accept the cancellation of outstanding options (whether granted by the Company or by another issuer) in return for the grant of new options for the same or a different number of shares and at the same or a different exercise price. The foregoing notwithstanding, no modification of an Option shall, without the consent of the Optionee, alter or impair his or her rights or obligations under such Option.
- 5.7 **BUYOUT PROVISIONS.** The Committee may at any time (a) offer to buy out for a payment in cash or cash equivalents an Option previously granted or (b) authorize an Optionee to elect to

cash out an Option previously granted, in either case at such time and based upon such terms and conditions as the Committee shall establish.

**ARTICLE 6.**  
**PAYMENT FOR OPTION SHARES.**

- 6.1 **GENERAL RULE.** The entire Exercise Price of Common Shares issued upon exercise of Options shall be payable in cash or cash equivalents at the time when such Common Shares are purchased, except as follows:
- (a) In the case of an ISO granted under the Plan, payment shall be made only pursuant to the express provisions of the applicable Stock Option Agreement. The Stock Option Agreement may specify that payment may be made in any form(s) described in this Article 6.
  - (b) In the case of an NQO, the Committee may at any time accept payment in any form(s) described in this Article 6.
- 6.2 **SURRENDER OF STOCK.** To the extent that this Section 6.2 is applicable, all or any part of the Exercise Price may be paid by surrendering, Common Shares that are already owned by the Optionee. Such Common Shares shall be valued at their Fair Market Value on the date when the new Common Shares are purchased under the Plan. The Optionee shall not surrender Common Shares in payment of the Exercise Price if such action would cause the Company to recognize compensation expense (or additional compensation expense) with respect to the Option for financial reporting purposes.
- 6.3 **EXERCISE/SALE.** To the extent that this Section 6.3 is applicable, all or any part of the Exercise Price and any withholding taxes may be paid by delivering (on a form prescribed by the Company) an irrevocable direction to a securities broker approved by the Company to sell all or part of the Common Shares being purchased under the Plan and to deliver all or part of the sales proceeds to the Company.
- 6.4 **EXERCISE/PLEDGE.** To the extent that this Section 6.4 is applicable, all or any part of the Exercise Price and any withholding taxes may be paid by delivering (on a form prescribed by the Company) an irrevocable direction to pledge all or part of the Common Shares being purchased under the Plan to a securities broker or lender approved by the Company, as security for a loan, and to deliver all or part of the loan proceeds to the Company.
- 6.5 **PROMISSORY NOTE.** To the extent that this Section 6.5 is applicable, all or any part of the Exercise Price and any withholding taxes may be paid by delivering (on a form prescribed by the Company) a full-recourse promissory note; provided that the par value of the Common Shares being purchased under the Plan shall be paid in cash or cash equivalents.
- 6.6 **OTHER FORMS OF PAYMENT.** To the extent that this Section 6.6 is applicable, all or any part of the Exercise Price and any withholding taxes may be paid in any other form that is consistent with applicable laws, regulations and rules.

**ARTICLE 7.  
[RESERVED]**

**ARTICLE 8.  
RESTRICTED SHARES.**

- 8.1 **TIME, AMOUNT AND FORM OF AWARDS.** Awards under the Plan may be granted in the form of Restricted Shares. Restricted Shares may also be awarded in combination with NQOs, and such an Award may provide that the Restricted Shares will be forfeited in the event that the related NQOs are exercised. The maximum aggregate number of Common Shares that may be granted in the form of Restricted Shares in any one calendar year to any one Participant is 45,000, except: (a) with respect to the Restricted Shares granted in 2014 pursuant to Section 3.4, for which the annual limit is 130,000, and (b) a new Employee may receive a grant of up to 75,000 Restricted Shares in the fiscal year of the Company in which his or her service with the Company begins.
- 8.2 **PAYMENT FOR AWARDS.** To the extent that an Award is granted in the form of newly issued Restricted Shares, the Award recipient, as a condition to the grant of such Award, shall be required to pay the Company in cash, cash equivalents or any other form of legal consideration acceptable to the Company, including but not limited to future services, an amount equal to the par value of such Restricted Shares. To the extent that an Award is granted in the form of Restricted Shares from the Company's treasury, no cash consideration shall be required of the Award recipients. Any amount not paid in cash may be paid with a full recourse promissory note.
- 8.3 **VESTING CONDITIONS.** Each Award of Restricted Shares may or may not be subject to vesting. Vesting shall occur, in full or in installments, upon satisfaction of the conditions specified in the Stock Award Agreement. A Stock Award Agreement may provide for accelerated vesting in the event of the Participant's death, disability or retirement or other events. The Committee may determine, at the time of granting Restricted Shares or thereafter, that all or part of such Restricted Shares shall become vested in the event that a Change in Control occurs with respect to the Company, except as provided in the next following sentence. If the Company and the other party to the transaction constituting a Change in Control agree that such transaction is to be treated as a "pooling of interests" for financial reporting purposes, and if such transaction in fact is so treated, then the acceleration of vesting shall not occur to the extent that the surviving entity's independent public accountants determine in good faith that such acceleration would preclude the use of "pooling of interests" accounting.
- 8.4 **VOTING AND DIVIDEND RIGHTS.** The holders of Restricted Shares awarded under the Plan shall have the same voting, dividend and other rights as the Company's other stockholders. A Stock Award Agreement, however, may require that the holders of Restricted Shares invest any cash dividends received in additional Restricted Shares. Such additional Restricted Shares shall be subject to the same conditions and restrictions as the Award with respect to which the dividends were paid.
- 8.5 **SECTION 162(M) PERFORMANCE RESTRICTIONS.**



- (a) ***In General.*** For purposes of qualifying grants of Restricted Shares as “performance-based compensation” under Code Section 162(m), the Committee, in its discretion, may make Restricted Shares subject to vesting based on the achievement of performance goals, in which case the Committee will specify in writing, by resolution or otherwise, the Participants eligible to receive such an Award (which may be expressed in terms of a class of individuals) and the performance goals applicable to such Awards within 90 days after the commencement of the period to which the performance goals relate, or such earlier time as required to comply with Section 162(m) of the Code. No such Award shall be payable unless the Committee certifies in writing, by resolution or otherwise, that the performance goals applicable to the Award were satisfied. In no case may the Committee increase the value of an Award granted under this Section 8.5 above the maximum value determined under the performance formula by the attainment of the applicable performance goals, but the Committee retains the discretion to reduce the value below such maximum.
- (b) ***Performance Goals.*** Unless and until the Committee proposes for stockholder vote and the stockholders approve a change in the general performance measures applicable to Awards, the performance goals upon which the payment or vesting of an Award that is intended to qualify as performance based compensation are limited to the following Performance Measures:
- (1) operating income;
  - (2) net earnings or net income (before or after taxes);
  - (3) basic or diluted earnings per share (before or after taxes);
  - (4) revenue, revenues, net revenue, net revenues, net revenue growth or net revenue growth;
  - (5) gross revenue or gross revenues;
  - (6) gross profit or gross profit growth;
  - (7) net operating profit (before or after taxes);
  - (8) return on assets, capital, invested capital, equity or sales;
  - (9) cash flow (including, but not limited to, operating cash flow, free cash flow, and cash flow return on capital);
  - (10) earnings before or after taxes, interest, depreciation and/or amortization;
  - (11) gross or operating margins;
  - (12) improvements in capital structure;
  - (13) budget and expense management;

- (14) productivity targets;
- (15) economic value added or other value added measurements;
- (16) share price (including, but not limited to, growth measures and total shareholder return);
- (17) expense targets;
- (18) margins;
- (19) operating efficiency;
- (20) working capital targets;
- (21) enterprise value;
- (22) safety record;
- (23) completion of business acquisition, divestment or expansion;
- (24) operating cash flow;
- (25) book value;
- (26) tangible book value;
- (27) pretax income;
- (28) net income plus deferred taxes;
- (29) cash position;
- (30) total shareholder return;
- (31) contract or other development of relationship with identified suppliers, distributors or other business partners; or
- (32) new product development (including but not limited to third-party collaborations or contracts, and with milestones that may include but are not limited to contract execution, proof of concept, regulatory approval, product launch and targets such as unit volume and revenue following product launch).

Any performance measures may be used to measure the performance of the Company as a whole and/or any one or more regional operations and/or Affiliates of the Company or any combination thereof, as the Committee may deem appropriate, and any performance measures may be used in comparison to the performance of a group of peer companies, or a published or special index that the Committee, in its sole discretion, deems appropriate. The Committee also has the authority to provide in an

Award for accelerated vesting of an Award based on the achievement of performance goals.

The Committee may provide in any Award that any evaluation of attainment of a performance goal may include or exclude any of the following events that occurs during the relevant period: (a) asset write downs; (b) litigation judgments or settlements; (c) the effect of changes in tax laws, accounting principles, or other laws or regulations affecting reported results; (d) any reorganization or restructuring transactions; (e) extraordinary nonrecurring items as described in Accounting Principles Board Opinion No. 30 and/or in management's discussion and analysis of financial condition and results of operations appearing in the Company's Annual Report on Form 10-K for the applicable year; and (f) significant acquisitions or divestitures.

In the event that applicable tax and/or securities laws change to permit discretion by the Committee to alter the governing performance measures without obtaining stockholder approval of such changes, the Committee shall have sole discretion to make such changes without obtaining stockholder approval. In addition, in the event that the Committee determines that it is advisable to grant Awards that do not qualify as performance based compensation, the Committee may make such grants without satisfying the requirements of Section 162(m) of the Code

## **ARTICLE 9. PROTECTION AGAINST DILUTION.**

- 9.1 **ADJUSTMENTS.** In the event of a subdivision of the outstanding Common Shares, a declaration of a dividend payable in Common Shares, a declaration of a dividend payable in a form other than Common Shares in an amount that has a material effect on the price of Common Shares, a combination or consolidation of the outstanding Common Shares (by reclassification or otherwise) into a lesser number of Common Shares, a recapitalization, a spin-off or a similar occurrence, the Committee shall make such adjustments as it, in its sole discretion, deems appropriate in one or more of (a) the number of Options and Restricted Shares available for future Awards under Article 3, (b) the limitations set forth in Section 5.2, (c) the number of Common Shares covered by each outstanding Option or (d) the Exercise Price under each outstanding Option. Except as provided in this Article 9, a Participant shall have no rights by reason of any issue by the Company of stock of any class or securities convertible into stock of any class, any subdivision or consolidation of shares of stock of any class, the payment of any stock dividend or any other increase or decrease in the number of shares of stock of any class.
- 9.2 **DISSOLUTION OR LIQUIDATION.** To the extent not previously exercised, Options shall terminate immediately prior to the dissolution or liquidation of the Company.
- 9.3 **REORGANIZATIONS.** In the event that the Company is a party to a merger or other reorganization, outstanding Options and Restricted Shares shall be subject to the agreement of merger or reorganization. Such agreement may provide, without limitation, for the continuation of outstanding Awards by the Company (if the Company is a surviving corporation), for their assumption by the surviving corporation or its parent or subsidiary, for the substitution by the surviving corporation or its parent or subsidiary of its own awards for

such Awards, for accelerated vesting and accelerated expiration, or for settlement in cash or cash equivalents.

**ARTICLE 10.  
AWARDS UNDER OTHER PLANS.**

The Company may grant awards under other plans or programs. Such awards may be settled in the form of Common Shares issued under this Plan. Such Common Shares shall be treated for all purposes under the Plan like Restricted Shares and shall, when issued, reduce the number of Common Shares available under Article 3.

**ARTICLE 11.  
LIMITATION ON RIGHTS.**

- 11.1 **RETENTION RIGHTS.** Neither the Plan nor any Award granted under the Plan shall be deemed to give any individual a right to remain an Employee, Outside Director or Consultant. The Company and its Parents, Subsidiaries and Affiliates reserve the right to terminate the service of any Employee, Outside Director or Consultant at any time, with or without cause, subject to applicable laws, the Company's certificate of incorporation and bylaws and a written employment agreement (if any).
- 11.2 **STOCKHOLDERS' RIGHTS.** A Participant shall have no dividend rights, voting rights or other rights as a stockholder with respect to any Common Shares covered by his or her Award prior to the time when a stock certificate for such Common Shares is issued or, in the case of an Option, the time when he or she becomes entitled to receive such Common Shares by filing a notice of exercise and paying the Exercise Price. No adjustment shall be made for cash dividends or other rights for which the record date is prior to such time, except as expressly provided in the Plan.
- 11.3 **REGULATORY REQUIREMENTS.** Any other provision of the Plan notwithstanding, the obligation of the Company to issue Common Shares under the Plan shall be subject to all applicable laws, rules and regulations and such approval by any regulatory body as may be required. The Company reserves the right to restrict, in whole or in part, the delivery of Common Shares pursuant to any Award prior to the satisfaction of all legal requirements relating to the issuance of such Common Shares, to their registration, qualification or listing or to an exemption from registration, qualification or listing.

**ARTICLE 12.  
WITHHOLDING TAXES.**

- 12.1 **GENERAL.** To the extent required by applicable federal, state, local or foreign law, a Participant or his or her successor shall make arrangements satisfactory to the Company for the satisfaction of any withholding tax obligations that arise in connection with the Plan. The Company shall not be required to issue any Common Shares or make any cash payment under the Plan until such obligations are satisfied.
- 12.2 **SHARE WITHHOLDING.** The Committee may permit a Participant to satisfy all or part of his or her withholding or income tax obligations by having the Company withhold all or a portion of any Common Shares that otherwise would be issued to him or her or by surrendering all or a portion of any Common Shares that he or she previously acquired. Such

Common Shares shall be valued at their Fair Market Value on the date when taxes otherwise would be withheld in cash.

- 12.3 **SECTION 280G.** To the extent that any of the payments and benefits provided for under the Plan or any other agreement or arrangement between the Company or its Affiliates and a Participant (collectively, the “Payments”) (i) constitute a “parachute payment” within the meaning of Code Section 280G and (ii) but for this paragraph would be subject to the excise tax imposed by Section 4999 of the Code, then the Payments shall be payable either (i) in full or (ii) as to such lesser amount which would result in no portion of such Payments being subject to excise tax under Section 4999 of the Code (determined in accordance with the reduction of payments and benefits paragraph set forth below); whichever of the foregoing amounts, taking into account the applicable federal, state and local income taxes and the excise tax imposed by Section 4999, results in the participant’s receipt on an after-tax basis, of the greatest amount of benefits under this Plan, notwithstanding that all or some portion of such benefits may be taxable under Section 4999 of the Code. Any determination required under this provision will be made by accountants chosen by the Company, whose determination shall be conclusive and binding upon the participant and the Company for all purposes.

Except to the extent, if any, otherwise agreed in writing between a participant and the Company, reduction of payments and benefits hereunder, if applicable, will be made by reducing, first, payments or benefits to be paid in cash in the order in which such payment or benefit would be paid or provided (beginning with such payment or benefit that would be made last in time and continuing, to the extent necessary, through to such payment or benefit that would be made first in time) and, then, reducing any benefit to be provided in-kind hereunder in a similar order; provided, however, that any reduction or elimination of accelerated vesting of any equity award will first be accomplished by reducing or eliminating the vesting of such awards that are valued in full for purposes of Section 280G of the Code, then the reduction or elimination of vesting of other equity awards.

### **ARTICLE 13. FUTURE OF THE PLAN.**

- 13.1 **TERM OF THE PLAN.** The Plan, as set forth herein, shall become effective on March 14, 1997. The Plan shall remain in effect until it is terminated under Section 13.2, except that no ISOs shall be granted after May 8, 2022.
- 13.2 **AMENDMENT OR TERMINATION.** The Board may, at any time and for any reason, amend or terminate the Plan. An amendment of the Plan shall be subject to the approval of the Company’s stockholders only to the extent required by applicable laws, regulations or rules. No Awards shall be granted under the Plan after the termination thereof. The termination of the Plan, or any amendment thereof, shall not affect any Award previously granted under the Plan.

### **ARTICLE 14. DEFINITIONS.**

- 14.1 **Affiliate** means any entity other than a Subsidiary, if the Company and/or one or more Subsidiaries own not less than 50% of such entity.

14.2 **Award** means any award of an Option or a Restricted Share under the Plan.

14.3 **Board** means the Company's Board of Directors, as constituted from time to time.

14.4 **Change in Control** shall mean:

- (a) The consummation of a merger or consolidation of the Company with or into another entity or any other corporate reorganization, if more than 50% of the combined voting power of the continuing or surviving entity's securities outstanding immediately after such merger, consolidation or other reorganization is owned by persons who were not stockholders of the Company immediately prior to such merger, consolidation or other reorganization;
- (b) The sale, transfer or other disposition of all or substantially all of the Company's assets;
- (c) A change in the composition of the Board, a result of which fewer than 50% of the incumbent directors are directors who either (i) had been directors of the Company on the date 24 months prior to the date of the event that may constitute a Change in Control (the "original directors") or (ii) were elected, or nominated for election, to the Board with the affirmative votes of at least a majority of the aggregate of the original directors who were still in office at the time of the election or nomination and the directors whose election or nomination was previously so approved; or
- (d) Any transaction as a result of which any person is the "beneficial owner" (as defined in Rule 13d-3 under the Exchange Act), directly or indirectly, of securities of the Company representing at least 30% of the total voting power represented by the Company's then outstanding voting securities. For purposes of this Paragraph (d), the term "person" shall have the same meaning as when used in sections 13(d) and 14(d) of the Exchange Act but shall exclude (i) any person, or person affiliated with said person, who, on March 15, 1997, is the beneficial owner of securities of the Company representing at least 20% of the total voting power represented by the Company's then outstanding voting securities (11,607,764), (ii) a trustee or other fiduciary holding securities under an employee benefit plan of the Company or of a Parent or Subsidiary and (iii) a corporation owned directly or indirectly by the stockholders of the Company in substantially the same proportions as their ownership of the common stock of the Company.

A transaction shall not constitute a Change in Control if its sole purpose is to change the state of the Company's incorporation or to create a holding company that will be owned in substantially the same proportions by the persons who held the Company's securities immediately before such transaction.

14.5 **Code** means the Internal Revenue Code of 1986, as amended.

14.6 **Committee** means a committee of the Board, as described in Article 2.

14.7 **Common Share** means, as may be applicable, one share of Common Stock, par value \$0.01 per share, of the Company to the extent any remains outstanding at the time of determination,

or one share of Public Common Stock, par value \$0.01 per share, of the Company, to the extent any remains outstanding at the time of determination.

- 14.8 **Company** means either (a) Heska Corporation, a California corporation (prior to the formation of Heska Corporation, a Delaware corporation), or (b) Heska Corporation, a Delaware corporation (following its formation).
- 14.9 **Consultant** means a consultant or adviser who provides bona fide services to the Company, a Parent, a Subsidiary or an Affiliate as an independent contractor. Service as a Consultant shall be considered employment for all purposes of the Plan, except as provided in Section 4.2.
- 14.10 **Employee** means a common-law employee of the Company, a Parent, a Subsidiary or an Affiliate.
- 14.11 **Exchange Act** means the Securities Exchange Act of 1934, as amended.
- 14.12 **Exercise Price** means the amount for which one Common Share may be purchased upon exercise of such Option, as specified in the applicable Stock Option Agreement.
- 14.13 **Fair Market Value** means the market price of Common Shares, determined by the Committee in good faith on such basis as it deems appropriate. Whenever possible, the determination of Fair Market Value by the Committee shall be based on the prices reported in The Wall Street Journal. Such determination shall be conclusive and binding on all persons.
- 14.14 **ISO** means an incentive stock option described in section 422(b) of the Code.
- 14.15 **NQO** means a stock option not described in sections 422 or 423 of the Code.
- 14.16 **Option** means an ISO or NQO granted under the Plan and entitling the holder to purchase Common Shares.
- 14.17 **Optionee** means an individual or estate who holds an Option.
- 14.18 **Outside Director** shall mean a member of the Board who is not an Employee. Service as an Outside Director shall be considered employment for all purposes of the Plan, except as provided in Section 4.2.
- 14.19 **Parent** means any corporation (other than the Company) in an unbroken chain of corporations ending with the Company, if each of the corporations other than the Company owns stock possessing 50% or more of the total combined voting power of all classes of stock in one of the other corporations in such chain. A corporation that attains the status of a Parent on a date after the adoption of the Plan shall be considered a Parent commencing as of such date.
- 14.20 **Participant** means an individual or estate who holds an Award.
- 14.21 **Plan** means this Heska Corporation 1997 Stock Incentive Plan, as amended from time to time.

- 14.22 **Predecessor Plans** means (a) the 1988 Heska Corporation Stock Plan and (b) the Heska Corporation 1994 Key Executive Stock Plan.
- 14.23 **Restricted Share** means a Common Share awarded under the Plan.
- 14.24 **Reverse Stock Split** means the Company's 1-for-10 reverse stock split of its then outstanding Common Shares, which was approved by the Company's stockholders and consummated and made effective December 30, 2010.
- 14.25 **Stock Award Agreement** means the agreement between the Company and the recipient of a Restricted Share that contains the terms, conditions and restrictions pertaining to such Restricted Share.
- 14.26 **Stock Option Agreement** means the agreement between the Company and an Optionee that contains the terms, conditions and restrictions pertaining to his or her Option.
- 14.27 **Subsidiary** means any corporation (other than the Company) in an unbroken chain of corporations beginning with the Company, if each of the corporations other than the last corporation in the unbroken chain owns stock possessing 50% or more of the total combined voting power of all classes of stock in one of the other corporations in such chain. A corporation that attains the status of a Subsidiary on a date after the adoption of the Plan shall be considered a Subsidiary commencing as of such date.

**ARTICLE 15.  
EXECUTION.**

To record the adoption of the Plan by the Board, the Company has caused its duly authorized officer to execute this document in the name of the Company.

**HESKA CORPORATION**

By: /s/ Jason A. Napolitano  
Executive Vice President and  
Chief Financial Officer





**HESKA CORPORATION 1997 STOCK INCENTIVE PLAN**

**STOCK OPTION AGREEMENT  
(EMPLOYEES AND CONSULTANTS)**

**Tax Treatment**

This option is intended to be an incentive stock option under section 422 of the Internal Revenue Code or a nonstatutory option, as provided in the Notice of Stock Option Grant.

**Vesting/  
Exercisability**

This option vests and becomes exercisable in installments, as shown in the Notice of Stock Option Grant. In addition, this option shall vest and become exercisable in full if one of the following events occurs:

- Your service as an Employee, Consultant or Outside Director of the Company or a Subsidiary terminates because of death, or
- The Company is a party to a merger or other reorganization while you are an Employee or Consultant of the Company or a Subsidiary, this option is not continued by the Company and is not assumed by the surviving corporation or its parent, and the surviving corporation or its parent does not substitute its own option for this option, or
- The Company is subject to a “Change in Control” while you are an Employee or Consultant of the Company or a Subsidiary and, within 12 months after the Change in Control, the surviving entity terminates your service without your consent and without Cause, as defined below. If the surviving entity demotes you to a lower position, materially reduces your authority or responsibilities, materially reduces your total compensation or announces its intention to relocate your principal place of work by more than 20 miles, then that action will be treated as a termination of your service.
- “Cause” shall mean (i) your failure to perform your assigned duties or responsibilities as an Employee or Consultant of the Company or a Subsidiary (other than a failure resulting from total and permanent disability, as discussed below) after notice thereof from the Company describing your failure to perform such duties or responsibilities; (ii) your material breach of any confidentiality agreement or invention assignment agreement between you and the Company or a Subsidiary; (iii) your engaging in any act of dishonesty, fraud, misrepresentation, moral turpitude or misappropriation of material property that was or is materially injurious to the Company or its affiliates; (iv) your violation of any federal or state law or regulation applicable to the Company’s business; or (v) your being convicted of, or entering a plea of nolo contendere to, any crime.

No additional shares become vested after your service as an Employee, Consultant or Outside Director of the Company or a Subsidiary has terminated for any reason other than those outlined herein.

<b>Term</b>	This option expires in any event at the close of business at Company headquarters on the day before the 10th anniversary of the Date of Grant, as shown in the Notice of Stock Option Grant. (It will expire earlier if your service terminates, as described below.)
<b>Regular Termination</b>	If your service as an Employee, Consultant or Outside Director of the Company or a Subsidiary terminates for any reason except death or total and permanent disability, then this option will expire at the close of business at Company headquarters on the date three months after your termination date. The Company determines when your service terminates for this purpose.
<b>Death</b>	If your service as an Employee, Consultant or Outside Director of the Company or a Subsidiary terminates because of your death, then this option will expire at the close of business at Company headquarters on the date 12 months after the date of death.
<b>Disability</b>	<p>If your service as an Employee, Consultant or Outside Director of the Company or a Subsidiary terminates because of your total and permanent disability, then this option will expire at the close of business at Company headquarters on the date 12 months after your termination date.</p> <p>For all purposes under this Agreement, “total and permanent disability” means that you are unable to engage in any substantial gainful activity by reason of any medically determinable physical or mental impairment which can be expected to result in death or which has lasted, or can be expected to last, for a continuous period of not less than one year.</p>
<b>Leaves of Absence</b>	<p>Vesting of this option shall be suspended during any unpaid leave of absence unless continued vesting is required by the terms of the leave or by applicable law.</p> <p>For purposes of this option, your service does not terminate when you go on a military leave, a sick leave or another <i>bona fide</i> leave of absence, if the Company approved your leave in writing and if continued crediting of service is required by the terms of the leave or by applicable law.</p> <p>For purposes of incentive stock options, no such leave may exceed 90 days, unless reemployment upon expiration of such leave is guaranteed by the terms of the leave or by applicable law. If reemployment upon expiration of a leave of absence approved by the Company is not so guaranteed, then three months following the 91<sup>st</sup> day of such leave, an incentive stock option shall cease to be treated as an incentive stock option and shall be treated for tax purposes as a nonstatutory option.</p> <p>Unless you immediately return to active work when the approved leave ends, your service will terminate.</p>
<b>Restrictions on Exercise</b>	The Company will not permit you to exercise this option if the issuance of shares at that time would violate any law or regulation.

**Notice of Exercise**

When you wish to exercise this option, you must notify the Company by filing the proper "Notice of Exercise" form at the address given on the form. Your notice must specify how many shares you wish to purchase. The exercise will be effective when the Company receives the Notice of Exercise with the option exercise payment described herein.

If someone else wants to exercise this option after your death, that person must prove to the Company's satisfaction that he or she is entitled to do so.

**Form of Payment**

When you submit your notice of exercise, you must include payment of the option exercise price for the shares you are purchasing. Payment may be made in one (or a combination of two or more) of the following forms:

- Your personal check, a cashier's check or a money order.
- Certificates for shares of Company stock that you own, along with any forms needed to affect a transfer of those shares to the Company. The value of the shares, determined as of the effective date of the option exercise, will be applied to the option exercise price. However, you may not surrender shares of Company stock in payment of the exercise price if your action would cause the Company to recognize compensation expense (or additional compensation expense) with respect to this option for financial reporting purposes.
- Irrevocable directions to a securities broker approved by the Company to sell all or part of your option shares and to deliver to the Company proceeds from the sale in an amount sufficient to pay the option exercise price and any withholding taxes. (The balance of the sale proceeds, if any, will be delivered to you.) The directions must be given by signing a special "Notice of Exercise" form provided by the Company.

**Withholding Taxes  
and Stock  
Withholding**

You will not be allowed to exercise this option unless you make arrangements acceptable to the Company to pay any withholding taxes that may be due as a result of the option exercise. These arrangements may include (with the Company's approval) withholding shares of Company stock that otherwise would be issued to you when you exercise this option. The value of these shares, determined as of the effective date of the option exercise, will be applied to the withholding taxes.

**Restrictions on  
Resale**

By signing this Agreement, you agree not to sell any option shares at a time when applicable laws, Company policies or an agreement between the Company and its underwriters prohibit a sale. This restriction will apply as long as you are an Employee, Consultant or Outside Director of the Company or a Subsidiary.

**Transfer of Option**

Prior to your death, only you may exercise this option. You cannot transfer or assign this option. For instance, you may not sell this option or use it as security for a loan. You may, however, dispose of this option in your will, by the laws of descent and distribution or through a beneficiary designation.

Regardless of any marital property settlement agreement, the Company is not obligated to honor a notice of exercise from your former spouse, nor is the Company obligated to recognize your former spouse's interest in your option in any other way.

**Retention Rights**

Neither your option nor this Agreement gives you the right to be employed or otherwise retained by the Company or a Subsidiary in any capacity. The Company or a Subsidiary reserves the right to terminate your service at any time, with or without cause.

**Stockholder Rights**

You, or your estate or heirs, have no rights as a stockholder of the Company until you have exercised this option by giving the required notice to the Company and paying the exercise price.

**Applicable Law**

This Agreement will be interpreted and enforced under the laws of the State of Colorado (without giving effect to its conflict of laws provisions).

**The Plan and Other Agreements**

The 1997 Stock Incentive Plan is incorporated in this Agreement by reference. Unless otherwise defined herein, all capitalized terms herein have the same defined meanings as in the 1997 Stock Incentive Plan.

This Agreement and the Plan constitute the entire understanding between you and the Company regarding this option. Any prior agreements, commitments or negotiations concerning this option are superseded. This Agreement may be amended only by another written agreement, signed by both parties.

**BY SIGNING THE NOTICE OF STOCK OPTION GRANT OF THIS AGREEMENT, YOU AGREE TO ALL OF THE TERMS AND CONDITIONS DESCRIBED ABOVE AND IN THE 1997 STOCK INCENTIVE PLAN.**

## HESKA CORPORATION 1997 STOCK INCENTIVE PLAN

STOCK OPTION AGREEMENT  
(OUTSIDE DIRECTORS)

<b>Tax Treatment</b>	This option is intended to be a nonstatutory option.
<b>Vesting/ Exercisability</b>	<p>This option is immediately exercisable, but subject to vesting as indicated in the Notice of Stock Option Grant. In the event of termination of your service as an Outside Director of the Company, any unvested shares issued upon exercise are subject to repurchase by the Company at the same price as the original Exercise Price Per Share. The Company's right to repurchase such shares shall lapse as the shares become vested as indicated in the Notice of Stock Option Grant.</p> <p>In addition, this option becomes vested in full if one of the following events occurs:</p> <ul style="list-style-type: none"><li>· Your service as an Outside Director of the Company terminates because of death, total and permanent disability, or retirement at or after age 65, or</li><li>· A Change in Control with respect to the Company occurs while you are an Outside Director of the Company.</li></ul> <p>No additional shares become vested after your service as an Employee, Consultant or Outside Director of the Company or a Subsidiary has terminated for any reason other than those outlined herein.</p>
<b>Term</b>	This option expires in any event at the close of business at Company headquarters on the day before the 10th anniversary of the Date of Grant, as shown in the Notice of Stock Option Grant. (It will expire earlier if your service terminates, as described below.)
<b>Regular Termination</b>	If your service as an Employee, Consultant or Outside Director of the Company or a Subsidiary terminates for any reason except death or total and permanent disability, then this option will expire at the close of business at Company headquarters on the date three months after your termination date. The Company determines when your service terminates for this purpose.
<b>Death</b>	If your service as an Employee, Consultant or Outside Director of the Company or a Subsidiary terminates because of your death, then this option will expire at the close of business at Company headquarters on the date 12 months after the date of death.
<b>Disability</b>	If your service as an Employee, Consultant or Outside Director of the Company or a Subsidiary terminates because of your total and permanent disability, then this option will expire at the close of business at Company headquarters on the date 12 months after your termination date.

For all purposes under this Agreement, “total and permanent disability” means that you are unable to engage in any substantial gainful activity by reason of any medically determinable physical or mental impairment which can be expected to result in death or which has lasted, or can be expected to last, for a continuous period of not less than one year.

**Restrictions on Exercise**

The Company will not permit you to exercise this option if the issuance of shares at that time would violate any law or regulation.

**Notice of Exercise**

When you wish to exercise this option, you must notify the Company by filing the proper “Notice of Exercise” form at the address given on the form. Your notice must specify how many shares you wish to purchase. The exercise will be effective when the Company receives the Notice of Exercise with the option exercise payment described herein.

If someone else wants to exercise this option after your death, that person must prove to the Company's satisfaction that he or she is entitled to do so.

**Exercise of Unvested Shares**

Exercise of unvested shares is allowed under the Plan. If you would like to exercise your option before it is vested, you must complete a Stock Repurchase Agreement, which provides for the repurchase of that portion of the shares that remain unvested at the time of your termination.

**Form of Payment**

When you submit your notice of exercise, you must include payment of the option exercise price for the shares you are purchasing. Payment may be made in one (or a combination of two or more) of the following forms:

- Your personal check, a cashier's check or a money order.
- Certificates for shares of Company stock that you own, along with any forms needed to affect a transfer of those shares to the Company. The value of the shares, determined as of the effective date of the option exercise, will be applied to the option exercise price. However, you may not surrender shares of Company stock in payment of the exercise price if your action would cause the Company to recognize compensation expense (or additional compensation expense) with respect to this option for financial reporting purposes.
- Irrevocable directions to a securities broker approved by the Company to sell all or part of your option shares and to deliver to the Company proceeds from the sale in an amount sufficient to pay the option exercise price and any withholding taxes. (The balance of the sale proceeds, if any, will be delivered to you.) The directions must be given by signing a special “Notice of Exercise” form provided by the Company.

**Withholding Taxes and Stock Withholding**

You will not be allowed to exercise this option unless you make arrangements acceptable to the Company to pay any withholding taxes that may be due as a result of the option exercise. These arrangements may include (with the Company's approval) withholding shares of Company stock that otherwise would be issued to you when you exercise this option. The value of these shares, determined as of the effective date of the option exercise, will be applied to the withholding taxes.

**Repurchase Rights**

In the event that you exercise unvested shares through the execution of a Stock Repurchase Agreement, the Company will have 90 days to repurchase any shares that remain unvested at the time of your termination. The terms of any such repurchase will be set forth in the Stock Repurchase Agreement.

**Restrictions on Resale**

By signing this Agreement, you agree not to sell any option shares at a time when applicable laws, Company policies or an agreement between the Company and its underwriters prohibit a sale. This restriction will apply as long as you are an Employee, Consultant or Outside Director of the Company or a Subsidiary.

**Transfer of Option**

Prior to your death, only you may exercise this option. You cannot transfer or assign this option. For instance, you may not sell this option or use it as security for a loan. You may, however, dispose of this option in your will, by the laws of descent and distribution or through a beneficiary designation.

Regardless of any marital property settlement agreement, the Company is not obligated to honor a notice of exercise from your former spouse, nor is the Company obligated to recognize your former spouse's interest in your option in any other way.

**Retention Rights**

Neither your option nor this Agreement give you the right to be employed or otherwise retained by the Company or a Subsidiary in any capacity.

**Stockholder Rights**

You, or your estate or heirs, have no rights as a stockholder of the Company until you have exercised this option by giving the required notice to the Company and paying the exercise price.



**Applicable Law**

This Agreement will be interpreted and enforced under the laws of the State of Colorado (without giving effect to its conflict of laws provisions).

**The Plan and Other Agreements**

The 1997 Stock Incentive Plan is incorporated in this Agreement by reference. Unless otherwise defined herein, all capitalized terms herein have the same defined meanings as in the 1997 Stock Incentive Plan.

This Agreement and the Plan constitute the entire understanding between you and the Company regarding this option. Any prior agreements, commitments or negotiations concerning this option are superseded. This Agreement may be amended only by another written agreement, signed by both parties.

**BY SIGNING THE NOTICE OF STOCK OPTION GRANT OF THIS AGREEMENT, YOU AGREE TO ALL OF THE TERMS AND CONDITIONS DESCRIBED ABOVE AND IN THE 1997 STOCK INCENTIVE PLAN.**

**HESKA CORPORATION**  
**1997 STOCK INCENTIVE PLAN**  
**RESTRICTED STOCK GRANT AGREEMENT**

THIS AGREEMENT is made as of the \_\_\_\_\_ day of \_\_\_\_\_, 2015 (the "Grant Date") by and between Heska Corporation (the "Company"), and \_\_\_\_\_ (the "Executive").

In consideration of the mutual covenants and representations herein set forth, the Company and Executive agree as follows:

**SECTION 1. GRANT OF STOCK.**

1.1 Precedence of Plan. This Agreement is subject to and shall be construed in accordance with the terms and conditions of the Heska Corporation 1997 Stock Incentive Plan (the "Plan"), as now or hereinafter in effect. Any capitalized terms that are used in this Agreement without being defined and that are defined in the Plan shall have the meaning specified in the Plan.

1.2 Grant of Stock. The Company hereby grants to Executive an aggregate of \_\_\_\_\_ shares of Restricted Stock (the "Shares"), subject to vesting as provided in Section 2.

**SECTION 2. UNVESTED SHARES SUBJECT TO FORFEITURE.**

2.1 Shares Subject to Forfeiture. The Shares are subject to time-based and performance-based vesting requirements.

a. The Shares will vest on the third anniversary of the Grant Date, but only if the Company has earned Operating Cash Flow of \$\_\_\_\_\_ in either calendar year 2015, 2016 or 2017. For this purpose, "Operating Cash Flow" means operating income plus depreciation plus amortization, calculated in the sole discretion of the Company.

b. In the event of a Change of Control prior to the third anniversary of the Grant Date, the Shares will vest. For this purpose, "Change of Control" means (i) a sale of all or substantially all of the Company's assets, (ii) any merger, consolidation, or other business combination transaction of the Company with or into another corporation, entity, or person, other than a transaction in which the holders of at least a majority of the shares of voting capital stock of the Company outstanding immediately prior to such transaction continue to hold (either by such shares remaining outstanding or by their being converted into shares of voting capital stock of the surviving entity) a majority of the total voting power represented by the shares of voting capital stock of the Company (or the surviving entity) outstanding immediately after such transaction, (iii) the direct or indirect acquisition (including by way of a tender or exchange offer) by any person, or persons acting as a group, of beneficial ownership or a right to acquire beneficial ownership of shares representing a majority of the voting power of the then outstanding shares of capital stock of the Company, (iv) a contested election of Directors, as a result of which or in connection with which the persons who were Directors before such election

or their nominees cease to constitute a majority of the Board, or (v) a dissolution or liquidation of the Company.

c. In the event that Executive's employment with the Company is terminated prior to vesting, Executive will forfeit all right to the Shares.

2.2 Restriction on Transfer. Until the Shares are vested, the Shares may not be sold, transferred, pledged, assigned, or otherwise alienated or hypothecated.

### **SECTION 3. STOCKHOLDER RIGHTS**

3.1 Stock Register and Certificates. The Shares will be recorded in the stock register of the Company in the name of Executive. If applicable, a stock certificate or certificates representing the Shares will be registered in the name of Executive, but such certificates shall remain in the custody of the Company. Executive shall deposit with the Company a Stock Assignment Separate from Certificate in the form attached below as Attachment 1, endorsed in blank, so as to permit retransfer to the Company of all or a portion of the Shares that are forfeited or otherwise do not become vested in accordance with the Plan and this Agreement.

3.2 Exercise of Stockholder Rights. Executive shall have the right to vote the Shares (to the extent of the voting rights of said Shares, if any), to receive and retain all regular cash dividends and such other distributions, as the Board of Directors of the Company may, in its discretion, designate, pay or distribute on such Shares, and to exercise all other rights, powers and privileges of a holder of Common Stock with respect to such Shares, except as set forth in this Agreement and the Plan.

3.3 Legends. Certificates, if any, representing the Shares will contain the following or other legends in the Company's discretion:

THE SHARES REPRESENTED BY THIS CERTIFICATE ARE SUBJECT TO CERTAIN RESTRICTIONS UPON AND OBLIGATIONS WITH RESPECT TO TRANSFER AND RIGHTS OF REPURCHASE AS SET FORTH IN AN AGREEMENT BETWEEN THE COMPANY AND THE ORIGINAL REGISTERED HOLDER, A COPY OF WHICH IS ON FILE AT THE PRINCIPAL OFFICE OF THE COMPANY.

### **SECTION 4. RESPONSIBILITY FOR TAXES.**

4.1 Section 83(b) Election. Executive may complete and file with the Internal Revenue Service an election pursuant to Section 83(b) of the Internal Revenue Code to be taxed currently on the fair market value of the Shares without regard to the vesting restrictions set forth in this Agreement. Executive shall be responsible for all taxes associated with the acceptance of the transfer of the Shares, including any tax liability associated with the representation of fair market value if the election is made pursuant to Code Section 83(b).

4.2 Withholding. In accordance with Section 12 of the Plan, Executive agrees to make arrangements satisfactory to the Company for the satisfaction of any withholding tax obligations that arise in connection with the Plan under applicable federal, state, local or foreign

law. The Company in its discretion may permit Executive to satisfy all or part of his withholding or income tax obligations by having the Company withhold all or a portion of the Shares that otherwise would be issued to him on vesting.

**SECTION 5. MISCELLANEOUS.**

5.1 Not an Employment Contract. This Agreement is not an employment contract and nothing in this Agreement shall be deemed to create in any way whatsoever any obligation on the part of Executive to remain in the service of the Company in any capacity, or of the Company to continue Executive's service in any capacity.

5.2 Effect on Employee Benefits. Executive agrees that the Award will constitute special incentive compensation that will not be taken into account as "salary" or "compensation" or "bonus" in determining the amount of any payment under any pension, retirement, profit sharing or other remuneration plan of the Company unless so provided in such plan.

5.3 Further Assurances. The parties agree to execute such further instruments and to take such further action as may reasonably be necessary to carry out the intent of this Agreement.

5.4 Entire Agreement. This Agreement, including any exhibits, is the entire agreement of the parties with respect to the subject matter hereof and supersedes all prior oral and written understandings of the parties.

5.5 Governing Law. This Agreement shall be governed by and construed in accordance with the laws of the State of Delaware as applied to contracts between Delaware residents to be wholly performed within the State of Colorado.

IN WITNESS WHEREOF, the parties hereto have executed this Agreement as of the day and year first above written.

**EXECUTIVE**

**HESKA CORPORATION**  
a Delaware corporation

\_\_\_\_\_  
Address \_\_\_\_\_  
\_\_\_\_\_

By: \_\_\_\_\_  
Title: \_\_\_\_\_

**ASSIGNMENT SEPARATE FROM CERTIFICATE**

FOR VALUE RECEIVED, I, \_\_\_\_\_, hereby sell, assign and transfer unto \_\_\_\_\_ (\_\_\_\_\_) shares of the Common Stock of Heska Corporation, standing in my name on the books of said corporation represented by Certificate No. \_\_\_\_\_ herewith and do hereby irrevocably constitute and appoint \_\_\_\_\_ to transfer said stock on the books of the within-named corporation with full power of substitution in the premises.

Dated: \_\_\_\_\_, 20\_\_.

Signature:

This Assignment Separate from Certificate was executed in conjunction with the terms of a Restricted Stock Grant Agreement between the above assignor and Heska Corporation, dated \_\_\_\_\_, 2015.

**Instruction: Please do not fill in any blanks other than the signature line.**

**HESKA CORPORATION**  
**1997 STOCK INCENTIVE PLAN**  
**RESTRICTED STOCK GRANT AGREEMENT**

*(Management Incentive Plan Award)*

THIS AGREEMENT is made as of the \_\_\_\_\_ day of \_\_\_\_\_, 2015 (the "Grant Date") by and between Heska Corporation (the "Company"), and \_\_\_\_\_ (the "Executive"), in connection with the Executive's election to receive a portion of Executive's 2015 award under the Management Incentive Plan in the form of Restricted Stock.

In consideration of the mutual covenants and representations herein set forth, the Company and Executive agree as follows:

**SECTION 1. GRANT OF STOCK.**

1.1 Precedence of Plan. This Agreement is subject to and shall be construed in accordance with the terms and conditions of the Heska Corporation 1997 Stock Incentive Plan (the "Plan"), as now or hereinafter in effect. Any capitalized terms that are used in this Agreement without being defined and that are defined in the Plan shall have the meaning specified in the Plan.

1.2 Grant of Stock. The Company hereby grants to Executive an aggregate of \_\_\_\_\_ shares of Restricted Stock (the "Shares"), subject to vesting as provided in Section 2.

**SECTION 2. UNVESTED SHARES SUBJECT TO FORFEITURE.**

2.1 Shares Subject to Forfeiture. The Shares are subject to vesting requirements as established in connection with the Management Incentive Plan, including the terms and conditions for awards made in 2015 under the Management Incentive Plan (the "MIP"). As described in more detail in the MIP, the portion of the Shares that vest will be calculated at the time payments are made under the MIP by multiplying the number of Shares by the "Payout Percentage," which this purpose means one-half of the percentage calculated by dividing the amount of the Executive's MIP Payout (as defined in the MIP) by the amount of the Executive's Incentive Target (as defined in the MIP), and rounding to the nearest whole Share. Executive will forfeit all Shares that do not vest at that time. In the event that Executive's employment with the Company is terminated prior to vesting, Executive will forfeit all right to the Shares.

2.2 Restriction on Transfer. Until the Shares are vested, the Shares may not be sold, transferred, pledged, assigned, or otherwise alienated or hypothecated.

**SECTION 3. STOCKHOLDER RIGHTS**

3.1 Stock Register and Certificates. The Shares will be recorded in the stock register of the Company in the name of Executive. If applicable, a stock certificate or certificates representing the Shares will be registered in the name of Executive, but such certificates shall remain in the custody of the Company. Executive shall deposit with the Company a Stock

Assignment Separate from Certificate in the form attached below as Attachment 1, endorsed in blank, so as to permit retransfer to the Company of all or a portion of the Shares that are forfeited or otherwise do not become vested in accordance with the Plan and this Agreement.

3.2 Exercise of Stockholder Rights. Executive shall have the right to vote the Shares (to the extent of the voting rights of said Shares, if any), to receive and retain all regular cash dividends and such other distributions, as the Board of Directors of the Company may, in its discretion, designate, pay or distribute on such Shares, and to exercise all other rights, powers and privileges of a holder of Common Stock with respect to such Shares, except as set forth in this Agreement and the Plan.

3.3 Legends. Certificates, if any, representing the Shares will contain the following or other legends in the Company's discretion:

THE SHARES REPRESENTED BY THIS CERTIFICATE ARE SUBJECT TO CERTAIN RESTRICTIONS UPON AND OBLIGATIONS WITH RESPECT TO TRANSFER AND RIGHTS OF REPURCHASE AS SET FORTH IN AN AGREEMENT BETWEEN THE COMPANY AND THE ORIGINAL REGISTERED HOLDER, A COPY OF WHICH IS ON FILE AT THE PRINCIPAL OFFICE OF THE COMPANY.

#### **SECTION 4. RESPONSIBILITY FOR TAXES.**

4.1 Section 83(b) Election. Executive may complete and file with the Internal Revenue Service an election pursuant to Section 83(b) of the Internal Revenue Code to be taxed currently on the fair market value of the Shares without regard to the vesting restrictions set forth in this Agreement. Executive shall be responsible for all taxes associated with the acceptance of the transfer of the Shares, including any tax liability associated with the representation of fair market value if the election is made pursuant to Code Section 83(b).

4.2 Withholding. In accordance with Section 12 of the Plan, Executive agrees to make arrangements satisfactory to the Company for the satisfaction of any withholding tax obligations that arise in connection with the Plan under applicable federal, state, local or foreign law. The Company in its discretion may permit Executive to satisfy all or part of his withholding or income tax obligations by having the Company withhold all or a portion of the Shares that otherwise would be issued to him on vesting.

#### **SECTION 5. MISCELLANEOUS.**

5.1 Not an Employment Contract. This Agreement is not an employment contract and nothing in this Agreement shall be deemed to create in any way whatsoever any obligation on the part of Executive to remain in the service of the Company in any capacity, or of the Company to continue Executive's service in any capacity.

5.2 Effect on Employee Benefits. Executive agrees that the Award will constitute special incentive compensation that will not be taken into account as "salary" or "compensation" or "bonus" in determining the amount of any payment under any pension, retirement, profit sharing or other remuneration plan of the Company unless so provided in such plan.

5.3 Further Assurances. The parties agree to execute such further instruments and to take such further action as may reasonably be necessary to carry out the intent of this Agreement.

5.4 Entire Agreement. This Agreement, including any exhibits, is the entire agreement of the parties with respect to the subject matter hereof and supersedes all prior oral and written understandings of the parties.

5.5 Governing Law. This Agreement shall be governed by and construed in accordance with the laws of the State of Delaware as applied to contracts between Delaware residents to be wholly performed within the State of Colorado.

IN WITNESS WHEREOF, the parties hereto have executed this Agreement as of the day and year first above written.

**EXECUTIVE**

**HESKA CORPORATION**  
a Delaware corporation

\_\_\_\_\_  
Address \_\_\_\_\_  
\_\_\_\_\_

By: \_\_\_\_\_  
Title: \_\_\_\_\_



**ASSIGNMENT SEPARATE FROM CERTIFICATE**

FOR VALUE RECEIVED, I, \_\_\_\_\_, hereby sell, assign and transfer unto \_\_\_\_\_(\_\_\_\_\_) shares of the Common Stock of Heska Corporation, standing in my name on the books of said corporation represented by Certificate No. \_\_\_\_\_herewith and do hereby irrevocably constitute and appoint \_\_\_\_\_ to transfer said stock on the books of the within-named corporation with full power of substitution in the premises.

Dated: \_\_\_\_\_, 20\_\_.

Signature:

This Assignment Separate from Certificate was executed in conjunction with the terms of a Restricted Stock Grant Agreement between the above assignor and Heska Corporation, dated \_\_\_\_\_, 2015.

**Instruction: Please do not fill in any blanks other than the signature line.**

## HESKA CORPORATION 2003 EQUITY INCENTIVE PLAN

STOCK OPTION AGREEMENT  
(EMPLOYEES AND CONSULTANTS)

<b>Tax Treatment</b>	This option is intended to be an incentive stock option under section 422 of the Internal Revenue Code or a nonstatutory option, as provided in the Notice of Stock Option Grant. To the extent this option is designated an incentive stock option and it does not qualify as an incentive stock option and it does not qualify as an incentive stock option under applicable laws, it will be treated as a nonstatutory option.
<b>Vesting/ Exercisability</b>	<p>This option vests and becomes exercisable in installments, as shown in the Notice of Stock Option Grant. In addition, in the event your service as an Employee, Director or Consultant terminates because of your death, your option shall become fully vested and exercisable as to the total number of shares subject thereto immediately upon the date of your death.</p> <p>Except as otherwise provided below following a Change in Control, no additional shares become vested after your Termination of Service and the option shall terminate as to any shares that are unvested as of the end of business on the date of your Termination of Service.</p>
<b>Term</b>	This option expires in any event at the close of business at Company headquarters on the day before the 10th anniversary of the Date of Grant, as shown in the Notice of Stock Option Grant. (It will expire earlier if your service terminates, as described below.)
<b>Regular Termination</b>	In the event of your Termination of Service for any reason except death or Disability, then this option will expire as to unexercised vested option shares at the close of business at Company headquarters on the date three months after your termination date. The Company determines when your service terminates for this purpose.
<b>Death</b>	In the event of your Termination of Service because of your death or your death within three months after your Termination of Service, then this option will expire as to unexercised vested option shares at the close of business at Company headquarters on the date one year after your date of death.

<b>Disability</b>	In the event of your Termination of Service because of your Disability, then this option will expire as to unexercised vested option shares at the close of business at Company headquarters on the date one year after your termination date.
<b>Leaves of Absence</b>	Vesting of this option shall be suspended during any unpaid leave of absence unless continued vesting is required by the terms of the leave or by applicable law.
<b>Change in Control</b>	<p>This option shall vest and become exercisable in full if (i) the Company is subject to a Change in Control, (ii) this option is not continued by the Company and (iii) this option is not either assumed by the surviving corporation or its parent or substituted for by the surviving corporation's or its parent's issuing its own option in replacement of this option. This option shall vest and become exercisable in full if (i) the Company is subject to a Change in Control and (ii) within twelve months thereafter the surviving corporation or its parent triggers a Termination of Service for you without your consent and without Cause. If the surviving corporation or its parent demotes you to a lower position, materially reduces your authority or responsibilities, materially reduces your total compensation or announces its intention to relocate your principal place of work by more than 20 miles, then that action shall be treated as triggering a Termination of Service under this Agreement. For the avoidance of doubt, a refusal by the surviving corporation or its parent to extend a consulting engagement beyond its current term shall not be deemed to trigger any option to vest and become immediately exercisable under this Agreement.</p> <p>“Cause” shall mean (i) your failure to perform your assigned duties or responsibilities as an Employee, Director or Consultant (other than a failure resulting from death or Disability) after notice thereof from the surviving corporation or its parent describing your failure to perform such duties or responsibilities; (ii) your material breach of any confidentiality agreement or invention assignment between you and the Company or a Subsidiary; (iii) your engaging in any act of dishonesty, fraud, misrepresentation, moral turpitude, or misappropriation of material property that was or is materially injurious to the Company or its Affiliates; (iv) your violation of any federal or state regulation applicable to the Company’s business; or (v) your being convicted of, or entering a plea of nolo contendere to, any crime.</p>

**Restrictions on Exercise**

The Company will not permit you to exercise this option if the issuance of shares at that time would violate any law or regulation, and the Company will have no liability for failure to issue or deliver any shares upon exercise of this option if the issuance or delivery would violate any law or regulation as determined by the Company in consultation with its legal counsel. This option may not be exercised for a fraction of a share.

**Notice of Exercise**

When you wish to exercise this option, you must notify the Company by filing the proper "Notice of Exercise" form at the address given on the form. Your notice must specify how many shares you wish to purchase. The exercise will be effective when the Company receives the Notice of Exercise with the option exercise payment described herein.

If someone else wants to exercise this option after your death, that person must prove to the Company's satisfaction that he or she is entitled to do so.

**Form of Payment**

When you submit your notice of exercise, you must include payment of the option exercise price for the shares you are purchasing. Payment may be made in one (or a combination of two or more) of the following forms:

- Cash, check or wire transfer.
- Certificates for shares of Company stock that you own, along with any forms needed to affect a transfer of those shares to the Company. The value of the shares, determined as of the effective date of the option exercise, will be applied to the option exercise price. However, the Company may restrict your ability to surrender shares of Company stock (including your ability to surrender any particular shares of Company Stock held by you) in payment of the exercise price if your doing so would result in the Company's recognizing additional compensation expense with respect to this option for financial reporting purposes.
- Irrevocable directions to a securities broker approved by the Company to sell all or part of your option shares and to deliver to the Company proceeds from the sale in an amount sufficient to pay the option exercise price and any withholding taxes. (The balance of the sale proceeds, if any, will be delivered to you.) The directions must be given by signing a special "Notice of Exercise" form provided by the Company.

<b>Withholding Taxes and Stock Withholding</b>	You will not be allowed to exercise this option unless you make arrangements acceptable to the Company to pay any withholding taxes that may be due as a result of the option exercise. These arrangements may include (with the Company's approval) withholding shares of Company stock that otherwise would be issued to you when you exercise this option. The value of these shares, determined as of the effective date of the option exercise, will be applied to the withholding taxes.
<b>Restrictions on Resale</b>	By signing this Agreement, you agree not to sell any option shares at a time when applicable laws, Company policies or an agreement between the Company and its underwriters prohibit a sale. This restriction will apply as long as you are an Employee, Consultant or Outside Director of the Company or a Subsidiary.
<b>Transfer of Option</b>	<p>Prior to your death, only you may exercise this option. You cannot sell, transfer, pledge or assign this option. For instance, you may not sell this option or use it as security for a loan. You may, however, dispose of this option in your will, by the laws of descent and distribution or through a beneficiary designation.</p> <p>Regardless of any marital property settlement agreement, the Company is not obligated to honor a notice of exercise from your former spouse, nor is the Company obligated to recognize your former spouse's interest in your option in any other way.</p>
<b>Retention Rights</b>	Neither your option nor this Agreement gives you the right to be employed or otherwise retained by the Company in any capacity. The Company reserves the right to terminate your service at any time, with or without cause.
<b>Stockholder Rights</b>	You, or your estate or heirs, have no rights as a stockholder of the Company until you have exercised this option by giving the required notice to the Company and paying the exercise price.
<b>Applicable Law</b>	This Agreement will be interpreted and enforced under the laws of the State of Delaware (without giving effect to its conflict of laws provisions).

**The Plan and  
Other Agreements**

The Amended and Restated 2003 Equity Incentive Plan is incorporated in this Agreement by reference. Unless otherwise defined herein, all capitalized terms herein have the same defined meanings as in the Amended and Restated 2003 Equity Incentive Plan. In the event of any conflict between the terms and provisions of the Plan and this Agreement, the Plan terms and provisions shall govern.

This Agreement and the Plan constitute the entire understanding between you and the Company regarding this option. Any prior agreements, commitments or negotiations concerning this option are superseded. This Agreement may be amended only by another written agreement, signed by both parties.

**BY SIGNING THE NOTICE OF STOCK OPTION GRANT OF THIS AGREEMENT, YOU AGREE TO ALL OF THE TERMS AND CONDITIONS DESCRIBED ABOVE AND IN THE PLAN.**



## HESKA CORPORATION 2003 EQUITY INCENTIVE PLAN

NON-QUALIFIED STOCK OPTION AGREEMENT  
(OUTSIDE DIRECTORS)

<b>Tax Treatment</b>	This option is intended to be a Non-qualified Stock Option and not an Incentive Stock Option under section 422 of the Internal Revenue Code.
<b>Vesting/ Exercisability</b>	<p>This option vests and becomes exercisable in installments, as shown in the Notice of Stock Option Grant. In addition, in the event your service as a Director terminates because of your death, this option shall become fully vested and exercisable as to the total number of shares subject thereto immediately upon the date of your death.</p> <p>Except as otherwise provided below following a Change in Control, no additional shares become vested after your Termination of Service and the option shall terminate as to any shares that are unvested as of the end of business on the date of your Termination of Service.</p>
<b>Term</b>	This option expires in any event at the close of business at Company headquarters on the day before the 10th anniversary of the Date of Grant, as shown in the Notice of Stock Option Grant or as provided in this Agreement or the Plan.
<b>Regular Termination</b>	In the event of your Termination of Service for any reason other than death or Disability, then this option will expire as to unexercised vested option shares at the close of business at Company headquarters on the date three months after your termination date. The Company determines when your service terminates for this purpose.
<b>Death</b>	In the event of your Termination of Service because of your death or your death within three months after your Termination of Service, then this option will expire as to unexercised vested option shares at the close of business at Company headquarters on the date one year after your date of death.
<b>Disability</b>	In the event of your Termination of Service because of your Disability, then this option will expire as to unexercised vested option shares at the close of business at Company headquarters on the date one year after your termination date.
<b>Leaves of Absence</b>	Vesting of this option shall be suspended during any unpaid leave of absence unless continued vesting is required by the terms of the leave or by applicable law.



**Change in Control**

This option shall vest and become exercisable in full if (i) the Company is subject to a Change in Control, (ii) this option is not continued by the Company and (iii) this option is not either assumed by the surviving corporation or its parent or substituted for by the surviving corporation's or its parent's issuing its own option in replacement of this option. This option shall vest and become exercisable in full if (i) the Company is subject to a Change in Control and (ii) within twelve months thereafter you are removed as a Director.

"Cause" shall mean (i) your failure to perform your assigned duties or responsibilities as a Director (other than a failure resulting from death or Disability) after notice thereof from the surviving corporation or its parent describing your failure to perform such duties or responsibilities; (ii) your material breach of any confidentiality agreement or invention assignment agreement between you and the Company or a Subsidiary; (iii) your engaging in any act of dishonesty, fraud, misrepresentation, moral turpitude, or misappropriation of material property that was or is materially injurious to the Company or its Affiliates; (iv) your violation of any federal or state regulation applicable to the Company's business; of (v) your being convicted of, or entering a plea of nolo contendere to, any crime.

**Restrictions on Exercise**

The Company will not permit you to exercise this option if the issuance of shares at that time would violate any law or regulation, and the Company will have no liability for failure to issue or deliver any shares upon exercise of this option if the issuance or delivery would violate any law or regulation as determined by the Company in consultation with its legal counsel. No shares shall be issued pursuant to this option unless and until any then applicable requirements of state or federal laws and regulatory agencies have been fully complied with to the satisfaction of the Company and its counsel. This option may not be exercised for a fraction of a share.

**Notice of Exercise**

When you wish to exercise this option, you must notify the Company by filing the proper "Notice of Exercise" form at the address given on the form. Your Notice of Exercise must specify how many shares you wish to purchase. The exercise will be effective when the Company receives the Notice of Exercise with the option exercise payment described herein.

If someone else wants to exercise this option after your death, that person must prove to the Company's satisfaction that he or she is entitled to do so.

**Form of Payment**

When you submit your Notice of Exercise, you must include payment of the option exercise price for the shares you are purchasing. Payment may be made in one (or a combination of two or more) of the following forms:

- Cash, check or wire transfer.
- Certificates for shares of Company stock that you own, along with any forms needed to affect a transfer of those shares to the Company. The value of the shares, determined as of the effective date of the option exercise, will be applied to the option exercise price. However, the Company may restrict your ability to surrender shares of Company stock (including your ability to surrender any particular shares of Company Stock held by you) in payment of the exercise price if your doing so would result in the Company's recognizing additional compensation expense with respect to this option for financial reporting purposes.
- Irrevocable directions to a securities broker approved by the Company to sell all or part of your option shares and to deliver to the Company proceeds from the sale in an amount sufficient to pay the option exercise price and any withholding taxes. (The balance of the sale proceeds, if any, will be delivered to you.) The directions must be given by signing a special "Notice of Exercise" form provided by the Company.

**Withholding Taxes  
and Stock  
Withholding**

You will not be allowed to exercise this option unless you make arrangements acceptable to the Company to pay any withholding taxes that may be due as a result of the option exercise. These arrangements may include (with the Company's approval) withholding shares of Company stock that otherwise would be issued to you when you exercise this option. The value of these shares, determined as of the effective date of the option exercise, will be applied to the withholding taxes.

**Restrictions on  
Resale**

By signing this Agreement, you agree not to sell any option shares at a time when applicable laws, Company policies or an agreement between the Company and its underwriters prohibit a sale. This restriction will apply as long as you are an Employee, Consultant or Outside Director of the Company or a Subsidiary.

**Transfer of Option**

Prior to your death, only you may exercise this option. You cannot sell, transfer, pledge or assign this option. For instance, you may not sell this option or use it as security for a loan. You may, however, dispose of this option in your will, by the laws of descent and distribution or through a beneficiary designation.

Regardless of any marital property settlement agreement, the Company is not obligated to honor a notice of exercise from your former spouse, nor is the Company obligated to recognize your former spouse's interest in your option in any other way.

<b>Retention Rights</b>	Neither your option nor this Agreement gives you the right to be employed or otherwise retained by the Company in any capacity. The Company reserves the right to terminate your service at any time, with or without cause.
<b>Stockholder Rights</b>	You, or your estate or heirs, have no rights as a stockholder of the Company until you have exercised this option by giving the required notice to the Company and paying the exercise price.
<b>Applicable Law</b>	This Agreement will be interpreted and enforced under the laws of the State of Delaware (without giving effect to its conflict of laws provisions).
<b>The Plan and Other Agreements</b>	<p>The Amended and Restated 2003 Equity Incentive Plan is incorporated in this Agreement by reference. Unless otherwise defined herein, all capitalized terms herein have the same defined meanings as in the Amended and Restated 2003 Equity Incentive Plan. In the event of any conflict between the terms and provisions of the Plan and this Agreement, the Plan terms and provisions shall govern.</p> <p>This Agreement and the Plan constitute the entire understanding between you and the Company regarding this option. Any prior agreements, commitments or negotiations concerning this option are superseded. This Agreement may be amended only by another written agreement, signed by both parties.</p>
<b>Acceptance</b>	You hereby acknowledge receipt of a copy of the Plan and this Agreement. You have read and understand the terms and provisions thereof, and accept this option subject to all the terms and conditions of the Plan and this Agreement. You acknowledge that there may be adverse tax consequences upon exercise of this option or disposition of the underlying shares and that you should consult a tax advisor prior to such exercise or disposition.

**BY SIGNING THE NOTICE OF STOCK OPTION GRANT, YOU AGREE TO ALL OF THE TERMS AND CONDITIONS DESCRIBED ABOVE AND IN THE PLAN.**



**Heska Corporation****Management Incentive Plan Master Document****Amended and Restated as of May 6, 2014**

This Management Incentive Plan Master Document (“MIP”) is intended to provide incentives to the senior management of Heska Corporation (“Heska” or the “Company”) for the achievement of goals and objectives that are essential to the growth and continued success of the Company. This MIP is to act as a master document for future plans and replaces in its entirety any and all previous management incentive plans of the Company. The MIP is intended to permit, if the Company desires, amounts paid to qualify as performance-based compensation deductible by the Company under Section 162(m). All employees of the Company and its affiliates are eligible for participation in the MIP.

**ARTICLE I  
ANNUAL BENEFIT**

Section 1.1 Annual Benefit. At the sole and absolute discretion of the Compensation Committee of the Board of Directors (the “Compensation Committee”), Heska may adopt an annual plan for a given year (a “Plan Year”) by agreeing upon Category Percentages, a Plan Allocation, Key Parameters and a Payout Structure, as defined and discussed below. For example, a plan effective January 1, 20xx and ending December 31, 20xx with given characteristics could be adopted by the Compensation Committee and would be referred to as the “20xx MIP”. As described below, any and all payments made under the MIP are referred to as a “MIP Payout.”

Section 1.2 Category Percentages. The MIP will include an “Incentive Target” for each eligible participant to be based on a percentage of the participants’ base salary earned during the year. This calculation excludes commissions, bonuses, relocation payments or other forms of compensation not considered part of the participants’ base pay. The percent of base salary used for determining the incentive target will be determined by the category of position held by the participant (the “Category Percentages”). The Compensation Committee shall agree upon the Category Percentages for each Plan Year.

Section 1.3 Plan Allocation. The Compensation Committee shall agree on a “Plan Allocation”, which may include parameters such as company, department or individual performance, for each Plan Year. The Plan Allocation is to be used as a guideline in determining any MIP Payout to each participant in a given Plan Year, although the Chief Executive Officer (the “CEO”) or the Compensation Committee, as outlined below, shall maintain sole and absolute discretion in determining the appropriate MIP Payout for any participant. For individuals becoming eligible for participation in the MIP after the beginning of a Plan Year, all MIP calculations shall be based on the amount of base pay earned while a plan participant. Earnings prior to becoming a plan participant shall be excluded.

Section 1.4 Key Parameters. The MIP will be structured to provide payments contingent on satisfaction of the “Key Parameters,” which will be determined by the Compensation Committee for each Plan Year, and which may include any of the following:

- (a) operating income;
- (b) net earnings or net income (before or after taxes);
- (c) basic or diluted earnings per share (before or after taxes);
- (d) revenue, revenues, net revenue, net revenues, net revenue growth or net revenues growth;
- (e) gross revenue or gross revenues;
- (f) gross profit or gross profit growth;
- (g) net operating profit (before or after taxes);
- (h) return on assets, capital, invested capital, equity or sales;
- (i) cash flow (including, but not limited to, operating cash flow, free cash flow, and cash flow return on capital);
- (j) earnings before or after taxes, interest, depreciation and/or amortization;
- (k) gross or operating margins;
- (l) improvements in capital structure;
- (m) budget and expense management;
- (n) productivity targets;
- (o) economic value added or other value added measurements;
- (p) share price (including, but not limited to, growth measures and total shareholder return);
- (q) expense targets;
- (r) margins;
- (s) operating efficiency;
- (t) working capital targets;

- (u) enterprise value;
- (v) safety record;
- (w) completion of business acquisition, divestment or expansion;
- (x) operating cash flow;
- (y) book value;
- (z) tangible book value;
- (aa) pretax income;
- (bb) net income plus deferred taxes;
- (cc) cash position;
- (dd) total shareholder return;
- (ee) contract or other development of relationship with identified suppliers, distributors or other business partners; or
- (ff) new product development (including but not limited to third-party collaborations or contracts, and with milestones that may include but are not limited to contract execution, proof of concept, regulatory approval, product launch and targets such as unit volume and revenue following product launch).

Such Key Parameters may relate to the performance of the Company as a whole, a business unit, division, department, individual or any combination of these and may be applied on an absolute basis and/or relative to one or more peer group companies or indices, or any combination thereof, as the Committee may determine.

Section 1.5 Payout Structure. For each Plan Year, the Compensation Committee shall agree upon a “Payout Structure” based on the Key Parameters. The Payout Structure will determine the amount of the “Incentive Pool” based on performance in relation to the Key Parameters.

Section 1.6 Certification. To the extent any Key Parameter targets are achieved and the MIP is intended to constitute performance-based compensation for purposes of Code Section 162(m), the Compensation Committee will certify as such in writing, in accordance with Internal Revenue Code Section 162(m), and will determine, in accordance with the Payout Structure, the amount of each plan participant’s MIP Payout.

Section 1.7 Adjustments. The Committee is authorized, in its sole discretion, to adjust or modify the calculation of a Payout Structure in connection with any one or more of the following events:

- results;
- a. asset write-downs;
  - b. significant litigation or claim judgments or settlements;
  - c. the effect of changes in tax laws, accounting standards or principles, or other laws or regulatory rules affecting reporting results;
  - d. any reorganization and restructuring programs;
  - e. extraordinary nonrecurring items as described in Accounting Principles Board Opinion No. 30 (or any successor pronouncement thereto) and/or in management's discussion and analysis of financial condition and results of operations appearing in the Company's annual report to shareholders for the applicable year or period;
  - f. acquisitions or divestitures;
  - g. any other specific unusual or nonrecurring events or objectively determinable category thereof;
  - h. foreign exchange gains and losses; and
  - i. a change in the Company's fiscal year.

No adjustment shall be made if the effect would be to cause a Payout Structure to fail to qualify as performance-based compensation under Section 162(m).



## **ARTICLE II PAYMENTS**

Section 2.1 Payment to Individual Participants. No MIP Payout to any single plan participant will exceed \$500,000 per calendar year. The Compensation Committee will determine any MIP Payout to the CEO. Any individual MIP Payouts to other executive officers will generally be recommended to the Compensation Committee by the CEO, although the Compensation Committee will make the final determination of any individual MIP Payouts to executive officers of the Company other than the CEO. Any individual MIP Payouts to other plan participants will be determined by the CEO.

Section 2.2 Medium of Payment. In the sole and absolute discretion of the Compensation Committee, the MIP Payout may be made in cash, in stock of the Company, in unsecured notes, or in any other alternative forms of compensation.

Section 2.3 Time of Payment. All MIP Payouts earned shall be paid only after the Compensation Committee has reviewed management's calculations of such MIP Payouts and ensured the Incentive Pool is large enough to cover all such MIP Payouts. MIP Payouts shall be made no later than March 15th of the year following the end of any Plan Year.

Section 2.4 Employment Required. MIP participants are determined by the CEO and, except in the case of the participant's death, must remain active employees of Heska Corporation or one of its affiliates in a position which qualifies for MIP participation through the end of a given Plan Year in order to be eligible to earn any MIP Payouts.

Section 2.5 In the case of a Change of Control. If the Company experiences a Change in Control (as defined in Heska's 1997 Stock Incentive Plan) during any Plan Year, the Plan Year Incentive Pool will be a Fully Funded Pool (meaning that the Incentive Pool will equal to the sum of the Incentive Targets of all MIP participants and any MIP Payouts will be prorated from the beginning of the Plan Year until the date of the Change of Control. Payouts will occur at a time as close as commercially reasonably practicable to the date of the closing of the Change of Control.

Section 2.6 In the case of disability. Time spent on Short Term Disability will count as active time in the MIP. Long Term Disability time will not count as active time in the MIP. Personal leave time will be considered by the Compensation Committee or its designee on a case by case basis.

Section 2.7 In the case of death. A prorated payment of any MIP Payout will be made to the employee's designated beneficiary. The payment will be paid at the normal payment time of the MIP Payouts.

Section 2.8 Partial Payments or Exceptions. The Compensation Committee must approve partial payments or exceptions to any major provision of this MIP.

**ARTICLE III  
MISCELLANEOUS**

Section 3.1 Parachute Payments. To the extent that any of the payments and benefits provided for under the MIP or any other agreement or arrangement between the Company and a participant (collectively, the "Payments") (i) constitute a "parachute payment" within the meaning of Code Section 280G and (ii) but for this paragraph would be subject to the excise tax imposed by Section 4999 of the Code, then the Payments shall be payable either (i) in full or (ii) as to such lesser amount which would result in no portion of such Payments being subject to excise tax under Section 4999 of the Code (determined in accordance with the reduction of payments and benefits paragraph set forth below); whichever of the foregoing amounts, taking into account the applicable federal, state and local income taxes and the excise tax imposed by Section 4999, results in the participant's receipt on an after-tax basis, of the greatest amount of benefits under this MIP, notwithstanding that all or some portion of such benefits may be taxable under Section 4999 of the Code. Except to the extent, if any, otherwise agreed in writing between a participant and the Company, any determination required under this provision will be made by accountants selected by the Company, whose determination shall be conclusive and binding upon the participant and the Company for all purposes.

Section 3.2 No Right to Employment. Nothing in this document is to be construed as a contract of employment of a defined period of time or otherwise altering the status of employee as an at-will employee of the Company. Either party may elect to terminate the employment relationship at any time, without cause or advance notice.



**Heska Corporation**  
**2015 Management Incentive Plan**

1. The Category Percentages for the 2015 MIP are as follows:

<u>Title</u>	<u>Category Percentage</u>
Executive Vice President-level	40.0% of base salary
Vice Presidents	35.0% of base salary
Directors	25.0% of base salary

2. The Plan Allocation for the 2015 MIP is as follows:

- 50% on achievement of the company-wide financial objective and 50% on individual performance

3. The Key Parameters for the 2015 MIP are as follows:

- 1) Pre-MIP Operating Income and 2) Revenue

4. The Payout Structure for the 2015 MIP is as follows:

Pre-MIP Operating Income (% MIP Goal)	Revenue (% MIP Goal)	Incentive Pool (% MIP Goal)	Post-MIP Operating Income
\$4,000K (44%)	\$90,000K (86%)	\$0 (0%)	\$4,000K
\$5,000K (55%)	\$91,000K (87%)	\$220K (20%)	\$4,780K
\$7,266K (80%)	\$93,000K (89%)	\$660K (60%)	\$6,606K
\$8,174K (90%)	\$94,268K (90%)	\$880K (80%)	\$7,294K
\$9,083K (100%)	\$104,742K (100%)	\$1,100K (100%)	\$7,983K
\$9,991K (110%)	\$115,216K (110%)	\$1,375K (125%)	\$8,616K
\$10,900K (120%)	\$125,690K (120%)	\$1,650K (150%)	\$9,250K

There shall be no MIP Payout if Pre-MIP Operating Income is less than \$4,000K or Revenue is less than \$90,000K. If necessary, MIP Payouts shall be determined by interpolating between MIP Payout result rows, subject to a minimum Post-MIP Operating Income interpolation.

5. MIP Payout Features

- Amount – The actual amount of a participant’s MIP Payout will be determined in the sole and absolute discretion of the CEO or the Compensation Committee, and may be more or less than the percentage of MIP Goals achieved above.
- Eligibility – To earn an MIP Payout, a participant must remain an active employee of Heska Corporation or one of its affiliates through the time of payment of MIP Payouts (to be no later than March 15, 2016).
- Medium of Payment – MIP Payouts are to be made in cash, although by March 13, 2015 Executive Vice President-level participants may elect to receive up to 50% of his or her MIP Payout in stock or options to acquire stock (which are to be valued based on market price and Heska Corporation’s GAAP option valuation policy), subject to a maximum grant of such participant’s Incentive Target and vesting based upon MIP Payout achieved.
- Maximum payout – The maximum payout to any participant shall be 200% such participant’s Incentive Target, which is calculated by multiplying such participant’s base salary by the Category Percentage applicable to such participant.

**HESKA CORPORATION**  
**1997 STOCK INCENTIVE PLAN**  
**RESTRICTED STOCK GRANT AGREEMENT**

THIS AGREEMENT is made as of the 6<sup>th</sup> day of May, 2014 (the "Grant Date") by and between Heska Corporation (the "Company"), and Kevin S. Wilson (the "Executive"), in connection with the execution of an Employment Agreement dated on or about the same date between the Company and Executive (the "Employment Agreement").

In consideration of the mutual covenants and representations herein set forth, the Company and Executive agree as follows:

**SECTION 1. GRANT OF STOCK.**

1.1 Precedence of Plan. This Agreement is subject to and shall be construed in accordance with the terms and conditions of the Heska Corporation 1997 Stock Incentive Plan (the "Plan"), as now or hereinafter in effect. Any capitalized terms that are used in this Agreement without being defined and that are defined in the Plan shall have the meaning specified in the Plan.

1.2 Grant of Stock. The Company hereby grants to Executive an aggregate of 130,000 shares of Restricted Stock (the "Shares"), subject to vesting as provided in Section 2.

**SECTION 2. UNVESTED SHARES SUBJECT TO FORFEITURE.**

2.1 Shares Subject to Forfeiture.

a. Vesting Conditions. The Shares will vest as follows:

i. Market Price Vesting. 13,000 shares will vest on each date that the 90-Day Price first equals or exceeds each of the following thresholds (the "Market-Vesting Thresholds"): (i) \$12.60, (ii) \$16.38, (iii) \$21.24, (iv) \$26.55 and (v) \$31.95 (collectively, the "Market-Vesting Shares"). In the event of a stock split, stock dividend or reverse stock split affecting the Common Stock, the Committee will adjust the Market-Vesting Thresholds to appropriately reflect such event. Each Market-Vesting Threshold is a distinct vesting trigger and multiple Market-Vesting Threshold events may be achieved simultaneously; for the avoidance of doubt and by way of illustration, if the 90-Day Price equals or exceeds \$16.38, then 26,000 shares would vest.

ii. EBITDA Vesting. 13,000 shares will vest on each Reporting Date that the Company's Adjusted EBITDA for the preceding fiscal year first equals or exceeds each of the following thresholds (the "EBITDA-Vesting Thresholds"): (i) \$2,460,000, (ii) \$3,200,000, (iii) \$4,150,000, (iv) \$5,180,000 and (v) \$6,240,000 (collectively, the "EBITDA-Vesting Shares"). Each EBITDA-Vesting Threshold is a distinct vesting trigger and multiple EBITDA-Vesting Threshold events may be achieved simultaneously; for the avoidance of doubt and by way of illustration, if on the Reporting Date for Fiscal Year 2014 the Adjusted EBITDA is \$3,400,000, then 26,000 shares would vest. For purposes of this Agreement, "Reporting Date" means the date in each fiscal year that the Company's independent public accountants issue their

audit report on the Company's financial statements for the preceding fiscal year (each, an "Audit Report"). For purposes of this Agreement, "Adjusted EBITDA" means for any fiscal year, the following, determined on a consolidated basis in accordance with generally-accepted accounting principles for the Company and its subsidiaries, based on the Audit Report for such year: (x) consolidated net income plus (y) the sum of the following, without duplication, to the extent deducted in determining such consolidated net income: (1) income and franchise tax expense, (2) interest and other expense (net), (3) amortization and depreciation and (4) compensation expense paid to the Company's Executive Chair, if any.

b. Financial Statement Restatement. Notwithstanding any provision of this Agreement to the contrary, in the event that the Company issues a restatement of its audited financial statements (a "Restatement") after any portion of the Shares have vested:

i. If any portion of the Shares have vested based on achievement of an EBITDA-Vesting Threshold and within 4 years thereafter the Company subsequently issues a Restatement affecting Adjusted EBITDA for the corresponding fiscal year such that the EBITDA-Vesting Threshold would not have been met, such portion of the Shares will be deemed not to have vested, and

ii. If any portion of the Shares have vested based on achievement of a Market-Vesting Threshold, and within 2 years thereafter the Company issues a Restatement affecting the Adjusted EBITDA for the corresponding fiscal year such that the Adjusted EBITDA set forth in the Restatement is less than the Adjusted EBITDA target corresponding to such Market-Vesting Threshold in the following table, then such portion of the Shares will be deemed not to have vested:

	Market-Vesting Threshold	Target Adjusted EBITDA
Level 1	\$12.60	\$2,460,000
Level 2	\$16.38	\$3,200,000
Level 3	\$21.24	\$4,150,000
Level 4	\$26.55	\$5,180,000
Level 5	\$31.95	\$6,240,000

iii. If any portion of the Shares is deemed not to have vested pursuant to the foregoing paragraphs (i) or (ii) (an "Unearned Grant"), then Executive shall either (x) promptly return the Shares comprising the Unearned Grant to the Company or (y) if Executive has sold such Shares, pay to the Company within one year from the date of the corresponding Restatement an amount equal to the proceeds Executive received from any sale of such Shares not returned by Executive pursuant to the foregoing clause (x). In addition to the foregoing, Executive's compensation and equity awards shall remain subject to any applicable law (including without limitation Section 302 of the Sarbanes Oxley Act and Section 954 of the Dodd Frank Act) or regulation in effect from time to time.

c. In the event that Executive's employment with the Company is terminated prior to vesting, Executive will forfeit all right to Shares that have not yet vested.

d. Notwithstanding the previous paragraph (c):

i. If Executive is terminated by the Company without Cause (other than in connection with a Change in Control) and within 180 days after such termination either (A) the Company achieves one or more Market-Vesting Thresholds or (B) a Reporting Date occurs on which the Company achieves one or more EBITDA-Vesting Thresholds, then any Shares that would have otherwise vested if such termination had not occurred will be deemed to vest.

ii. If Executive is terminated by the Company without Cause or voluntarily with Good Reason, and such termination is In Connection with a Change of Control, (y) Shares that would otherwise vest in accordance with the Market-Vesting Threshold if the 90-Day Price were to equal the Change of Control Price will be deemed to vest, and (z) Shares that would otherwise vest in accordance with the EBITDA-Vesting Threshold will vest if the Committee estimates that, as of the last day of the month immediately preceding the Change of Control, if such date were a Reporting Date and taking into account the twelve-month period ending on such date, the EBITDA-Vesting Threshold would be met.

e. Definitions. For purposes of this Agreement, the following definitions will apply:

i. "90-Day Price" means, with respect to any date, the average of the closing prices per share of the Company's Common Stock for the 90 trading days ending on such date (inclusive) on the NASDAQ Stock Market, or if the Shares are not traded on the NASDAQ Stock Market, the average of the high bid and low asked prices on such trading days quoted on the NASDAQ OTC Bulletin Board or by the National Quotation Bureau, Inc., or a comparable service as determined in the discretion of the Committee.

ii. "Cause" means mean the occurrence of one or more of the following: (i) conviction of, or entry of a plea of nolo contendere to, any felony crime (including one involving moral turpitude), or any crime which reflects so negatively on the Company to be detrimental to the Company's image or interests, or any act of fraud or dishonesty that has such negative reflection upon the Company; (ii) the repeated commitment of insubordination or refusal to comply with any reasonable request of the Board related to the scope or performance of Executive's duties; (iii) possession of any illegal drug on Company premises or being under the influence of illegal drugs or abusing prescription drugs or alcohol while on Company business, attending Company -sponsored functions, or on the Company premises; (iv) the gross misconduct or gross negligence in the performance of Executive's responsibilities which, based upon good faith and reasonable factual investigation of the Board, demonstrates Executive's unfitness to serve; (v) material breach of Executive's obligations under this Agreement; or (vi) material breach of any fiduciary duty of Executive to the Company, which results in material damage to the Company or its business; provided, however, that if any occurrence under subsections (ii), (iv), (v), and (vi) may be cured, the Company will provide notice to Executive describing the nature of such event and Executive will thereafter have thirty (30) days to cure such event, and if such event is cured with that 30-day period, then grounds will no longer exist for terminating Executive's employment for Cause.

iii. "Change of Control" means (i) a sale of all or substantially all of the Company's assets, (ii) any merger, consolidation, or other business combination transaction of the Company with or into another corporation, entity, or person, other than a transaction in which the holders of at least a majority of the shares of voting capital stock of the Company outstanding immediately prior to such transaction continue to hold (either by such shares remaining outstanding or by their being converted into shares of voting capital stock of the surviving entity) a majority of the total voting power represented by the shares of voting capital stock of the Company (or the surviving entity) outstanding immediately after such transaction, (iii) the direct or indirect acquisition (including by way of a tender or exchange offer) by any person, or persons acting as a group, of beneficial ownership or a right to acquire beneficial ownership of shares representing a majority of the voting power of the then outstanding shares of capital stock of the Company, (iv) a contested election of Directors, as a result of which or in connection with which the persons who were Directors before such election or their nominees cease to constitute a majority of the Board, or (v) a dissolution or liquidation of the Company.

iv. "Change of Control Price" means the net price per share of Company Common Stock, determined by the Committee in good faith, based on the fair market value of the total consideration received by the Company and its stockholders in connection with the transaction resulting in the Change of Control, net of fees, expenses and commissions incurred by the Company in connection with such transaction and any compensation or other payments made by the Company or its successor to Company employees as a result of such Change of Control.

v. "Committee" means the Compensation Committee of the Board.

vi. "Good Reason" means the occurrence of any of the following without Executive's express written consent:

(1) Executive's authority with the Company is, or Executive's duties or responsibilities as President and Chief Executive Officer are, materially diminished relative to Executive's authority, duties, and responsibilities as in effect immediately prior to such change;

(2) a material diminution in Executive's Base Salary as in effect immediately prior to such diminution; provided, that an across-the-board reduction in the base compensation and benefits of all other executive officers of the Company by the same percentage amount (or under the same terms and conditions) as part of a general base compensation reduction and/or benefit reduction shall not constitute such a qualifying material diminution;

(3) a material change in the geographic location of Executive's principal place of employment such that the new location results in a commute for Executive that is both (A) longer than Executive's commute prior to the relocation and (B) greater than fifty (50) road miles each way from Executive's home in the Beaver Creek, Colorado area;

(4) any material breach by the Company of any provision of the Employment Agreement; and



(5) any acquiring company fails to assume or be bound by the terms of the Employment Agreement In Connection with a Change of Control.

The aforementioned occurrences shall not be deemed Good Reason unless Executive gives the Company written notice of the existence of the condition which Executive believes constitutes Good Reason (which notice must be given within ninety (90) days of the initial existence of the condition) and such condition remains uncured for a period of thirty (30) days after the date of such notice. An event of Good Reason shall occur automatically at the expiration of such 30-day period if the relevant condition remains uncured at such time.

vii. "In Connection with a Change of Control" means that Executive's employment is terminated without Cause or for Good Reason during the period beginning three months prior to a Change of Control and ending eighteen months following a Change of Control.

2.2 Restriction on Transfer. Until the Shares are vested, the Shares may not be sold, transferred, pledged, assigned, or otherwise alienated or hypothecated.

### **SECTION 3. STOCKHOLDER RIGHTS**

3.1 Stock Register and Certificates. The Shares will be recorded in the stock register of the Company in the name of Executive. If applicable, a stock certificate or certificates representing the Shares will be registered in the name of Executive, but such certificates shall remain in the custody of the Company. Executive shall deposit with the Company a Stock Assignment Separate from Certificate in the form attached below as Attachment 1, endorsed in blank, so as to permit retransfer to the Company of all or a portion of the Shares that are forfeited or otherwise do not become vested in accordance with the Plan and this Agreement.

3.2 Exercise of Stockholder Rights. Executive shall have the right to vote the Shares (to the extent of the voting rights of said Shares, if any), to receive and retain all regular cash dividends and such other distributions, as the Board of Directors of the Company may, in its discretion, designate, pay or distribute on such Shares, and to exercise all other rights, powers and privileges of a holder of Common Stock with respect to such Shares, except as set forth in this Agreement and the Plan.

3.3 Legends. Certificates, if any, representing the Shares will contain the following or other legends in the Company's discretion:

THE SHARES REPRESENTED BY THIS CERTIFICATE ARE SUBJECT TO CERTAIN RESTRICTIONS UPON AND OBLIGATIONS WITH RESPECT TO TRANSFER AND RIGHTS OF REPURCHASE AS SET FORTH IN AN AGREEMENT BETWEEN THE COMPANY AND THE ORIGINAL REGISTERED HOLDER, A COPY OF WHICH IS ON FILE AT THE PRINCIPAL OFFICE OF THE COMPANY.

### **SECTION 4. RESPONSIBILITY FOR TAXES.**

4.1 Section 83(b) Election. Executive may complete and file with the Internal Revenue Service an election pursuant to Section 83(b) of the Internal Revenue Code to be taxed

currently on the fair market value of the Shares without regard to the vesting restrictions set forth in this Agreement. Executive shall be responsible for all taxes associated with the acceptance of the transfer of the Shares, including any tax liability associated with the representation of fair market value if the election is made pursuant to Code Section 83(b).

4.2 Withholding. In accordance with Section 12 of the Plan, Executive agrees to make arrangements satisfactory to the Company for the satisfaction of any withholding tax obligations that arise in connection with the Plan under applicable federal, state, local or foreign law. The Company in its discretion may permit Executive to satisfy all or part of his withholding or income tax obligations by having the Company withhold all or a portion of the Shares that otherwise would be issued to him on vesting.

**SECTION 5. MISCELLANEOUS.**

5.1 Not an Employment Contract. This Agreement is not an employment contract and nothing in this Agreement shall be deemed to create in any way whatsoever any obligation on the part of Executive to remain in the service of the Company in any capacity, or of the Company to continue Executive's service in any capacity.

5.2 Effect on Employee Benefits. Executive agrees that the Award will constitute special incentive compensation that will not be taken into account as "salary" or "compensation" or "bonus" in determining the amount of any payment under any pension, retirement, profit sharing or other remuneration plan of the Company unless so provided in such plan.

5.3 Further Assurances. The parties agree to execute such further instruments and to take such further action as may reasonably be necessary to carry out the intent of this Agreement.

5.4 Entire Agreement. This Agreement, including any exhibits, is the entire agreement of the parties with respect to the subject matter hereof and supersedes all prior oral and written understandings of the parties.

5.5 Governing Law. This Agreement shall be governed by and construed in accordance with the laws of the State of Delaware as applied to contracts between Delaware residents to be wholly performed within the State of Colorado.

IN WITNESS WHEREOF, the parties hereto have executed this Agreement as of the day and year first above written.

**EXECUTIVE**

**HESKA CORPORATION**  
a Delaware corporation

/s/ Kevin Wilson

By: /s/ Jason Napolitano  
Title: Chief Financial Officer

Address Box 4605  
Edwards, CO 81632

**ASSIGNMENT SEPARATE FROM CERTIFICATE**

FOR VALUE RECEIVED, I, \_\_\_\_\_, hereby sell, assign and transfer unto \_\_\_\_\_ (\_\_\_\_\_) shares of the Common Stock of Heska Corporation, standing in my name on the books of said corporation represented by Certificate No. \_\_\_\_herewith and do hereby irrevocably constitute and appoint \_\_\_\_\_ to transfer said stock on the books of the within-named corporation with full power of substitution in the premises.

Dated: \_\_\_\_\_, 20\_\_.

Signature: /s/ Kevin Wilson

This Assignment Separate from Certificate was executed in conjunction with the terms of a Restricted Stock Grant Agreement between the above assignor and Heska Corporation, dated \_\_\_\_\_, 2014.

**Instruction: Please do not fill in any blanks other than the signature line.**

**AMENDMENT TO EMPLOYMENT AGREEMENT BETWEEN HESKA  
CORPORATION AND STEVEN M. ASAKOWICZ**

This Amendment to Employment Agreement is dated effective as of March 1, 2015 (this "Amendment") and amends the Employment Agreement dated as of February 22, 2013 (the "Employment Agreement"), between Heska Corporation, a Delaware corporation ("Company"), and Steven M. Asakowicz ("Employee"). Unless otherwise defined in herein, all capitalized terms used herein shall have the meaning ascribed to them in the Employment Agreement.

**RECITALS**

Section 13 of the Employment Agreement requires the parties to modify the Employment Agreement in writing and to reference such Section, and the Employee and Company have agreed to modify the Employment Agreement to the extent set forth in this Amendment.

**AGREEMENT**

NOW, THEREFORE, in consideration of the foregoing, and other good and valuable consideration, including Employee's continued employment with Company, the receipt and sufficiency of which are hereby acknowledged, Employee and Company hereby agree as follows:

1. The first sentence of Section 3(a) of the Employment Agreement, which reads, "**Base Salary.** Heska will pay Executive an annual salary of \$175,000 as compensation for Executive's services (the "**Base Salary**")", is deleted in its entirety and replaced with the following, "**Base Salary.** Heska will pay Executive an annual salary of \$262,500 as compensation for Executive's services (the "**Base Salary**")."
2. The last sentence of Section 3(b) of the Employment Agreement, which reads, "In addition, Executive will be eligible for variable performance commissions for successful sales revenue and margin achievement, targeted, to be earned under separate schedule, from between \$50,000 and \$125,000." is hereby deleted in its entirety.
3. All other terms and conditions of the Employment Agreement shall remain in full force and effect. This Amendment, together with the Employment Agreement, contains all the terms and conditions agreed upon by the parties hereto regarding the subject matter hereof and thereof. All prior agreements, promises, negotiations and representations, either oral or written, relating to the subject matter of this Amendment or the Employment Agreement not expressly set forth in this Amendment or the Employment Agreement are of no force or effect.
4. Any waiver, alteration or modification of any of the terms of this Amendment or the Employment Agreement shall be valid only if made in writing and signed by the parties hereto.
5. This Amendment may be executed in counterparts, each of which shall constitute an original but all of which together shall constitute one and the same document. This Amendment, to the extent signed and delivered by facsimile or electronic means will be treated in all manner and respects as an original agreement or instrument and will be considered to have the same binding legal effect as if it were the original signed version thereof delivered in person.

*[Signature Page(s) to Follow]*

***[Signature Page(s) to Follow]***

IN WITNESS WHEREOF, the parties hereto have executed this Amendment effective as of the day and year first above written.

**ESKA CORPORATION**

**EMPLOYEE**

By: /s/ Kevin S. Wilson

By: /s/ Steven M. Asakowicz

Name: Kevin S. Wilson

Name: Steven M. Asakowicz

Title: Chief Executive Officer and President

Title: Executive Vice President, Companion Animal Sales

**AMENDMENT TO EMPLOYMENT AGREEMENT BETWEEN HESKA  
CORPORATION AND RODNEY A. LIPPINCOTT**

This Amendment to Employment Agreement is dated effective as of March 1, 2015 (this "Amendment") and amends the Employment Agreement dated as of February 22, 2013 (the "Employment Agreement"), between Heska Corporation, a Delaware corporation ("Company"), and Rodney A. Lippincott ("Employee"). Unless otherwise defined in herein, all capitalized terms used herein shall have the meaning ascribed to them in the Employment Agreement.

**RECITALS**

Section 13 of the Employment Agreement requires the parties to modify the Employment Agreement in writing and to reference such Section, and the Employee and Company have agreed to modify the Employment Agreement to the extent set forth in this Amendment.

**AGREEMENT**

NOW, THEREFORE, in consideration of the foregoing, and other good and valuable consideration, including Employee's continued employment with Company, the receipt and sufficiency of which are hereby acknowledged, Employee and Company hereby agree as follows:

1. The first sentence of Section 3(a) of the Employment Agreement, which reads, "**Base Salary.** Heska will pay Executive an annual salary of \$175,000 as compensation for Executive's services (the "**Base Salary**")", is deleted in its entirety and replaced with the following, "**Base Salary.** Heska will pay Executive an annual salary of \$262,500 as compensation for Executive's services (the "**Base Salary**")."
2. The last sentence of Section 3(b) of the Employment Agreement, which reads, "In addition, Executive will be eligible for variable performance commissions for successful sales revenue and margin achievement, targeted, to be earned under separate schedule, from between \$50,000 and \$125,000." is hereby deleted in its entirety.
3. All other terms and conditions of the Employment Agreement shall remain in full force and effect. This Amendment, together with the Employment Agreement, contains all the terms and conditions agreed upon by the parties hereto regarding the subject matter hereof and thereof. All prior agreements, promises, negotiations and representations, either oral or written, relating to the subject matter of this Amendment or the Employment Agreement not expressly set forth in this Amendment or the Employment Agreement are of no force or effect.
4. Any waiver, alteration or modification of any of the terms of this Amendment or the Employment Agreement shall be valid only if made in writing and signed by the parties hereto.
5. This Amendment may be executed in counterparts, each of which shall constitute an original but all of which together shall constitute one and the same document. This Amendment, to the extent signed and delivered by facsimile or electronic means will be treated in all manner and respects as an original agreement or instrument and will be considered to have the same binding legal effect as if it were the original signed version thereof delivered in person.

*[Signature Page(s) to Follow]*

IN WITNESS WHEREOF, the parties hereto have executed this Amendment effective as of the day and year first above written.

**HESKA CORPORATION**

**EMPLOYEE**

By: /s/ Kevin S. Wilson

By: /s/ Rodney A. Lippincott

Name: Kevin S. Wilson

Name: Rodney A. Lippincott

Title: Chief Executive Officer and President

Title: Executive Vice President, Companion Animal  
Sales

**SUBSIDIARIES OF COMPANY**

Diamond Animal Health, Inc., an Iowa corporation

Heska Imaging US, LLC, a Delaware Limited Liability Company (54.6% owned)

Heska AG, a corporation incorporated under the laws of Switzerland

Sensor Devices, Inc., a Wisconsin Corporation (inactive)



## CERTIFICATION

I, Kevin S. Wilson, certify that:

1. I have reviewed this annual report on Form 10-K of Heska Corporation;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal controls over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
  - a. Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
  - b. Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles; and
  - c. Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
  - d. Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
  - a. All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
  - b. Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Dated: March 24, 2015

/s/ Kevin S. Wilson  
KEVIN S. WILSON  
Chief Executive Officer and President  
(Principal Executive Officer)

**CERTIFICATION**

I, Jason A. Napolitano, certify that:

1. I have reviewed this annual report on Form 10-K of Heska Corporation;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal controls over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
  - a. Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
  - b. Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles; and
  - c. Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
  - d. Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
  - a. All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
  - b. Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Dated: March 24, 2015

/s/ Jason A. Napolitano

JASON A. NAPOLITANO

Executive Vice President and Chief Financial Officer

(Principal Financial Officer and Principal Accounting Officer)

CERTIFICATION OF CHIEF EXECUTIVE OFFICER AND CHIEF FINANCIAL OFFICER  
PURSUANT TO  
18 U.S.C. SECTION 1350,  
AS ADOPTED PURSUANT TO  
SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002

I, Kevin S. Wilson, certify, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that the Annual Report of Heska Corporation on Form 10-K for the year ended December 31, 2014 fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934 and that information contained in such Form 10-K fairly presents in all material respects the financial condition and results of operations of Heska Corporation.

Dated: March 24, 2015

By: /s/ Kevin S. Wilson  
Name: KEVIN S. WILSON  
Title: Chief Executive Officer and President

I, Jason A. Napolitano, certify, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that the Annual Report of Heska Corporation on Form 10-K for the year ended December 31, 2014 fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934 and that information contained in such Form 10-K fairly presents in all material respects the financial condition and results of operations of Heska Corporation.

Dated: March 24, 2015

By: /s/ Jason A. Napolitano  
Name: JASON A. NAPOLITANO  
Title: Executive Vice President and  
Chief Financial Officer

A signed original of this written statement required by Section 906 has been provided to Heska Corporation and will be retained by Heska Corporation and furnished to the Securities and Exchange Commission or its staff upon request.