OPTION CARE INC/DE
Form 10-K
March 16, 2006

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-K

x **ANNUAL REPORT PURSUANT TO SECTION 13 or 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**
FOR THE FISCAL YEAR ENDED DECEMBER 31, 2005

OR

o **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: 0-19878

OPTION CARE, INC.

(Exact name of registrant as specified in its charter)

DELAWARE	**36-3791193**
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)
485 Half Day Road, Suite 300 Buffalo Grove, IL	**60089**
(Address of principal executive offices)	(Zip Code)

Registrant s telephone number, including area code **(847) 465-2100**

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

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

Title of each class	**Name of each exchange on which registered**
Common Stock, $0.01 par value per share	National Association of Securities Dealers Automated Quotation (Nasdaq) National Market System

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

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

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 x No o

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

Form 10-K. x

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

Large accelerated filer o Accelerated filer x Non-accelerated filer o

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

As of June 30, 2005, the aggregate market value of the registrant s common stock held by non-affiliates of the registrant was $333,906,000 based on the closing sale price of $14.10 as reported on the Nasdaq National Market System. Solely for purposes of the foregoing calculation of aggregate market value of voting stock held by non-affiliates, the registrant has assumed that all directors and executive officers of the registrant are affiliates of the registrant. Such assumption shall not be deemed a determination by the registrant that such persons are affiliates of the registrant for any purposes.

The number of shares of our Common Stock, $0.01 par value per share, outstanding as of March 1, 2006 was 32,919,277.

DOCUMENTS INCORPORATED BY REFERENCE

Document	Parts Into Which Incorporated
Proxy Statement for the Annual Meeting of Stockholders to be held by April 30, 2006 (Proxy Statement)	Part III

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ANNUAL REPORT ON FORM 10-K
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FORWARD-LOOKING STATEMENTS

The Private Securities Litigation Reform Act of 1995 provides a safe harbor for forward-looking statements. Certain information included or incorporated by reference in this Annual Report on Form 10-K, including information in Item 7 Management s Discussion and Analysis of Financial Condition and Results of Operations and other materials filed or to be filed by us with the Securities and Exchange Commission (as well as information included in oral statements or other written statements made or to be made by us) contain, or may contain, statements that are or will be forward-looking, such as statements relating to acquisitions and other business development activities, future capital expenditures and the anticipated or potential effects of future regulation and competition, as well as other statements identified by may , should , expect and similar words. Such forward-looking information involves important risks and uncertainties that could significantly affect anticipated results in the future and, accordingly, such results may differ from those expressed in any forward-looking statements made by us, or on our behalf. These risks and uncertainties include, but are not limited to, uncertainties affecting our businesses and our franchisees relating to acquisitions and divestitures (including continuing obligations with respect to completed transactions), sales and renewals of franchises, government and regulatory policies (including federal, state and local efforts to reform the delivery of and payment for healthcare services), general economic conditions (including economic conditions affecting the healthcare industry in particular), the pricing and availability of goods and services, technological developments and changes in the competitive environment in which we operate, as well as those identified under Item 1A. Risk Factors in this Form 10-K. We do not undertake any obligation to release publicly any revisions to such forward-looking statements to reflect events or circumstances occurring after the date of this Annual Report or to reflect the occurrence of unanticipated events.

PART I

Item 1. BUSINESS

GENERAL

Option Care is a leading provider of home infusion pharmacy services and specialty pharmacy services to patients with acute or chronic conditions that can be treated at home, at one of our local ambulatory infusion centers or in a physician s office. We provide these services to patients on behalf of managed care organizations, government healthcare programs and biopharmaceutical manufacturers through two company-owned, high-volume distribution facilities, 53 company-owned and managed locations and 65 franchised locations throughout the United States. Our services include the distribution and administration of infused and injectible medications, patient care coordination, clinical and compliance management and reimbursement support. For the years ended December 31, 2005 and 2004, we generated net revenue of $506.4 million and $414.4 million, respectively, and net income of $22.7 million and $18.9 million, respectively.

We are a leading provider to managed care organizations and other third party payors, patients, physicians and pharmaceutical manufacturers with a cost-effective solution for both home infusion pharmacy services and specialty pharmacy services nationwide. Our combination of national and local distribution capabilities, our sales and marketing resources, and our clinical staff and information systems support our customers as follows:

- **Payors** We provide payors with a comprehensive approach to meeting their pharmacy services needs. Our provision of infusion pharmacy services in the patient s home or at one of our local ambulatory infusion centers offers a lower cost alternative to providing these therapies in a hospital setting. Our specialty pharmacy services offer payors a cost effective solution for the distribution of specialty pharmaceuticals directly to patients for self-administration. We also provide the direct distribution of biotech pharmaceuticals to physicians offices for in-office administration. This provides payors with a cost-effective alternative to direct billing of biotech pharmaceuticals by physicians. We also provide payors with utilization and outcomes data to evaluate therapy effectiveness.

- **Patients** We improve patients quality of life by allowing them to remain at home while receiving necessary medications, supplies and services or visit one of our ambulatory infusion centers to receive care. In addition, we help manage patients conditions through counseling and education regarding their treatment and by providing ongoing monitoring to encourage patient compliance with the prescribed therapy. We also provide services to help patients receive reimbursement benefits.

- **Physicians** We assist physicians with time-intensive patient support by providing care management related to their patients pharmacy needs and improving compliance with therapy protocols. We eliminate the need for physicians to carry inventories of high cost prescriptions by distributing the medications directly to patients homes or, if required, to the physicians offices. We either bill the payor directly or assist the patient in the submission of claims to the payor.

- **Pharmaceutical Manufacturers** We provide pharmaceutical manufacturers with a broad distribution channel for their existing pharmaceuticals and their new product launches. We implement patient monitoring programs that encourage compliance with the prescribed therapy. We also provide valuable clinical information in the form of outcomes and compliance data to manufacturers to aid in their evaluation of the efficacy of their products.

Our company was founded in 1979 and was a pioneer in the delivery of home infusion services. The industry was formed when the technology emerged allowing for the safe and cost-effective administration of infused medications in a home environment. In addition, Medicare reimbursement changes in 1984 encouraged hospitals to reduce length of stays creating increased discharges to alternate site settings. During the 1980 s, we expanded our services nationally with a franchise model targeting markets with populations of fewer than 300,000. We completed our initial public offering on April 23, 1992 and embarked on transitioning the company from a franchise organization to a healthcare services provider through an acquisition program targeting franchised and non-affiliated operations.

Since the mid-1990 s, we have focused on building a leadership position in the home infusion industry in markets of all sizes and have been able to leverage our local pharmacy capabilities to distribute niche, high cost therapies targeting chronic conditions. Due to the robust biotech pharmaceutical product pipeline, we have seen a significant increase in the distribution of these high cost specialty medications. As a result, we have created a specialized service offering that meets the needs of patients, product manufacturers and managed care organizations.

We are engaged in one reportable industry segment containing three service lines: specialty pharmacy, infusion and related healthcare services, and other. The following table presents summarized information about our revenue by service line for the years ended December 31, 2005, 2004 and 2003 (amounts in thousands):

	Years Ended December 31,					
	2005		**2004**		**2003**	
	Amounts	**% of Total**	**Amounts**	**% of Total**	**Amounts**	**% of Total**
Revenue:						
Specialty pharmacy	$ 290,884	57.5 %	$ 249,697	60.2 %	$ 208,557	58.7 %
Infusion and related healthcare services	198,679	39.2 %	153,302	37.0 %	136,192	38.3 %
Other	16,801	3.3 %	11,431	2.8 %	10,691	3.0 %
Total revenue	$ 506,364	100.0 %	$ 414,430	100.0 %	$ 355,440	100.0 %

AVAILABLE INFORMATION

We maintain our internet website at http://www.optioncare.com and make available free of charge through our internet website reports we file with the SEC, including our Annual Reports 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(c) or 15(d) of the Securities and Exchange Act of 1934, as soon as reasonably practical after we electronically file such materials with the SEC. Also available through our internet site is our Code of Ethics for our directors, officers and employees. Information on our website is not incorporated by reference into this report. Our common stock is traded on the Nasdaq National Market under the symbol OPTN.

We were incorporated in Delaware in July 1991. Our principal executive offices are located at 485 Half Day Road, Suite 300, Buffalo Grove, Illinois 60089, and our telephone number is (847) 465-2100.

INDUSTRY

Healthcare related expenditures constitute a large and growing segment of the US economy. According to estimates by the Centers for Medicare & Medicaid Services, national health expenditures reached an estimated $1.9 trillion in 2004, are expected to reach $2.2 trillion in 2006 and are projected to increase to $3.6 trillion by 2014. In 2003, prescription drug expenditures were $179 billion, representing 11% of national healthcare expenditures for that year. Prescription drugs remain among the fastest-growing categories of healthcare expenditure, having grown at double-digit rates each year from 1995 to 2003. Two important trends that impact our business have emerged in relation to healthcare spending. These trends are positively impacting the growth of the many services we provide:

- Government programs, private insurance companies, managed care organizations and self-insured employers have implemented various cost-containment measures to limit the growth of healthcare expenditures. These cost-containment measures, together with technological advances, have resulted in a shift in the delivery of many healthcare services away from traditional hospital settings to more cost-effective settings, including patients homes.

- As a result of the proliferation of biotech research and development, biotech companies and pharmaceuticals manufacturers have developed a variety of high cost biotech pharmaceuticals. These biotech pharmaceuticals are most often used in the treatment of chronic conditions such as multiple sclerosis, growth hormone disorders, hemophilia, cancer and immune deficiency disorders. These biotech pharmaceuticals, which in many cases cost over $10,000 per patient per year, are typically used on a recurring basis for extended periods of time and require special inventory handling, administration and patient compliance monitoring. Historically, traditional pharmacy distribution channels have not been designed to handle the additional services required by many of these medications.

Pharmacy Services

Pharmacy services include the treatment of a wide range of chronic and acute health conditions with a range of injectible and infusible specialty pharmaceuticals. Less acute, chronic conditions are generally treated with self-administered, injectible pharmaceuticals but may also be administered by a physician or nurse. These pharmaceuticals can be directly distributed to the patient or the patient s physician for in-office administration and in many cases cost over $10,000 per patient per year. These pharmaceuticals may require refrigeration during shipping as well as special handling to prevent potency degradation. Patients receiving treatment usually require special counseling and education regarding their condition and treatment programs. This segment of the pharmacy services industry primarily treats conditions such as multiple sclerosis, growth hormone disorders, hemophilia, cancer, immune deficiency disorders, asthma and other chronic conditions. Retail pharmacies and other traditional distributors generally are designed to carry inventories of low cost, high volume products and therefore are not equipped to handle the high cost, low volume specialty pharmaceuticals that have specialized handling and administration requirements. As a result, these specialty pharmaceuticals are generally provided by pharmacies that focus primarily on filling, labeling and delivering injectible pharmaceuticals and related support services.

IMS Health has estimated the U.S. market for specialty pharmaceuticals at nearly $38 billion and the market is growing rapidly. We expect several factors to contribute to the continuing growth of the specialty pharmacy services industry, including the following:

- Healthcare cost containment pressures;

- Development of new pharmaceuticals;

- Direct to consumer advertising;

- Increased acceptance of mail-order distribution; and

- Growing emphasis on care management and compliance monitoring to improve outcomes for these high-cost, chronic diseases.

More acute, chronic conditions are generally treated with infusible pharmaceuticals that require administration of a more complex nature. These pharmaceuticals are primarily administered to treat infections, dehydration, cancer, pain and nutritional deficiencies. Patients are generally referred to infusion pharmacy services providers by physicians, hospital discharge planners and case managers. The medications are mixed and dispensed under the supervision of a registered pharmacist and the therapy is typically delivered in the home of the patient by a registered nurse or trained caregiver. Depending on the preferences of the patient and/or the payor, these services may also be provided at an ambulatory infusion center. According to the National Home Infusion Association, the size of the home infusion pharmacy services industry is currently between $4 and $5 billion. We believe that several factors will contribute to the continuing growth in non-hospital based infusion therapy services, including the following:

- Healthcare cost containment pressures;

- Increased number of therapies that can be safely administered in patients homes;

- Patient preference for at-home treatment;

- Increased acceptance of home infusion by the medical community and by managed care organizations and other payors;

- Technological innovations such as implantable injection ports, vascular access devices and portable infusion control devices; and

- Increased utilization of home infusion therapies due to demographic trends, in particular increasing life expectancies.

GROWTH STRATEGY

We intend to leverage our 26 years of clinical experience managing a wide range of pharmaceutical therapies with the national coverage of our high-volume distribution facilities and local pharmacy locations to deliver a single source solution for infused and injected pharmaceuticals and services to our customers. Our ability to provide a flexible distribution model which includes the delivery of our cost effective services to patients homes, physicians offices or our local ambulatory infusion centers, makes us an attractive provider to government health plans, managed care organizations, insurance companies and other third party payors and referral sources.

We intend to increase our revenue and profitability through organic growth as well as selective acquisitions, start-ups and joint ventures that expand our geographic coverage into new markets and consolidate providers in existing markets that we serve.

- ***Organic Growth***

We intend to expand our infusion and specialty services through sales and marketing activities targeting managed care organizations, pharmaceutical manufacturers, and local referral sources.

- We currently have contracts with most major managed care organizations, which cover approximately 75 million lives, and are actively expanding the range of infusion and specialty services under these relationships. In addition, we are actively targeting new managed care relationships to contract for a wide variety of our services.

- Our pharmaceutical manufacturer strategy includes expanding our relationships with biotech and other pharmaceutical manufacturers in order to acquire distribution rights to existing and new products targeting chronic diseases or conditions.

- Our local sales force continuously markets to a wide variety of referral sources stressing our clinical capabilities to meet the needs of patients with a wide range of acute and chronic conditions.

- ***Acquisitions***

The home infusion industry is highly fragmented with the majority of service providers operating primarily in local or regional markets. Currently, there are approximately 4,000 home infusion providers operating in the United States 80% are small, individually owned or closely held operations while the remaining 20% include a variety of local and national providers that are either hospital affiliated or independent. We believe that few competitors possess the scale and resources to consolidate the industry and that our financial resources and operating strength affords us an advantage in this area. Additionally, our franchise network provides us with an established pipeline of potential acquisition opportunities. Our typical franchise agreement provides us with a right of first refusal for the potential acquisition of an existing franchise.

- ***Start-Ups***

We intend to open new pharmacies in the following types of markets:

- New markets with large and growing populations;

- Markets where our existing franchisees do not renew their franchise agreements with us; and

- Markets adjacent to areas we currently serve and which will allow us to leverage existing infrastructure and managed care relationships.

- ***Joint Ventures***

We intend to enter into joint ventures in select markets with established hospitals by merging with or partially acquiring a hospital system s home care business, or by contracting with a hospital system to jointly develop start-up operations. Hospital partners may include centers of academic excellence, regional hospitals and community hospitals.

OUR SERVICES

Home Infusion Pharmacy and Related Healthcare Services

We provide home infusion pharmacy services through our local pharmacy network of 53 company-owned and managed pharmacies throughout the United States. Our services are most typically provided in the patient s home, but may also be provided at clinics, the physician s office or at one of our ambulatory infusion centers. We offer patients and physicians the following products and services:

- Medication and supplies for administration and use at home or within one of our ambulatory infusion centers;

- Consultation and education regarding the patient s condition and the prescribed medication;

- Clinical monitoring and assistance in monitoring potential side effects; and

- Assistance in obtaining reimbursement.

We provide the following home infusion therapies:

- ***Total Parenteral Nutrition:*** intravenous therapy providing required nutrients to patients with digestive or gastro-intestinal problems, most of whom have chronic conditions requiring treatment for life;

- ***Anti-infective Therapy:*** intravenous therapy providing medication for infections related to diseases such as osteomyelitis and urinary tract infections;

- ***Pain Management:*** intravenous or continuous injection therapy, delivered by a pump, providing analgesic pharmaceuticals to reduce pain;

- ***Enteral Nutrition:*** providing nutritional formula by tube directly into the stomach or colon;

- ***Chemotherapy:*** intravenous therapy providing prescription medications to treat cancer; and

- ***Other therapies:*** treating a wide range of medical conditions.

Several of our company-owned pharmacies also provide home health nursing services, respiratory therapy services and home medical equipment sales and rentals. We also have one location that provides home hospice services.

Specialty Pharmacy Services

We provide specialty pharmacy services through our two company-owned, high-volume distribution facilities and our 53 company-owned and managed local pharmacies. We purchase specialty pharmaceuticals from manufacturers and wholesale distributors, fill prescriptions provided by physicians, and label, package and deliver the pharmaceuticals to patients homes or physicians offices, either ourselves or through contract couriers. Depending on therapy, we may also administer the specialty pharmaceuticals to the patient at one of our ambulatory infusion centers. Our approach to delivering specialty pharmacy services includes a manufacturer strategy and managed care strategy to meet the unique needs of each customer segment. For selected drugs, we also supply clinical efficacy and outcomes data to the manufacturers.

We provide specialty pharmacy services to treat the following chronic diseases or conditions:

- ***Growth Hormone Deficiency:*** a condition that prevents normal growth patterns in children, generally caused by disorders of the pituitary gland or kidneys. Therapy consists of daily injections of growth hormone and usually lasts seven to nine years.

- ***Respiratory Synctial Virus (RSV) Prevention:*** RSV is a major cause of respiratory disease in young children and infants. Treatment is directed toward high-risk pediatric patients, typically from infant to age two. The most common treatment consists of monthly injections of Synagis®, a specialty pharmaceutical we distribute, throughout the RSV season which lasts from approximately October through April.

The following table illustrates the seasonal impact of the sales of Synagis® on our quarterly revenues for 2005 and 2004 (amounts in thousands):

	2005				2004			
	Q4	Q3	Q2	Q1	Q4	Q3	Q2	Q1
Synagis® revenue	$ 15,905	$ 862	$ 4,492	$ 15,536	$ 9,455	$ 571	$ 3,955	$ 14,251
Percent of total revenue	11.0 %	0.7 %	3.8 %	12.9 %	8.4 %	0.6 %	4.0 %	13.8 %

- ***Hepatitis C Virus:*** a viral infection which results in the inflammation of the liver. Left untreated, hepatitis C virus can cause serious liver damage. Treatment includes injections of interferon alfa with the concomitant oral administration of ribavirin products. Treatment can last up to 24 months.

- ***Multiple Sclerosis:*** a chronic, incurable, progressive disease of the central nervous system. The goal of treatment is to decrease the severity, intensity and duration of outbreaks and to slow the progression of the disease. Treatment regimens involve pharmaceutical injections, and products vary widely.

- ***Hemophilia:*** an inherited bleeding disorder that is caused by a blood clotting deficiency that results in a longer bleeding time. Hemophilia is one of the most costly diseases to treat. The treatment goal is to raise the level of the deficient clotting factor and maintain it in order to stop the bleeding. Treatments include infusion of the clotting factor products. The length of treatment depends on the severity of the bleeding episode, and the need for treatment continues throughout the life of the patient.

- ***Immune Deficiency:*** immune deficiencies are disorders which reduce the patient s ability to identify and destroy substances which do not belong in the human body and are characterized by reduced levels of antibodies. Intravenous immune globulins, which are infused to treat the immune deficiencies, are concentrated antibodies that have been purified from large numbers of human blood donors.

- ***Cancer:*** includes a wide spectrum of tumors, abnormal growths and cellular abnormalities. Treatment includes radiation, chemotherapy and/or surgery. As a result of these treatments, patients may require therapies that combat anemia and increase white blood cell counts. Our specialty pharmacy programs provide chemothorapy and related products to physicians offices for in-office administration and to patients homes.

- ***Asthma:*** an inflammatory condition of the bronchial airways, most commonly caused by allergies. The inflammation leads to airway obstruction, chest tightness, coughing and wheezing. Treatment focuses on controlling symptoms and typically consists of inhaled corticosteroids. Our specialty pharmacy program provides patients with an injectible drug, Xolair®, designed for adults and adolescents with moderate to severe allergic asthma that is inadequately controlled by the use of inhaled corticosteroids.

OUR SUPPLIERS

We obtain the pharmaceuticals and medical supplies and equipment that we provide to our patients through pharmaceutical manufacturers, distributors and group purchasing organizations. Most of the pharmaceuticals that we purchase are available from multiple sources and are available in sufficient quantities to meet our needs and the needs of our patients. However, some biotech drugs are only available through the manufacturer and may be subject to limits on distribution. In such cases, it is important for us to establish and maintain good working relations with the manufacturer in order to assure sufficient supply to meet our patients needs. We utilize several national delivery companies as an important part of the local and national distribution of our products and services, particularly in the delivery of certain specialty pharmaceutical products.

Additionally, certain drugs may become subject to general supply shortages, as was the case in 2005 with IVIG immune globulin products. Such shortages can result in cost increases or hamper our ability to obtain sufficient quantities to meet the needs of our patients. We work diligently to obtain commitments from our suppliers, whenever possible, to secure ample supply of drugs that are potentially subject to supply shortages.

Through the coverage and clinical expertise of our two company-owned, high-volume distribution facilities, our 53 company-owned locations and our 65 franchised locations, we provide pharmaceutical manufacturers with a broad distribution channel for their existing pharmaceutical products. This strength also provides us the opportunity to become a selected partner in the launch of their new products. When providing new products to patients, we implement a monitoring program to encourage compliance with the prescribed therapy and we provide valuable clinical information to the manufacturer in the form of outcomes and compliance data to aid in their evaluation of the efficacy of the product. We may receive fees, which we record as other revenue, from certain biotech manufacturers for providing them with clinical outcomes data. Our continued growth will be dependent on maintaining our existing relationships with manufacturers and establishing new relationships with additional manufacturers as they launch new specialty products.

Through the combined purchasing power of our company-owned and franchised locations, we are able to sign pharmaceutical purchase contracts with these supplies that provide us and our franchisees with volume discount pricing and provide us the opportunity to earn volume purchase rebates and vendor administration fees. Such fees are recorded as reductions to cost of goods sold to the extent they are earned by purchases made by our company-owned locations and as revenue to the extent that they are related to purchases made by our franchised locations, with the majority of these fees being derived from purchases made by our company-owned locations.

BILLING & SIGNIFICANT PAYORS

We derive most of our revenue from contracts with third party payors, such as managed care organizations, insurance companies, self-insured employers and Medicare and Medicaid programs. Where permissible, we bill patients for any amounts not reimbursed by third party payors. For the most part, our infusion pharmacy revenue consists of reimbursement for both the cost of the pharmaceuticals sold and the cost of services provided. Pharmaceuticals are typically reimbursed on a percentage discount from the published average wholesale price (AWP) of each drug. Nursing services are typically paid separately, on a per visit basis, while other patient support services and ancillary medical supplies are either reimbursed separately or on a per diem basis, where applicable. Specialty pharmaceuticals are typically pre-packaged drugs that are self-injected by the patient or a trained in-home caregiver. Therefore, minimal service is provided and no per diem revenue is generated.

Our principal managed care contract is with Blue Cross and Blue Shield of Florida, Inc. (BC/BS of Florida). We provide infusion pharmacy and specialty pharmacy services to BC/BS of Florida members throughout the state of Florida. This contract renews each September for an additional one-year term and may be terminated by either party upon 90 days notice. For 2005, our contract with BC/BS of Florida produced $68.0 million in revenue. In 2005, 2004 and 2003, respectively, approximately 13%, 15% and 17% of our total revenue was related to this contract. As of December 31, 2005 and 2004, approximately 9% and 7% of Option Care s accounts receivable were due from BC/BS of Florida. No other single managed care payor represents more than 10% of our revenue.

We also provide services that are reimbursable through government healthcare programs such as Medicare and state Medicaid programs. For the twelve months ended December 31, 2005, 2004 and 2003, respectively, approximately 17%, 18% and 18% of our revenue came from government healthcare programs such as Medicare and Medicaid. The amounts due from these programs represented approximately 22% and 18% of our total accounts receivable, respectively, as of December 31, 2005 and 2004.

We bill payors and track all of our accounts receivable through computerized billing systems. These systems allow our billing staff the flexibility to review and edit claims in the system before they are submitted to payors. Claims are submitted to payors either electronically or through the mail. We utilize

electronic claim submission whenever possible to expedite claim review and payment, and to minimize errors and omissions.

The net revenue that we report is based on usual and customary billing rates for the products and services we provide, less applicable contractual adjustments. In most cases, our computerized billing systems generate contractual adjustments based on the fee schedules of the underlying insurance contracts when the claims are billed. If our computerized billing systems cannot automatically generate the contractual adjustment for a given claim, we calculate the contractual adjustment manually and key the adjustment into our billing system when the claim is billed. For revenue that is not yet billed, we estimate the contractual adjustments using a claim-by-claim analysis of the unbilled charges, by applying historic contractual adjustment percentages, or a combination of the two methods.

We generate accounts receivable aging reports from our billing systems and utilize these reports to help us monitor the condition of our outstanding receivables and evaluate the performance of our billing and reimbursement staff. We also utilize these aging reports, combined with historic write-off statistics generated from our billing systems, to determine our allowance for doubtful accounts.

Our financial performance is highly dependent upon effective billing and collection practices at each of our company-owned pharmacies. The process begins with an accurate and complete patient admission process, in which all critical information about the patient, the patient s insurance and their care needs is gathered. A critical part of this process is verification of insurance coverage and authorization from insurance to provide the required care, which typically takes place before we initiate services. An exception occurs when a patient referral is received outside of normal business hours, but we have an existing contractual relationship with the patient s insurance carrier. In such cases, we provide the patient with sufficient drugs and services to last until the next business day, when the patient s insurance coverage can be verified.

FRANCHISE PROGRAM

Our franchise program was developed to increase our geographical presence and to provide a national network of pharmacies to service the needs of our managed care customers without requiring extensive capital expenditures. In marketing our franchise program, we target independent infusion pharmacies that would benefit from participating in our national and regional managed care and manufacturer contracts as well as in our marketing programs. Our franchised locations are sold a license to operate an Option Care branded pharmacy in a defined territory to provide infusion therapy and related products and services.

We receive a start-up fee upon execution of the franchise agreement with subsequent royalties based on a percentage of gross receipts of the franchised location. Each franchisee is required to maintain a licensed pharmacy equipped to compound medications in a sterile environment as prescribed by physicians. In the program that we are currently marketing, the franchisee must obtain specified liability insurance protecting the franchise owner and us against claims arising from the operation of the franchised business. Our franchisees may participate in our managed care and manufacturer contracts. They may also purchase pharmaceuticals and supplies from a preferred list of vendors under contract with us. This frequently allows us and the franchisee to obtain volume discount pricing. For certain pharmaceuticals, the franchise may also purchase directly from us. Most of our franchise agreements also provide us with a right of first refusal for the potential acquisition of the franchise. However, none of our current agreements grants us the option to purchase the franchise at our will.

As of December 31, 2005, we had 65 franchised pharmacy locations operating under 52 separate franchise agreements. Approximately 62% of our franchise agreements come up for renewal in the four-year period from 2006 through 2009. As a franchise agreement nears expiration, we expect to propose a new agreement or evaluate the franchise for possible acquisition. If we cannot reach agreement with the franchisee and the franchise expires, the franchisee is required to cease using the Option Care service

mark and will not be able to access our managed care agreements or purchasing contracts. We would then be free to re-franchise the territory or to service the territory with a company-owned facility. Termination of a franchise agreement by the franchise prior to its scheduled expiration date may subject the franchisee to early termination fees. Accordingly, we may record revenue as a result of such early terminations. In addition, upon our acquisition of an existing franchise prior to the scheduled expiration of its underlying franchise agreement, we may record a gain or loss on settlement equal to the excess or shortfall of the present value of the estimated future royalties receivable under the terminated franchise agreement versus our current royalty market rates.

The following table summarizes the termination dates of our franchise agreements, by year, and presents the amount and percentage of our 2005 royalty revenue attributable to franchises terminating in each year as well as to franchises that were acquired or terminated from the network during 2005 (dollar amounts in thousands):

Year ended December 31,	Number of Franchise Agreements expiring	Attributable 2005 Royalty Revenue	Percent of 2005 Royalty Revenue
2006	8	$ 677	9.5 %
2007	6	831	11.7 %
2008	9	976	13.8 %
2009	9	1,216	17.1 %
2010	5	558	7.9 %
2011	7	864	12.2 %
2012-2017	8	700	9.9 %
Total continuing agreements	52	5,822	82.1 %
Terminated during 2005(1)	6	606	8.5 %
Acquired during 2005(1)	6	667	9.4 %
Total all agreements	64	$ 7,095	100.0 %

(1) For comparative purposes, the 2004 royalty revenue attributable to franchise locations that were terminated and acquired during 2005 was $2,017 representing 24.9% of 2004 total royalty revenue.

DISPOSAL OF ASSETS

For the past decade, our subsidiary, Management by Information, Inc. (MBI), has developed and licensed proprietary software systems designed to manage the intake, dispensing, clinical, billing and collection processes for home infusion pharmacies. During the quarter ended December 31, 2005, we completed the sale of MBI and its existing software products, including iEmphsys , to Definitive Homecare Solutions, Ltd., which specializes in infusion pharmacy management software.

We have retained the right to utilize and develop our customized version of the iEmphsys product as well as MBI s older DOS-based product. We have retained and redeployed certain of MBI s employees to help maintain our version of these products. Upon our sale of MBI, we wrote off that portion of the iEmphsys development costs that related to the standard product that was sold to Definitive Homecare Solutions, Ltd., while we will continue to capitalize and amortize past and continuing costs related to development of our customized version. We do not expect the sale of MBI to have a material affect on our future revenue or results of operations.

SALES AND MARKETING

Our sales and marketing efforts focus on three primary objectives: (1) building new relationships and expanding existing contracts with managed care organizations; (2) establishing, maintaining and strengthening relationships with local and regional patient referral sources; and (3) maintaining existing

and developing new relationships with biotech drug manufacturers to gain distribution access as they release new products. Our national and regional sales directors focus primarily on establishing and expanding our contracts with managed care organizations, while our local account managers focus on pull-through from these contracts by developing and maintaining relationships with local and regional referral sources, such as physicians, hospital discharge planners and case managers. In addition, we have a sales force focused on maintaining and expanding our relationships with biotech drug manufacturers to establish our position as a participating provider when they release new products.

Most new patients are referred to us by physicians, medical groups, hospital discharge planners, case managers employed by Health Maintenance Organizations (HMOs), Preferred Provider Organizations (PPOs) or other managed care organizations, insurance companies and home care agencies. Our sales force is responsible for establishing and maintaining these referral relationships.

Our sales structure allows us to take advantage of our national managed care relationships to provide sales and contract pull-through by our local field-based sales personnel. Additionally, the existence of our contracts with national managed care organizations provides our local sales personnel with more flexibility and leverage for sales in local markets. This cross-utility enables us to market our services to numerous sources of patient referrals, including physicians, hospital discharge planners, hospital personnel, HMOs, PPOs or other managed care organizations, and insurance companies. Local marketing focuses on our infusion pharmacy business and our care management programs, with an emphasis on certain key therapies.

COMPETITION

Our pharmacies compete in the large and highly fragmented home infusion and specialty pharmacy markets. We compete with others for contracts with managed care organizations and other third party payors and compete to receive referrals from physicians, case managers and hospital discharge planners. Competition in the home infusion market is based on quality of care, cost of service and reputation. Competition in the specialty pharmacy market is based on price, reliability of service, compliance programs and reputation. Some of our existing and potential competitors in the home infusion market include integrated home healthcare providers such as Apria Healthcare Group Inc. and Coram Healthcare Corporation, and local providers of alternate site healthcare services such as hospitals, local home health agencies and other local providers. In the specialty pharmacy market, our existing and potential competitors include specialty pharmacy providers such as Medco Health Solutions, Caremark Rx, Express Scripts, Curative Health Services and others, specialized retail pharmacies such as PharmaCare, a division of CVS Corporation, pharmacy benefit management companies, wholesalers and retail pharmacies. In each market, some of these current competitors have, and our potential future competitors may have, greater financial, operational, sales and marketing resources than us. However, we believe that our reputation for providing quality services, the strength of our growing national presence and our ability to effectively market our services at national, regional and local levels places us in a strong position against existing and potential competitors.

GOVERNMENTAL REGULATION

The healthcare industry is subject to extensive regulation by a number of governmental entities at the federal, state and local level. The industry is also subject to frequent regulatory change. Laws and regulations in the healthcare industry are extremely complex and, in many instances, the industry does not have the benefit of significant regulatory or judicial interpretation. Moreover, our business is impacted not only by those laws and regulations that are directly applicable to us but also by certain laws and regulations that are applicable to our managed care and other clients. If we fail to comply with the laws and regulations directly applicable to our business, we could suffer civil and/or criminal penalties, and we could

be excluded from participating in Medicare, Medicaid and other federal and state healthcare programs, which would have an adverse impact on our business.

If our franchisees fail to comply with the laws and regulations applicable to their businesses, they could suffer civil and/or criminal penalties and/or be excluded from participating in Medicare, Medicaid and other federal and state healthcare programs, which could have an adverse impact on our business.

Professional Licensure. Nurses, pharmacists and certain other healthcare professionals employed by us are required to be individually licensed or certified under applicable state law. We perform criminal and other background checks on employees and take steps to ensure that our employees possess all necessary licenses and certifications, and we believe that our employees comply in all material respects with applicable licensure laws.

Each of our franchisees is responsible for ensuring the licensing or certification of its employees in accordance with applicable law, performing any criminal or other background checks required by state law, and ensuring that all employees perform only those tasks which fall within their authorized scope of practice. While each franchisee is responsible for any failure or non-compliance with respect to these licensure and scope of practice issues, any such failure or non-compliance by a franchisee that impacts such franchisee s operations could have an adverse effect on our business.

Pharmacy Licensing and Registration. State laws require that each of our pharmacy locations be licensed as an in-state pharmacy to dispense pharmaceuticals in that state. Certain states also require that our pharmacy locations be licensed as an out-of-state pharmacy if we deliver prescription pharmaceuticals into those states from locations outside of the state. We believe that we substantially comply with all state licensing laws applicable to our business. If we are unable to maintain our licenses or if states place burdensome restrictions or limitations on non-resident pharmacies, our ability to operate in some states would be limited, which could have an adverse impact on our business.

Laws enforced by the Drug Enforcement Administration, as well as some similar state agencies, require our pharmacy locations to individually register in order to handle controlled substances, including prescription pharmaceuticals. A separate registration is required at each principal place of business where we dispense controlled substances. Federal and state laws also require that we follow specific labeling, reporting and record-keeping requirements for controlled substances. We maintain federal and state controlled substance registrations for each of our facilities that require such registration and follow procedures intended to comply with all applicable federal and state requirements regarding controlled substances.

Many states in which we operate also require home infusion companies to be licensed as home health agencies. We believe we are in compliance with these laws, as applicable.

Food, Drug and Cosmetic Act. Certain provisions of the federal Food, Drug and Cosmetic Act govern the handling and distribution of pharmaceutical products. This law exempts many pharmaceuticals and medical devices from federal labeling and packaging requirements as long as they are not adulterated or misbranded and are dispensed in accordance with and pursuant to a valid prescription. We believe that we comply with all applicable requirements.

Fraud and Abuse Laws Anti-Kickback Statute. The federal Anti-Kickback Statute prohibits individuals and entities from knowingly and willfully paying, offering, receiving, or soliciting money or anything else of value in order to induce the referral of patients or to induce a person to purchase, lease, order, arrange for, or recommend services or goods covered by Medicare, Medicaid, or other government healthcare programs. The federal courts have held that an arrangement violates the Anti-Kickback Statute if any one purpose of the remuneration is to induce the referral of patients covered by the Medicare or Medicaid programs, even if another purpose of the payment is to compensate an individual for rendered services. The Anti-Kickback Statute is broad and potentially covers many standard business arrangements.

Violations can lead to significant penalties, including criminal fines of up to $25,000 per violation and/or five years imprisonment, civil monetary penalties of up to $50,000 per violation plus treble damages, and/or exclusion from participation in Medicare, Medicaid, and other federal government healthcare programs. In an effort to clarify the conduct prohibited by the Anti-Kickback Statute, the Office of the Inspector General (OIG) of the United States Department of Health and Human Services has published regulations that identify a limited number of safe harbors. Business arrangements that satisfy all of the elements of a safe harbor are immune from criminal enforcement or civil administrative actions. The Anti-Kickback Statute is an intent based statute and the failure of a business relationship to satisfy all of the elements of a safe harbor does not in and of itself mean that the business relationship violates the Anti-Kickback Statute. The OIG, in its commentary to the safe harbor regulations, has recognized that many business arrangements that do not satisfy a safe harbor nonetheless operate without the type of abuses the Anti-Kickback Statute is designed to prevent. We attempt to structure our business relationships to satisfy an applicable safe harbor. However, in those situations where a business relationship does not fully satisfy the elements of a safe harbor, or where no safe harbor exists, we attempt to satisfy as many elements of an applicable safe harbor as possible. The OIG is authorized to issue advisory opinions regarding the interpretation and applicability of the Anti-Kickback Statute, including whether an activity constitutes grounds for the imposition of civil or criminal sanctions. We have not, however, sought any opinions regarding our business relationships.

A number of states have statutes and regulations that prohibit the same general types of conduct as those prohibited by the Anti-Kickback Statute described above. Some state anti-fraud and anti-kickback laws apply only to goods and services covered by Medicaid. Other state anti-fraud and anti-kickback laws apply to all healthcare goods and services, regardless of whether the source of payment is governmental or private. Where applicable, we attempt to structure our business relationships to comply with these statutes.

Fraud and Abuse Laws False Claims Act. We are subject to state and federal laws that govern the submission of claims for reimbursement. These laws generally prohibit an individual or entity from knowingly and willfully presenting a claim or causing a claim to be presented for payment from a federal healthcare program that is false or fraudulent. The standard for knowing and willful may include conduct that amounts to a reckless disregard for the accuracy of information presented to payors. Penalties under these statutes include substantial civil and criminal fines, exclusion from the Medicare or Medicaid programs and imprisonment. One of the most prominent of these laws is the federal False Claims Act, which may be enforced by the federal government directly or by a private plaintiff by filing a *qui tam* lawsuit on the government s behalf. Under the False Claims Act, the government and private plaintiffs, if any, may recover monetary penalties in the amount of $5,500 to $11,000 per false claim, as well as an amount equal to three times the amount of damages sustained by the government as a result of the false claim. A number of states, including states in which we operate, have adopted their own false claims statutes as well as statutes that allow individuals to bring *qui tam* actions. We believe that we have procedures in place to ensure the accuracy of our claims.

Ethics in Patient Referrals Law (Stark Law). The federal Stark Law generally prohibits a physician from making referrals for certain Designated Health Services (DHS), reimbursable by Medicare or Medicaid, to entities with which the physician or an immediate family member has a financial relationship, unless an exception applies. A financial relationship is generally defined as an ownership, investment or compensation relationship. DHS include, but are not limited to, outpatient pharmaceuticals, parenteral and enteral nutrition products, home health services, durable medical equipment, physical and occupational therapy services, and inpatient and outpatient hospital services. Among other sanctions, a civil monetary penalty of up to $15,000 may be imposed for each bill or claim for a service a person knows or should know is for a service for which payment may not be made due to the Stark Law. Such persons or entities are also subject to exclusion from the Medicare and Medicaid programs. Any person or entity participating in a circumvention scheme to avoid the referral prohibitions is liable for a civil monetary

penalty of up to $100,000. A $10,000 fine may be imposed for failure to comply with reporting requirements regarding an entity s ownership, investment and compensation arrangements for each day for which reporting is required to have been made under the Stark Law.

The Stark Law exempts certain business relationships that meet its exception requirements. However, unlike the Anti-Kickback Statute under which an activity may fall outside a safe harbor and still be lawful, a referral for DHS that does not fall within an exception is strictly prohibited by the Stark Law. We attempt to structure all of our relationships with physicians who make referrals to us in compliance with an applicable exception to the Stark Law.

In addition to the Stark Law, many of the states in which we and our franchisees operate have comparable restrictions on the ability of physicians to refer patients for certain services to entities with which they have a financial relationship. Certain of these state statutes mirror the Stark Law while others may be more restrictive. We attempt to structure all of our business relationships with physicians to comply with any applicable state self-referral laws.

Health Insurance Portability and Accountability Act of 1996 (HIPAA). To improve the efficiency and effectiveness of the healthcare system, the Health Insurance Portability and Accountability Act of 1996, Public Law 104-191, included Administrative Simplification provisions that required the Department of Health and Human Services (HHS) to adopt national standards for electronic health care transactions. At the same time, Congress recognized that advances in electronic technology could erode the privacy of health information. Consequently, Congress incorporated provisions into HIPAA that mandated the adoption of federal privacy protections for individually identifiable health information.

In response to the HIPAA mandate, in December 2000, HHS published a final regulation in the form of the Privacy Rule, which became effective on April 14, 2001. This Privacy Rule set national standards for the protection of health information, as applied to the three types of covered entities: health plans, health care clearinghouses, and health care providers who conduct certain health care transactions electronically. Pursuant to the Privacy Rule, covered entities are required to have standards in place to protect and guard against the misuse of individually identifiable health information.

The Privacy Rule establishes a foundation of federal protections for the privacy of protected health information. The Privacy Rule does not replace federal, state, or other laws that grant individuals even greater privacy protections, and covered entities are free to retain or adopt more protective policies or practices. We have implemented the standards set forth in the Privacy Rule, and believe that we and all of our franchisees are in compliance with the Privacy Rule or any more stringent federal or state laws relating to privacy.

Additionally, the Administrative Simplification provisions address electronic health care transactions and the security of electronic health information systems. Providers are required to comply with the standards by specific compliance dates established by HHS. For standards relating to electronic health care transactions, all providers were required to comply by October 16, 2003. The security standards applicable to individually identifiable health information maintained electronically were required to be implemented by April 21, 2005. We were materially compliant with these standards by the applicable compliance date. The standards for a unique national health identifier for providers used in connection with the electronic healthcare transactions must be implemented by May 23, 2007. We expect to be able to materially comply with this requirement by the applicable compliance date.

Penalties for non-compliance with the Privacy Rule and other HIPAA Administrative Simplification provisions range from a civil penalty of $100 for each violation (which can total up to $25,000 per person per year), to criminal penalties, including up to $50,000 and/or one year imprisonment, up to $100,000 and/or five years imprisonment if the offense is committed under false pretenses and up to $250,000 and/or

ten years imprisonment for violating a standard with the intent to sell, transfer or use individually identifiable health information for commercial advantage, personal gain or malicious harm.

In addition to regulating privacy of individual health information and other provisions relating to Administrative Simplification, HIPAA includes several anti-fraud and abuse laws, extends criminal penalties to private health care benefit programs and, in addition to Medicare and Medicaid, to other federal health care programs, and expands the Office of Inspector General s authority to exclude persons and entities from participating in the Medicare and Medicaid programs.

Medicare Prescription Drug, Improvement and Modernization Act of 2003. The Medicare Prescription Drug, Improvement and Modernization Act of 2003 regulates the manner in which covered outpatient drugs are reimbursed by the Medicare program, which could result in lower reimbursement for physicians. A small portion of the infusion drugs we provide are covered under Medicare s durable medical equipment (DME) benefit. The payment rates for drugs and services administered by us in this manner generally were not affected by the enacted legislation and will continue to be 95% of the AWP in effect as of October 1, 2003.

As part of the Medicare Prescription Drug, Improvement and Modernization Act of 2003, a prescription drug benefit has been added under Medicare Part D. Under the Part D final regulations, the ingredient costs and dispensing fees associated with the provision of home infusion therapies will now be covered under Medicare. Prior to the passage of this Act, no reimbursement of these costs was available through Medicare to beneficiaries. For eligible Medicare beneficiaries, the cost of equipment, supplies and professional services associated with infused covered Part D drugs will continue to be reimbursed under Part A or Part B, as applicable. For beneficiaries who are dually eligible for benefit under Medicare and a state Medicaid program, covered infused drugs will be reimbursed under individual state coverage guidelines.

Franchise Regulation. We are subject to regulations adopted by the Federal Trade Commission (FTC), and to certain state laws that regulate the offer and sale of franchises. The FTC Franchise Rule (Disclosure Requirements and Prohibitions Concerning Franchising and Business Opportunity Ventures) and certain state laws require that we furnish prospective franchise owners with a Uniform Franchise Offering Circular (UFOC) containing information prescribed by the FTC Franchise Rule and applicable state laws and regulations. There are certain states that also regulate the offer and sale of franchises and, in almost all cases, require registration of the UFOC with state authorities.

We are also subject to a number of state laws that regulate some substantive aspects of the franchisor-franchisee relationship. These laws may limit a franchisor s ability to:

- terminate or not renew a franchise without good cause;
- interfere with the right of free association among franchise owners;
- disapprove the transfer of a franchise;
- discriminate among franchisees regarding charges, royalties and other fees; and
- place new facilities near existing franchisees.

These laws also may limit the duration and scope of non-competition provisions. To date, these laws have not precluded us from seeking franchisees in any given area and have not had a material adverse effect on our operations.

Although bills intended to regulate certain aspects of franchise relationships have been introduced into Congress on several occasions, none have been enacted. We are not aware of any pending franchise legislation that in our view is likely to significantly affect our operations. We believe that our operations comply substantially with the FTC Franchise Rule and applicable state franchise laws.

SERVICE MARKS

We have registered with the federal government OPTION CARE® and OptionMed®, among others, as service marks. We believe that Option Care is becoming increasingly recognized by many referral sources as representing a reliable, cost-effective source of pharmacy services.

INSURANCE

Our business of providing specialized pharmacy services and other related home healthcare services may subject us to litigation and liability for damages. We currently maintain insurance for general and professional liability claims in the amount of $1 million per claim and $3 million in aggregate per policy year, plus $5 million in umbrella coverage. Accordingly, the maximum coverage for a first claim in any policy year is $6 million, and the maximum aggregate coverage for all claims in a policy year is $8 million. We also require each franchisee to maintain general liability and professional liability insurance covering both the franchise and us, at coverage levels that we believe to be sufficient. These policies provide coverage on a claims-made or occurrence basis and have certain exclusions from coverage. These insurance policies generally must be renewed annually. There can be no assurance that our insurance coverage will be adequate to cover liability claims that may be asserted against us.

In addition, we carry property insurance coverage for the value of the physical assets, including drugs inventory, at all of our leased facilities. The deductible on our property policies is $10,000 per claim, with higher deductibles applicable to certain other losses, such as wind and flood damage. These policies, which generally must be renewed annually, also include coverage for business interruption. While we believe our coverage to be sufficient, there can be no assurance that our property insurance coverage will be adequate to cover any and all property losses that we may suffer.

EMPLOYEES

As of December 31, 2005, we employed 1,781 persons on a full-time basis and 808 persons on a part-time basis. Of our full-time employees, 132 were corporate management and administrative personnel and the remaining 1,649 were employees of company-owned locations, primarily in clinical, management and administrative positions. The majority of our part-time employees are clinicians due to the nature and timing of the services we provide.

A group of 24 nurses working at our home health agency in Portland, Oregon are covered by a collective bargaining agreement. No other group of our employees is covered by a collective bargaining agreement. We believe our employee relations are good.

Item 1A. RISK FACTORS

You should carefully consider the risks and uncertainties we describe below, together with all of the other information contained in this Annual Report on Form 10-K and our other filings with the Securities and Exchange Commission. Some of the following factors relate principally to our business and the industry in which we operate. Other factors relate principally to an investment in our common stock. (The risks and uncertainties described below are not the only risks and uncertainties that could develop. Other risks and uncertainties that we have not predicted or evaluated could also adversely affect our company.) If any of the following risks occur, our earnings, financial condition or business could be materially harmed, the trading price of our common stock could decline, and you could lose all or part of your investment.

Our revenue and profitability will decline if the pharmaceutical industry undergoes certain changes, including limiting or discontinuing research, development, production and marketing of the pharmaceuticals that are compatible with the services we provide.

Our business is highly dependent on the ability of biotech and other pharmaceutical companies to develop, supply and market pharmaceuticals that are compatible with the services we provide. Our revenue and profitability will decline if those companies were to sell pharmaceuticals directly to the public, fail to support existing pharmaceuticals or develop new pharmaceuticals with different administration requirements than our service offerings are currently equipped to handle. Our business could also be harmed if the pharmaceutical industry experiences any of the following developments:

- supply shortages;
- pharmaceutical recalls;
- an inability to finance product development because of capital shortages;
- a decline in product research, development or marketing;
- a reduction in the retail price of pharmaceuticals;
- changes in the FDA approval process; or
- government or private initiatives that alter how pharmaceutical manufacturers, health care providers or pharmacies promote or sell products and services.

If we lose relationships with managed care organizations and other non-governmental third party payors, we could lose access to a significant number of patients and our revenue and profitability could decline.

We are highly dependent on reimbursement from managed care organizations and other non-governmental third party payors. For the fiscal years ended December 31, 2005, 2004 and 2003, respectively, 83%, 82% and 82% of our revenue came from managed care organizations and other non-governmental payors, including self-pay patients. Many payors seek to limit the number of providers that supply pharmaceuticals to their enrollees in order to build volume that justifies their discounted pricing. From time to time, payors with whom we have relationships require that we bid against our competitors to keep their business. As a result of such bidding process, we may not be retained, and even if we are retained, the prices at which we are able to retain the business may be reduced. The loss of a payor relationship could significantly reduce the number of patients we serve and have a material adverse effect on our revenue and net income, and a reduction in pricing could reduce our gross margins and our net income.

The loss of our contract with Blue Cross and Blue Shield of Florida would materially decrease our revenue.

Our principal managed care contract is with Blue Cross and Blue Shield of Florida, Inc. For the fiscal years ended December 31, 2005, 2004 and 2003, respectively, 13%, 15% and 17% of our revenue was related to this contract. The contract is terminable by either party on 90 days notice and, unless terminated, renews annually each September for an additional one-year term. The loss of this contract, or a material reduction in our pricing or pharmaceutical sales under this contract, would materially decrease our revenue and net income.

Changes in reimbursement rates from Medicare and Medicaid for the services we provide may cause our revenue and profitability to decline.

For the fiscal years ended December 31, 2005, 2004 and 2003, respectively, 17%, 18% and 18% of our revenue came from reimbursement by federal and state programs such as Medicare and Medicaid. Reimbursement from these and other government programs is subject to statutory and regulatory requirements, administrative rulings, interpretations of policy, implementation of reimbursement procedures, retroactive payment adjustments, governmental funding restrictions and changes to or new legislation, all of which may materially affect the amount and timing of reimbursement payments to us. Changes to the way Medicare pays for our services may reduce our revenue and profitability on services provided to Medicare patients and increase our working capital requirements.

In addition, we are sensitive to possible changes in state Medicaid programs as we do business with a number of state Medicaid providers. Budgetary concerns in many states have resulted in and may continue to result in, reductions to Medicaid reimbursement as well as delays in payment of outstanding claims. Any reductions to or delays in collecting amounts reimbursable by state Medicaid programs for our products or services, or changes in regulations governing such reimbursements, could cause our revenue and profitability to decline and increase our working capital requirements.

Our actual financial results might vary from our publicly disclosed results and forecasts.

Our actual financial results might vary from those anticipated by us, and these variations could be material. From time to time we publicly provide earnings guidance. Our forecasts reflect numerous assumptions concerning our expected performance, as well as other factors, which are beyond our control, and which might not turn out to be correct. Although we believe that the assumptions underlying our projections are reasonable, actual results could be materially different. Our financial results are subject to numerous risks and uncertainties and estimates, including those identified throughout these Risk Factors and elsewhere in this report and the documents incorporated by reference.

Our gross profit could decrease if there are changes in the calculation of Average Wholesale Price (AWP) for the pharmaceuticals we sell, or if managed care organizations and other private payors replace Average Wholesale Price with a different reimbursement system, such as Average Sales Price (ASP).

Our gross margin rates and our gross profit are largely controlled by our ability to purchase pharmaceutical products at discounted prices and to negotiate profitable managed care contracts. In many cases, we purchase pharmaceuticals at less than the published AWP for those pharmaceuticals. The AWP has been a standard form of pricing often used in the healthcare industry to determine discount and reimbursement amounts. Accordingly, we have contracted with a number of private payors, primarily managed care providers, to sell pharmaceuticals at AWP or at a percentage discount off of the AWP. AWP for most pharmaceuticals is compiled and published by private companies, including First DataBank, Inc. A reduction in AWP for the products we provide to patients could reduce our revenue and narrow our gross margins.

Some managed care providers are adopting ASP as the standard measure for determining reimbursement rates in new or renegotiated contracts. ASP-based pricing is generally lower than AWP-based pricing. To the extent that we are not able to negotiate new ASP-based contracts with managed care providers that contain gross profit margins comparable to our existing AWP-based contracts, our revenue and gross profit may be reduced.

We are subject to pricing pressures and other risks involved with third party payors.

Competition for patients, efforts by traditional third party payors to contain or reduce healthcare costs, and the increasing influence of managed care payors such as health maintenance organizations, has resulted in reduced rates of reimbursement for home infusion and specialty pharmacy services. Changes in reimbursement policies of governmental third party payors, including policies relating to Medicare, Medicaid and other federal and state funded programs, could reduce the amounts reimbursed to our customers for our products and, in turn, the amount these customers would be willing to pay for our products and services, or could directly reduce the amounts payable to us by such payors. Pricing pressures by third party payors may continue, and these trends may adversely affect our business.

Also, continued growth in managed care plans has pressured healthcare providers to find ways of becoming more cost competitive. Managed care organizations have grown substantially in terms of the percentage of the population they cover and in terms of the portion of the healthcare economy they control. Managed care organizations have continued to consolidate to enhance their ability to influence the delivery of healthcare services and to exert pressure to control healthcare costs. A rapid concentration of revenue derived from individual managed care payors could harm our business.

If we do not adequately respond to competitive pressures, demand for our products and services could decrease.

The markets we serve are highly competitive and subject to relatively few barriers to entry. Local, regional and national companies are currently competing in many of the healthcare markets we serve and others may do so in the future. Some of our competitors have greater financial, technical, marketing and managerial resources than we have. Consolidation among our competitors, such as pharmacy benefit managers (PBMs) and regional and national infusion pharmacy or specialty pharmacy providers could result in price competition and other competitive factors that could cause a decline in our revenue and profitability. We expect to continue to encounter competition in the future that could limit our ability to grow revenue and/or maintain acceptable pricing levels.

Some biotech pharmaceutical suppliers in the specialty pharmacy industry have chosen to limit the number of distributors of their products. If we are not selected as a preferred distributor of one or more of our core products, our business and results of operations could be seriously harmed.

Some biotech pharmaceutical manufacturers attempt to limit the number of preferred distributors that may market certain of their biopharmaceutical products. If this trend continues, we cannot be certain that we will be selected and retained as a preferred distributor or can remain a preferred distributor to market these products. Although we believe we can effectively meet our suppliers requirements, there can be no assurance that we will be able to compete effectively with other specialty pharmacy companies to retain our position as a distributor of each of our core products. Adverse developments with respect to this trend could have a material adverse effect on our business and results of operations.

Any termination of, or adverse change in, our relationships with a single source product manufacturer or the loss of supply of a specific, single source specialty drug could have a material adverse effect on our operations.

We sell biotech pharmaceuticals that are supplied to us by a variety of manufacturers, many of which are the only source of that specific pharmaceutical. In order to have access to these pharmaceuticals, and to be able to participate in the launch of new biotech pharmaceuticals, we must maintain good working relations with the manufacturers. Most of the manufacturers of the pharmaceuticals we sell have the right to cancel their supply contracts with us without cause and after giving only minimal notice. One biotech pharmaceutical, Synagis®, which is manufactured and distributed by MedImmune, Inc., represented 7.3%, 6.8% and 7.1% of our revenue, respectively, for the fiscal years ended December 31, 2005, 2004 and 2003. The loss of our relationship with MedImmune, Inc. or with one or more other biotech pharmaceutical manufacturer would reduce our revenue and profitability.

We have recently experienced rapid growth by acquisitions. If we fail to manage our growth effectively, our business could be disrupted and our operating results could suffer.

Our ability to successfully offer our products and services in evolving markets requires an effective planning and management process. In 2005, 2004 and 2003 combined, we completed fifteen separate pharmacy business acquisitions, ten of which were completed during 2005. Our growth through acquisitions, combined with the internal growth of our business based on our business plan, may place a strain on our management systems and resources. This growth has resulted in, and will continue to result in an increase in responsibilities for management. To accommodate our growth and compete effectively, we will need to continue to enhance, expand and improve our management and our operational and financial information systems and controls, and to expand, train, manage and motivate our workforce. Our personnel, systems, procedures, or controls may not be adequate to support our operations in the future in light of anticipated growth. In addition, if we focus our financial resources and management attention on the expansion of our operations rather than on our ongoing operations, our financial results may suffer.

If we are unable to acquire additional pharmacy facilities on favorable terms, we will be unable to execute our acquisition and development strategy.

Our strategy includes increasing our revenue and earnings through strategic acquisitions of infusion therapy pharmacies and related businesses. Our efforts to execute our acquisition strategy may be affected by our ability to identify suitable candidates and negotiate and close acquisitions. We continue to evaluate potential acquisition opportunities, including the acquisition of certain of our franchisees, and expect to complete acquisitions in the future. The facilities we purchase may require working capital from us during the initial months of operation, depending on whether or not we acquire receivables as part of the acquisition agreement. We may acquire businesses with significant unknown or contingent liabilities, including liabilities for failure to comply with health care or reimbursement laws and regulations. While we generally obtain contractual rights to indemnification from owners of the businesses we acquire, our ability to realize on any indemnification claims will depend on many factors, including, among other things, the availability of assets of the indemnifying parties. In the future, we may not be successful in acquiring pharmacies or in achieving satisfactory operating results at acquired pharmacies, and we may not be able to acquire healthcare businesses that produce returns justifying our related investment. Furthermore, we may not be able to obtain sufficient capital resources to fund our acquisitions at terms acceptable to us, or at all.

An impairment of goodwill on our financial statements could adversely affect our financial position and results of operations.

Our acquisitions have resulted in the recording of a significant amount of goodwill on our financial statements. Goodwill was recorded because the purchase price was in excess of the fair value of the net identifiable tangible and intangible assets acquired. We may not realize the full value of this goodwill. As such, we evaluate on at least an annual basis whether events and circumstances indicate that all or some of the carrying value of goodwill is no longer recoverable, in which case we would write off the unrecoverable goodwill as a charge against our earnings.

Since our growth strategy will likely involve the acquisition of other companies, we may record additional goodwill in the future. The possible write-off of this goodwill could negatively impact our future earnings. We will also be required to allocate a portion of the purchase price of any acquisition to the value of any intangible assets other than goodwill that meet the criteria specified in the Statement of Financial Accounting Standards No. 141, Business Combinations, such as marketing, customer or contract-based intangibles. The amount allocated to these intangible assets could be amortized over a fairly short period, which may negatively affect our earnings.

As of December 31, 2005, we had goodwill of $112.2 million, or 36% of our total assets and approximately 63% of stockholders equity.

Changes in state and federal government regulation could restrict our ability to conduct our business.

The marketing, sale and purchase of pharmaceuticals and medical supplies and provision of healthcare services generally is extensively regulated by federal and state governments. Other aspects of our business are also subject to government regulation. We believe we are operating our business in compliance with applicable laws and regulations. The applicable regulatory framework is complex, and the laws are very broad in scope. Many of these laws remain open to interpretation and have not been addressed by substantive court decisions. Accordingly, we cannot provide any assurance that our interpretation would prevail or that one or more government agencies will not interpret them differently. Changes in the law or new interpretations of existing law can have a dramatic effect on what we can do, our cost of doing business and the amount of reimbursement we receive from governmental third party payors, such as Medicare and Medicaid. Also, we could be affected by interpretations of what the appropriate charges are under government programs.

Some of the healthcare laws and regulations that apply to our activities include:

- The federal Anti-Kickback Statute prohibits individuals and entities from knowingly and willfully paying, offering, receiving, or soliciting money or anything else of value in order to induce the referral of patients or to induce a person to purchase, lease, order, arrange for, or recommend services or goods covered in whole or in part by Medicare, Medicaid, or other government healthcare programs. Although there are safe harbors under the Anti-Kickback Statute, some of our business arrangements and the services we provide may not fit within these safe harbors or a safe harbor may not exist that covers the arrangement. The Anti-Kickback Statute is an intent based statute and the failure of a business arrangement to satisfy all elements of a safe harbor will not necessarily render the arrangement illegal, but it may subject that arrangement to increased scrutiny by enforcement authorities. Violations of the Anti-Kickback Statute can lead to significant penalties, including criminal penalties, civil fines and exclusion from participation in Medicare and Medicaid.

- The Stark Law prohibits physicians from making referrals to entities with which the physicians or their immediate family members have a financial relationship (i.e., an ownership, investment or compensation relationship) for the furnishing of certain Designated Health Services (DHS) that are

reimbursable under Medicare. The Stark Law exempts certain business relationships which meet its exception requirements. However, unlike the Anti-Kickback Statute under which an activity may fall outside a safe harbor and still be lawful, a referral for DHS that does not fall within an exception is strictly prohibited by the Stark Law. A violation of the Stark Law is punishable by civil sanctions, including significant fines and exclusion from participation in Medicare and Medicaid.

- The Health Insurance Portability and Accountability Act of 1996 (HIPAA) provides federal privacy protections for individually identifiable health information. Through the adoption of the Privacy Rule, HIPAA set national standards for the protection of health information for providers and others who transmit health information electronically. In addition to regulating privacy of individual health information, HIPAA includes several anti-fraud and abuse laws, extends criminal penalties to private health care benefit programs and, in addition to Medicare and Medicaid, to other federal health care programs, and expands the Office of Inspector General s (OIG s) authority to exclude persons and entities from participating in the Medicare and Medicaid programs.

- Pharmacies and pharmacists must obtain state licenses to operate and dispense pharmaceuticals. If we are unable to maintain our licenses or if states place burdensome restrictions or limitations on non-resident pharmacies, this could limit or affect our ability to operate in some states which could adversely impact our business and results of operations.

We may become subject to federal and state investigations.

Both federal and state government agencies have heightened and coordinated civil and criminal enforcement efforts as part of numerous ongoing investigations of healthcare companies, as well as their executives and managers. These investigations relate to a wide variety of topics, including referral and billing practices. Further, amendments to the federal False Claims Act have made it easier for private parties to bring whistleblower lawsuits against companies. Some states have adopted similar state whistleblower and false claims provisions. The Office of the Inspector General of the Department of Health and Human Services and the Department of Justice have, from time to time, established national enforcement initiatives that focus on specific billing practices or other suspected areas of abuse. Some of our activities could become the subject of governmental investigations or inquiries. For example, we have significant Medicare and Medicaid billings. In addition, our executives, some of whom have worked at other healthcare companies that are or may become the subject of federal and state investigations and private litigation, could be included in governmental investigations or named as defendants in private litigation, resulting in adverse publicity against us. We are not aware of any governmental investigations involving any of our company-owned facilities or our executives. A future investigation of us could result in significant liabilities or penalties to us, as well as adverse publicity, and could seriously undermine our ability to compete for business, negotiate acquisitions, hire new personnel and otherwise conduct our business.

We may be subject to liability for the services we offer and the products we sell.

We and other participants in the health care market are, have been and are likely to continue to be subject to lawsuits based upon alleged malpractice, product liability, negligence or similar legal theories, many of which involve large claims and significant defense costs. A successful claim not covered by our professional liability insurance or substantially in excess of our insurance coverage could cause us to pay out a substantial award. In addition, we retain liability on claims up to the amount of our deductibles, which generally are $250,000 per occurrence. Further, our insurance policy is subject to annual renewal and it may not be possible to obtain liability insurance in the future on acceptable terms, with adequate coverage against potential liabilities, or at all. Also, claims against us, regardless of their merit or eventual outcome, could be a serious distraction to management and could harm our reputation.

Labor strikes or similar work stoppages within the companies that provide our local and national distribution services could have a negative impact on our results of operations.

We utilize several national delivery companies as an important part of the local and national distribution of our products and services, particularly in the delivery of certain specialty pharmaceutical products. A portion of the workforce utilized by these delivery companies are members of labor unions. A labor strike or similar work stoppage within any of the delivery companies that we utilize for distribution could have a negative impact on our results of operations.

Our image and reputation may be harmed by actions taken by our franchisees that are outside of our control.

The majority of our local pharmacy locations are operated by franchisees. Franchisees are independent business owners and are not our subsidiaries or employees. Consequently, the quality of a franchised operation is dependent upon its owner(s) and manager(s). Franchisees may not successfully operate facilities or they may fail to comply with federal and state health care statutes and regulations. If they do not operate their franchises effectively or do not comply with applicable industry regulations, our image and reputation may suffer which could negatively impact our results of operations.

Our gross profit margins may decline if our franchise royalties are reduced.

We rely on royalty payments from our franchisees. For the fiscal years ended December 31, 2005, 2004 and 2003, we derived 1.4%, 1.9% and 2.3%, respectively, of our revenue from franchise royalties (excluding any acquisition settlement or termination gains). Our franchisees pay royalties on their gross receipts. Because there is no cost of goods sold associated with this revenue, franchise royalties and other fees represent a significant portion of our gross profit. For the fiscal years ended December 31, 2005, 2004 and 2003, royalties and other franchise fees represented 4.8%, 6.8% and 7.6%, respectively, of our gross profit. If our franchisees encounter business or operational difficulties, our revenue from royalties may be adversely affected. Such difficulties may also negatively impact our ability to sell new franchises. In addition, if we are unable to successfully attract new franchisees or if our existing franchise owners either do not enter into new franchise agreements with us when their current agreements expire or enter into new franchise agreements with royalty payment rates less favorable to us than current rates, our franchise revenue, gross profit and overall profitability will decline.

The loss of one or more of our key employees could harm our operations.

Our success depends upon the availability and performance of our key executives, including our Chief Executive Officer, Rajat Rai, and our President and Chief Operating Officer, Richard M. Smith. We do not have key person insurance for any of our key executives. The loss of the services of Mr. Rai, Mr. Smith or any of our other key executives could have a material adverse effect upon our business and results of operations.

The current or future shortage in licensed pharmacists, nurses and other clinicians could adversely affect our business.

The healthcare industry is currently experiencing a shortage of licensed pharmacists, nurses and other healthcare professionals. Consequently, hiring and retaining qualified personnel will be difficult due to intense competition for their services and employment. Any failure to hire or retain pharmacists, nurses or other healthcare professionals could impair our ability to expand or maintain our operations.

The market price of our common stock may experience substantial fluctuations for reasons over which we have little control.

Our common stock is traded on the Nasdaq National Market. The stock price and the share trading volume for companies in the healthcare and health services industry is subject to significant volatility. Both company-specific and industry-wide developments, as well as changes to the overall condition of the US economy and stock market, may cause this volatility. The market price of our common stock could continue to fluctuate up or down substantially based on a variety of factors, including the following:

- future announcements concerning us, our competitors, the pharmaceutical manufacturers and managed care companies with whom we have relationships or the health care market;
- changes in operating results from quarter to quarter;
- sales of stock by insiders;
- changes in government regulations;
- changes in estimates by analysts;
- news reports relating to trends in our markets;
- the seasonal nature of pharmaceuticals we offer, including Synagis®;
- acquisitions and financings in our industry; and
- the overall volatility of the stock market.

Furthermore, stock prices for many companies fluctuate widely for reasons that may be unrelated to their operating results. These fluctuations, coupled with changes in our results of operations and general economic, political and market conditions, may adversely affect the market price of our common stock.

Increases in the per share market price of our common stock in future periods could result in dilution of our earnings per share.

Increases in the market price of our common stock may result in dilution of our earnings per share related to the conversion feature of our 2.25% senior convertible notes. In accordance with Emerging Issues Task Force (EITF) Issue 04-8, *The Effect of Contingently Convertible Instruments on Diluted Earnings per Share,* our diluted shares must include the dilutive effect of our convertible notes for periods during which the average market price of our common stock exceeds its conversion price per the terms of the notes during a given period. The conversion price is currently set at $11.99 per share (subject to future adjustment, as needed). If the average market price of our common stock should exceed the conversion price per share in a given period, our diluted shares would increase, which could reduce our net income per diluted share for such period. For the fiscal year ending December 31, 2005, the average market price of our common stock exceeded the conversion price of $11.99 per share and the dilutive effects of the 2.25% senior convertible notes, which totaled approximately 600,000 shares, are included in our diluted earnings per share reported for that period.

We may not have the ability to raise the funds to purchase our outstanding convertible senior notes on the purchase dates or upon a fundamental change or to pay the cash payment due upon conversion.

On each of November 1, 2009, November 1, 2014 and November 1, 2019, holders of our convertible senior notes may require us to purchase, for cash, all or a portion of their 2.25% senior convertible notes at 100% of their principal amount, plus any accrued and unpaid interest to, but excluding, that date. If a fundamental change occurs, holders of the notes may require us to repurchase, for cash, all or a portion of their notes. In addition, upon conversion of the notes, we will be required to pay the principal, or, in

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certain circumstances, other amounts, in cash. We may not have sufficient funds for any required repurchase of the notes. In addition, the terms of any borrowing agreements that we may enter into from time to time may require early repayment of borrowings under circumstances similar to those constituting a fundamental change. These agreements may also make our repurchase of notes, or the cash payment due upon conversion of the notes, an event of default under the agreements. If we fail to repurchase the notes or pay the cash payment due upon conversion when required, we will be in default under the indenture for the notes.

Our leverage, primarily relating to our outstanding convertible senior notes, may harm our financial condition and results of operations.

Our total consolidated long-term debt as of December 31, 2005 was $86.3 million, which represents 32.7% of our total capitalization as of that date. In addition, the indenture for our convertible senior notes will not restrict our ability to incur additional indebtedness.

Our level of indebtedness could have important consequences, because:

- it could affect our ability to satisfy our obligations under the notes;
- a portion of our cash flows from operations will have to be dedicated to interest and principal payments and may not be available for operations, working capital, capital expenditures, expansion, acquisitions or general corporate or other purposes;
- it may impair our ability to obtain additional financing in the future;
- it may limit our flexibility in planning for, or reacting to, changes in our business and industry; and
- it may make us more vulnerable to downturns in our business, our industry or the economy in general.

Our single largest stockholder owns approximately 23.0% of our common stock and may be able to exercise significant influence over the outcome of matters to be voted on by our stockholders.

As of March 1, 2006, Dr. John Kapoor had beneficial ownership both individually and through several partnerships and a trust of approximately 23.0% of the outstanding shares of our common stock. Dr. Kapoor is the Chairman of our Board of Directors. Accordingly, Dr. Kapoor, alone or together with members of our management team, may be able to exercise significant influence with respect to the election of directors, offers to acquire us and other matters submitted to a vote of our stockholders.

Our certificate of incorporation, our bylaws, and Delaware law contain provisions that could discourage a change in control.

Some provisions of our certificate of incorporation and bylaws, as well as Delaware law, may be deemed to have an anti-takeover effect or may delay or make more difficult an acquisition or change in control not approved by our board of directors, whether by means of a tender offer, open market purchases, a proxy contest or otherwise. These provisions could have the effect of discouraging third parties from making proposals involving an acquisition or change in control, although such a proposal, if made, might be considered desirable by a majority of our stockholders. These provisions may also have the effect of making it more difficult for third parties to cause the replacement of our current management team without the concurrence of our board of directors.

Item 1B. UNRESOLVED STAFF COMMENTS

None.

Item 2. PROPERTIES

Our executive offices, located at 485 Half Day Road, Suite 300, Buffalo Grove, Illinois, 60089, consist of approximately 29,000 square feet of leased space, pursuant to a ten-year and three month lease that began in June 2002. Monthly base rent payments increase from approximately $35,000 per month for the first year of the lease to approximately $53,000 per month for the last year, plus applicable real estate taxes and maintenance costs. We have the option to accelerate the expiration date of this lease by three years upon payment of an acceleration fee.

In addition to our executive offices, we have over 70 facilities located in more than 60 cities throughout the United States, not including storage units. Our most significant building lease commitments, aside from our executive office lease described above, are for the following facilities:

Location (City, State)	Street Address	Lease Term		Approximate Square Footage	Total Remaining Commitment at December 31, 2005 (in thousands)
Everett, Washington	8130 Evergreen Way	10/01/2005	09/30/2013	15,000	$ 2,350
Miramar, Florida	2804 Corporate Way	08/27/2002	10/31/2012	20,000	$ 2,209
Carlsbad, California	1989 Palomar Oaks Way	12/01/2005	11/30/2012	14,000	$ 1,465
Englewood, Colorado	345 Inverness Drive	09/12/2005	08/11/2012	11,000	$ 928

Our facilities, most of which contain pharmacies, warehouse space and administrative offices, are all leased, with remaining terms ranging from one month to approximately 8 years, and consist of approximately 540,000 square feet in total. The offices are in good condition, well maintained, and are adequate to fulfill our operational needs for the foreseeable future. We believe that if necessary, we could replace any of our leased facilities without significant additional cost or adverse affect on our business.

Item 3. LEGAL PROCEEDINGS

From time to time, we are named as a party to legal claims and proceedings in the ordinary course of business. Additionally, from time to time, governmental and regulatory agencies may initiate investigations or proceedings against us in the ordinary course of business, or which have general application to the businesses we operate. Presently, we are not aware of any claims, investigations or proceedings against us or any of our franchisees that we believe are likely to have a material adverse effect on our results of operations or financial condition.

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

There were no matters submitted to a vote of security holders during the fourth quarter of the fiscal year ended December 31, 2005.

PART II

Item 5. MARKET FOR REGISTRANT S COMMON EQUITY, RELATED STOCKHOLDER MATTERS AND ISSUER REPURCHASES OF EQUITY SECURITIES

PRICE RANGE OF COMMON STOCK

Option Care is traded on the Nasdaq National Market under the symbol OPTN . The following table shows the high and low bid prices for our common stock for the periods indicated.

Calendar Quarter	High	Low
2005		
Fourth Quarter	$ 14.97	$ 11.39
Third Quarter	$ 15.11	$ 12.71
Second Quarter	$ 14.72	$ 12.47
First Quarter	$ 14.13	$ 10.58
2004		
Fourth Quarter	$ 12.56	$ 8.51
Third Quarter	$ 12.41	$ 8.87
Second Quarter	$ 10.55	$ 7.37
First Quarter	$ 9.26	$ 6.89

On March 1, 2006, the closing price of our common stock on the Nasdaq National Market was $14.02. As of March 1, 2006, there were 273 holders of record reported to us by our transfer agent, U.S. Stock Transfer Corporation.

All share and per share amounts in this Annual Report on Form 10-K for the fiscal years 2001, 2002, 2003 and 2004 have been adjusted to reflect the pro forma effects of the 3-for-2 stock split completed April 1, 2005 for stockholders of record on March 17, 2005. The share and per share amounts in this Annual Report on Form 10-K for the fiscal years 2001 and 2002 have also been adjusted to reflect the pro forma effects of the 5-for-4 stock split completed May 1, 2002 for stockholders of record as of April 10, 2002.

DIVIDEND POLICY

In May 2004, our Board of Directors authorized the adoption of a quarterly dividend policy. Each quarter, our Board of Directors will determine the dividend amount per share. During each of the quarters ended June 30, September 30 and December 31, 2004, and March 31, 2005, our Board declared a $0.0133 per share dividend. During each of the quarters ended June 30, September 30 and December 31, 2005, our Board declared a $0.02 per share dividend.

Item 6. SELECTED CONSOLIDATED FINANCIAL DATA

The table below provides you with certain of our summary historical financial data. We have prepared this information using our consolidated financial statements for the five years ended December 31, 2005, which have been audited by Ernst & Young LLP, independent registered public accounting firm. The selected consolidated financial data reflects our acquisitions, all of which were accounted for using the purchase method of accounting. This summary should be read in conjunction with our Consolidated Financial Statements and Notes thereto, and Item 7 Management s Discussion and Analysis of Financial Condition and Results of Operations.

Consolidated Statement of Income data (in thousands, except per share data):

	Years Ended December 31,			
	2005	**2004**	**2003**	**2002**