

RITE AID CORP  
Form 10-K  
April 24, 2012

Use these links to rapidly review the document

[TABLE OF CONTENTS](#)  
[Item 9B. Other Information](#)

[Table of Contents](#)

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

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**FORM 10-K**

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

**For The Fiscal Year Ended March 3, 2012**

**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 1-5742**

**RITE AID CORPORATION**

(Exact name of registrant as specified in its charter)

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

**23-1614034**  
(I.R.S. Employer  
Identification No.)

**30 Hunter Lane, Camp Hill, Pennsylvania**  
(Address of principal executive offices)

**17011**  
(Zip Code)

Registrant's telephone number, including area code: **(717) 761-2633**

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

**Title of each class**  
Common Stock, \$1.00 par value

**Name of each exchange on which registered**  
New York Stock Exchange

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

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

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

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

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Website, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the Registrant was required to submit and post such files). Yes  No

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

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, 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       Accelerated Filer       Non-Accelerated Filer       Smaller reporting company   
(Do not check if a smaller reporting company)

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

The aggregate market value of the voting and non-voting common stock of the registrant held by non-affiliates of the registrant based on the closing price at which such stock was sold on the New York Stock Exchange on August 27, 2011 was approximately \$682,941,816. For purposes of this calculation, executive officers, directors and 5% shareholders are deemed to be affiliates of the registrant.

As of April 10, 2012 the registrant had outstanding 898,966,064 shares of common stock, par value \$1.00 per share.

### DOCUMENTS INCORPORATED BY REFERENCE

Portions of the proxy statement for the registrant's annual meeting of stockholders to be held on June 21, 2012 are incorporated by reference into Part III.

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Table of Contents**TABLE OF CONTENTS**

|   | <b>Page</b>    |
|---|----------------|
| <u>Cautionary Statement Regarding Forward-Looking Statements</u>  | <u>3</u>       |
| <b><u>PART I</u></b>  |                |
| <u>ITEM 1. Business</u>   | <u>4</u>       |
| <u>ITEM 1A. Risk Factors</u>  | <u>11</u>      |
| <u>ITEM 1B. Unresolved Staff Comments</u>   | <u>20</u>      |
| <u>ITEM 2. Properties</u>   | <u>20</u>      |
| <u>ITEM 3. Legal Proceedings</u>  | <u>23</u>      |
| <u>ITEM 4. Mine Safety Disclosures</u>  | <u>24</u>      |
| <b><u>PART II</u></b>   |                |
| <u>ITEM 5. Market for Registrant's Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities</u> | <u>24</u>      |
| <u>ITEM 6. Selected Financial Data</u>  | <u>25</u>      |
| <u>ITEM 7. Management's Discussion and Analysis of Financial Condition and Results of Operations</u>                        | <u>27</u>      |
| <u>ITEM 7A. Quantitative and Qualitative Disclosures About Market Risk</u>  | <u>45</u>      |
| <u>ITEM 8. Financial Statements and Supplementary Data</u>  | <u>46</u>      |
| <u>ITEM 9. Changes in and Disagreements with Accountants on Accounting and Financial Disclosure</u>                         | <u>46</u>      |
| <u>ITEM 9A. Controls and Procedures</u>   | <u>46</u>      |
| <u>ITEM 9B. Other Information</u>   | <u>49</u>      |
| <b><u>PART III</u></b>  |                |
| <u>ITEM 10. Directors, Executive Officers and Corporate Governance</u>  |                |
| <u>ITEM 11. Executive Compensation</u>  |                |
| <u>ITEM 12. Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters</u>              |                |
| <u>ITEM 13. Certain Relationships and Related Transactions, and Director Independence</u>                                   |                |
| <u>ITEM 14. Principal Accountant Fees and Services</u>  |                |
| <b><u>PART IV</u></b>   |                |
| <u>ITEM 15. Exhibits and Financial Statement Schedule</u>   | <u>49</u>      |
| <br><u>SIGNATURES</u>   | <br><u>117</u> |

Table of Contents

**CAUTIONARY STATEMENT REGARDING FORWARD-LOOKING STATEMENTS**

This report, as well as our other public filings or public statements, include forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995. These forward-looking statements are often identified by terms and phrases such as "anticipate," "believe," "intend," "estimate," "expect," "continue," "should," "could," "may," "plan," "project," "predict," "will" and similar expressions and include references to assumptions and relate to our future prospects, developments and business strategies.

Factors that could cause actual results to differ materially from those expressed or implied in such forward-looking statements include, but are not limited to:

our high level of indebtedness;

our ability to make interest and principal payments on our debt and satisfy the other covenants contained in our senior secured credit facility and other debt agreements;

general economic conditions (including the impact of continued high unemployment and changing consumer behavior), inflation and interest rate movements;

our ability to improve the operating performance of our stores in accordance with our long term strategy;

our ability to realize same store sales growth;

our ability to hire and retain qualified personnel;

the efforts of private and public third party payors to reduce prescription drug reimbursement and encourage mail order;

competitive pricing pressures, including aggressive promotional activity from our competitors;

decisions to close additional stores and distribution centers, which could result in further charges to our operating statement;

our ability to manage expenses and our investment in working capital;

continued consolidation of the drugstore and the pharmacy benefit management industries;

changes in state or federal legislation or regulations, and the impact of healthcare reform, including the forthcoming Supreme Court ruling on the Patient Protection and Affordable Care Act,

the outcome of lawsuits and governmental investigations;

our ability to maintain the listing of our common stock on the New York Stock Exchange (the "NYSE"), and the resulting impact on our indebtedness, results of operations and financial condition; and

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other risks and uncertainties described from time to time in our filings with the Securities and Exchange Commission (the "SEC").

We undertake no obligation to update or revise the forward-looking statements included in this report, whether as a result of new information, future events or otherwise, after the date of this report. Our actual results, performance or achievements could differ materially from the results expressed in, or implied by, these forward-looking statements. Factors that could cause or contribute to such differences are discussed in the sections entitled "Risk Factors" and "Management's Discussion and Analysis of Financial Condition and Results of Operations - Overview and Factors Affecting Our Future Prospects" included in this annual report on Form 10-K.

Table of Contents

**PART I**

**Item 1. Business**

**Overview**

We are the third largest retail drugstore chain in the United States based on revenues and number of stores. We operate our drugstores in 31 states across the country and in the District of Columbia. As of March 3, 2012, we operated 4,667 stores.

In our stores, we sell prescription drugs and a wide assortment of other merchandise, which we call "front end" products. In fiscal 2012, prescription drug sales accounted for 68.1% of our total sales. We believe that our pharmacy operations will continue to represent a significant part of our business due to favorable industry trends, including an aging population, increased life expectancy, anticipated growth in the federally funded Medicare Part D prescription program as "baby boomers" start to enroll, expanded coverage for uninsured Americans as the result of the Patient Protection and Affordable Care Act and the discovery of new and better drug therapies. We carry a full assortment of front end products, which accounted for the remaining 31.9% of our total sales in fiscal 2012. Front end products include over-the-counter medications, health and beauty aids, personal care items, cosmetics, household items, beverages, convenience foods, greeting cards, seasonal merchandise and numerous other everyday and convenience products, as well as photo processing. We attempt to distinguish our stores from other national chain drugstores, in part, through our wellness + loyalty program, private brands and our strategic alliance with GNC, a leading retailer of vitamin and mineral supplements. We offer a wide variety of products under our private brands, which contributed approximately 17.0% and 16.0% of our front end sales in the categories where private brand products were offered in fiscal 2012 and fiscal 2011, respectively.

The overall average size of each store in our chain is approximately 12,600 square feet. The average size of our stores is larger in the western United States. As of March 3, 2012, 60% of our stores were freestanding; 51% of our stores included a drive-thru pharmacy; 24% included one-hour photo shops; and 46% included a GNC store-within-Rite Aid-store.

Our headquarters are located at 30 Hunter Lane, Camp Hill, Pennsylvania 17011, and our telephone number is (717) 761-2633. Our common stock is listed on the New York Stock Exchange under the trading symbol of "RAD." We were incorporated in 1968 and are a Delaware corporation.

**Industry Trends**

The rate of pharmacy sales growth in the United States in recent years has slowed, driven by the decline in new blockbuster drugs, a longer FDA approval process, drug safety concerns, higher copays, the loss of individual health insurance with the rise of unemployment and an increase in the use of generic (non-brand name) drugs, which are less expensive but generate higher gross margins. However, we expect prescription sales to grow in the coming years due to the aging population, increased life expectancy, "baby boomers" becoming eligible for the federally funded Medicare prescription program and new drug therapies. Furthermore, we expect the estimated additional 33 million people who will be covered by health insurance in 2014, and the closing of the "donut hole" in Medicare Part D to be good for our business.

Generic prescription drugs help lower overall costs for customers and third party payors. We believe the utilization of existing generic pharmaceuticals will continue to increase. Further, a significant number of new generics are expected to be introduced in 2012 and 2013 as many popular branded drugs are scheduled to lose patent protection. The gross profit from a generic drug prescription in the retail drugstore industry is greater than the gross profit from a brand drug prescription, however, the sale amount can be substantially less.

Table of Contents

The retail drugstore industry is highly competitive and has been experiencing consolidation. We believe that the continued consolidation of the drugstore industry, continued new store openings, increased competition from internet based providers and aggressive generic pricing programs at competitors such as Wal-Mart and various supermarket chains will further increase competitive pressures in the industry. The pharmacy business has become increasingly promotional, which contributes to additional competitive pressures.

The retail drugstore industry relies significantly on third party payors. Third party payors, including the Medicare Part D plans and the state sponsored Medicaid and related managed care Medicaid agencies, at times change the eligibility requirements of participants or reduce certain reimbursement rates. These changes and reductions are expected to continue. When third party payors, including the Medicare Part D program and state sponsored Medicaid agencies, reduce the number of participants and/or reduce their reimbursement rates, sales and margins in the industry could be reduced, and profitability of the industry adversely affected. These possible adverse effects can be partially or entirely offset by controlling expenses, dispensing more higher margin generics and dispensing more prescriptions overall.

**Strategy**

Our primary goal for fiscal 2013, consistent with fiscal 2012, is to grow same stores sales, which is critical for our future financial success. Same store sales growth will enable us to take full advantage of the improvements that we have made in the areas of cost control and working capital management. We also plan to take advantage of the costs savings and gross profit improvement opportunities that will result from the conversion of numerous brand drugs to generic alternatives in fiscal 2013 and beyond. We also plan to increase our capital investment in our store base, which we expect to lead to additional sales growth. We expect these initiatives to lead to growth in long term shareholder value. Following is a description of these initiatives:

*wellness +* We rolled out our *wellness +* loyalty program in April of 2010. *wellness +* is a free customer loyalty program that provides benefits to enrolled members based on the accumulation of points for certain front end and prescription purchases. This program provides significant value to customers who achieve Gold, Silver, and Bronze tier levels in the program and has been very well received by our customers. As of April 2012, we had over 52 million members enrolled in the *wellness +* program. At the end of our fiscal year, *wellness +* members accounted for 74% of front end sales and 68% of prescriptions filled. *wellness +* members have higher basket sizes than non-members and also have a much higher rate of prescription retention. *wellness +* members also are eligible to receive plus-up rewards, which are discounts on certain items featured in our weekly circular and provide members with additional savings for return shopping trips. Beginning in January 2012, we added additional features to the program, which include the creation of a Bronze member tier and the rollout of our Load2Card feature. The Bronze tier is achieved when a member reaches 250 points, Bronze tier members receive 10% off on the purchase of all Rite Aid private brand merchandise and a one-time 10% shopping pass. Load2Card is a new coupon management program and is the first of its kind in the drugstore retailer space. It enables customers to save, manage and redeem Rite Aid and manufacturer coupons available throughout the internet via their *wellness +* card. Customers have responded favorably to these enhancements.

We believe that the *wellness +* program has contributed to the improvement in our fiscal 2012 sales trends. We plan on making additional incremental investments in *wellness +* in fiscal 2013, primarily in additional discounts, as we expect more customers to move into the Gold, Silver, and Bronze levels.

*Express Scripts customers* As of January 1, 2012, the Express Scripts pharmacy benefit management network decreased the number of participating pharmacies. This has contributed to an

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### Table of Contents

increase in same store script volume in the fourth quarter of fiscal 2012. To the extent that the Express Scripts pharmacy benefit management network continues to exclude other pharmacies from their network, we have the opportunity to pick up incremental share. We plan to work proactively to ensure that we attract and retain as many new customers as possible. Efforts to do so will include adjusting pharmacy staffing levels where appropriate, encouraging customers to sign up for wellness +, and continuing to communicate in print, signage and other advertising channels that we accept Express Scripts pharmacy benefit management network patients.

*Wellness remodels* During fiscal 2012, we introduced our new Wellness format store. These stores offer expanded clinical pharmacy services and new health and wellness product offerings. They are staffed with our unique Wellness Ambassadors, who serve as an added customer resource and bridge from the front end of the stores to the pharmacy. We completed 274 wellness remodels in fiscal 2012 and expect to complete an additional 500 in fiscal 2013. Our customers have responded favorably to this unique store format and recent sales results in these stores have been encouraging.

*Healthcare services* During fiscal 2012, we increased the number of Rite Aid immunizing pharmacists to 11,000, expanded our immunization services to all of our stores and administered 1.5 million flu shots. In addition to flu shots, we also expanded the scope of our immunization services to 14 different disease states. Continuing to expand the volume and types of immunizations that we can perform will be an area of focus for fiscal 2013. In conjunction with Optum Health, last August we introduced NowClinic Online Care services inside select Rite Aid pharmacies in the greater Detroit area. These clinics provide on-line access to a physician, who has the ability to diagnose and potentially write prescriptions for our patients. We have also introduced wellness + for diabetes, the first extension of our wellness + program to provide discounts on front-end products and resources for diabetes patients and caregivers. One such resource is "Diabetes Head2Toe", a unique collaboration with Web MD to provide online tools to help patients manage and live well with diabetes. We are focused on healthcare-related services because we believe these services will help build loyalty with existing customers and attract new ones.

*Script file purchases* We intend to increase the amount of capital allocated to the purchase of prescription files from \$35.0 million in fiscal 2012 to \$50.0 million in fiscal 2013.

*Private brands* During fiscal 2011, we began the rollout of a new private brand architecture, which includes the consolidation of our private brands in three separate tiers. We have converted about 2,900 items to the new architecture and have improved our private brand penetration by 100 basis points over the prior year. We expect to have approximately 3,000 items in these brands in fiscal 2013. Many of the new items are in our price fighter brand, Simplify, and we believe customers have found these products to be of high quality and provide great value.

*Customer service* We have put programs in place in store operations to stress the importance of greeting our customers more frequently and assisting them with their purchases. We made investments in technology in fiscal 2011 and 2012 that make it easier for our store associates to perform necessary tasks, such as price changes and backroom inventory management, which will free up their time to focus on the customer. During fiscal 2012, we increased the amount of dollars spent on training our store and field associates on customer service skills. We believe this additional focus has helped drive our same store sales increases in fiscal 2012 and this will continue to be an area of focus for us in fiscal 2013.

We made significant reductions to our SG&A expense over the past few years through better control of store labor and other controllable costs in the stores, consolidation of our distribution center network, a centralized indirect procurement function for all non-merchandise purchases and through initiatives aimed to simplify our processes in the stores and at our Corporate office. We will continue to focus on controlling costs in fiscal 2013 so that we can maximize the benefits of our sales initiatives.



Table of Contents**Products and Services**

Sales of prescription drugs represented approximately 68.1%, 67.8%, and 67.9% of our total sales in fiscal years 2012, 2011 and 2010, respectively. In fiscal years 2012, 2011 and 2010, prescription drug sales were \$17.7 billion, \$17.0 billion, and \$17.4 billion, respectively. See "Item 7 Management's Discussion and Analysis of Financial Condition and Results of Operations" and our consolidated financial statements.

We carry a full assortment of non-prescription, or front end products. The types and number of front end products in each store vary, and selections are based on customer needs and preferences and available space. No single front end product category contributed significantly to our sales during fiscal 2012. Our principal classes of products in fiscal 2012 were the following:

| <b>Product Class</b>                           | <b>Percentage of Sales</b> |
|--|----------------------------|
| Prescription drugs                             | 68.1%                      |
| Over-the-counter medications and personal care | 9.8%                       |
| Health and beauty aids                         | 5.2%                       |
| General merchandise and other                  | 16.9%                      |

We offer a wide variety of products under our private brands, which contributed approximately 17.0% of our front end sales in the categories where private brand products were offered in fiscal 2012. We intend to increase the number of private brand products during fiscal 2013, many of which will be in our price fighter brand, Simplify. We believe that our customers find these products to be of high quality and provide great value.

We have a strategic alliance with GNC under which we have opened over 2,100 GNC "stores-within-Rite Aid-stores" as of March 3, 2012 and a contractual commitment to open additional stores by December 2014. We incorporate the GNC store-within-Rite Aid-store concept into many of our new and relocated stores and into many of our Wellness remodels. GNC is a leading nationwide retailer of vitamin and mineral supplements, personal care, fitness and other health-related products.

**Technology**

All of our stores are integrated into a common information system, which enables our customers to fill or refill prescriptions in any of our stores throughout the country, reduces chances of adverse drug interactions, and enables our pharmacists to fill prescriptions more accurately and efficiently. This system can be expanded to accommodate new stores. Our customers may also order prescription refills over the Internet through [www.riteaid.com](http://www.riteaid.com), or over the phone through our telephonic automated refill systems for pick up at a Rite Aid store. We have automated pharmacy dispensing units in high volume stores, which are linked to our pharmacists' computers that fill and label prescription drug orders. The efficiency of these units allows our pharmacists to spend more time consulting with our customers. Additionally, each of our stores employs point-of-sale technology that supports sales analysis and recognition of customer trends. This same point-of-sale technology facilitates the maintenance of perpetual inventory records which, together with our sales analysis, drives our automated inventory replenishment process.

We continue to embrace technology as a way to enhance the customer experience. We completed the development of our new mobile app, which is now available for download for both the Android and iPhone platforms. This free app allows our customers to use their smartphones to order refills by scanning their prescription bottle, manage their wellness + account, access the weekly circular to view sale items and locate a nearby Rite Aid store using GPS.

Table of Contents

**Suppliers**

During fiscal 2012, we purchased brand pharmaceuticals and some generic pharmaceuticals, which amounted to approximately 90.9% of the dollar volume of our prescription drugs, from a single wholesaler, McKesson Corp ("McKesson"), under a contract which runs through April 1, 2013. Under the contract, with limited exceptions, we are required to purchase all of our branded pharmaceutical products from McKesson. If our relationship with McKesson was disrupted, we could temporarily have difficulty filling prescriptions for brand-named drugs until we executed a replacement wholesaler agreement or developed and implemented self-distribution processes, which could negatively affect our business.

We purchase most of our generic (non-brand name) pharmaceuticals directly from manufacturers which account for approximately 76% of our prescription volume. We believe the loss of any one generic supplier would not disrupt our ability to fill generic (non-brand name) prescriptions but could negatively impact our results.

We purchase our non-pharmaceutical merchandise from numerous manufacturers and wholesalers. We believe that competitive sources are readily available for substantially all of the non-pharmaceutical merchandise we carry and that the loss of any one supplier would not have a material effect on our business.

We sell private brand and co-branded products that generally are supplied by numerous competitive sources. The Rite Aid and GNC co-branded PharmAssure vitamin and mineral supplement products and the GNC branded vitamin and mineral supplement products that we sell in our stores are developed by GNC, and along with our Rite Aid brand vitamin and mineral supplements, are manufactured by GNC.

**Customers and Third Party Payors**

During fiscal 2012, our stores filled approximately 295 million prescriptions and served an average of 2.1 million customers per day. The loss of any one customer would not have a material adverse impact on our results of operations.

In fiscal 2012, 96.5% of our pharmacy sales were to customers covered by third party payors (such as insurance companies, prescription benefit management companies, government agencies, private employers or other managed care providers) that agree to pay for all or a portion of a customer's eligible prescription purchases based on negotiated and contracted reimbursement rates. During fiscal 2012, the top five third party payors accounted for approximately 66.4% of our pharmacy sales. The largest third party payor represented 22.9% of our pharmacy sales.

During fiscal 2012, Medicaid and related managed care Medicaid payors sales were approximately 17.7% of our pharmacy sales, of which the largest single Medicaid payor was approximately 2.1% of our pharmacy sales. During fiscal 2012, approximately 28.2% of our pharmacy sales were to customers covered by Medicare Part D.

**Competition**

The retail drugstore industry is highly competitive. We compete with, among others, retail drugstore chains, independently owned drugstores, supermarkets, mass merchandisers, discount stores, dollar stores and mail order pharmacies. We compete on the basis of store location and convenient access, customer service, product selection and price. We believe continued consolidation of the drugstore industry, the aggressive discounting of generic drugs by supermarkets and mass merchandisers and the increase of promotional incentives to drive prescription sales will further increase competitive pressures in the industry.

Table of Contents

**Marketing and Advertising**

In fiscal 2012, marketing and advertising expense was approximately \$369.4 million, which was spent primarily on weekly circular advertising. Our marketing and advertising activities centered primarily on the following:

Product price promotions to draw customers to our stores;

Our wellness + loyalty program, which benefits members based on accumulating points for certain front end and prescription purchases, and offers + UP rewards to provide members additional savings;

Our value plus concept pilot stores offer our customers specific shopping experiences and high value products in addition to those found in a traditional drug store;

Emphasis on the value of our private brand products;

Support of specific initiatives and stores, including competitor market intrusion and prescription file buys; and

Our vision to be the customer's first choice for health and wellness products, services and information.

Under the umbrella of our "With Us It's Personal" brand positioning, we promote educational programs focusing on specific health conditions and incentives for patients to transfer their prescriptions to Rite Aid. We are also emphasizing our automated courtesy refill service. We believe all of these programs will help us improve customer satisfaction and grow profitable sales.

**Associates**

We believe that our relationships with our associates are good. As of March 3, 2012, we had approximately 90,000 associates: 12% were pharmacists, 43% were part-time and 26% were represented by unions. Associate satisfaction is critical to the success of our strategy. We have surveyed our associates to obtain feedback on various employment-related topics, including job satisfaction and their understanding of our core values and mission. We have also instituted an internal group, consisting of managers and staff from all components of our business that is responsible for using feedback from associates throughout the Company to create a better work environment.

The pharmacist shortage has eased significantly. The increase in the number of graduates from U.S. Schools of Pharmacy is starting to meet the workforce demand. However, pharmacist employment opportunities still exist in certain areas.

**Research and Development**

We do not make significant expenditures for research and development.

**Licenses, Trademarks and Patents**

The Rite Aid name is our most significant trademark and the most important factor in marketing our stores and private brand products. We hold licenses to sell beer, wine and liquor, cigarettes and lottery tickets. As part of our strategic alliance with GNC, we have a license to operate GNC "stores-within-Rite Aid-stores." We also hold licenses to operate our pharmacies and our distribution facilities. Collectively, these licenses are material to our operations.

Table of Contents

**Seasonality**

We experience moderate seasonal fluctuations in our results of operations concentrated in the first and fourth fiscal quarters as the result of the concentration of the cough, cold and flu season and the holidays. We tailor certain front end merchandise to capitalize on holidays and seasons. We increase our inventory levels during our third fiscal quarter in anticipation of the seasonal fluctuations described above. Our results of operations in the fourth and first fiscal quarters may fluctuate based upon the timing and severity of the cough, cold and flu season, both of which are unpredictable.

**Regulation**

Our business is subject to federal, state, and local government laws, regulations and administrative practices. We must comply with numerous provisions regulating health and safety, equal employment opportunity, minimum wage and licensing for the sale of drugs, alcoholic beverages, tobacco and other products. In addition we must comply with regulations pertaining to product content, labeling, dating and pricing.

Pursuant to the Omnibus Budget Reconciliation Act of 1990 ("OBRA") and comparable state regulations, our pharmacists are required to offer counseling, without additional charge, to our customers about medication, dosage, delivery systems, common side effects and other information deemed significant by the pharmacists and may have a duty to warn customers regarding any potential adverse effects of a prescription drug if the warning could reduce or negate such effect.

The appropriate state boards of pharmacy must license our pharmacies and pharmacists. Our pharmacies and distribution centers are also registered with the Federal Drug Enforcement Administration and are subject to Federal Drug Enforcement Agency regulations relative to our pharmacy operations, including regulations governing purchasing, storing and dispensing of controlled substances. Applicable licensing and registration requirements require our compliance with various state statutes, rules and/or regulations. If we were to violate any applicable statute, rule or regulation, our licenses and registrations could be suspended or revoked or we could be subject to fines or penalties. Any such violation could also damage our reputation and brand.

In recent years, an increasing number of legislative proposals have been enacted (including the Patient Protection and Affordable Care Act), introduced or proposed in Congress and in some state legislatures that affect or would affect major changes in the healthcare system, either nationally or at the state level. The legislative initiatives include changes in reimbursement levels, changes in qualified participants, changes in drug safety regulations and e-prescribing. We cannot predict the timing of enactment of any such proposals to the extent not yet approved or the long-term outcome or effect of legislation from these efforts on our business.

Our pharmacy business is subject to patient privacy and other obligations, including corporate, pharmacy and associate responsibility imposed by the Health Insurance Portability and Accountability Act. As a covered entity, we are required to implement privacy standards, train our associates on the permitted uses and disclosures of protected health information, provide a notice of privacy practice to our pharmacy customers and permit pharmacy customers to access and amend their records and receive an accounting of disclosures of protected health information. Failure to properly adhere to these requirements could result in the imposition of civil as well as criminal penalties.

We are also subject to laws governing our relationship with our associates, including minimum wage requirements, overtime, working conditions and unionizing efforts. Increases in the federal minimum wage rate, associate benefit costs or other costs related to associates could adversely affect our results of operations.

In addition, in connection with the ownership and operations of our stores, distribution centers and other sites, we are subject to laws and regulations relating to the protection of the environment and

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### Table of Contents

health and safety matters, including those governing the management and disposal of hazardous substances and the cleanup of contaminated sites. Violations or liabilities under these laws and regulations as a result of our current or former operations or historical activities at our sites, such as gasoline service stations and dry cleaners, could result in significant costs.

### **Corporate Governance and Internet Address**

We recognize that good corporate governance is an important means of protecting the interests of our stockholders, associates, customers and the community. We have closely monitored and implemented relevant legislative and regulatory corporate governance reforms, including provisions of the Sarbanes-Oxley Act of 2002 ("Sarbanes-Oxley"), the rules of the SEC interpreting and implementing Sarbanes-Oxley and the corporate governance listing standards of the NYSE.

Our corporate governance information and materials, including our Certificate of Incorporation, Bylaws, Corporate Governance Guidelines, the charters of our Audit Committee, Compensation Committee and Nominating and Governance Committee, our Code of Ethics for the Chief Executive Officer and Senior Financial Officers, our Code of Ethics and Business Conduct and our Related Person Transaction Policy are posted on the corporate governance section of our website at [www.riteaid.com](http://www.riteaid.com) and are available in print upon request to Rite Aid Corporation, 30 Hunter Lane, Camp Hill, Pennsylvania 17011, Attention: Corporate Secretary. Our Board will regularly review corporate governance developments and modify these materials and practices as warranted.

Our website also provides information on how to contact us and other items of interest to investors. We make available on our website, free of charge, our annual reports on Form 10-K, quarterly reports on Form 10-Q, Extensible Business Reporting Language (XBRL) data files of our annual report and quarterly reports beginning with our fiscal 2011 second quarter 10-Q, current reports on Form 8-K and all amendments to these reports, as soon as reasonably practicable after we file these reports with, or furnish them to, the SEC. We do not intend for the information contained on our website to be part of this annual report on Form 10-K.

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

#### **Factors Affecting our Future Prospects**

Set forth below is a description of certain risk factors which we believe may be relevant to an understanding of us and our business. Security holders are cautioned that these and other factors may affect future performance and cause actual results to differ from those which may be anticipated. See "Cautionary Statement Regarding Forward-Looking Statements."

#### **Risks Related to our Financial Condition**

#### ***Current economic conditions may adversely affect our industry, business and results of operations.***

The United States economy is continuing to feel the impact of the economic downturn that began in late 2007, and the future economic environment may not fully recover to levels prior to the downturn. This economic uncertainty has and could further lead to reduced consumer spending for the foreseeable future. If consumer spending continues to decrease or does not recover, we may not be able to sustain the improvement in our same store sales. In addition, reduced or flat consumer spending may drive us and our competitors to offer additional products at promotional prices, which would have a negative impact on our gross profit. We operate a number of stores in areas that are experiencing a lower recovery than the economy on a national level. A continued softening or slow recovery in consumer spending may adversely affect our industry, business and results of operations. Reduced revenues as a result of decreased consumer spending may also reduce our liquidity and otherwise hinder our ability to implement our long term strategy.

Table of Contents

***We are highly leveraged. Our substantial indebtedness could limit cash flow available for our operations and could adversely affect our ability to service debt or obtain additional financing if necessary.***

We had, as of March 3, 2012, \$6.3 billion of outstanding indebtedness and stockholders' deficit of \$2.6 billion. We also had additional borrowing capacity under our \$1.175 billion senior secured revolving credit facility of approximately \$910.8 million, net of outstanding letters of credit of \$128.2 million. Our earnings were insufficient to cover fixed charges and preferred stock dividends for fiscal 2012, 2011, 2010, 2009 and 2008 by \$412.4 million, \$564.8 million, \$498.4 million, \$2.6 billion and \$340.6 million, respectively.

Our high level of indebtedness will continue to restrict our operations. Among other things, our indebtedness will:

limit our flexibility in planning for, or reacting to, changes in the markets in which we compete;

place us at a competitive disadvantage relative to our competitors with less indebtedness;

render us more vulnerable to general adverse economic, regulatory and industry conditions; and

require us to dedicate a substantial portion of our cash flow to service our debt.

Our ability to meet our cash requirements, including our debt service obligations, is dependent upon our ability to substantially improve our operating performance, which will be subject to general economic and competitive conditions and to financial, business and other factors, many of which are beyond our control. We cannot provide any assurance that our business will generate sufficient cash flow from operations to fund our cash requirements and debt service obligations.

We believe we have adequate sources of liquidity to meet our anticipated requirements for working capital, debt service and capital expenditures through fiscal 2013 and have no significant maturities prior to June 2014. However, if our operating results, cash flow or capital resources prove inadequate, or if interest rates rise significantly, we could face substantial liquidity problems and might be required to dispose of material assets or operations to meet our debt and other obligations or otherwise be required to delay our planned activities. If we are unable to service our debt or experience a significant reduction in our liquidity, we could be forced to reduce or delay planned capital expenditures and other initiatives, sell assets, restructure or refinance our debt or seek additional equity capital, and we may be unable to take any of these actions on satisfactory terms or in a timely manner. Further, any of these actions may not be sufficient to allow us to service our debt obligations or may have an adverse impact on our business. Our existing debt agreements limit our ability to take certain of these actions. Our failure to generate sufficient operating cash flow to pay our debts or refinance our indebtedness could have a material adverse effect on us.

***Borrowings under our senior secured credit facility are based upon variable rates of interest, which could result in higher expense in the event of increases in interest rates.***

As of March 3, 2012, approximately \$1.5 billion of our outstanding indebtedness bore interest at a rate that varies depending upon the London Interbank Offered Rate ("LIBOR"). Borrowings under our Tranche 5 Term Loan due March 2018 are subject to a minimum LIBOR floor of 125 basis points. Our Tranche 2 Term Loan due June 2014 and borrowings under our senior secured revolving credit facility are most sensitive to LIBOR fluctuations because there is no floor. If LIBOR rises, the interest rates on outstanding debt will increase. Therefore an increase in LIBOR would increase our interest payment obligations under those loans and have a negative effect on our cash flow and financial condition. We currently do not maintain hedging contracts that would limit our exposure to variable rates of interest.

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### Table of Contents

#### ***The covenants in the instruments that govern our current indebtedness may limit our operating and financial flexibility.***

The covenants in the instruments that govern our current indebtedness limit our ability to:

incur debt and liens;

pay dividends;

make redemptions and repurchases of capital stock;

make loans and investments;

prepay, redeem or repurchase debt;

engage in acquisitions, consolidations, asset dispositions, sale-leaseback transactions and affiliate transactions;

change our business;

amend some of our debt and other material agreements;

issue and sell capital stock of subsidiaries;

restrict distributions from subsidiaries; and

grant negative pledges to other creditors.

The senior secured credit facility contains covenants which place restrictions on the incurrence of debt beyond the restrictions described above, the payment of dividends, sale of assets, mergers and acquisitions and the granting of liens. Our credit facility has a financial covenant which requires us to maintain a minimum fixed charge coverage ratio. The covenant requires that, if availability on the revolving credit facility is less than \$150.0 million, we maintain a minimum fixed charge coverage ratio of 1.05 to 1.00. As of March 3, 2012, we had availability under our revolving credit facility of approximately \$910.8 million and were in compliance with the senior secured credit facility's financial covenant.

#### ***Our stockholders will experience dilution if we issue additional common stock.***

Subject to any required approval under the stockholder agreement (the "Stockholder Agreement") that we entered into at the time of the Brooks Eckerd acquisition, we are generally not restricted from issuing additional shares of our common shares or preferred stock, including, subject to the terms of our outstanding debt instruments, any securities that are convertible into or exchangeable for, or that represent the right to receive, common shares or preferred stock or any substantially similar securities, whether for cash, as part of incentive compensation or in refinancing transactions. Any additional future issuances of common stock will reduce the percentage of our common stock owned by investors who do not participate in such issuances. In most circumstances, stockholders will not be entitled to vote on whether or not we issue additional shares of common stock. The market price of our common stock could decline as a result of issuances of a large number of shares of our common stock or the perception that such issuances could occur.

***Subject to certain limitations, Jean Coudu Group may sell Rite Aid common stock at any time, which could cause our stock price to decrease.***

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The shares of Rite Aid common stock that the Jean Coutu Group currently holds are generally restricted, but Jean Coutu Group may sell these shares under certain circumstances, including pursuant to a registered underwritten public offering under the Securities Act or in accordance with Rule 144 under the Securities Act. On April 20, 2012, the Jean Coutu Group announced that it had disposed of



Table of Contents

56,000,000 of its 234,401,162 shares of our common stock. We have entered into a registration rights agreement with Jean Coutu Group, which will give Jean Coutu Group the right to require us to register all or a portion of its shares at any time (subject to certain exceptions). The sale of a substantial number of our shares by Jean Coutu Group or our other stockholders within a short period of time could cause our stock price to decrease, make it more difficult for us to raise funds through future offerings of Rite Aid common stock or acquire other businesses using Rite Aid common stock as consideration.

***We are in compliance with all New York Stock Exchange continued listing requirements. However, if we do not continue to maintain compliance with such requirements, our common stock may be delisted.***

On March 1, 2011, we were notified by the NYSE that, as of March 1, 2011, we regained compliance with the NYSE minimum share price listing requirement. We are now in compliance with all NYSE listing rules, have actively been taking steps to maintain our listing and expect our efforts to maintain our NYSE listing will be successful. However, there can be no assurance that we will maintain compliance with the NYSE minimum share price rule or other continued listing requirements. In the event of a delisting, all holders of our \$64.2 million of outstanding 8.5% Convertible Notes due May 2015 ("Convertible Notes") would be entitled to require us to repurchase their Convertible Notes. Our senior secured credit facility permits us to make such a repurchase of the Convertible Notes; provided that, before and after such transaction, no default or event of default shall have occurred and be continuing under the senior secured credit facility and we have more than \$100.0 million of availability under our revolving credit facility. Our ability to pay cash to holders of the Convertible Notes may be limited by our financial resources at the time of such repurchase. We cannot assure you that sufficient financing will be available on terms acceptable to us if necessary to make any required repurchase of the Convertible Notes.

**Risks Related to our Operations**

***We need to improve our operations in order to improve our financial condition, but our operations will not improve if we cannot effectively implement our business strategy or if our strategy is negatively affected by worsening economic conditions.***

We have not yet achieved the sales productivity level of our major competitors. We believe that improving the sales of existing stores is important to improving profitability and operating cash flow. If we are not successful in implementing our strategies, including our efforts to increase sales and further reduce costs, or if our strategies are not effective, we may not be able to improve our operations. In addition, any further adverse change or continued weakness in general economic conditions or major industries can adversely affect drug benefit plans and reduce our pharmacy sales. Adverse changes in general economic conditions could affect consumer buying practices and consequently reduce our sales of front end products, and cause a decrease in our profitability. Failure to improve operations or a continued weakness in major industries or general economic conditions would adversely affect our results of operations, financial condition and cash flows and our ability to make principal or interest payments on our debt.

***For so long as Jean Coutu Group (and, subject to certain conditions, certain members of the Coutu family) maintain certain levels of Rite Aid stock ownership, Jean Coutu Group (and, subject to certain conditions, certain members of the Coutu family) could exercise significant influence over us.***

At March 3, 2012, Jean Coutu Group owned approximately 25.2% of the voting power of Rite Aid. Jean Coutu Group (and, subject to certain conditions, certain members of the Coutu family) generally has the ability to significantly influence the outcome of any matter submitted for the vote of our stockholders. The Stockholder Agreement provides that Jean Coutu Group (and, subject to certain conditions, certain members of the Coutu family) has the right to designate three of the eleven

Table of Contents

members of our board of directors, subject to adjustment based on its ownership position in us. On April 20, 2012, the Jean Coutu Group announced that it had disposed of 56,000,000 of its 234,401,162 shares of our common stock. As a result of such sale, the Jean Coutu Group was required to cause one of its designees to immediately resign from our board of directors and Andre Belzile resigned from our board of directors effective April 23, 2012. Following Mr. Belzile's resignation and reduction of the size of our board of directors from eleven to ten members, the Jean Coutu Group will continue to have the right to designate two members of our board of directors, subject to adjustment for future reductions in its ownership position in us. Accordingly, Jean Coutu Group generally is, and is expected to continue to be, able to significantly influence the outcome of all matters that come before our board of directors. As a result of its significant interest in us, Jean Coutu Group may have the power, subject to applicable law (including the fiduciary duties of the directors designated by Jean Coutu Group), to significantly influence actions that might be favorable to Jean Coutu Group, but not necessarily favorable to our financial condition and results of operations. In addition, the ownership position and governance rights of Jean Coutu Group could discourage a third party from proposing a change of control or other strategic transaction concerning us.

***Conflicts of interest may arise between us and Jean Coutu Group, which may be resolved in a manner that adversely affects our business, financial condition or results of operations.***

Following the Brooks Eckerd acquisition, Jean Coutu Group has continued its Canadian operations but no longer has any operations in the United States, and we currently have no operations in Canada. Despite the lack of geographic overlap, conflicts of interest may arise between us and Jean Coutu Group in areas relating to past, ongoing and future relationships, including corporate opportunities, potential acquisitions or financing transactions, sales or other dispositions by Jean Coutu Group of its interests in us and the exercise by Jean Coutu Group of its influence over our management and affairs.

A number of the directors on our board of directors are persons who are also officers or directors of Jean Coutu Group or its subsidiaries. Service as a director or officer of both Rite Aid and Jean Coutu Group or its other subsidiaries could create conflicts of interest if such directors or officers are faced with decisions that could have materially different implications for Rite Aid and for Jean Coutu Group. Apart from the conflicts of interest policy contained in our Code of Ethics and Business Conduct and applicable to our directors, we and Jean Coutu Group have not established any formal procedures for us and Jean Coutu Group to resolve potential or actual conflicts of interest between us. There can be no assurance that any of the foregoing conflicts will be resolved in a manner that does not adversely affect our business, financial condition or results of operations.

***We are dependent on our management team, and the loss of their services could have a material adverse effect on our business and the results of our operations or financial condition.***

The success of our business is materially dependent upon the continued services of our executive management team. The loss of key personnel could have a material adverse effect on the results of our operations, financial condition or cash flows. Additionally, we cannot assure you that we will be able to attract or retain other skilled personnel in the future.

Table of Contents

***We are substantially dependent on a single wholesaler of branded pharmaceutical products to sell products to us on satisfactory terms. A disruption in this relationship may have a negative effect on our results of operations, financial condition and cash flow.***

We purchase all of our brand prescription drugs from a single wholesaler, McKesson, pursuant to a contract that runs through April 1, 2013. Pharmacy sales represented approximately 68.1% of our total sales during fiscal 2012, and, therefore, our relationship with McKesson is important to us. Any significant disruptions in our relationship with McKesson would make it difficult for us to continue to operate our business until we executed a replacement wholesaler agreement or developed and implemented self-distribution processes. There can be no assurance that we would be able to find a replacement wholesaler on a timely basis or that such a wholesaler would be able to fulfill our demands on similar terms, which would have a material adverse effect on our results of operations, financial condition and cash flows. In addition, because McKesson acts as a wholesaler for drugs purchased from ultimate manufacturers worldwide, any disruption in the supply of a given drug could adversely impact McKesson's ability to fulfill our demands, which would have a material adverse effect on our results of operations, financial condition and cash flows.

***A significant disruption in our computer systems or a cyber security breach could adversely affect our operations.***

We rely extensively on our computer systems to manage our ordering, pricing, point-of-sale, inventory replenishment and other processes. Our systems are subject to damage or interruption from power outages, computer and telecommunications failures, computer viruses, cyber security breaches, vandalism, severe weather conditions, catastrophic events and human error, and our disaster recovery planning cannot account for all eventualities. If our systems are damaged, fail to function properly or otherwise become unavailable, we may incur substantial costs to repair or replace them, and may experience loss of critical data and interruptions or delays in our ability to perform critical functions, which could adversely affect our business and results of operations. Any compromise of our security could also result in a violation of applicable privacy and other laws, significant legal and financial exposure, damage to our reputation, loss or misuse of the information and a loss of confidence in our security measures, which could harm our business.

#### **Risks Related to our Industry**

***The markets in which we operate are very competitive and further increases in competition could adversely affect us.***

We face intense competition with local, regional and national companies, including other drugstore chains, independently owned drugstores, supermarkets, mass merchandisers, dollar stores and internet pharmacies. Competition from discount stores and mail order has significantly increased during the past few years. Our industry also faces growing competition from companies who import drugs directly from other countries, such as Canada, as well as from large-scale retailers that offer generic drugs at a substantial discount. Some of our competitors have or may merge with or acquire pharmaceutical services companies or pharmacy benefit managers, which may further increase competition. We may not be able to effectively compete against them because our existing or potential competitors may have financial and other resources that are superior to ours. In addition, we may be at a competitive disadvantage because we are more highly leveraged than our competitors. The ability of our stores to achieve profitability depends on their ability to achieve a critical mass of loyal, repeat customers. We believe that the continued consolidation of the drugstore industry will further increase competitive pressures in the industry. We cannot assure you that we will be able to continue to effectively compete in our markets or increase our sales volume in response to further increased competition.

Table of Contents

***Consolidation in the healthcare industry could adversely affect our business, financial condition and results of operations.***

Many organizations in the healthcare industry, including pharmacy benefit managers, have consolidated or are in the process of consolidating, such as the recent merger of Express Scripts and Medco Health Solutions, to create larger healthcare enterprises with greater market power, which has resulted in greater pricing pressures. If this consolidation trend continues, it could give the resulting enterprises even greater bargaining power, which may lead to further pressure on the prices for our products and services. If these pressures result in reductions in our prices, our business will become less profitable unless we are able to achieve corresponding reductions in costs or develop profitable new revenue streams. We expect that market demand, government regulation, third-party reimbursement policies, government contracting requirements, and societal pressures will continue to cause the healthcare industry to evolve, potentially resulting in further business consolidations and alliances among the industry participants we engage with, which may adversely impact our business, financial condition and results of operations.

***Drug benefit plan sponsors and third party payors could change their plan eligibility criteria and further encourage or require the use of mail-order prescriptions which could decrease our sales and reduce our margins and have a material adverse effect on our business.***

An adverse trend for drugstore retailing has been initiatives to contain rising healthcare costs leading to the rapid growth in mail-order prescription processors. These prescription distribution methods have grown in market share relative to drugstores as a result of the rapid rise in drug costs experienced in recent years and are predicted to continue to rise. Mail-order prescription distribution methods are perceived by employers and insurers as being less costly than traditional distribution methods and are being encouraged, and, in some cases, required, by third party pharmacy benefit managers, employers and unions that administer benefits. As a result, some labor unions and employers are requiring, and others may encourage or require, that their members or employees obtain medications from mail-order pharmacies which offer drug prescriptions at prices lower than we are able to offer.

Another adverse trend for drugstore retailing has been for drug benefit plan sponsors and third party payors to change their plan eligibility requirements resulting in fewer beneficiaries covered and a reduction in the number of prescriptions allowed.

Mail-order prescription distribution and drug benefit plan eligibility changes have negatively affected sales for traditional chain drug retailers, including us, and we expect such negative effect to continue in the future. There can be no assurance that our efforts to offset the effects of mail order and eligibility changes will be successful nor can we predict whether the recently adopted health care reform legislation will exacerbate this risk.

***The availability of pharmacy drugs is subject to governmental regulations.***

The continued conversion of various prescription drugs, including the planned conversion of a number of popular medications, to over-the-counter medications may reduce our pharmacy sales and customers may seek to purchase such medications at non-pharmacy stores. Also, if the rate at which new prescription drugs become available slows or if new prescription drugs that are introduced into the market fail to achieve popularity, our pharmacy sales may be adversely affected. The withdrawal of certain drugs from the market or concerns about the safety or effectiveness of certain drugs or negative publicity surrounding certain categories of drugs may also have a negative effect on our pharmacy sales or may cause shifts in our pharmacy or front end product mix.

Table of Contents

***Changes in third party reimbursement levels for prescription drugs and changes in industry pricing benchmarks could reduce our margins and have a material adverse effect on our business.***

Sales of prescription drugs reimbursed by third party payors, including the Medicare Part D plans and state sponsored Medicaid and related managed care Medicaid agencies, represented 96.5% of our business in fiscal 2012.

The continued efforts of the Federal government, health maintenance organizations, managed care organizations, pharmacy benefit management companies, other State and local government entities, and other third-party payors to reduce prescription drug costs and pharmacy reimbursement rates, as well as litigation relating to how drugs are priced, may impact our profitability. In addition, some of these entities may offer pricing terms that we may not be willing to accept or otherwise restrict our participation in their networks of pharmacy providers. Any significant loss of third-party business could have a material adverse effect on our business and results of operations.

Certain provisions of the Deficit Reduction Act of 2005 ("DRA") sought to reduce federal spending by altering the Medicaid reimbursement formula for multi-source (i.e., generic) drugs ("AMP"). Although those reductions did not go into effect, the Patient Protection and Affordable Care Act, signed into law on March 23, 2010 (the "Patient Care Act") enacted a modified AMP reimbursement formula for multi-source drugs. The modified formula, when implemented, may reduce Medicaid reimbursements which could affect our revenues and profits. There have also been a number of other recent proposals and enactments by the Federal government and various states to reduce Medicare Part D and Medicaid reimbursement levels in response to budget problems. We expect other similar proposals in the future.

***We are subject to governmental regulations, procedures and requirements; our noncompliance or a significant regulatory change could adversely affect our business, the results of our operations or our financial condition.***

Our business is subject to numerous federal, state and local regulations. Changes in these regulations may require extensive system and operating changes that may be difficult to implement. Untimely compliance or noncompliance with applicable regulations could result in the imposition of civil and criminal penalties that could adversely affect the continued operation of our business, including: (i) suspension of payments from government programs; (ii) loss of required government certifications; (iii) loss of authorizations to participate in or exclusion from government reimbursement programs, such as the Medicare and Medicaid programs; (iv) loss of licenses; or (v) significant fines or monetary penalties. The regulations to which we are subject include, but are not limited to, federal, state and local registration and regulation of pharmacies; applicable Medicare and Medicaid regulations; the Health Insurance Portability and Accountability Act or ("HIPAA"); laws and regulations relating to the protection of the environment and health and safety matters, including those governing exposure to and the management and disposal of hazardous substances; regulations of the U. S. Federal Trade Commission, the U. S. Department of Health and Human Services and the Drug Enforcement Administration as well as state regulatory authorities, governing the sale, advertisement and promotion of products we sell; anti-kickback laws; false claims laws and federal and state laws governing the practice of the profession of pharmacy. We are also governed by federal and state laws of general applicability, including laws regulating matters of wage and hour laws, working conditions, health and safety and equal employment opportunity.

***Certain risks are inherent in providing pharmacy services; our insurance may not be adequate to cover any claims against us.***

Pharmacies are exposed to risks inherent in the packaging and distribution of pharmaceuticals and other healthcare products, such as with respect to improper filling of prescriptions, labeling of prescriptions, adequacy of warnings, unintentional distribution of counterfeit drugs and expiration of