

HealthWarehouse.com, Inc.  
Form 10-K  
April 15, 2011

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, 2010

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

For the transition period from \_\_\_\_\_.

Commission file number 0-13117

HEALTHWAREHOUSE.COM, INC.  
(Exact name of registrant as specified in its charter)

Delaware  
(State or other jurisdiction of  
incorporation or organization)

22-2413505  
(I.R.S. Employer  
Identification No.)

100 Commerce Boulevard, Cincinnati, Ohio  
(Address of principal executive offices)

45140  
(Zip Code)

Registrant's telephone number, including area code: (513) 618-0911

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

|                |   |
|----------------|---|
| Title of Class | Name of each exchange on which registered |
| None           | None                                      |

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

Common Stock, \$.001 par value  
(Title of Class)

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

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

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

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§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 (§229.405 of this chapter) is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K.

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer or a smaller reporting company. See definition of "accelerated filer" and "large accelerated filer" in Rule 12b-2 of the Act. (Check one):

Large accelerated filer  Accelerated filer  Non-accelerated filer  Smaller reporting company

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Act).

Yes  No

The aggregate market value of voting and nonvoting common equity held by non-affiliates, based on the closing price of the common stock, par value \$0.001 (the "Common Stock") on June 30, 2010 of \$2.80, as reported on the OTC Bulletin Board was approximately \$12,466,000. Shares of Common Stock held by each officer and director and by each person who owns 5% or more of the outstanding Common Stock have been excluded in that such persons may be deemed to be affiliates. This determination of affiliate status is not necessarily a conclusive determination for any other purpose.

There were 10,577,719 shares of Common Stock outstanding as of April 1, 2011.

DOCUMENTS INCORPORATED BY REFERENCE: None

## Information Regarding Forward-Looking Statements

This report contains “forward-looking statements” within the meaning of the Private Securities Litigation Reform Act of 1995 that involve risks and uncertainties, many of which are beyond our control. Our actual results could differ materially and adversely from those anticipated in such forward-looking statements as a result of certain factors, including those set forth in this report. Important factors that may cause actual results to differ from projections include, but are not limited to, for example:

- adverse economic conditions;
- inability to raise sufficient additional capital to operate our business;
- unexpected costs, lower than expected sales and revenues, and operating deficits;
- adverse results of any legal proceedings;
- the volatility of our operating results and financial condition;
- inability to attract or retain qualified senior management personnel; and
- other specific risks that may be referred to in this report.

All statements, other than statements of historical facts, included in this report regarding our strategy, future operations, financial position, estimated revenue or losses, projected costs, prospects and plans and objectives of management are forward-looking statements. When used in this report, the words “will,” “may,” “believe,” “anticipate,” “intend,” “estimate,” “expect,” “project,” “plan” and similar expressions are intended to identify forward-looking statements, although not all forward-looking statements contain such identifying words. All forward-looking statements speak only as of the date of this report. We undertake no obligation to update any forward-looking statements or other information contained herein. Stockholders and potential investors should not place undue reliance on these forward-looking statements. Although we believe that our plans, intentions and expectations reflected in or suggested by the forward-looking statements in this report are reasonable, we cannot assure stockholders and potential investors that these plans, intentions or expectations will be achieved. We disclose important factors that could cause our actual results to differ materially from our expectations under “Risk Factors” and elsewhere in this report. These cautionary statements qualify all forward-looking statements attributable to us or persons acting on our behalf.

Information regarding market and industry statistics contained in this report is included based on information available to us that we believe is accurate. It is generally based on academic and other publications that are not produced for purposes of securities reports or economic analysis. Forecasts and other forward-looking information obtained from these sources are subject to the same qualifications and the additional uncertainties accompanying any estimates of future market size, revenue and market acceptance of products and services. We have no obligation to update forward-looking information to reflect actual results or changes in assumptions or other factors that could affect those statements. See “Risk Factors” for a more detailed discussion of risks and uncertainties that may have an impact on our future results.

## PART I

### Item 1: Business.

#### Overview

We are a Verified Internet Pharmacy Practice Sites (“VIPPS”) accredited retail mail-order pharmacy and healthcare e-commerce company that sells discounted generic and brand name prescription drugs, as well as, over-the-counter (OTC) medical products. Our web address is <http://www.healthwarehouse.com>. At present, we sell:

- a range of prescription drugs (we are licensed as a mail-order pharmacy for sales to 50 states and the District of Columbia);

- diabetic supplies including glucometers, lancets, syringes and test strips;
- OTC medications covering a range of conditions from allergy and sinus to pain and fever to smoking cessation aids;
- home medical supplies including incontinence supplies, first aid kits and mobility aids; and
- diet and nutritional products including supplements, weight loss aids, and vitamins and minerals.

Our objectives are to make the pharmaceutical supply chain more efficient and to pass the savings on to the consumer. We are becoming known by consumers as a convenient, reliable, discount provider of over-the-counter and prescription medications and products. We intend to continue to expand our product line as our business grows. We are presently licensed as a mail-order pharmacy for sales to 50 states and the District of Columbia

Our customers tend to be under-insured or uninsured consumers who rely on our service for their daily medications. In addition, due to a trend of rising health insurance co-pays and with many prescription drugs going from brands to generics, our prices are often below the insurance co-pay. This makes it unnecessary for us to accept consumer insurance as a payment option, and we focus on cash-paying customers.

In March 2007, Hwareh.com, Inc. (“Old HW”), a Delaware corporation formerly named HealthWarehouse.com, Inc., was incorporated to carry on the business of selling OTC products. In November 2007, we began to develop the proprietary software necessary for our business, and in February 2008, version 1.0 of the <http://www.healthwarehouse.com> website was successfully launched running on our own proprietary software.

In March 2008, as part of our expansion into prescription drugs, we completed construction of a full service licensed pharmacy within our warehouse in Cincinnati, Ohio. The pharmacy includes a robot which counts and packages prescriptions. This machine can fill up to 1,200 prescriptions per day. Our pharmacy passed inspection by the Ohio State Pharmacy Board in April 2008.

Our growth strategy includes:

- aggressively marketing our website to customers both online and offline,
- expanding and hiring key personnel, and
- continuing to develop our proprietary software and technology.

#### Corporate Information and History

On May 14, 2009, we completed a share exchange transaction (the “Exchange”) with Clacendix, Inc. (“Clacendix”) pursuant to the terms of a Securities Exchange Agreement. Under the Securities Exchange Agreement, we acquired all the outstanding capital stock of Old HW. The consideration issued in the Exchange was determined as a result of arm’s-length negotiations between the parties.

As a result of the Exchange, Old HW became our subsidiary, with Old HW’s former stockholders acquiring approximately 82.4% of the then outstanding shares of our common stock. This transaction was accounted for as a reverse recapitalization, whereby Old HW is deemed to be the accounting acquirer for accounting purposes. Following the closing of the Exchange, the business of Old HW continues as our sole line of business. Effective August 5, 2009, we changed our corporate name to HealthWarehouse.com, Inc. Simultaneously, with our

name change, we changed the corporate name of our subsidiary to Hwareh.com, Inc. In connection with the name change, we also obtained a new ticker symbol for quotation on the OTC Bulletin Board (OTC BB), which is "HEWA.OB."

As part of the closing of the Exchange, we assumed Old HW's rights and obligations under Old HW convertible promissory notes with a principal value of \$1,200,000 and Old HW warrants to purchase our Common Stock. The Old HW convertible promissory notes and the Old HW warrants relate to Old HW's private placement in April and May 2009, under which Old HW completed a private placement to 18 investors of convertible promissory notes, for gross proceeds of \$1,200,000. During the period from November 2009 through January 2011, the Old HW convertible promissory notes were converted into approximately 792,000 shares of our Common Stock at a conversion price of approximately \$1.51 per share. As part of the private placement, Old HW issued warrants to purchase up to a maximum of 403,410 shares of our Common Stock. Of those Old HW warrants, a warrant to purchase 46,392 shares of our Common Stock at an exercise price of approximately \$0.022 was exercised, and warrants to purchase up to 357,018 shares of our Common Stock at an exercise price of approximately \$1.12 expired without being exercised.

Prior to the share exchange, Clacendix's predecessor company was formed as a New Jersey corporation in 1982 as MicroFrame, Inc. In March 1999 MicroFrame, Inc. was reincorporated in the State of Delaware and in the process changed its name to ION Networks, Inc. In December 2007, ION sold substantially all of its operating assets to Cryptek, Inc., a Delaware corporation. Pursuant to the Cryptek sale, ION changed its name to Clacendix, Inc. Following the date of the Cryptek sale and until the closing of our Exchange transaction with Old HW, Clacendix existed as a shell company with no operations that was seeking a target company with which to merge or to complete a business combination.

On December 15, 2009, we entered into a Loan and Security Agreement (the "Initial Loan Agreement") with HWH Lending LLC, a Delaware limited liability company (the "Lender"). Under the terms of the Initial Loan Agreement, we borrowed a total of \$1,015,000 from the Lender (the "Initial Loans"). We used the proceeds of the Initial Loans for working capital purposes. The Initial Loans bore interest at the rate of 12% per annum, payable at maturity. The maturity date of the Initial Loans was one year from the date of the Loans. The Initial Loans were exchanged in connection with the 2010 Private Placement described below. In consideration of the Initial Loans, the Company granted the Lender warrants to purchase a total of 625,000 shares of our Common Stock at a purchase price of \$1.60 per share. Each warrant may be exercised in whole or in part and from time to time for a term of five years from its grant date.

On July 16, 2010, we filed a Certificate of Amendment to our Certificate of Incorporation with the Secretary of State of the State of Delaware. The Certificate of Amendment effected a reverse split or combination of our Common Stock of one (1) share for every twenty (20) shares outstanding (the "Reverse Split"). As a result of the Reverse Split, every twenty (20) shares of Common Stock outstanding before the Reverse Split represents one share of Common Stock after the Reverse Split, with any fractional shares rounded up to the next whole share. The Certificate of Amendment also reduced the number of authorized shares of the Company's Common Stock from 750,000,000 to 50,000,000. Unless otherwise specifically indicated, all share numbers and all share price numbers presented in this Annual Report on Form 10-K have been adjusted to reflect the Reverse Split.

On November 8, 2010, we entered into a Securities Purchase Agreement (the "Purchase Agreement") with four accredited investors (the "Investors") and sold certain securities to the Investors in a non-public offering under Section 4(2) and under Rule 506 of Regulation D under the Securities Act of 1933 (the "2010 Private Placement"). Under the terms of the Purchase Agreement, we sold a total of 365,265 newly authorized shares of \$0.001 par value Series B Convertible Preferred Stock (the "Series B Convertible Preferred Stock") to the Investors at \$9.45 per share, for an aggregate price of approximately \$3,450,000. Each share of the Series B Convertible Preferred Stock may be converted at any time, in whole or in part, into five shares of our Common Stock, as adjusted. We also entered into a separate Loan and Security Agreement dated November 8, 2010 with two of the Investors (the "2010 Loan Agreement"). Under the terms of the 2010 Loan Agreement and the Purchase Agreement, we issued convertible promissory notes to those Investors in the aggregate principal amount of \$1,000,000 (the "Convertible Notes"). The

Convertible Notes bear interest at the rate of 7% per annum compounded annually. The principal amount and all accrued interest on the Convertible Notes are payable on December 31, 2012, or earlier on an event of default or a sale or liquidation of the Company. The principal amount and accrued interest on the Convertible Notes may be converted at any time into shares of Series B Convertible Preferred Stock at a conversion price of \$9.45 per share, as adjusted. Under the terms of the Purchase Agreement, we also issued warrants to the Investors, pro-rata to their investment amounts, to purchase an aggregate of 1,271,590 shares of our Common Stock at an exercise price of \$3.00 per share (the "Warrants"). Each Warrant may be exercised in whole or in part and from time to time for a term of five years from its grant date. We intend to use the net proceeds from the 2010 Private Placement to expand our online presence, upgrade our technology infrastructure, and pay existing indebtedness and accrued expenses, and for general working capital purposes.



On February 14, 2011, Hocks Acquisition Corporation (“Hocks Acquisition”), our newly formed wholly-owned subsidiary, entered into an Asset Purchase Agreement (the “Asset Purchase Agreement”) with Hocks Pharmacy Inc., an Ohio corporation (“Hocks Pharmacy”) and its shareholders. Under the Asset Purchase Agreement, Hocks Acquisition purchased all of the inventory and fixed assets (the “Purchased Assets”) owned by Hocks Pharmacy and used in the operation of its internet pharmacy business (the “Internet Business”). The Internet Business consists primarily of the internet sale of over-the-counter health and medical products and supplies. Hocks Acquisition paid \$200,000 in cash to Hocks Pharmacy for the Purchased Assets.

Also on February 14, 2011, we entered into a Merger Agreement (the “Merger Agreement”) with Hocks Pharmacy and its shareholders and Hocks.com Inc. (“Hocks.com”), a newly formed Ohio corporation and a wholly-owned subsidiary of Hocks Pharmacy. Under the Merger Agreement, Hocks Acquisition merged into Hocks.com and Hocks.com became our wholly-owned subsidiary. At the time of the Merger, Hocks.com owned all of the intangible assets of the Internet Business, including trademarks, domain names, customer accounts and goodwill. The merger consideration consisted of 166,667 shares of our Common Stock issued to Hocks Pharmacy.

### Our Business Model

Our business model seeks to improve both the efficiency and convenience by which consumers obtain prescription medications. To increase efficiency, we make efforts to source products from either the manufacturer or wholesaler level, eliminating unnecessary costs associated with distribution. In addition, we distribute medications to the consumer from a single warehouse, as opposed to retail locations, which we believe eliminates unnecessary costs such as real estate, rents, inventory, and personnel. By going directly to the consumer via the Internet, we reduce our marketing expense and increase convenience for consumers, especially those taking maintenance medications for conditions ranging from diabetes to high blood pressure.

| Current Healthcare<br>Distribution<br>Model | Our Distribution<br>Model |
|---|---------------------------|
| Manufacturer                                | Manufacturer              |
| ,   | ,                         |
| Wholesaler                                  | ,                         |
| ,   | ,                         |
| Distributor                                 | HealthWarehouse.com       |
| ,   | ,                         |
| Pharmacy                                    | ,                         |
| ,   | ,                         |
| Consumer                                    | Consumer                  |

Our target is consumers who are uninsured or underinsured, as well as, elderly patients in the Medicare “donut hole”. In addition, as insured consumers are seeing co-pays rise, many of our medications can be purchased for cash at prices less than the co-pay.

### Our Online Retail Mail-Order Pharmacy

We operate a full-service retail mail-order pharmacy within our warehouse in Cincinnati, Ohio. The pharmacy includes a robotic machine which counts and packages prescriptions that can fill up to 1,200 prescriptions per day. Our pharmacy passed inspection by the Ohio State Pharmacy Board and we are presently licensed as a mail-order pharmacy for sales to 50 states and the District of Columbia. Our retail mail-order pharmacy offers the

following advantages:

- Legitimacy. We have obtained certifications to separate ourselves from the many uncertified “rogue” pharmacies which exist. We are the 19th pharmacy in the U.S. to receive Verified Internet Practice Sites (VIPPS) certification, issued by the National Board of Pharmacies (NABP). Google, Yahoo, and Bing now all require VIPPS as a requirement to advertise on their sites.

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- **Convenience.** Our online store is available to consumers 24 hours a day, 7 days a week through the Internet. We deliver medications free of charge to any location in the United States including Alaska and Hawaii. We offer 6-month and 12-month supplies of medications to reduce the need for refills. All of our products are also available for purchase by phone. We offer additional convenience to our customers through an easy-to-use website, robust search technology, and a variety of features such as multiple checkout options including Google Checkout.
- **Selection.** Due to our online structure, we are able to offer a significantly broader assortment of products, with greater depth in each product category, because we do not have the shelf display space limitations of brick-and-mortar drugstores.
- **Information.** We provide a broad array of interactive tools and information on our website to help consumers make informed purchasing decisions. Our information services include detailed product information pages, product user manuals and brochures, links to manufacturer websites, detailed product descriptions which contain the manufacturer's phone number, and customer reviews. Our customer care representatives are available by phone or email to provide personal guidance and answer customers' questions.
- **Privacy.** When shopping at a "brick-and-mortar" drugstore, many consumers may feel embarrassed or uncomfortable about buying items or asking questions that may reveal personally sensitive aspects of their health or lifestyle to pharmacists, store personnel, or other shoppers. Our customers avoid these problems by shopping from the privacy of their home or office.
- **Value.** Our goal is to offer shoppers a broad assortment of generic drugs and health products with competitive pricing. We strive to improve our operating efficiencies and to leverage our fixed costs so that we can pass along the savings to our customers in the form of lower prices and exclusive deals. Since we source drugs direct from the manufacturer at the wholesale level, we believe that we have lower costs than traditional pharmacies which allows us to provide consumers with the better values. We also strive to inform customers of additional cost-saving opportunities when they become available. For example, we show the generic equivalents of all brand name products.
- **Customer Service.** Our focus has been on customer service and we endeavor to lead the industry in our policies and procedures. We currently offer a satisfaction guarantee with what we believe is an industry-leading 90-day return policy with no restocking fees, and 100% free standard shipping on all orders. We received the BizRate Circle of Excellence Award in 2009 and 2010 for exceptional customer service and satisfaction.

Our customer support representatives operate from our call center in Cincinnati, Ohio. Our customer support specialists are available 9 a.m. to 5 p.m. Eastern Standard Time, Monday through Friday, via e-mail, fax or telephone to handle customer inquiries and assist customers in finding desired products. Our online Help Center outlines store policies and provides answers to customers' frequently asked questions.

We ship our OTC products to all 50 states, the U.S. Territories, and APO/FPO military and embassy addresses. We process all orders from our primary distribution center in Cincinnati, Ohio. We based our logistics operation there to maintain proximity to UPS, located 90 miles away in Louisville, Kentucky, and FedEx, located in Memphis, Tennessee. Processing from this location allows us to reach 80% of the U.S. population by standard ground shipping in two days. In order to try to maintain high customer satisfaction ratings and quality control over the process, we avoid drop shipping of orders. Due to the relatively short lead time required to fill orders for our products, usually 24 to 48 hours, order backlog has not proven material to our business.

## Marketing and Sales

Our marketing strategy aims to build brand recognition, increase customer traffic to our online store, add new customers, build strong customer loyalty, maximize repeat purchases and develop incremental revenue opportunities. It is centered on Internet-based advertising.

Our online advertising campaigns focus on the following areas:

- Search Engines: Google, MSN and Yahoo;
- Price Comparison Engines: Become, Google Product Search, NexTag, PriceGrabber.com, Pronto, Shopping.com, Shopzilla, Smarter and Yahoo Shopping; and
- Social Networking: Facebook, Foursquare and Twitter.

To date, our online advertising has proven to be an effective sales strategy for our business. Apart from any personnel involved with our online advertising campaigns, we do not have a dedicated sales force.

### Suppliers

There are a number of suppliers available for the pharmaceutical and non-pharmaceutical products that we sell. Our principal suppliers are Masters Pharmaceutical, Inc., from which we source the majority of our supplies, Amerisource Bergen, Cardinal Health, Allison Medical, Inc., Masters Healthcare, LLC and Prescription Supply, Inc. While we source our supplies from a limited number of suppliers, we do not believe that our business is dependent on any one supplier since the products that we sell are readily available from a number of alternative suppliers. If a supplier, even if a significant supplier such as Masters Pharmaceutical, were to no longer be available to us, we believe that we could source replacement product through one or more alternative suppliers.

### Customers

We sell directly to the individual consumers of the pharmaceutical and non-pharmaceutical products that we sell. In addition, we work with an insurance company called Atlantis Health Plan based in New York, NY as well as self-insured companies. We are not dependent on any one or any few major customers.

### Seasonality

Historically, the largest amount of our net sales occurs during our fourth quarter. As a result, we sometimes experience an increase in our shipping cost due to complimentary upgrades, split-shipments, and additional long-zone shipments necessary to ensure timely delivery during this time of year.

### Competition

The market for prescription and OTC health products is intensely competitive and highly fragmented. Our competitors in the segment include chain drugstores, mail order pharmacies, pharmacy benefits managers (PBMs), mass market retailers, warehouse clubs and supermarkets. Many of these potential competitors in the market are also established organizations with greater access to resources and capital than we have. In addition, we face competition from foreign online pharmacies that can often sell drugs to U.S. residents at a lower price because they do not comply with U.S. pharmacy regulations, are not subject to U.S. regulatory oversight, or both. We also compete with Internet portals and online service providers that feature shopping services and with other online or mail-order retailers that offer products similar or the same to those that we sell.

We believe that the principal competitive factors in our market segments include brand awareness and preference, company credibility, product selection and availability, convenience, price, actual or perceived value, website features, functionality and performance, ease of purchasing, customer service, privacy, quality and quantity of information supporting purchase decisions (such as product information and reviews), and reliability and speed of

order shipment.

#### Intellectual Property and Technology

We filed for a trademark on the name “HealthWarehouse.com” on August 14, 2007 with the U.S. Patent and Trademark Office, which trademark was granted with a registration date of May 19, 2009. On February 14, 2011, we acquired the registered trademark “Hocks.com” in connection with our purchase of the online reseller business of Hocks Pharmacy Inc. We are continuing to use the Hocks.com trademark in connection with the online sale of over-the-counter health and medical supplies. We also rely on trade secret law and contractual restrictions to protect our intellectual property, and we do not intend to seek patent or copyright protection for our intellectual property at this time.

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We have implemented a broad array of services and systems for website management, product searching, customer interaction, transaction processing, and order fulfillment functions. These services and systems use a combination of our own proprietary technologies, open-source technologies and commercially-available, licensed technologies.

We focus our internal development efforts on creating and enhancing the specialized, proprietary software that is unique to our business. For example, our core merchandise catalog, as well as our customer interaction, order collection, fulfillment and back-end systems are proprietary to us. Our systems are designed to provide real-time connectivity to our distribution center systems for both pharmacy and OTC products. They include an inventory tracking system, a real-time order tracking system, an executive information system and an inventory replenishment system.

Our website at <http://www.healthwarehouse.com> is hosted on the Amazon EC2 platform due to the platform's perceived cost effectiveness and scalability. EC2 allows us to pay only for bandwidth used. In addition, due to Amazon's lengthy experience at running servers capable of serving one of the largest commerce sites on the web, our site remains scalable on days where our traffic spikes.

Our website was developed using 100% open source code. We use a 100% open source platform which runs on Linux, Apache, MySQL and PHP (LAMP).

In addition, we have utilized open source software from other vendors to speed up our development time. For management of our content and commerce catalog, we utilize Magento, an open source e-commerce platform. For our reporting and tools, we utilize Google Analytics. Our checkout process has two options including Google Checkout for OTC orders and our own proprietary checkout for OTC and prescription orders which uses Authorize.net.

#### Government Regulation

Federal and state laws and regulations govern many aspects of our business and are specific to pharmacies and the sale of OTC drugs. Our pharmacy passed inspection by the Ohio State Pharmacy Board and we are presently licensed as a mail-order pharmacy for sales to 50 states and the District of Columbia. We ship our non-prescription products to all 50 states, the U.S. Territories, and APO/FPO military and embassy addresses.

We believe we are in substantial compliance with all existing legal and regulatory requirements material to the operation of our business. We have standard operating procedures and controls designed to assist in ensuring compliance with existing contractual requirements and state and federal law. We diligently monitor and audit our adherence to these procedures and controls, and we take prompt corrective and disciplinary action when appropriate. However, we cannot predict how courts or regulatory agencies may interpret existing laws or regulations or what additional federal or state legislation or regulatory initiatives may be enacted in the future regarding healthcare or the pharmacy industry, and the application of complex standards to the operation of our business creates areas of uncertainty.

In addition, we may in the future participate in federal and state programs such as Medicare and Medicaid. If we do, we would be subject to extensive government regulation including numerous state and federal laws and corresponding regulations directed at preventing fraud and abuse and regulating reimbursement.

Among the federal and state laws and regulations that currently affect or may reasonably affect in the future aspects of our business are the following:





### Regulation of Our Pharmacy Operations.

The practice of pharmacy is generally regulated at the state level by state boards of pharmacy. Our pharmacy must be licensed in the state in which it is located. In some states, regulations require compliance with standards promulgated by the United States Pharmacopeia (USP). The USP creates standards in the packaging, storage and shipping of pharmaceuticals. Also, many of the states where we deliver pharmaceuticals, including controlled substances, have laws and regulations that require out-of-state mail-order pharmacies to register with that state's board of pharmacy or similar regulatory body. In addition, some states have proposed laws to regulate online pharmacies, and we may be subject to this legislation if it is passed. Furthermore, if our pharmacy dispenses durable medical equipment items, such as infusion pumps, that bear a federal legend requiring dispensing pursuant to a prescription, we would also be regulated by applicable state and federal durable medical equipment laws.

Federal agencies further regulate our pharmacy operations. Pharmacies must register with the Drug Enforcement Administration (DEA) and individual state controlled substance authorities in order to dispense controlled substances. Currently, we do not sell any controlled substances and therefore do not require a DEA license. In addition, the FDA inspects facilities in connection with procedures to effect recalls of prescription drugs. The Federal Trade Commission (FTC) also has requirements for mail-order sellers of goods. The U.S. Postal Service (USPS) has statutory authority to restrict the transmission of drugs and medicines through the mail to a degree that could have an adverse effect on our mail-order operations. The USPS historically has exercised this statutory authority only with respect to controlled substances. If the USPS restricts our ability to deliver drugs through the mail, alternative means of delivery are available to us. However, alternative means of delivery could be significantly more expensive. The Department of Transportation has regulatory authority to impose restrictions on drugs inserted in the stream of commerce. These regulations generally do not apply to the USPS and its operations.

Additionally, under the Omnibus Budget Reconciliation Act of 1990 and related state and local regulations, our pharmacists are required to offer counseling to our customers about medication, dosage, delivery systems, common side effects, adverse effects or interactions and therapeutic contraindications, proper storage, prescription refill and other information deemed significant by the pharmacists. We are also subject to requirements under the Controlled Substances Act and federal DEA regulations, as well as related state and local laws and regulations, relating to our pharmacy operations, including registration, security, recordkeeping and reporting requirements related to the purchase, storage and dispensing of controlled substances, prescription drugs and some OTC drugs.

“Compendial standards,” which can also be called “official compendium,” means the standards for drugs related to strength, purity, weight, quality, labeling and packing contained in the official Pharmacopeia of the United States, official National Formulary, or any supplement to any of them. Under the Food, Drug and Cosmetic Act of 1938, a drug recognized by the Homeopathic Pharmacopeia of the United States must meet all compendial standards and labeling requirements contained therein, or it will be considered adulterated (for example, lacking appropriate strength, quality or purity; or containing poisonous or unsanitary ingredients) or misbranded (for example, having a false or misleading label; or a label containing an inaccurate description of contents). If we add homeopathic remedies to our product offerings, we will be required to comply with the Food, Drug and Cosmetic Act. The distribution of adulterated or misbranded homeopathic remedies or other drugs is prohibited under the Food, Drug and Cosmetic Act, and violations could result in substantial fines and other monetary penalties, seizure of the misbranded or adulterated items, and/or criminal sanctions.

We also are required to comply with the Dietary Supplement Health and Education Act when selling dietary supplements and vitamins.

We believe that our operations have the appropriate licenses required under the laws of the states in which they are located and that we conduct our pharmacy operations in accordance with the laws and regulations of these states.

## Drug Importation

In the face of escalating costs for plan sponsors providing a prescription drug benefit for their employees, and uninsured individuals seeking to lower their drug costs, the issue of importing drugs from Canada or other foreign countries has received significant attention. Drug importation, sometimes called drug re-importation, occurs when prescription medicines from other countries are imported for personal use or commercial distribution. Individual importation activities are generally prohibited under U.S. law, and the FDA has issued warnings and safety alerts to a number of entities seeking to promote or facilitate systematic importation activities. However, there has been considerable legislative and political activity seeking to change the FDA requirements to enable drug importation, and we are evaluating appropriate actions if such legislation were to be enacted.

### Health Management Services Regulation

All states regulate the practice of medicine and require licensing under applicable state law. It is not our intent to practice medicine and we have tried to structure our website and our business to avoid violation of state licensing requirements. However, the application of this area of the law to Internet services such as ours is not well established and, accordingly, a state regulatory authority could at some time allege that some portion of our business violates these statutes. Any such allegation could harm our business. Further, any liability based on a determination that we engaged in the unlawful practice of medicine may be excluded from coverage under the terms of our general liability insurance policy.

### Consumer Protection Laws

Most states have consumer protection laws designed to ensure that information provided to consumers is adequate, fair and not misleading. We believe that our practices conform to the requirements of state consumer protection laws. However, we may be subject to further scrutiny under these laws as they are often interpreted broadly.

### Regulation Relating to Data Transmission and Confidentiality of Patient Identifiable Information

Dispensing of prescriptions and management of prescription drug benefits require the ability to utilize patient-specific information. Government regulation of the use of patient identifiable information has grown substantially over the past several years. At the federal level, Congress enacted the Health Insurance Portability and Accountability Act of 1996 (HIPAA), which extensively regulates the transmission, use and disclosure of health information by all participants in healthcare delivery, including physicians, hospitals, insurers and other payors. Our pharmacy operations are covered entities, which are directly subject to these requirements. Additionally, regulation of the use of patient-identifiable information is likely to increase. Congress is currently reviewing proposals that would alter HIPAA, which would create additional administrative burdens. Many states have passed or are considering laws addressing the use and disclosure of health information. These proposals vary widely, some relating to only certain types of information, others to only certain uses, and yet others to only certain types of entities. These laws and regulations have a significant impact on our operations, products and services, and compliance with them is a major operational requirement. Regulations and legislation that severely restrict or prohibit our use of patient identifiable information could materially adversely affect our business.

Sanctions for failing to comply with HIPAA standards include criminal and civil penalties. If we are found to have violated any state or federal statute or regulation with regard to the confidentiality, dissemination or use of patient medical information, we could be liable for significant damages, fines or penalties.

### Fraudulent Billing, Anti-Kickback, Stark, Civil Monetary Penalties and False Claims Laws and Regulations

Our operations may in the future participate in federal and state programs such as Medicare and Medicaid. If we do, we would be subject to extensive government regulation including numerous state and federal laws and corresponding regulations directed at preventing fraud and abuse and regulating reimbursement. The government's Medicare and Medicaid regulations are complex and sometimes subjective and therefore may require our management's interpretation. If we were to participate in federal and state programs such as Medicare and Medicaid, our compliance with Medicare and Medicaid regulations may be reviewed by federal or state agencies, including the Department of Health and Human Services' (HHS) Office of the Inspector General (OIG), the Centers for Medicare and Medicaid Services (CMS), the Department of Justice (DOJ), and the FDA. To ensure compliance with Medicare, Medicaid and other regulations, government agencies conduct periodic audits to ensure compliance with various supplier standards and billing requirements. Similarly, regional health insurance carriers routinely conduct audits and request patient records and other documents to support claims submitted for payment.



Federal law prohibits the payment, offer, receipt or solicitation of any remuneration that is knowingly and willfully intended to induce the referral of Medicare, Medicaid or other federal healthcare program beneficiaries for the purchase, lease, ordering or recommendation of the purchase, lease or ordering of items or services reimbursable under federal healthcare programs. These laws are commonly referred to as anti-remuneration or anti-kickback laws. Several states also have similar laws, known as “all payor” statutes, which impose anti-kickback prohibitions on services not covered by federal healthcare programs. Anti-kickback laws vary between states, and courts have rarely interpreted them.

Courts, the OIG and some administrative tribunals have broadly interpreted the federal anti-kickback statute and regulations. Courts have ruled that a violation of the statute may occur even if only one of the purposes of a payment arrangement is to induce patient referrals or purchases. Should we enter the government payor sector, it is possible that our current practices in the commercial sector may not be appropriate in the government payor sector.

The Ethics in Patient Referrals Law (Stark Law) prohibits physicians from making a referral for certain health items or services if they, or their family members, have a financial relationship with the entity receiving the referral. No bill may be submitted in connection with a prohibited referral. Violations are punishable by civil monetary penalties upon both the person making the referral and the provider rendering the service. Such persons or entities are also subject to exclusion from Medicare and Medicaid. Many states have adopted laws similar to the Stark Law, which restrict the ability of physicians to refer patients to entities with which they have a financial relationship.

The Federal False Claims Act prohibits the submission of a false claim or the making of a false record or statement in order to secure a reimbursement from a government-sponsored program. In recent years, the federal government has launched several initiatives aimed at uncovering practices that violate false claims or fraudulent billing laws. Civil monetary penalties may be assessed for many types of conduct, including conduct that is outlined in the statutes above and other federal statutes in this section. Under the Deficit Reduction Act of 2005 (DRA), states are encouraged to pass state false claims act laws similar to the federal statute.

Sanctions for fraudulent billing, kickback violations, Stark’s law violations or violations of the False Claims Act include criminal or civil penalties. If we do participate in federal payor programs and are found to have violated any state or federal kickback, Stark Law or False Claims Act law, we could be liable for significant damages, fines or penalties and potentially be ineligible to participate in federal payor programs.

#### Legislation and Regulation Affecting Drug Prices and Potentially Affecting the Market for Prescription Benefit Plans and Reimbursement for Durable Medical Equipment

Recently, the federal government has increased its focus on methods drug manufacturers employ to develop pricing information, which in turn is used in setting payments under the Medicare and Medicaid programs. One element common to many payment formulas, the use of “average wholesale price” (AWP) as a standard pricing unit throughout the industry, has been criticized as not accurately reflecting prices actually charged and paid at the wholesale or retail level. The DOJ is currently conducting, and the House Commerce Committee has conducted, an investigation into the use of AWP for federal program reimbursement, and whether the use of AWP has inflated drug expenditures by the Medicare and Medicaid programs. Federal and state proposals have sought to change the basis for calculating reimbursement of certain drugs by the Medicare and Medicaid programs.

The DRA revised the formula used by the federal government to set the Federal Upper Limit (FUL) for multiple source drugs by adopting 250 percent of the average manufacturer’s price (AMP) without regard to customary prompt pay discounts to wholesalers for the least costly therapeutic equivalent. On July 17, 2006, HHS published a Final Rule for the Medicaid Prescription Drug Program implementing the DRA in which AMP was defined to exclude discounts and rebates to pharmacy benefit managers and include sales to mail-order and specialty pharmacies in the AMP

calculation by manufacturers.

These proposals and other legislative or regulatory adjustments that may be made to the program for reimbursement of drugs by Medicare and Medicaid, if implemented, could affect our ability to negotiate discounts with pharmaceutical manufacturers. They could also impact the reimbursement we may receive from government payors in the future. In addition, they may affect our relationships with health plans. In some circumstances, they might also impact the reimbursement that we would receive from managed care organizations that contract with government health programs to provide prescription drug benefits or otherwise elect to rely on the revised pricing information. Furthermore, private payors may choose to follow the government's example and adopt different drug pricing bases. This could affect our ability to negotiate with plans, manufacturers and pharmacies regarding discounts and rebates.

Relative to our durable medical equipment operations, The Medicare Prescription Drug, Improvement and Modernization Act of 2003 (DIMA), established a program for the competitive acquisition of certain covered items of durable medical equipment, prosthetics, orthotics and supplies (DMEPOS). Diabetes testing supplies, including test strips and lancets, which are commonly supplied via mail-order delivery, are subject to the competitive acquisition program. Only qualified suppliers that meet defined participation standards specified in the final rule will be permitted to engage in the competitive acquisition program. In 2010, mail-order diabetes testing supplies may be subject to a national or regional program, which would require mail-order suppliers to bid on supplying certain DMEPOS items.

#### Medicare Part D and Part B; State Prescription Drug Assistance Programs

The DIMA also offers far-reaching changes to the Medicare program. The DIMA established a new Medicare Part D outpatient prescription drug benefit for over 40 million Americans who are eligible for Medicare. Qualified beneficiaries, including senior citizens and disabled individuals, have had the opportunity to enroll in Medicare Part D since January 1, 2006.

In addition, many states have expanded state prescription drug assistance programs to increase access to drugs by those currently without coverage and/or supplement the Medicare Part D benefit of those with coverage to offer options for a seamless benefit. In accordance with applicable CMS requirements, to participate we may have to enter into agreements with a number of state prescription drug assistance programs and collaborate to coordinate benefits with Medicare Part D plans.

#### Industry Standards for Pharmacy Operations

The National Committee on Quality Assurance, the American Accreditation Health Care Commission (known as URAC), the Joint Commission on Accreditation of Healthcare Organizations and other quasi-regulatory and accrediting bodies have developed standards relating to services performed by pharmacies, including mail order, formulary, drug utilization management and specialty pharmacy. While the actions of these bodies do not have the force of law, pharmacy benefit managers and many clients for pharmacy benefit manager services seek certification from them, as do other third parties. These bodies may influence the federal government or states to adopt requirements or model acts that they promulgate. The federal government and some states incorporate accreditation standards of these bodies, as well as the standards of the National Association of Insurance Commissioners and the National Association of Boards of Pharmacy, a coalition of state pharmacy boards, into their drug utilization review regulation. Future initiatives of these bodies are uncertain, and resulting standards or legislation could impose restrictions on us in a manner that could significantly impact our business.

The National Association of Boards of Pharmacy has also developed a program, the Verified Internet Pharmacy Practice Sites, as a model for self-regulation for online pharmacies. We believe we comply with its criteria for certification.

#### Employees

As of March 1, 2011, we employed 31 full-time employees and 2 part-time employees. None of our employees are subject to a collective bargaining agreement and we believe that relations with our employees are good. The Company at December 31, 2010 has 7 non-contractual laborers.

Item 1A: Risk Factors.

Risks Relating to Our Business and Industry

We have a limited operating history, a history of generating significant losses, and may not be able to sustain profitability.

Old HW, which now constitutes our principal business, was formed in March 2007 and has a limited operating history upon which you can evaluate our business and prospects. To date, we have not been profitable, and we may never achieve profitability on a full-year or consistent basis. We incurred net losses of \$3,691,674 for the year ended December 31, 2010 and \$2,439,502 for the year ended December 31, 2009. Although our management anticipates that we should achieve operating cash flow breakeven during 2011, if our plans or assumptions change or prove to be inaccurate, we may continue to incur net losses in 2011, and possibly longer. As a result, investors may lose all or a part of their investment.

We may experience significant fluctuations in our operating results and rate of growth.

Our evolving business model and the unpredictability of our industry make it difficult for us to forecast accurately the level or source of our revenues and our rate of growth. Our financial projections are based on assumptions and estimates that inherently are subject to significant business, economic, competitive, regulatory and operational uncertainties, contingencies and risks, many of which are beyond our control. Our projections assume the success of our business strategy. The success of this strategy is subject to uncertainties and contingencies beyond our control, and we cannot assure you that the strategy will be successful or that the anticipated benefits from the strategy will be realized in the manner or during the periods reflected in our projections or at all. These uncertainties may result in material changes in our financial condition and results of operations, which may differ materially from our projections.

Our revenues and operating results may vary significantly from quarter to quarter.

Our revenues and operating results may vary significantly from quarter to quarter due to a number of factors, including:

- our ability to retain and increase sales to existing customers, attract new customers, and satisfy our customers' demands;
- the frequency and size of customer orders and the quantity and mix of OTC and prescription products our customers purchase;
  - changes in demand with respect to existing and new OTC and prescription products;
  - changes in consumer acceptance and usage of the Internet, online services, and e-commerce;
- the price we charge for our OTC and prescription products and for shipping those products, or changes in our pricing policies or the pricing policies of our competitors;
  - the extent to which we offer free shipping or other promotional discounts to our customers;
  - our ability to acquire merchandise, manage inventory, and fulfill orders;



- technical difficulties, system downtime, or interruptions;
- timing and costs of upgrades and developments in our systems and infrastructure;
- timing and costs of marketing and other investments;
- disruptions in service by shipping carriers;
- the introduction by our competitors of new websites, products, or services;
- the extent of reimbursements available from third-party payors; and

- changes in government regulation.

In addition, our operating expenses are largely based on anticipated revenue trends and a high percentage of our expenses are fixed in the short term. As a result, a delay in generating or recognizing revenue for any reason could result in substantial additional operating losses.

We face significant competition from both traditional and online domestic pharmaceutical and medical product retailers.

The market segments in which we compete are rapidly evolving and intensely competitive, and we have many competitors in different industries, including both the retail and e-commerce services industries. These competitors include chain drugstores, mass market retailers, warehouse clubs, supermarkets, specialty retailers, major department stores, insurers and health care providers, mail-order pharmacies, Internet portals and online service providers that feature shopping services, and various online stores that offer products within one or more of our product categories. Many of our current and potential competitors have longer operating histories, larger customer bases, greater brand recognition, and significantly greater financial, marketing, and other resources than we have. They may be able to secure merchandise from vendors on more favorable terms, operate with a lower cost structure, adopt more aggressive pricing policies, or devote more resources to technology development and marketing than we do. In addition, other companies in the retail and e-commerce service industries may enter into business combinations or alliances that would strengthen their competitive positions and prevent them, their affiliated companies, or their strategic partners from entering into relationships with us. For example, our inability to enter into or maintain relationships with major insurance companies or managed care organizations could be a major competitive disadvantage to us.

We face competition from online pharmacies outside the United States.

Although it is currently illegal to re-import prescription drugs into the United States from any foreign country, we nonetheless face competition from online pharmacies outside the United States. A growing number of U.S. consumers seek to fill their prescriptions through Canadian and other foreign online pharmacies, and a number of state and local governments have set up websites directing their constituents to Canadian pharmacies. The FDA has taken only limited action to date, and may not take aggressive action in the future, against those who illegally re-import prescription drugs or support or facilitate illegal re-importation. In the U.S. Congress, legislation allowing for re-importation of prescription drugs by individuals for personal use has repeatedly been introduced. If such legislation were to be enacted, or if consumers increasingly use foreign-based online prescription drug websites instead of U.S.-based online pharmacies, such as ours, to fill their prescription needs, our business and operating results could be harmed.

We may be unable to increase the migration of consumers of health and pharmacy products from brick-and-mortar stores to our online solution, which would harm our revenues and prevent us from becoming profitable.

If we do not attract and retain higher volumes of customers to our Internet store at a reasonable cost, we will not be able to increase our revenues or achieve consistent profitability. Our success depends on our ability to continue to convert a large number of customers from traditional shopping methods to online shopping for health and pharmacy products. Specific factors that could prevent widespread customer acceptance of our online solution include:

- shipping charges, which do not apply to purchases made at a “brick-and-mortar” store;
- delivery time associated with Internet orders, as compared to the immediate receipt of products at a brick-and-mortar store;

- lack of consumer awareness of our website;
- additional steps and delays in verifying prescriptions and ensuring insurance coverage for prescription products;

- non-participation in the networks of some insurance carriers;
- regulatory restrictions or reform at the state and federal levels that could affect our ability to serve our customers;
- the general acceptance or legalization of prescription drug re-importation;
- customer concerns about the security of online transactions, identity theft, or the privacy of their personal information;
- product damage from shipping or shipments of wrong or expired products from us or other vendors, resulting in a failure to establish, or loss of, customers' trust in buying drugstore items online;
- inability to serve the acute care needs of customers, including emergency prescription drugs and other urgently needed products;
  - delays in responses to customer inquiries;
  - difficulties or delays in returning or exchanging orders; and
- activity that diminishes a user's online experience or subjects online shoppers to security risks, such as viruses, spam, spyware, phishing (spoofing e-mails directed at Internet users), "denial of service" attacks directed at Internet service providers and online businesses, and breaches of data security.

If our marketing efforts are not effective at attracting and retaining customers at an acceptable cost, we will be unable to achieve profitability.

If we do not maintain our brand and continue to increase awareness of our Internet shopping presence, we may not build a critical mass of customers. Promoting and positioning our brand depends largely on the success of our marketing efforts and our ability to provide consistent, high quality customer experiences. We believe that, because we are a small company with low public brand awareness, achieving significant market awareness will require significant marketing expense. To promote our brand and our products and services, we have incurred and expect to continue to incur substantial expense in our marketing efforts both to attract and to retain customers. Our promotional activities may not be effective at building our brand awareness and customer base to the extent necessary to generate sufficient revenue to become consistently profitable. Search engine and other online marketing initiatives comprise a substantial part of our marketing efforts, and our success depends in part on our ability to manage costs associated with these initiatives, or to find other channels to acquire and retain customers cost-effectively. The demand for and cost of online advertising has been increasing and may continue to increase. An inability to acquire and retain customers at a reasonable cost would increase our operating costs and prevent us from achieving profitability.

Since our business is Internet-based, we are vulnerable to system interruption and damage, which would harm our operations and reputation.

Our ability to receive and fulfill orders promptly and accurately is critical to our success and largely depends on the efficient and uninterrupted operation of our computer and communications hardware and software systems. We experience periodic system interruptions that impair the performance of our transaction systems or make our website inaccessible to our customers. These systems interruptions delay us from efficiently accepting and fulfilling orders, sending out promotional e-mails and other customer communications in a timely manner, introducing new products and features on our website, promptly responding to customers, or providing services to third parties. Frequent or persistent interruptions in our services could cause current or potential customers to believe that our systems are

unreliable, which could cause them to avoid our website, drive them to our competitors, and harm our reputation. To minimize future system interruptions, we need to continue to add software and hardware and to improve our systems and network infrastructure to accommodate increases in website traffic and sales volume, to replace aging hardware and software, and to make up for two years of underinvestment in technology. We may be unable to promptly and effectively upgrade and expand our systems and integrate additional functionality into our existing systems. Any unscheduled interruption in our services could result in fewer orders, additional operating expenses, or reduced customer satisfaction, any of which would harm our revenues and operating results and could delay or prevent our becoming consistently profitable. In addition, the timing and cost of upgrades to our systems and infrastructure may substantially affect our ability to achieve or maintain profitability.

All of our fulfillment operations and inventory are located in our distribution facility, and any significant disruption of this center's operations would hurt our ability to make timely delivery of our products.

We conduct all of our fulfillment operations from our distribution facility in Cincinnati, Ohio, which houses our entire product inventory. A natural disaster or other catastrophic event, such as an earthquake, fire, flood, severe storm, break-in, server or systems failure, terrorist attack, or other comparable event at this facility, would cause interruptions or delays in our business and loss of inventory and could render us unable to process or fulfill customer orders in a timely manner, or at all. Further, we have no formal disaster recovery plan, and our business interruption insurance may not adequately compensate us for losses that may occur. In the event that a significant part of this facility was destroyed or our operations were interrupted for any extended period of time, our business, financial condition, and operating results would be harmed.

Our operating results will be harmed if we are unable to manage and sustain our growth.

Our business is unproven on a large scale and actual operating margins may be less than expected. If we are unable to scale capacity efficiently, we may fail to achieve expected operating margins, which would have an adverse effect on our operating results.

If we are unable to obtain shipments of products from our vendors, our business and results of operations would be harmed.

We have significant vendors that are important to our sourcing of pharmaceutical and non-pharmaceutical products. We do not have long-term arrangements with most of our vendors to guarantee availability of merchandise, particular payment terms, or extension of credit limits. If our current vendors were to stop selling merchandise to us on acceptable terms, we may not be able to acquire merchandise from other vendors in a timely and efficient manner and on acceptable terms, or at all.

We have significant inventory risk.

We must maintain sufficient inventory levels to operate our business successfully and to meet our customers' expectations that we will have the products they order in stock. However, we must also guard against the risk of accumulating excess inventory. We are exposed to significant inventory risk as a result of rapid changes in product cycles, changes in consumer tastes, uncertainty of success of product launches, seasonality, manufacturer backorders, and other vendor-related problems. In order to be successful, we must accurately predict these trends and events, which we may be unable to do, and avoid over- or under-stocking products. In addition, demand for products can change significantly between the time product inventory is ordered and the time it is available for sale. When we begin selling a new product, it is particularly difficult to forecast product demand accurately. A failure to optimize inventory would increase our expenses if we have too much inventory, and would harm our margins by requiring us to make split shipments for backordered items or pay for expedited delivery from the manufacturer if we had insufficient inventory. In addition, we may be unable to obtain certain products for sale on our website as a result of general shortages (for example, in the case of some prescription drugs), manufacturer policies (for example, in the case of some contact lenses and prestige beauty items), manufacturer or distributor problems, or popular demand. Failure to have inventory in stock when a customer orders it could cause us to lose that order or that customer. The acquisition of some types of inventory, or inventory from some of our sources, may require significant lead time or prepayment, and this inventory may not be returnable. We carry a broad selection of products and significant inventory levels of a substantial number of products, and we may be unable to sell this inventory in sufficient quantities or during the relevant selling seasons. The occurrence of one or more of these inventory risks may adversely affect our business and operating results.



If we make an error in filling or packaging the prescription drugs that we sell, we would be subject to liability and negative publicity.

Errors relating to prescriptions, dosage, and other aspects of the prescription medication could result in liability for us that our insurance may not cover. Because we distribute pharmaceutical products directly to the consumer, we are one of the most visible participants in the distribution chain and therefore have increased exposure to liability claims. Our pharmacists are required by law 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. Our pharmacists may have a duty to warn customers regarding any potential adverse effects of a prescription drug if the warning could reduce or negate those effects. This counseling is in part accomplished through e-mails to our customers and inserts included with the prescription, which may increase the risk of miscommunication because the customer is not personally present to receive the counseling or advice or may not have provided us with all relevant information. Although we also post product information on our website, customers may not read this information. Providing information on pharmaceutical and other products creates the potential for claims to be made against us for negligence, personal injury, wrongful death, product liability, malpractice, invasion of privacy, or other legal theories based on our product or service offerings. Our general liability and business owners' liability insurance may not cover potential claims of this type or may not be adequate to protect us from all liabilities that may be imposed if any such claims were to be successful. In addition, errors by either us or our competitors may also produce significant adverse publicity either for us or for the online pharmacy industry in general, which could result in an immediate reduction in the amount of orders we receive and would harm our ability to conduct and sustain our business.

Security breaches would damage our reputation, expose us to liability and otherwise harm our business.

Our security measures may not prevent security breaches that could harm our business. To succeed, we must provide a secure transmission of confidential information over the Internet and protect the confidential customer and patient information we retain, such as credit card numbers and prescription records. A third party who compromises or breaches the physical and electronic security measures we use to protect transaction data and customer records could misappropriate proprietary information, cause interruptions in our operations, damage our computers or those of our customers, or otherwise harm our business. Any of these would harm our reputation and expose us to a risk of loss or litigation and possible liability. We may need to expend significant resources to protect against security breaches or to address problems caused by breaches.

Expanding the breadth and depth of our product offerings is expensive and difficult, and we may receive no benefit from our expansion.

We intend to continue to expand the breadth and depth of our prescription and OTC product offerings by promoting new or complementary products or sales formats. Expansion of our offerings in this manner could require significant additional expenditures and could strain our management, financial, and operational resources. For example, we may need to incur significant marketing expenses, develop relationships with new fulfillment partners or manufacturers, or comply with new regulations. We may be unable to expand our product offerings or sales formats in a cost-effective or timely manner, and any new offerings or formats may not generate satisfactory revenues to offset the costs involved. Furthermore, any new product offering or sales format that is not favorably received by consumers could damage the reputation of our brand. A lack of market acceptance of our efforts or our inability to generate sufficient revenues to offset the cost of expanded offerings would harm our business.



The implementation of the Medicare Part D prescription drug benefit has and will likely continue to adversely affect drug pricing, which decreases our profitability.

In 2006, the Medicare Part D prescription drug benefit under the Medicare Prescription Drug, Improvement, and Modernization Act of 2003 (“DIMA”) became effective. The Medicare Part D prescription drug benefit has negatively affected, and is likely to continue to have a negative impact on, our business. Medicare Part D prescription drug coverage will likely increase the number of senior citizens with prescription drug coverage and reduce the number of customers who pay for their prescription drugs themselves. Customers who choose to obtain coverage under a Medicare Part D plan will likely purchase fewer drugs, or no longer purchase drugs, from us. Because we are not currently processing claims for Medicare Part D, we will be able to serve Medicare D customers only when those customers elect to purchase outside of their Medicare Part D plan and purchase their prescriptions out-of-pocket, such as when the particular medication is not covered by the customer’s Medicare plans or when the customer’s purchase is not covered because of a deductible, co-payment, or other exclusion. Moreover, the DIMA calls for significant changes to the formulas the Medicare program uses to calculate its payments for prescription drugs, as well as introduction of managed care elements and changes to the administration of the drug benefit program. When fully implemented, these changes could exert downward pressure on prescription drug prices and payments by the government, even as the number of people who use the Medicare benefits to pay for prescription drugs increases. All of these factors could adversely affect our drug prices and dispensing fees, and ultimately could reduce our profit margins.

Government regulation of our business is extensive, and our failure to comply fully with regulations could result in civil and criminal penalties for us.

Our business is subject to extensive federal, state and local regulations. For example:

- entities engaging in the practice of pharmacy are subject to numerous federal and state regulatory requirements, including those relating to pharmacy licensing and registration, the dispensing of prescription drugs, pharmacy record keeping and reporting, and the confidentiality, security, storage, and release of patient records; and
- the sale, advertisement, and promotion of, among other things, prescription, OTC and homeopathic medications, dietary supplements, medical devices, cosmetics, foods, and other consumer products that we sell are subject to regulation by the FDA, the FTC, the Consumer Product Safety Commission, and state regulatory authorities, as the case may be.

As we expand our product offerings and more non-pharmaceutical products become subject to FDA, FTC and other regulation, more of our products will likely be subject to regulation. In addition, regulatory requirements to which our business is subject may expand over time, and some of these requirements may have a disproportionately negative effect on Internet pharmacies. For example, the federal government and a majority of states now regulate the retail sale of OTC products containing pseudoephedrine that might be used as precursors in the manufacture of illegal drugs. As a result, we are currently unable to sell these products to customers residing in states that require retailers to obtain a physical form of identification or maintain a signature log. Some members of Congress have proposed additional regulation of Internet pharmacies in an effort to combat the illegal sale of prescription drugs over the Internet, and state legislatures could add or amend legislation related to the regulation of nonresident pharmacies. In addition to regulating the claims made for specific types of products, the FDA and the FTC may attempt to regulate the format and content of websites that offer products to consumers. The laws and regulations applicable to our business often require subjective interpretation, and we cannot be certain that our efforts to comply with these regulations will be deemed sufficient by the appropriate regulatory agencies. Violations of any regulations could result in various civil and criminal penalties, including suspension or revocation of our licenses or registrations, seizure of our inventory, or monetary fines, any of which could harm our business, financial condition, or operating results. Compliance with new

laws or regulations could increase our expenses or lead to delays as we adjust our website and operations.

Increasing concern about privacy, spam, and the use and security of customer information could restrict our marketing efforts and harm our business.

Internet retailers are also subject to increasing regulation and scrutiny relating to privacy, spam, and the use and security of personal user information. These regulations, along with increased governmental or private enforcement (for example, by Internet service providers), may increase the cost of growing our business. Current and proposed regulations and enforcement efforts may restrict our ability to collect and use demographic and personal information from users and send promotional e-mails, which could be costly or harm our marketing efforts. For example, if one or more Internet service providers were to block our promotional e-mails to customers, our ability to generate orders and revenue could be harmed. Further, any violation of privacy, anti-spam, or data protection laws or regulations may subject us to fines, penalties, and damages and may otherwise have a material adverse effect on our business, results of operations, and financial condition.

If people or property is harmed by the products we sell, product liability claims could damage our business and reputation.

Some of the products we sell may expose us to product liability claims relating to personal injury, death, or property damage caused by these products and may require us to take actions such as product recalls. Any such product liability claim or product recall may result in adverse publicity regarding us and the products we sell, which may harm our reputation. If we are found liable under product liability claims, we could be required to pay substantial monetary damages. Further, even if we successfully defend ourselves against this type of claim, we could be forced to spend a substantial amount of money in litigation expenses, our management could be required to spend valuable time in the defense against these claims, and our reputation could suffer, any of which could harm our business. Our current vendors do not, and future vendors may not, indemnify us against product liability. Further, our liability insurance may not be adequate to protect us from all liability that may be imposed as a result of these claims, and we cannot be certain that insurance will continue to be available to us on economically reasonable terms, or at all. Any imposition of product liability that is not covered by vendor indemnification or our insurance could harm our business, financial condition, and operating results. We do not have vendor indemnification clauses with our current vendors.

If we are required to collect sales and use taxes on the products we sell in additional jurisdictions, we may be subject to liability for past sales and our future sales may decrease.

In accordance with current industry practice, historically we have not collected sales and use taxes or other taxes with respect to shipments of goods into states other than Ohio and Nevada. The operation of our distribution center, the operations of any future distribution centers and other aspects of our evolving business, however, may result in additional sales and use tax collection obligations. In addition, one or more other states may successfully assert that we should collect sales and use or other taxes on the sale of our products in that state. One or more states or the federal government may seek, either through unilateral action or through federal legislation, to impose sales or other tax collection obligations on out-of-jurisdiction companies that engage in electronic commerce as we do. Moreover, one or more states could begin to impose sales taxes on sales of prescription products, which are not generally taxed at this time, or impose sales taxes on sales of certain prescription products. The imposition of additional tax obligations on our business by state and local governments could create significant administrative burdens for us, decrease our future sales, and harm our cash flow and operating results.

We are dependent on key personnel and their loss would adversely affect our ability to conduct our business.

In order to execute our business plan, we must be able to keep our existing management and professionals and, when necessary, hire additional personnel who have the expertise we need. We cannot assure you that we will be able to this, and our failure to do so could have a material adverse effect on our business, results of operations and financial condition. We are particularly dependent on the services of Lalit Dhadphale, our Chief Executive Officer and President. We do not carry key-man life insurance for our benefit on Mr. Dhadphale or on any other employee of our company.

We are a public company and, as such, are subject to the reporting requirements of federal securities laws, which are expensive and may divert resources from other projects, thus impairing our ability to grow.

We are a public reporting company and, accordingly, are subject to the information and reporting requirements of the Securities Exchange Act of 1934, as amended (the "Exchange Act"), and other U.S. federal securities laws, including compliance with the Sarbanes-Oxley Act of 2002 (the "Sarbanes-Oxley Act"). Compliance with these obligations requires significant time and resources from our management and increases our legal, insurance and financial compliance costs. It is also time consuming and costly for us to develop and implement the internal controls and reporting procedures required by Section 404 of the Sarbanes-Oxley Act. If we are unable to comply with the

requirements of the Sarbanes-Oxley Act, it may preclude us from keeping our filings with the SEC current. Non-current reporting companies may be subject to various restrictions, such as the inability to be quoted on the OTC BB. See “If we fail to remain current in our reporting requirements, we could be removed from the OTC BB, which would limit the ability of broker-dealers to sell our securities and the ability of our shareholders to sell their securities in the secondary market.”

## Risks Related to Our Common Stock

Our common stock may be considered a “penny stock” and may be difficult to sell.

The SEC has adopted regulations which generally define “penny stock” to be an equity security that has a market or exercise price of less than \$5.00 per share, subject to specific exemptions. The market price of our common stock has been below \$5.00 per share and therefore we are designated as a “penny stock” according to SEC rules. This designation requires any broker or dealer selling these securities to disclose certain information concerning the transaction, obtain a written agreement from the purchaser and determine that the purchaser is reasonably suitable to purchase the securities. These rules restrict the ability of brokers or dealers to sell our common stock and may affect the ability of our stockholders to sell their shares. In addition, since our common stock is quoted on the OTC BB, our stockholders may find it difficult to obtain accurate quotations of our common stock and may find few buyers to purchase the stock or a lack of market makers to support the stock price.

Our stock price may continue to be volatile and may decrease in response to various factors, which could adversely affect our business and cause our stockholders to suffer significant losses.

Our common stock is illiquid, and its price has been and may continue to be volatile in the indefinite future. Following the reverse split, which was effective for trading purposes on July 29, 2010 and through December 31, 2010, the high and low sale prices of our common stock were \$4.00 and \$2.00, respectively. The price of our stock could fluctuate widely in response to various factors, many of which are beyond our control, including the following:

- changes in our industry;
- government regulations;
- competitive pricing pressures;
- our ability to obtain working capital;
- additions or departures of key personnel;
- limited “public float” in the hands of a small number of persons, whose sales or lack of sales could result in positive or negative pricing pressure on the market price for our common stock;
- sales of our common stock;
- our ability to execute our business plan;
- operating results that fall below expectations;
- loss of any strategic relationship;
- economic and other external factors; and
- period-to-period fluctuations in our financial results.

In addition, the securities markets have from time to time experienced significant price and volume fluctuations that are unrelated to the operating performance of particular companies. These market fluctuations may also materially and adversely affect the market price of our common stock.

If we fail to remain current in our reporting requirements, we could be removed from the OTC BB, which would limit the ability of broker-dealers to sell our securities and the ability of our shareholders to sell their securities in the secondary market.

Companies trading on the OTC BB, such as us, must be reporting issuers under Section 12 of the Exchange Act, and must be current in their reports under Section 13 of the Exchange Act, in order to maintain price quotation privileges on the OTC BB. We failed to file our Form 10-Q for the quarterly period ended June 30, 2009 on time, although we ultimately filed it on August 24, 2009. If we fail to remain current in our reporting requirements, we could be removed from the OTC BB. As a result, the market liquidity for our securities could be adversely affected by limiting the ability of broker-dealers to sell our securities and the ability of our shareholders to sell their securities in the secondary market. See “We must comply with Section 404 of the Sarbanes-Oxley Act, which requires us to document and test our internal controls over financial reporting. Any delays or difficulty in satisfying these requirements could adversely affect our future stock price.”

Our stock trading volume may not provide adequate liquidity for investors, and the price of our common stock may fluctuate significantly. This may make it difficult for you to resell our common stock when you want or at prices you find attractive.

Shares of our common stock are traded on the over-the-counter markets, including the OTCQB market tier for the OTC Markets Group Inc. (formerly the Pink Sheets). The average daily trading volume in our common stock is generally less than that of larger companies whose stocks are listed on an exchange and can often be sporadic and very limited. Given the limited and sporadic trading of our common stock, holders of our common stock may be unable to make significant sales of the common stock in a brief period of time. In addition, our common stock may be subject to significant price swings even when a relatively small number of shares are traded. We cannot predict the volume or prices at which our common stock will trade in the future.

Our officers, directors and 5% or greater stockholders have significant voting power.

Our executive officers, directors, and our 5% or greater stockholders beneficially own approximately 62% of our outstanding voting securities. If these stockholders act together, they will be able to exert significant control over our management and affairs requiring stockholder approval, including approval of significant corporate transactions.

We could issue “blank check” preferred stock without stockholder approval with the effect of diluting then current stockholder interests and impairing their voting rights and provisions in our charter documents could discourage a takeover that stockholders may consider favorable.

Our certificate of incorporation authorizes the issuance of up to 1,000,000 shares of “blank check” preferred stock with designations, rights and preferences as may be determined from time to time by our board of directors. To date, we have designated 200,000 of these shares as Series A Convertible Preferred Stock, and 625,000 of these shares as Series B Convertible Preferred Stock, leaving 175,000 shares of “blank check” preferred stock available for designation and issuance. Our board of directors is empowered, without stockholder approval, to issue a series of preferred stock with dividend, liquidation, conversion, voting or other rights which could dilute the interest of, or impair the voting power of, our common stockholders. The issuance of a series of preferred stock could be used as a method of discouraging, delaying or preventing a change in control. For example, it would be possible for our board of directors to issue preferred stock with voting or other rights or preferences that could impede the success of any attempt to change control of our company.

We may engage in additional financing that could lead to dilution of existing stockholders.

To date, we have financed our activities through revenues from our online sales, the proceeds from sales of our equity securities in private placement financings and the proceeds from the issuance of our promissory notes in private financings. Any future financings by us may result in substantial dilution of the holdings of existing stockholders and could have a negative impact on the market price of our common stock. Furthermore, we cannot assure you that such future financings will be possible.



We do not anticipate paying dividends in the foreseeable future; you should not buy our stock if you expect dividends.

We currently intend to retain our future earnings to support operations and to finance expansion and, therefore, we do not anticipate paying any cash dividends on our common stock in the foreseeable future.

Item 1B. Unresolved Staff Comments.

Not applicable.

Item 2. Properties.

Our corporate headquarters, which also house our pharmacy and customer service operations as well as our inventory, are located at 100 Commerce Boulevard, Cincinnati, Ohio 45140. We occupy 16,000 square feet of warehouse space under a lease with a monthly rental rate of \$9,417. The lease expired in March 2011, and we are currently on a month-to-month tenancy.

Item 3. Legal Proceedings.

In the ordinary course of business, we may become subject to lawsuits and other claims and proceedings, that might arise from litigation matters or regulatory audits. Such matters are subject to uncertainty and outcomes are often not predictable with assurance. Our management does not presently expect that any such matters will have a material adverse effect on the Company's financial condition or results of operations. We are not currently involved in any pending or threatened material litigation, other material legal proceedings nor have we been made aware of any penalties from regulatory audits.

Item 4. Removed & Reserved.

PART II

Item 5. Market for Registrant's Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities.

Market Information

Our shares of common stock are currently quoted on the OTC BB under the symbol HEWA.OB. Our symbol prior to the closing of the Exchange and until August 5, 2009, when we changed it, was IONN.OB.

The following table sets forth the high ask and low bid prices for our common stock for the periods indicated as reported by the OTC BB. On July 16, 2010, we effected a one (1) for twenty (20) reverse split or combination of our Common Stock (the "Reverse Split"). The Reverse Split became effective for trading purposes on the OTC BB on July 29, 2010. All prices in the following table have been adjusted to reflect the Reverse Split.

| Quarter | Year ended<br>December 31, 2010 |         | Year ended<br>December 31, 2009 |         |
|---------|---------------------------------|---------|---------------------------------|---------|
|         | High                            | Low     | High                            | Low     |
| First   | \$ 3.00                         | \$ 1.20 | \$ 0.80                         | \$ 0.40 |
| Second  | \$ 4.00                         | \$ 2.20 | \$ 7.00                         | \$ 0.20 |
| Third   | \$ 4.00                         | \$ 2.20 | \$ 3.40                         | \$ 2.20 |
| Fourth  | \$ 4.00                         | \$ 2.20 | \$ 2.80                         | \$ 1.40 |

On April 1, 2011, the closing price of our common stock, as reported by the OTC BB, was \$5.84 per share.

These bid prices represent prices quoted by broker-dealers on the OTC BB. The quotations reflect inter-dealer prices, without retail mark-up, mark-down or commissions, and may not represent actual transactions.

As of April 1, 2011, there were 10,577,719 shares of our common stock outstanding.

#### Holders

As of April 1, 2011, there were approximately 379 holders of record of our common stock. However, we believe that there are significantly more beneficial holders of our common stock as many beneficial holders hold their stock in "street name."

#### Dividends

We have never declared cash dividends on our common stock, nor do we anticipate paying any dividends on our common stock in the future.

#### Recent Sales of Unregistered Securities

All recent sales of unregistered securities have been previously reported in the Company's Quarterly Reports on Form 10-Q or Current Reports on Form 8-K.

#### Item 6. Selected Financial Data.

Not applicable.

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

##### Overview

We are a VIPPS accredited retail mail-order pharmacy and healthcare e-commerce company that sells discounted generic and brand name prescription drugs, as well as, over-the-counter (OTC) medical products. Our web address is <http://www.healthwarehouse.com>. At present, we sell:

- a range of prescription drugs (we are licensed as a mail-order pharmacy for sales to 50 states and the District of Columbia);
  - diabetic supplies including glucometers, lancets, syringes and test strips;
- OTC medications covering a range of conditions from allergy and sinus to pain and fever to smoking cessation aids;
  - home medical supplies including incontinence supplies, first aid kits and mobility aids; and
  - diet and nutritional products including supplements, weight loss aids, and vitamins and minerals.

Our objectives are to make the pharmaceutical supply chain more efficient and to pass the savings on to the consumer. We are becoming known by consumers as a convenient, reliable, discount provider of over-the-counter and prescription medications and products. We intend to continue to expand our product line as our business grows. We are presently licensed as a mail-order pharmacy for sales to 50 states and the District of Columbia. For additional information see Part I Item 1 page 3.



## Results of Operations

The years ended December 31, 2010 compared to the year ended December 31, 2009.

|  | The year ended<br>December 31, 2010 | % of<br>Revenue |    | The year ended<br>December 31, 2009 | % of<br>Revenue |
|--|-------------------------------------|-----------------|----|-------------------------------------|-----------------|
| Revenue                                    | \$ 5,691,765                        | 100.0 %         | \$ | 3,783,542                           | 100.0 %         |
| Cost of sales                              | 3,450,021                           | 60.6 %          |    | 2,635,258                           | 69.7 %          |
| Gross profit                               | 2,241,744                           | 39.4 %          |    | 1,148,284                           | 30.3 %          |
| Selling, general & administrative expenses | 5,303,617                           | 93.2 %          |    | 3,646,915                           | 96.4 %          |
| Loss from operations                       | (3,061,873 )                        | (53.8 )%        |    | (2,498,631 )                        | (66.0 )%        |
| Interest income                            | 642                                 | 0 %             |    | 605                                 | 0 %             |
| Interest expense                           | 679,330                             | 11.9 %          |    | 38,150                              | 0.1 %           |
| Gain on litigation settlement              | 48,887                              | 0.9 %           |    | -                                   | 0 %             |
| Other income (expense)                     | -                                   | (0 )%           |    | 96,674                              | 2.6 %           |
| Net loss before taxes                      | (3,691,674 )                        | (64.9 )%        |    | (2,439,502 )                        | (64.5 )%        |
| Income tax expense                         | -                                   | - %             |    | -                                   | - %             |
| Net loss                                   | \$ (3,691,674 )                     | (64.9 )%        | \$ | (2,439,502 )                        | (64.5 )%        |

## Revenue

|               | The year ended<br>December 31, 2010 | %<br>Change |    | The year ended<br>December 31, 2009 |
|---------------|-------------------------------------|-------------|----|-------------------------------------|
| Total revenue | \$ 5,691,765                        | 50.4 %      | \$ | 3,783,542                           |

Revenues for the year ended December 31, 2010 grew to \$5,691,765 from \$3,783,542 for the year ended December 31, 2009. Revenues increased for the year ended December 31, 2010 compared to the prior year as a result of an increase in order volume to customers and over-the-counter products offset in part by a decrease from the sale of certain prescription products to manufacturers during the year ended December 31, 2010 compared to the year ended December 31, 2009. Higher margin prescription revenues of \$2,053,902 in 2010 increased by approximately 230% from 2009 while lower margin over-the-counter revenue of \$3,004,853 in 2010 declined as a percentage of total revenue from 62.2% to 52.7% for the year ended December 31, 2009. The Company's core business of consumer prescription fulfillment continues to grow rapidly from year to year. The Company has taken steps to increase its over the counter product revenue beginning on January 1, 2011 and expects that the sale of prescription products to manufacturers will continue to decline as a percentage of total revenue.

Another indicator of increased business activity was that our website attracted over 1,549,075 visits with over 5,248,524 pageviews during the year ended December 31, 2010 compared to 1,104,190 visits and 4,057,959 pageviews during the year ended December 31, 2009.

## Costs and Expenses

## Cost of Sales and Gross Margin

|                            | The year ended<br>December 31, 2010 | %<br>Change |    | The year ended<br>December 31, 2009 |
|----------------------------|-------------------------------------|-------------|----|-------------------------------------|
| Total cost of sales        | \$ 3,450,021                        | 30.9 %      | \$ | 2,635,258                           |
| Total gross profit dollars | \$ 2,241,744                        | 95.2 %      | \$ | 1,148,284                           |

|                               |      |   |     |   |      |   |
|-------------------------------|------|---|-----|---|------|---|
| Total gross margin percentage | 39.4 | % | 9.0 | % | 30.4 | % |
|-------------------------------|------|---|-----|---|------|---|

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Total cost of sales increased to \$3,450,021 for the year ended December 31, 2010 as compared to \$2,635,258 for the year ended December 31, 2009 as a result of growth in order volume and revenue. Gross margin percentage increased year-over-year from 30.4% for the year ended December 31, 2009 to 39.4% for the year ended December 31, 2010. The improvement in gross profit margins was due primarily to the shift in product mix from primarily lower margin OTC product sales for the year ended December 31, 2009 to an increase in higher margin revenue for prescription drugs and the sale of certain prescription products to manufacturers. The Company believes that revenue for higher margin products will continue to grow at a faster rate than lower margin over the counter products.

#### Selling, General and Administrative Expenses

|  | The year ended<br>December 31, 2010 | %<br>Change | The year ended<br>December 31, 2009 |
|--|-------------------------------------|-------------|-------------------------------------|
| Selling, general and administrative expenses | \$ 5,303,617                        | 45.4 %      | \$ 3,646,915                        |
| Percentage of revenue                        | 93.2 %                              | (2.0 )%     | 96.4 %                              |

Selling, general and administrative expenses increased by \$1,656,702 in the year ended December 31, 2010 compared to the same period in 2009, an increase of 45.4%. The year ended December 31, 2010, expense increases were due primarily to expenses related to the maturing of business activities including increased headcount and increases of approximately \$1,196,235 for payroll, bad debt, rent, contract labor, shipping and fulfillment, and travel related expenses offset in part by a reduction in advertising expenses of \$135,667 and legal expenses of \$278,557 compared to the year ended December 31, 2009. In addition the recognition of \$490,765 for non-cash based stock compensation expense compared to \$260,319 in the year ended December 31, 2009, software engineering for \$197,270 and compared to \$0 in the year ended December 31, 2009 and amortization of capitalized software expenses of \$100,200 for the year ended December 31, 2010 and \$39,275 in the year ended December 31, 2009 due to capitalization.

The increase in payroll related expenses was due to primarily two factors: head count increase from 12 in 2009 to 29 in 2010 and the hiring of certain more highly compensated employees in 2010 compared to 2009. The increase in expenses for software engineering and amortization of software expenses compared to 2009 was due primarily to the recognition of amortization due to the launch of the Company's web site and non-capitalizable improvements to the web site as reflected in software engineering expenses in 2010. The Company expects that selling, general and administrative expenses will continue to decline as a percentage of total revenue primarily due to increased operating efficiencies for head count, rent, and professional fees as the Company matures.

#### Other income (expense)

|                               | The year ended<br>December 31, 2010 | %<br>Change | The year ended<br>December 31, 2009 |
|-------------------------------|-------------------------------------|-------------|-------------------------------------|
| Interest income               | 642                                 | 6.1 %       | 605                                 |
| Interest expense              | 679,330                             | 1,680.7 %   | 38,150                              |
| Gain on litigation settlement | 48,887                              | (0 )%       | -                                   |
| Other income (expense)        | -                                   | (0 )%       | 96,674                              |

Interest expense increased from \$38,150 in the year ended December 31, 2009 to \$679,330 in the year ended December 31, 2010, primarily due to the recognition of the non-cash accretion of debt discount for the year ended December 31, 2010 of \$543,407 compared to \$6,858 for the same period in 2009, and increased loan interest expense of \$135,279 for the year ended December 31, 2010 compared to \$30,686 in the prior year, primarily related to the Company's debt financing transactions in December 2009 and May 2010.

#### Off-Balance Sheet Arrangements

We have not entered into any transactions with unconsolidated entities in which we have financial guarantees, subordinated retained interests, derivative instruments or other contingent arrangements that expose us to material continuing risks, contingent liabilities or any other obligations under a variable interest in an unconsolidated entity that provides us with financing, liquidity, market risk or credit risk support.



### Impact of Inflation

We believe that inflation has not had a material impact on our results of operations for the years ended December 31, 2010 and 2009. We cannot assure you that future inflation will not have an adverse impact on our operating results and financial condition.

### Liquidity and Capital Resources

As of December 31, 2010, the Company had \$1,397,583 in cash and working capital of \$1,058,984. During the year ended December 31, 2010, the Company generated revenue of \$5,691,765 and a net loss of \$3,691,674. For the year ended December 31, 2010, cash flows included net cash used in operating activities of \$2,483,168, net cash used in investing activities of \$151,600 and net cash provided by financing activities of \$3,841,170.

Since inception, the Company has financed its operations primarily through product sales to customers, debt and equity financing agreements. During the year ended December 31, 2010, the Company's cash was increased by \$1,206,402. Our sources and uses of funds during this period were as follows:

For the year ended December 31, 2010, cash flows included net cash used in operating activities of \$2,483,168. This amount included a decrease in operating cash related to a net loss of \$3,691,674 and an increase in accounts receivable \$(507,707) due primarily to the sale of prescription products to manufacturers offset by additions for the following items; (i) amortization of debt discount, \$543,407 due primarily to the debt discount related to warrants issued for two short term notes (ii) stock-based compensation expense, \$490,765 for options issued during 2009 and additional options issued during 2010 (iii) depreciation and amortization, \$198,836 (iv) accounts payable-related parties, \$159,604 the increase was related to improved payment terms (iv) accrued expenses, \$98,098 the majority of which was related to the November 8, 2010 financing. For the year ended December 31, 2009, cash flows included net cash used in operating activities of \$2,810,461. This amount included a decrease in operating cash related to a net loss of \$2,439,502 and additions for the following items: (i) depreciation and amortization, \$122,379; (ii) stock-based compensation expense, \$260,318; (iii) accounts payable, \$388,279. The increase in cash used in operating activities in 2009 was primarily offset by the following decreases: (i) accounts payable-related parties, \$(307,024), (ii) accounts receivable, \$(265,399); (iii) prepaid expenses and other current assets, \$(191,001); and (iv) inventories, \$(304,268).

For the year ended December 31, 2010, net cash used in investing activities was \$151,600. For the year ended December 31, 2009, net cash provided by investing activities was \$854,593 and was attributable to cash received in share exchange of \$1,220,520, offset by expenses paid in conjunction with share exchange of \$150,000; acquisitions of property and equipment of \$85,928 and website development costs of \$129,999.

For the year ended December 31, 2010, net cash provided by financing activities was \$3,841,170, consisting of a sale of preferred stock of \$3,205,170 net of expenses paid in conjunction with the sale of approximately \$145,012; and the sale of convertible notes of \$150,000. For the year ended December 31, 2009, net cash provided by financing activities was \$1,789,111, consisting of a sale of convertible notes of \$1,200,000; sale of common stock of \$50,196 and proceeds from option and warrant exercises of \$23,915.

During the quarter ended December 31, 2010, the Company received net cash proceeds of approximately \$3,200,000 for the sale of 349,392 shares of Series B Preferred Stock and restructured \$1,000,000 in short term debt to long term. (see Note 12). Management believes that the Company is taking certain steps to improve its operations and cash flows, including the re-launch of its corporate website, improved inventory management and an increase in the number of suppliers. Considering the new financial resources, current operating projections and additional potential funding sources, the Company believes that it should have sufficient working capital through the next fiscal year.

Management believes that if the Company needs to raise additional capital in order to meet operations and execute its business plan, it will be successful. However, there is no assurance that additional financing will be available when needed or that management will be able to obtain financing on terms acceptable to the Company and whether the Company will be able to turn into a profitable position and generate positive operating cash flow. If the Company is unable to raise sufficient additional funds, it will have to develop and implement a plan to extend payables and reduce overhead until sufficient additional capital is raised to support further operations. There can be no assurance that such a plan will be successful. The consolidated financial statements do not include any adjustments that might result from the outcome of this uncertainty.

### Critical Accounting Policies and Estimates

The preparation of our consolidated financial statements in conformity with accounting principles generally accepted in the United States of America requires our management to exercise its judgment. We exercise considerable judgment with respect to establishing sound accounting policies and in making estimates and assumptions that affect the reported amounts of our assets and liabilities, our recognition of revenues and expenses, and disclosures of commitments and contingencies at the date of the financial statements. Our significant estimates include the allowance for doubtful accounts, depreciation, stock-based compensation, evaluation of warrants, debt discount and deferred tax assets, including a valuation allowance.

On an ongoing basis, we evaluate our estimates and judgments. We base our estimates and judgments on a variety of factors including our historical experience, knowledge of our business and industry, current and expected economic conditions, the composition of our products/services and the regulatory environment. We periodically re-evaluate our estimates and assumptions with respect to these judgments and modify our approach when circumstances indicate that modifications are necessary.

While we believe that the factors we evaluate provide us with a meaningful basis for establishing and applying sound accounting policies, we cannot guarantee that the results will always be accurate. Since the determination of these estimates requires the exercise of judgment, actual results could differ from such estimates.

We account for stock-based compensation in accordance with the fair value recognition provisions of Accounting Standards Codification (“ASC”) 718, for all stock-based payment awards is based on the estimated grant-date fair value. We recognize these compensation costs over the requisite service period of the award, which is generally the option vesting term. Option valuation models require the input of highly subjective assumptions including the expected life of the option. Because our employee stock options have characteristics significantly different from those of traded options, and because changes in the subjective input assumptions can materially affect the fair value estimate, in our management’s opinion, the existing models do not necessarily provide a reliable single measure of the fair value of our employee stock options. The fair value of stock-based payment awards was estimated using the Black-Scholes option pricing model using a volatility figure derived from an index of comparable entities. Our management will review this assumption as our trading history becomes a better indicator of value. We account for the expected life of options in accordance with the “simplified” method provisions of SEC Staff Accounting Bulletin (“SAB”) No. 110, which enables the use of the simplified method for “plain vanilla” share options as defined in SAB No. 107.

### Recently-issued Accounting Pronouncements

The information contained in Footnote 12 to the Company’s consolidated financial statements included in Item 8 to this annual report is incorporated herewith by reference.

### Item 7A. Quantitative and Qualitative Disclosure About Market Risk.

Not applicable.

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

The financial statements required hereby are located on pages 67 through 82.

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

none

ITEM 9A. CONTROLS AND PROCEDURES

Evaluation of Disclosure Controls and Procedures

Disclosure controls and procedures are controls and other procedures that are designed to ensure that information required to be disclosed by our Company is recorded, processed, summarized and reported, within the time periods specified in the rules and forms of the SEC. Our Chief Executive Officer and Chief Financial Officer are responsible for establishing and maintaining disclosure controls and procedures for our Company.

Our management, with the participation of our Chief Executive Officer and Chief Financial Officer, carried out an evaluation of the effectiveness of our “disclosure controls and procedures” (as defined in the Securities Exchange Act of 1934 (the “Exchange Act”) Rules 13a-15(e) and 15d-15(e)) as of the end of the period covered by this annual report on Form 10-K (the “Evaluation Date”). Based upon that evaluation, our Chief Executive Officer and Chief Financial Officer concluded that, as of the Evaluation Date, our disclosure controls and procedures are not effective as of December 31, 2010, to ensure that information required to be disclosed by us in the reports that we file or submit under the Exchange Act (i) is recorded, processed, summarized and reported, within the time periods specified in the SEC rules and forms and (ii) is accumulated and communicated to our management, including our Chief Executive Officer and Chief Financial Officer, as appropriate to allow timely decisions regarding required disclosure.

Management conducted an evaluation of the effectiveness of the Company’s internal control over financial reporting based on the criteria in Internal Control-Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). Based on this evaluation under the criteria in Internal Control-Integrated Framework, and upon consideration of the material weakness discussed below, management concluded that the Company’s internal control over financial reporting was not effective as of December 31, 2010.

Internal Control over Financial Reporting

The term “internal control over financial reporting” is defined as a process designed by, or under the supervision of, the registrant’s principal executive and principal financial officers, or persons performing similar functions, and effected by the registrant’s board of directors, management and other personnel, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles and includes those policies and procedures that:

- pertain to the maintenance of records that in reasonable detail accurately and fairly reflect the transactions and dispositions of the assets of the registrant;
- provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the registrant are being made only in accordance with authorizations of management and directors of the registrant; and
- provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use or disposition of the registrant’s assets that could have a material effect on the financial statements.

As of December 31, 2010 and for the year then ended, the Company has identified certain matters involving our internal control over financial reporting that constitute a material weakness under standards established by the Public Company Accounting Oversight Board (“PCAOB”).



The PCAOB defines a material weakness as a significant deficiency, or combination of significant deficiencies, that results in more than a remote likelihood that a material misstatement of our annual or interim financial statement will not be presented or detected by our employees. A significant deficiency is defined as a control deficiency, or a combination of control deficiencies, that adversely affects the company's ability to initiate, authorize, record, process, or report external financial data reliably in accordance with generally accepted accounting principles such that there is more than a remote likelihood that a misstatement of the company's annual or interim financial statements that is more than inconsequential will not be prevented or detected. A control deficiency exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect misstatements on a timely basis. A deficiency in design exists when:

- a control necessary to meet the control objective is missing; or
- an existing control is not properly designed so that, even if the control operates as designed, the control objective is not always met.

A deficiency in operation exists when a properly designed control does not operate as designed, or when the person performing the control does not possess the necessary authority or qualifications to perform the control effectively.

Specifically, as of December 31, 2010, the following material weaknesses existed:

- **Financial Reporting Systems:** We did not maintain a fully integrated financial consolidation and reporting system throughout the year and as a result, extensive manual analysis, reconciliation and adjustments were required in order to produce financial statements for external reporting purposes.
- **Accounting for Complex Transactions:** We lack adequately trained accounting personnel with appropriate United States generally accepted accounting principles (US GAAP) expertise for complex transactions.
- **Segregation of Duties:** Although it has improved during the period ended December 31, 2010, we do not currently have a sufficient complement of technical accounting and external reporting personnel commensurate to support standalone external financial reporting under public company or SEC requirements. Specifically, the Company did not effectively segregate certain accounting duties due to the small size of its accounting staff, and maintain a sufficient number of adequately trained personnel necessary to anticipate and identify risks critical to financial reporting and the closing process. In addition, there were inadequate reviews and approvals by the Company's personnel of certain reconciliations and other processes in day-to-day operations due to the lack of a full complement of accounting staff.
- **Policies and Procedures:** We have not commenced design, implementation and documentation of the policies and procedures used for external financial reporting, accounting and income tax purposes.

We believe that our internal control risks are mitigated by the fact that our Chief Executive Officer reviews and approves substantially all of our major transactions. We believe that our weaknesses in internal control over financial reporting and our disclosure controls relate in part to the fact that we are an emerging business with limited personnel. Management and the audit committee of the Board of Directors believe that the company must allocate additional human and financial resources to address these matters. Throughout the year, the Company has been continuously improving its monitoring of current reporting systems and its personnel and has recently hired a corporate controller to support the Company in its compliance process. To ensure the proper remediation of the above-mentioned material weaknesses, we intend to hire additional senior staff, as necessary, to mitigate these weaknesses, as well as to implement other planned improvements. Additional senior staff will enable us to document and apply transactional and periodic control procedures, permit a better closing, review and approval process, and improve the quality of our financial reporting. The Company intends to continue making necessary changes until its material weaknesses are remediated.



Additional measures may be necessary and the measures we expect to take to improve our internal controls may not be sufficient to address the issues identified, to ensure that our internal controls are effective or to ensure that such material weakness or other material weaknesses would not result in a material misstatement of our annual or interim financial statements. In addition, other material weaknesses or significant deficiencies may be identified in the future. If we are unable to correct deficiencies in internal controls in a timely manner, our ability to record, process, summarize and report financial information accurately and within the time periods specified in the rules and forms of the SEC will be adversely affected. This failure could negatively affect the market price and trading liquidity of our common stock, cause investors to lose confidence in our reported financial information, subject us to civil and criminal investigations and penalties, and generally materially and adversely impact our business and financial condition.

#### Inherent Limitation of the Effectiveness of Internal Control

Our internal control system is designed to provide reasonable assurance to our management and board of directors regarding the preparation and fair presentation of published financial statements. All internal control systems, no matter how well designed, have inherent limitations. Therefore, even those systems determined to be effective can provide only reasonable assurance with respect to financial statement preparation and presentation. Further, the design of a control system must reflect the fact that there are resource constraints and the benefits of controls must be considered relative to their costs. In addition, because of changes in conditions, the effectiveness of internal control may vary over time.

#### Changes in Internal Control Over Financial Reporting

During the three months ended December 31, 2010, the corporate controller was relocated to the corporate offices in order to improve internal control over financial reporting and financial effectiveness. There were no other changes in our internal control over financial reporting or in other factors that have materially effected, or are reasonably likely to materially affect, our internal control over financial reporting. The Company is a non-accelerated filer and is not subject to Section 404(b) of the Sarbanes Oxley Act.

#### Item 9B. Other Information.

None.

### PART III

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

##### Executive Officers and Directors

The names, ages and positions of our executive officers and directors as of April 1, 2011 are as follows:

| Name               | Age | Position   |
|--------------------|-----|--|
| Lalit Dhadphale    | 39  | President, Chief Executive Officer and Director  |
| Patrick E. Delaney | 57  | Chief Financial Officer, Treasurer and Secretary |
| Youssef Bennani    | 44  | Director   |



|                 |    |          |
|-----------------|----|----------|
| Norman E. Corn  | 64 | Director |
| Matthew Stecker | 42 | Director |
| Joseph Savarino | 40 | Director |

The principal occupations for the past five years (and, in some instances, for prior years) of each of our executive officers and directors are as follows:

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Lalit Dhadphale co-founded HealthWarehouse.com in August 2007 and launched the company's prescription drug business in 2008. He has been President and CEO of the company since its inception and has served as Chairman of the Board of Directors since May 2009. The company has grown from start-up to publicly traded on the OTC Bulletin Board (Ticker: HEWA), servicing 180,000 customers and shipping nearly 70,000 prescriptions in 2010. The company has acquired 50 state licenses to sell prescription medications and is 1 of only 27 VIPPS (Verified Internet Pharmacy Practice Sites) accredited pharmacies in the U.S. HealthWarehouse.com is also a 2009 and 2010 winner of the BizRate Circle of Excellence Award for outstanding customer service and satisfaction. Earlier in his career, Lalit founded Zengine, Inc. serving as Vice President of Product Development, Chief International Officer and later as Chief Operating Officer of Zengine, Inc. from founding in 1999 through its sale in 2002. Under his day-to-day leadership, Zengine grew from start-up to \$30+ million in annualized sales, achieving profitability in its second quarter as a public company in the first quarter of 2001. Prior to co-founding Zengine, Mr. Dhadphale was a co-founder of Excite Japan, where he was involved with product development, internationalization and localization of web sites and Internet products. He produced the launch of both Excite Japan and Netscape Netcenter Japan. Prior thereto, Mr. Dhadphale was International Business Development Manager for CNET, securing relationships throughout Asia and the Pacific Rim. Mr. Dhadphale received his BA degree from the University of Michigan, Ann Arbor in Japanese Language & Literature and Asian Studies.

Patrick E. Delaney became our Chief Financial Officer, Treasurer and Secretary on May 14, 2009, and served as the Chief Financial Officer of Clacendix from September 2003 to the merger date. Prior to joining our company, from 2000 until 2003, Mr. Delaney was the President of Taracon, Inc. a privately owned independent consulting firm that provides management consulting for early and mid-stage technology and financial services companies. Mr. Delaney also served as Chief Financial Officer for two publicly traded telecommunications providers, Pointe Communications Corporation from 1993 to 2000 and Advanced Telecommunications Corporation from 1986 to 1993. Mr. Delaney has served other companies in executive capacities including RealCom Communications, Argo Communications and ACF Industries.

Youssef Bennani became a member of our Board of Directors on November 11, 2009. Mr. Bennani is a Senior Managing Director in Kaufman Bros., L.P.'s Investment Banking department which he joined in 1995. His responsibilities range from public and private financing transactions to general financial advisory for mergers and acquisition, restructuring, acquisition financing and recapitalization. Prior to joining Kaufman Bros., L.P., Mr. Bennani was an investment banker at Barington Capital, L.P., where primary industry focus was technology. Mr. Bennani received his MBA in international finance from New York University's Stern School of Business. He also received his Masters in computer science as well as a BS in mathematics and physics from the University of Pierre and Marie Curie in Paris. In addition to the international and investment banking experiences, Mr. Bennani brings a depth of knowledge of finance that permits him to qualify as the "financial expert" on the Board of Directors.

Norman E. Corn became a member of our board of directors on May 14, 2009. Mr. Corn served as Director of Clacendix from November 2005 through May 14, 2009, and served as the Chief Executive Officer of Clacendix from August 2003 to May 14, 2009. From 2000 until 2003, Mr. Corn was Executive Vice President of Liquent, Inc., a Pennsylvania-based software company that provides electronic publishing solutions, focused on the life sciences industry. Mr. Corn also served from 1994 to 2000 as CEO of TCG Software, Inc., an offshore software services organization providing custom development to large corporate enterprises in the United States. Over the course of his career, Mr. Corn has led other companies, including Axiom Systems Group, The Cobre Group, Inc., The Office Works, Inc. and Longview Results, Inc., and spent the early part of his career in sales, marketing and executive positions at AT&T and IBM. Mr. Corn's combination of both small and large business experience provides the Company a skill set which should be invaluable as it grows. Since the merger of Healthwarehouse.com and Clacendix, Mr. Corn has been consulting with clients and partnering with accounting and legal firms supporting their clients in both turnaround and growth situations.

Matthew Stecker became a member of our board of directors on December 8, 2010. Since 2009 through present, Mr. Stecker is the CEO and President of Livewire Mobile, a leading provider of managed personalization services for mobile operators. From 2005 - 2009, Mr. Stecker was Principal and Vice President of The Management Network group. Under the Certificate of Designation designating the rights and privileges of the Company's Series B Preferred Stock, the holders of the Company's Series B Preferred Stock have the right to designate or elect one of the Company's directors (the "Series B Director"). The holders of a majority of the Company's outstanding Series B Preferred shares have designated Mr. Stecker as the initial Series B Director.

Joseph Savarino became a member of our board of directors on December 22, 2010. Mr. Savarino is a partner of Carpeturn.com, Inc. since June 2010, which provides flooring materials and services to the multi-family housing industry. Mr. Savarino was engaged in select internet consulting projects during 2002 through June 2010, and has prior experience in sales, business development and market research positions. Mr. Savarino was the President and Chief Executive Officer of Zengine Inc., a public company that was a sell-side e-business software and service provider, from 1998 until its sale in 2002.

All directors hold office until the next annual meeting of stockholders and the election and qualification of their successors. Officers are appointed annually by the board of directors and serve at the discretion of the board.

#### Committees of the Board of Directors

Our board of directors had previously established an audit committee and a compensation committee, and a nominating committee. In conjunction with the Exchange, we disbanded these committees. On April 8, 2010, our board of directors by written consent recreated an audit committee and during 2011 the Board expects to recreate a compensation committee, in compliance with established corporate governance requirements.

#### Audit Committee

The Company established an audit committee of the board of directors. The audit committee's duties are to recommend to the board of directors the engagement of independent registered public accountants to audit our financial statements and to review our accounting and auditing principles. The audit committee will review the scope, timing and fees for the annual audit and the results of audits performed by the independent registered public accountants, including their recommendations to improve the system of accounting and internal controls. The audit committee will at all times be composed exclusively of directors who are, in the opinion of the board of directors, free from any relationship which would interfere with the exercise of independent judgment as a committee member and who possess an understanding of financial statements and generally accepted accounting principles. Mr. Youssef Bennani will serve as the "audit committee financial expert," as defined under securities laws.

#### Compensation Committee

We plan to reestablish a compensation committee of the board of directors. The compensation committee would review and approve our salary and benefits policies, including compensation of executive officers. The compensation committee would also administer our 2009 Incentive Compensation Plan, and recommend and approve grants of stock options and restricted stock under that plan.

#### Nominating Committee

We do not plan to reestablish a standing nominating committee. Nominations for election to our board of directors may be made by the board of directors or by any stockholder entitled to vote for the election of directors in accordance with our bylaws and Delaware law.

#### Board Operation and Leadership Structure

The Board has adopted Corporate Governance Principles which along with the Charters for of its Committees and the Company Code of Business Conduct and Ethics, provides a framework for the governance of the Company. The Company's Corporate Governance Principles address matters such as the responsibilities and composition of the Board, Director Independence and the conduct of Board and Committee meetings. The Company's Code of Business Conduct and Ethics sets forth guiding principles of business ethics and certain legal requirements applicable to all

Company employees and Directors.

Currently, the Company's Chief Executive Officer also holds the position of Chairman of the Board of Directors. In the future, however, the Board may reconsider whether its Chief Executive Officer should also serve as Board Chairman.

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### Code of Ethics

We have adopted a code of ethics that applies to all of our employees, including our principal executive officer, principal financial officer, and principal accounting officer or controller. A copy of the Company's code of ethics will be provided free of charge, upon written request to 100 Commerce Boulevard, Cincinnati, Ohio 45140, and our telephone number is (513) 618-0913.

### Indebtedness of Directors and Executive Officers

None of our executive officers or directors, or their respective associates or affiliates, is indebted to us.

### Legal Proceedings

As of April 1, 2011, there were no material proceedings to which any of our directors, executive officers, affiliates or stockholders is a party adverse to us.

### Family Relationships

There are no family relationships among our executive officers and directors.

### Compliance with Section 16(a) of the Exchange Act

Matthew Stecker, a director, failed to timely file a Form 4 with respect to the grant to him of options to purchase 30,000 shares of common stock on December 8, 2010. The Form 4 was filed one day late.

### Stockholder Recommendations of Board Nominees

There have been no material changes to the procedures by which our stockholders may recommend nominees to our board of directors since our last proxy statement filed with the SEC.

### Item 11. Executive Compensation.

The table below summarizes the compensation earned for services rendered to Clacendix and Old HW, as applicable, in all capacities, for the years indicated, by its Chief Executive Officer and two most highly-compensated officers other than the Chief Executive Officer.

Summary Compensation Table

| Name and Principal Position                                 | Year | Salary (\$) | Bonus (\$) | Option Awards (\$) | (1) | All Other Compensation (\$) | (2) | Total (\$) |
|---|------|-------------|------------|--------------------|-----|-----------------------------|-----|------------|
| Lalit Dhadphale<br>President and Chief<br>Executive Officer | 2010 | 92,434      | 142,606    | 323,726            | (1) | 0                           |     | 558,766    |
|   | 2009 | 59,982      | 0          | 48,487             | (1) | 0                           |     | 108,469    |
| Norman E. Corn (2)<br>former Chief<br>Executive Officer     | 2010 | 0           | 0          | 0                  | (1) | 0                           | (3) | 0          |
|   | 2009 | 42,000      | 0          | 71,372             | (1) | 2,150                       | (3) | 115,522    |

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|  |      |         |   |        |     |       |     |         |
|--|------|---------|---|--------|-----|-------|-----|---------|
| Patrick E. Delaney                                     | 2010 | 81,625  | 0 | 0      | (1) | 1,948 | (3) | 83,573  |
| Chief Financial<br>Officer, Treasurer<br>and Secretary | 2009 | 90,000  | 0 | 76,468 | (1) | 5,700 | (3) | 172,168 |
| Kip Ferguson   | 2010 | 121,538 | 0 | 0      | (1) | 0     |     | 121,538 |
| Pharmacist   |      |         |   |        |     |       |     |         |

- (1) The amounts in the "Option Awards" column reflect the dollar amounts recognized as compensation expense for financial statement reporting purposes for stock options for the fiscal years ended December 31, 2010 and 2009 in accordance with ASC Topic 718. The assumptions we used to calculate these amounts are discussed in the notes to our consolidated financial statements included in this report on Form 10-K.
- (2) Mr. Corn resigned as an officer of our company on May 14, 2009. He continues to serve as a director.
- (3) Includes life insurance and disability insurance premiums paid by Company for executives.

#### Narrative Disclosure to the Summary Compensation Table

On May 15, 2009, we awarded Mr. Corn 210,900 non-qualified stock options to purchase common stock at \$0.80 per share. One-half of these stock options vested on the grant date and have a five year term. The remainder of the stock options granted vest 33 % on the first anniversary of the grant date, and then 8 % on the last day of each calendar quarter beginning June 30, 2010, and have a ten year term.

In connection with the closing of the Exchange, effective May 15, 2009, we adjusted Mr. Delaney's compensation to an annualized base salary of \$84,000. Mr. Delaney remains eligible to receive reimbursement for medical benefits and life and disability insurance, as well as reimbursement for reasonable business expenses.

On May 15, 2009, we awarded Mr. Delaney 210,900 incentive stock options to purchase common stock at \$0.80 per share. One-half of these stock options vested on the grant date, and have a five year term. The remainder of the stock options granted vest 33 % on the first anniversary of the grant date, and then 8 % on the last day of each calendar quarter beginning June 30, 2010, and have a ten year term.

On November 11, 2009, we awarded Mr. Delaney 100,000 incentive stock options to purchase common stock at \$2.50 per share, all of which have a ten year term. These options vest in equal annual installments on November 11, 2010, November 11, 2011 and November 11, 2012.

On May 20, 2009, we awarded Mr. Dhadphale 250,000 incentive stock options to purchase common stock at \$2.20 per share, all of which have a five year term. These options vest in equal annual installments on May 20, 2010, May 20, 2011 and May 20, 2012.

On October 14, 2010, we awarded Mr. Dhadphale 250,000 incentive stock options to purchase common stock at \$3.03 per share, all of which have a five year term. These options vest in equal annual installments on October 14, 2011, October 14, 2012, and October 14, 2013.

On October 14, 2010, we increased the annual base salary of Mr. Dhadphale to \$250,000 effective October 1, 2010, and granted Mr. Dhadphale a discretionary bonus of \$86,000, to be paid in 12 equal monthly installments.

#### Outstanding Equity Awards at Fiscal Year End

The following table summarizes equity awards outstanding at December 31, 2010, for each of the executive officers named in the Summary Compensation Table above:



| Name  | Number of Securities Underlying Unexercised Options (#) |               | Option Awards   |   | Option Exercise Price (\$) | Option Expiration Date |
|---|---|---------------|---|---|----------------------------|------------------------|
|   | Exercisable   | Unexercisable | Number of Securities Underlying Unexercised Options (#) | Equity Incentive Plan Awards: Number of Securities Underlying Unexercised Options (#) |                            |                        |
| Lalit Dhadphale<br>Chief Executive Officer and President    | 83,333 (1)  | 166,667 (1)   | —   | —   | 2.20                       | 5/20/14                |
|   | —   | 250,000 (2)   | —   | —   | 3.03                       | 10/14/15               |
| Norman E. Corn<br>former Chief Executive Officer (2)        | 12,500 (4)  | —             | —   | —   | 3.60                       | 1/23/11                |
|   | 105,450 (5)   | —             | —   | —   | 0.80                       | 5/15/14                |
|   | 61,511 (6)  | 43,939 (6)    | —   | —   | 0.80                       | 5/15/19                |
| Patrick E. Delaney<br>Chief Financial Officer and Treasurer | 12,500 (4)  | —             | —   | —   | 3.60                       | 1/23/11                |
|   | 105,450 (5)   | —             | —   | —   | 0.80                       | 5/15/14                |
|   | 61,511 (6)  | 43,939 (6)    | —   | —   | 0.80                       | 5/15/19                |
|   | 33,333 (7)  | 66,667 (7)    | —   | —   | 2.50                       | 11/11/19               |

- (1) Options vested 33 % on May 20, 2010, and then vest 33 % on each of May 20, 2011 and May 20, 2012.
- (2) Options vest 33 % on each of October 14, 2011, October 14, 2012 and October 14, 2013.
- (3) Mr. Corn resigned as an officer of our Company on May 14, 2009. He continues to serve as a director.
- (4) Options vested 34% on 12 months from date of grant, and then vested in 8 equal installments of 8.25% at the end of every three month period following the 12 month anniversary of the grant date.
- (5) All options were fully vested as of the grant date.
- (6) Options vested 33 % on May 15, 2010, and then vest 8 % on the last day of each calendar quarter beginning June 30, 2010.
- (7) Options vested 33 % on November 11, 2010, and then vest 33 % on each of November 11, 2011 and November 11, 2012.

#### Employment Agreements

None of our employees are subject to employment agreements with us at the moment. We intend to enter into employment agreements with Lalit Dhadphale, our President and Chief Executive Officer, and Patrick E. Delaney, our Chief Financial Officer and Treasurer, in the near future.

### Severance and Change in Control Arrangements

We do not have any agreements or arrangements providing for payments to any of our officers and directors in the event of a change in control or termination.

### Director Compensation

We expect to compensate non-management directors primarily through stock option or restricted stock grants under our stock option plans. At this time, we grant non-management directors options to purchase 30,000 shares upon their initial election to the board, and options to purchase 15,000 shares on an annual basis for serving on the board. Directors are expected to timely and fully participate in all regular and special board meetings, and all meetings of committees that they may serve on.

The table below summarizes the compensation we paid to non-management directors for the fiscal year ended December 31, 2010.

| Name                | Option Awards<br>(\$) <sup>(2)</sup> | Total<br>(\$) |
|---------------------|--------------------------------------|---------------|
| Matthew Stecker (1) | 51,316                               | 51,316        |

(1) Mr. Stecker was elected to our Board effective December 8, 2010. In connection with his election, we granted Mr. Stecker options to purchase 30,000 shares of our common stock, at an exercise price of \$3.75 per share, and with a term of ten years. The options vest 33 % on each of December 8, 2011, December 8, 2012, and December 8, 2013.

(2) The amounts in the “Option Awards” column reflect the dollar amounts recognized as compensation expense for financial statement reporting purposes for stock options for the fiscal year ended December 31, 2010 in accordance with ASC Topic 718.

### Equity Compensation Plan Information

On May 15, 2009, we adopted our 2009 Incentive Compensation Plan (the 2009 Plan). The total number of shares of common stock that may be subject to the granting of awards under the 2009 Plan is 2,700,000, plus 181,425 shares that remained available on May 15, 2009 under our 2006 Stock Option Plan. The 2009 Plan imposes individual limitations on the amount of certain awards. Under these limitations, during any fiscal year of our company, the number of options, stock appreciation rights, shares of restricted stock, shares of deferred stock, performance shares and other stock based-awards granted to any one participant under the 2009 Plan may not exceed 250,000 shares, subject to adjustment in certain circumstances. The maximum amount that may be paid out as performance units in any 12-month performance period is \$2,000,000, and the maximum amount that may be paid out as performance units in any performance period greater than 12 months is \$4,000,000. The maximum term of each option or stock appreciation right, the times at which each option or stock appreciation right will be exercisable, and provisions requiring forfeiture of unexercised options or stock appreciation rights at or following termination of employment generally are fixed by the Board, except that no option or stock appreciation right may have a term exceeding ten years. The exercise price per share subject to an option and the grant price of a stock appreciation rights are determined by the Board, but in the case of an incentive stock option (ISO) must not be less than the fair market value of a share of common stock on the date of grant. As of December 31, 2010, stock options to purchase up to 1,971,300 shares of common stock have been awarded under the 2009 Plan, with exercise prices ranging from \$0.80 to \$3.75 per share, of which approximately 660,000 are exercisable. All of these options have a five or ten year term.



In January 2006, we adopted our 2006 Stock Option Plan (the 2006 Plan). The aggregate number of shares of common stock for which options may be granted under the 2006 Plan was 200,000. Effective May 15, 2009, the 181,425 shares that remained available under the 2006 Plan were incorporated into the 2009 Plan. Accordingly, there will be no more issuances under the 2006 Plan. The maximum number of options which could be granted to an employee during any calendar year under the 2006 Plan was 15,000. The term of these non-transferable stock options could not exceed ten years. The exercise price of these stock options could not be less than 100% (110% if the person granted such options owned more than ten percent of the outstanding common stock) of the fair value of one share of common stock on the date of grant. As of December 31, 2010, 12,500 options are outstanding under the 2006 Plan, with an exercise price of \$3.60 per share, all of which are exercisable.

In June 1998, we adopted our 1998 Stock Option Plan (the 1998 Plan). The aggregate number of shares of common stock for which options may be granted under the 1998 Plan is 150,000. The maximum number of options which may be granted to an employee during any calendar year under the 1998 Plan is 20,000. The term of these non-transferable stock options may not exceed ten years. The exercise price of these stock options may not be less than 100% (110% if the person granted such options owns more than ten percent of our outstanding common stock) of the fair value of one share of common stock on the date of grant. As of December 31, 2010, 12,500 options are outstanding under the 1998 Plan, with an exercise price of \$3.60 per share, all of which are exercisable. The 1998 Plan terminated on June 16, 2008.

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

### Securities Authorized for Issuance Under Equity Compensation Plans

The following table provides information as of December 31, 2010, with respect to the shares of common stock that may be issued under our existing equity compensation plan.

### Equity Compensation Plan Information

| Plan category  | Number of shares of common stock to be issued upon exercise of outstanding options, warrants and rights<br>(a) | Weighted-average exercise price of outstanding options, warrants and rights<br>(b) | Number of securities remaining available for future issuance under equity compensation plans (excluding securities reflected in column (a))<br>(c) |
|--|--|--|--|
| Equity compensation plans approved by security holders         | 1,996,300 (1)  | \$ 2.14  | 910,125 (2)  |
| Equity compensation plans not approved by security holders (3) | 1,915,340  | \$ 2.79  | -0-  |
| <b>Total</b>   | <b>3,911,640</b>   | <b>\$ 2.47</b>   | <b>910,125</b>   |

(1) Includes options to purchase 1,971,300 shares of our Common Stock granted under our 2009 Incentive Compensation Plan (the "2009 Plan"), options to purchase 12,500 shares of our Common Stock granted under our

2006 Stock Option Plan (the “2006 Plan”), and options to purchase 12,500 shares of our Common Stock granted under our 1998 Stock Option Plan, with exercise prices ranging from \$0.80 to \$3.75 per share.

(2) Remaining shares available as of December 31, 2009 for future issuance under our 2009 Plan (including 181,425 shares that remained available on May 15, 2009 under our 2006 Plan and that are now available for issuance under our 2009 Plan).

(3) Description of equity compensation plans not approved by security holders:

On December 15, 2009, we entered into a Loan and Security Agreement (the "Loan Agreement") with HWH Lending LLC, a Delaware limited liability company ("HWH"). Under the terms of the Loan Agreement, we borrowed \$515,000 from HWH on December 15, 2009, and we borrowed an additional \$500,000 from HWH on May 3, 2010 (together, the "Loans"). The proceeds of the Loans were used by us for working capital purposes. The Loans bore interest at the rate of 12% per annum, payable at maturity. The maturity date of each Loan was one year from the date of the Loan. The Loans were repaid by us in connection with the 2010 Private Placement described below. In consideration of the Loans, we granted HWH warrants to purchase 625,000 shares of our Common Stock at a purchase price of \$1.60 per share. Each warrant may be exercised in whole or in part and from time to time for a term of five years from its grant date. The warrants contain customary anti-dilution and purchase price adjustment provisions. The warrants are transferable in whole or in part, so long as the transfers comply with applicable securities laws. In November 2010, HWH transferred warrants to purchase 312,500 shares of our Common Stock to Milfam I, L.P., a Georgia limited partnership.

In consideration for providing investment banking services in connection with the Loans, we granted Kaufman Bros., L.P., warrants to purchase 18,750 shares of our Common Stock at a purchase price of \$1.60 per share. The Kaufman Bros. warrants have the same terms and conditions as HWH's warrants.

On November 8, 2010, we entered into a Securities Purchase Agreement (the "Purchase Agreement" with four accredited investors (the "Investors") and sold certain securities to the Investors in a non-public offering under Section 4(2) and under Rule 506 of Regulation D under the Securities Act of 1933 (the "2010 Private Placement"). Under the terms of the Purchase Agreement, we sold a total of 365,265 newly authorized shares of \$0.001 par value Series B preferred stock (the "Series B Preferred Stock") to the Investors at \$9.45 per share, for an aggregate price of approximately \$3,450,000. Each share of the Series B Preferred Stock may be converted at any time, in whole or in part, into five shares of our Common Stock, as adjusted. We also entered into a separate Loan and Security Agreement dated November 8, 2010 with two of the Investors (the "2010 Loan Agreement"). Under the terms of the 2010 Loan Agreement and the Purchase Agreement, we sold convertible promissory notes to those Investors in the aggregate principal amount of \$1,000,000 (the "Convertible Notes"). The Convertible Notes bear interest at the rate of 7% per annum compounded annually. The principal amount and all accrued interest on the Convertible Notes are payable on December 31, 2012, or earlier on an event of default or a sale or liquidation of the Company. The principal amount and accrued interest on the Convertible Notes may be converted at any time into shares of Series B Preferred Stock at a conversion price of \$9.45 per share, as adjusted. We intend to use the net proceeds from the 2010 Private Placement to expand our online presence, upgrade our technology infrastructure, and pay existing indebtedness and accrued expenses, and for general working capital purposes. Under the terms of the Purchase Agreement, we also issued warrants to the Investors, prorata to their investment amounts, to purchase an aggregate of 1,271,590 shares of our Common Stock at an exercise price of \$3.00 per share (the "Warrants"). Each Warrant may be exercised in whole or in part and from time to time for a term of five years from its grant date. The warrants contain customary anti-dilution and purchase price adjustment provisions. The warrants are transferable in whole or in part, so long as the transfers comply with applicable securities laws.

#### Security Ownership of Certain Beneficial Owners and Management

The following table sets forth certain information regarding the ownership of our Common Stock as of March 10, 2011 by: (a) each current director; (b) each executive officer; (c) all of our current executive officers and directors as a

group; and (d) all those known by us to be beneficial owners of more than five percent of our Common Stock.

| Name (1)  | Number of Shares Beneficially Owned (2) | Percentage of Shares Beneficially Owned (3) |   |
|---|---|---|---|
| <b>5% or Greater Stockholders:</b>                          |   |   |   |
| Cape Bear Partners, LLC (4)                                 | 1,302,540                               | 12.3  | % |
| Jason Smith (5)   | 1,369,333                               | 12.8  | % |
| Karen Singer (6)  | 1,991,728                               | 15.9  | % |
| Lloyd I. Miller III (7)                                     | 1,991,728                               | 15.9  | % |
| John C. Backus and Todd L. Hixon Group(8)                   | 1,623,024                               | 15.3  | % |
| <b>Executive Officers and Directors:</b>                    |   |   |   |
| Lalit Dhadphale (9)   | 2,046,720                               | 19.2  | % |
| Patrick E. Delaney (10)                                     | 215,331                                 | 2.0   | % |
| Youssef Bennani (11)  | 50,000                                  | *   |   |
| Norman E. Corn (12)   | 189,578                                 | 1.8   | % |
| Matthew Stecker (13)  | -0-                                     | 0   | % |
| Joseph Savarino (14)  | 109,948                                 | 1.0   | % |
| All executive officers and directors as a group (6 persons) | 2,611,577                               | 23.5  | % |

\* Less than 1.0%

- (1)The address of each officer and director is c/o HealthWarehouse.com, Inc., 100 Commerce Boulevard, Cincinnati, Ohio 45140.
- (2)This table is based upon information supplied by officers, directors and principal stockholders and Schedules 13D and 13G filed with the SEC. Unless otherwise indicated, includes shares owned by a spouse, minor children and relatives sharing the same home, as well as the entities owned or controlled by the named person. Also includes shares if the named person has the right to acquire those shares within 60 days after March 10, 2011, by the exercise of any warrant, stock option, convertible note, or other right. Unless otherwise indicated in the footnotes to this table and subject to community property laws where applicable, we believe that each of the stockholders named in this table has sole voting and investment power with respect to the shares indicated as beneficially owned.
- (3)Applicable percentages are based on 10,577,719 shares of Common Stock outstanding on March 10, 2011, adjusted as required by rules promulgated by the SEC. Does not include 368,862 shares of Series B Preferred Stock outstanding on March 10, 2011, which shares are convertible into 1,844,300 shares of Common Stock. The shares of Common Stock and shares underlying convertible preferred stock, convertible notes, and stock options or warrants are deemed outstanding for purposes of computing the percentage of the person holding such convertible preferred stock, convertible notes, and/or stock options or warrants but are not deemed outstanding for the purpose of computing the percentage of any other person.
- (4)Lynn Peppel is the Managing Member of Cape Bear Partners LLC and has sole voting and investment power over the shares owned by Cape Bear Partners LLC. Cape Bear Partners LLC's address is 703 Solana Shores Drive, Apt 406B Cape Canaveral, Fl 32920
- (5)Includes (i) 1,252,667 shares owned by Rock Castle Holdings, LLC, (ii) stock options to purchase 33,333 shares of Common Stock held by Jason Smith, and (iii) stock options to purchase 83,333 shares of Common Stock held by Rock Castle. Does not include stock options to purchase 66,667 and 166,667 shares of Common Stock held by Jason Smith and Rock Castle, respectively, that are not currently exercisable. As the Manager of Rock Castle,



Jason Smith has sole dispositive and voting power with respect to the securities owned by Rock Castle. Rock Castle Holdings, LLC's address is 6434 Hamilton Mason Road Hamilton , Ohio 45069.

(6) Includes (i) warrants to purchase 898,308 shares of Common Stock, (ii) 165,774 shares of Series B Preferred Stock convertible into 828,870 shares of Common Stock, and (iii) a convertible note in the amount of \$500,000 convertible into 264,550 shares of Common Stock. The securities described above are owned by HWH Lending, LLC, a Delaware limited liability company ("HWH"). Ms. Singer is the sole trustee of The Singer Children's Management Trust (the "Trust"). The Trust is the sole member of HWH. As the trustee of the Trust, Ms. Singer has sole dispositive and voting power with respect to the securities owned by HWH. Ms. Singer's address is 212 Vaccaro Drive, Cresskill, NJ 07626. The information in this Note 6 is based on the information contained in the Schedule 13D filed with the SEC by Ms. Singer on November 18, 2010.

(7) Includes (i) warrants to purchase 898,308 shares of Common Stock, (ii) 165,774 shares of Series B Preferred Stock convertible into 828,870 shares of Common Stock, and (iii) a convertible note in the amount of \$500,000 convertible into 264,550 shares of Common Stock. The securities described above are owned by Milfam I L.P., a Georgia limited partnership (“Milfam L.P.”) Milfam LLC, an Ohio limited liability company (“Milfam LLC”) is the general partner of Milfam L.P. Mr. Miller is the manager of Milfam LLC. As the manager of Milfam LLC, Mr. Miller has sole dispositive and voting power with respect to the securities owned by Milfam L.P. Mr. Miller’s address is 4550 Gordon Drive, Naples FL 34102. The information in this Note 7 is based on the information contained in the Schedule 13D filed with the SEC by Mr. Miller on November 18, 2010.

(8) Consists of (i) 1,548,143 shares owned by New Atlantic Venture Fund III, L.P., a Delaware limited partnership (“NAV”), (ii) 57,519 shares owned by New Atlantic Entrepreneur Fund III, L.P., a Delaware limited partnership (“NAE”), and (iii) 17,362 shares owned by NAV Managers Fund, LLC, a Delaware limited liability company (“NAV Managers”). New Atlantic Fund III, LLC, a Delaware limited liability Company (“NAF”), is the general partner of NAV and NAE. Each of NAV, NAE and NAV Managers has shared voting and dispositive power over the shares owned by such entity.

John C. Backus is a managing member of NAV, NAE and NAF, and is a member of NAV Managers. As such, Mr. Backus has shared voting and dispositive power over the 1,623,024 shares owned in total by NAV, NAE, and NAV Managers.

Todd L. Hixon is a managing member of NAV, NAE and NAF, and is a member of NAV Managers. As such, Mr. Hixon has shared voting and dispositive power over the 1,623,024 shares owned in total by NAV, NAE, and NAV Managers.

Scott M. Johnson is a managing member of NAV, NAE and NAF. As such, Mr. Johnson has shared voting and dispositive power over the 1,605,662 shares owned in total by NAV and NAE.

Thanasis Delistathis is a managing member of NAV, NAE and NAF. As such, Mr. Delistathis has shared voting and dispositive power over the 1,605,662 shares owned in total by NAV and NAE.

As the general partner of NAV and NAE, NAF has shared voting and dispositive power over the 1,605,662 shares owned in total by NAV and NAE.

The business address for NAV, NAE, NAV Managers, NAF, John C. Backus, Todd C. Hixon, Scott M. Johnson and Thanasis Delistathis is 11911 Freedom Drive, Suite 1080, Reston, VA 20190.

The information in this Note 8 is based on the information contained in the Schedule 13D filed with the SEC by the John C. Backus and Todd L. Hixon group on January 6, 2011.

(9) Includes stock options to purchase 83,333 shares of Common Stock. Does not include stock options to purchase 416,667 shares of Common Stock that are not currently exercisable.

(10) Includes stock options to purchase 209,081 shares of Common Stock. Does not include stock options to purchase 101,819 shares of Common Stock that are not currently exercisable.

(11) Includes stock options to purchase 50,000 shares of Common Stock. Does not include stock options to purchase 115,000 shares of Common Stock that are not currently exercisable.

(12)

Includes stock options to purchase 175,748 shares of Common Stock. Does not include options to purchase 50,152 shares of Common Stock that are not currently exercisable.

(13) Does not include stock options to purchase 30,000 shares of Common Stock that are not currently exercisable.

(14) Does not include stock options to purchase 30,000 shares of Common Stock that are not currently exercisable.

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

#### Related Party Transactions

Lalit Dhadphale, our President and Chief Executive Officer, and Cape Bear Partners LLC, the beneficial owner of 12.3% of our Common Stock, guaranteed Old HW's obligations under certain Old HW convertible promissory notes with an original principal value of approximately \$1,200,000, which notes we assumed in connection with the Exchange. The guarantees state that Mr. Dhadphale and Cape Bear Partners LLC each guarantee the full payment of principal and interest under the notes. The guarantees terminate with respect to each note upon the earlier of repayment of principal and interest under each note or conversion of the note to equity. In the event of note conversion, the guarantees remain in place with respect to any interest due and unpaid through the date of conversion until that interest has been paid. During the fourth quarter of 2009 and during 2010, the holders of notes in an aggregate principal amount of \$1,000,000 elected to convert their notes. The maximum principal exposure of each of Mr. Dhadphale and Cape Bear Partners LLC pursuant to the guarantees as of December 31, 2010 is \$200,000, plus interest. On January 5, 2011, the remaining convertible note balance of \$200,000 was converted plus all accrued interest was paid eliminating any exposure for each of Mr. Dhadphale and Cape Bear Partners LLC pursuant to the guarantees.

On December 15, 2009, we entered into a Loan and Security Agreement (the "Loan Agreement") with HWH Lending LLC, a Delaware limited liability company ("HWH"). Under the terms of the Loan Agreement, we borrowed \$515,000 from HWH on December 15, 2009, and we borrowed an additional \$500,000 on May 3, 2010 (together, the "Loans"). The proceeds of the Loans were used by us for working capital purposes. The Loans were evidenced by promissory notes (the "Notes"), and bore interest at the rate of 12% per annum, payable at maturity. The maturity date of each Loan was one year from the date of the Loan. The Loans could be prepaid in whole or in part at any time by us without penalty, upon 15 days notice. Lalit Dhadphale, our President and Chief Executive Officer, personally guaranteed our payment and other obligations under the Loan Agreement and the Notes. Mr. Dhadphale also entered into a Lock-up Agreement with HWH prohibiting Mr. Dhadphale from selling or transferring 625,000 shares of our common stock until the Loans are repaid in full, subject to certain exceptions, such as gifts. We prepaid the Loans in full on November 8, 2010, and Mr. Dhadphale's personal guaranty and the Lock-Up were terminated.

As of March 10, 2011, Jason Smith is the beneficial owner of 1,369,333 shares, or 12.8% of our Common Stock, of which 33,333 shares are beneficially owned by him directly, and 1,336,000 shares are beneficially owned by Rock Castle Holdings, LLC ("Rock Castle"). As the Manager of Rock Castle, Jason Smith has sole voting and dispositive power over the shares owned by Rock Castle and, as such, is deemed to beneficially own such shares.

We are a party to oral consulting agreements with Jason Smith and Rock Castle under which Jason Smith and affiliates of Rock Castle provide purchasing and advisory services to us. Pursuant to these consulting agreements, on May 20, 2009, we granted to Jason Smith and Rock Castle, respectively, non-qualified options to purchase 100,000 and 250,000 shares of our common stock, all with a ten year term. These options vest in equal annual installments on May 20, 2010, May 20, 2011 and May 20, 2012. The consulting agreements are terminable at will.

The Company occupies approximately 16,000 square feet of office and storage space under a Commercial Sublease Agreement with Masters Healthcare, LLC, an entity that is also controlled by Jason Smith. The sublease currently has a monthly rental rate of \$9,417, through March 2011, its expiration date. The rent expense under the sublease for the years ended December 31, 2010 and December 31, 2009 was \$113,004 and \$93,750, respectively. We are currently on a month-to-month tenancy.

Jason Smith is also the son of Dennis Smith, the controlling stockholder of Masters Pharmaceutical, Inc., one of the Company's principal suppliers. We purchased from Masters Pharmaceutical, Inc., \$959,847 and \$1,342,997 of supplies, representing approximately 29% and 49% of total purchases during the years ended December 31, 2010 and 2009, respectively. Accounts payable due to Masters Pharmaceutical, Inc. at December 31, 2010 and 2009 was \$215,858 and \$24,969, respectively. At December 31, 2010, we also had accrued interest expense due to Masters Pharmaceutical, Inc. of \$17,000. Wayne A. Corona, formerly our Secretary and a member of our board of directors, is Vice President of Business Development at Masters Pharmaceutical, Inc.

For the year ended December 31, 2010 and 2009, sales to Masters Pharmaceuticals were approximately 8.76% and 4.27%, respectively, of net sales.

On April 29, 2009, as a part of the Old HW private financing completed before the Exchange, we issued to Wayne A Corona, formerly our Secretary and a member of our board of directors, \$75,000 in principal amount of convertible promissory notes convertible into 49,551 shares of our Common Stock in consideration of \$75,000 in cash. On the same date, we issued to MKW Partners, LLC, of which Mr. Corona is the Manager, \$50,000 in principal amount of convertible promissory notes convertible into 33,032 shares of our Common Stock in consideration of \$50,000 in cash. Mr. Corona and MKW Partners elected to convert these notes in the fourth quarter of 2009, and received an aggregate of 82,583 shares of our Common Stock in exchange.

On April 30, 2009, also as a part of such Old HW private financing, we issued to Kip Ferguson, the brother of a former Old HW director, Ron Ferguson, \$25,000 in principal amount of convertible promissory notes convertible into 16,520 shares of our Common Stock in consideration of \$25,000 in cash. Mr. Ferguson elected to convert his note in the fourth quarter of 2009, and received 16,520 shares of our Common Stock in exchange.

On May 8, 2009, also as a part of such Old HW private financing, we issued to Rock Castle \$300,000 in principal amount of convertible promissory notes convertible into 198,180 shares of our Common Stock in consideration of \$300,000 in cash. Rock Castle elected to convert its promissory note in the fourth quarter of 2009, and received 198,180 shares of our Common Stock in exchange.

On May 20, 2009, we granted Mr. Corona non-qualified options to purchase 250,000 shares of our common stock, all with a five year term. These options would have vested in equal annual installments on May 20, 2010, May 20, 2011 and May 20, 2012. These options terminated on November 9, 2009, the date Mr. Corona resigned from our Board.

Ron Ferguson, a former Old HW director, has guaranteed Old HW's obligations to supplier Prescription Supply Inc. Mr. Ferguson is the spouse of Diane Ferguson, a stockholder of our company. The guarantee, and Mr. Ferguson's maximum exposure under the guarantee, does not have a fixed dollar limit. As of December 31, 2010 and 2009, there was \$0 and \$6,172, respectively, due to Prescription Supply Inc.

During the year ended December 31, 2010, a former director advanced \$521,000 in short term financing to the Company. A payment of \$535,000 was made during the year ended December 31, 2010. During the year ended December 31, 2009, a former director advanced \$25,000 in short term financing to the Company. A payment of \$25,000 was made during the year ended December 31, 2009.

Although we have not adopted formal procedures for the review, approval or ratification of transactions with related persons, we adhere to a general policy that such transactions should only be entered into if they are on terms that, on the whole, are no more favorable, or no less favorable, than those available from unaffiliated third parties and their approval is in accordance with applicable law. Such transactions require the approval of our board of directors.

#### Director Independence

Our board of directors has determined that Youssef Bennani is "independent" within the meaning of Rule 5605(a)(2) of the National Association of Securities Dealers' Marketplace Rules of the Nasdaq Stock Market (the "NASDAQ Rules"), and that he is also "independent" for purposes of Rule 10A-3 of the Exchange Act. Lalit Dhadphale and Norman E. Corn are not "independent" within the meaning of Rule 5605(a)(2) of the NASDAQ Rules. In addition, Frank S. Russo and Stephen M. Deixler, who resigned from our board of directors effective May 14, 2009 and June 27, 2009, respectively, and who were formerly members of our audit committee, compensation committee and nominating committee, were "independent" within the meaning of Rule 5605(a)(2) of the NASDAQ Rules and for purposes of Rule

10A-3 of the Exchange Act.

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In making each of these independence determinations, our board of directors considered and broadly assessed, from the standpoint of materiality and independence, all of the information provided by each director in response to detailed inquiries concerning the director’s independence and any direct or indirect business, family, employment, transactional or other relationship or affiliation of such director with our company

Item 14. Principal Accounting Fees and Services.

The following table presents fees for professional services rendered by the Company’s principal accountants. Prior to May 14, 2009, Clark Schaeffer Hackett LLP served as principal accountants. Marcum LLP, formerly known as Marcum & Kliegman LLP (“Marcum”) became our principal accountant on May 14, 2009 the table below represents amounts billed for the audit of the Company’s annual consolidated financial statements for the years ended December 31, 2010, and December 31, 2009, and fees billed for other services rendered by our principal accountants during those periods.

|                        | Year Ended<br>December 31, 2010 | Year Ended<br>December 31, 2009 |
|------------------------|---------------------------------|---------------------------------|
| Audit Fees (1)         | \$ 118,178                      | \$ 95,628                       |
| Audit Related Fees (2) | -                               | -                               |
| Tax Fees (3)           | -                               | -                               |
| All Other Fees (4)     | -                               | -                               |

(1) Audit fees were principally for audit work performed on our annual financial statements and review of our interim financial statements.

(2) There were no “audit-related services” during the period.

(3) There were no “tax services” during the period.

(4) There were no “other services” during the period.

An audit committee was formed on April 8, 2010 (see item 10 of this report). During the year ended December 31, 2010, the Audit Committee met to review and approve the filing of forms 10K and 10Q. All audit and non-audit services performed by Marcum were pre-approved by the Board of Directors. During the year ended December 31, 2009, the Company did not have an audit committee.



PART IV

Item 15. Exhibits, Financial Statement Schedules.

(a) Exhibits:

| Exhibit No. | Description   |
|-------------|---|
| 2.1         | Share Exchange Agreement, dated May 14, 2009, between Clacendix, Inc. and HealthWarehouse.com, Inc. (1)   |
| 2.2         | Asset Purchase Agreement, dated February 14, 2011, among Hocks Acquisition Corporation, and Hocks Pharmacy, Inc. and its shareholders (16)                                    |
| 2.3         | Merger Agreement dated February 14, 2011, among HealthWarehouse.com, Inc., Hocks Acquisition Corporation, Hocks Pharmacy, Inc. and its shareholders, and Hocks.com, Inc. (16) |
| 3.1         | Certificate of Incorporation of the Company, as amended through December 31, 2005 (2)   |
| 3.2         | Certificate of Amendment of the Certificate of Incorporation of the Company, filed on January 4, 2008 (3)   |
| 3.3         | Certificate of Amendment of the Certificate of Incorporation of the Company, filed on July 14, 2008 (4)   |
| 3.4         | Certificate of Amendment of the Certificate of Incorporation of the Company, filed on July 31, 2009 (5)   |
| 3.5         | Certificate of Amendment to the Company's Certificate of Incorporation filed on July 16, 2010 (13)  |
| 3.6         | Certificate of Designation of Preferences, Rights and Limitations of Series B Preferred Stock Pursuant to Section 151 of the Delaware General Corporation Law (14)            |

- 3.7 Amended and Restated By-Laws of the Company (14)
- 4.1 Form of Old HW Convertible Promissory Note (11)
- 4.2 Senior Secured Promissory Note dated December 15, 2009 in the principal amount of \$515,000 payable by the Company to the order of HWH Lending, LLC (7)
- 4.3 Senior Secured Promissory Note dated May 3, 2010 in the principal amount of \$500,000, payable by the Company to the order of HWH Lending, LLC (12)
- 4.4 Warrant to Purchase 156,250 Shares of the Common Stock of HealthWarehouse.com, Inc. dated November 8, 2010 and Issued to HWH Lending, LLC, as Lender \*
- 4.5 Warrant to Purchase 156,250 Shares of Common Stock of HealthWarehouse.com, Inc. dated November 8, 2010 and issued to HWH Lending, LLC as Lender \*
- 4.6 Warrant to Purchase 156,250 Shares of Common Stock of HealthWarehouse.com, Inc. dated November 8, 2010 and issued to Milfam I L.P. \*
- 4.7 Warrant to Purchase 156,250 Shares of Common Stock of HealthWarehouse.com, Inc. dated November 8, 2010 and issued to Milfam I L.P. \*
- 4.8 Form of Common Stock Purchase Warrant (14)
- 4.9 Senior Secured Convertible Promissory Note dated November 8, 2010 in the amount of \$500,000 payable by the Company to the order of Milfam I L.P. (14)
- 4.10 Senior Secured Convertible Promissory Note dated November 8, 2010 in the amount of \$500,000 payable by the Company to the order of HWH Lending, LLC (14)
- 10.1 1998 Stock Option Plan of the Company (6) +
- 10.2 2000 Stock Option Plan of the Company (2) +
- 10.3 2006 Stock Option Plan of the Company (2) +
- 10.4 Form of Incentive Stock Option Agreement under 2006 Stock Option Plan of the Company (8) +
- 10.5 Old HW Convertible Promissory Note Subscription Agreement (11)
- 10.6 Old HW Convertible Promissory Note and Warrants to Purchase Common Stock Subscription Agreement (11)
- 10.7 2009 Incentive Compensation Plan (9) +
- 10.8 Form of Stock Option Agreements under 2009 Incentive Compensation Plan (11) +
- 10.9 Loan and Security Agreement dated December 15, 2009 among HealthWarehouse.com, Inc. and Hwareh.com, Inc. as Borrowers, and HWH Lending LLC, as Lender (7)

- 10.10 Securities Purchase Agreement dated November 8, 2010 (14)
- 10.11 Loan and Security Agreement dated November 8, 2010 among HealthWarehouse.com, Inc. and Hwareh.com, Inc., as Borrowers, and HWH Lending, LLC and Milfam I L.P. as Lenders (14)

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- 10.12 Commercial Sublease Agreement between the Company and Masters Healthcare, LLC dated effective April 1, 2008, as amended by a First Amendment dated effective June 1, 2009 (15)
- 21.1 Subsidiaries of the Registrant \*
- 31.1 Certification of CEO Pursuant to Section 302 of the Sarbanes Oxley Act of 2002\*
- 31.2 Certification of CFO Pursuant to Section 302 of the Sarbanes Oxley Act of 2002\*
- 32.1 Certification of CEO Pursuant to Section 906 of the Sarbanes Oxley Act of 2002\*
- 32.2 Certification of CFO Pursuant to Section 906 of the Sarbanes Oxley Act of 2002\*

\* Filed herewith.

+ Denotes Management Compensatory Plan or Contract.

- (1) Incorporated by reference to the Company's Current Report on Form 8-K filed on May 15, 2009.
- (2) Incorporated by reference to the Company's Annual Report on Form 10-K SB filed on March 29, 2006.
- (3) Incorporated by reference to the Company's Annual Report on Form 10-K filed on March 27, 2009.
- (4) Incorporated by reference to the Company's Annual Report Amendment on Form 10-KA filed on May 14, 2009.
- (5) Incorporated by reference to the Company's Current Report on Form 8-K filed on August 6, 2009.
- (6) Incorporated by reference to the Company's Registration Statement on Form S-8 filed on April 22, 1999.
- (7) Incorporated by reference to the Company's Current Report on Form 8-K filed on December 17, 2009.
- (8) Incorporated by reference to the Company's Current Report on Form 8-K filed on November 14, 2006.
- (9) Incorporated by reference to the Company's Current Report Amendment on Form 8-KA filed on May 26, 2009.
- (10) Incorporated by reference to the Company's Current Report Amendment on Form 8-KA filed on August 17, 2009.
- (11) Incorporated by reference to the Company's Annual Report on Form 10-K filed on April 15, 2010.
- (12) Incorporated by reference to the Company's Current Report on Form 8-K filed on May 5, 2010.
- (13) Incorporated by reference to the Company's Current Report on Form 8-K filed on July 21, 2010.
- (14) Incorporated by reference to the Company's Current Report on Form 8-K filed on November 12, 2010.
- (15) Incorporated by reference to the Company's Amendment No. 1 on Form 10-K/A filed on November 30, 2010.
- (16) Incorporated by reference to the Company's Current Report on Form 8-K filed on February 16, 2011.



SIGNATURES

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

Dated: April 15, 2011

HEALTHWAREHOUSE.COM, INC.

By: /s/ Lalit Dhadphale  
Lalit Dhadphale  
President and Chief Executive Officer  
(principal executive officer)

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

| Name   | Title   | Date           |
|--|---|----------------|
| /s/ Lalit Dhadphale<br>Lalit Dhadphale       | President, Chief Executive Officer<br>and<br>Director<br>(principal executive officer)                  | April 15, 2011 |
| /s/ Patrick E. Delaney<br>Patrick E. Delaney | Chief Financial Officer, Treasurer,<br>and<br>Secretary (principal financial and<br>accounting officer) | April 15, 2011 |
| /s/ Youssef Bennani<br>Youssef Bennani       | Director  | April 15, 2011 |
| /s/ Norman E. Corn<br>Norman E. Corn         | Director  | April 15, 2011 |
| Matthew Stecker                              | Director  | April 15, 2011 |
| Joseph Savarino                              | Director  | April 15, 2011 |

Healthwarehouse.com, Inc. and Subsidiaries

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For the Years Ended December 31, 2010 and 2009

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Report of Independent Registered Public Accounting Firm

To the Audit Committee of the Board of Directors and Stockholders of Healthwarehouse.com, Inc.

We have audited the accompanying consolidated balance sheets of Healthwarehouse.com, Inc. and Subsidiaries (the “Company”) as of December 31, 2010 and 2009, and the related consolidated statements of operations, stockholders’ equity (deficiency) and cash flows for the years then ended. These consolidated financial statements are the responsibility of the Company’s management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

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

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the consolidated financial position of Healthwarehouse.com, Inc. and Subsidiaries as of December 31, 2010 and 2009, and the consolidated results of their operations and their cash flows for the years then ended, in conformity with accounting principles generally accepted in the United States of America.

/s/ Marcum LLP

New York, NY  
April 15, 2011

HEALTHWAREHOUSE.COM, INC. AND SUBSIDIARIES  
CONSOLIDATED BALANCE SHEETS

|  | December 31, 2010   | December 31, 2009   |
|--|---------------------|---------------------|
| <b>Assets</b>  |                     |                     |
| <b>Current assets</b>  |                     |                     |
| Cash   | \$ 1,397,583        | \$ 191,181          |
| Accounts receivable, net   | 604,524             | 277,716             |
| Inventories  | 374,519             | 388,748             |
| Employee advances  | 51,429              | -                   |
| Prepaid expenses and other current assets  | 126,708             | 190,999             |
| <b>Total current assets</b>  | <b>\$ 2,554,763</b> | <b>\$ 1,048,644</b> |
| <b>Property and equipment, net</b>   | <b>320,328</b>      | <b>318,793</b>      |
| Website development costs, net of accumulated amortization of \$139,475 and \$39,275, respectively   | 60,921              | 161,121             |
| <b>Total assets</b>  | <b>\$ 2,936,012</b> | <b>\$ 1,528,558</b> |
| <b>Liabilities and Stockholders' Equity (Deficiency)</b>   |                     |                     |
| <b>Current liabilities</b>   |                     |                     |
| Accounts payable – related parties   | \$ 232,858          | \$ 73,254           |
| Accounts payable – trade   | 807,481             | 802,607             |
| Accrued expenses and other current liabilities   | 240,098             | 72,766              |
| Convertible notes, net of deferred debt discount of \$9,658 and \$0, respectively  | 215,342             | -                   |
| Note payable, net of deferred debt discount of \$0 and \$157,713, respectively   | -                   | 357,287             |
| <b>Total current liabilities</b>   | <b>\$ 1,495,779</b> | <b>\$ 1,305,914</b> |
| Convertible notes payable, net of deferred debt discount of \$600,354 and \$30,737, respectively   | 399,646             | 594,263             |
| <b>Total liabilities</b>   | <b>\$ 1,895,425</b> | <b>\$ 1,900,177</b> |
| <b>Commitments and contingencies</b>   |                     |                     |
| <b>Stockholders' equity (deficiency)</b>   |                     |                     |
| Convertible preferred stock - Series A – par value \$.001 per share; authorized 1,000,000 shares; 200,000 shares designated Series A; 0 and 107,501 shares issued, and outstanding respectively (aggregate liquidation preference \$0)         | -                   | 108                 |
| Convertible preferred stock - Series B – par value \$.001 per share; authorized 1,000,000 shares; 625,000 shares designated Series B; 365,265 and 0 shares issued, and outstanding respectively (aggregate liquidation preference \$3,451,754) | 365                 | -                   |
| Common stock – par value \$.001 per share; authorized 50,000,000 shares; 10,278,934 and 9,881,767 shares issued and outstanding  | 10,279              | 9,882               |
| Additional paid-in capital   | 9,540,036           | 2,735,851           |
| Accumulated deficit  | (8,510,093 )        | (3,117,460 )        |

|   |              |              |
|---|--------------|--------------|
| Total stockholders' equity (deficiency)                 | 1,040,587    | (371,619 )   |
| Total liabilities and stockholders' equity (deficiency) | \$ 2,936,012 | \$ 1,528,558 |

The accompanying notes are an integral part of these consolidated financial statements.

HEALTHWAREHOUSE.COM, INC. AND SUBSIDIARIES  
CONSOLIDATED STATEMENTS OF OPERATIONS

|  | For the Year Ended<br>December 31, 2010 | For the Year Ended<br>December 31, 2009 |
|--|---|---|
| Net sales  | \$ 5,691,765                            | \$ 3,783,542                            |
| Cost of sales  | 3,450,021                               | 2,635,258                               |
| Gross profit   | 2,241,744                               | 1,148,284                               |
| Operating expenses:  |   |   |
| Selling, general and administrative expenses                               | 5,303,617                               | 3,646,915                               |
| Loss from operations   | (3,061,873 )                            | (2,498,631 )                            |
| Other income (expense):  |   |   |
| Interest income  | 642                                     | 605                                     |
| Interest expense   | (679,330 )                              | (38,150 )                               |
| Gain on litigation settlement  | 48,887                                  | -                                       |
| Other income (expense)   | -                                       | 96,674                                  |
| Total other income (expense)   | (629,801 )                              | 59,129                                  |
| Net loss   | \$ (3,691,674 )                         | \$ (2,439,502 )                         |
| Series B Convertible Preferred Stock:                                      |   |   |
| Contractual dividends  | (33,992 )                               | -                                       |
| Deemed dividends - beneficial conversion feature                           | (1,666,967 )                            | -                                       |
| Loss attributable to common stockholders                                   | \$ (5,392,633 )                         | \$ (2,439,502 )                         |
| Per share data:  |   |   |
| Net loss per common share from operations - Basic and diluted              | \$ (0.37 )                              | \$ (0.28 )                              |
| Series B convertible preferred stock contractual dividends                 | \$ (0.00 )                              | \$ (0.00 )                              |
| Series B convertible preferred stock deemed dividends                      | \$ (0.17 )                              | \$ (0.00 )                              |
| Net loss attributable to common stockholders per share – basic and diluted | \$ (0.54 )                              | \$ (0.28 )                              |
| Weighted average number of common shares outstanding - Basic and diluted   | 10,068,575                              | 8,884,844                               |

The accompanying notes are an integral part of these consolidated financial statements.

HEALTHWAREHOUSE.COM, INC. AND SUBSIDIARIES  
CONSOLIDATED STATEMENTS OF CASH FLOWS

|  | For the Year<br>Ended December 31, 2010 | For the Year<br>Ended December 31, 2009 |
|--|---|---|
| <b>Cash flows from operating activities</b>                              |   |   |
| Net loss   | \$ (3,691,674 )                         | \$ (2,439,502 )                         |
| Adjustments to reconcile net loss to net cash from operating activities: |   |   |
| Provision for doubtful accounts  | 180,899                                 | -                                       |
| Depreciation and amortization  | 198,836                                 | 122,379                                 |
| Stock-based compensation   | 490,765                                 | 260,318                                 |
| Amortization of deferred debt discount                                   | 543,407                                 | 21,574                                  |
| Extinguishment of debt   | -                                       | (96,069 )                               |
| Gain on litigation settlement  | (48,887 )                               | -                                       |
| Changes in operating assets and liabilities:                             |   |   |
| Accounts receivable  | (507,707 )                              | (265,399 )                              |
| Inventories  | 14,229                                  | (304,268 )                              |
| Prepaid expenses and other current assets                                | 64,291                                  | (191,001 )                              |
| Accounts payable – trade   | 14,973                                  | 388,279                                 |
| Accounts payable – related parties                                       | 159,604                                 | (307,024 )                              |
| Accrued expenses and other current liabilities                           | 98,098                                  | 252                                     |
| Net cash used in operating activities                                    | (2,483,166 )                            | (2,810,461 )                            |
| <b>Cash flow from investing activities</b>                               |   |   |
| Cash received in share exchange  | -                                       | 1,220,520                               |
| Acquisition of property and equipment                                    | (100,171 )                              | (85,928 )                               |
| Employee advances  | (51,429 )                               | -                                       |
| Expenses paid in conjunction with share exchange                         | -                                       | (150,000 )                              |
| Website development costs  | -                                       | (129,999 )                              |
| Net cash (used in) provided by investing activities                      | (151,600 )                              | 854,593                                 |
| <b>Cash flows from financing activities</b>                              |   |   |
| Proceeds from notes payable  | 500,000                                 | 515,000                                 |
| Proceeds from sale of common stock                                       | -                                       | 50,196                                  |
| Proceeds from option/warrant exercises                                   | -                                       | 23,915                                  |
| Proceeds from issuance of convertible notes                              | 150,000                                 | 1,200,000                               |
| Proceeds from issuance of convertible preferred stock, net               | 3,205,168                               | -                                       |
| Advances from former director  | 521,000                                 | 25,000                                  |
| Repayment of advances from former director                               | (535,000 )                              | (25,000 )                               |
| Net cash provided by financing activities                                | 3,841,168                               | 1,789,111                               |
| Net increase (decrease) in cash  | 1,206,402                               | (166,757 )                              |
| Cash - beginning of year   | 191,181                                 | 357,938                                 |
| Cash - end of year   | \$ 1,397,583                            | \$ 191,181                              |
| Cash paid for:   |   |   |

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|  |              |               |
|--|--------------|---------------|
| Interest   | \$ 8,065     | \$ 1,680      |
| Taxes  | \$ -         | \$ -          |
| Non-cash investing and financing activities:                       |              |               |
| Liabilities assumed in share exchange:                             |              |               |
| Accounts payable   | -            | \$ (147,276 ) |
| Accrued expenses   | -            | (168,531 )    |
| Net assets   | -            | \$ (315,807 ) |
| Conversion of convertible notes to common stock                    | \$ 550,000   | \$ 575,000    |
| Warrants issued in financing transaction                           | -            | \$ 210,024    |
| Share exchange expenses included in accounts payable               | -            | \$ 110,656    |
| Deemed dividends – convertible preferred stock                     | \$ 1,666,967 | -             |
| Deferred debt discount – convertible notes                         | \$ 660,932   | -             |
| Deferred debt discount – notes payable                             | \$ 304,037   | -             |
| Accrued costs of convertible preferred stock                       | \$ 174,788   | -             |
| Exchange of accrued expenses for series B preferred stock          | \$ 86,758    | -             |
| Accrued dividends  | \$ 33,992    | -             |
| Exchange of convertible notes payable for series B preferred stock | \$ 15,000    | -             |
| Conversion of series A preferred stock to common stock             | \$ 108       | -             |

The accompanying notes are an integral part of these consolidated financial statements.

Healthwarehouse.com, Inc. and Subsidiaries  
Consolidated Statements of Stockholders' (Deficiency) Equity  
For the Years Ended December 31, 2010 and 2009

|   | Convertible<br>Series A Preferred<br>Shares | Convertible<br>Series B Preferred<br>Stock | Convertible<br>Series B Preferred<br>Shares | Common<br>Stock | Common<br>Shares | Stock | Additional<br>Paid-In<br>Capital | Accumulated<br>Deficit<br>(Deficiency) | Total<br>Stockholders'<br>Equity<br>(Deficiency) |
|---|---|--|---|-----------------|------------------|-------|----------------------------------|--|--|
| Balances,<br>January 1, 2009                                    | -   | -  | -   | -               | 7,743,821        | 7,744 | \$974,588                        | \$(677,958 )                           | \$304,374  |
| Common Stock<br>issued in<br>Private<br>Placement               |   |  |   |                 | 15,906           | 16    | 50,180                           |  | 50,196   |
| Effects<br>of reverse<br>capitalization<br>on May 14,<br>2009   | 155,557                                     | 156  |   |                 | 1,652,808        | 1,653 | 902,904                          |  | 904,713  |
| Costs<br>associated with<br>reverse<br>recapitalization         |   |  |   |                 |                  |       | (260,656 )                       |  | (260,656 )                                       |
| Exercise of<br>Stock Options<br>and Warrants,<br>net            |   |  |   |                 | 65,342           | 65    | 23,849                           |  | 23,914   |
| Conversion of<br>Preferred Stock                                | (48,056 )                                   | (48 )                                      |   |                 | 24,028           | 24    | 24                               |  | -  |
| Conversion of<br>convertible<br>Debentures into<br>common stock |   |  |   |                 | 379,862          | 380   | 574,620                          |  | 575,000  |
| Debt Discount -<br>convertible<br>notes                         |   |  |   |                 |                  |       | 45,453                           |  | 45,453   |
| Debt Discount –<br>Note Payable                                 |   |  |   |                 |                  |       | 164,571                          |  | 164,571  |

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|   |           |       |         |       |            |          |             |               |             |
|---|-----------|-------|---------|-------|------------|----------|-------------|---------------|-------------|
| Non-cash stock-based compensation                             |           |       |         |       |            | 260,318  |             | 260,318       |             |
| Net Loss  |           |       |         |       |            |          | (2,439,502) | (2,439,502)   |             |
| Balances, December 31, 2009                                   | 107,501   | 108   | -       | -     | 9,881,767  | 9,882    | 2,735,851   | (3,117,460)   | (371,619)   |
| Conversion of Series A Preferred stock to common stock        | (107,501) | (108) |         |       | 53,752     | 54       | 54          |               | -           |
| Issuance of Series B Preferred stock, net of costs            |           |       | 365,265 | 365   |            |          | 3,131,775   |               | 3,132,140   |
| Conversion of Convertible Debt into common stock              |           |       |         |       | 343,415    | 343      | 549,657     |               | 550,000     |
| Debt Discount – convertible notes                             |           |       |         |       |            |          | 304,037     |               | 304,037     |
| Debt Discount - note payable                                  |           |       |         |       |            |          | 660,930     |               | 660,930     |
| Stock-based compensation                                      |           |       |         |       |            |          | 490,765     |               | 490,765     |
| Contractual dividends on Series B Convertible Preferred Stock |           |       |         |       |            |          |             | (33,992)      | (33,992)    |
| Deemed dividends on Series B Convertible Preferred Stock      |           |       |         |       |            |          | 1,666,967   | (1,666,967)   | -           |
| Net Loss  |           |       |         |       |            |          | (3,691,674) | (3,691,674)   |             |
|   | -         | -     | 365,265 | \$365 | 10,278,934 | \$10,279 | \$9,540,036 | \$(8,510,093) | \$1,040,587 |



Balances,  
December 31,  
2010

The accompanying notes are an integral part of these consolidated financial statements.

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## HEALTHWAREHOUSE.COM, INC. AND SUBSIDIARIES

### Notes to Consolidated Financial Statements

#### 1. Organization, Basis of Presentation and Reverse Recapitalization

On May 14, 2009, Hwareh.com, Inc. completed a share exchange transaction with Clacendix, Inc. (“Clacendix”), pursuant to the terms of a Securities Exchange Agreement, dated as of May 14, 2009. Under the Securities Exchange Agreement, Clacendix acquired all the outstanding capital stock of Hwareh.com, Inc. As a result of the exchange, the former stockholders of Hwareh.com, Inc. owned 7,759,729 shares or approximately 82.4% of the outstanding shares of common stock of Clacendix. Each share of Hwareh.com was exchanged for 7.05 new shares. This transaction was accounted for as a reverse recapitalization, whereby Hwareh.com, Inc. is deemed to be the accounting acquirer for accounting purposes. Following the closing of the share exchange transaction with Hwareh.com, Clacendix succeeded to the business of Hwareh.com as its sole line of business. Effective August 5, 2009, Clacendix changed its corporate name to HealthWarehouse.com, Inc. The financial statements set forth in this report for all periods prior to the reverse re-capitalization are the historical financial statements of Healthwarehouse.com Inc. and subsidiaries (the “Company”), and have been retroactively restated to give effect to the share exchange transaction.

Prior to the share exchange, Clacendix’s predecessor company was formed as a New Jersey corporation in 1982 as MicroFrame, Inc. In March 1999 MicroFrame, Inc. was reincorporated in the State of Delaware and in the process changed its name to ION Networks, Inc. In December 2007, ION sold substantially all of its operating assets to Cryptek, Inc., a Delaware corporation. Pursuant to the Cryptek sale, ION changed its name to Clacendix, Inc. Following the date of the Cryptek sale and until the closing of the Company’s share exchange transaction with Hwareh.com, Inc. (“Old HW”), Clacendix existed as a shell company with no operations that was seeking a target company with which to merge or to complete a business combination.

On May 5, 2010, the Company announced that its Board of Directors had approved a 1-for-20 reverse split of its common stock, pursuant to previously obtained stockholder authorization. This reverse stock split became effective, on July 16, 2010, which reduced the number of authorized shares of common stock from 750 million to 50 million.

All share amounts included in the consolidated financial statements and notes thereto have been retroactively adjusted for the reverse stock split. Impacted amounts include shares of common stock authorized and outstanding, common share issuances, shares of common stock underlying stock options and warrants, convertible notes, convertible preferred stock, common shares reserved and loss per share.

The Company is a U.S. licensed virtual retail pharmacy (“VRP”) and healthcare e-commerce company that sells brand name and generic prescription drugs as well as over-the-counter (“OTC”) medical products. The Company’s objective is to be viewed by individual healthcare product consumers as a low-cost, reliable and hassle-free provider of prescription drugs and OTC medical products.

The Company is presently licensed as a mail-order pharmacy for sales to 50 states and the District of Columbia.

#### 2. Management’s Liquidity Plans

Since inception, the Company has financed its operations primarily through product sales to customers and debt and equity financing agreements. As of December 31, 2010, the Company had \$1,397,583 in cash and working capital of \$1,058,984 which represents increases of \$1,206,402 and \$1,318,254, respectively. During the year ended December 31, 2010, the Company generated revenue of \$5,691,765 and a net loss of \$3,691,674. For the year ended December 31, 2010, cash flows included net cash used in operating activities of \$2,483,166, net cash used in investing activities of \$151,600 and net cash provided by financing activities of \$3,841,168.

During November and December 2010, the Company received net cash proceeds of approximately \$3,200,000 for the sale of 365,365 shares of Series B Preferred Stock and restructured \$1,000,000 in short term debt to long term (see Note 5). Management believes that the Company has taken certain steps to improve its operations and cash flows, including the re-launch of its corporate website, improved inventory management and an increase in the number of suppliers. Considering the new financial resources, current operating projections and additional potential funding sources the Company believes that it should be able to secure sufficient financial resources through the next fiscal year.

Management believes that if the Company needs to raise additional capital in order to meet operations and execute its business plan, it will be successful. However, there is no assurance that additional financing will be available when needed or that management will be able to obtain financing on terms acceptable to the Company and whether the Company will become profitable and generate positive operating cash flow. If the Company is unable to raise sufficient additional funds, it will have to develop and implement a plan to extend payables and reduce overhead until sufficient additional capital is raised to support further operations. There can be no assurance that such a plan will be successful. The consolidated financial statements do not include any adjustments that might result from the outcome of this uncertainty.

### 3. Summary of Significant Accounting Policies

#### Principles of Consolidation

The consolidated financial statements include the accounts of HealthWarehouse.com, Inc., Hwareh.com, Inc., ION Holding NV, and ION Belgium NV, its wholly-owned subsidiaries. All material inter-company balances and transactions have been eliminated in consolidation.

#### Use of Estimates

The preparation of consolidated financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates. The Company's significant estimates include the allowance for doubtful accounts, depreciation, stock-based compensation, evaluation of warrants, debt discount and deferred tax assets, including a valuation allowance.

#### Reclassifications

Certain accounts in the prior period consolidated financial statements have been reclassified for comparison purposes to conform to the presentation of the current period financial statements. These reclassifications had no effect on the previously reported net loss.

#### Cash

The Company considers all highly liquid investments with an original maturity of three months or less when purchased to be cash equivalents. As of December 31, 2010 and 2009, the Company does not have any cash equivalents.

#### Allowance for Doubtful Accounts Receivable

Accounts receivable are shown net of an allowance for doubtful accounts of \$120,000 and \$0 as of December 31, 2010 and 2009, respectively. The Company's management has established an allowance for doubtful accounts sufficient to cover probable and reasonably estimable losses. The nature of the business is that the majority of the payments are made before the product is sent. If the financial conditions of customers were to materially deteriorate or the nature of the business were to change from prepayment to post payment an increase in the allowance amount could be required. The allowance for doubtful accounts considers a number of factors, including collection experience, current economic trends, estimates of forecasted write-offs, aging of the accounts receivable, and other factors.

#### Inventories

Inventory consists primarily of finished goods. The inventories were stated at the lower of cost (using the first-in, first-out method) or market. No reserves for slow moving and obsolete inventories are provided based on historical experience and current product demand. If the Company's estimate of future demand is not correct or if its customers place significant order cancellations, an inventory reserve could result from the Company's estimate.

### Property and Equipment

Property and equipment are stated at cost. Depreciation is calculated using the straight-line method over the estimated useful lives of the assets. Expenditures for maintenance and repairs, which do not extend the economic useful life of the related assets, are charged to operations as incurred. Gains or losses on disposal of property and equipment are reflected in the statements of operations in the period of disposal.

### Impairment of Long-Lived Assets

The Company reviews for the impairment of long-lived assets whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. An impairment loss would be recognized when estimated future cash flows expected to result from the use of the asset and its eventual disposition are less than its carrying amount. The Company has not identified any such impairment losses.

### Website Development Costs

The Company capitalized \$0 and \$129,999 of website development costs during the years ended December 31, 2010 and 2009, respectively. During the years ended December 31, 2010 and 2009, the Company recorded amortization expense of \$100,200 and \$39,275, relating to these projects, respectively. The Company is amortizing the website development costs on a three year straight-line basis.

### Shipping and Handling Costs

Shipping and handling costs incurred are recognized in selling, general and administrative expenses. Such amounts aggregated \$346,631 and \$280,728 for years ended December 31, 2010 and 2009 respectively.

### Fair Value of Financial Instruments

The carrying value of items included in working capital approximates fair value because of the relatively short maturity of these instruments. The convertible debt approximates fair value because the terms are substantially similar to comparable debt in the marketplace

Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. These fair value measurements apply to all financial instruments that are measured and reported on a fair value basis. Fair value measurements did not have a material impact on the fair value measurements of the Company's investments.

Based on the observability of the inputs used in the valuation techniques, financial instruments are categorized according to the fair value hierarchy, which ranks the quality and reliability of the information used to determine fair values. Financial assets and liabilities carried at fair value are classified and disclosed in one of the following three categories:

Level 1 - Observable inputs such as quoted prices in active markets. At December 31, 2010 and 2009, the Company did not hold any Level 1 investments.

Level 2 - Inputs, other than the quoted prices in active markets, that are observable either directly or indirectly. At December 31, 2010 and 2009, the Company did not hold any level 2 investments.

Level 3 - Unobservable inputs in which there is little or no market data, which require the reporting entity to develop its own assumptions. At December 31, 2010 and 2009, the Company did not hold any Level 3 investments.

In certain cases, the inputs used to measure fair value may fall into different levels of the fair value hierarchy. In such cases, the assignment of an asset or liability within the fair value hierarchy is based on the lowest level of input that is significant to the fair value measurement. The Company's assessment of the significance of a particular input to the fair value measurement in its entirety requires judgment, and considers factors specific to the asset or liability.

### Convertible Debentures

The Company records, as a discount to convertible notes, the intrinsic value of such conversion options based upon the differences between the fair value of the underlying common stock at the commitment date of the note transaction and the effective conversion price embedded in the note. Debt discounts under these arrangements are amortized to interest expense over the term of the related debt to their earliest date of redemption.

### Income Taxes

The Company recognizes deferred income tax assets and liabilities for future tax consequences resulting from differences between the book and tax bases of existing assets and liabilities. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. The effect on deferred tax assets and liabilities of a change in tax rates is recognized in the results of operations in the period that includes the enactment date. A valuation allowance is provided for that portion of deferred income tax assets which may not be realized.

The Company recognizes tax liabilities when, despite the Company's belief that its tax return positions are supportable, the Company believes that certain positions may not be fully sustained upon review by tax authorities. Benefits from tax positions are measured at the largest amount of benefit that is greater than 50 percent likely of being realized upon settlement. The current portion of tax liabilities is included in other current liabilities and the noncurrent portion of tax liabilities is included in other long-term liabilities in the consolidated balance sheet. To the extent that the final tax outcome of these matters is different than the amounts recorded, such differences impact income tax expense in the period in which such determination is made.

### Revenue Recognition

Revenues for the sales of products are recognized when persuasive evidence of an arrangement exists, delivery has occurred, the fee is fixed and determinable and collectability is reasonably assured.

### Advertising

The Company expenses all advertising costs as incurred. Advertising expense for the years ended December 31, 2010 and 2009 was \$450,687 and \$586,354, respectively.

### Sales Taxes

The Company accounts for sales taxes imposed on its goods and services on a net basis in the statement of operations.

### Net Loss Per Share of Common Stock

Basic net loss per share is computed by dividing net loss attributable to common stockholders by the weighted average number of common shares outstanding during the period. Diluted net loss per share reflects the potential dilution that could occur if securities or other instruments to issue common stock were exercised or converted into common stock. Potentially dilutive securities of 5,884,652 at December 31, 2010 are excluded from the computation of diluted net loss per share as their inclusion would be anti-dilutive. These potentially dilutive securities consist of stock options to purchase up to 1,996,300 shares of common stock, warrants to purchase up to 1,915,340 shares of common stock, convertible promissory notes convertible into 146,687 shares of common stock and convertible preferred stock convertible into 1,826,325 shares of common stock. Potentially dilutive securities of 2,293,451 at December 31, 2009 are excluded from the computation of diluted net loss per share as their inclusion would be anti-dilutive. These



potentially dilutive securities consist of stock options to purchase up to 1,514,300 shares of common stock, warrants to purchase up to 312,500 shares of common stock, convertible promissory notes convertible into 412,900 shares of common stock and convertible preferred stock convertible into 53,751 shares of common stock.

## Stock-Based Compensation

Stock-based compensation expense for all stock-based payment awards is based on the estimated grant-date fair value. The Company recognizes these compensation costs over the requisite service period of the award, which is generally the option vesting term. Option valuation models require the input of highly subjective assumptions including the expected life of the option. Because the Company's employee stock options have characteristics significantly different from those of traded options, and because changes in the subjective input assumptions can materially affect the fair value estimate, in management's opinion, the existing models do not necessarily provide a reliable single measure of the fair value of its employee stock options. The fair value of stock-based payment awards was estimated using the Black-Scholes option pricing model using a volatility figure derived from an index of comparable entities. Management will review this assumption as the Company's trading history becomes a better indicator of value. The Company accounts for the expected life of options in accordance with the "simplified" method which enables the use of the simplified method for "plain vanilla" share options as defined in SAB No. 107.

Stock-based compensation for the years ended December 31, 2010 and 2009 was recorded in the consolidated statements of operations in selling general and administrative line item and totaled \$490,765 and \$260,318, respectively.

The fair value of stock-based payment awards was estimated using the Black-Scholes pricing model with the following assumptions and weighted average fair values ranges as follows:

|   | For the Year Ended<br>December 31, 2010 | For the Year Ended<br>December 31, 2009 |
|---|---|---|
| Risk-free interest rate                 | 2.39% to 2.71%                          | 1.09% to 2.65%                          |
| Dividend yield                          | N/A                                     | N/A                                     |
| Expected volatility                     | 57.6%-58.7%                             | 57.6%                                   |
| Expected life in years                  | 6.00                                    | 2.5 to 6.00                             |
| Expected forfeiture rate (through term) | 0%                                      | 0%                                      |

## 4. Property and Equipment

Property and equipment consist of the following:

|   | December 31, |            | Estimated   |
|---|--------------|------------|-------------|
|   | 2010         | 2009       | Useful Life |
| Computer software                               | \$ 191,665   | \$ 128,198 | 5 years     |
| Equipment                                       | 182,637      | 158,508    | 15 years    |
| Office furniture and equipment                  | 20,085       | 10,093     | 7 years     |
| Computer hardware                               | 27,746       | 25,163     | 5 years     |
| Leasehold improvements                          | 87,914       | 87,914     | (a)         |
| Total   | 510,047      | 409,876    |             |
| Less: accumulated depreciation and amortization | (189,719 )   | (91,083 )  |             |
| Property and equipment, net                     | \$ 320,328   | \$ 318,793 |             |

(a) Lesser of useful life or initial term of lease

Depreciation and amortization expense for the years ended December 31, 2010 and 2009 was \$98,636 and \$93,000, respectively.

## 5. Convertible Instruments

### a. Convertible Debt

In contemplation of and contingent to closing the share exchange transaction, in the quarter ended June 30, 2009, Hwareh.com, Inc. received the proceeds of convertible promissory notes aggregating \$1,200,000 (“Convertible Debentures”). The notes have a maturity date of two years from the date of issuance and bear interest at 3.25% per annum, payable quarterly in arrears and in full upon conversion. The notes are convertible into 792,762 shares of the Company’s common stock at an effective conversion price of \$1.5137 per share. The notes are convertible at any time at the option of the holder. The Company can also cause the conversion of the notes at its option at any time before maturity and after the shares of the Company’s common stock that are issuable upon conversion of the notes have been registered for resale pursuant to an effective registration statement. The notes have customary anti-dilution provisions in connection with any split, subdivision or combination of the Company’s common stock. Payment of principal, if not converted, and interest under the notes has been guaranteed by the Company’s President and Chief Executive Officer and a 10% or greater stockholder. (See Note 10.) The debt discount applicable to the notes from the issuance of warrants along with the notes was \$45,453 (see below). As of December 31, 2010, \$1,000,000 of the Hwareh.com convertible promissory notes had been converted. The Company has accrued approximately \$22,000 of interest and is in technical default; however the default is not triggered unless notice is given by one of the convertible debenture holders. The Company would have fifteen days to cure the default. Subsequent to December 31, 2010, all of the Convertible Debentures have been converted into common stock. See note 10.

In connection with the issuance of the Hwareh.com convertible promissory notes, Hwareh.com, Inc. also issued warrants to purchase common stock for up to 403,410 shares of the Company’s common stock (warrants expiring on May 31, 2009, June 30, 2009 and December 31, 2009 to purchase up to a maximum of 46,390, 178,510 and 178,510 shares, respectively, of the Company’s common stock at an exercise price of \$0.021556, \$1.120392 and \$1.120392 per share, respectively). Of these warrants, warrants to purchase 46,392 shares of the Company’s common stock were exercised on May 31, 2009, warrants to purchase up to 178,510 shares of the Company’s common stock expired on June 30, 2009 and warrants to purchase up to 178,510 shares of the Company’s common stock expired on December 31, 2009 without being exercised. The warrants had customary anti-dilution provisions in connection with any split, subdivision or combination of the Company’s common stock. The fair value of the warrants was estimated at \$45,453 using the Black-Scholes option pricing model and recorded as a debt discount. During the years ended December 31, 2010 and 2009, the Company recognized \$21,079 and \$14,716 in amortization of the deferred debt discount, respectively.

The convertible promissory notes and warrants have registration rights with respect to the shares of the Company’s common stock that are issuable upon conversion or exercise of the notes or warrants, respectively. The Company was obligated to file an initial registration statement providing for the resale of the shares of the Company’s common stock underlying the convertible promissory notes and warrants by August 12, 2009, and to use its best efforts to have the registration statement declared effective as soon as practicable thereafter. Since the Company did not file on or before August 12, 2009, it must pay liquidated damages of \$12,000 in the aggregate, an amount equal to 1% of the aggregate investment amount; such amount has been recorded in the accompanying consolidated financial statements, however, the Company continues to discuss with the holders to have them waive these penalties.

During the year ended December 31, 2010, the Company sold four convertible debentures for \$25,000 each and one convertible debenture for \$50,000 for an aggregate amount of \$150,000. Each convertible debenture carries a term of two years, bears a 10% per annum interest rate payable annually. Each of the four \$25,000 convertible debentures are

convertible into 12,500 shares of the Company's common stock. The \$50,000 convertible debenture is convertible into 25,000 shares of the Company's common stock. The Lender has customary "piggy-back" registration rights with respect to the common stock issued or issuable upon the exercise of the convertible debenture. See note 7.

The following table summarizes the remaining debt principal payment obligations by year for the long-term debt:

|       |             |
|-------|-------------|
| 2011  | \$225,000   |
| 2012  | 1,000,000   |
| Total | \$1,225,000 |

#### b. Convertible Preferred Stock

On November 8, 2010, the Company entered into a Securities Purchase Agreement (the “Purchase Agreement”) with investors (the “Investors”) and sold certain securities to the Investors (the “2010 Private Placement”). Under the terms of the Purchase Agreement, the Company sold a total of 365,265 newly authorized shares of \$0.001 par value Series B preferred stock (the “Series B Preferred Stock”) to the Investors at \$9.45 per share, for an aggregate price of approximately \$3,450,000. Each share of the Series B Preferred Stock may be converted at any time, in whole or in part, into five shares of the Company’s Common Stock, as adjusted. The Company also entered into a separate Loan and Security Agreement dated November 8, 2010 with two of the Investors (the “2010 Loan Agreement”). Under the terms of the 2010 Loan Agreement and the Purchase Agreement, the Company exchanged \$1,015,000 of short-term debt (Note 6) with these investors for convertible promissory notes in the aggregate principal amount of \$1,000,000 (the “Convertible Notes”). The Convertible Notes bear interest at the rate of 7% per annum compounded annually (effective interest rate of 47% per annum). The principal amount and all accrued interest on the Convertible Notes are payable on December 31, 2012, or earlier on an event of default or a sale or liquidation of the Company. The principal amount and accrued interest on the Convertible Notes may be converted at any time into shares of Series B Preferred Stock at a conversion price of \$9.45 per share, as adjusted. Under the terms of the Purchase Agreement, the Company also issued warrants to the Investors, prorata to their investment amounts, to purchase an aggregate of 1,271,590 shares of the Company’s Common Stock at an exercise price of \$3.00 per share (the “Warrants”). Each Warrant may be exercised in whole or in part and from time to time for a term of five years from its grant date. The aggregate deferred debt discount related to the Convertible Notes was estimated at \$660,932 using the Black Scholes model. The debt discount amortization associated with the Convertible Notes was \$60,578 in the year ended December 31, 2010. The Company recorded a deemed dividend of \$1,666,967 in the year ended December 31, 2010 for the issued portion of the Series B convertible preferred stock not attributable to the Convertible Notes. The Company incurred transaction costs to advisors in the amount of approximately \$320,000 and received net proceeds of approximately \$3,200,000 (gross proceeds of approximately \$3,450,000).

#### 6. Short Term Debt

On December 15, 2009, the Company entered into a Loan and Security Agreement (the “Loan Agreement”) with HWH Lending LLC, a Delaware limited liability company (the “Lender”). Under the terms of the Loan Agreement, the Company borrowed \$515,000 from the Lender on December 15, 2009 (the “First Loan”). The Company had the right to borrow an additional \$500,000 from the Lender upon the Company’s request, after the end of the first calendar month in which the Company realized positive cash flow (the “Second Loan”, and together with the First Loan, the “Loans”). In addition, the Lender had the right to require the Company to accept the Second Loan upon notice, after the end of the first month in which the Company realized positive cash flow. The Lender’s right and obligation to make the Second Loan terminated on the later of 12 months after the date of the First Loan, or 12 months after the Company first realized positive cash flow. The proceeds of the Loans were used by the Company for working capital purposes. The Loans were evidenced by promissory notes (the “Notes”), and will bear interest at the rate of 12% per annum, payable at maturity. The Loans were collateralized by substantially all of the Company’s assets. The maturity date of each Loan is one year from the date of the Loan. The Loans may be prepaid in whole or in part at any time by us without penalty, upon 15 days notice.



In consideration of the First Loan, the Company granted the Lender a warrant to purchase 312,500 shares of the Company's common stock at a purchase price of \$1.60 per share. On May 3, 2010, the Company received the proceeds from the Second Loan, and granted the Lender an additional warrant to purchase 312,500 shares of common stock at a purchase price of \$1.60 per share. Each warrant may be exercised in whole or in part and from time to time for a term of five years from its grant date. The Lender has customary "piggy-back" registration rights with respect to the common stock issued or issuable upon the exercise of the warrants (the "Warrant Shares"). In addition, the Lender has demand registration rights with respect to the Warrant Shares, so that upon written request of the Lender, the Company will be obligated to prepare and file with the U.S. Securities and Exchange Commission a registration statement sufficient to permit the resale of the Warrant Shares. The Lenders' registration rights terminate on the date on which all of the Warrant Shares may be sold under Rule 144 of the Securities Act of 1933 without any limitations. The warrants contain customary anti-dilution and purchase price adjustment provisions. The warrants are transferable in whole or in part, so long as the transfers comply with applicable securities laws. The relative fair value of the warrants was estimated at \$304,037 using the Black Scholes method.

As discussed in Note 5, as part of the November 8, 2010 financing transaction, the balance of loans aggregating \$1,015,000 and accrued interest of approximately \$87,000 were satisfied. The remaining debt discount at the time of repayment and after issuance of the convertible notes on November 8, 2010 (see note 5) was recorded to interest expense in the year ended 2010 for \$172,589. The total debt discount amortized on these Loans during the year ended December 31, 2010 and 2009 was \$461,750 and \$6,858, respectively.

## 7. Stockholders' Equity (Deficiency)

### Common Stock

From January 1, 2009 to May 13, 2009, Hwareh.com, Inc. sold 15,906 shares of common stock in a private placement and received proceeds of \$50,196.

On May 31, 2009, the holder of a warrant exercised that warrant, for cash proceeds of \$1,000, and received 46,392 shares of the Company's common stock.

On June 10, 2009, a former director and holder of a warrant exercised that warrant for cash proceeds of \$6,250, and received 6,250 shares of the Company's common stock. In a separate transaction on the same day, the same person exercised stock options to purchase 4,475 shares of common stock for cash proceeds of \$7,806.

On August 31, 2009, the Company received cash proceeds of \$5,000 from the exercise of warrants to purchase 5,000 shares of the Company's common stock.

On September 16, 2009, a former director exercised stock options to purchase 3,225 shares of common stock for cash proceeds of \$3,858.

In November 2009, the Company issued 198,180 common shares per conversion of a convertible note to Rock Castle Holdings, LLC, 45,551 common shares per conversion of a convertible note to a former director, and an additional 132,132 common shares per conversion of a convertible notes to various other note holders, aggregating \$575,000.

During the year ended December 31, 2010, convertible debentures in the aggregate amount of \$550,000 were converted into approximately 343,000 shares of common stock.

### Preferred Stock

The Company has designated 200,000 of the 1,000,000 authorized shares of preferred stock as convertible Series A Preferred Stock (“Series A Preferred Stock”). The Series A Preferred Stock is non-voting, has a liquidation preference equal to its purchase price, and does not pay dividends. The holders can call the conversion of the Series A Preferred Stock at any time.

On December 16, 2009, the Company issued 24,028 shares of common stock to a shareholder trust per conversion of 48,056 shares of Series A Preferred Stock.

On October 29, 2010, all 107,501 Series A Preferred Stock shares outstanding were converted into 53,752 shares of the Company’s common stock.



The Company has designated 625,000 of the 1,000,000 authorized shares of preferred stock as Series B Convertible Preferred Stock (“Series B Preferred Stock”). The Series B Preferred Stock is non-voting, has a liquidation preference equal to its purchase price, and receives preferred dividends equal to 7% of all outstanding shares in either cash or payment-in-kind (“pik”). As of December 31, 2010, the Company has recorded accrued dividends of \$33,992 related to the Series B Preferred Stock. As of December 31, 2010, there were 365,265 shares of Series B Preferred Stock outstanding, which are convertible into 1,826,325 shares of common stock. The holders can call the conversion of the convertible Series B Preferred Stock at any time.

#### Incentive Compensation/Stock Option Plans

On May 15, 2009, the Company adopted its 2009 Incentive Compensation Plan (the “2009 Plan”). The total number of shares of common stock that may be subject to the granting of awards under the 2009 Plan is 2,700,000, plus 181,425 shares that remained available to be issued on May 15, 2009 and were assumed as part of the share exchange from Clacendix’ previously existing stock option plans. The 2009 Plan imposes individual limitations on the amount of certain awards. Under these limitations, during any fiscal year of the Company, the number of options, stock appreciation rights, shares of restricted stock, shares of deferred stock, performance shares and other stock based-awards granted to any one participant under the 2009 Plan may not exceed 250,000 shares, subject to adjustment in certain circumstances. The maximum amount that may be paid out as performance units in any 12-month performance period is an aggregate value of \$2,000,000, and the maximum amount that may be paid out as performance units in any performance period greater than 12 months is an aggregate value of \$4,000,000. The maximum term of each option or stock appreciation right, the times at which each option or stock appreciation right will be exercisable, and provisions requiring forfeiture of unexercised options or stock appreciation rights at or following termination of employment generally are fixed by the board of directors or committee of the Company’s board of directors designated to administer the 2009 Plan (the “committee”), except that no option or stock appreciation right may have a term exceeding ten years. The exercise price per share subject to an option and the grant price of a stock appreciation rights are determined by the committee, but in the case of an incentive stock option (ISO) must not be less than the fair market value of a share of common stock on the date of grant.

On May 15, 2009, the Company granted to one board member and one executive officer options to purchase an aggregate of 421,800 shares of common stock with an exercise price of \$0.80 per share for a total value of approximately \$158,000 under a previously approved option plan. One-half of these stock options vested on the grant date and have a five year term. The remainder of the stock options granted vest over a three year period and have a term of ten years.

On May 20, 2009, the Company granted to one board member, employees and consultants options to purchase an aggregate of 812,500 shares of common stock with an exercise price of \$2.00 per share for a total value of approximately \$936,000 under a previously approved option plan. The options vest over a three year period and have a term of ten years.

On May 20, 2009, the Company granted an executive officer options to purchase an aggregate of 250,000 shares of common stock with an exercise price of \$2.20 for a total value of \$237,000 under a previously approved option plan. The options vest over a three year period and have a term of five years.

On November 11, 2009, the Company granted one board member, one executive officer and one employee options to purchase an aggregate of 255,000 shares of common stock with an exercise price of \$2.50 for a total value of \$316,000 under a previously approved option plan. The options vest over a three year period and have a term of ten years.

On February 10, 2010, the Company granted to employees and consultants, options to purchase an aggregate of 82,500 shares of common stock with an exercise price of \$2.80 per share for a total fair value of \$127,853 under a previously approved option plan. The options vest over a three year period and have a term of ten years.

On April 6, 2010, the Company granted to a consultant for services, options to purchase an aggregate of 15,000 shares of common stock with an exercise price of \$2.50 per share for a total fair value of \$20,923 under a previously approved option plan. The options vest over a three year period and have a term of ten years.

On April 22, 2010, the Company granted to a consultant for services, options to purchase 12,500 shares of common stock with an exercise price of \$2.40 per share for a total fair value of \$16,680 under a previously approved option plan. The options vest over a three year period and have a term of ten years.

On May 3, 2010, the Company granted to employees and consultants options to purchase an aggregate of 122,500 shares of common stock with an exercise price of \$3.60 per share for a total fair value of \$244,578 under a previously approved option plan. The options vest over a three year period and have a term of ten years.

On October 14, 2010, the Company granted to employees options to purchase an aggregate of 122,000 shares of common stock with an exercise price of \$2.75 per share for a total fair value of \$180,096 under a previously approved option plan. The options vest over a three year period and have a term of ten years.

On October 14, 2010, the Company granted an employee options to purchase an aggregate of 250,000 shares of common stock with an exercise price of \$3.03 per share for a total fair value of \$353,069 under a previously approved option plan. The options vest over a three year period and have a term of five years.

On December 8, 2010, the Company granted a director options to purchase an aggregate of 30,000 shares of common stock with an exercise price of \$3.75 per share for a total fair value of \$55,773 under a previously approved option plan. The options vest over a three year period and have a term of ten years.

As of December 31, 2010, stock compensation of approximately \$1,500,000 remains unamortized and is being amortized on a straight-line basis over three years from the date of grant.

Details of the options outstanding under all plans are as follows:

|  | Shares     | Weighted<br>Average<br>Exercise<br>Price (\$) | Weighted-<br>Average<br>Remaining<br>Contractual<br>Term | Aggregate<br>Intrinsic<br>Value |
|--|------------|---|--|---------------------------------|
| Options outstanding at January 1, 2009   | -          | -   | -  | -                               |
| Assumed in exchange                      | 34,475     | \$ 2.80                                       | -  | -                               |
| Granted                                  | 1,739,300  | \$ 1.80                                       | -  | -                               |
| Expired                                  | -          | -   | -  | -                               |
| Canceled                                 | (251,775 ) | -   | -  | -                               |
| Exercised                                | (7,700 )   | \$ 1.60                                       | -  | -                               |
| Options outstanding at January 1, 2010   | 1,514,300  | 1.80  | 7.48   | \$ 336,000                      |
| Granted                                  | 634,500    | \$ 3.07                                       | -  | -                               |
| Expired                                  | -          | -   | -  | -                               |
| Canceled                                 | (152,500 ) | 2.47  | -  | -                               |
| Exercised                                | -          | -   | -  | -                               |
| Options outstanding at December 31, 2010 | 1,996,300  | 2.14  | 6.92   | \$ 1,383,760                    |
| Options exercisable at December 31, 2010 | 660,531    | \$ 1.48                                       | 6.22   | \$ 836,914                      |

| Range of Exercise | Number<br>Outstanding | Weighted<br>Average<br>Remaining<br>Years of<br>Contractual<br>Life | Weighted<br>Average<br>Exercise<br>Price | Number<br>Exercisable | Weighted<br>Average<br>Exercise<br>Price |
|-------------------|-----------------------|---|--|-----------------------|--|
| \$0.80 – 2.00     | 921,800               | 7.01  | \$ 1.45                                  | 492,214               | \$ 1.19                                  |
| \$2.00 – 3.75     | 1,074,500             | 6.84  | \$ 2.73                                  | 168,317               | \$ 2.35                                  |
| \$0.80 – \$3.75   | 1,996,300             | 6.92  | \$ 2.14                                  | 660,531               | \$ 1.48                                  |

#### Warrants

The Company granted its investment advisor, as part of the compensation related to securing the \$515,000 loan in December 2009 and \$500,000 loan in May 2010, a warrant to purchase 18,750 shares of the Company's common stock at an exercise price of \$1.60 per share for a total fair value of approximately \$25,245. The warrant may be exercised in whole or in part from time to time for a term of five years from its grant date. The chairman of the Company's Audit Committee is a senior managing director of this investment advisory firm.

Details of outstanding warrants are as follows:

|   | Shares     | Weighted<br>Average<br>Exercise Price<br>(\$) | Weighted-<br>Average<br>Remaining<br>Contractual<br>Term | Aggregate<br>Intrinsic<br>Value |
|---|------------|---|--|---------------------------------|
| Warrants outstanding at January 1, 2009   | -          | -   | -  | -                               |
| Assumed in exchange                       | 13,750     | \$ 1.00                                       |  |                                 |
| Granted                                   | 715,910    | 1.20  | -  | -                               |
| Expired                                   | (359,518 ) | 1.20  | -  | -                               |
| Exercised                                 | (57,642 )  | 0.20  | -  | -                               |
| Warrants outstanding at January 1, 2010   | 312,500    | 1.60  | 4.96   | \$ 62,500                       |
| Granted                                   | 1,602,840  | 2.71  | -  | -                               |
| Expired                                   | -          | -   | -  | -                               |
| Exercised                                 | -          | -   | -  | -                               |
| Warrants outstanding at December 31, 2010 | 1,915,340  | 2.53  | 4.62   | \$ 740,313                      |

## 8. Commitments and Contingent Liabilities

### Operating Leases

The Company occupies approximately 16,000 square feet of office and storage space under a month-to-month Commercial Sublease Agreement with Masters Healthcare, LLC (an entity owned by Jason Smith – see Note 10). The sublease has a current monthly rental rate of \$9,417(as amended) with an original term through March 31, 2011. During the years ended December 31, 2010 and 2009, the Company recorded rent expense of \$113,004 and \$93,750, respectively.

### Litigation

On or about January 15, 2010, the Company's former outside counsel, Duval & Stachenfeld LLP(“Duval”), commenced litigation against the Company in federal court in New York, New York asserting that the Company owed Duval \$213,887 in unpaid legal fees. Duval was also seeking to recover interest and its fees in connection with the litigation. On May 25, 2010 the Company and Duval settled all litigation by the payment by the Company to Duval in the amount of \$165,000. The Company, for the period ended December 31, 2009 had previously established a reserve in the amount of \$213,887. Pursuant to the settlement agreement, the Company reflected a benefit equal to \$48,887 during the year ended December 31, 2010. All legal fees related to this action were expensed as incurred.

In the normal course of business the Company may be involved in legal proceedings, claims and assessments arising in the ordinary course of business. Such matters are subject to many uncertainties, and outcomes are not predictable with assurance. Currently, the Company is not involved in any such matters.

## 9. Concentrations

The Company maintains deposits in financial institutions which are insured by the Federal Deposit Insurance Corporation (“FDIC”). At various times, the Company has deposits in this financial institution in excess of the amount insured by the FDIC.

As of December 31, 2010 and 2009, a substantial portion of the Company's accounts receivable related to two and three customers, respectively, which comprised approximately 61.1% and 21.9% of 2010 and 42.7%, 32.2% and 13.1% of 2009 of the total accounts receivable for each period.

## 10. Related Party Transactions

Lalit Dhadphale, the Company's President and Chief Executive Officer, and Cape Bear Partners LLC, the beneficial owner of greater than 10% of the Company's Common Stock, guaranteed Old HW's obligations under certain Old HW convertible promissory notes with an original principal value of approximately \$1,200,000, which notes were assumed by the Company in connection with the Exchange. The guarantees state that Mr. Dhadphale and Cape Bear Partners LLC each guarantee the full payment of principal and interest under the notes. The guarantees terminate with respect to each note upon the earlier of repayment of principal and interest under each note or conversion of the note to equity. In the event of note conversion, the guarantees remain in place with respect to any interest due and unpaid through the date of conversion until that interest has been paid. During the fourth quarter of 2009 and during 2010, the holders of notes in an aggregate principal amount of \$1,000,000 elected to convert their notes. The maximum principal exposure of each of Mr. Dhadphale and Cape Bear Partners LLC pursuant to the guarantees as of December 31, 2010 is \$200,000, plus interest. On January 5, 2011, the remaining Convertible Note balance of \$200,000 was converted into 132,118 shares of common stock plus all accrued interest was paid.

On December 15, 2009, the Company entered into a Loan and Security Agreement (the "Loan Agreement") with HWH Lending LLC, a Delaware limited liability company ("HWH"). Under the terms of the Loan Agreement, the Company borrowed \$515,000 from HWH on December 15, 2009, and borrowed an additional \$500,000 on May 3, 2010 (together, the "Loans"). The proceeds of the Loans were used for working capital purposes. The Loans were evidenced by promissory notes (the "Notes"), and bore interest at the rate of 12% per annum, payable at maturity. The maturity date of each Loan was one year from the date of the Loan. The Loans could be prepaid in whole or in part at any time by us without penalty, upon 15 days notice. Mr. Dhadphale personally guaranteed the Company's payment and other obligations under the Loan Agreement and the Notes. Mr. Dhadphale also entered into a Lock-up Agreement with HWH prohibiting Mr. Dhadphale from selling or transferring 625,000 shares of the Company's common stock until the Loans are repaid in full, subject to certain exceptions, such as gifts. The Company satisfied the Loans in full on November 8, 2010 (see Note 5), and Mr. Dhadphale's personal guaranty and the Lock-Up were terminated.

As of December 31, 2010, Jason Smith is the beneficial owner of greater than 10% of the Company's Common Stock. As the Manager of Rock Castle, Jason Smith has sole voting and dispositive power over the shares owned by Rock Castle Holdings, LLC ("Rock Castle") and, as such, is deemed to beneficially own such shares.

The Company is a party to oral consulting agreements with Jason Smith and Rock Castle under which Jason Smith and affiliates of Rock Castle provide purchasing and advisory services to the Company. Pursuant to these consulting agreements, on May 20, 2009, the Company granted to Jason Smith and Rock Castle, respectively, non-qualified options to purchase 100,000 and 250,000 shares of the Company's common stock, with an aggregate value of \$17,362 all with a ten year term. These options vest in equal annual installments on May 20, 2010, May 20, 2011 and May 20, 2012. The consulting agreements are terminable at will.

Jason Smith is also the son of Dennis Smith, the controlling stockholder of Masters Pharmaceutical, Inc., one of the Company's principal suppliers. The Company purchased from Masters Pharmaceutical, Inc., \$959,847 and \$1,342,997 of supplies, representing approximately 29% and 49% of total purchases during the years ended December 31, 2010 and 2009, respectively. Accounts payable due to Masters Pharmaceutical, Inc. at December 31, 2010 and 2009 was \$215,858 and \$24,969, respectively. At December 31, 2010, accrued interest expense due to Masters Pharmaceutical, Inc. was \$17,000. Wayne A. Corona, formerly the Company's Secretary and a member of the board of directors, is Vice President of Business Development at Masters Pharmaceutical, Inc.

For the years ended December 31, 2010 and 2009, sales to Masters Pharmaceuticals were approximately 8.76% and 4.27%, respectively, of net sales.

On April 29, 2009, as a part of the Old HW private financing completed before the Exchange, the Company issued to Wayne A Corona, formerly the Company's Secretary and a member of the board of directors, \$75,000 in principal amount of convertible promissory notes convertible into 49,551 shares of the Company's Common Stock in consideration of \$75,000 in cash. On the same date, the Company issued to MKW Partners, LLC, of which Mr. Corona is the Manager, \$50,000 in principal amount of convertible promissory notes convertible into 33,032 shares of the Company's Common Stock in consideration of \$50,000 in cash. Mr. Corona and MKW Partners elected to convert these notes in the fourth quarter of 2009, and received an aggregate of 82,583 shares of the Company's Common Stock in exchange.

On April 30, 2009, also as a part of such Old HW private financing, the Company issued to Kip Ferguson, the brother of a former Old HW director, Ron Ferguson, \$25,000 in principal amount of convertible promissory notes convertible into 16,520 shares of the Company's Common Stock in consideration of \$25,000 in cash. Mr. Ferguson elected to convert his note in the fourth quarter of 2009, and received 16,520 shares of the Company's Common Stock in exchange.



On May 8, 2009, also as a part of such Old HW private financing, the Company issued to Rock Castle \$300,000 in principal amount of convertible promissory notes convertible into 198,180 shares of the Company's Common Stock in consideration of \$300,000 in cash. Rock Castle elected to convert its promissory note in the fourth quarter of 2009, and received 198,180 shares of the Company's Common Stock in exchange.

On May 20, 2009, the Company granted Mr. Corona non-qualified options to purchase 250,000 shares of the Company's common stock, all with a five year term. These options would have vested in equal annual installments on May 20, 2010, May 20, 2011 and May 20, 2012. These options terminated on November 9, 2009, the date Mr. Corona resigned from the Company's Board.

Ron Ferguson, a former Old HW director, has guaranteed Old HW's obligations to supplier Prescription Supply Inc. Mr. Ferguson is the spouse of Diane Ferguson, a stockholder of the company. The guarantee, and Mr. Ferguson's maximum exposure under the guarantee, does not have a fixed dollar limit. As of December 31, 2010 and 2009, there was \$0 and \$6,172, respectively, due to Prescription Supply Inc.

During the year ended December 31, 2010, a former director advanced \$521,000 in short term financing to the Company. A payment of \$535,000 was made during the year ended December 31, 2010. During the year ended December 31, 2009, a former director advanced \$25,000 in short term financing to the Company. A payment of \$25,000 was made during the year ended December 31, 2009.

Although the Company has not adopted formal procedures for the review, approval or ratification of transactions with related persons, the Company adheres to a general policy that such transactions should only be entered into if they are on terms that, on the whole, are no more favorable, or no less favorable, than those available from unaffiliated third parties and their approval is in accordance with applicable law. Such transactions require the approval of the Company's board of directors.

## 11. Income Taxes

At December 31, 2010 and 2009 the Company had approximately \$4,200,000 and \$3,000,000, respectively, of federal and state net operating losses that may be available to offset future taxable income. The federal net operating loss carry forwards, if not utilized, will expire from 2029 to 2030.

As of December 31, 2010 and 2009, the Company believes that there are no significant uncertain tax positions requiring recognition in these consolidated financial statements. The Company does not expect any significant changes in the unrecognized tax benefits within the next twelve months.

The Company classifies interest expense and any related penalties related to income tax uncertainties as a component of income tax expense. No interest or penalties have been recognized as of December 31, 2010.

The Company files income tax returns in the U.S. federal jurisdiction and various local jurisdictions and is subject to examination by the various taxing authorities. The Company's federal and local income tax returns for tax years beginning in 2007 remain subject to examination.

As discussed in Note 1, the Company consummated a share exchange transaction with Hwareh.com, Inc on May 14, 2009. The share exchange transaction is being accounted for as a "reverse recapitalization," since the former stockholders of Hwareh.com own a majority of the outstanding shares of the Company's common stock immediately following the transaction, and Hwareh.com is deemed to be the accounting acquirer in the transaction. In accordance with Section 382 of the Internal Revenue code, the usage of the Company's net operating loss carryforward could be limited in the event of a change in ownership. Based upon a study that analyzed the Company's stock ownership

activity from inception to December 31, 2010, a change of ownership was deemed to have occurred in 2009. This change of ownership created an annual limitation on the usage of the Company's losses which are available through 2029.

The effects of the differences that give rise to significant portions of the deferred tax assets and liabilities as of December 31, 2010 and 2009 are as follows:

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|  | 2010        | 2009        |
|--|-------------|-------------|
| Deferred tax assets:                               |             |             |
| Operating loss carryforwards                       | \$1,460,277 | \$1,024,771 |
| Non-qualified stock options                        | —           | 48,280      |
| Allowance for bad debt                             | 40,800      | —           |
| Charitable contribution carryforward               | 2,382       | —           |
| Total deferred tax assets                          | 1,503,459   | 1,073,051   |
| Deferred tax liabilities:                          |             |             |
| Property and Equipment                             | (50,210 )   | (71,222 )   |
| Total deferred tax liabilities                     | (50,210 )   | (71,222 )   |
| Net deferred tax assets before valuation allowance | 1,453,249   | 1,001,829   |
| Less: Valuation Allowance                          | (1,453,249) | (1,001,829) |
| Net deferred tax asset                             | \$—         | \$—         |
| Change in valuation allowance                      | \$451,420   | \$782,171   |

The Company assesses the likelihood that deferred tax assets will be realized. To the extent that realization is not likely, a valuation allowance is established. Based upon the last two years' history of losses, management believes that it is more likely than not that future benefits of deferred tax assets will not be realized.

A reconciliation of income tax (benefit) provision for the years ended December 31, 2010 and 2009, with the amounts computed at the statutory federal rate follows:

|   | December 31, |    |         |    |
|---|--------------|----|---------|----|
|   | 2010         |    | 2009    |    |
| Tax expense (benefit) at statutory rate | (34.0 )      | )% | (34.0 ) | )% |
| Non-deductible stock compensation       | 4.5          | %  | —       | %  |
| Write-off of deferred tax assets        | 11.2         | %  | —       | %  |
| Other permanent differences             | 6.1          | %  | 2.0     | %  |
| Change in valuation allowance           | 12.2         | %  | 32.0    | %  |
| Effective income tax rate               | —            |    | —       |    |

## 12. New Accounting Pronouncements

In March 2010, the FASB issued new accounting guidance, under ASC Topic 605 on Revenue Recognition. This standard provides that the milestone method is a valid application of the proportional performance model for revenue recognition if the milestones are substantive and there is substantive uncertainty about whether the milestones will be achieved. Determining whether a milestone is substantive requires judgment that should be made at the inception of the arrangement. To meet the definition of a substantive milestone, the consideration earned by achieving the milestone (1) would have to be commensurate with either the level of effort required to achieve the milestone or the enhancement in the value of the item delivered, (2) would have to relate solely to past performance, and (3) should be reasonable relative to all deliverables and payment terms in the arrangement. No bifurcation of an individual milestone is allowed and there can be more than one milestone in an arrangement. The standard is effective for annual periods, and interim periods within those annual periods, beginning on or after June 15, 2010. The adoption of the

guidance is not anticipated to have a material impact on the Company's consolidated financial statements.

In January 2010, the FASB issued new accounting guidance under ASC Topic 820 on Fair Value Measurements and Disclosures, which requires new disclosures and clarifies some existing disclosure requirements about fair value measurement. Under the new guidance, a reporting entity should (a) disclose separately the amounts of significant transfers in and out of Level 1 and Level 2 fair value measurements and describe the reasons for the transfers, and (b) present separately information about purchases, sales, issuances, and settlements in the reconciliation for fair value measurements using significant unobservable inputs. This guidance was effective for interim and annual reporting periods beginning after December 15, 2009, except for the disclosures about purchases, sales, issuances, and settlements in the roll forward of activity in Level 3 fair value measurements which are effective for fiscal years beginning after December 15, 2010, and for interim periods within those fiscal years. The adoption of the guidance effective for interim and annual reporting periods beginning after December 15, 2009 did not have a material impact upon the Company's consolidated financial position or results of operations. The adoption of the guidance effective for fiscal years beginning after December 15, 2010 is not expected to have a material effect on the Company's consolidated financial position or results of operations.

In October 2009, the FASB issued new accounting guidance, under ASC Topic 985 on software, which amends the scope of existing software revenue recognition accounting. Tangible products containing software components and non-software components that function together to deliver the product's essential functionality would be scoped out of the accounting guidance on software and accounted for based on other appropriate revenue recognition guidance. This guidance is effective for all new or materially modified arrangements entered into on or after January 1, 2011 with earlier application permitted as of the beginning of a fiscal year. Full retrospective application of this new guidance is optional. This guidance must be adopted in the same period that the company adopts the amended accounting for arrangements with multiple deliverables described in the preceding paragraph. The Company has not completed its assessment of this new guidance on its consolidated financial position or results of operations.

In June 2009, the FASB issued ASC 810, which eliminates the exceptions to consolidating qualifying special-purpose entities, contains new criteria for determining the primary beneficiary, and increases the frequency of required reassessments to determine whether a company is the primary beneficiary of a variable interest entity. ASC810 also contains a new requirement that any term, transaction, or arrangement that does not have a substantive effect on an entity's status as a variable interest entity, a company's power over a variable interest entity, or a company's obligation to absorb losses or its right to receive benefits of an entity must be disregarded in applying Interpretation 46(R)'s provisions. The elimination of the qualifying special-purpose entity concept and its consolidation exceptions means more entities will be subject to consolidation assessments and reassessments. ASC810 is effective as of January 1, 2010. The adoption of this pronouncement did not have a material impact on the Company's consolidated financial position and results of operations.

The FASB has issued Accounting Standard Update (ASU) 2009-17, Consolidations (Topic 810) - Improvements to Financial Reporting by Enterprises Involved with Variable Interest Entities. ASU 2009-17 changes how a reporting entity determines when an entity that is insufficiently capitalized or is not controlled through voting (or similar rights) should be consolidated. This determination is based on, among other things, the other entity's purpose and design and the Company's ability to direct the activities of the other entity that most significantly impact the other entity's economic performance. ASU 2009-17 was effective at the start of the Company's first fiscal year beginning after November 15, 2009. The adoption of this standard has had no material impact on the Company's consolidated financial position and results of operations.

### 13. Subsequent Events

On January 1, 2011, the Company granted 3,597 shares of Series B convertible preferred stock to the Series B convertible preferred stock owners issued as payment in kind for dividends.

On February 14, 2011, Hocks Acquisition Corporation (“Hocks Acquisition”), the Company’s wholly-owned subsidiary (formed February 2011), entered into an Asset Purchase Agreement (the “Asset Purchase Agreement”) with Hocks Pharmacy Inc., an Ohio corporation (“Hocks Pharmacy”) and its shareholders. Under the Asset Purchase Agreement, Hocks Acquisition purchased all of the inventory and fixed assets (the “Purchased Assets”) owned by Hocks Pharmacy and used in the operation of its internet pharmacy business (the “Internet Business”). The Internet Business consists primarily of the internet sale of over-the-counter health and medical products and supplies. Hocks Acquisition paid \$200,000 in cash to Hocks Pharmacy for the Purchased Assets.

Also on February 14, 2011, the Company entered into a Merger Agreement (the “Merger Agreement”) with Hocks Pharmacy and its shareholders and Hocks.com Inc. (“Hocks.com”), a newly formed Ohio corporation and a wholly-owned subsidiary of Hocks Pharmacy. Under the Merger Agreement, Hocks Acquisition merged into Hocks.com and Hocks.com became the Company’s wholly-owned subsidiary. At the time of the Merger, Hocks.com owned all of the intangible assets of the Internet Business, including trademarks, domain names, customer accounts and goodwill. The merger consideration consisted of 166,667 shares of the Company’s Common Stock issued to Hocks Pharmacy.

The following table presents the unaudited pro-forma combined results of operations of the Company and Hocks .com for each of the years ended December 31, 2010 and 2009, respectively, as if Hocks.com had been acquired at the beginning of each of the periods.

|  | For the years Ended December 31, |              |
|--|----------------------------------|--------------|
|  | 2010                             | 2009         |
|  | (unaudited)                      | (unaudited)  |
| Revenue  | \$ 10,171,453                    | \$ 8,580,786 |
| Net loss   | (3,712,812 )                     | (2,557,011 ) |
| Pro-forma basic and diluted net loss per common share          | \$ (0.36 )                       | \$ (0.28 )   |
| Weighted average common shares outstanding – basic and diluted | 10,235,242                       | 9,051,511    |

The Company was unable to prepare required disclosure at the time of the preparation of this document.

On February 11, 2011, the Company granted three Board of directors options to purchase an aggregate of 60,000 shares of common stock with an exercise price of \$4.10 for a total value of \$133,110 under a previously approved option plan. The options vest over a three year period and have a term of ten years.

On February 11, 2011, the Company granted employees options to purchase an aggregate of 145,000 shares of common stock with an exercise price of \$4.10 for a total value of \$321,683 under a previously approved option plan. The options vest over a three year period and have a term of ten years.

On February 11, 2011, the Company granted outside consultants options to purchase an aggregate of 100,000 shares of common stock with an exercise price of \$4.10 for a total value of \$221,850 under a previously approved option plan. The options vest over a three year period and have a term of ten years.

Management has evaluated subsequent events or transactions occurring through the date on which the financial statements were issued.