

NEOGEN CORP  
Form 10-K  
August 14, 2007  
Table of Contents

---

**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 May 31, 2007

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

For The Transition Period From \_\_\_\_\_ To \_\_\_\_\_.

COMMISSION FILE NUMBER 0-17988

---

**NEOGEN CORPORATION**

*(Exact name of registrant as specified in its charter)*

---

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

**38-2367843**  
*(I.R.S. Employer  
Identification No.)*

**620 Leshar Place**  
**Lansing, Michigan 48912**

*(Address of principal executive offices including zip code)*

Edgar Filing: NEOGEN CORP - Form 10-K

517-372-9200

*(Registrant's telephone number, including area code)*

---

**SECURITIES REGISTERED PURSUANT TO SECTION 12(b) OF THE ACT: NONE**

**SECURITIES REGISTERED PURSUANT TO SECTION 12(g) OF THE ACT:**

**COMMON STOCK, \$0.16 par value per share**

*(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  No

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

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

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

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

Large accelerated filer  Accelerated filer  Non-accelerated filer

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

Based on the closing sale price on November 30, 2006 the aggregate market value of the voting stock held by non-affiliates of the registrant was \$171,500,000. For these purposes, the registrant considers its Directors and executive officers to be its only affiliates.

The number of shares outstanding of the registrant's Common Stock was 9,360,000 on July 31, 2007.

---

**Table of Contents**

**DOCUMENTS INCORPORATED BY REFERENCE**

The Registrant's definitive proxy statement to be prepared pursuant to regulation 14a and filed in connection with solicitation of proxies for its October 11, 2007 annual meeting of shareholders is incorporated by reference into part III of this Form 10-K.

**Table of Contents**

**TABLE OF CONTENTS**

	<b>Page</b>
<b><u>PART I</u></b>	
ITEM 1. <u>BUSINESS</u>	4
ITEM 1A. <u>RISK FACTORS</u>	12
ITEM 1B. <u>UNRESOLVED STAFF COMMENTS</u>	15
ITEM 2. <u>PROPERTIES</u>	15
ITEM 3. <u>LEGAL PROCEEDINGS</u>	15
ITEM 4. <u>SUBMISSION OF MATTER TO A VOTE OF SECURITY HOLDERS</u>	15
<b><u>PART II</u></b>	
ITEM 5. <u>MARKET FOR REGISTRANT'S COMMON EQUITY, RELATED STOCKHOLDER MATTERS AND ISSUER PURCHASES OF EQUITY SECURITIES</u>	16
ITEM 6. <u>SELECTED FINANCIAL DATA</u>	17
ITEM 7. <u>MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS</u>	18
ITEM 7A. <u>QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISKS</u>	25
ITEM 8. <u>FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA</u>	25
ITEM 9. <u>CHANGES IN AND DISAGREEMENTS WITH ACCOUNTANTS ON ACCOUNTING AND FINANCIAL DISCLOSURE</u>	25
ITEM 9A. <u>CONTROLS AND PROCEDURES</u>	25
ITEM 9B. <u>OTHER</u>	26
<b><u>PART III</u></b>	
ITEM 10. <u>DIRECTORS, EXECUTIVE OFFICERS OF THE REGISTRANT AND CORPORATE GOVERNANCE</u>	27
ITEM 11. <u>EXECUTIVE COMPENSATION</u>	28
ITEM 12. <u>SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS, MANAGEMENT AND RELATED STOCKHOLDER MATTERS</u>	29
ITEM 13. <u>CERTAIN RELATIONSHIPS, RELATED TRANSACTIONS AND DIRECTOR INDEPENDENCE</u>	29
ITEM 14. <u>PRINCIPAL ACCOUNTANT FEES AND SERVICES</u>	29
<b><u>PART IV</u></b>	
ITEM 15. <u>EXHIBITS, FINANCIAL STATEMENT SCHEDULE</u>	30
<u>SIGNATURES</u>	31
<u>LIST OF FINANCIAL STATEMENTS AND FINANCIAL STATEMENT SCHEDULE</u>	32
Subsidiaries	
Consent of independent registered public accounting firm Ernst & Young LLP	
Section 302 Certification of Chief Executive Officer	
Section 302 Certification of Chief Financial Officer	
Section 1350 Certification pursuant to Section 906	

**Table of Contents**

**CAUTIONARY STATEMENT REGARDING FORWARD-LOOKING INFORMATION**

Forward-looking statements, within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended, are made throughout this Annual Report on Form 10-K, including statements relating to management's expectations regarding new product introductions; the adequacy of the Company's sources for certain components, raw materials and finished products; and the Company's ability to utilize certain inventory. For this purpose, any statements contained herein that are not statements of historical fact may be deemed to be forward-looking statements. Without limiting the foregoing, the words believes, anticipates, plans, expects, seeks, estimates, and similar expressions are intended to identify forward-looking statements. There are a number of important factors that could cause Neogen Corporation's results to differ materially from those indicated by such forward-looking statements, including those detailed under the caption Management's Discussion and Analysis of Financial Condition and Results of Operations Critical Accounting Policies and Estimates and - Future Operating Results.

In addition, any forward-looking statements represent management's views only as of the day this Annual Report on Form 10-K was first filed with the Securities and Exchange Commission and should not be relied upon as representing management's views as of any subsequent date. While management may elect to update forward-looking statements at some point in the future, it specifically disclaims any obligation to do so, even if its views change.

**Table of Contents****PART I.****ITEM 1. BUSINESS**

Neogen Corporation and subsidiaries (Neogen or the Company) develop, manufacture, and market a diverse line of products dedicated to food and animal safety. The Company's food safety segment consists primarily of diagnostic test kits and complementary products (e.g., dehydrated culture media) marketed by company sales personnel in the United States, Canada, the United Kingdom and other parts of Europe and by distributors elsewhere to food producers and processors to detect dangerous and/or unintended substances in human food and animal feed, such as foodborne pathogens, spoilage organisms, natural toxins, food allergens, genetic modifications, ruminant by-products, drug residues, pesticide residues and general sanitation concerns. The diagnostic test kits are generally less expensive, easier to use and provide greater accuracy and speed than conventional diagnostic methods. The majority of the tests are disposable, single-use, immunoassay and gene probe products that rely on the Company's proprietary antibodies and RNA and DNA probes to produce rapid and accurate test results. The Company's expanding line of food safety products also includes bioluminescence-based diagnostic technology.

Neogen's animal safety segment is engaged in the development, manufacture and marketing of pharmaceuticals, rodenticides, disinfectants, vaccines, veterinary instruments, topicals and diagnostic products for the worldwide animal safety market. The majority of these consumable products are marketed through a network of national and international distributors, as well as a number of large farm supply retail chains in the United States and Canada. The Company's USDA-licensed facility in Tampa, which is expected to be moved to Lansing MI in fiscal 2008, produces immunostimulant products for horses and dogs, and a unique equine botulism vaccine. The Company's line of drug detection products are sold worldwide for the detection of abused and therapeutic drugs in animals and animal products.

Management's vision is for Neogen to become a world leader in development and marketing of products dedicated to food and animal safety. To meet this vision, a growth strategy consisting of the following elements has been developed: (i) increasing sales of existing products; (ii) introducing new products and product lines; (iii) expanding international sales; and (iv) acquiring businesses and forming strategic alliances. While the elements of the strategy are stated in order of importance over the long term, management understands and believes that strategic acquisitions will provide the best opportunity for more rapid growth in the short term. For that reason, an active acquisition program is maintained and financial and other resources are maintained to capitalize on opportunities as they arise.

Neogen Corporation was formed as a Michigan corporation in June 1981 and actual operations began in 1982. The Company's principal executive offices are located at 620 Leshar Place, Lansing, Michigan 48912-1595 and its telephone number is (517) 372-9200.

Neogen's Annual Report on Form 10-K, Quarterly Reports on Form 10-Q, Current Reports on Form 8-K, and amendments to those reports are available free of charge via our Internet website ([www.neogen.com](http://www.neogen.com)) as soon as reasonably practicable after such information is filed with, or furnished to, the United States Securities and Exchange Commission.

**PRODUCTS**

Trademarks and registered trademarks Neogen markets its products under include: **Corporate:** Neogen®, Neogen flask®, **Food Safety:** AccuScan®, AccuPoint®, AccuClean®, Acumed®, *fa* and logo®, Agri-Screen®, Agri-Screen Ticket®, Alert®, BetaStar®, Centrus®, GeneQuence®, Gene-Trak®, ISO-GRID®, NeoGrid®, Rev@r®, Revive®, Soleris®, Verato®, **Animal Safety:** AluShield®, AmVet®, BottomHoof®, BotVax®, Calf Eze®, D3 Needles®, DC&R®, Dr. Frank®, ElectroJac®, ELISA Technologies®, EqStim®, EquiMax®, Fura-Zone®, Gnat-Away®, GNatural®, Gold Nugget® and logo®, Gold Wrap®, Ideal®, ImmunoRegulin®, ImmunoVet®, Injecto-Stik®, Insignifit®, Iso-Prine®, K-Blue®, K-Gold®, MegaShot®, Mini-Shot®, MycAseptic®, NFZ®, NeogenVet®, NeedleGuard®, Paddock & Pasture®, PanaKare®, Penzyme®, Poridon®, Pro-Pistol®, Pro-Shot®, ProZap®, Pyril-Pam®, Ramik®, RenaKare®, Shine N' Glo®, Spec-Tuss®, Sustran-N-Aid®, Stress-De®, TCA Paint®, ThrushCrusher®, ThyroKare®, TopHoof®, Tri-Hist®, Tri-Seal®, Triple Block®, Triple Cast®, Triple Crown® and Logo®, Triple Heat®, Tri-Soxsuprine®, UriKare®, UriCon®, Vita-15®, Rodex®, Havoc®, CyKill®, Hacc®.

---

## **Table of Contents**

Neogen operates in two primary business areas: products for the detection of pathogens, natural toxins and other unwanted substances in food and feed products, the Food Safety segment, and products dedicated to animal health, the Animal Safety segment. See Notes to Consolidated Financial Statements elsewhere in this Form 10-K for financial information about the Company's business segments and international operations.

### **FOOD SAFETY SEGMENT**

The products of Neogen's food safety segment consist primarily of diagnostic test kits and complementary products marketed to food and feed producers and processors to detect dangerous and/or unintended substances in food and animal feed, such as foodborne pathogens, spoilage organisms, natural toxins, food allergens, genetic modifications, ruminant by-products, drug residues, pesticide residues and general sanitation concerns.

Many of Neogen's food safety test kits use immunoassay technology to rapidly detect target substances. The Company's ability to produce superior antibodies sets its products apart from immunoassay test kits produced and sold by other companies. The Company's kits are available in microwell formats, which allow for the rapid processing of a large number of samples and automated procedures, and lateral flow and other similar devices that provide distinct visual results. Typically test kits use antibody-coated test devices and chemical reagents to produce a color change to indicate a positive or negative result for the presence of a target substance in a test sample. The simplicity of the tests make them accessible to all levels of food producers, processors and handlers.

Neogen's test kits are used to detect potential hazards in food and animal feed by testers ranging from small local grain elevators to the largest, best-known food and feed processors in the world, and numerous regulatory agencies.

Meat and poultry processors, seafood processors, fruit and vegetable producers and many other market segments are the primary users of the Neogen's Reveal<sup>®</sup> and Alert<sup>®</sup> tests for foodborne bacteria, including *E. coli* O157:H7, *Salmonella*, *Listeria* and *Campylobacter*. Grain producers and processors of all types and sizes use the Company's Verato<sup>®</sup>, Agri-Screen<sup>®</sup> and Reveal<sup>®</sup> tests for mycotoxins, including aflatoxin, deoxynivalenol, fumonisin, ochratoxin, zearalenone and T-2 toxin, to help ensure product safety and quality. The world's largest producers of cookies, crackers, candy, ice cream, and many other foods, use the Company's Verato<sup>®</sup>, Alert<sup>®</sup> and Reveal<sup>®</sup> testing products for food allergens to help protect their food-allergenic customers from the inadvertent contamination of products with food allergens, such as peanut, milk, egg, almond, wheat, soy, and hazelnut residues.

Dairies are primary users of Neogen's Beta Star and Penzyme diagnostic tests to detect the presence of Beta Lactam antibiotics in milk. The presence of these drugs in milk is an economic risk to processors as it limits further processing and is also a public health hazard.

Neogen developed the first rapid immunoassay test kits to detect ruminant by-products in animal feed ingredients and finished feed. The Reveal<sup>®</sup> tests were designed to help prevent ruminants (cattle, sheep and goats) from being fed rendered materials containing ruminant by-products in an effort to prevent the spread of BSE (a.k.a., mad cow disease) from animal to animal. The Company's specialty products for the seafood market include tests for histamine, a highly allergenic substance that occurs when certain species of fish begin to decay; chloramphenicol, a banned antibiotic in most of the world, but still used by some shrimp farmers to improve the yield of their product; and sulfites, an effective but potentially allergenic shrimp preservative.

Neogen also offers other test methods and products to complement its immunoassay tests. The Company's line of Gene-Tra<sup>®</sup> and GeneQuence<sup>®</sup> assays utilize DNA probe hybridization technology to create exceptionally sensitive and specific tests to detect foodborne bacteria. Instead of using antibodies as in an immunoassay to capture a target pathogen that may be present in a sample, this technology uses a portion of the target pathogen's unique ribosomal RNA (rRNA) sequence to bind to complementary rRNA strands of the pathogen in a sample. The result is a test with the ease and speed of a rapid test method, but the specificity of a time-consuming conventional laboratory method (specificity is a test's ability to distinguish between a target pathogen, and a closely-related but innocuous bacterium).

---

## **Table of Contents**

Neogen's Soleris® product is used by food processors to identify the presence of spoilage organisms and other microbiological contamination.

Neogen's Acumed® subsidiary offers dehydrated culture media for varied purposes, including traditional bacterial testing, and growing beneficial bacteria, such as cultures for sausages and beer. The Company's customers for dehydrated culture media also include commercial and research laboratories and producers of pharmaceuticals, cosmetics and veterinary vaccines.

Neogen manufactures and markets its AccuPoint® rapid sanitation test for adenosine triphosphate (ATP), a chemical found in all living cells. This easy to use and inexpensive test uses bioluminescence to quickly (in less than 30 seconds) determine if a food contact surface has been sanitized completely. When ATP comes into contact with the firefly reagent luciferin luciferase contained in the test device, a reaction takes place that produces light. The more light, the more present ATP and the greater the need for more thorough sanitation. The Company's worldwide customer base for its ATP sanitation testing products includes food and beverage processors, the foodservice industry, as well as many other users.

Revenues from Neogen's Food Safety Division accounted for 54.5%, 48.3% and 44.9% of the Company's total revenues for fiscal years ended May 31, 2007, 2006 and 2005, respectively.

## **ANIMAL SAFETY SEGMENT**

Neogen's animal safety segment is primarily engaged in the development, manufacture and marketing of pharmaceuticals, rodenticides, disinfectants, vaccines, veterinary instruments, topicals and diagnostic products to the worldwide animal safety market.

Neogen's AmVet® product line provides innovative, value-added, high quality products to the veterinary market. Top AmVet products include PanaKare®, a digestive aid that serves as a replacement therapy where digestion of protein, carbohydrate and fat is inadequate due to exocrine pancreatic insufficiency; Natural Vitamin E-AD, which aids in the prevention and treatment of vitamin deficiencies in swine, cattle and sheep; and RenaKare®, a supplement for potassium deficiency in cats and dogs. Products sold under the NeogenVet® brand include Vita-15® and Liver 7®, which are used in the treatment and prevention of nutritional deficiencies in horses.

On November 21, 2003, Neogen acquired Hacco, Inc., a manufacturer of rodenticides, including the brands Ramik®, Havoc® and Prozap®. On the same date, it also acquired Hess & Clark, Inc. Hess & Clark's principal products are disinfectants, such as DC&R®, used in animal and food production facilities.

Neogen's in-house equine protozoal myeloencephalitis (EPM) testing service offers veterinarians accurate, timely results for early diagnosis of the disease that can devastate a horse's central nervous system. In addition, the Company's BotVax® vaccine has successfully protected thousands of high value horses and foals against type B botulism, commonly known as Shaker Foal Syndrome. The Company's product is the only USDA-approved vaccine for the prevention of Type B botulism in horses.

Years of research and many thousands of doses have proven Neogen's EqStim® immunostimulant to be safe and effective as a veterinarian-administered adjunct to conventional treatment of equine bacterial and viral respiratory infections. The Company's ImmunoRegul® product uses similar immunostimulant technology to aid in the treatment of pyoderma (a bacterial skin inflammation) in dogs.

Neogen markets a complete line of veterinary instruments and animal health delivery systems under the Ideal product brand name. Approximately 250 different products are offered, many of which are used to deliver animal health products, such as antibiotics and vaccines. Ideal's D3 Needles® are stronger than conventional veterinary needles, and are uniquely detectable by common meat processing facility metal detectors—a big market advantage in the safety-conscious beef and swine industries.

Animal safety products offered by Neogen to the retail over-the-counter market include many of the Ideal brand veterinary instruments and products sold under the Squire® and Gold Nugget® brands. Squire products include Stress-Dex® oral electrolyte replacer for performance horses, and Fura-Zone, for the prevention and treatment of surface bacterial infections in wounds, burns and cutaneous ulcers. Gold Nugget OTC products include GNatural® Spray, to protect horses from biting insects, and Porido®, a pour-on insecticide for horses.



## **Table of Contents**

Neogen's line of approximately 100 drug detection immunoassay test kits are sold worldwide for the detection of approximately 200 abused and therapeutic drugs in racing animals, such as horses, greyhounds and camels, as well as for testing fair animals and for detection of drug residues in meat and meat products. The test kits are also used for human forensic toxicology drug screening applications. This line includes tests for narcotics, analgesics, stimulants, depressants, tranquilizers, anesthetics, steroids and diuretics.

Neogen also has several products used by researchers for the detection of biologically-active substances. These products include tests for cyclic nucleotides, hormones, leukotrienes, prostaglandins and steroids. Marketed under the trademarks of K-Blue and K-Gold, Neogen offers proprietary substrates that it uses in its own testing products, and that are sold to other diagnostic test kit manufacturers.

Revenues from Neogen's Animal Safety Division accounted for 45.5%, 51.7% and 55.1% of the Company's total revenues for fiscal years ended May 31, 2007, 2006 and 2005 respectively.

## **GENERAL SALES AND MARKETING**

Neogen's domestic sales efforts are generally organized by market segments, rather than by products or geography. During the fiscal year that ended May 31, 2007, the Company had more than 5,000 customers for its products. Since many customers for animal safety products are distributors, and certain animal safety products are offered to the general retail market, the total number of end users of the Company's products is considerably greater than 5,000. A total of 128 employees are assigned to sales and marketing functions within the Company. During the year ended May 31, 2007 one food safety distributor customer had revenues of 11.8%. No other customer had revenues in excess of 10%.

## **FOOD SAFETY SALES AND MARKETING**

To reach each customer and prospect with expertise and experience, Neogen has a staff of specialized food safety sales and technical service representatives assigned to specific markets. This staff sells Company products directly to end users, and also handles technical support issues that arise with customers.

Neogen's food safety markets are comprised of: milling and grain, including grain elevators, feed mills, pet food manufacturers, and grain inspection companies; meat and poultry, including meat and poultry processors, producers of ready-to-eat meat and poultry products; and the USDA's Food Safety Inspection Service (FSIS); grocery products, including flour millers, malters, bakeries, candy and confection manufacturers, manufacturers of prepared meals, nuts, spices, cookies, crackers and other snack foods; fruits and vegetables, including growers and processors of juice and packaged fresh cut grocery items; seafood, including harvesters and processors of a wide variety of seafood products; dairy and beverage, including milk processors and soft drink bottlers; Acumedia dehydrated culture media, including commercial and research laboratories and producers of pharmaceuticals, cosmetics and veterinary vaccines; food service and retail, including fast food service establishments and retail grocery market chains, and nutraceuticals including producers and marketers of a wide variety of nutraceutical products.

## **ANIMAL SAFETY SALES AND MARKETING**

Neogen markets a broad range of pharmaceuticals, vitamin injectibles, wound care products, topicals, instruments, testing services and biologicals to the ethical veterinary market. The product range is focused on the food (cattle and pigs) and companion (horses, dogs, and cats) animal markets. Neogen's sales group works directly with veterinarians, clinics and universities and markets through established ethical distributors by supporting the efforts of over 500 domestic distributor sales representatives calling on 35,000 plus veterinarians. Neogen further supports its veterinary distribution channel through product training, field support, promotions and technical service.

The over-the-counter (OTC) animal health market also offers significant growth opportunities for Neogen and its products. Neogen offers a broad range of products including well recognized brands of rodenticides, disinfectants, instruments and horse care products. To reach the OTC market, Neogen's sales team works with

## **Table of Contents**

a large network of animal health distributors including marketing groups, traditional two-step distributors, catalogers and large retail chains. Support includes product training, field support, planogram solutions, promotions and advertising.

### **INTERNATIONAL SALES AND MARKETING**

#### **FOOD SAFETY:**

Internationally, Neogen uses its own sales managers to work closely with and coordinate the efforts of a network of more than 120 distributors in 100 countries. The distributors provide local training and technical support, perform market research, and promote Company products within designated countries around the world.

Neogen's March 2003 acquisition of Adgen Ltd., (now Neogen Europe, Ltd.), provides the Company better access to the European Union, and allows it to better serve its network of customers and distributors throughout the EU. Customers in United Kingdom, France and Germany are served by Company employees. Other European region customers are serviced by distributors managed by Neogen Europe personnel. Prior to the acquisition, Adgen was a major distributor of Neogen products in Europe, and a producer and marketer of its own agricultural diagnostic testing products. Adding Adgen's experienced research and development team continues to be a strong asset in the development of products tailored to meet unique requirements of the European market.

Neogen's dairy antibiotics diagnostic products are distributed outside of North America by Denmark based Chr. Hansen, an international supplier of natural ingredient solutions for the food and health and nutritional industries.

Distribution of Soleris diagnostic test system for general spoilage organisms is marketed worldwide by Neogen personnel and Denmark based Foss Analytical.

Since 2002, Neogen has continued to maintain a presence in Shanghai, China, to better serve the expanding food safety market, as well as more closely manage its Chinese food and animal safety manufacturing. Neogen intends to use local distributors to introduce the Company's products in the Chinese market.

#### **ANIMAL SAFETY:**

The Animal Safety's international sales group has established a strong presence in several key markets with rodenticides, disinfectants, instruments and veterinary products. Primarily, utilizing in-country distributors and US-based exporters, these markets include Mexico, Canada, Australia, EU, South America, and the Caribbean. Diagnostic products are sold around the world through an extensive distributor network.

#### **GENERAL:**

Revenues from Neogen's international sales accounted for 38.0%, 28.6% and 27.1% of the Company's total revenues for fiscal years ended May 31, 2007, 2006 and 2005, respectively.

Risks associated with foreign operations include the need for additional regulatory approvals, possible disruptions of product delivery, the differing product needs of foreign customers, difficulties in building and managing foreign operations, fluctuations in the value of foreign currencies, import/export duties and quotas, and unexpected regulatory, economic or political changes in foreign markets. The level of foreign activities does not currently require hedging to reduce the effect of currency fluctuations.

### **RESEARCH AND DEVELOPMENT**

Management maintains a strong commitment to Neogen's research and development activities. The Company's product development efforts are focused on the enhancement of existing product lines and in development of new products that fit its business strategy. The Company employs 32 individuals in its research and development department, including immunologists, chemists, engineers and microbiologists. Research and development expenditures were approximately \$3.3 million, \$3.0 million and \$2.7 million representing

---

**Table of Contents**

3.8%, 4.1% and 4.3% of total revenues in fiscal 2007, 2006 and 2005, respectively. Management currently intends to maintain the Company's research and development expenditures at approximately 4% to 6% of total revenues.

Neogen has ongoing development projects for new diagnostic tests and other complimentary products for both the food safety and animal safety markets. Management expects that these products will be available for marketing in fiscal years 2008 to 2010.

Portions of certain technologies utilized in some products marketed by Neogen were acquired from or developed in collaboration with affiliated partnerships, independent scientists, governmental units, universities and other third parties. The Company has entered into agreements with these parties that provide for the payment of royalties based upon sales of products that utilize the pertinent technology. Royalty expense under these agreements amounted to \$1,124,000, \$911,000 and \$742,000 in 2007, 2006 and 2005, respectively.

**PROPRIETARY PROTECTION AND APPROVALS**

Patents and trademarks are applied for whenever appropriate. Since its inception, Neogen has acquired and received more than 50 patents and trademarks, and has several pending patents and trademarks. The patents expire at various times over the next 20 years.

Management believes that Neogen has adequate protection as to proprietary rights for its products. However, it is aware that substantial research has taken place at universities, governmental agencies and other companies throughout the world and that numerous patent applications have been filed and that numerous patents have been issued. To the extent some of the Company's products may now, or in the future, embody technologies protected by patents, copyrights or trade secrets of others, licenses to use such technologies may need to be obtained in order to continue to sell the products. These licenses may not be available on commercially reasonable terms. Failure to obtain any such licenses may delay or prevent the sale of certain new or existing products. In addition, patent litigation is not uncommon. Accordingly, there can be no assurance that the Company's existing patents will be sufficient to completely protect its proprietary rights.

Neogen uses trade secrets as proprietary protection in numerous of its food and animal safety products. In many cases, the Company has developed unique antibodies capable of detecting microorganisms and residues at minute levels. The supply of these antibodies, and the proprietary techniques utilized for their development, may offer better protection than the filing of patents. Such proprietary reagents are maintained in secure facilities and stored in more than one location to reduce exposure to complete destruction by natural disaster or other means.

One of the major areas affecting the success of biotechnology development involves the time, costs and uncertainty surrounding regulatory approvals. Currently, Neogen products requiring regulatory approval include BotVax B, EqStim and ImmunoRegulin. The Company's general strategy is to select technical and proprietary products that do not require mandatory approval to be marketed. In China three of the Company's immunoassay based test kits are listed in the GB, or National Standard. Listings of these products are expected to assist generating future sales into Government and other laboratories in China.

Neogen utilizes third party validations on many of its disposable test kits as a marketing tool to provide its customers with the proper assurances. These include validation by the Association of Official Analytical Chemists, independently administered third-party, multi-laboratory collaborative studies and approvals by the U.S. Federal Grain Inspection Service and the U.S. Food Safety Inspection Service for the use of Company products in their operations.

**PRODUCTION AND SUPPLY**

Neogen manufactures its products in Lansing, Michigan; Lexington, Kentucky; Randolph, Wisconsin; Tampa, Florida; and Ayr, Scotland. There are currently approximately 196 full-time employees assigned to manufacturing in these five locations. Most locations operate on a one-shift basis, but could be increased to a two-shift basis. Management believes it could increase the current output of its primary product lines by more than 50% using the current space available with a minimum of additional capital equipment.

## **Table of Contents**

Manufacturing of diagnostic tests for detection of natural toxins, pathogens, food allergen and pesticides, final kit assembly, quality assurance and shipping takes place in the Company's facilities in Lansing. Proprietary monoclonal and polyclonal antibodies for the Neogen's diagnostic kits are produced on a regular schedule in the Company's immunology laboratories. Other reagents are similarly prepared by the R&D employees.

Manufacturing of diagnostic tests for the presence of dairy antibiotics in milk is completed in the Company's Lansing facilities. Generally, final assembly and shipment to customers are performed in the Company's Ayr, Scotland facility.

Assembly and shipment of electronic readers and disposable single-use samplers takes place in the Company's facilities in Lansing.

Dehydrated culture media products are manufactured in a FDA monitored facility in Lansing. Products are blended following strict formulations or custom blended to customer specification and shipped directly to customers from Lansing.

Soleris single-use vials and equipment are produced and shipped to customers mostly by third party vendors.

Manufacture of pharmacological diagnostic test kits, test kits for drug residues and of animal health products takes place in the Company's facility in Lexington. In general, manufacturing operations including reagent manufacturing, quality assurance, final kit assembly and packaging are performed by Neogen personnel. Certain animal health products that are purchased finished or that are toll manufactured by third party vendors and veterinary instruments are warehoused and shipped from the Company's Lexington, facility. Other veterinary instruments are produced in the Company's facilities in Lansing, and are generally then shipped to Lexington, for distribution to customers.

Manufacture of rodenticides and disinfectants takes place in Randolph. Manufacturing consists of blending technical material (active ingredient) with bait consisting principally of various grains.

The Tampa facility is an USDA-approved manufacturing plant devoted to the production of the biologic products EqStim® and ImmunoRegulin®. *P. acnes* seed cultures are added to media and then subjected to several stages of further processing resulting in a product that is filled and packaged within the Tampa facility. The Company's BotVax B vaccine is also produced in the Tampa facility utilizing Type B botulism seed cultures and a traditional fermentation process. All completed biologic products are then shipped to Neogen's Lexington, facilities for inventory and distribution to customers.

Neogen purchases component parts and raw materials from more than 200 suppliers. Though many of these supplies are purchased from a single source in order to achieve the greatest volume discounts, the Company believes it has identified acceptable alternative suppliers for all of its components and raw materials.

Shipments of products are generally accomplished within a 48-hour turnaround time. As a result of this quick response time, Neogen's backlog of unshipped orders at any given time is not significant.

## **COMPETITION**

Although competitors vary in individual markets, management knows of no competitor that is pursuing Neogen's fundamental strategy of developing and marketing a full line of products, ranging from disposable tests and dehydrated culture media to veterinary pharmaceuticals and veterinary instruments for a large number of food safety and animal safety concerns. For each of its individual products, the Company faces intense competition from companies ranging from small businesses to divisions of large international companies. Some of these organizations have substantially greater financial resources than the Company. The Company competes primarily on the basis of ease of use, speed, accuracy, and other similar performance characteristics of its products. The breadth of the Company's product line, the effectiveness of its sales and customer service organizations and pricing are also components in management's competitive plan. Management is not aware of any factors within its product lines that place the Company in an unfavorable position relative to its competitors.

## **Table of Contents**

Future competition may become even more intense, including the development of changing technologies, which could affect the marketability of Neogen's products. The Company's competitive position also will depend on management's ability to develop proprietary products, attract and retain qualified scientific and other personnel, develop and implement production and marketing plans and obtain patent protection and adequate capital resources.

### **FOOD SAFETY:**

Neogen's Food Safety Division has strong distribution of its products using Company employees domestically and from an active and aggressive distributor group outside of North America. With one of the largest professional sales organizations in the industry, management believes that it maintains a general competitive advantage as sales personnel are in a position to be with customers and prospects more frequently than those of its competitors. Additionally, as an agricultural based company, Neogen has what is believed to be a unique insight into the food industry as opposed to clinically based competition.

Competition for pathogen detection products includes traditional methods and antibody and genetic based platforms. Neogen's product offerings compete across the entire spectrum of methods. Competition for natural toxins and allergen detection products include instrumentation and antibody based tests. Generally, the Company's products fall within the non-instrument category. While for these and other food safety products the Company's offerings will not always compete on all platforms in all markets, the products that are offered provide tests that can be well utilized by most customers to meet their testing needs.

Besides its strong product offerings and its superior distribution, the Company focuses its competitive advantage in the areas of customer service and speed and ease of use of its products. Additionally, by aggressively maintaining itself as a low cost producer, Neogen assures that it can be competitive with new market entrants that may choose a low pricing strategy in an attempt to gain market share.

### **ANIMAL SAFETY:**

Neogen's Animal Safety Division faces no one competitor across the products and markets it serves. In the racing industry market, the Company believes it holds the position of dominant market share, facing only one other significant company in the marketplace. In the Life Sciences market, the Company competes against several other diagnostic and reagent companies with similar product offerings.

In the veterinary market, Neogen markets BotVax B, the only USDA approved vaccine for the prevention of botulism Type B in horses. The Company competes on other key products through differentiated product performance and superior customer and technical support. With some of its products, the Company provides solutions as a lower cost alternative and offers a private label option for its distributors.

Competition in the rodenticide market includes several companies of comparable size that offer products into similar market segments. The rodenticide retail market is dominated by a single brand. While the technical materials used by the competing companies are similar, Neogen uses manufacturing and bait formula techniques to better draw rodents to the product and thereby improve overall product performance.

Neogen competes in the retail market by providing solutions to common retail problems – stock outs, wasted floor space, and inconsistent brand identity. The Company offers plan-o-grams and reordering systems to maximize turns and profitability for its retail customers.

### **GOVERNMENT REGULATION**

A significant portion of the Neogen's products and revenues are affected by the regulations of various domestic and foreign government agencies, including the U.S. Department of Agriculture, the Environmental Protection Agency, and the U.S. Food and Drug Administration. Changes in these regulations could affect revenues and/or costs of production and distribution.

Neogen's development and manufacturing processes involve the use of certain hazardous material, chemicals and compounds. Management believes that the Company's safety features for handling and disposing of such commodities comply with the standards prescribed by local, state and federal regulations. The Company's cost to comply with these regulations is not significant and the Company has no reason to believe that any such future legislation or rules would be materially adverse to its business.

## **Table of Contents**

The Company's rodenticide products generally require registration with U.S. governmental agencies at federal and state levels and with foreign governments.

### **EMPLOYEES**

Currently, the Company employs 427 full-time persons. None of the employees are covered by collective bargaining agreements. There have been no work stoppages or slow downs due to labor-related problems. Management believes that its relationship with its employees is good. All employees having access to proprietary information have executed confidentiality agreements with the Company.

### **ITEM 1A. RISK FACTORS**

An investment in our common shares involves a high degree of risk. The risks described below are not the only ones that an investor faces. Additional risks that are not yet known to us or that we currently think are immaterial could also impair our business, financial condition or results of operations. If any of the following risks actually occurs, our business, financial condition or results of operations could be adversely affected.

#### **Risks Relating to Our Business**

##### **Our business strategy is dependent on successfully identifying and integrating acquisitions as well as promoting internal growth.**

Our business has grown significantly over the past several years as a result of both internal growth and acquisitions of existing businesses and their products. Identifying and pursuing acquisition opportunities, integrating these acquisitions into our business and managing their growth require a significant amount of management time and skill. We cannot assure that we will be effective in identifying, integrating or managing any acquisition target in the future. Our failure to successfully integrate and manage any future acquisition may have a material adverse effect on our operating results and financial condition.

In addition, if we continue to experience growth in our business, our growth could place a significant strain on our management, customer service, operations, sales and administrative personnel and other resources. To serve the needs of our existing and future customers, we will be required to train, motivate and manage qualified employees. We have incurred and will continue to incur significant costs to retain qualified management, sales and marketing, engineering, production, manufacturing and administrative personnel, as well as expenses for marketing and promotional activities. Our ability to manage our planned growth depends upon our success in expanding our operating, management and information and financial systems, which might significantly increase our operating expenses.

We might not be able to manage effectively our future growth, and if we fail to do so, our business, financial condition and results of operations would be adversely affected.

##### **The development of new products entails substantial risk of failure.**

We are continually developing new products for which we believe there should be significant market demand. We cannot assure that we will successfully develop commercially viable products, that the products will be developed on a timely basis to meet market demand or that the relevant market will be properly identified. If we expend substantial resources in developing an unsuccessful product, operating results will be adversely affected.

##### **Our international operations are subject to different product standards as well as other operational risks.**

In fiscal 2007, international sales accounted for 38% of the Company's total revenue. We expect that our international business will continue to account for a significant portion of our total revenue. Foreign regulatory bodies may establish product standards different from those in the U.S. and with which the Company's current

## **Table of Contents**

products do not comply. Our inability to design products that comply with foreign standards could have a material adverse effect on our future growth. Other risks related to our international sales include the possible disruption in transportation, difficulties in building and managing foreign distribution, fluctuation in the value of foreign currencies, import duties and quotas and unexpected economic and political changes in foreign markets. These factors might adversely affect international sales and our overall financial performance.

### **The markets for our products are extremely competitive, and our competitors may be able to utilize existing resource advantages to our detriment.**

The markets in which the Company competes are subject to rapid and substantial changes in technology and are characterized by extensive research and development and intense competition. Many of our competitors and potential competitors have greater financial, technical, manufacturing, marketing, research and development and management resources than we do. These competitors might be able to use their resources, reputations and ability to leverage existing customer relationships to give them a competitive advantage over us. They might also succeed in developing products that are at least as reliable and effective as our products that make additional measurements, that are less costly than our products or that provide alternatives to our products.

### **We are dependent on the agricultural marketplace, which is affected by factors beyond our control.**

Our primary customers are in the agricultural and food production industries. Economic conditions affecting agricultural industries are cyclical and are dependent upon many factors outside our control, including weather conditions or changes in consumption patterns. An economic downturn in the agricultural marketplace could adversely affect our sales.

### **Our quarterly operating results are subject to significant fluctuations.**

We have experienced, and may experience in the future, significant fluctuations in our quarterly operating results. The mix of products sold and the acceptance of new products, in addition to other factors, could contribute to this quarterly variability. We operate with relatively little backlog and have few long-term customer contracts. Substantially all of our product revenue in each quarter results from orders received in that quarter. In addition, our expense levels are based, in part, on expectation of future revenue levels. A shortfall in expected revenue could, therefore, result in a disproportionate decrease in our net income.

### **Our success is highly dependent on our ability to obtain protection for the intellectual property utilized in our products.**

Our success and ability to compete depends in part upon our ability to obtain protection in the United States and other countries for our products by establishing and maintaining intellectual property rights relating to or incorporated into our technology and products. Patent applications filed by the Company may not result in the issuance of patents or, if issued, may not be issued in a form that will be commercially advantageous to us. Even if issued, patents may be challenged, narrowed, invalidated or circumvented, which could limit our ability to stop competitors from marketing similar products or limit the length of time of patent protection we may have for our products. We also cannot assure that our nondisclosure agreements, together with trade secrets and other common law rights, will provide meaningful protection for the Company's trade secrets and other proprietary information. Moreover, the laws of some foreign jurisdictions may not protect intellectual property rights to the same extent as in the United States, and many companies have encountered significant difficulties in protecting and defending such rights in foreign jurisdictions. If we encounter such difficulties or we are otherwise precluded from effectively protecting our intellectual property rights domestically or in foreign jurisdictions, we may incur substantial costs and our business, including our business prospects, could be substantially harmed. From time to time, the Company has received notices alleging that the Company's products infringe third party proprietary rights. Whether the manufacture, sale or use of current products, or whether any products under development would, upon commercialization, infringe any patent claim will not be known with certainty unless and until a court interprets the patent claim in the context of litigation. If an infringement allegation is made against us, we may seek to invalidate the asserted patent claim and/or to allege non-infringement of the asserted patent claim. In order for us to invalidate a U.S. patent claim, we would need to rebut the presumption of validity afforded to issued patents in the United States with clear and convincing evidence of invalidity, which is a high burden of proof. The outcome of infringement litigation is

## **Table of Contents**

subject to substantial uncertainties, and also the testimony of experts as to technical facts upon which experts may reasonably disagree. Our defense of an infringement litigation lawsuit could result in significant expense. Regardless of the outcome, infringement litigation could significantly disrupt our marketing, development and commercialization efforts, divert our management's attention and consume our financial resources.

In the event that we are found to infringe any valid claim in a patent held by a third party, we may, among other things, be required to:

pay damages, including up to treble damages and the other party's attorneys' fees, which may be substantial;

cease the development, manufacture, importation, use and sale of products that infringe the patent rights of others, through a court-imposed sanction called an injunction;

expend significant resources to redesign our technology so that it does not infringe others' patent rights, or to develop or acquire non-infringing intellectual property, which may not be possible;

discontinue manufacturing or other processes incorporating infringing technology; and/or

Obtain licenses to the infringed intellectual property, which may not be available to us on acceptable terms, or at all.

Any development or acquisition of non-infringing products or technology or licenses could require the expenditure of substantial time and other resources and could have a material adverse effect on our business and financial results. If we are required to, but cannot, obtain a license to valid patent rights held by a third party, we would likely be prevented from commercializing the relevant product, or from further manufacture, sale or use of the relevant product.

### **We are subject to substantial governmental regulation.**

A portion of our products are regulated by various domestic and foreign government agencies, including the U.S. Department of Agriculture and the U.S. Food and Drug Administration. Although less than 10% of our revenues is currently derived from products requiring government approval prior to sale, a significant portion of our revenues is derived from products used to monitor and detect the presence of residues that are regulated by various government agencies. Furthermore, a significant portion of the Company's growth may be affected by the implementation of new regulations.

### **We are dependent on key employees.**

The Company's success depends, in large part, on its chairman, president and other members of its management team. Our loss of any of these key employees could have a material adverse effect on the Company. The Company maintains certain incentive plans for its key employees, and most of these employees have been with the Company in excess of five years. However, the Company has not executed long-term employment agreements with any of these employees and does not expect to do so in the foreseeable future. The Company's success also depends, significantly, on its ability to continue to attract such personnel. We cannot assure that we will be able to retain our existing personnel or attract additional qualified persons when required and on acceptable terms.

### **Our business may be subject to product liability claims.**

The manufacturing and distribution of the Company's products involve an inherent risk of product liability claims being asserted against us. Regardless of whether we are ultimately determined to be liable or our products are determined to be defective, we might incur significant legal expenses not covered by insurance. In addition, product liability litigation could damage our reputation and impair our ability to market our products, regardless of the outcome. Litigation could also impair our ability to retain product liability insurance or make our insurance more expensive. Although the Company currently maintains liability insurance, we cannot assure that we will be able to continue to obtain such insurance on acceptable terms, or that such insurance



## **Table of Contents**

will provide adequate coverage against all potential claims. If we are subject to an uninsured or inadequately insured product liability claim, our business, financial condition and results of operations could be adversely affected.

### **Market prices for securities of technology companies are highly volatile.**

The market prices for securities of technology companies have been volatile in the past and could continue to be volatile in the future. Fluctuations in our financial performance from period to period could have a significant impact on the market price of our common shares.

## **ITEM 1B. UNRESOLVED STAFF COMMENTS - NONE**

### **ITEM 2. PROPERTIES**

Neogen owns several separate buildings located in Lansing, Michigan. A 26,000 square foot building located at 620 Leshar Place includes senior corporate administrative offices, food safety sales and marketing offices and research facilities. A 12,000 square foot building located at 600 Leshar Place is used for corporate accounting, human resources, and communications functions. Two adjacent buildings, located at 703 and 720 Shiawassee, total 25,000 square feet and are used for manufacture and warehousing of food safety products. Two buildings on Hosmer Street with a combined total of 49,000 square feet, are used for manufacturing and warehousing of dehydrated culture media and veterinary instruments. A 50,000 square foot building at 1614 East Kalamazoo Avenue is used for research and production of vaccines. 17,000 square feet of the Kalamazoo Avenue building is held for expansion.

Animal Safety sales and marketing, diagnostic test kit manufacturing, warehousing and distribution of all other Animal Safety products takes place from an 82,000 square foot Company owned facility at 944 Nandino Drive in Lexington, Kentucky.

Animal Safety pharmaceutical, supplement and topical product manufacturing takes place in 16,000 square feet of leased space at 2040 Creative Drive in Lexington, Kentucky. The lease covering the space is a non-cancelable operating lease through December 31, 2007 currently requiring monthly payments of \$5,700. Upon expiration the company expects to renew the lease on similar terms.

Neogen Europe Ltd. operations take place in 12,948 square feet in the Cunningham Building at Auchincruive Ayrshire Scotland (on the campus of The Scottish Agricultural College at Ayr). The lease agreement on this property expires May 31, 2018, however, Neogen Europe may terminate the lease after 5 years (2008) or 10 years (2013) from inception with a payment of 6 months or 3 months rent, respectively. The current rental rate is £56,700 annually increasing to £63,000 in 2008 (all plus value added tax) as more space is acquired for European operations.

Rodenticide and disinfectant manufacturing and warehousing is conducted in 80,000 square feet of Company owned buildings at 110 Hopkins Drive in Randolph, Wisconsin. Additionally the Company leases 9,000 square feet of warehouse space in Cambria, Wisconsin for \$1,600 per month. The lease expires October 31, 2007.

These properties are in good condition, well-maintained, and generally suitable and adequate to carry on the Company's business.

### **ITEM 3. LEGAL PROCEEDINGS**

Neogen is subject to certain legal proceedings in the normal course of business that, in the opinion of management, will not have a material effect on its future results of operations or financial position.

### **ITEM 4. SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS**

No matters were submitted to a vote of security holders during the fourth quarter of the fiscal year covered by this report.

**Table of Contents****PART II****ITEM 5. MARKET FOR REGISTRANT'S COMMON EQUITY, RELATED STOCKHOLDER MATTERS AND ISSUER PURCHASES OF EQUITY SECURITIES**

## MARKET INFORMATION:

Neogen Common Stock is traded on the NASDAQ Global Select Market under the symbol **NEOG**. The following table sets forth, for the fiscal periods indicated, the high and low sales prices for the Common Stock as reported on the NASDAQ Stock Market.

	<b>HIGH</b>	<b>LOW</b>
<b>YEAR ENDED MAY 31, 2007</b>		
First Quarter	21.00	17.48
Second Quarter	22.09	19.02
Third Quarter	23.60	19.27
Fourth Quarter	27.50	21.20
<b>YEAR ENDED MAY 31, 2006</b>		
First Quarter	17.40	13.50
Second Quarter	20.48	15.35
Third Quarter	23.15	19.75
Fourth Quarter	25.22	18.00

## HOLDERS:

As of July 31, 2007, there were approximately 500 stockholders of record of Common Stock that management believes represents a total of approximately 5,000 beneficial holders.

## DIVIDENDS:

Neogen has never paid any cash dividends on its Common Stock and does not anticipate paying any cash dividends in the foreseeable future.

The graph below matches the cumulative 5-year total return of holders of Neogen Corporation's common stock with the cumulative total returns of the NASDAQ Composite index, the NASDAQ Medical Equipment index and the NASDAQ Non-Financial index. The company will transition from comparing to the NASDAQ Non-Financial to using the NASDAQ Composite and the NASDAQ Medical Equipment going forward. The graph assumes that the value of the investment in the company's common stock, in each index was \$100 on 5/31/2002 and tracks it through 5/31/2007.

**Table of Contents**

	5/02	5/03	5/04	5/05	5/06	5/07
Neogen Corporation	100.00	108.68	129.16	118.15	166.45	223.40
NASDAQ Composite	100.00	98.31	123.42	129.37	141.08	172.42
NASDAQ Non-Financial	100.00	98.21	121.58	124.97	131.10	158.71
NASDAQ Medical Equipment	100.00	98.73	146.07	159.52	169.28	199.58

*The stock price performance included in this graph is not necessarily indicative of future stock price performance.*

**ITEM 6. SELECTED FINANCIAL DATA**

The following tables set forth selected consolidated financial data of Neogen for each of the five fiscal years ended May 31, 2007. The selected consolidated financial data presented below have been derived from the Company's consolidated financial statements. These financial data should be read in conjunction with the consolidated financial statements, related notes and other financial information appearing elsewhere in this Form 10-K.

**Table of Contents**

	Years Ended May 31				
	2003(1)(2)	2004(2)	2005(2)	2006(2)	2007
(In thousands, except share and per share data)					
<b>Income Statement Data:</b>					
Food Safety Sales	\$ 26,476	\$ 27,567	\$ 28,156	\$ 34,951	\$ 46,956
Animal Safety Sales	21,209	27,931	34,600	37,482	39,182
Net Sales	47,685	55,498	62,756	72,433	86,138
Cost of Goods Sold	21,763	27,989	32,153	35,427	41,575
Sales and Marketing	12,077	12,052	13,484	15,799	18,463
General and Administrative	5,265	6,420	6,938	7,414	9,301
Research and Development	2,914	2,893	2,729	2,988	3,295
Operating Income	5,666	6,144	7,452	10,805	13,504
Interest and Other Income	488	132	147	46	371
Income Before Income Taxes	6,154	6,276	7,599	10,851	13,875
Provision for Income Taxes	2,286	2,074	2,670	3,822	4,750
Net Income	\$ 3,868	\$ 4,202	\$ 4,929	\$ 7,029	\$ 9,125
Net Income per Share (basic) (1)(4)	\$ .51	\$ .53	\$ .61	\$ .85	\$ .99
Net Income per Share (diluted) (1)(4)	\$ .50	\$ .51	\$ .59	\$ .83	\$ .97
Common Shares Outstanding (diluted) (1)(4)	7,803	8,233	8,354	8,457	9,441
	2003	2004	May 31 2005	2006	2007
(In thousands)					
<b>Balance Sheet Data:</b>					
Cash and Cash Equivalents	\$ 8,897	\$ 1,696	\$ 1,972	\$ 1,959	\$ 13,424
Working Capital (3)	22,208	20,619	22,644	26,252	41,060
Total Assets	48,036	59,975	63,884	88,290	105,284
Long-Term Debt		3,900		9,955	
Stockholders' Equity	45,408	50,617	56,623	65,424	91,945

- (1) On December 31, 2003, the Company paid a 5-for-4 stock split affected in the form of a dividend of its common stock. All share and per share amounts have been adjusted for all periods to reflect the stock split as if it had taken place at the beginning of the period presented.
- (2) On June 1, 2006 the Company adopted FAS 123R related to options. Financial statements of prior years were restated to conform to the new standards.
- (3) Defined as current assets less current liabilities.
- (4) On July 26, 2007 the Company announced a 3-for-2 stock split effected in the form of a dividend of its common stock. No effect has been given to the subsequent event in this selected financial data information.

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

The information in this Management's Discussion and Analysis of Financial Condition and Results of Operations contains both historical financial information and forward-looking statements. Neogen Corporation management does not provide forecasts of future financial performance. While management is optimistic about the Company's long-term prospects, historical financial information may not be indicative of future financial results.

Any statements contained herein that are not statements of historical fact may be deemed to be forward-looking

## **Table of Contents**

statements. Without limiting the foregoing, the words believes, anticipates, plans, expects, seeks, estimates, and similar expressions are intended to identify forward-looking statements. There are a number of important factors, including competition, recruitment and dependence on key employees, impact of weather on agriculture and food production, identification and integration of acquisitions, research and development risks, patent and trade secret protection, government regulation and other risks detailed from time to time in the Company's reports on file at the Securities and Exchange Commission, that could cause Neogen Corporation's results to differ materially from those indicated by such forward-looking statements, including those detailed in this Management's Discussion and Analysis of Financial Condition and Results of Operations.

In addition, any forward-looking statements represent management's views only as of the day this Report on Form 10-K was first filed with the Securities and Exchange Commission and should not be relied upon as representing management's views as of any subsequent date. While management may elect to update forward-looking statements at some point in the future, it specifically disclaims any obligation to do so, even if its views change.

## **CRITICAL ACCOUNTING POLICIES AND ESTIMATES**

The discussion and analysis of the Company's financial condition and results of operations are based on the consolidated financial statements that have been prepared in accordance with accounting principles generally accepted in the United States. The preparation of these financial statements requires that management make estimates and judgments that affect the reported amounts of assets, liabilities, revenues and expenses, and related disclosure of contingent assets and liabilities. On an ongoing basis, management evaluates the estimates, including those related to receivable allowances, inventories and intangible assets. These estimates are based on historical experience and on various other assumptions that are believed to be reasonable under the circumstances, the results of which form the basis for making judgments about the carrying values of assets and liabilities that are not readily apparent from other sources. Actual results may differ from these estimates under different assumptions or conditions.

The following critical accounting policies reflect management's more significant judgments and estimates used in the preparation of the consolidated financial statements.

### **Revenue Recognition**

Revenue from sales of products is recognized at the time title of goods passes to the buyer and the buyer assumes the risks and rewards of ownership, which is generally at the time of shipment. Where right of return exists, allowances are made at the time of sale to reflect expected returns based on historical experience.

### **Accounts Receivable Allowance**

Management attempts to minimize credit risk by reviewing customers' credit history before extending credit and by monitoring credit exposure on a regular basis. An allowance for possible losses on accounts receivable is established based upon factors surrounding the credit risk of specific customers, historical trends and other information, such as changes in overall changes in customer credit and general credit conditions. Actual collections can differ from historical experience, and if economic or business conditions deteriorate significantly, adjustments to these reserves could be required.

### **Inventory**

A reserve for obsolescence is established based on an analysis of the inventory taking into account the current condition of the asset as well as other known facts and future plans. The amount of reserve required to record inventory at lower of cost or market may be adjusted as conditions change. Product obsolescence may be caused by shelf-life expiration, discontinuance of a product line, replacement products in the marketplace or other competitive situations.

---

## **Table of Contents**

### **Valuation of Intangible Assets and Goodwill**

Management assesses goodwill and other non-amortizable intangible assets for possible impairment on no less often than an annual basis. This test was performed in the fourth quarter of fiscal 2007 and it was determined that no impairment exists. There was also no impairment indicated for 2006 or 2005. In the event of changes in circumstances that indicate the carrying value of these assets may not be recoverable, management will make an assessment at any time. Factors that could cause an impairment review to take place would include:

Significant under performance relative to expected historical or projected future operating results.

Significant changes in the use of acquired assets or strategy of the Company.

Significant negative industry or economic trends.

When management determines that the carrying value of intangible assets may not be recoverable based on the existence of one or more of the above indicators of impairment, the carrying value of the reporting unit's net assets is compared to the projected discounted cash flows of the reporting unit using a discount rate commensurate with the risk inherent in the Company's current business model. If the carrying amounts of these assets are not recoverable based upon a discounted cash flow analysis, such assets are reduced by the estimated shortfall of fair value to recorded value. Changes to the discount rate or projected cash flows used in the analysis can have a significant impact on the results of the impairment test.

### **Stock Options**

At May 31, 2007, the Company had stock option plans, which are described more fully in Note 7. Effective June 1, 2006, the Company adopted the provisions of Financial Accounting Standards Board (FASB) Statement No. 123 (revised), Share-Based Payment. The revised Statement requires companies to measure the cost of employee stock options based on the grant-date fair value and recognize that cost over the period during which a recipient is required to provide services in exchange for the options, typically the vesting period. The Company adopted the provisions of the revised Statement using the modified-retrospective transition method provided in the revised Statement. Under this method, the Company restated all prior periods presented on a consistent basis, based on the pro forma expense previously disclosed.

Prior to the adoption of the revised Statement, the Company presented all of the income tax benefits resulting from the exercise of stock options as cash flows provided by operating activities in the consolidated statements of cash flows. The revised Statement requires the income tax benefit from deductions, resulting from the exercise of stock options, in excess of the compensation cost recognized (excess income tax benefit) to be classified as cash flows provided by financing activities. Excess income tax benefit from exercise of stock options reported as cash flows provided by financing activities for the years ended May 31, 2006 and 2005, respectively, would have been classified as cash flows provided by operating activities if the Company had not adopted the provisions of the revised Statement.

## **RESULTS OF OPERATIONS**

### **Executive Overview**

On an overall basis, the 2007 fiscal year had a 19% revenue increase in comparison with the fiscal year ended May 31, 2006, as a result of revenue increases and operating improvements in both of the Company's operating segments. A portion of the revenue increases came from the Company's December 2005 acquisition of the dairy antibiotic testing business of UCB and from the February 2006 acquisition of Centrus International Inc. Revenue from continuing product sales increased by 9%. This continuing product growth came as a result of the further implementation of sales and marketing plans and continuing recognition of the ease of use and beneficial results from the Company's products. Gross margins increased by 60 basis points to 52% for the year and net income was up 30% to \$9,125,000. These increases resulted principally due to sales gains translating to higher percentage increases in gross margins and net income, changes in product mix, the current year effect of reorganizations completed in past years and continued strong control of costs. Operating expenses remained at 36% in fiscal 2007.

**Table of Contents****REVENUES**

<i>(dollars in thousands)</i>	Increase		Twelve Months Ended		May 31, 2005
	May 31, 2007	(Decrease)	May 31, 2006	(Decrease)	
<b>Food Safety:</b>					
Natural Toxins, Allergens & Drug Residues	\$ 25,090	51%	\$ 16,633	51%	\$ 10,982
Bacterial & General Sanitation	13,250	31%	10,115	2%	9,943
Dry Culture Media & Other	8,616	5%	8,203	13%	7,231
	\$ 46,956	34%	\$ 34,951	24%	\$ 28,156
<b>Animal Safety:</b>					
Life Sciences & Other	\$ 4,863	7%	\$ 4,553	5%	\$ 4,331
Vaccine	2,997	6%	2,837	11%	2,564
Rodenticides & Disinfectants	10,926	3%	10,651	7%	9,941
Veterinary Instruments & Other	20,396	5%	19,441	9%	17,764
	\$ 39,182	5%	\$ 37,482	8%	\$ 34,600
<b>Total Revenues</b>	<b>\$ 86,138</b>	<b>19%</b>	<b>\$ 72,433</b>	<b>15%</b>	<b>\$ 62,756</b>

Within the Food Safety Segment, Natural Toxins, Allergens and Drug Residue sales were up 51% in fiscal year 2007 in comparison with sales in 2006 following a similar 51% increase in the prior year. A significant portion of the gain in this category in both years resulted from sales of products acquired in December 2005. Exclusive of the dairy antibiotic testing products, Natural Toxins and Allergens revenues increased by 16% in comparison with the 2006 fiscal year and 18% in the 2006 fiscal year comparison with the 2005 fiscal year. Increases in diagnostic test kit sales to detect naturally occurring toxins such as aflatoxin continue to be realized due to superior technologies and marketing by the Company. Sales of food allergen test kits to detect the presence of harmful allergens increased in part because of the implementation of new labeling regulations in January 2006. The growth in this area is fueled by public and producer recognition of this food safety threat.

Sales of Bacterial and General Sanitation products, including the sales of products contributed by the acquisition of Centrus International in February 2006, increased by 31% in fiscal year 2007 in comparison with fiscal 2006 and increased by 2% from fiscal year 2005 to 2006. Sales of the AccuPoint ATP general sanitation test continued to gain momentum domestically and internationally throughout fiscal year 2007 and 2006 following a move from an outside supplier of ATP product to a more user friendly and stable internally produced product with improved margins. Sales of diagnostic tests for the detection of bacteria did not increase as much as a result of newer competition and some pricing erosion in the marketplace. The Centrus acquisition added 3% to sales increases of existing products in fiscal year 2007.

Dehydrated culture media and other sales increased by 5% in 2007 and by 13% in 2006 primarily as a result of increased market penetration both domestically and internationally. The Company's focus on customer service and resolution of customer operating problems has resulted in sales increases in each fiscal year.

Within the Animal Safety Segment, sales of life science and other products increased by 7% in fiscal year 2007 in comparison with 2006 and by 5% in 2006 in comparison with the 2005 fiscal year. Sales of forensic drug tests, TMB Substrates and diagnostic research kits each contributed to the sales growth as the Company continues to add business from the existing customer base as well as by adding new customers.

Vaccine product sales increased by 6% in 2007 in comparison with 2006 and by 11% in fiscal 2006 in comparison with 2005, fueled by strong increases in sales in international markets and due to the addition of new channel partners.

**Table of Contents**

Sales of Hacco rodenticides and Hess and Clark disinfectants increased 3% in fiscal year 2007 following a 7% increase in fiscal 2006. Rodenticide revenue increases in 2007 and 2006 are due to increased market penetration with OEM customers and added international sales. In general, mild weather conditions have led to fewer infestations in 2007 and 2006.

Veterinary instruments and other sales increased in 2007 by 5% and increased by 9% in 2006. Fiscal year 2007 increases of 25% in Ideal Instrument veterinary products were broad based but were offset by declines in revenues related to equine supplements, certain wound care and other products. In 2006 increases were driven by 9% increase in sales of veterinary instruments.

**COST OF GOODS SOLD**

<i>(dollars in thousands)</i>	2007	Increase	2006	Increase	2005
Cost of Goods Sold	\$ 41,575	17%	\$ 35,427	10%	\$ 32,153

Cost of goods sold increased by 17% in 2007 and by 10% in 2006 in comparison with the prior year. This compares against a 19% increase in revenues in 2007 and a 15% increase in revenues in 2006. Expressed as a percentage of revenues, cost of goods sold was 48%, 49% and 51% in 2007, 2006, and 2005 respectively. Overall margins in 2005 were affected negatively by costs related to relocation of operating facilities in Chicago and Baltimore to Lansing and Lexington.

Food Safety gross margins were 60%, 59% and 57% in 2007, 2006 and 2005, respectively. Changes in margins between periods relate primarily to changes in product mix. In fiscal 2005, the Company increased overhead costs related to the new diagnostic manufacturing facility and the new ATP product introduction that adversely affected gross margins. Margins in 2005 were also adversely affected by the cost of moving the Company's Acumedia unit and the start up costs of the new facility in Lansing. Food Safety margins sequentially increased during the 2005 fiscal year and more fully during the 2006 and 2007 fiscal years as the effects of efficiencies resulting from investments in manufacturing facilities and the ATP change to manufacture this product internally began to be realized.

Animal Safety gross margins were 41%, 43% and 42% in 2007, 2006 and 2005, respectively. Changes in margins between periods relate primarily to product mix.

**OPERATING EXPENSES**

<i>(dollars in thousands)</i>	2007	Increase (Decrease)	2006	Increase (Decrease)	2005
Sales and Marketing	\$ 18,463	17%	\$ 15,799	17%	\$ 13,484
General and Administrative	9,301	25%	7,414	7%	6,938
Research and Development	3,295	10%	2,988	9%	2,729

Sales and marketing expense categories increased by 17% in both 2007 and 2006 as compared with the prior year. As a percentage of sales, sales and marketing expense was substantially unchanged when the years are compared. Management plans to continue to expand the Company's sales and marketing efforts both domestically and internationally in the future and currently expects related expenses to remain between 20% and 25% expressed as a percentage of sales.

General and administrative expenses increased by 25% in 2007 and by 7% in 2006. These expenses have remained between 10% and 11% over the past three fiscal years. Increases in 2006 resulted primarily from the acquisitions as well as due to increased levels of operations. Increases in 2007 were related to litigation costs surrounding the Company's detectable needle and added amortization related to business acquired. In addition, the increase was due to costs to relocate the Tampa production facility and normal costs related to growth. In general these expenses do not vary as much with sales as compared to many other Company expenses.



**Table of Contents**

Research and development expenses increased by 10% in comparison with 2006 and by 9% in 2006 in comparison with 2005. As a percentage of revenue these expenses were 4% in each the years ended May 31, 2007, 2006 and 2005 respectively. Although some fluctuation in research and development expenses will occur, management expects research and development expenses to approximate 4% to 6% of revenues over time. These expenses approximate 8% to 10% of revenues from products and product lines that are supported by research and development. Certain Company products require relatively less in research and development expenses.

**OPERATING INCOME**

<i>(dollars in thousands)</i>	2007	Increase	2006	Increase	2005
Operating Income	\$ 13,504	25%	\$ 10,805	45%	\$ 7,452

During fiscal year 2007 and 2006, the Company's operating income increased by 25% and 45%. As a percentage of revenues it was 16%, 15% and 12% in 2007, 2006 and 2005 respectively. The Company has been successful in improving its operating income in 2007 and 2006 from the positive effects of restructurings in 2005 and 2004, economies of sales and the effects of new acquisitions.

**OTHER INCOME (NET)**

<i>(dollars in thousands)</i>	2007	Increase (Decrease)	2006	Increase (Decrease)	2005
Other Income Interest and Other (Net)	\$ 371	706%	\$ 46	(69%)	\$ 147

Other income increased by 706% in comparison with 2006 and decreased by 69% in 2006 in comparison with 2005. Interest revenue and expense is a result of the Company's cash versus debt position in the periods. Debt exceeded interest earning assets in fiscal 2005 and 2006. Investment earnings were \$373,000 in fiscal 2007. In 2006 and 2005, the Company recognized grant income of \$250,000 in each year related to a grant from governmental units.

**FEDERAL AND STATE INCOME TAXES**

<i>(dollars in thousands)</i>	2007	Increase	2006	Increase	2005
Federal and State Income Taxes	\$ 4,750	24%	\$ 3,822	43%	\$ 2,670

Federal and state income tax rates used in the computation of income tax expense in the periods remained comparable to those in the prior year. Expressed as a percentage of income before tax, such rates were 34%, in 2007 and 35% in 2006 and 2005. In major part, the change in percentage taxes paid resulted from changes in profitability of individual operating units and state tax credits awarded and recognized in any given year.

**NET INCOME AND NET INCOME PER SHARE**

<i>(dollars in thousands-except per share data)</i>	2007	Increase	2006	Increase	2005
Net Income	\$ 9,125	30%	\$ 7,029	43%	\$ 4,929
Net Income Per Share-Basic	.99		\$ .85		\$ .61
Net Income Per Share-Diluted	.97		\$ .83		\$ .59

Net income and net income per share increased by 30% in 2007 and 43% in 2006 in comparison with the prior year. As a percentage of revenue, net income was 11%, 10% and 8% in 2007, 2006 and 2005 respectively.

**FUTURE OPERATING RESULTS**

Neogen Corporation's future operating results involve a number of risks and uncertainties. Actual events or results may differ materially from those discussed in this report. Factors that could cause or contribute to such differences include, but are not limited to, the factors discussed below as well as those discussed elsewhere in this report. Management's ability to grow the business in the future depends upon its ability to

successfully implement various strategies, including:

developing, manufacturing and marketing new products with new features and capabilities;

**Table of Contents**

expanding the Company's markets by fostering increased use of Company products by customers;

strengthening sales and marketing activities in geographies outside of the U.S.;

developing and implementing new technology development strategies; and

identifying and completing acquisitions that enhance existing businesses or create new business areas.

**FINANCIAL CONDITION AND LIQUIDITY**

On May 31, 2007, the Company had \$13,424,000 in cash and cash equivalents, working capital of \$41,060,000 and stockholders' equity of \$91,945,000. In addition to cash and security balances, a bank line with unused borrowings of \$10,000,000 was available if necessary to, support ongoing operations or to make acquisitions.

Cash and cash equivalents increased \$11,465,000 during 2007. Cash provided from operations was \$10,158,000 and stock sales provided an additional \$15,736,000 of cash. Additions to property and equipment and other non-current assets used cash of \$4,704,000 and the repayment of bank debt used \$9,955,000.

Accounts receivable increased \$1,798,000 or 14% when compared to May 31, 2006. This resulted from increased sales. Days sales outstanding decreased from 56 days at May 31, 2006 to 54 days at May 31, 2007.

Inventory levels increased 8% or \$1,490,000 in 2007 as compared to 2006. The Company maintains sufficient levels of inventory to assure that customer demands can be met on a timely basis. Increases are proportionate with increases in sales.

Acquisitions of long-lived assets totaled \$4,704,000 and resulted from purchases and renovations of new manufacturing facilities and equipment for the Food Safety segment and other expenditures during the year.

On June 2, 2006, the Company announced that it had completed an offering of 800,000 shares of common stock, of which 650,000 were sold by the Company and 150,000 were sold by two members of management, for an aggregate purchase price of approximately \$16.0 million. The net proceeds of the offering to the Company were approximately \$12.2 million after deducting the placement agency fees and offering expenses that were payable by the Company. The Company did not receive any proceeds from the sale of the shares by the Selling Stockholders. Proceeds were used to repay the Company's borrowings and add to working capital.

**CONTRACTUAL OBLIGATIONS**

The Company has the following contractual obligations due by period:

<i>(in thousands)</i>	<b>Total</b>	<b>Less than one year</b>	<b>1-3 years</b>	<b>3-5 years</b>	<b>More than 5 years</b>
Long-Term Debt	\$	\$	\$	\$	\$
Operating Leases	518,000	288,000	230,000		
Unconditional Purchase Obligations	8,291,000	8,291,000			
	\$ 8,809,000	\$ 8,579,000	\$ 230,000	\$	\$

Neogen has been profitable from operations for its last 57 quarters and has generated positive cash flow from operations during the period. However, the Company's current funds may not be sufficient to meet the Company's cash requirements to commercialize products currently under development or its plans to acquire additional technology and products that fit within the Company's mission statement. Accordingly, the Company may be required to or may choose to issue equity securities or enter into other financing arrangements for a portion of the Company's future capital needs.

## **Table of Contents**

The Company is subject to certain legal and other proceedings in the normal course of business that, in the opinion of management, will not have a material effect on its results of operations or financial position.

### **NEW ACCOUNTING PRONOUNCEMENTS**

See discussion of any New Accounting Pronouncements in Note 1 to Consolidated Financial Statements.

### **ITEM 7A. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISKS**

The Company has moderate interest rate and foreign exchange rate risk exposure and no long-term fixed rate investments or borrowings. The Company's primary interest rate risk is due to potential fluctuations of interest rates for variable rate borrowings.

Because Neogen markets and sells its products throughout the world, it could be affected by weak economic conditions in foreign markets that could reduce the demand for its products. Sales in certain foreign countries as well as certain expenses related to those sales are transacted in currencies other than the U.S. dollar. The Company's operating results are primarily exposed to changes in exchange rates between the U.S. dollar and the British Pound and Euro. When the U.S. dollar weakens against foreign currencies, the dollar value of sales denominated in foreign currencies increases. When the U.S. dollar strengthens, the opposite situation occurs.

Neogen has asset, liabilities and operations outside of the United States that are located primarily in Ayr, Scotland where the functional currency is the British Pound. The Company's investment in its foreign subsidiary is considered long-term; accordingly, it does not hedge the net investment or engage in other foreign currency hedging activities due to the insignificance of these balances to the Company as a whole.

### **ITEM 8. FINANCIAL STATEMENTS AND SUPPLEMENTAL DATA**

The response to this item is submitted in a separate section of this report.

### **ITEM 9. CHANGES IN AND DISAGREEMENTS WITH ACCOUNTANTS ON ACCOUNTING AND FINANCIAL DISCLOSURE**

There were no disagreements or reportable events with Ernst & Young LLP.

### **ITEM 9A. CONTROLS AND PROCEDURES**

**Evaluation of Disclosure Controls and Procedures** - An evaluation of the effectiveness of the design and operation of the Company's disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) as of May 31, 2007 was carried out under the supervision and with the participation of the Company's management, including the Chief Executive Officer and Chief Financial Officer (the Certifying Officers). Based on that evaluation, the Certifying Officers concluded that the Company's disclosure controls and procedures are effective to bring to the attention of the Company's management the relevant information necessary to permit an assessment of the need to disclose material developments and risks pertaining to the Company's business in its periodic filings with the Securities and Exchange Commission. There was no change to the Company's internal control over financial reporting during the year ended May 31, 2007 that materially affected, or is reasonably likely to materially affect, the Company's internal control over financial reporting.

**Management's Report on Internal Control Over Financial Reporting** - The management of Neogen Corporation is responsible for establishing and maintaining adequate internal control over financial reporting, as such term is defined in Exchange Act Rules 13a-15(f). Neogen Corporation's internal control system was designed to provide reasonable assurance to the Company's management and Board of Directors regarding the preparation and fair presentation of published financial statements.

Neogen Corporation's management assessed the effectiveness of the Company's internal control over financial reporting as of May 31, 2007 under the supervision and with the participation of the Chief Executive

---

**Table of Contents**

Officer and the Chief Financial Officer. In making this assessment, it used the criteria set forth by the Committee of Sponsoring Organizations of the Treadway Commission in Internal Control-Integrated Framework. Based on that assessment, management believes that, as of May 31, 2007 the Company's internal control over financial reporting is effective.

Neogen Corporation's independent registered public accounting firm, Ernst & Young LLP, has issued an attestation report on management's assessment of the Company's internal control over financial reporting. This report appears below.

**Report of Independent Registered Public Accounting Firm on Internal Control over Financial Reporting**

The Board of Directors and Stockholders of Neogen Corporation

We have audited management's assessment, included in the accompanying Management's Report on Internal Control over Financial Reporting, that Neogen Corporation and subsidiaries (the Company) maintained effective internal control over financial reporting as of May 31, 2007, based on criteria established in Internal Control - Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (the COSO criteria). The Company's management is responsible for maintaining effective internal control over financial reporting and for its assessment of the effectiveness of internal control over financial reporting. Our responsibility is to express an opinion on management's assessment and an opinion on the effectiveness of the Company's internal control over financial reporting based on our audit.

We conducted our audit in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether effective internal control over financial reporting was maintained in all material respects. Our audit included obtaining an understanding of internal control over financial reporting, evaluating management's assessment, testing and evaluating the design and operating effectiveness of internal control, and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion.

A company's internal control over financial reporting is a process designed 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. A company's internal control over financial reporting includes those policies and procedures that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (2) 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 company are being made only in accordance with authorizations of management and directors of the company; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company's assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

In our opinion, management's assessment that Neogen Corporation and subsidiaries maintained effective internal control over financial reporting as of May 31, 2007, is fairly stated, in all material respects, based on the COSO criteria. Also, in our opinion, the Company maintained, in all material respects, effective internal control over financial reporting as of May 31, 2007, based on the COSO criteria.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the fiscal 2007 consolidated financial statements of Neogen Corporation and subsidiaries and our report dated August 1, 2007 expressed an unqualified opinion thereon.

/s/ Ernst & Young LLP

Grand Rapids, Michigan

August 1, 2007

**ITEM 9B. OTHER INFORMATION NONE**

**Table of Contents****PART III****ITEM 10. DIRECTORS AND EXECUTIVE OFFICERS OF THE REGISTRANT**

Information regarding the Company and certain corporate governance matters appearing under the captions Election of Directors, Audit Committee, and Miscellaneous-Section 16(a) Beneficial Ownership Reporting Compliance in the 2007 proxy statement is included herein by reference.

The Company has adopted a Code of Conduct that applies to all of its directors, officers and employees. The Company has made a copy of this Code of Conduct available on its Website at [http://www.neogen.com/pdf/Code\\_of\\_Conduct.pdf](http://www.neogen.com/pdf/Code_of_Conduct.pdf).

**OFFICERS AND OTHER KEY INDIVIDUALS OF THE REGISTRANT**

The officers of Neogen are elected by and serve at the discretion of the Board of Directors. The Board of Directors has also named a Scientific Review Council to serve at the pleasure of the Board. The Scientific Review Council meets several times annually to review the research progress of the Company and to recommend or approve new research and product development activities of the Company. The names and occupations of the Company's officers are set forth below.

<b>Name</b>	<b>Position with the Company</b>	<b>Year Joined the Company</b>
Lon M. Bohannon	President & Chief Operating Officer, Director	1985
Edward L. Bradley	Vice President, Food Safety	1995
Richard R. Current	Vice President & Chief Financial Officer and Secretary	1999
James L. Herbert	Chairman of the Board & Chief Executive Officer	1982
Kenneth V. Kodilla	Vice President, Manufacturing	2003
Joseph M. Madden, Ph.D.	Vice President, Scientific Affairs	1997
Anthony E. Maltese	Vice President, Corporate Development	1999
Terri A. Morrical	Vice President, Animal Safety	1992
Mark A. Mozola, Ph.D.	Vice President, Research & Development	2001
Paul S. Satoh, Ph.D.	Vice President, Basic and Exploratory Research	1998

There are no family relationships among officers. Information concerning the executive officers of Neogen follows:

Lon M. Bohannon, age 54, joined the Company in October 1985 as Vice President of Finance, was promoted to Chief Financial Officer in June 1987, was promoted to Vice President Administration and Chief Financial Officer in November 1994, was elected to the Board of Directors in October 1996, and was named Chief Operating Officer in September 1999. Mr. Bohannon was named President and Chief Operating Officer in June 2006. He is responsible for all Company operations except research, Neogen Europe and corporate development. A CPA, he was Administrative Controller for Federal Forge, Inc., a metal forging and stamping firm, from March 1980 until October 1985, and was associated with the public accounting firm of Ernst & Young LLP from June 1975 to March 1980.

Edward L. Bradley, age 47, joined Neogen in February 1995 as Vice President of Sales and Marketing for AMPCOR Diagnostics, Inc. In June 1996, he was made a Vice President of Neogen Corporation. In June 2006, Mr. Bradley was named Vice President Food Safety. From 1988 to 1995, Mr. Bradley served in several sales and marketing capacities for Mallinckrodt Animal Health, including the position of National Sales Manager responsible for 40 employees in its Food Animal Products Division. Prior to joining Mallinckrodt, he held several sales and marketing positions for Stauffer Chemical Company.

Richard R. Current, age 63, joined the Company in November 1999 as Vice President and Chief Financial Officer. In 2007 he was appointed as Secretary of the Company. Prior to joining Neogen, Mr. Current served as Executive Vice President and Chief Financial Officer of Integral Vision, Inc. from 1994 to 1999 and as Vice President and Chief Financial Officer of the Shane Group, Inc., a privately held company from 1991 to 1994. Mr. Current was associated with the public accounting firm of Ernst & Young LLP for 24 years and served as Managing Partner of the Lansing, Michigan office from 1986 to 1991.

## **Table of Contents**

James L. Herbert, age 67, has been Chief Executive Officer and a director of the Company since he joined Neogen in June 1982. He served as President from June 1982 through June 2006. From 1999 to 2001 he was Chairman of the Company's Board; and was again named Chairman in June 2006. He previously held the position of Corporate Vice President of DeKalb Ag Research, a major agricultural genetics and energy company. He has management experience in animal biologics, specialized chemical research, medical instruments, aquaculture, animal nutrition, and poultry and livestock breeding and production.

Kenneth V. Kodilla, age 50, joined the Company in November 2003 as Vice President of Manufacturing. He has responsibility for all manufacturing, inventory management, shipping and quality system operations for the Company's Food Safety Division in Lansing, Michigan. Prior to Neogen, Mr. Kodilla served as plant manager for Facet Technologies in Atlanta, Georgia from 2001, as Manufacturing Manager for Becton Dickinson and Difco Laboratories from 1988, and as Quality Manager for Lee Laboratories from 1984. Mr. Kodilla's manufacturing and regulatory experience includes FDA/ISO regulated Class II and III diagnostic reagents and devices, high volume automated assembly and packaging, materials management and plant operations.

Dr. Joseph M. Madden, age 58, joined Neogen in December 1997 as Vice President of Scientific Affairs after retiring from the Food and Drug Administration as its Microbiology Strategic Manager. He joined the FDA in 1978 and spent his first 10 years as a research microbiologist for the agency. Dr. Madden has served on numerous committees on food safety, including his current appointment to the National Advisory Committee on Microbiological Criteria for Foods. He is regarded by regulatory agencies and the food industry as being one of the nation's top experts on both scientific and regulatory issues relating to food safety.

Anthony E. Maltese, age 63, joined Neogen on June 1, 1999 as Manager of Corporate Development. He was promoted to Vice President in October 2000. Prior to joining Neogen, Mr. Maltese served as Vice President of Business Development for Creatogen Biosciences, GmbH of Angsburg, Germany. From 1990 to 1998, he worked in production and special project management positions for REMEL, Inc. including Manager of Business Development. Prior to REMEL, Mr. Maltese spent 20 years at Difco Laboratories, where he served in several management positions in the areas of purchasing, technical sales support, production and research.

Terri A. Morrical, age 42, joined Neogen Corporation on September 1, 1992 as part of the Company's acquisition of WTT, Incorporated. In June 2006, Ms. Morrical was named Vice President, Animal Safety. From 1986 to 1991, she was Controller for Freeze Point Cold Storage Systems and concurrently served in the same capacity for Powercore, Inc. In 1990, she joined WTT, Incorporated as VP/CFO and then became President, the position she held at the time Neogen acquired the business.

Dr. Mark A. Mozola, age 52, became Neogen's Vice President of Research and Development in 2001 following the Company's acquisition of GENE-TRAK Systems. He served in various technical and managerial positions at GENE-TRAK Systems for 16 years, most recently as General Manager. He has also served as a Laboratory Director for Silliker Laboratories. Dr. Mozola's particular technical expertise is in the area of development of modern, rapid methods for the detection of foodborne pathogens.

Dr. Paul S. Satoh, age 70, became Neogen's Vice President for Research and Development in March 1998 after having spent 26 years as a senior scientist, specialist in information analysis and competitive intelligence and research manager in the Diagnostic Group at Pharmacia & Upjohn Inc. He joined Neogen after serving nearly six years on Neogen's Scientific Review Council as an immunology specialist. Dr. Satoh also taught immunopharmacology at the University of Michigan in Ann Arbor while on sabbatical leave from the Upjohn Company. He is an adjunct professor at the National Food Safety and Toxicology Center at Michigan State University since 1998. He has been Vice President for Basic and Exploratory Research since September 2001.

## **ITEM 11. EXECUTIVE COMPENSATION**

The information required by this Item is incorporated by reference to Neogen's Proxy Statement to be filed within 120 days of May 31, 2007.

**Table of Contents**

**ITEM 12. SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS, MANAGEMENT AND RELATED STOCKHOLDER MATTERS**

The information required by this Item is incorporated by reference to Neogen's Proxy Statement to be filed within 120 days of May 31, 2007.

**ITEM 13. CERTAIN RELATIONSHIPS, RELATED TRANSACTIONS AND DIRECTOR INDEPENDENCE**

Jack C. Parnell, a Director of the Company, is a governmental relations advisor to the law firm of Kahn, Soares & Conway. Kahn, Soares & Conway has been retained by Neogen to represent it in governmental relations matters. The Company pays Kahn, Soares & Conway a monthly fee of \$750 effective August 1, 2007 for ten hours of consulting. The agreement with Kahn, Soares & Conway is terminable by either party at the end of any month.

**ITEM 14. PRINCIPAL ACCOUNTANT FEES AND SERVICES**

During the year ended May 31, 2007 and 2006, Ernst & Young billed Neogen for its services as follows:

**Audit Fees:** Fees for audit services totaled \$239,000 in 2007 and \$411,000 in 2006 including fees incurred for the annual audit of the Company's consolidated financial statements, internal control over financial reporting, interim reviews of quarterly financial information, audit procedures related to acquisitions Form S-3 filings, and consultations concerning accounting matters associated with the acquisitions and annual audit.

**Audit-Related Fees:** Fees for audit-related services totaled \$0 in 2007 and 2006. Audit related fees consist of services associated with accounting consultations that were not related to the annual audit.

**Tax Fees:** Fees associated with tax matters were incurred with the principal auditing firm in the amount of \$12,000 and \$0 in 2007 and 2006, respectively.

**All Other Fees:** There were no other fees incurred with the principal auditing firm in 2007 or 2006.



**Table of Contents**

**PART IV**

**ITEM 15. EXHIBITS, FINANCIAL STATEMENT SCHEDULE**

(a) (1) and (2) and (c). The response to this portion of ITEM 15 is submitted as a separate section of this report.

(a) (3). The Exhibits listed on the accompanying Exhibits Index, which immediately follows the signature page, is incorporated herein by reference.

**Table of Contents**

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.

NEOGEN CORPORATION

/s/ James L. Herbert  
James L. Herbert, Chairman &  
Chief Executive Officer

/s/ Richard R. Current  
Richard R. Current, Vice President &  
Chief Financial Officer & Secretary

Dated: August 14, 2007

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

<b>Signature</b>	<b>Title</b>	<b>Date</b>
/s/ James L. Herbert James L. Herbert	Chairman of the Board of Directors & Chief Executive Officer,  (Principal Executive Officer)	August 14, 2007
/s/ Lon M. Bohannon Lon M. Bohannon	President & Chief Operating  Officer	August 14, 2007
* Robert M. Book	Director	
A. Charles Fischer	Director	
* Gordon E. Guyer, Ph.D.	Director	
* G. Bruce Papesh	Director	
* Jack C. Parnell	Director	
* Thomas H. Reed	Director	
* Clayton K Yeutter, Ph.D.	Director	

\*By: /s/ James L. Herbert  
James L. Herbert, Attorney-in-fact

August 14, 2007

---

**Table of Contents**

Neogen Corporation

Annual Report on Form 10-K

Year Ended May 31, 2007

**EXHIBIT INDEX**

<b>EXHIBIT NO.</b>	<b>DESCRIPTION</b>
4.1	Articles of Incorporation, as restated (Incorporated by reference to Exhibit 3.1 to the Registrant's Quarterly Report on Form 10-Q dated February 29, 2000).
4.2	By-Laws, as amended (Incorporated by reference to Exhibit 3.2 to the Registrant's Quarterly Report on Form 10-Q dated February 29, 2000).
10.1	Neogen Corporation/United States Department of Agriculture License Agreement dated June 29, 1994 (Incorporated by reference to Exhibit 10(f) to the Registrant's Registration Statement on Form S-2 (No. 333-12193) filed September 17, 1996 and amended on October 18, 1996, which Registration became effective October 22, 1996).
10.2	Loan Agreement between Registrant and LaSalle Bank dated December 16, 2005 (Incorporated by reference to Exhibit 10.AC to the Registrant's Current Report on Form 8-K dated December 16, 2005).
10.3	Amendment to LaSalle Bank Agreement Dated April 25, 2007
10.5	Neogen Corporation 2002 Employee Stock Purchase Plan Agreement (Incorporated by reference to Exhibit 99.1 to the Registrant's Registration Statement on Form S-8 (No. 333-101638) filed December 4, 2002).
10.6	Neogen Corporation 401(k) Retirement Savings Plan Agreement (Incorporated by reference to Exhibit 99.1 to the Registrant's Registration Statement on Form S-8 (No. 333-101639) filed December 4, 2002).
10.7	Neogen Corporation Stock Option Plan, as amended (Incorporated by reference to Exhibit 4.3 to the Registration Statement on Form S-8 (No. 333-122110) filed January 18, 2005).
10.8	Sale and purchase agreement between Registrant and UCB S.A. dated July 1, 2005, related to agreement to purchase of UCB's food diagnostic business (Incorporated by reference to Exhibit 10.(H) to the Registrant's Annual Report on Form 10-K filed August 15, 2005).
21	Subsidiaries of the Registrant.
23(a)	Consent of Independent Registered Public Accounting Firm Ernst & Young LLP.
24.2	Power of Attorney.
31.1	Section 302 Certification of Principal Executive Officer.
31.2	Section 302 Certification of Principal Financial Officer.
32	Certification Pursuant to 18 U.S.C Section 1350, as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

**Table of Contents**

ANNUAL REPORT ON FORM 10-K

ITEM 15 (a)(1)(2) (3) (a) and (c)

LIST OF FINANCIAL STATEMENTS, EXHIBITS AND FINANCIAL STATEMENT SCHEDULE

YEAR ENDED MAY 31, 2007

NEOGEN CORPORATION

LANSING, MICHIGAN

FORM 10-K ITEM 15(a)(1) AND (2)

LIST OF FINANCIAL STATEMENTS AND FINANCIAL STATEMENT SCHEDULES

The following consolidated financial statements of Neogen Corporation and subsidiaries are included in ITEM 8:

Report of Independent Registered Public Accounting Firm on Financial Statements

Consolidated Balance Sheets May 31, 2007 and 2006

Consolidated Statements of Income Years ended May 31, 2007, 2006 and 2005

Consolidated Statements of Stockholders Equity Years ended May 31, 2007, 2006 and 2005

Consolidated Statements of Cash Flows Years ended May 31, 2007, 2006 and 2005

Notes to Consolidated Financial Statements

The following consolidated financial statement schedule of Neogen Corporation and subsidiaries is included in Item 15(a) (2) and 15 (c)

Schedule II Valuation and qualifying accounts and reserves

All other schedules for which provision is made in the applicable accounting regulation of the United States Securities and Exchange Commission are not required under the related instructions or are inapplicable and, therefore, have been omitted.

FORM 10-K Item 15 (a) (3)

A list of Exhibits required to be filed as a part of this report is set forth in the Exhibit Index, which immediately follows the signature page, and is incorporated herein by reference.

**Table of Contents**

Report of Independent Registered Public Accounting Firm on Financial Statements

The Board of Directors and Stockholders of Neogen Corporation

We have audited the accompanying consolidated balance sheets of Neogen Corporation (the Company) and subsidiaries as of May 31, 2007 and 2006, and the related consolidated statements of income, stockholders' equity, and cash flows for each of the three years in the period ended May 31, 2007. Our audits also included the financial statement schedule listed in the Index at Item 15(a). These financial statements and schedule are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements and schedule based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes 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 financial statements referred to above present fairly, in all material respects, the consolidated financial position of Neogen Corporation and subsidiaries at May 31, 2007 and 2006, and the consolidated results of their operations and their cash flows for each of the three years in the period ended May 31, 2007, in conformity with U.S. generally accepted accounting principles. Also, in our opinion, the related financial statement schedule, when considered in relation to the basic financial statements taken as a whole, presents fairly in all material respects the information set forth therein.

As discussed in note 1, the Company adopted Financial Accounting Standards Board statement No. 123 (R), Share-Based Payment following the modified retrospective method. As a result, prior year financial statements have been restated.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the effectiveness of Neogen Corporation's internal control over financial reporting as of May 31, 2007, based on criteria established in Internal Control-Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission and our report dated August 1, 2007 expressed an unqualified opinion thereon.

/s/ Ernst & Young LLP

Grand Rapids, Michigan

August 1, 2007

**Table of Contents****Neogen Corporation and Subsidiaries****Consolidated Balance Sheets**

	2007	May 31, 2006 (Restated)
<b>Assets</b>		
<b>Current Assets</b>		
Cash and cash equivalents	\$ 13,424,000	\$ 1,959,000
Accounts receivable, less allowance of \$500,000 and \$530,000	14,914,000	13,116,000
Inventories	19,116,000	17,626,000
Deferred income taxes	787,000	1,264,000
Prepaid expenses and other current assets	2,857,000	2,304,000
<b>Total Current Assets</b>	<b>51,098,000</b>	<b>36,269,000</b>
<b>Property and Equipment</b>		
Land and improvements	1,057,000	970,000
Buildings and improvements	10,196,000	9,403,000
Machinery and equipment	14,000,000	11,159,000
Furniture and fixtures	745,000	606,000
	25,998,000	22,138,000
Less accumulated depreciation	(9,596,000)	(7,883,000)
<b>Net Property and Equipment</b>	<b>16,402,000</b>	<b>14,255,000</b>
<b>Other Assets</b>		
Goodwill	24,448,000	28,937,000
Other non-amortizable intangible assets	3,181,000	2,076,000
Customer based intangibles, net of accumulated amortization of \$1,215,000 and \$639,000	6,182,000	5,049,000
Other non-current assets, net of accumulated amortization of \$1,290,000 and \$924,000	3,973,000	1,704,000
<b>Total Other Assets</b>	<b>37,784,000</b>	<b>37,766,000</b>
	<b>\$ 105,284,000</b>	<b>\$ 88,290,000</b>

See accompanying notes to consolidated financial statements.

**Table of Contents****Neogen Corporation and Subsidiaries****Consolidated Balance Sheets**

	May 31, 2007	2006 (Restated)
<b>Liabilities and Stockholders Equity</b>		
Current Liabilities		
Accounts payable	\$ 4,507,000	\$ 2,832,000
Accruals		
Compensation and benefits	1,737,000	1,642,000
Federal income taxes	1,377,000	876,000
Other	2,417,000	4,667,000
<b>Total Current Liabilities</b>	<b>10,038,000</b>	<b>10,017,000</b>
Long-Term Debt		9,955,000
Deferred Income Taxes	1,441,000	1,105,000
Other Long-Term Liabilities	1,860,000	1,789,000
<b>Total Liabilities</b>	<b>13,339,000</b>	<b>22,866,000</b>
<b>Stockholders Equity</b>		
Preferred stock, \$1.00 par value - shares authorized 100,000; none issued and outstanding		
Common stock, \$0.16 par value - shares authorized 20,000,000; 9,347,204 and 8,310,624 shares issued and outstanding	1,496,000	1,330,000
Additional paid-in capital	52,446,000	35,517,000
Accumulated other comprehensive income	386,000	85,000
Retained earnings	37,617,000	28,492,000
<b>Total Stockholders Equity</b>	<b>91,945,000</b>	<b>65,424,000</b>
	<b>\$ 105,284,000</b>	<b>\$ 88,290,000</b>

See accompanying notes to consolidated financial statements.

**Table of Contents****Neogen Corporation and Subsidiaries****Consolidated Statements of Income**

	2007	Year Ended May 31 2006 (Restated)	2005
Net Sales	\$ 86,138,000	\$ 72,433,000	\$ 62,756,000
Cost of Goods Sold	41,575,000	35,427,000	32,153,000
Gross Margin	44,563,000	37,006,000	30,603,000
Operating Expenses			
Sales and marketing	18,463,000	15,799,000	13,484,000
General and administrative	9,301,000	7,414,000	6,938,000
Research and development	3,295,000	2,988,000	2,729,000
	31,059,000	26,201,000	23,151,000
Operating Income	13,504,000	10,805,000	7,452,000
Other Income (Expense)			
Interest income	373,000	80,000	7,000
Interest expense	(15,000)	(283,000)	(83,000)
Grant income and other	13,000	249,000	223,000
	371,000	46,000	147,000
Income Before Income Taxes	13,875,000	10,851,000	7,599,000
Income Taxes	4,750,000	3,822,000	2,670,000
Net Income	\$ 9,125,000	\$ 7,029,000	\$ 4,929,000
Net Income Per Share			
Basic	\$ .99	\$ .85	\$ .61
Diluted	\$ .97	\$ .83	\$ .59

See accompanying notes to consolidated financial statements.



**Table of Contents****Neogen Corporation and Subsidiaries****Notes to Consolidated Financial Statements**

	Common Stock		Additional	Other	Retained	Total
	Shares	Amount	Paid-in	Income(1)	Earnings	Stockholders
			Capital			Equity
Balance, June 1, 2004, as Restated	8,010,222	\$ 1,282,000	\$ 32,702,000	\$ 99,000	\$ 16,534,000	\$ 50,617,000
Exercise of options and warrants, net of share based compensation, including \$330,000 income tax benefit	149,816	24,000	1,117,000			1,141,000
Issuance of warrants			55,000			55,000
Issuance of shares under Employee Stock Purchase Plan	6,895	1,000	100,000			101,000
Repurchase of common stock	(19,922)	(3,000)	(254,000)			(257,000)
Comprehensive income:						
Net income for 2005 (restated)					4,929,000	4,929,000
Foreign currency translation adjustments				37,000		37,000
<b>Total comprehensive income</b>						<b>5,953,000</b>
Balance, May 31, 2005	8,147,011	1,304,000	33,720,000	136,000	21,463,000	56,623,000
Exercise of options and warrants, net of share based compensation, including \$328,000 income tax benefit	154,786	25,000	1,626,000			1,651,000
Issuance of warrants			51,000			51,000
Issuance of shares under Employee Stock Purchase Plan	10,865	2,000	148,000			150,000
Repurchase of common stock	(2,038)	(1,000)	(28,000)			(29,000)
Comprehensive income:						
Net income for 2006 (restated)					7,029,000	7,029,000
Foreign currency translation adjustments				(51,000)		(51,000)
<b>Total comprehensive income</b>						<b>7,890,000</b>
Balance, May 31, 2006	8,310,624	1,330,000	35,517,000	85,000	28,492,000	65,424,000
Issuance of Common Stock	650,000	104,000	12,890,000			12,994,000
Exercise of options and warrants, net of share based compensation, including \$460,000 income tax benefit	377,057	60,000	3,789,000			3,849,000
Issuance of warrants			66,000			66,000
Issuance of shares under Employee Stock Purchase Plan	9,523	2,000	184,000			186,000
Comprehensive income:						
Net income for 2007					9,125,000	9,125,000
Foreign currency translation adjustments				301,000		301,000
<b>Total comprehensive income</b>						<b>9,426,000</b>
Balance, May 31, 2007	9,347,204	\$ 1,496,000	\$ 52,446,000	\$ 386,000	\$ 37,617,000	\$ 91,945,000

---

(1) Other represents accumulated other comprehensive income

See accompanying notes to consolidated financial statements.

-F4-

**Table of Contents****Neogen Corporation and Subsidiaries****Notes to Consolidated Financial Statements**

	2007	Year Ended May 31 2006 (Restated)	2005
<b>Cash Flows From Operating Activities</b>			
Net income	\$ 9,125,000	\$ 7,029,000	\$ 4,929,000
Adjustments to reconcile net income to net cash provided from operating activities:			
Depreciation and amortization	2,840,000	2,417,000	1,703,000
Deferred income taxes	813,000	485,000	309,000
Share based compensation	1,293,000	1,240,000	1,317,000
Excess income tax benefit from the exercise of stock options	(460,000)	(328,000)	(330,000)
Other	367,000		92,000
Changes in operating assets and liabilities, net of business acquisitions:			
Accounts receivable	(1,798,000)	(1,346,000)	(545,000)
Inventories	(1,490,000)	(671,000)	(1,331,000)
Prepaid expenses and other current assets	(553,000)	(930,000)	256,000
Accounts payable	1,675,000	90,000	(715,000)
Accruals and other changes	(1,654,000)	3,573,000	855,000
<b>Net Cash From Operating Activities</b>	<b>10,158,000</b>	<b>11,559,000</b>	<b>6,540,000</b>
<b>Cash Flows Used In Investing Activities</b>			
Purchases of property, equipment and other noncurrent assets	(4,704,000)	(2,692,000)	(2,688,000)
Business and product line acquisitions, net of cash acquired		(20,658,000)	(874,000)
<b>Net Cash Used In Investing Activities</b>	<b>(4,704,000)</b>	<b>(23,350,000)</b>	<b>(3,562,000)</b>
<b>Cash Flows From (Used In) Financing Activities</b>			
Net proceeds from issuance of common stock	12,994,000		
Exercise of options	2,441,000	1,524,000	875,000
Repurchase of common stock		(29,000)	(257,000)
Proceeds from long-term debt		14,640,000	
Payments on long-term debt	(9,955,000)	(4,685,000)	(3,900,000)
Excess income tax benefit from the exercise of stock options	460,000	328,000	330,000
Increase in other long-term liabilities	71,000		250,000
<b>Net Cash From (Used In) Financing Activities</b>	<b>6,011,000</b>	<b>11,778,000</b>	<b>(2,702,000)</b>
<b>Net Increase (Decrease) In Cash</b>	<b>11,465,000</b>	<b>(13,000)</b>	<b>276,000</b>
<b>Cash and cash equivalents at beginning of year</b>	<b>1,959,000</b>	<b>1,972,000</b>	<b>1,696,000</b>
<b>Cash and cash equivalents at end of year</b>	<b>\$ 13,424,000</b>	<b>\$ 1,959,000</b>	<b>\$ 1,972,000</b>
<b>Supplemental Cash Flow Information</b>			
Income taxes paid, net of refunds	\$ 3,295,000	\$ 1,194,000	\$ 2,249,000
Interest paid	\$ 15,000	\$ 283,000	\$ 53,000

See accompanying notes to consolidated financial statements.

## **Table of Contents**

### **Neogen Corporation and Subsidiaries**

#### **Notes to Consolidated Financial Statements**

##### **1. Summary of Accounting Policies Nature of Operations**

Neogen Corporation develops, manufactures, and sells a diverse line of products dedicated to food safety testing and animal health applications.

##### **Basis of Consolidation**

The consolidated financial statements include the accounts of Neogen Corporation and its subsidiaries all of which are wholly owned (collectively, the Company).

All intercompany accounts and transactions have been eliminated in consolidation.

##### **Use of Estimates**

The preparation of financial statements in conformity with U.S. generally accepted accounting principles requires management to make estimates and assumptions that affect the amounts reported in the consolidated financial statements and accompanying notes. Actual results could differ from these estimates.

##### **Comprehensive Income**

Comprehensive income represents net income and any revenues, expenses, gains and losses that, under U.S. generally accepted accounting principles, are excluded from net income and recognized directly as a component of stockholders' equity. Accumulated other comprehensive income consists solely of foreign currency translation adjustments.

##### **Accounts Receivable and Concentrations of Credit Risk**

Financial instruments which potentially subject the Company to concentrations of credit risk consist principally of accounts receivable. Management attempts to minimize credit risk by reviewing customers' credit history before extending credit and by monitoring credit exposure on a regular basis. An allowance for possible losses on accounts receivable is established based upon factors surrounding the credit risk of specific customers, historical trends and other information. Collateral or other security is generally not required for accounts receivable. During the year ended May 31, 2007, one Food Safety distributor customer had revenues of 11.8%. No other customer had revenues in excess of 10%. No single customer accounted for more than 10% of accounts receivable at May 31, 2007 and 2006.

##### **Fair Value of Financial Instruments**

The carrying amounts of the Companies financial instruments, including accounts receivable, accounts payable, accrued expenses and long-term debt approximate fair value based on either their short maturity or current terms for similar instruments.

##### **Cash and Cash Equivalents**

Cash and cash equivalents are used to support current operations and may be invested to take advantage of short-term investment opportunities. The Company invests in only high quality, short-term investments with original maturity dates of less than 90 days. These securities are considered to be available-for-sale marketable securities. However, there were no significant differences between cost and estimated fair market value at May 31, 2007 and 2006. Additionally, since investments are short-term and carried to maturity, there were no realized gains and losses in 2007, 2006 or 2005. At May 31, 2007 cash equivalents included short term high grade commercial paper and amounted to \$11,400,000 and \$150,000 at May 31, 2007 and 2006 respectively.



**Table of Contents****Neogen Corporation and Subsidiaries****Notes to Consolidated Financial Statements****Inventories**

Inventories are stated at the lower of cost, determined on the first-in, first-out method, or market. The components of inventories were as follows:

	2007	2006
Raw materials	\$ 7,884,000	\$ 8,033,000
Work-in-process	390,000	411,000
Finished goods	10,842,000	9,182,000
	\$ 19,116,000	\$ 17,626,000

**Property and Equipment**

Property and equipment is stated at cost. Expenditures for major improvements are capitalized while repairs and maintenance are charged to expense. Depreciation is provided on the straight-line method over the estimated useful lives of the respective assets, which are generally seven to thirty-nine years for buildings and improvements and three to five years for furniture, machinery and equipment. Depreciation expense was \$1,901,000, \$1,779,000 and \$1,444,000 in 2007, 2006 and 2005, respectively.

**Goodwill and Intangible Assets**

Goodwill represents the excess of purchase price over fair value of tangible net assets of acquired businesses after amounts allocated to other intangible assets. Other intangible assets include customer relationships trademarks, licenses, trade names and patents. Amortizable intangible assets are amortized on either an accelerated or a straight-line basis over five to twenty years. The Company reviews the carrying amounts of goodwill and other non-amortizable intangible assets annually to determine if such assets may be impaired. If the carrying amounts of these assets are deemed to be less than fair value based upon a discounted cash flow analysis, such assets are reduced to their estimated fair value.

**Long-lived Assets**

Management reviews the carrying values of its long-lived assets for possible impairment whenever events or changes in business conditions indicate that the carrying amount of the assets may not be recoverable. Impairment is first evaluated by comparing the carrying value of the long-lived assets to undiscounted future cash flows over the remaining useful life of the assets. If the undiscounted cash flows are less than the carrying value of the assets, the fair value of the long-lived assets is determined, and if lower, than the carrying value, impairment is recorded.

**Reclassification**

Certain amounts in the 2006 and 2005 financial statements have been reclassified to conform to the 2007 presentation.

**Stock Options**

At May 31, 2007, the Company had stock option plans, which are described more fully in Note 7. Effective June 1, 2006, the Company adopted the provisions of Financial Accounting Standards Board (FASB) Statement No. 123 (revised), Share-Based Payment. The revised Statement requires companies to measure the cost of employee stock options based on the grant-date fair value and recognize that cost over the period during which a recipient is required to provide services in exchange for the options, typically the vesting period. The Company adopted the provisions of the revised Statement using the



**Table of Contents****Neogen Corporation and Subsidiaries****Notes to Consolidated Financial Statements**

modified-retrospective transition method provided in the revised Statement. Under this method, the Company restated all prior periods presented on a consistent basis, based on the pro forma expense previously disclosed.

As a result of the adoption of the revised Statement, the Company's operating income for the years ended May 31, 2007, 2006 and 2005 was reduced by \$1,293,000, \$1,240,000 and \$1,317,000 respectively, and the Company's net earnings for the same periods were reduced by \$833,000, \$913,000 and \$987,000 respectively. Basic and diluted net earnings per share for the years ended May 31, 2007, 2006 and 2005 were reduced by \$.09, \$.09 and \$.11, respectively. In addition, prior period balance sheets were adjusted to reflect the cumulative impact of stock option compensation expense and stock option exercise activity as required by the modified-retrospective transition method. Such restatements resulted in additional deferred tax assets and changes in stockholder equity of \$877,000 and \$876,000 at May 31, 2006 and \$753,000 and \$1,788,000 at May 31, 2005 respectively.

Prior to the adoption of the revised Statement, the Company presented all of the income tax benefits resulting from the exercise of stock options as cash flows provided by operating activities in the consolidated statements of cash flows. The revised Statement requires the income tax benefit from deductions, resulting from the exercise of stock options, in excess of the compensation cost recognized (excess income tax benefit) to be classified as cash flows provided by financing activities. Excess income tax benefit from exercise of stock options reported as cash flows provided by financing activities for the years ended May 31, 2006 and 2005, respectively, would have been classified as cash flows provided by operating activities if the Company had not adopted the provisions of the revised Statement.

The weighted-average fair value per share of options granted during 2007, 2006 and 2005, estimated on the date of grant using the Black-Scholes option pricing model, was \$8.53, \$6.37 and \$6.06, respectively. The fair value of options granted was estimated using the following weighted-average assumptions:

	2007	2006	2005
Risk-free interest rate	4.7%	4.9%	3.25%
Expected dividend yield	0%	0%	0%
Expected stock price volatility	46.5%	44.5%	44.5%
Expected option life	4.0 years	4.0 years	4.0 years

The risk-free interest rate for periods within the expected life of options granted is based on the United States Treasury yield curve in effect at the time of grant. Expected stock price volatility is based on historical volatility of the Company's stock. The expected option life, representing the period of time that options granted are expected to be outstanding, is based on historical option exercise and employee termination data. The Company recognizes the cost of stock options using the straight-line method over their vesting periods.

**Revenue Recognition**

Revenue from sales of products is recognized at the time title of goods passes to the buyer and the buyer assumes the risks and rewards of ownership, which generally is at the time of shipment. Where right of return exists, allowances are made at the time of sale to reflect expected returns based on historical experience.

**Shipping and Handling Costs**

Shipping and handling costs that are charged to and reimbursed by the customer are recognized as sales, while the related expenses incurred by the Company are recorded in sales and marketing expense and totaled \$3,426,000, \$3,223,000 and \$2,649,000 in 2007, 2006 and 2005, respectively.



**Table of Contents****Neogen Corporation and Subsidiaries****Notes to Consolidated Financial Statements****Research and Development**

Research and development expenditures are charged to operations as incurred.

**Income Taxes**

The Company accounts for income taxes using the liability method. Under this method, deferred income tax assets and liabilities are determined based on differences between the financial reporting and tax bases of assets and liabilities and are measured using the enacted tax rates in effect for the years in which the differences are expected to reverse. Deferred income tax expense represents the change in net deferred income tax assets and liabilities during the year.

No provision has been made for United States federal income taxes that may result from future remittances of the undistributed earnings of Neogen Europe, Ltd. Because it is expected that such earnings will be reinvested overseas indefinitely.

**Advertising Costs**

Advertising costs are expensed as incurred and totaled \$393,000, \$364,000 and \$264,000 in 2007, 2006, 2005, respectively.

**Net Income Per Share**

Basic net income per share is based on the weighted average number of common shares outstanding during each year. Diluted earnings per share is based on the weighted average number of common shares and dilutive potential common shares outstanding. The Company's dilutive potential common shares outstanding during the years result entirely from dilutive stock options and warrants. The following table presents the net income per share calculations:

	Year ended May 31,		
	2007	2006	2005
		(Restated)	
<b>Numerator for basic and diluted net income per share</b>			
Net income	\$ 9,125,000	\$ 7,029,000	\$ 4,929,000
<b>Denominator</b>			
Denominator for basic net income per share weighted average shares	9,194,000	8,247,000	8,097,000
Effect of dilutive stock options and warrants	247,000	210,000	257,000
Denominator for diluted net income per share	9,441,000	8,457,000	8,354,000
<b>Net income per share</b>			
Basic	\$ .99	\$ .85	\$ .61
Diluted	\$ .97	\$ .83	\$ .59

In 2006 and 2005, approximately 100,000 options were excluded from the computations of net income per share as the result of option prices exceeding the average market price of the common shares. No options were excluded in 2007.



**Table of Contents****Neogen Corporation and Subsidiaries****Notes to Consolidated Financial Statements**

## New Accounting Pronouncements

In July 2006, the FASB issued FASB Interpretation No. 48, *Accounting for Uncertainty in Income Taxes-an interpretation of FASB Statement No. 109* (FIN 48), which clarifies the accounting for uncertainty in tax positions. This Interpretation requires that the Company recognize in their financial statements, the impact of a tax position, if that position is more likely than not of being sustained on audit, based on the technical merits of the position. This interpretation is effective for fiscal years beginning after December 15, 2006, with the cumulative effect of the change in accounting principle recorded as an adjustment to opening retained earnings. The Company does not believe the effect of this interpretation will materially effect its financial statements.

## 2. Goodwill and Other Intangible Assets

The Company follows the provisions of SFAS No. 142, *Goodwill and Other Intangible Assets*. SFAS No. 142 prohibits the amortization of goodwill and intangible assets with indefinite lives and requires that the Company evaluate these intangibles for impairment on an annual basis. Management has completed the required annual impairment tests of goodwill and intangible assets with indefinite lives as prescribed by SFAS No. 142 as of the first day of the fourth quarter of 2007 and determined that recorded amounts were not impaired and that no write-down was necessary.

The following table summarizes goodwill by business segment:

	<b>Food Safety</b>	<b>Animal Safety</b>
Balance, June 1, 2005	\$ 6,548,000	\$ 12,051,000
Goodwill acquired	10,338,000	
Balance, May 31, 2006	16,886,000	12,051,000
Goodwill acquisition valuation adjustments	(4,489,000)	
Balance, May 31, 2007	\$ 12,397,000	\$ 12,051,000

Non-amortizable intangible assets include licenses of \$377,000, trademarks of \$1,587,000, and customer relationship intangibles of \$1,224,000.

Other amortizable intangible assets consisted of the following and are included in customer based intangible and other noncurrent assets within the consolidated balance sheets:

	<b>Gross Carrying Amount</b>	<b>Less Accumulated Amortization</b>	<b>Net Carrying Amount</b>
Licenses	\$ 1,172,000	\$ 391,000	\$ 781,000
Covenants not to compete	260,000	233,000	27,000
Patents	491,000	300,000	191,000
Customer relationship intangibles	5,688,000	639,000	5,049,000
Balance, May 31, 2006	\$ 7,611,000	\$ 1,563,000	\$ 6,048,000

Edgar Filing: NEOGEN CORP - Form 10-K

Licenses	\$ 1,117,000	\$ 482,000	\$ 635,000
Covenants not to compete	260,000	249,000	11,000
Patents	2,622,000	559,000	2,063,000
Customer relationship intangibles	7,397,000	1,215,000	6,182,000
Balance, May 31, 2007	\$ 11,396,000	\$ 2,505,000	\$ 8,891,000

-F10-

---

**Table of Contents**

**Neogen Corporation and Subsidiaries**

**Notes to Consolidated Financial Statements**

Amortization expense for other intangibles totaled \$939,000, \$638,000 and \$259,000 in 2007, 2006 and 2005, respectively. The estimated amortization expense for each of the five succeeding years is as follows: \$1,062,000 in 2008, \$1,011,000 in 2009, \$938,000 in 2010, \$892,000 in 2011, and \$850,000 in 2012. The other amortizable intangible assets useful lives are 5 to 20 years for licenses, 5 years for covenants not to compete, 5 to 17 years for patents, and 12 to 20 years for customer relationship intangibles.

**3. Business and Product Line Acquisitions.**

The Consolidated Statements of Income reflect the results of operations for business and product line acquisitions since the respective dates of purchase. All are accounted for using the purchase method.

As of October 1, 2004, Neogen Europe, Ltd., the Company's subsidiary in Scotland, UK, acquired the distribution business of Biologische Analysensysteme GmbH (BAG), a privately held company based in Lich, Germany. BAG was a distributor of Neogen Corporation's products in Germany. BAG's revenues in the 12 months ended September 30, 2004 were approximately \$600,000. Consideration for the acquisition was cash of \$448,000. The allocation of the purchase price included inventory of \$68,000, equipment of \$21,000 and customer based intangibles of \$359,000. As of October 1, 2005 the Company made a second payment of \$180,000 related to the revenues of BAG in the first year following the acquisition. The acquisition is expected to improve distribution of the Company's products in Germany and is included in the Company's Food Safety segment.

On October 13, 2004, the Company acquired the UriCon product line of Animal Health Ventures, Inc., a privately held company. UriCon is a product used for the treatment of urinary incontinence in dogs. Consideration for the purchase was cash of \$200,000. The allocation of the purchase price included inventory of \$23,000 and intangibles of \$177,000. The acquisition adds to the Company's product lines directed toward the treatment of medical disorders in companion animals and is included in the Company's Animal Safety segment.

On December 19, 2005, Neogen Corporation purchased certain assets of the dairy antibiotics business of UCB FD Bioproducts, a division of Belgium based UCB Group. Consideration for the sale, including transaction costs of \$500,000, was \$17,100,000 in cash, and post closing adjustments. The allocation of the purchase price, included \$1,000,000 of accounts receivable, \$2,900,000 of inventory, \$1,200,000 of fixed assets, \$4,600,000 of goodwill and \$7,400,000 of other intangibles. Other intangibles include \$6,400,000 of amortizable assets (distributor agreement and acquired patents) that have been assigned nine to eleven year lives. The dairy antibiotic business is believed to be a strong synergistic fit into Neogen's overall strategy of providing food and animal safety solutions. Intangible assets in this transaction are expected to be deducted for tax purposes as amortized. During the third quarter of fiscal 2007 the Company completed the allocation of the purchase price to the individual assets acquired and liabilities assumed, of UCB FD Bioproducts, which resulted in an increase of \$1,000,000 and \$1,950,000 to other nonamortizable assets and other non-current assets, respectively on the consolidated balance sheet and a decrease of \$2,786,000 to goodwill compared to amounts reported as of May 31, 2006. The goodwill, along with the other assets and liabilities of UCB FD Bioproducts, are included in the Company's Food Safety segment.

**Table of Contents****Neogen Corporation and Subsidiaries****Notes to Consolidated Financial Statements**

Unaudited pro forma financial information, as if the acquisition of the dairy antibiotics business had taken place on June 1, 2004 is as follows:

	Years Ended May 31,	
	2006	2005
	(Restated)	
Revenue	\$ 76,828,000	\$ 71,958,000
Net Income	6,947,000	6,036,000
Diluted net income per share	\$ .84	\$ .73

On February 17, 2006, Neogen Corporation purchased the common stock of Centrus International, Inc., a wholly owned subsidiary of Eastman Chemical Company, of Kingsport, Tennessee. Consideration consisted of \$3,300,000 in cash. The allocation of the purchase price included accounts receivable of \$280,000, inventory of \$270,000, fixed assets of \$180,000, \$860,000 of goodwill and \$1,740,000 of other intangibles. Other intangibles include \$1,640,000 of amortizable assets (customer based intangible and acquired patents) that have been assigned thirteen to fifteen year lives and deferred tax assets of \$300,000 related to net operating loss carry forwards and assumed liabilities of \$330,000. Centrus produces Soleris™, a user-friendly, rapid optical testing system that accurately detects microbial contamination and represents a synergistic fit with Neogen's Food Safety solutions. Centrus unaudited sales in the 12 month period ended December 31, 2005 (prior to the acquisition) were \$2,800,000. Intangible assets in this transaction are not expected to be deducted for tax purposes as amortized. During fiscal 2007 the Company completed the allocation of the purchase price to the individual assets acquired and liabilities assumed, of Centrus International, Inc. which resulted in an increase of \$104,000 and \$1,641,000 to other nonamortizable assets, respectively on the consolidated balance sheet and a decrease of \$1,720,000 to goodwill compared to amounts reported as of May 31, 2006. The goodwill, along with other assets and liabilities of Centrus International, Inc. are included in the Company's Food Safety segment.

#### 4. Long-Term Debt

The Company has a financing agreement with a bank (nothing drawn at May 31, 2007) providing for an unsecured revolving line of credit of \$10,000,000 that matures on December 1, 2008. Interest is at LIBOR plus 95 basis points (rate under the terms of the agreement was 6.27% at May 31, 2007). Financial covenants include maintaining specified funded debt to EBITDA and debt service ratios as well as specified levels of tangible net worth, all of which are complied with at May 31, 2007.

#### 5. Equity Compensation Plans

Qualified and non-qualified options to purchase shares of common stock may be granted to directors, officers and employees of the Company at an exercise price of not less than the fair market value of the stock on the date of grant under the terms of the Company's stock option plans. The number of shares initially authorized for issuance under the plans is 4,074,219. Remaining shares available for grant under stock option plans were 599,134, 804,175 and 985,731 at May 31, 2007, 2006 and 2005, respectively. Options vest over periods ranging from three to five years and option terms are generally five years.

**Table of Contents****Neogen Corporation and Subsidiaries****Notes to Consolidated Financial Statements**

The following is a summary of stock option plan activity:

	Shares	Weighted-Average Exercise Price
Outstanding at May 31, 2004 (301,839 exercisable)	1,202,746	\$ 10.53
Granted	198,500	19.36
Exercised	(149,502)	6.77
Forfeited	(32,625)	13.74
Outstanding at May 31, 2005 (455,732 exercisable)	1,219,119	12.31
Granted	202,250	18.41
Exercised	(172,570)	7.15
Forfeited	(20,694)	16.73
Outstanding at May 31, 2006 (587,631 exercisable)	1,228,105	14.02
Granted	215,000	20.30
Exercised	(424,012)	10.92
Forfeited	(9,959)	14.14
Outstanding at May 31, 2007 (458,674 exercisable)	1,009,134	\$ 16.65

The following is a summary of stock options outstanding at May 31, 2007:

Range of Exercise Price	Options Outstanding		Options Exercisable		
	Number	Average Remaining Contractual Life (Years)	Weighted-Average Exercise Price	Number	Weighted-Average Exercise Price
\$ 4.09 6.13	28,958	3.1	\$ 5.10	28,958	\$ 5.10
8.18 10.22	118,590	2.9	9.79	84,278	9.78
10.23 12.27	15,418	3.7	11.04	15,418	11.04
14.32 16.36	261,718	3.8	15.21	197,606	15.21
16.37 18.40	81,100	2.4	18.19	32,267	18.19
18.41 20.45	503,350	4.8	19.61	100,147	19.52
4.09 20.45	1,009,134	4.1	\$ 16.65	458,674	\$ 14.58

The weighted-average exercise price of shares that were exercisable at May 31, 2006 and 2005 was \$11.82 and \$9.98, respectively.

The aggregate intrinsic value of options outstanding and options exercisable was \$3,793,000 and \$2,421,000 at May 31, 2005, \$7,900,000 and \$5,500,000 at May 31, 2006 and \$10,826,000 and \$5,869,000 at May 31, 2007. The aggregate intrinsic value of options exercised during the year was \$1,769,000 in FY 2005, \$1,987,000 in FY 2006 and \$6547,000 in FY 2007. Remaining compensation cost for nonvested shares was \$1,770,000 at May 31, 2007.

**Table of Contents****Neogen Corporation and Subsidiaries****Notes to Consolidated Financial Statements**

The following table summarizes warrant activity with non-employees that are expensed at fair value. All warrants are exercisable for common stock of the Company and expire through 2011.

	Shares	Weighted-Average Exercise Price
Outstanding warrants at June 1, 2004	45,625	\$ 11.01
Warrants exercised during the year	(10,000)	9.43
Warrants granted during the year	13,000	18.19
Outstanding warrants at May 31, 2005	48,625	13.15
Warrants exercised during the year	(3,750)	5.50
Warrants granted during the year	11,000	17.61
Warrants forfeited during the year	(1,250)	5.50
Outstanding warrants at May 31, 2006	54,625	14.53
Warrants exercised during the year	(6,250)	10.48
Warrants granted during the year	8,000	20.30
Warrants forfeited during the year	(2,500)	14.15
Outstanding warrants at May 31, 2007	53,875	\$ 15.87

Common stock totaling 100,000 shares is reserved for issuance under the terms of the 2002 Employee Stock Purchase Plan. The plan give eligible employees the option to purchase common stock (total purchases in any year are limited to 10% of compensations) at 95% of the lower of the market value of the stock at the beginning or end of each participation period. Shares purchased by employees were 9,523, 10,865 and 6,895 in 2007, 2006 and 2005, respectively.

**6. Income Taxes**

The provision for income taxes consisted of the following:

	Year ended May 31,		
	2007	2006	2005
Current:			
U.S. Federal and foreign	\$ 3,989,000	\$ 3,217,000	\$ 1,824,000
State	(52,000)	296,000	334,000
Deferred	813,000	309,000	512,000
	\$ 4,750,000	\$ 3,822,000	\$ 2,670,000



**Table of Contents****Neogen Corporation and Subsidiaries****Notes to Consolidated Financial Statements**

Deferred income taxes reflect the tax effects of temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for income tax purposes. Significant components of the Company's deferred income tax liabilities and assets are as follows:

	May 31,	
	2007	2006
Deferred income tax liabilities		
Depreciation and amortization	\$ (2,339,000)	\$ (2,274,000)
Intangible assets and other	526,000	293,000
	(1,813,000)	(1,981,000)
Deferred income tax assets		
Inventories and accounts receivable	859,000	1,522,000
Acquired net operating loss carry forwards	300,000	300,000
	1,159,000	1,822,000
Net deferred income tax liabilities	\$ (654,000)	\$ (159,000)

Net operating loss carry forwards resulting in a deferred tax asset of \$300,000 will expire in 2019.

The reconciliation of income taxes computed at the U.S. federal statutory tax rate to income tax expense is as follows:

	Year ended May 31,		
	2007	2006	2005
Tax at U.S. statutory rates	\$ 4,756,000	\$ 3,698,000	\$ 2,584,000
Tax credits and other	28,000	(68,000)	(134,000)
Provisions for state income taxes, net of federal benefit	(34,000)	192,000	220,000
	\$ 4,750,000	\$ 3,822,000	\$ 2,670,000

**7. Commitments and Contingencies**

The Company is involved in environmental remediation and monitoring activities at its Randolph, Wisconsin manufacturing facility and accrues for related costs when such costs are determined to be probable and estimable. Remaining anticipated cost of remediation through 2024 have been discounted at 4% and recorded within other long term liabilities in the consolidated balance sheet at its net present value of \$935,000 at May 31, 2007. Estimated payments over the succeeding five years are \$90,000 annually, with \$1,080,000 due thereafter.

The Company has agreements with unrelated third parties that provide for the payment of royalties on the sale of certain products. Royalty expense under the terms of these agreements for was \$1,124,000, \$911,000 and \$742,000 for 2007, 2006 and 2005, respectively.

The Company leases office and manufacturing facilities under noncancelable operating leases. Rent expense for 2007, 2006 and 2005 was \$346,000, \$239,000 and \$205,000, respectively. Future minimum rental payments for these leases over the remaining terms are as follows: 2008 - \$288,000; 2009 - \$200,000 and 2010 - \$30,000.



**Table of Contents**

**Neogen Corporation and Subsidiaries**

**Notes to Consolidated Financial Statements**

The Company is subject to certain legal and other proceedings in the normal course of business that, in the opinion of management, will not have a material effect on its future results of operations or financial position.

**8. Defined Contribution Benefit Plan**

The Company maintains a defined contribution 401(k) benefit plan covering substantially all employees. Employees are permitted to defer up to 15% of compensation, with the Company matching 100% of the first 3% deferred and 50% of the next 2% deferred. The Company's expense under this plan was \$409,000, \$348,000 and \$343,000 in 2007, 2006 and 2005, respectively.

**9. Segment Information**

The Company has two reportable segments: Food Safety and Animal Safety. The Food Safety segment produces and markets diagnostic test kits and related products used by food producers and processors to detect harmful natural toxins, foodborne bacteria, allergens and levels of general sanitation. The Animal Safety segment is primarily engaged in the production and marketing of products dedicated to animal health, including a complete line of consumable products marketed to veterinarians and animal health product distributors. Additionally, the Animal Safety segment produces and markets a line of rodenticides to assist in the control of rats and mice in and around agricultural, food production and other facilities.

These segments are managed separately because they represent strategic business units that offer different products and require different marketing strategies. The Company evaluates performance based on total sales and operating income of the respective segments. The accounting policies of the segments are the same as those described in Note 1.

**Table of Contents****Neogen Corporation and Subsidiaries****Notes to Consolidated Financial Statements**

Segment information is as follows:

	Food Safety	Animal Safety	Corporate and Eliminations (1)	Total
<b>2007</b>				
Net sales to external customers	\$ 46,956,000	\$ 39,182,000	\$	\$ 86,138,000
Operating income	9,619,000	4,845,000	(960,000)	13,504,000
Depreciation and amortization	1,952,000	888,000		2,840,000
Interest income			373,000	373,000
Interest expense			15,000	15,000
Income taxes	3,383,000	1,704,000	(337,000)	4,750,000
Total assets	55,426,000	39,104,000	10,754,000	105,284,000
Expenditures for long-lived assets	3,692,000	1,012,000		4,704,000
<b>2006</b>				
Net sales to external customers	\$ 34,951,000	\$ 37,482,000	\$	\$ 72,433,000
Operating income	6,753,000	6,083,000	(2,031,000)	10,805,000
Depreciation and amortization	1,593,000	824,000		2,417,000
Interest income			80,000	80,000
Interest expense			283,000	283,000
Income taxes	2,369,000	2,134,000	(681,000)	3,822,000
Total assets	52,869,000	35,970,000	(549,000)	88,290,000
Expenditures for long-lived assets	2,049,000	643,000		2,692,000
<b>2005</b>				
Net sales to external customers	\$ 28,156,000	\$ 34,600,000	\$	\$ 62,756,000
Operating income	4,051,000	5,284,000	(1,883,000)	7,452,000
Depreciation and amortization	908,000	795,000		1,703,000
Interest income			7,000	7,000
Interest expense			83,000	83,000
Income taxes	1,423,000	1,857,000	(610,000)	2,670,000
Total assets	27,378,000	35,738,000	768,000	63,884,000
Expenditures for long-lived assets	1,828,000	860,000		2,688,000

(1) Includes corporate assets, consisting of marketable securities, and overhead expenses not allocated to specific business segments. Also includes the elimination of intersegment transactions and minority interests.

Sales to customers outside the United States amounted to \$32,727,000 or 38% of consolidated sales in 2007 and \$20,750,000 or 29% of consolidated sales in 2006, \$17,002,000 or 27% in 2005 and were derived primarily in the geographic areas of South and Central America, Canada, Asia and Europe. The Company has one Food Safety distributor customer with revenues of 11.8%. No other customer had revenues in excess of 10% of consolidated net sales.

#### 10. Government Grant

The Company received a \$500,000 grant from Ingham County in fiscal 2005 that was restricted for the purchase of machinery and equipment at its location in Lansing, Michigan. The grant was repayable in cash plus interest to the extent not offset by allowances for new employees hired in Lansing over a period of 6 years. Grant monies received from the County for eligible purchases were initially recognized as a long-term liability. The liability is reduced and other income was recognized for the allowances granted as eligible new employees were hired. The Company recognized other income of \$250,000 in 2006 and 2005 related to the grant.



**Table of Contents****Neogen Corporation and Subsidiaries****Notes to Consolidated Financial Statements**

## 11. Stock Repurchase

The Company's Board of Directors has authorized the purchase of up to 1,250,000 shares of the Company's common stock. As of May 31, 2006, 892,885 cumulative shares had been purchased in negotiated and open market transactions for a total price, including commissions, of approximately \$5,226,000. There were no purchases in 2007 or 2006. Shares purchased under this buy-back program were retired.

## 12. Summary of Quarterly Data (Unaudited)

	Quarter Ended			
	August	November	February	May
	2005	2005	2006	2006
	(Restated)			
	(In thousands, except per share data)			
Net sales	\$ 16,778	\$ 18,256	\$ 17,584	\$ 19,815
Gross margin	8,841	9,490	8,522	10,153
Net income	1,987	1,937	1,386	1,719
Basic net income per share	.24	.23	.17	.21
Diluted net income per share	.24	.23	.16	.20

	Quarter Ended			
	August	November	February	May
	2006	2006	2007	2007
	(In thousands, except per share data)			
Net sales	\$ 22,220	22,189	21,054	20,675
Gross margin	10,320	11,709	10,950	11,584
Net income	2,406	2,426	1,990	2,303
Basic net income per share	.27	.26	.22	.24
Diluted net income per share	.26	.26	.21	.24

Quarterly net income per share is based on weighted-average shares outstanding and potentially dilutive stock options and warrants for the specific period, and as a result, will not necessarily aggregate to total net income per share as computed for the year as disclosed in the consolidated statements of income.

## 13. Subsequent Event

On July 26, 2007 the Board of Directors approved a 3-for-2 stock split for shareholders of record on August 15, 2007, in which shareholders of will receive one additional share for each two shares held. The split will be effected in the form of a stock dividend and will be paid in newly issued Common Stock on September 4, 2007. No effect of this split has been reflected in these financial statements.

**Table of Contents****Neogen Corporation and Subsidiaries****Notes to Consolidated Financial Statements**

## Neogen Corporation and Subsidiaries

## Schedule II

## Valuation and Qualifying Accounts

Year Ended May 31

	<b>Balance</b>	<b>Charged to</b>		<b>Balance</b>
	<b>at Beginning</b>	<b>Costs and</b>		<b>at End</b>
	<b>of Year</b>	<b>Expenses</b>	<b>Acquisitions</b>	<b>Write-Offs</b>
				<b>of Year</b>
<b>Valuation Allowance for Accounts Receivable:</b>				
2007	\$ 530,000	\$ 30,000		\$ 60,000
2006	531,000	165,000		166,000
2005	571,000	134,000		174,000
Year Ended May 31:				

	<b>Balance</b>	<b>Charged to</b>		<b>Balance</b>
	<b>at Beginning</b>	<b>Costs and</b>		<b>at End</b>
	<b>of Year</b>	<b>Expenses</b>	<b>Acquisitions</b>	<b>Write-Offs</b>
				<b>of Year</b>
<b>Valuation Allowance for Inventories:</b>				
2007	\$ 487,000	\$ 442,000		\$ 419,000
2006	471,000	433,000		417,000
2005	415,000	69,000		13,000

-F19-