FORM 10-K

Annual report pursuant to section 13 and 15(d)

Filing Date: **2000-03-30** | Period of Report: **1999-12-31**
SEC Accession No. 0000950147-00-000480

FILER

ORTHOLOGIC CORP

CIK:**887151**| IRS No.: **860585310** | State of Incorp.:**DE** | Fiscal Year End: **1231**
Type: **10-K** | Act: **34** | File No.: **000-21214** | Film No.: **585575**
SIC: **3841** Surgical & medical instruments & apparatus

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U.S. SECURITIES AND EXCHANGE COMMISSION
Washington, DC 20549

FORM 10-K

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

For the fiscal year ended December 31, 1999

[ ] TRANSITION REPORT UNDER SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the transition period from _____ to _____

Commission file number: 0-21214

ORTHOLOGIC CORP.
(Exact Name of Registrant as Specified in Its Charter)

Delaware	86-0585310
(State or Other Jurisdiction of Incorporation or Organization)	(I.R.S. Employer Identification No.)

1275 West Washington Street, Tempe, Arizona 85281
(Address of Principal Executive Offices)

Issuer's telephone number: (602) 286-5520

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

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

Common Stock, par value $.0005 per share
(Title of Class)

Rights to purchase 1/100 of a share of Series A Preferred Stock
(Title of Class)

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 report(s)), and (2) has been subject to such filing requirements for the past 90 days. Yes [X] 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. [ ]

The aggregate market value of the voting and non-voting common equity held by non-affiliates of the registrant, based upon the closing bid price of the registrant's Common Stock as reported on the Nasdaq National Market on March 23, 2000 was approximately $173,609,383. Shares of Common Stock held by each officer and director and by each person who owns 10% or more of the outstanding Common Stock have been excluded in that such persons may be deemed to be affiliates. This determination of affiliate status is not necessarily conclusive.

The number of outstanding shares of the registrant's Common Stock on March 23, 2000 was 29,738,263.

DOCUMENTS INCORPORATED BY REFERENCE

Portions of the Registrant's Annual Report to Stockholders for the fiscal year ended December 31, 1999 are incorporated by reference in Part II hereof and portions of the Registrant's Proxy Statement for the Annual Meeting of Stockholders to be held on May 19, 2000 are incorporated by reference in Part III hereof.

ORTHOLOGIC CORP.
FORM 10-K ANNUAL REPORT
YEAR ENDED DECEMBER 31, 1999

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PART I

ITEM 1. BUSINESS

GENERAL

The Company was incorporated as a Delaware corporation in July 1987 as IatroMed, Inc. and changed its name to OrthoLogic Corp. in July 1991. Unless the context otherwise requires, the "Company" or "OrthoLogic" as used herein refers

to OrthoLogic Corp. and its subsidiaries. The Company's executive offices are located at 1275 West Washington Street, Tempe, Arizona 85281, and its telephone number is (602) 286-5520.

OrthoLogic develops, manufactures and markets proprietary, technologically advanced orthopedic products and packaged services for the orthopedic health care market including bone growth stimulation devices, continuous passive motion ("CPM") devices and ancillary orthopedic recovery products and a therapeutic injectable for relief of pain from osteoarthritis of the knee. OrthoLogic's products are designed to enhance the healing of diseased, damaged, degenerated or recently repaired musculoskeletal tissue. The Company's products focus on improving the clinical outcomes and cost-effectiveness of orthopedic procedures that are characterized by compromised healing, high-cost, potential for complication and long recuperation time.

OrthoLogic periodically discusses with third parties the possible acquisition of technology, product lines and businesses in the orthopedic health care market and from time to time enters into letters of intent that provide OrthoLogic with an exclusivity period during which it considers possible acquisitions.

PRODUCTS AND OTHER PRODUCT DEVELOPMENT

OrthoLogic's product line includes bone growth stimulation and fracture fixation devices, CPM devices and related products and Hyalgan. The Company's product line is sold primarily through the Company's direct sales force. However, the Company plans to use regional spine product distributors coupled with its direct sales force for the sale of its new bone growth stimulation device, the SPINALOGIC.

BONE GROWTH STIMULATION PRODUCTS

ORTHOLOGIC(R) 1000; OL-1000 SC. The ORTHOLOGIC 1000 is a U.S. Food and Drug Administration ("FDA") approved, portable, noninvasive physician prescribed magnetic field bone growth stimulator designed for home treatment of patients who have a nonunion fracture of certain long bones. A nonunion fracture was defined for the purposes of this study as a fracture that remains unhealed for at least nine months post-injury. The ORTHOLOGIC 1000 comprises two magnetic field treatment transducers (coils) and a microprocessor-controlled signal generator that delivers highly specific, low energy combined static and alternating magnetic fields.

In July 1997, the Company received a Pre-Market Approval ("PMA") supplement from the FDA for a single-coil model of the ORTHOLOGIC 1000. The single-coil device, the OL-1000 SC, utilizes the same magnetic fields as the ORTHOLOGIC 1000, is available in four sizes and is designed to be more comfortable for patients with fractures of some long bones, such as the upper femur or the scaphoid. The Company released this product during the first quarter of 1998.

SPINALOGIC(R). The SPINALOGIC is a portable, noninvasive magnetic field bone growth stimulator which enhances the healing process as either an adjunct to spinal fusion surgery or as treatment for a failed spinal fusion surgery. The Company believes that the SPINALOGIC offers benefits similar to those of the ORTHOLOGIC 1000 in that it is relatively easy to use, requires a small power supply and requires only 30 minutes of treatment per day. The SPINALOGIC consists of one magnetic field treatment transducer and a microprocessor-controlled signal generator, both of which are positioned near the spine through use of an adjustable belt which the patient places around the torso. The Company received approval of an Investigational Device Exemption from the FDA in August 1992 and commenced clinical trials for the SPINALOGIC as an

adjunct to spinal fusion surgery in February 1993. The Company received approval of an IDE supplement from the FDA in September of 1995 to conduct a clinical trial of the SPINALOGIC as a noninvasive treatment for a failed spinal fusion surgery. After OrthoLogic submitted several amendments to the PMA Supplement in response to discussions with the FDA, the U.S. Food and Drug Administration approved the SPINALOGIC PMA Supplement on December 20, 1999 allowing the Company to begin selling SPINALOGIC to customers.

CPM DEVICES AND RELATED PRODUCTS

CONTINUOUS PASSIVE MOTION. CPM devices provide controlled, continuous movement to joints and limbs without requiring the patient to exert muscular effort and are intended to be applied immediately following orthopedic trauma or surgery. The products are designed to reduce swelling, increase joint range of motion, reduce the length of hospital stay and reduce the incidence of post-trauma and post-surgical complication. The primary use of CPM devices occurs in the hospital and home environments, but they are also utilized in skilled nursing facilities, sports medicine and rehabilitation centers. The Company offers a wide range of lower and upper extremity CPM devices. Lower extremity CPM is a widely accepted treatment for rehabilitation from knee surgical procedures such as total knee replacement and anterior cruciate ligament reconstruction. Consequently the number of companies competing in this line of business has increased, resulting in decreased reimbursement rates from managed care providers. Upper extremity CPM for the shoulder, elbow, wrist and hand are not yet standard rehabilitation procedures but are continuing to gain acceptance. No clinical studies have been completed supporting the efficiency of upper extremity CPM. As a result, there is no Medicare reimbursement to date for this treatment. Currently, the majority of upper extremity CPM reimbursement payments are workers' compensation related. The Company maintains a fleet of CPM devices that are rented to patients upon receipt of a written prescription.

ANCILLARY ORTHOPEDIC PRODUCTS. The Company offers a complete line of bracing, electrotherapy, cryotherapy and dynamic splinting products. The bracing line includes post-operative, custom and pre-sized functional and osteoarthritis models. Post-operative braces are used in the early phases of post-surgical rehabilitation while functional braces are applied as the patient returns to work or sports activities. The electrotherapy line consists of TENS, NMES, high volt pulsed current, interferential, and biofeedback units. Cryotherapy is used to cool the operative or injured site in order to prevent pain and swelling. OrthoLogic produces its own motorized cryotherapy device, the Blue Arctic, which provides temperature-controlled cold therapy using a reservoir of ice water and a pump that circulates the water through a pad over the injury/surgical site.

HYALGAN

The Company began marketing Hyalgan to orthopedic surgeons during July 1997 under a Co-Promotion Agreement with Sanofi Pharmaceuticals, Inc. (the "Co-Promotion Agreement"). Hyalgan is used for relief of pain from osteoarthritis of the knee for those patients who have failed to respond adequately to conservative non-pharmacological therapy and to simple analgesics, such as acetaminophen. Orthopedic surgeons administer Hyalgan in their offices, with each patient receiving five injections over a period of four weeks. Hyalgan is a preparation of highly purified sodium hyaluronate, a chemical found in the body and present in high amounts in joints and synovial fluid. The body's own hyaluronate plays a number of key roles in normal joint function, and in osteoarthritis, the quality and quantity of hyaluronate in the joint fluid and tissues may be deficient. On January 24, 2000, the U.S. Food and Drug Administration approved new labeling for Hyalgan which states Hyalgan can

produce pain relief beyond 26 weeks. The labeling will allow the Company to utilize published clinical papers exhibiting up to 12 months of pain relief with a single course of therapy. In addition, the revised label allows the Company to promote Hyalgan for repeated cycles of treatment.

FUTURE PRODUCTS

CHRYSALIN. In January 1998 the Company made a minority equity investment in Chrysalis BioTechnology, Inc. As part of the transaction, the Company has been awarded a world-wide exclusive option to license the orthopedic applications of Chrysalin, a patented 23-amino acid peptide that has shown promise in accelerating the healing process of fractured bones. In pre-clinical animal studies, Chrysalin was shown to double the rate of fracture healing with a single injection into the fracture gap. In November, 1999 the U.S. Food and Drug Administration approved the Company's Investigational New Drug Application, authorizing the Company to proceed on human clinical trials for Chrysalin. In January 2000, the Company began enrolling patients in double blind clinical trials. Depending on the rate of patient enrollment, the trials could be completed by the end of 2000. However, there can be no assurance that the trials will be completed at that time or the nature of the findings. The trial consists of prospective, randomized double blind studies of 90 patients in three clinical centers to study the safety and efficiency of Chrysalin on healing fractures.

ORTHOSOUND(TM). The Company currently is conducting preclinical and a pilot clinical trial relating to the design, development and testing of diagnostic and therapeutic devices utilizing its nonthermal ultrasound technology ("ORTHOSOUND") for use in medical applications that relate to bone, cartilage, ligament or tendon diagnostics and healing. In the area of diagnostics, the ORTHOSOUND research projects address the potential use of ultrasound for the assessment of bone strength and fracture risk in osteoporotic patients and the assessment of fracture healing. In therapeutic applications, the focus of the ORTHOSOUND research is on the potential use of ultrasound for the treatment of at-risk fractures to increase the healing rate and reduce the need for subsequent surgical procedures. The Company has not yet applied for FDA approval to market ORTHOSOUND based products, and there can be no assurance that the Company will do so or that it would receive such approval if sought.

MARKETING AND SALES

The ORTHOLOGIC 1000, OL-1000 SC, and the Orthopedic Products are prescribed by orthopedic surgeons and podiatrists practicing in private practices, hospitals and orthopedic and podiatric treatment centers. The Company is focusing its marketing and sales efforts on these groups, with particular emphasis on those clinicians who treat bone healing problems. CPM products are prescribed by orthopedic surgeons, hospitals, orthopedic trauma centers and allied health professionals. Additionally, the Company utilizes physician-to-physician selling via presentations and scientific and clinical articles published in medical journals. CPM devices are leased to the patient, typically for a period of one to three weeks. Orthopedic surgeons purchase Hyalgan from an exclusive distributor who sells Hyalgan under an agreement with Sanofi Pharmaceuticals, Inc. The Company's sales force calls on orthopedic surgeons to provide them with product information relative to Hyalgan. In marketing the SPINALOGIC, the Company is using a combination of its own direct sales force and regional spine product distributors. Because the SPINALOGIC'S PMA was only recently approved by the FDA on December 20, 1999, there is no assurance that the marketing strategy or the level of sales of the SPINALOGIC will be successful.

The Company's sales and marketing efforts are primarily conducted directly through the Company's own sales people with some marketing by outside spine product distributors for the SPINALOGIC. Of the Company's approximately 521 employees at December 31, 1999, approximately 301 are involved in sales and marketing. The Company employs 9 area vice presidents to manage territory sales, each of whom has responsibility for the Company's sales and marketing efforts in a designated geographic area.

Through the efforts of the Company's specialized direct sales force servicing third party payors, the Company has contracted with over 513 third party payors, including various Blue Cross/Blue Shield organizations, Aetna U.S. Healthcare and the Department of Veteran Affairs. In addition, the Company is an approved Medicare provider and is also an approved Medicaid provider for a majority of states. Effective April 1, 2000, Medicare patients with non- healing fractures are eligible to be treated with the ORTHOLOGIC 1000 90 days after the injury. Prior to this change in the Medicare acceptance criteria, patients were required to wait six months before their non-union fractures were eligible for the ORTHOLOGIC 1000. Because this change in the acceptance criteria has not yet become effective, there is no assurance what effect, if any, this change will have on the demand for the ORTHOLOGIC 1000.

While OrthoLogic has not experienced seasonality of revenues from sales of the ORTHOLOGIC 1000 and related products, revenues from leasing CPM equipment are seasonal. CPM devices are used most commonly as adjuncts to surgery and historically the strongest quarter tends to be the first and fourth quarters of the calendar year. The Company believes this trend may be because (i) individuals tend to put off elective surgical intervention until later in the year when their insurance deductibles have been met, and (ii) sports-related injuries tend to increase in the fall and winter months. There has been no seasonal impact on sales of Hyalgan.

RESEARCH AND DEVELOPMENT

Individuals within the research and development organization have extensive experience in the areas of biomaterials, bioengineering, animal modeling and cell biology. Research and development efforts emphasize product engineering, activities related to the clinical trials conducted by the Company and basic research. With regard to basic research, the research and development staff conducts in-house research projects in the area of fracture healing. The staff also supports and monitors external research projects in biophysical stimulation of growth factors and the potential use of ultrasound technology in diagnostic and therapeutic applications relating to bone, cartilage, ligament or tendon. Both the in-house and external research and development projects also provide technical marketing support for the Company's products and explore the

development of new products and also additional therapeutic applications for existing products. The Company also has a clinical regulatory group that initiates and monitors clinical trials. The Company's clinical regulatory group recently began accepting enrollment into its double blind human clinical trials on Chrysalin. The Company's research and development expenditures totaled $2.3 million, $2.9 million and $2.9 million in the years ended December 31, 1997, 1998 and 1999, respectively. See "Item 7 -- Management's Discussion and Analysis of Financial Condition and Results of Operations."

MANUFACTURING

The Company assembles the ORTHOLOGIC 1000 and SPINALOGIC products from parts supplied by third parties, performs tests on both the components and

assembled product and calibrates the assembled product to specifications. The Company currently purchases the microprocessors used in the ORTHOLOGIC 1000 and SPINALOGIC products from a single manufacturer. The ORTHOLOGIC 1000 and SPINALOGIC are not dependent on this microprocessor, and the Company believes that each could be redesigned to incorporate another microprocessor. At any point in time, the Company maintains a supply of the microprocessor on hand or with its suppliers to meet its sales forecast and provide for any such redesign work. In addition, the magnetic field sensor employed in the ORTHOLOGIC 1000 and SPINALOGIC products is available from two sources. Establishment of additional or replacement suppliers for these components cannot be accomplished quickly. Other components and materials used in the manufacture and assembly of the ORTHOLOGIC 1000 and SPINALOGIC are available from multiple sources.

The Company assembles CPM devices from parts that it manufactures in-house or purchases from third parties. These parts are assembled, calibrated and tested at the Company's facilities in Pickering (outside of Toronto), Canada. The Company purchases several CPM components, including microprocessors, motors and custom key panels from sole-source suppliers. The Company believes that its CPM products are not dependent on these components and could be redesigned to incorporate comparable components. The Company places orders for these components to meet sales forecast for up to six months. Other components and materials used in the manufacture and assembly of CPM products are available from multiple sources.

Fidia S.p.A., an Italian corporation, manufactures Hyalgan under an agreement with Sanofi Pharmaceuticals, Inc. Future revenues of the Company could be adversely affected in the event Fidia S.p.A. experiences disruptions in the manufacture of Hyalgan.

A third party drug manufacturer produces Chrysalin for the Company. Because Chrysalin is currently still in the clinical trial phase and not being sold to the public, it is manufactured by a sole supplier.

COMPETITION

The orthopedic industry is characterized by rapidly evolving technology and intense competition. With respect to the treatment of bone fractures, the Company believes that patients with non-healing fractures are primarily treated with surgery, and this represents the Company's primary competition, although other manufacturers of noninvasive bone growth stimulators also represent competition for the ORTHOLOGIC 1000, SpinaLogic and OL-1000 SC. The Company's main competitors for these products are Electro-Biology, Inc. ("EBI"), a subsidiary of Biomet, Inc., OrthoFix International N.V. ("OrthoFix"), Biolectron Inc., and Exogen, Inc. With respect to the adjunctive treatment of spinal fusion surgery, the primary competitors are EBI, OrthoFix and Biolectron Inc. With respect to external fixation devices, the Company's primary competitors are OrthoFix, Stryker, EBI, Smith & Nephew Richards, Inc., Synthes, Inc. and ACE Orthopedic Manufacturing (a division of Depuy, Inc.). The same group of companies and Applied OsteoSystems, Inc. represent its primary competition in the internal fixation market. The Company's primary competitors in the United States for CPM devices are privately held Thera-Kinetics, Inc., many independent owners/lessors of CPM devices and suppliers of traditional orthopedic rehabilitation services including orthopedic immobilization and follow up physical therapy. The Company also believes that there are several foreign CPM device manufacturers and providers with whom the Company will compete if it increases international sales efforts or as those competitors sell in the United States. The Company's primary competitor for Hyalgan is Biomatrix, Inc.

Many of the Company's competitors have substantially greater resources and experience in research and development, obtaining regulatory approvals,

manufacturing, and marketing and sales of medical devices and services, and therefore represent significant competition for the Company. The Company is aware that its competitors are conducting clinical trials for other medical

applications of their respective technologies. In addition, other companies are developing or may develop a variety of other products and technologies to be used in CPM devices, the treatment of fractures and spinal fusions, including growth factors, bone graft substitutes combined with growth factors, nonthermal ultrasound and the treatment of pain associated with osteoarthritis of the knee. The Company believes that competition is based on, among other factors, the safety and efficacy of products in the marketplace, physician familiarity with the product, ease of patient use, product reliability, reputation, price, sales and marketing capability and reimbursement.

Any product developed by the Company that gains any necessary regulatory approval will have to compete for market acceptance and market share in an intensely competitive market. An important factor in such competition may be the timing of market introduction of competitive products. Accordingly, the relative speed with which the Company can develop products, complete clinical testing as well as any necessary regulatory approval processes and supply commercial quantities of the product to the market will be critical to its competitive success. There can be no assurance the Company can successfully compete on these bases. See "Item 7 -- Management's Discussion and Analysis of Financial Condition and Results of Operations -- Intense Competition" and "-- Rapid Technological Change."

PATENTS, LICENSES AND PROPRIETARY RIGHTS

The Company's practice is to require its employees, consultants and advisors to execute a confidentiality agreement upon the commencement of an employment or consulting relationship with the Company. The agreements provide that all confidential information developed by or made known to an individual during the course of the employment or consulting relationship will be kept confidential and not disclosed to third parties except in specified circumstances. In the case of employees, the agreements provide that all inventions conceived by the individual relating to the Company's business while employed by the Company shall be the exclusive property of the Company. There can be no assurance, however, that these agreements will provide meaningful protection for the Company's trade secrets in the event of unauthorized use or disclosure of such information.

It is also the Company's policy to protect its owned and licensed technology by, among other things, filing patent applications for the technologies that it considers important to the development of its business. The Company uses the BIOLOGIC(R) technology in its bone growth stimulation devices through a worldwide exclusive license granted by a corporation owned by university professors who discovered the technology. With respect to the BIOLOGIC technology, the delivery of such technology to the patient and specific applications of such technology, the Company holds title to five United States patents and to a European patent (Switzerland, Germany, and France), as well as to a pending patent application in Japan, and holds an exclusive worldwide license to 27 United States patents, seven Australian patents, five Canadian patents, two European patents (Germany, France, the United Kingdom, Spain and Italy) and three Japanese patents. Currently there are also pending patent application in Canada and Germany. The Company's license for the BIOLOGIC technology extends for the life of the underlying patents (which are due to expire over a period of years beginning in 2006 and extending through 2016) and covers all improvements and applies to the use of the technology for all medical

applications in man and animals. The license provides for payment of royalties by the Company from the net sales revenues of products using the BIOLOGIC technology. The license agreement can be terminated for breach of any material provision of the license. See Note 6 of Notes to Consolidated Financial Statements.

The Company has been assigned eight United States patents covering methods for ultrasonic bone assessment by noninvasively and quantitatively evaluating the status of bone tissue IN VIVO through measurement of bone mineral density, strength and fracture risk. Additionally, patent applications are pending for this technology in Europe and Japan.

With respect to CPM technology, the Company currently owns 21 United States patents, 8 foreign patents and 5 foreign patent applications pending and applications being distributed in Canada, Europe and Japan. The issued patents on this technology are due to expire over a period of years beginning in the year 2002 and extending through 2017. These patents could expire at an earlier date if the patents are not maintained by paying certain fees and/or annuities to the United States Patent and Trademark Office and/or appropriate foreign patent offices at certain intervals over the life of the patents.

ORTHOLOGIC(R), ORTHOLOGIC & DESIGN(R), ORTHOFRAME(R), BIOLOGIC(R), SPINALOGIC(R), TOMORROW'S TECHNOLOGY TODAY(R), TALON(R), CASELOG(R), ORTHOSONIC(R), LEGASUS SPORT CPM(R), LITELIFT(R), SPORTLITE(R), SUTTER(R), DANNINGER MEDICAL(R), MOBILIMB(R), WAVEFLEX(R), and TOTALCARE(R) are federally registered trademarks of the Company. Additionally, The Company claims trademark rights in PERIOLOGIC(TM), OSTEOLOGIC(TM), ORTHONAIL(TM), ORTHOSOUND(TM), QUICKFIX(TM), CPM 9000AT(TM), LEGASUS CPM(TM), SUTTER CAREPLAN(TM), HOME REHAB SYSTEM(TM) and DANNIFLEX(TM).

GOVERNMENT REGULATION

The activities of the Company are regulated by foreign, federal, state and local governments. Government regulation in the United States and other countries is a significant factor in the development and marketing of the Company's products and in the Company's ongoing manufacturing and research and development activities. The Company and its products are regulated by the FDA under a number of statutes, including the Medical Device Amendments Act of 1976 to the Federal Food, Drug and Cosmetic Act, as amended, and the Safe Medical Devices Act of 1990, as amended (collectively, the "FDC Act").

The Company's current BIOLOGIC technology-based products are classified as Class III Significant Risk Devices, which are subject to the most stringent FDA review, and are required to be tested under an Investigational Device Exemption ("IDE") clinical trial and approved for marketing under a PMA. To begin human clinical studies the Company must apply to the FDA for an IDE. Generally, preclinical laboratory and animal tests are required to establish a scientific basis for granting of an IDE. Once an IDE is granted, clinical trials can commence which involve rigorous data collection as specified in the IDE protocol. After the clinical trial is completed, the data are compiled and submitted to the FDA in a PMA application. FDA approval of a PMA application occurs after the applicant has established safety and efficacy to the satisfaction of the FDA. The FDA approval process may include review by an FDA advisory panel. Approval of a PMA application includes specific requirements for labeling of the medical device with regard to appropriate indications for use. Among the conditions for PMA approval is the requirement that the prospective manufacturer's quality control and manufacturing procedures comply with the FDA

regulations setting forth Good Manufacturing Practices ("GMP"). The FDA monitors compliance with these requirements by requiring manufacturers to register with the FDA, which subjects them to periodic FDA inspections of manufacturing facilities. In addition, the Company must comply with post-approval reporting requirements of the FDA. If violations of applicable regulations are noted during FDA inspections, the continued marketing of any products manufactured by the Company may be adversely affected. No significant deficiencies have been noted in FDA inspections of the Company's manufacturing facilities.

The ORTHOFRAME and ORTHOFRAME/MAYO WRIST FIXATOR are Class II devices. If a medical device manufacturer can establish that a newly developed device is "substantially equivalent" to a device that was legally marketed prior to May 28, 1976, the date on which the Medical Device Amendments Act of 1976 was enacted, the manufacturer may seek marketing clearance from the FDA to market the device by filing a 510(k) pre-market notification with the agency. The Company obtained 510(k) pre-market notification clearances from the FDA for the ORTHOFRAME and ORTHONAIL products.

The Company's CPM devices are Class I devices which do not require 510(k) pre-market notification. However, CPM manufacturers must comply with GMP regulations. The devices must also meet Underwriters Laboratories standards for electrical safety. For sales to the European Community, CPM devices must meet established electromechanical safety and electromagnetic emissions regulations. The European Community requires compliance with newly formed quality control standards. The Company currently complies with the new standards.

Manufacturers outside the United States that export devices to the United States may be subject to FDA inspection. The FDA generally inspects companies every few years. The frequency of inspection depends upon the Company's status with respect to regulatory compliance. To date, the Company's foreign operations have not been the subject of any inspections conducted by the FDA.

Under Canada's Food and Drugs Act and the rules and regulations thereunder (the "Food and Drugs Act"), the CPM devices sold by the Company are Class I devices and therefore do not require any Canadian regulatory approvals prior to their introduction to the market. However, the Company must provide Health Canada with notice concerning the sale of a device and obtain a license to sell the devices. Notice for all of the CPM devices currently manufactured by the Company in Canada has been provided to Health Canada and the Company license was renewed. Subsequent to such notification, Health Canada may request the Company to provide it with the results of the testing conducted on the device. If the results of such testing do not substantiate the nature of the benefits claimed to be obtainable from the use of the device or the performance characteristics claimed for such device to the satisfaction of Health Canada, the sale of the device in Canada would be prohibited until appropriate results had been submitted. The Company has not been asked to provide such testing results to the Canadian authorities. The Company's Biologic technology-based products require and have obtained pre-market approval under Canadian law.

CPM devices must comply with the applicable provincial regulations regarding the sale of electrical products by receiving the prior approval of either the Canadian Standards Association ("CSA") or the provincial hydro-electric authority, unless the device is otherwise exempt from such requirement. The CPM devices have, unless otherwise exempt, obtained such necessary approvals.

The FDC Act regulates the labeling of medical devices to indicate the uses for which they are approved, both in connection with PMA approval and

thereafter, including any sponsored promotional activities or marketing materials distributed by or on behalf of the manufacturer or seller. A determination by the FDA that a manufacturer or seller is engaged in marketing of a product for other than its approved use may result in administrative, civil or criminal actions against the manufacturer or seller.

Regulations governing human clinical studies outside the United States vary widely from country to country. Historically, some countries have permitted human studies earlier in the product development cycle than the United States. This disparity in regulation of medical devices may result in more rapid product approvals in certain foreign countries than the United States, while approvals in countries such as Japan may require longer periods than in the United States. In addition, although certain of the Company's products have undergone clinical trials in the United States and Canada, such products have not undergone clinical studies in any other foreign country and the Company does not currently have any arrangements to begin any such foreign studies.

Hyalgan is considered a Class III Significant Risk Device and is subject to the same clinical trial and GMP reviews as described for the BIOLOGIC technology-based products. The product is manufactured by Fidia S.p.A. in Italy and is imported into the United States. As a result, each shipment of the product into the United States is subject to inspections, including by the United States Department of Agriculture. The import of Hyalgan could be delayed or denied for numerous reasons, and, if this occurs, it could have a material adverse affect on sales of the product. To the Company's knowledge, no significant deficiencies have been noted in the FDA inspections of Fidia S.p.A.'s manufacturing facility.

As a new drug product, Chrysalin is subject to clinical trial and GMP reviews, similar to those described for the BioLogic technology-based products. Under the FDC Act, drug products are required to be tested under Investigational New Drug ("IND") Phase I, II, and III clinical trials and approved for marketing under a New Drug Application ("NDA"). To begin human clinical trials the Company must apply to the FDA for an IND approval. Generally, preclinical laboratory and animal tests are required to establish a scientific basis for granting of an IND application. Once an IND application is granted, the clinical trials may commence and involve rigorous data collection as specified in the IND protocol(s). Data from earlier phases may need to be reviewed by FDA before proceeding to later phases. After all phases of clinical trials are completed, data are compiled and submitted to the FDA in an NDA application. FDA approval of an NDA application occurs after the applicant has established safety and efficacy to the satisfaction of the FDA. Approval of an NDA application includes specific requirements for labeling, manufacturing, and controls. The approval process may include review by an FDA advisory panel. Among conditions for NDA approval is the requirement that the prospective manufacturer's quality control and manufacturing procedures comply with the FDA regulations setting forth Good Manufacturing Practices. A third party manufactures Chrysalin for the Company. The manufacturer is required to register with the FDA and is subject to periodic FDA inspections of manufacturing facilities. Because Chrysalin is currently manufactured by a sole supplier, if violations of applicable regulation are noted during FDA inspections, the continued marketing of the product may be adversely affected.

The process of obtaining necessary government approvals is time-consuming and expensive. There can be no assurance that the necessary approvals for new products or applications will be obtained by the Company or, if they are obtained, that they will be obtained on a timely basis. Furthermore, the Company or the FDA must suspend clinical trials upon a determination that the subjects

or patients are being exposed to an unreasonable health risk. The FDA may also require post-approval testing and surveillance programs to monitor the effects of the Company's products. In addition to regulations enforced by the FDA, the Company is also subject to regulations under the Occupational Safety and Health Act, the Environmental Protection Act, the Toxic Substances Control Act, the Resource Conservation and Recovery Act and other present and potential future federal, state and local regulations. The ability of the Company to operate profitably will depend in part upon the Company obtaining and maintaining all necessary certificates, permits, approvals and clearances from the United States and foreign and other regulatory authorities and operating in compliance with applicable regulations. Failure to comply with regulatory requirements could have a material adverse effect on the Company's business, financial condition and results of operations. Regulations regarding the manufacture and sale of the Company's current products or other products that may be developed or acquired by the Company are subject to change. The Company cannot predict what impact, if any, such changes might have on its business. See "Item 7 -- Management's Discussion and Analysis of Financial Condition and Results of Operations -- Government Regulation" and "-- Condition of Acquired Facilities."

THIRD PARTY PAYMENT

Most medical procedures are reimbursed by a variety of third party payors, including Medicare and private insurers. The Company's strategy for obtaining reimbursement authorization for its products is to establish their safety, efficacy and cost effectiveness as compared to other treatments. The Company is an approved Medicare provider and is also an approved Medicaid provider for a majority of states. The Company contracts with over 513 third party payors as an approved provider for its fracture healing and orthopedic rehabilitation products, including the Department of Veterans Affairs, Aetna U.S. Healthcare and various Blue Cross/Blue Shield organizations. Because the process of obtaining reimbursement for products through third-party payors is longer than through direct invoicing of patients, the Company must maintain sufficient working capital to support operations during the collection cycle. In addition, third party payors as an industry have undergone consolidation, and that trend appears to be continuing. The concentration of such economic power may result in third party payors obtaining additional leverage and thus negatively affecting the Company's profitability and cash flows.

PRODUCT LIABILITY INSURANCE

The business of the Company entails the risk of product liability claims. The Company maintains a product liability and general liability insurance policy and an umbrella excess liability policy. There can be no assurance that liability claims will not exceed the coverage limit of such policies or that such insurance will continue to be available on commercially reasonable terms or at all. Consequently, product liability claims could have a material adverse effect on the business, financial condition and results of operations of the Company. The Company has not experienced any product liability claims to date resulting from its Fracture Healing Products. To date, liability claims resulting from the Company's CPM Products have not had a material adverse effect on business. Additionally, the agreements by which the Company acquired its CPM businesses generally require the seller to retain liability for claims arising before the acquisition. See "Item 7 -- Management's Discussion and Analysis of Financial Condition and Results of Operations -- Risk of Product Liability Claims."

YEAR 2000 COMPLIANCE

The Company did not experience any material Year 2000 computer problems on its primary computer systems. The Company's computer systems functioned properly

into the year 2000. As a result, the Company was able to service its customers, communicate with its suppliers, and submit billings to third party payers without disruption. The Company, however, continues to monitor its systems, suppliers, and customers for any unanticipated issues that have yet to surface.

EMPLOYEES

As of December 31, 1999, the Company had 521 employees, including 301 in sales and marketing, 15 in research and development and clinical and regulatory affairs, approximately 4 in managed care, 100 in reimbursement and 101 in manufacturing, finance and administration. The managed care staff is charged with changing the practice patterns of the orthopedic community through the influence of third party payors on treatment regimes. The Company believes that the success of its business will depend, in part, on its ability to identify, attract and retain qualified personnel. In the future, the Company will need to add additional skilled personnel or retain consultants in such areas as research and development, manufacturing and marketing and sales. The Company considers its relationship with its employees to be good. See "Item 7 -- Management's Discussion and Analysis of Financial Condition and Results of Operations -- Dependence on Key Personnel; Recent Management Changes."

ITEM 2. PROPERTIES

The Company leases facilities in Tempe, Arizona and Pickering, Ontario, Canada. These facilities are designed and constructed for industrial purposes and are located in industrial districts. Each facility is suitable for the Company's purposes and is effectively utilized. The table below sets forth certain information about the Company's principal facilities.

Location	Approx. Square Feet	Lease Expires	Description	Principal Activity
Tempe	80,000	11/07	2-story, in industrial park	Assembly, Administration
Pickering	28,500	2/02	1-story, in industrial park	CPM assembly

The Company believes that each facility is well maintained.

In 1997, the Company consolidated all CPM manufacturing in its Pickering facility and all CPM administrative and service functions in Tempe. The Company has ceased operations at facilities in San Diego, California in connection with the consolidation. See "Item 7 -- Management's Discussion and Analysis of Financial Condition Results of Operations -- Condition of Acquired Facilities."

ITEM 3. LEGAL PROCEEDINGS

On June 24, 1996, and on several days thereafter, lawsuits were filed in the United States District Court for the District of Arizona against the Company and certain officers and directors alleging violations of Sections 10(b) of the Securities Exchange Act of 1934 ("Exchange Act") and SEC Rule 10b-5 promulgated thereunder, and, as to other defendants, Section 20(a) of the Exchange Act. These lawsuits are:

MARK SILVERIA V. ALLAN M. WEINSTEIN, ALLEN R. DUNAWAY, DAVID E. DERMINIO AND ORTHOLOGIC CORPORATION, Cause No. CIV 96-1563 PHX EHC, filed in the United States District Court for the District of Arizona (Phoenix Division) on July 1,

1996.

DERRIC C. CHAN AND ANNA CHAN AS ATTORNEY IN FACT FOR MOON-YUNG CHOW, ON BEHALF OF THEMSELVES AND ALL OTHERS SIMILARLY SITUATED V. ORTHOLOGIC CORPORATION, ALLAN M. WEINSTEIN, FRANK P. MAGEE AND DAVID E. DERMINIO, Cause No. CIV 96-1514 PHX RCB, filed in the United States District Court for the District of Arizona (Phoenix Division) on June 21, 1996.

JEFFREY M. BOREN AND CHARLES E. PETERSON, JR., ON BEHALF OF THEMSELVES AND ALL OTHERS SIMILARLY SITUATED V. ALLAN M. WEINSTEIN AND ORTHOLOGIC CORP., Cause No. CIV 96-1520 PHX RCB, filed in the United States District Court for the District of Arizona on June 24, 1996.

DOROTHY COHEN, ON BEHALF OF HERSELF AND ALL OTHERS SIMILARLY SITUATED V. ORTHOLOGIC CORP. AND ALLAN M. WEINSTEIN, Cause No. CIV 96-1615 PHX SMM, filed in the United States District Court for the District of Arizona (Phoenix Division) on July 9, 1996.

JOSEPH C. BARTON, ON BEHALF OF HIMSELF AND ALL OTHERS SIMILARLY SITUATED V. ORTHOLOGIC CORP. AND ALLAN M. WEINSTEIN, Cause No. CIV 96-1643 PHX ROS, filed in the United States District Court for the District of Arizona (Phoenix Division) on July 12, 1996.

JEFFREY DRAKER, ON BEHALF OF HIMSELF AND ALL OTHERS SIMILARLY SITUATED V. ALLAN M. WEINSTEIN AND ORTHOLOGIC CORP., Cause No. CIV 96-1667 PHX RCB, filed in the United States District Court for the District of Arizona (Phoenix Division) on July 16, 1996.

EDWARD AND ELEANOR KATZ V. ORTHOLOGIC CORP. AND ALLAN M. WEINSTEIN, Cause No. CIV 96-1668 PHX RGS, filed in the United States District Court for the District of Arizona (Phoenix Division) on July 17, 1996.

MARK J. RUTKIN, PAUL A. WALLACE, MALCOLM E. BRATHWAITE, ELAINE K. DAVIES AND DAVID G. DAVIES, LARRY E. CARDER AND CARL HUST, ON BEHALF OF THEMSELVES AND ALL OTHERS SIMILARLY SITUATED V. ALLAN M. WEINSTEIN, ALLEN R. DUNAWAY, DAVID E. DERMINIO AND ORTHOLOGIC CORP., Cause No. CIV 96-1678 PHX EHC, filed in the United States District Court for the District of Arizona (Phoenix Division), on July 17, 1996.

FRANK J. DEFELICE, ON BEHALF OF HIMSELF AND ALL OTHERS SIMILARLY SITUATED V. ORTHOLOGIC CORP. AND ALLAN M. WEINSTEIN, Cause No. CIV 96-1713 PHX EHC, filed in the United States District Court for the District of Arizona (Phoenix Division), on July 23, 1996.

SCOTT LONGACRE, JOSEPH E. SHEEDY, TRUSTEE, RICKIE TRAINOR, W. PRESTON BATTLE, III, TAYLOR D. SHEPHERD, DIANNA LYNN SHEPHERD, GORDON H. HOGAN, TRUSTEE, AND DALLAS WAREHOUSE CORP., INC., ON BEHALF OF THEMSELVES AND ALL OTHERS SIMILARLY SITUATED V. ALLAN M. WEINSTEIN, ALLEN R. DUNAWAY, DAVID E. DERMINIO, FRANK P. MAGEE AND ORTHOLOGIC CORP., Cause No. CIV 96-1891 PHX PGR, filed in the United States District Court for the District of Arizona (Phoenix Division) on August 16, 1996.

JEFFREY D. BAILEY, MILTON BERG, BRYAN BOATWRIGHT, CHARLES R. CAMPBELL, MARK AND CATHY DANIEL, TOM DROTAR, RUDY GONNELLA, DAVID GROSS, JANET GUSTAFSON, WILLA P. KORETZ, DR. RICHARD LEWIS, JOHN MAYNARD, MARGARET MILOSH, MICHELLE MILOSH, THERESA L. ONN, WARD B. PERRY, WILLIAM SCHILLINGS, DARWIN AND MERLE SEN, NESTOR SERRANO AND LARRY E. AND GLORIA M. SWANSON V. ALLAN M. WEINSTEIN, ALLEN R. DUNAWAY, DAVID E. DERMINIO AND ORTHOLOGIC CORPORATION, Cause No. CIV 96-1910 PHX

PGR, filed in the United States District Court for the District of Arizona (Phoenix Division) on August 19, 1996.

NANCY Z. KYSER AND MARK L. NICHOLS, ON BEHALF OF THEMSELVES AND ALL OTHERS SIMILARLY SITUATED V. ORTHOLOGIC CORPORATION, ALLAN M. WEINSTEIN, FRANK P. MAGEE AND DAVID E. DERMINIO, Cause No. CIV 96-1937 PHX ROS, filed in the United States District Court for the District of Arizona (Phoenix Division) on August 22, 1996.

Plaintiffs in these actions allege generally that information concerning the May 31, 1996 letter received by the Company from the FDA regarding the Company's OrthoLogic 1000 Bone Growth Stimulator, and the matters set forth therein, was material and undisclosed, leading to an artificially inflated stock price. Plaintiffs further allege that the Company's non-disclosure of the FDA correspondence and of the alleged practices referenced in that correspondence operated as a fraud against plaintiffs, in that the Company allegedly made untrue statements of material facts or omitted to state material facts necessary in order to make the statements not misleading. Plaintiffs further allege that once the FDA letter became known, a material decline in the stock price of the Company occurred, causing damage to plaintiffs. All plaintiffs seek class action status, unspecified compensatory damages, fees and costs. Plaintiffs also seek extraordinary, equitable and/or injunctive relief as permitted by law. The actions were consolidated for all purposes in the United States District Court for the District of Arizona. On March 31, 1999, the judge in the consolidated case before the United States District Court granted the Company's Motion to Dismiss and entered an order dismissing all claims in the suit against the Company and two individual officers/directors. The judge allowed certain narrow claims based on insider trading theories to proceed against certain individual defendants. On December 21, 1999, the District Court granted plaintiffs' motion for class certification to include purchasers of common stock between June 4 through June 18, 1996, inclusive.

On or about June 20, 1996, a lawsuit entitled NORMAN COOPER, ET AL. V. ORTHOLOGIC CORP., ET AL., Cause No. CV 96- 10799, was filed in the Superior Court, Maricopa County, Arizona. The plaintiffs allege violations of Arizona Revised Statutes Sections 44-1991 (state securities fraud) and 44-1522 (consumer fraud) and common law fraud based upon factual allegations substantially similar to those alleged in the federal court class action complaints. Plaintiffs seek class action status, unspecified compensatory and punitive damages, fees and costs. Plaintiffs also seek injunctive and/or equitable relief. The Company filed a Motion to Dismiss the Complaint in Arizona State Court in May 1999. The Court denied the motion in July 1999 and granted the plaintiffs' motion for the class certification on November 24, 1999. The Company has appealed the state court's class certification and the appeal is now pending in the Arizona Supreme Court.

On or about July 16, 1996, Jacob B. Rapoport filed a Shareholder Derivative Complaint for Breach of Fiduciary Duty and Misappropriation of Confidential Corporation Information (based on similar factual issues underlying the above lawsuits) in the Superior Court of the State of Arizona, Maricopa County, No. CV 96-12406 against Allan M. Weinstein, John M. Holliman, Augustus A. White, Fredric J. Feldman, Elwood D. Howse, George A. Oram, Frank P. Magee and David E. Derminio, Defendants and OrthoLogic Corp., Nominal Defendant. On October 29, 1996 the defendants removed the case to the United States District Court for the District of Arizona (Phoenix Division) No. CIV 96-2451 PHX RCB on grounds of diversity pursuant to 28 U.S.C. ss. 1332. The Company filed a Motion to DismisS the Complaint which was granted on December 13, 1999. As of March 13, the Plaintiff had not appealed the dismissal.

The Company continues to deny the substantive allegations in the aforesaid lawsuits and will continue to defend the action vigorously.

As of December 31, 1999, in addition to other matters disclosed above, the Company is involved in other various legal proceedings that arose in the ordinary course of business.

The costs associated with defending the above allegations and potential outcome cannot be determined at this time and accordingly, no estimate for such costs have been included in the accompanying Financial Statements. In management's opinion, the ultimate resolution of the above proceedings will not have a material effect on the financial position of the Company.

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

Not applicable.

EXECUTIVE OFFICERS OF THE REGISTRANT

The following table sets forth information regarding the executive officers of the Company:

Name	Age	Title
Thomas R. Trotter	52	Chief Executive Officer, President and Director
Frank P. Magee, D.V.M.	43	Executive Vice President, Research and Development
Terry D. Meier	61	Senior Vice President, Chief Financial Officer
William C. Rieger	50	Vice President, Marketing Worldwide
David K. Floyd	39	Vice President, Sales
Ruben Chairez, Ph.D.	57	Vice President, Medical Regulatory and Clinical Affairs
MaryAnn G. Miller	42	Vice President, Human Resources
Kevin Lunau	42	Vice President, Manufacturing

Thomas R. Trotter joined the Company as President and Chief Executive Officer and a Director in October 1997. From 1988 to October 1997, Mr. Trotter held various positions at Mallinckrodt, Inc. in St. Louis, Missouri, most recently as President of the Critical Care Division and a member of the Corporate Management Committee. From 1984 to 1988, he was President and Chief

Executive Officer of Diamond Sensor Systems, a medical device company in Ann Arbor, Michigan. From 1976 to 1984, he held various senior management positions at Shiley, Inc. (a division of Pfizer, Inc.) in Irvine, California.

Frank P. Magee, D.V.M. joined the Company as a Vice President in November 1989 and became Executive Vice President, Research and Development in 1991. Mr. Magee served as President between August 1997 and October 1997. From 1984 to 1989, Dr. Magee was head of Experimental Surgery at Harrington Arthritis Research Center, a not-for- profit independent research and development organization.

Terry D. Meier joined the Company in March 1998 as Senior Vice President and on April 1, 1998, began serving as its Chief Financial Officer. From 1974 to 1997, Mr. Meier held several positions at Mallinckrodt, Inc., a healthcare and specialty chemicals company. Most recently, he served as their Vice President and Corporate Controller and from 1989 to 1996, as the Senior Vice President and Chief Financial Officer.

William C. Rieger joined the Company in January 1998 as Vice President, Marketing and Sales. From 1994 to 1997, Mr. Rieger held the position of Vice President of Sales and Marketing at Hollister Inc., a privately held manufacturer of medical products. From 1985-1994, he held several positions as Vice President at Miles Inc. Diagnostic Division, a manufacturer of diagnostic products.

David K. Floyd joined the Company in May 1998 as Vice President, Sales. From September 1994 through April 1998, Mr. Floyd was associated with Sulzer Orthopedics, most recently as Vice President of Sales with responsibility for sales activity in North America and South America. From May 1987 through August 1994. Mr. Floyd held positions in sales and marketing with Zimmer Inc., a Bristol-Myers Squibb Company and a manufacturer of medical devices.

Ruben Chairez, Ph.D., joined the Company in May 1998 as Vice President, Medical Regulatory and Clinical Affairs. From November, 1993 through April 1998, Dr. Chairez served as Vice President, Regulatory Affairs/Quality Assurance of SenDx Medical, Inc., a manufacturer of blood gas analyzer systems. From July 1990 to November 1993, Mr. Chairez was the Director of Regulatory Affairs with Glen - Probe Incorporated, an in retro diagnostic device manufacturer.

MaryAnn G. Miller joined the Company as Vice President of Human Resources in October 1996. From November 1995 to June 1996, Ms. Miller was Human Resources Director for Southwestco Wireless, Inc. doing business as CellularOne, a subsidiary of Bell Atlantic Nynex Mobile, a provider of wireless telecommunications services in the Southwest. From October 1992 to July 1995, Ms. Miller was a human resources officer with Firstar Corporation, a Wisconsin-based bank holding company. She was previously First Vice President and Regional Human Resources Director of Firstar from January 1994 to July 1995.

Kevin Lunau joined the Company as Vice President of Manufacturing on March 17, 1999. From 1991 to 1999, Mr. Lunau held management positions at OrthoLogic Canada (previously Toronto Medical Corp.), a subsidiary of OrthoLogic. Most recently, he served as OrthoLogic Canada's Executive Vice President and General Manager.

PART II

ITEM 5. MARKET FOR THE REGISTRANT'S COMMON EQUITY AND RELATED STOCKHOLDER MATTERS

The information under the heading "Stockholder Information" on page 16 of the Company's Annual Report to Stockholders for the year ended December 31, 1999 (the "Annual Report") is incorporated herein by reference.

ITEM 6. SELECTED FINANCIAL DATA

The information on pages 16 through 29 of the Annual Report under the heading "Selected Financial Data" is incorporated herein by reference.

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

The information on pages 11 through 15 of the Annual Report under the heading "Management's Discussion and Analysis of Financial Condition and Results of Operations" is incorporated herein by reference.

The Company may from time to time make written or oral forward-looking statements, including statements contained in the Company's filings with the Securities and Exchange Commission and its reports to stockholders. This Report contains forward-looking statements made pursuant to the "safe harbor" provisions of the Private Securities Litigation Reform Act of 1995. In connection with these "safe harbor" provisions, the Company identifies important factors that could cause actual results to differ materially from those contained in any forward-looking statements made by or on behalf of the Company. Any such forward-looking statement is qualified by reference to the following cautionary statements.

LIMITED HISTORY OF PROFITABILITY; QUARTERLY FLUCTUATIONS IN OPERATING RESULTS. The Company was founded in 1987 and only began generating revenues from the sale of its primary product in 1994. The Company has experienced significant operating losses since its inception and had an accumulated deficit of approximately $[51.4] million at December 31, 1999. There can be no assurance that the Company will ever generate sufficient revenues to attain operating profitability or retain net profitability on an on-going annual basis. In addition, the Company may experience fluctuations in revenues and operating results based on such factors as demand for the Company's products, the timing, cost and acceptance of product introductions and enhancements made by the Company or others, levels of third party payment, alternative treatments which currently exist or may be introduced in the future, completion of acquisitions, changes in practice patterns, competitive conditions, regulatory announcements and changes affecting the Company's products in the industry and general economic conditions. The development and commercialization by the Company of additional products will require substantial product development and regulatory, clinical and other expenditures. See "Item 1 -- Business -- Competition."

POTENTIAL ADVERSE OUTCOME OF LITIGATION. The Company is a defendant in a number of investor lawsuits relating generally to correspondence received by the Company from the FDA in mid-1996 regarding the promotion and configuration of the ORTHOLOGIC 1000. See "Item 1 -- Business -- Governmental Regulation" and "Item 3 -- Legal Proceedings." The Company intends to defend these lawsuits vigorously. However, an adverse litigation outcome could have a material adverse effect on the Company's business, financial condition and results of operations.

DEPENDENCE ON SALES FORCE. A substantial portion of the Company's sales are generated through the Company's internal sales force of approximately 301 employees. During 1996, the Company shifted its primary focus from sales through independent orthopedic specialty dealers to an internal sales force. To enhance market penetration of the recently approved SPINALOGIC product, the Company plans to supplement the distribution of the product using a combination of its own direct sales force and regional spine product distributors. See "Item 1 -- Business -- Marketing and Sales."

DEPENDENCE ON KEY PERSONNEL; RECENT MANAGEMENT CHANGES. The success of the Company is dependent in large part on the ability of the Company to attract and retain its key management, operating, technical, marketing and sales personnel as well as clinical investigators who are not employees of the Company. Such individuals are in high demand, and the identification, attraction and retention of such personnel could be lengthy, difficult and costly. The Company competes for its employees and clinical investigators with other companies in the orthopedic industry and research and academic institutions. There can be no

assurance that the Company will be able to attract and retain the qualified personnel necessary for the expansion of its business. A loss of the services of one or more members of the senior management group, or the Company's inability

to hire additional personnel as necessary, could have an adverse effect on the Company's business, financial condition and results of operations. See "Item 1 -- Business -- Employees."

HISTORICAL DEPENDENCE ON PRIMARY PRODUCT; FUTURE PRODUCTS. During 1997, 1998 and 1999 revenues from CPM devices and Hyalgan reduced the Company's dependence on revenues from the ORTHOLOGIC 1000. Near the end of 1999 the Company began human clinical trials of its Chrysalin product and received approval from the FDA to begin marketing SPINALOGIC. However, the Company believes that, to sustain long-term growth, it must continue to develop and introduce additional products and expand approved indications for its existing products. The development and commercialization by the Company of additional products will require substantial product development, regulatory, clinical and other expenditures. There can be no assurance that the Company's technologies will allow it to develop new products or expand indications for existing products in the future or that the Company will be able to manufacture or market such products successfully. Any failure by the Company to develop new products or expand indications could have a material adverse effect on the Company's business, financial condition and results of operations. See "Item 1 -- Business -- Products" and "Item 1 -- Business -- Competition."

UNCERTAINTY OF MARKET ACCEPTANCE. The Company believes that the demand for bone growth stimulators is still developing and the Company's success will depend in part upon the growth of this demand. There can be no assurance that this demand will develop. The long-term commercial success of the ORTHOLOGIC 1000 and SPINALOGIC and the Company's other products will also depend in significant part upon its widespread acceptance by a significant portion of the medical community as a safe, efficacious and cost-effective alternative to invasive procedures. The Company is unable to predict how quickly, if at all, its products may be accepted by members of the orthopedic medical community. The widespread acceptance of the Company's primary products represents a significant change in practice patterns for the orthopaedic medical community and in reimbursement policy for third party payors. Historically, some orthopedic medical professionals have indicated hesitancy in prescribing bone growth stimulator products such as those manufactured by the Company. The use of CPM is more widely accepted, however the Company must continue to prove that the products are safe, efficacious and cost-effective in order to maintain and grow its market share. Hyalgan, although it has been in use for about 12 years, is still a relatively new therapeutic treatment for relief of pain from osteoarthritis of the knee. The long-term commercial success of the product will depend upon its widespread acceptance by a significant portion of the medical community and third party payors as a safe, efficacious and cost-effective alternative to other treatment options such as simple analgesics. As a new product to the market, SPINALOGIC'S sales and acceptance by the medical community are unknown. Failure of the Company's products to achieve widespread market acceptance by the orthopedic medical community and third party payors would have a material adverse effect on the Company's business, financial condition and results of operations. See "Item 1 -- Business -- Third Party Payment."

INTEGRATION OF ACQUISITIONS. The Company acquired three businesses in 1996 and 1997. In the first quarter of 1997, the Company commenced the consolidation of the recent acquisitions. The administrative operations, manufacturing and servicing operations were consolidated by the end of 1997. The sales force management was consolidated in early 1998 and computer hardware and software systems were consolidated during 1998.

MANAGEMENT OF GROWTH. The Company's future performance will depend in part on its ability to manage change in its operations and changes in the healthcare industry, including integration of acquired businesses. In addition, the

Company's ability to manage its growth effectively will require it to continue to improve its manufacturing, operational and financial control systems and infrastructure and management information systems, and to attract, train, motivate, manage and retain key employees. If the Company's management were to become unable to manage growth effectively, the Company's business, financial condition, and results of operations could be adversely affected.

LIMITATIONS ON THIRD PARTY PAYMENT; UNCERTAIN EFFECTS OF MANAGED CARE. The Company's ability to commercialize its products successfully in the United States and in other countries will depend in part on the extent to which acceptance of payment for such products and related treatment will continue to be available from government health administration authorities, private health insurers and other payors. Cost control measures adopted by third party payors in recent years have had and may continue to have a significant effect on the purchasing and practice patterns of many health care providers, generally causing them to be more selective in the purchase of medical products. In addition, payors are increasingly challenging the prices and clinical efficacy of medical products and services. Payors may deny reimbursement if they

determine that the product used in a procedure was experimental, was used for a nonapproved indication or was unnecessary, inappropriate, not cost-effective, unsafe, or ineffective. The Company's products are reimbursed by most payors, however there are generally specific product usage requirements or documentation requirements in order for the Company to receive reimbursement. In certain circumstances the Company is successful in appealing reimbursement coverage for those applications which are not in compliance with the payor requirements. Significant uncertainty exists as to the reimbursement status of newly approved health care products, and there can be no assurance that adequate third party coverage will continue to be available to the Company at current levels. See "Item 1 - Business - Third Party Payment."

UNCERTAINTY AND POTENTIAL NEGATIVE EFFECTS OF HEALTH CARE REFORM. The health care industry is undergoing fundamental changes resulting from political, economic and regulatory influences. In the United States, comprehensive programs have been proposed that seek to (i) increase access to health care for the uninsured, (ii) control the escalation of health care expenditures within the economy and (iii) use health care reimbursement policies to help control the federal deficit. The Company anticipates that Congress and state legislatures will continue to review and assess alternative health care delivery systems and methods of payment, and public debate of these issues will likely continue. Due to uncertainties regarding the outcome of reform initiatives and their enactment and implementation, the Company cannot predict which, if any, of such reform proposals will be adopted and when they might be adopted. Other countries also are considering health care reform. The Company's plans for increased international sales are largely dependent upon other countries' adoption of managed care systems and their acceptance of the potential benefits of the Company's products and the belief that managed care plans will have a positive effect on sales. For the reasons identified in this and in the preceding paragraph, however, those assumptions may be incorrect. Significant changes in health care systems are likely to have a substantial impact over time on the manner in which the Company conducts its business and could have a material adverse effect on the Company's business, financial condition and results of operations and ability to market its products as currently contemplated.

INTENSE COMPETITION. The orthopedic industry is characterized by intense competition. Currently, there are three major competitors other than the Company selling electromagnetic bone growth stimulation products approved by the FDA for the treatment of nonunion fractures, one large domestic and several foreign

manufacturers of CPM devices and one competitor selling a therapeutic injectable for treatment of osteoarthritis of the knee. The Company also competes with many independent owners/lessors of CPM devices in addition to the providers of traditional orthopedic immobilization products and rehabilitation services. The Company estimates that one of its competitors has a dominant share of the market for electromagnetic bone growth stimulation products for non-healing fractures in the United States, and another has a dominant share of the market for use of their device as an adjunct to spinal fusion surgery. In addition, there are several large, well-established companies that sell fracture fixation devices similar in function to those sold by the Company. Many participants in the medical technology industry, including the Company's competitors, have substantially greater capital resources, research and development staffs and facilities than the Company. Such participants have developed or are developing products that may be competitive with the products that have been or are being developed or researched by the Company. Other companies are developing a variety of other products and technologies to be used in CPM devices, the treatment of fractures and spinal fusions, including growth factors, bone graft substitutes combined with growth factors, and nonthermal ultrasound. One company has received FDA approval for a nonthermal ultrasound device to treat nonsevere fresh fractures of the lower leg and lower forearm. There can be no assurance that products marketed by these or other companies will not be sold for use in treating non-healing fractures or spinal fusions, even in the absence of regulatory approval to do so. Any such sales could have a material adverse effect on the Company. Many of the Company's competitors have substantially greater experience than the Company in conducting research and development, obtaining regulatory approvals, manufacturing and marketing and selling medical devices. Any failure by the Company to develop products that compete favorably in the marketplace would have a material adverse effect on the Company's business, financial condition and results of operations. See "Item 1 -- Business -- Research and Development" and "Item 1 -- Business -- Competition."

RAPID TECHNOLOGICAL CHANGE. The medical device industry is characterized by rapid and significant technological change. There can be no assurance that the Company's competitors will not succeed in developing or marketing products or technologies that are more effective or less costly, or both, and which render the Company's products obsolete or non- competitive. In addition, new technologies, procedures and medications could be developed that replace or reduce the value of the Company's products. The Company's success will depend in part on its ability to respond quickly to medical and technological changes through the development and introduction of new products. There can be no assurance that the Company's new product development efforts will result in any commercially successful products. A failure to develop new products could have a material adverse effect on the company's business, financial condition and results of operations. See "Item 1 -- Business -- Research and Development."

GOVERNMENT REGULATION. The Company's current and future products and manufacturing activities are and will be regulated under the Medical Device Amendments Act of 1976 to the Food, Drug and Cosmetic Act and the 1990 Safe Medical Devices Act. The Company's current BIOLOGIC technology-based products and Hyalgan are classified as Class III Significant Risk Devices, which are subject to the most stringent level of FDA review for medical devices and are required to be tested under IDE clinical trials and approved for marketing under a PMA. The Company's fracture fixation devices are Class II devices that are marketed pursuant to 510(k) clearance from the FDA. Chrysalin, as a new drug, is subject to clinical trial and Good Manufacturing Practices review similar to those that apply to the BioLogic technology-based products.

The FDA and comparable agencies in many foreign countries and in state and

local governments impose substantial limitations on the introduction of medical devices through costly and time-consuming laboratory and clinical testing and other procedures. The process of obtaining FDA and other required regulatory approvals is lengthy, expensive and uncertain. Moreover, regulatory approvals, if granted, typically include significant limitations on the indicated uses for which a product may be marketed. In addition, approved products may be subject to additional testing and surveillance programs required by regulatory agencies, and product approvals could be withdrawn and labeling restrictions may be imposed for failure to comply with regulatory standards or upon the occurrence of unforeseen problems following initial marketing.

The Company is also required to adhere to applicable requirements for FDA Good Manufacturing Practices, to engage in extensive record keeping and reporting and to make available its manufacturing facilities for periodic inspections by governmental agencies, including the FDA and comparable agencies in other countries. Failure to comply with these and other applicable regulatory requirements could result in, among other things, significant fines, suspension of approvals, seizures or recalls of products, or operating restrictions and criminal prosecutions. From time to time, the Company receives letters from the FDA regarding regulatory compliance. The Company has responded to all such letters and believes all outstanding issues raised in such letters have been resolved. See "Item 1 -- Business -- Government Regulation."

Changes in existing regulations or interpretations of existing regulations or adoption of new or additional restrictive regulations could prevent the Company from obtaining, or affect the timing of, future regulatory approvals. If the Company experiences a delay in receiving or fails to obtain any governmental approval for any of its current or future products or fails to comply with any regulatory requirements, the Company's business, financial condition and results of operations could be materially adversely affected. See "Item 1 -- Business -- Products" and "Item 1 -- Business -- Government Regulation."

DEPENDENCE ON KEY SUPPLIERS. The Company purchases the microprocessor used in the ORTHOLOGIC 1000 and SPINALOGIC devices from a single manufacturer, Phillips N.V. Although there are feasible alternate microprocessors that might be used immediately, all are produced by Phillips. In addition, there are single suppliers for other components used in the ORTHOLOGIC 1000 and SPINALOGIC devices and only two suppliers for the magnetic field sensor employed in them. Establishment of additional or replacement suppliers for these components cannot be accomplished quickly. Therefore, the Company maintains sufficient inventories of such components in an attempt to ensure availability of finished products in the event of supply shortage or in the event that a redesign is required. The Company purchases several CPM components, including microprocessors, motors and custom key panels from sole-source suppliers. The Company believes that its CPM products are not dependent on these components and could be redesigned to incorporate comparable components without a material interruption to product availability. Hyalgan is also manufactured by a single company, Fidia S.p.A. Fidia has been manufacturing Hyalgan for sale in Europe since 1987. The Company maintains a supply of certain ORTHOLOGIC 1000 and SPINALOGIC components to meet sales forecasts for 3 to 12 months. The distributor of Hyalgan maintains a supply of product to last several months. Chrysalin, which is currently only in the clinical trial phase, is produced by a third party sale supplier. Any delay or interruption in supply of components or products could significantly impair the Company's ability to deliver its products in sufficient quantities, and therefore, could have a material adverse effect on its business, financial condition and results of operations.

DEPENDENCE ON PATENTS, LICENSES AND PROPRIETARY RIGHTS. The Company's success will depend in significant part on its ability to obtain and maintain patent protection for products and processes, to preserve its trade secrets and proprietary know-how and to operate without infringing the proprietary rights of third parties. While the Company holds title to numerous United States and foreign patents and patent applications, as well as licenses to numerous United States and foreign patents (see "Item 1 -- Business -- Patents, Licenses and Proprietary Rights"), no assurance can be given that any additional patents will be issued or that the scope of any patent protection will exclude competitors or that any of the patents held by or licensed to the Company will be held valid if subsequently challenged. The validity and breadth of claims covered in medical technology patents involves complex legal and factual questions and therefore may be highly uncertain. In addition, although the Company holds or licenses patents for certain of its technologies, others may hold or receive patents which contain claims having a scope that covers products developed by the Company. There can be no assurance that licensing rights to the patents of others, if required for the Company's products, will be available at all or at a cost acceptable to the Company.

The Company's licenses covering the BIOLOGIC and ORTHOFRAME technologies provide for payment by the Company of royalties. A Co-Promotion Agreement with Sanofi provides the Company with exclusive marketing rights for Hyalgan to orthopedic surgeons in the United States. The Company is paid a fee which is based upon the number of units sold at the wholesale acquisition cost less amounts for distribution costs, discounts, rebates, returns, product transfer price, overhead factor and a royalty factor. Each license may be terminated if the Company breaches any material provision of such license. The termination of any license would have a material adverse effect on the Company's business, financial condition and results of operations. See Note 15 of Notes to Consolidated Financial Statements.

The Company also relies on unpatented trade secrets and know-how. The Company generally requires its employees, consultants, advisors and investigators to enter into confidentiality agreements which include, among other things, an agreement to assign to the Company all inventions that were developed by the employee while employed by the Company that are related to its business. There can be no assurance, however, that these agreements will protect the Company's proprietary information or that others will not gain access to, or independently develop similar trade secrets or know-how.

There has been substantial litigation regarding patent and other intellectual property rights in the orthopedic industry. Litigation, which could result in substantial cost to, and diversion of effort by the Company may be necessary to enforce patents issued or licensed to the Company, to protect trade secrets or know-how owned by the Company or to defend the Company against claimed infringement of the rights of others and to determine the scope and validity of the proprietary rights of others. There can be no assurance that the results of such litigation would be favorable to the Company. In addition, competitors may employ litigation to gain a competitive advantage. Adverse determinations in litigation could subject the Company to significant liabilities, and could require the Company to seek licenses from third parties or prevent the Company from manufacturing, selling or using its products, any of which determinations could have a material adverse effect on the Company's business, financial condition and results of operations. See "Item 1 -- Business -- Patents, Licenses and Proprietary Rights."

RISK OF PRODUCT LIABILITY CLAIMS. The Company faces an inherent business risk of exposure to product liability claims in the event that the use of its technology or products is alleged to have resulted in adverse effects. To date, no product liability claims have been asserted against the Company for its

fracture healing and Hyalgan products and only limited claims for its CPM products. The Company maintains a product liability and general liability insurance policy with coverage of an annual aggregate maximum of $2.0 million per occurrence. The Company's product liability and general liability policy is provided on an occurrence basis. The policy is subject to annual renewal. In addition, the Company maintains an umbrella excess liability policy which covers product and general liability with coverage of an additional annual aggregate maximum of $25.0 million. There can be no assurance that liability claims will not exceed the coverage limits of such policies or that such insurance will continue to be available on commercially reasonable terms or at all. If the Company does not or cannot maintain sufficient liability insurance, its ability to market its products may be significantly impaired. In addition, product liability claims could have a material adverse effect on the business, financial condition and results of operations of the Company. See "Item 1 -- Business -- Product Liability Insurance."

POSSIBLE VOLATILITY OF STOCK PRICE. Factors such as fluctuations in the Company's operating results, developments in litigation to which the Company is subject, announcements and timing of potential acquisitions, conversion of preferred stock, announcements of technological innovations or new products by the Company or its competitors, FDA and international regulatory actions, actions with respect to reimbursement matters, developments with respect to patents or proprietary rights, public concern as to the safety of products developed by the Company or others, changes in health care policy in the United States and internationally, changes in stock market analyst recommendations regarding the Company, other medical device companies or the medical device industry generally and general market conditions may have a significant effect on the market price of the Common Stock. In addition, the stock market has from time to time experienced significant price and volume fluctuations that are unrelated to the operating performance of particular companies. These broad market fluctuations may adversely affect the market price of the Company's Common Stock.

Developments in any of these areas, which are more fully described elsewhere in "Item 1 -- Business," "Item 3 -- Legal Proceedings," and "Item 7 -- Management's Discussion and Analysis of Financial Condition and Results of Operations" on pages 11 through 15 of the Company's Annual Report to stockholders, each of which is incorporated into this section by reference, could cause the Company's results to differ materially from results that have been or may be projected by or on behalf of the Company.

The Company cautions that the foregoing list of important factors is not exclusive. The Company does not undertake to update any forward-looking statement that may be made from time to time by or on behalf of the Company.

ITEM 7A. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

The Company has exposure to foreign exchange rates through its manufacturing subsidiary in Canada.

The Company does not use foreign currency exchange forward contracts or commodity contracts to limit its exposure. The Company is not currently vulnerable to a material extent to fluctuations in interest rates and commodity prices.

ITEM 8. FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA

The information on pages 11 through 29 of the Annual Report is incorporated

herein by reference.

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

Not applicable.

PART III

ITEM 10. DIRECTORS AND EXECUTIVE OFFICERS OF THE REGISTRANT

Information in response to this Item is incorporated by reference to (i) the biographical information relating to the Company's directors under the caption "Election of Directors" and the information relating to Section 16 compliance under the caption, "Section 16(a) Beneficial Ownership Reporting Compliance" in the Company's definitive Proxy Statement for its Annual Meeting of Stockholders to be held May 19, 2000 (the "Proxy Statement"), and (ii) the information under the caption "Executive Officers of the Registrant" in Part I hereof. The Company anticipates filing the Proxy Statement within 120 days after December 31, 1999.

ITEM 11. EXECUTIVE COMPENSATION

The information under the heading "Executive Compensation" and "Compensation of Directors" in the Proxy Statement is incorporated herein by reference.

ITEM 12. SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT

The information under the heading "Voting Securities and Principal Holders Thereof - Security Ownership of Certain Beneficial Owners and Management" in the Proxy Statement is incorporated herein by reference.

ITEM 13. CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS

The information under the heading "Certain Transactions" in the Proxy Statement is incorporated herein by reference.

PART IV

ITEM 14. EXHIBITS, FINANCIAL STATEMENT SCHEDULES AND REPORTS ON FORM 8-K

(a) THE FOLLOWING DOCUMENTS ARE FILED AS PART OF THIS REPORT:

1. FINANCIAL STATEMENTS

The following financial statements of OrthoLogic Corp. and Independent Auditors' Report are incorporated by reference from pages 17 through 29 of the Annual Report:

Balance Sheets - December 31, 1999 and 1998.

Statements of Operations - Each of the three years in the period ended December 31, 1999.

Statements of Comprehensive Income - Each of the three years in the period ended December 31, 1999.

Statements of Stockholders' Equity - Each of the three years in the period ended December 31, 1999.

Statements of Cash Flows - Each of the three years in the period ended December 31, 1999.

Notes to Financial Statements

2. FINANCIAL STATEMENT SCHEDULES

Valuation and Qualifying Accounts.

Allowance for doubtful accounts

Balance December 31, 1996		$ (8,595,000)
1997 Additions charged to expense	(11,246,229)	
1997 Deductions to allowance	8,470,705	
Balance December 31, 1997		(11,370,524)
1998 Additions charged to expense	(19,529,547)	
1998 Deductions to allowance	11,582,247	
Balance December 31, 1998		(19,317,824)
1999 Additions charged to expense	(18,800,728)	
1999 Deductions to allowance	22,615,832	
Balance December 31, 1999		$(15,502,720)

Allowance for inventory reserves

Balance December 31, 1996		$ (260,602)
1997 Additions charged to expense	(944,313)	
1997 Deductions to allowance	843,277	
Balance December 31, 1997		(361,638)
1998 Additions charged to expense	(1,239,181)	
1998 Deductions to allowance	852,421	
Balance December 31, 1998		(748,398)
1999 Additions charged to expense	(1,422,333)	
1999 Deductions to allowance	1,190,929	
Balance December 31, 1999		$ (979,802)

3. EXHIBITS AND MANAGEMENT CONTRACTS, AND COMPENSATORY PLANS AND ARRANGEMENTS

All management contracts and compensatory plans and arrangements are identified by footnote after the Exhibit Descriptions on the attached Exhibit Index.

(b) REPORTS ON FORM 8-K.

None.

(c) EXHIBITS

See the Exhibit Index immediately following the signature page of this report, which Index is incorporated herein by reference.

(d) FINANCIAL STATEMENTS AND SCHEDULES

See Item 14(a)(1) and (2) above.

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.

ORTHOLOGIC CORP.

Date: March 30, 2000

By /s/ Thomas R. Trotter

Thomas R. Trotter
President and Chief Executive Officer

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.

Signature	Title	Date
/s/ Thomas R. Trotter Thomas R. Trotter	President, Chief Executive Officer and Director (Principal Executive Officer)	March 30, 2000
/s/ John M. Holliman III John M. Holliman III	Chairman of the Board of Directors and Director	March 30, 2000
/s/ Fredric J. Feldman Fredric J. Feldman	Director	March 30, 2000
/s/ Elwood D. Howse, Jr. Elwood D. Howse, Jr.	Director	March 30, 2000
/s/ Stuart H. Altman Stuart H. Altman, Ph.D.	Director	March 30, 2000
/s/ Augustus A. White III Augustus A. White III, M.D.	Director	March 30, 2000
/s/ Terry D. Meier Terry D. Meier	Senior Vice President and Chief Financial Officer (Principal Financial and Accounting Officer)	March 30, 2000

ORTHOLOGIC CORP.
EXHIBIT INDEX TO REPORT ON FORM 10-K
FOR THE FISCAL YEAR ENDED DECEMBER 31, 1999
(FILE NO. 0-21214)

<TABLE>
<CAPTION>

Exhibit No.	Description	Incorporated by Reference To:	Filed Herewith
<S>	<C>	<C>	<C>
3.1	Amended and Restated Certificate of Incorporation	Exhibit 3.1 to the Company's Form 10-Q for the quarter ended March 31, 1997 ("March 1997 10-Q")	
3.2	Certificate of Designation in respect of Series A Preferred Stock	Exhibit 3.1 to Company's Form 10-Q for the quarter ended March 31, 1997 ("March 1997 10-Q")	
3.3	Bylaws of the Company	Exhibit 3.4 to Company's Amendment No. 2 to Registration Statement on Form S-1 (No. 33-47569) filed with the SEC on January 25, 1993 ("January 1993 S-1")	
4.1	Stock Purchase Warrant, dated September 20, 1995, issued to Registered Consulting Group, Inc.	Exhibit 4.6 to Company's Registration Statement on Form S-1 (No. 33-97438) filed with the SEC on September 27, 1995 ("1995 S-1")	
4.2	Stock Purchase Warrant dated October 15, 1996 issued to Registered Consulting Group, Inc.	Exhibit 4.7 to the Company's Form 10-K for the year ended December 31, 1996 ("1996 10-K")	
4.3	Rights Agreement dated as of March 4, 1997 between the Company and Bank of New York, and Exhibits A, B and C thereto	Exhibit 4.1 to the Company's Registration Statement on Form 8-A filed with the SEC on March 6, 1997	
4.4	1987 Stock Option Plan of the Company, as amended and approved by stockholders (1)	Exhibit 4.4 to the Company's Form 10-Q for the quarter ended June 30, 1997 ("June 1997 10-Q")	
4.5	1987 Stock Option Plan of the Company(1)	Exhibit 4.5 to the Company's June 1997 10-Q	
4.6	Stock Purchase Warrant dated March 2, 1998 issued to Silicon Valley Bank	Exhibit 4.10 to the Company's 1997 10-K	
4.7	Antidilution Agreement dated March 2, 1998 by and between the Company and Silicon Valley Bank	Exhibit 4.11 to the Company's 1997 10-K	

4.8	Amendment to Stock Purchase Warrant dated May 12, 1998 issued to Silicon Valley Bank	Exhibit 4.1 to the Company's form 10-Q for the quarter ended March 31, 1998
4.9	Form of Warrant	Exhibit 4.1 to the Company's Form 8-K filed on July 13, 1998
4.10	Registration Rights Agreement	Exhibit 4.2 to the Company's Form 8-K filed on July 13, 1998
10.1	License Agreement dated September 3, 1987 between the Company and Life Resonances, Inc.	Exhibit 10.6 to January 1993 S-1
10.2	Invention, Confidential Information and Non-Competition Agreement dated January 10, 1989 between the Company and Frank P. Magee	Exhibit 10.11 to January 1993 S-1
10.3	Form of Indemnification Agreement*	Exhibit 10.16 to January 1993 S-1
10.4	License Agreement dated December 2, 1992 between Orthotic Limited Partnership and Company	Exhibit 10.22 to January 1993 S-1
10.5	Consulting Agreement dated May 1, 1990 between Augustus A. White III and the Company(1)	Exhibit 10.11 to the Company's September 30, 1994 Form 10-Q
10.6	Employment Agreement by and between MaryAnn G. Miller and the Company effective as of December 1, 1996 (1)	Exhibit 10.8 to the Company's March 1997 10-Q
10.7	Co-promotion Agreement dated June 23, 1997 by and between the Company and Sanofi Pharmaceuticals, Inc.	Exhibit 10.1 to the Company's June 1997 10-Q

</TABLE>

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Exhibit No.	Description	Incorporated by Reference To:	Filed Herewith
<S>	<C>	<C>	<C>
10.8	Single-tenant Lease-net dated June 12, 1997 by and between the Company and Chamberlain Development, L.L.C.	Exhibit 10.2 to the Company's Form 10-Q for the quarter ended September 30, 1997 ("September 1997 10-Q")	
10.9	Employment Agreement dated October 20, 1997 by and between the Company and Thomas R. Trotter, including Letter of Incentive Option Grant, OrthoLogic Corp. 1987 Stock Option Plan (1)	Exhibit 10.3 to the Company's September 1997 10-Q	

10.10	Employment Agreement dated October 17, 1997 by and between the Company and Frank P. Magee (1)	Exhibit 10.4 to the Company's September 1997 10-Q	
10.11	Employment Agreement effective as of December 15, 1997 by and between the Company and William C. Rieger (1)	Exhibit 10.40 to the Company's 1997 10-K	
10.12	Employment Agreement effective as of March 16, 1998 by and between the Company and Terry D. Meier (1)	Exhibit 10.42 to the Company's 1997 10-K	
10.13	Registration Rights Agreement dated March 2, 1998 by and between the Company and Silicon Valley Bank	Exhibit 10.45 to the Company's 1997 10-K	
10.14	Licensing Agreement with Chrysalis Biotechnolgoy, Inc.	Exhibit 10.1 to the Company's September 1998 10-Q	
10.15	1998 Management Bonus Program	Exhibit 10.2 to the Company's September 1998 10-Q	
10.16	Securities Purchase Agreement	Exhibit 10.1 to the Company's Form 8-K filed on July 13, 1998	
10.17	First Amendatory Agreement to March 4, 1997 Rights Agreement	Exhibit 10.1 to the Company's Form 8-K filed August 24, 1999	
10.18	Credit and Security Agreement between the Company and Wells Fargo Business Credit, Inc. dated February 28, 2000		X
10.19	Lease Extension and Amendment Agreement dated September 29, 1998 between the Company and the Heritage Corp. for the Pickering property		X
11.1	Statement of Computation of Net Income (Loss) per Weighted Average Number of Common Shares Outstanding		X
13.1	Portions of 1999 Annual Report to Stockholders		X
21.1	Subsidiaries of Registrant	Exhibit 21.1 to the Company's 1997 10-K	
23.1	Consent of Deloitte & Touche LLP		X
23.2	Independent Auditors' Report		X
27	Financial Data Schedule		X

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(1) Management contract or compensatory plan or arrangement

* The Company has entered into a separate indemnification agreement with each of its current direct and executive officers that differ only in party names and dates. Pursuant to the instructions accompanying Item 601 of Regulation S-K, the Company has filed the form of such indemnification agreement.

CREDIT AND SECURITY AGREEMENT

Dated as of February 28, 2000

ORTHOLOGIC CORP., a Delaware corporation (the "Borrower"), and WELLS FARGO BUSINESS CREDIT, INC., a Minnesota corporation (the "Lender"), hereby agree as follows:

ARTICLE I
DEFINITIONS

SECTION 1.1 DEFINITIONS. For all purposes of this Agreement, except as otherwise expressly provided or unless the context otherwise requires:

(a) the terms defined in this Article have the meanings assigned to them in this Article, and include the plural as well as the singular; and

(b) all accounting terms not otherwise defined herein have the meanings assigned to them in accordance with GAAP.

"Accounts" means all of the Borrower's accounts, as such term is defined in the UCC, including without limitation the aggregate unpaid obligations of customers and other account debtors to the Borrower arising out of the sale or lease of goods or rendition of services by the Borrower on an open account or deferred payment basis.

"Advance" means a Revolving Advance.

"Affiliate" or "Affiliates" means any Person controlled by, controlling or under common control with the Borrower, including (without limitation) any Subsidiary of the Borrower. For purposes of this definition, "control," when used with respect to any specified Person, means the power to direct the management and policies of such Person, directly or indirectly, whether through the ownership of voting securities, by contract or otherwise.

"Agreement" means this Credit and Security Agreement, as amended, supplemented or restated from time to time.

"Allowed Investments" means Borrower's Co-Promotion Agreement with Sanofi Pharmaceuticals, Inc. and Borrower's Minority Equity Investment with Chrysalis Biotechnology, Inc.

"Availability" means the positive difference, if any, between (i) the Borrowing Base, and (ii) the outstanding principal balance of the Revolving Note.

"Banking Day" means a day other than a Saturday, Sunday or other day on which banks are generally not open for business in Phoenix, Arizona.

"Borrowing Base" means, at any time the lesser of:

(a) the Maximum Line; or

(b) subject to change from time to time in the Lender's sole discretion if the nature of the Collateral changes, 75% of Eligible Accounts.

"Capital Expenditures" for a period means any expenditure of money for the lease, purchase or other acquisition of any capital asset, or for the lease of any other asset whether payable currently or in the future.

"Collateral" means all of the Borrower's Equipment, General Intangibles (except Patents unless and until the occurrence of an Event of Default), Inventory, Accounts, Receivables, all sums on deposit in any Collection Account, and any items in any lockbox; together with (i) all substitutions and replacements for and products of any of the foregoing; (ii) proceeds of any and all of the foregoing; (iii) in the case of all tangible goods, all accessions; (iv) all accessories, attachments, parts, equipment and repairs now or hereafter attached or affixed to or used in connection with any tangible goods; and (v) all warehouse receipts, bills of lading and other documents of title now or hereafter covering such goods.

"Collection Account" has the meaning given in Section 4.3.

"Commitment" means the Lender's commitment to make Advances to or for the Borrower's account pursuant to Article II.

"Credit Facility" means the credit facility being made available to the Borrower by the Lender pursuant to Article II.

"Debt" of any Person means all items of indebtedness or liability which in accordance with GAAP would be included in determining total liabilities as shown on the liabilities side of a balance sheet of that Person as of the date as of which Debt is to be determined. For purposes of determining a Person's aggregate Debt at any time, "Debt" shall also include the aggregate payments required to be made by such Person at any time under any lease that is considered a capitalized lease under GAAP.

"Debt to Tangible Net Worth Ratio" as of a given date means the ratio of the Borrower's Debt to the Borrower's Tangible Net Worth.

"Default" means an event that, with giving of notice or passage of time or both, would constitute an Event of Default.

"Default Period" means any period of time beginning on the first day of any month during which a Default or Event of Default has occurred and ending on the date the Lender notifies the Borrower in writing that such Default or

Event of Default has been cured or waived.

"Default Rate" means an annual rate equal to three percent (3%) over the Floating Rate, which rate shall change when and as the Floating Rate changes.

"ERISA" means the Employee Retirement Income Security Act of 1974, as amended.

"Eligible Accounts" means all unpaid Accounts, net of any credits, except the following shall not in any event be deemed Eligible Accounts:

(i) That portion of Accounts over 120 days past invoice date;

(ii) That portion of Accounts that is disputed or subject to a claim of offset or a contra account;

(iii) That portion of Accounts not yet earned by the final delivery of goods or rendition of services, as applicable, by the Borrower to the customer;

(iv) Accounts owed by any unit of government (including without limitation through the Medicare/Medicaid programs), whether foreign or domestic (provided, however, that there shall be included in Eligible Accounts that portion of Accounts owed by such units of government for which the Borrower has provided evidence satisfactory to the Lender that (A) the Lender has a first priority perfected security interest and (B) such Accounts may be enforced by the Lender directly against such unit of government under all applicable laws);

(v) Accounts owed by an account debtor located outside the United States which are not (A) backed by a bank letter of credit naming the Lender as beneficiary or assigned to the Lender, in the Lender's possession and acceptable to the Lender in all respects, in its sole discretion, or (B) covered by a foreign receivables insurance policy acceptable to the Lender in its sole discretion;

(vi) Accounts owed by an account debtor that is insolvent, the subject of bankruptcy proceedings or has gone out of business;

(vii) Accounts owed by a Subsidiary, Affiliate, officer or employee of the Borrower;

(viii) Accounts not subject to a duly perfected security interest in the Lender's favor or which are subject to any lien, security interest or claim in favor of any Person other than the Lender including without limitation any payment or performance bond;

(ix) That portion of Accounts that has been restructured, extended, amended or modified;

(x) That portion of Accounts that constitutes advertising, finance charges, service charges or sales or excise taxes; and

(xi) Accounts, or portions thereof, otherwise deemed ineligible by the Lender in its sole discretion.

"Environmental Laws" has the meaning specified in Section 5.12.

"Equipment" means all of the Borrower's equipment, as such term is defined in the UCC, whether now owned or hereafter acquired, including but not limited to all present and future machinery, vehicles, furniture, fixtures, manufacturing equipment, shop equipment, office and recordkeeping equipment, parts, tools, supplies, and including specifically (without limitation) the goods described in any equipment schedule or list herewith or hereafter furnished to the Lender by the Borrower.

"Event of Default" has the meaning specified in Section 8.1.

"Existing Lockbox Agreement" has the meaning specified in Section 6.10.

"Floating Rate" means an annual rate equal to the Prime Rate, which annual rate shall change when and as the Prime Rate changes.

"Funding Date" has the meaning given in Section 2.1.

"GAAP" means generally accepted accounting principles, applied on a basis consistent with the accounting practices applied in the financial statements described in Section 5.5, except for any change in accounting practices to the extent that, due to a promulgation of the Financial Accounting Standards Board changing or implementing any new accounting standard, the Borrower either (i) is required to implement such change, or (ii) for future periods will be required to and for the current period may in accordance with generally accepted accounting principles implement such change, for its financial statements to be in conformity with generally accepted accounting principles (any such change is herein referred to as a "Required GAAP Change"), provided that (1) the Borrower shall fully disclose in such financial statements any such Required GAAP Change and the effects of the Required GAAP Change on the Borrower's income, retained earnings or other accounts, as applicable, and (2) the Borrower's financial covenants set forth in Sections 6.12 through 6.13, and 7.10 shall be adjusted as necessary to reflect the effects of such Required GAAP Change.

"General Intangibles" means all of the Borrower's general intangibles, as such term is defined in the UCC, whether now owned or hereafter acquired, including (without limitation) all Patents, copyrights, trademarks, trade names, trade secrets, customer or supplier lists and contracts, manuals, operating instructions, permits, franchises, the right to use the Borrower's name, and the

goodwill of the Borrower's business.

"Hazardous Substance" has the meaning given in Section 5.12.

"Inventory" means all of the Borrower's inventory, as such term is defined in the UCC, whether now owned or hereafter acquired, whether consisting of whole goods, spare parts or components, supplies or materials, whether acquired, held or furnished for sale, for lease or under service contracts or for manufacture or processing, and wherever located.

"Loan Documents" means this Agreement, the Note and the Security Documents.

"Lockbox Agreement" has the meaning specified in Section 6.10.

"Maturity Date" means February 28, 2003.

"Maximum Line" means on any given day the lesser of (i) $10,000,000.00, or (ii) an amount equal to 1.25 multiplied by the total cash (resulting from continuing operations) received by the Borrower during the immediately preceding 60 days. The Maximum Line may be reduced pursuant to Section 2.6, in which event "Maximum Line" means the amount to which said amount is reduced.

"Net Income" means fiscal year-to-date after-tax net income from continuing operations as determined in accordance with GAAP.

"Net Loss" means fiscal year-to-date after-tax net loss from continuing operations as determined in accordance with GAAP.

"Note" means the Revolving Note.

"Obligations" means the Note and each and every other debt, liability and obligation of every type and description which the Borrower may now or at any time hereafter owe to the Lender, whether such debt, liability or obligation now exists or is hereafter created or incurred, whether it arises in a transaction involving the Lender alone or in a transaction involving other creditors of the Borrower, and whether it is direct or indirect, due or to become due, absolute or contingent, primary or secondary, liquidated or unliquidated, or sole, joint, several or joint and several, and including specifically, but not limited to, all indebtedness of the Borrower arising under this Agreement, the Note or any other loan or credit agreement or guaranty between the Borrower and the Lender, whether now in effect or hereafter entered into.

"Patents" means all present and future patents and patent applications.

"Permitted Lien" has the meaning given in Section 7.1.

"Person" means any individual, corporation, partnership, joint venture, limited liability company, association, joint-stock company, trust, unincorporated organization or government or any agency or political subdivision thereof.

"Plan" means an employee benefit plan or other plan maintained for the Borrower's employees and covered by Title IV of ERISA.

"Premises" means all premises where the Borrower conducts its business and has any rights of possession, including (without limitation) the premises legally described in Exhibit C attached hereto.

"Prime Rate" means the rate of interest publicly announced from time to time by Wells Fargo Bank, N.A. as its "prime rate" or, if such bank ceases to announce a rate so designated, any similar successor rate designated by the Lender.

"Principal Premises" means Borrower's Premises in Phoenix, Arizona and Toronto, Ontario, Canada.

"Quick Assets" means, on any date, the Borrower's consolidated, unrestricted cash, cash equivalents, net billed accounts receivable and investments with maturities of fewer than 12 months determined according to GAAP.

"Quick Ratio" means as of a given date the ratio of Borrower's Quick Assets divided by Borrower's current liabilities, as determined in accordance with GAAP.

"Receivables" means each and every right of the Borrower to the payment of money, whether such right to payment now exists or hereafter arises, whether such right to payment arises out of a sale, lease or other disposition of goods or other property, out of a rendering of services, out of a loan, out of the overpayment of taxes or other liabilities, or otherwise arises under any contract or agreement, whether such right to payment is created, generated or earned by the Borrower or by some other person who subsequently transfers such person's interest to the Borrower, whether such right to payment is or is not already earned by performance, and howsoever such right to payment may be evidenced, together with all other rights and interests (including all liens and security interests) which the Borrower may at any time have by law or agreement against any account debtor or other obligor obligated to make any such payment or against any property of such account debtor or other obligor; all including but not limited to all present and future accounts, contract rights, loans and obligations receivable, chattel papers, bonds, notes and other debt instruments, tax refunds and rights to payment in the nature of general intangibles.

"Reportable Event" shall have the meaning assigned to that term in Title IV of ERISA.

"Revolving Advance" has the meaning given in Section 2.1.

"Revolving Note" means the Borrower's revolving promissory note, payable to the order of the Lender in substantially the form of Exhibit A hereto, as the same may hereafter be amended, supplemented or restated from time to time, and any note or notes issued in substitution therefor, as the same may hereafter be amended, supplemented or restated from time to time and any note or notes issued in substitution therefor.

"Security Documents" means this Agreement, the Collection Account Agreement, the Lockbox Agreement, and any other document delivered to the Lender from time to time to secure the Obligations, as the same may hereafter be amended, supplemented or restated from time to time.

"Security Interest" has the meaning given in Section 3.1.

"Subordinated Debt" is debt incurred by Borrower subordinated to Borrower's debt to Lender (and identified as subordinated by Borrower and Lender).

"Subsidiary" means any corporation of which more than 50% of the outstanding shares of capital stock having general voting power under ordinary circumstances to elect a majority of the board of directors of such corporation, irrespective of whether or not at the time stock of any other class or classes shall have or might have voting power by reason of the happening of any contingency, is at the time directly or indirectly owned by the Borrower, by the Borrower and one or more other Subsidiaries, or by one or more other Subsidiaries.

"Tangible Net Worth" means, on any date, the consolidated total assets of Borrower and its Subsidiaries MINUS, (i) any amounts attributable to (a) goodwill, (b) intangible items such as unamortized debt discount and expense, Patents, trade and service marks and names, copyrights and research and development expenses except prepaid expenses, and (c) reserves not already deducted from assets, AND (ii) Total Liabilities plus Subordinated Debt.

"Termination Date" means the earliest of (i) the Maturity Date, (ii) the date the Borrower terminates the Credit Facility, or (iii) the date the Lender demands payment of the Obligations after an Event of Default pursuant to Section 8.2.

"Threshold Amount" means the lesser of (i) $2,000,000.00, or (ii) an amount equal to the value of 20% of Eligible Accounts as set forth in the most recent collateral reporting complying with the requirements of Section 6.1 below.

"Threshold Event" means the earlier to occur of (i) Borrower's request for an Advance which Lender has been informed by Borrower shall cause the

Threshold Amount to be outstanding for thirty days or more, or (ii) the date when outstanding Revolving Advances shall have exceeded the Threshold Amount for thirty consecutive days.

"Total Liabilities" is on any day, obligations that should, under GAAP, be classified as liabilities on Borrower's consolidated balance sheet, including all indebtedness, and current portion Subordinated Debt allowed to be paid, but excluding all other Subordinated Debt.

"UCC" means the Uniform Commercial Code as in effect from time to time in the state designated in Section 9.13 as the state whose laws shall govern this Agreement, or in any other state whose laws are held to govern this Agreement or any portion hereof.

"Wells Fargo Bank, N.A." means Wells Fargo Bank, National Association.

SECTION 1.2 CROSS REFERENCES. All references in this Agreement to Articles, Sections and subsections, shall be to Articles, Sections and subsections of this Agreement unless otherwise explicitly specified.

ARTICLE II
Amount and Terms of the Credit Facility

SECTION 2.1 REVOLVING ADVANCES. The Lender agrees, on the terms and subject to the conditions herein set forth, to make advances to the Borrower from time to time from the date all of the conditions set forth in Section 4.1 are satisfied (the "Funding Date") to the Termination Date, on the terms and subject to the conditions herein set forth (the "Revolving Advances"). The Lender shall have no obligation to make a Revolving Advance if, after giving effect to such requested Revolving Advance, the sum of the outstanding and unpaid Revolving Advances would exceed the Borrowing Base. The Borrower's obligation to pay the Revolving Advances shall be evidenced by the Revolving Note and shall be secured by the Collateral as provided in Article III. Within the limits set forth in this Section 2.1, the Borrower may borrow, prepay pursuant to Section 2.6 and reborrow. The Borrower agrees to comply with the following procedures in requesting Revolving Advances under this Section 2.1:

(a) The Borrower shall make each request for a Revolving Advance to the Lender before 11:00 a.m. (Phoenix time) of the day of the requested Revolving Advance, provided however, that in the event that the requested Revolving Advance shall cause a Threshold Event, the Borrower shall make such request for a Revolving Advance to the Lender before 11:00 a.m. (Phoenix time)

on that date which is thirty (30) days prior to the date of the disbursement of the requested Revolving Advance. Requests may be made in writing or by telephone, specifying the date of the requested Revolving Advance and the amount thereof. Each request shall be by (i) any officer of the Borrower; or (ii) any person designated as the Borrower's agent by any officer of the Borrower in a writing delivered to the Lender; or (iii) any person whom the Lender reasonably

believes to be an officer of the Borrower or such a designated agent.

(b) Upon fulfillment of the applicable conditions set forth in Article IV, the Lender shall disburse the proceeds of the requested Revolving Advance by crediting the same to the Borrower's demand deposit account maintained with Wells Fargo Bank, N.A. unless the Lender and the Borrower shall agree in writing to another manner of disbursement. Upon the Lender's request, the Borrower shall promptly confirm each telephonic request for an Advance by executing and delivering an appropriate confirmation certificate to the Lender. The Borrower shall repay all Advances even if the Lender does not receive such confirmation and even if the person requesting an Advance was not in fact authorized to do so. Any request for an Advance, whether written or telephonic, shall be deemed to be a representation by the Borrower that the conditions set forth in Section 4.2 have been satisfied as of the time of the request.

SECTION 2.2 INTEREST; DEFAULT INTEREST; PARTICIPATIONS; USURY. Interest accruing on the Note shall be due and payable in arrears on the first day of each month.

(a) REVOLVING NOTE. Except as set forth in Sections 2.2(b) and 2.2(d), the outstanding principal balance of the Revolving Note shall bear interest at the Floating Rate.

(b) DEFAULT INTEREST RATE. At any time during any Default Period, commencing with the first day of the first month following the Default, in the Lender's sole discretion and without waiving any of its other rights and remedies, the principal of the Advances outstanding from time to time shall bear interest at the Default Rate, effective for any periods designated by the Lender from time to time during that Default Period.

(c) PARTICIPATIONS. If any Person shall acquire a participation in the Advances under this Agreement, the Borrower shall be obligated to the Lender to pay the full amount of all interest calculated under Section 2.2(a), along with all other fees, charges and other amounts due under this Agreement, regardless if such Person elects to accept interest with respect to its participation at a lower rate than the Floating Rate, or otherwise elects to accept less than its pro rata share of such fees, charges and other amounts due under this Agreement.

(d) USURY. In any event no rate change shall be put into effect which would result in a rate greater than the highest rate permitted by law. Notwithstanding anything to the contrary contained in any Loan Document, all agreements which either now are or which shall become agreements between the Borrower and the Lender are hereby limited so that in no contingency or event whatsoever shall the total liability for payments in the nature of interest, additional interest and other charges exceed the applicable limits imposed by the usury laws of the State of California. If any payments in the nature of interest, additional interest and other charges made under any Loan Document are held to be in excess of the applicable limits imposed by the usury laws of the State of California, it is agreed that any such amount held to be in excess shall be considered payment of principal hereunder, and the indebtedness evidenced hereby shall be reduced by such amount so that the total liability for

payments in the nature of interest, additional interest and other charges shall not exceed the applicable limits imposed by the usury laws of the State of California, in compliance with the desires of the Borrower and the Lender. This provision shall never be superseded or waived and shall control every other provision of the Loan Documents and all agreements between the Borrower and the Lender, or their successors and assigns.

(e) SAVINGS CLAUSE. The Borrower agrees that the interest rate contracted for includes the interest rate set forth herein plus any other charges or fees set forth herein and costs and expenses incident to this transaction paid by the Borrower to the extent that the same are deemed interest under applicable law.

SECTION 2.3 FEES.

(a) ORIGINATION FEE. The Borrower hereby agrees to pay the Lender a fully earned and non-refundable origination fee of $50,000.00 due and payable upon the execution of this Agreement.

(b) UNUSED LINE FEE. For the purposes of this Section 2.3(b), "Unused Amount" means the Maximum Line reduced by outstanding Revolving Advances. The Borrower agrees to pay to the Lender an unused line fee at the rate of one-quarter of one percent (0.25%) per annum on the average daily Unused Amount from the date of this Agreement to and including the Termination Date, due and payable monthly in arrears on the first day of the month and on the Termination Date.

(c) COMMITMENT FEE. The Borrower hereby agrees to pay the Lender an annual commitment fee in the amount of $50,000.00 due and payable commencing on the first anniversary of the Funding Date, and continuing on each subsequent anniversary of the Funding Date.

(d) ADMINISTRATION FEE. The Borrower hereby agrees to pay the Lender an administration fee in the amount of $1,000.00 per month commencing on the first day of the first calendar month after the initial Revolving Advance and on the first day of each month thereafter.

(e) AUDIT FEES. The Borrower hereby agrees to pay the Lender, on demand, audit fees in connection with any audits or inspections conducted by the Lender of any Collateral or the Borrower's operations or business at the rates established from time to time by the Lender as its audit fees (which fees are currently $75.00 per hour per auditor), together with all actual out-of-pocket costs and expenses incurred in conducting any such audit or inspection; PROVIDED, HOWEVER, that Lender will not perform such audits until either (i) a Default, or (ii) the occurrence of the first Threshold Event.

SECTION 2.4 COMPUTATION OF INTEREST AND FEES; WHEN INTEREST DUE AND PAYABLE. Interest accruing on the outstanding principal balance of the Advances

and fees hereunder outstanding from time to time shall be computed on the basis of actual number of days elapsed in a year of 360 days. Interest shall be payable in arrears on the first day of each month and on the Termination Date.

SECTION 2.5 [INTENTIONALLY OMITTED]

SECTION 2.6 VOLUNTARY PREPAYMENT; TERMINATION OF CREDIT FACILITY BY THE BORROWER; PERMANENT REDUCTION OF THE MAXIMUM LINE; WAIVER OF REDUCTION AND TERMINATION FEES. Except as otherwise provided herein, the Borrower may terminate the Credit Facility or prepay the Advances in whole at any time or from time to time in part, and, subject to payment and performance of all Obligations and termination of the Credit Facility, the Lender shall release or terminate the Security Interest and the Security Documents to which the Borrower is entitled by law.

(a) TERMINATION BY BORROWER. The Borrower may terminate the Credit Facility at any time by (i) giving at least 30 days' prior written notice to the Lender of the Borrower's intention to terminate the Credit Facility; and (ii) paying the Lender fees in accordance with Subsection (b) if the Borrower terminates the Credit Facility effective as of any date other than a Maturity Date.

(b) PERMANENT REDUCTION OF MAXIMUM LINE. The Borrower may at any time and from time to time, upon at least 30 days' prior written notice to the Lender, permanently reduce in part or completely the Maximum Line or terminate the Credit Facility in accordance with the following provisions:

(i) The Borrower may not reduce the Maximum Line to an amount less than the then-aggregate outstanding balance of the Revolving Advances.

(ii) If a reduction of the Maximum Line occurs at any time other than the Maturity Date, the Borrower shall pay to the Lender a premium in an amount equal to one-half of one percent (0.5%) of the reduction.

(iii) Any reduction in the Maximum Line must be in an amount not less than $1,000,000.00 or an integral multiple thereof.

(iv) If the Borrower reduces the Maximum Line to zero, all Obligations shall be immediately due and payable.

(c) WAIVER OF REDUCTION FEES. The Borrower will not be required to pay the fees otherwise due under Subsection (b) if such reduction is requested is made because of increased cash flow generated from the Borrower's operations or refinancing by an affiliate of the Lender.

SECTION 2.7 MANDATORY PREPAYMENT. Without notice or demand, if the outstanding principal balance of the Revolving Advances shall at any time exceed the Borrowing Base, the Borrower shall immediately prepay the Revolving Advances to the extent necessary to eliminate such excess. Any payment received by the

Lender under this Section 2.7 or under Section 2.6 may be applied to the Obligations, in such order and in such amounts as the Lender, in its discretion, may from time to time determine. For each day or portion thereof that the Revolving Advances shall exceed the Borrowing Base, the Borrower shall pay to the Lender an overadvance charge (which charge shall be in addition to and not in lieu of any other interest, fees, or charges payable by Borrower hereunder) in the amount of $100.00; provided, however, that if such day occurs during a Default Period, the overadvance charge for such day shall be $200.00.

SECTION 2.8 PAYMENT. All payments to the Lender shall be made in immediately available funds and shall be applied to the Obligations upon receipt by the Lender. Notwithstanding anything in Section 2.1, the Borrower hereby authorizes the Lender, in its discretion at any time or from time to time without the Borrower's request and even if the conditions set forth in Section 4.2 would not be satisfied, to make a Revolving Advance in an amount equal to the portion of the Obligations from time to time due and payable.

SECTION 2.9 PAYMENT ON NON-BANKING DAYS. Whenever any payment to be made hereunder shall be stated to be due on a day which is not a Banking Day, such payment may be made on the next succeeding Banking Day, and such extension of time shall in such case be included in the computation of interest on the Advances or the fees hereunder, as the case may be.

SECTION 2.10 USE OF PROCEEDS. The Borrower shall use the proceeds of Advances for ordinary working capital purposes and to repay all outstanding indebtedness of the Borrower owed to Silicon Valley Bank.

SECTION 2.11 LIABILITY RECORDS. The Lender may maintain from time to time, at its discretion, liability records as to the Obligations. All entries made on any such record shall be presumed correct until the Borrower establishes the contrary. Upon the Lender's demand, the Borrower will admit and certify in writing the exact principal balance of the Obligations that the Borrower then asserts to be outstanding. Any billing statement or accounting rendered by the Lender shall be conclusive and fully binding on the Borrower unless the Borrower gives the Lender specific written notice of exception within 30 days after receipt.

ARTICLE III
SECURITY INTEREST; OCCUPANCY; SETOFF

SECTION 3.1 GRANT OF SECURITY INTEREST. The Borrower hereby pledges, assigns and grants to the Lender a security interest (collectively referred to as the "Security Interest") in the Collateral, as security for the payment and performance of the Obligations.

SECTION 3.2 NOTIFICATION OF ACCOUNT DEBTORS AND OTHER OBLIGORS. The Lender may at any time (upon a Default or the occurrence of a Threshold Event) notify any account debtor or other person obligated to pay the amount due that such right to payment has been assigned or transferred to the Lender for security and

shall be paid directly to the Lender. The Borrower will join in giving such notice if the Lender so requests. At any time after the Borrower or the Lender gives such notice to an account debtor or other obligor, the Lender may, but need not, in the Lender's name or in the Borrower's name, (a) demand, sue for, collect or receive any money or property at any time payable or receivable on account of, or securing, any such right to payment, or grant any extension to, make any compromise or settlement with or otherwise agree to waive, modify, amend or change the obligations (including collateral obligations) of any such account debtor or other obligor; and (b) as the Borrower's agent and attorney-in-fact, notify the United States Postal Service to change the address for delivery of the Borrower's mail to any address designated by the Lender, otherwise intercept the Borrower's mail, and receive, open and dispose of the Borrower's mail, applying all Collateral as permitted under this Agreement and holding all other mail for the Borrower's account or forwarding such mail to the Borrower's last known address.

SECTION 3.3 ASSIGNMENT OF INSURANCE. As additional security for the payment and performance of the Obligations, the Borrower hereby assigns to the Lender any and all monies (including, without limitation, proceeds of insurance and refunds of unearned premiums) due or to become due under, and all other rights of the Borrower with respect to, any and all policies of insurance now or at any time hereafter covering the Collateral or any evidence thereof or any business records or valuable papers pertaining thereto, and the Borrower hereby directs the issuer of any such policy to pay all such monies directly to the Lender. At any time, if a Default Period then exists, the Lender may (but need not), in the Lender's name or in the Borrower's name, execute and deliver proof of claim, receive all such monies, endorse checks and other instruments representing payment of such monies, and adjust, litigate, compromise or release any claim against the issuer of any such policy.

SECTION 3.4 OCCUPANCY.

(a) The Borrower hereby irrevocably grants to the Lender the right to take possession of the Premises at any time during each Default Period.

(b) The Lender may use the Premises only to hold, process, manufacture, sell, use, store, liquidate, realize upon or otherwise dispose of goods that are Collateral and for other purposes that the Lender may in good faith deem to be related or incidental purposes.

(c) The Lender's right to hold the Premises shall cease and terminate upon the earlier of (i) payment in full and discharge of all Obligations and termination of the Commitment, (ii) final sale or disposition of all goods constituting Collateral and delivery of all such goods to purchasers, or (iii) the end of the applicable Default Period.

(d) The Lender shall not be obligated to pay or account for any rent or other compensation for the possession, occupancy or use of any of the Premises; provided, however, that if the Lender does pay or account for any rent

or other compensation for the possession, occupancy or use of any of the Premises, the Borrower shall reimburse the Lender promptly for the full amount thereof. In addition, the Borrower will pay, or reimburse the Lender for, all taxes, fees, duties, imposts, charges and expenses at any time incurred by or imposed upon the Lender by reason of the execution, delivery, existence, recordation, performance or enforcement of this Agreement or the provisions of this Section 3.4.

SECTION 3.5 LICENSE. The Borrower hereby grants to the Lender a non-exclusive, worldwide and royalty-free license to use or otherwise exploit all trademarks, franchises, trade names, copyrights and patents of the Borrower for the purpose of selling, leasing or otherwise disposing of any or all Collateral during any Default Period.

SECTION 3.6 FINANCING STATEMENT. A carbon, photographic or other reproduction of this Agreement or of any financing statements signed by the Borrower is sufficient as a financing statement and may be filed as a financing statement in any state to perfect the security interests granted hereby. For this purpose, the following information is set forth:

Name and address of Debtor:
OrthoLogic Corp.
1275 West Washington Street
Tempe, AZ 85281

Federal Tax Identification No. 86-0585310

Name and address of Secured Party:
Wells Fargo Business Credit, Inc.
100 West Washington Street, 7th Floor
MAC S4101-076
Phoenix, AZ 85003

Federal Tax Identification No. 41-1237652

SECTION 3.7 SETOFF. The Borrower agrees that the Lender may at any time or from time to time, at its sole discretion and without demand and without notice to anyone, setoff any liability owed to the Borrower by the Lender, whether or not due, against any Obligation, whether or not due. In addition, each other Person holding a participating interest in any Obligations (so long as Borrower has been made aware of such participation) shall have the right to appropriate or setoff any deposit or other liability then owed by such Person to the Borrower, whether or not due, and apply the same to the payment of said participating interest, as fully as if such Person had lent directly to the Borrower the amount of such participating interest.

ARTICLE IV
CONDITIONS OF LENDING

SECTION 4.1 CONDITIONS PRECEDENT TO THE INITIAL REVOLVING ADVANCE. The Lender's obligation to make the initial Revolving Advance hereunder shall be subject to the conditions precedent that (i) after giving effect to the initial Revolving Advance there is not less than $1,500,000.00 in excess Availability, and (ii) the Lender shall have received all of the following, each in form and substance satisfactory to the Lender:

(a) This Agreement, properly executed by the Borrower.

(b) The Note, properly executed by the Borrower.

(c) A true and correct copy of any and all leases pursuant to which the Borrower is leasing the Principal Premises, together with a landlord's disclaimer and consent with respect to the lease for the principal premises in Phoenix, Arizona.

(d) A true and correct copy of any and all agreements pursuant to which the Borrower's property at its Principal Premises is in the possession of any Person other than the Borrower, together with, (i) an acknowledgment and waiver of liens from each subcontractor who has possession of the Borrower's goods from time to time, (ii) UCC financing statements sufficient to protect the Borrower's and the Lender's interests in such goods, and (iii) UCC searches showing that no other secured party has filed a financing statement covering such Person's property other than the Borrower, or if there exists any such secured party, evidence that each such secured party has received notice from the Borrower and the Lender sufficient to protect the Borrower's and the Lender's interests in the Borrower's goods from any claim by such secured party.

(e) Current searches of appropriate filing offices showing that (i) no state or federal tax liens have been filed and remain in effect against the Borrower, (ii) no financing statements or assignments of patents, trademarks or copyrights have been filed and remain in effect against the Borrower except those financing statements and assignments of patents, trademarks or copyrights relating to Permitted Liens or to liens held by Persons who have agreed in writing that upon receipt of proceeds of the Advances, they will deliver UCC releases and/or terminations and releases of such assignments of patents, trademarks or copyrights satisfactory to the Lender, and (iii) the Lender has duly filed all financing statements necessary to perfect the Security Interest, to the extent the Security Interest is capable of being perfected by filing.

(f) A certificate of the Borrower's Secretary or Assistant Secretary certifying as to (i) the resolutions of the Borrower's directors and, if required, shareholders, authorizing the execution, delivery and performance of the Loan Documents, (ii) the Borrower's articles of incorporation and bylaws, and (iii) the signatures of the Borrower's officers or agents authorized to execute and deliver the Loan Documents and other instruments, agreements and certificates, including Advance requests, on the Borrower's behalf.

(g) A current certificate issued by the Secretary of State of

Delaware, certifying that the Borrower is in compliance with all applicable organizational requirements of the State of Delaware.

(h) Evidence that the Borrower is duly licensed or qualified to transact business in Arizona and Ontario, Canada.

(i) A certificate of an officer of the Borrower confirming, in his corporate capacity, the representations and warranties set forth in Article V.

(j) An opinion of counsel to the Borrower, addressed to the Lender.

(k) Certificates of the insurance required hereunder, with all hazard insurance containing a lender's loss payable endorsement in the Lender's favor and with all liability insurance naming the Lender as an additional insured.

(l) Payment of the fees and commissions due through the date of the initial Advance under Section 2.3 and expenses incurred by the Lender through such date and required to be paid by the Borrower under Section 9.6, including all legal expenses incurred through the date of this Agreement.

(m) Such other documents as the Lender in its sole discretion may require.

SECTION 4.2 CONDITIONS PRECEDENT TO ALL ADVANCES. The Lender's obligation to make each Advance shall be subject to the further conditions precedent that on such date:

(a) the representations and warranties contained in Article V are correct on and as of the date of such Advance as though made on and as of such date, except to the extent that such representations and warranties relate solely to an earlier date; and

(b) no event has occurred and is continuing, or would result from such Advance which constitutes a Default or an Event of Default.

SECTION 4.3 CONDITIONS PRECEDENT TO AN ADVANCE CREATING A THRESHOLD EVENT. The Lender's obligation to make any Advance which shall constitute a Threshold Event shall be subject to the further conditions precedent that on such date:

(a) The Borrower shall have entered into an agreement with Lender and Wells Fargo Bank, N.A. or such other bank (including Silicon Valley Bank) as Borrower and Lender shall agree, establishing a collection account into which all payments on Receivables shall be deposited (the "Collection Account") pursuant to terms satisfactory to Lender and Wells Fargo Bank, N.A. or such other bank.

(b) Borrower shall have directed all account debtors to make all payments on Receivables to the lockbox established under the Lockbox Agreement and/or the Existing Lockbox Agreement, as set forth in Section 6.10.

(c) If the Existing Lockbox Agreement shall then still exist, Borrower shall have obtained either an acknowledgment from the bank maintaining the Existing Lockbox Agreement that all Receivables deposited into the lockbox maintained thereunder shall be directed to the Collection Account, or Borrower shall have cooperated with Lender in submitting a change of address to all of Borrower's account debtors to direct the payment of all Receivables to the lockbox established under the Lockbox Agreement.

(d) Lender shall have completed a Collateral examination at the expense of Borrower, the results of which shall be satisfactory to Lender.

(e) Lender shall have received an acknowledgment and agreement (in form and substance satisfactory to Lender) from each licensor in favor of the Lender, together with a true, correct and complete copy of all license agreements.

ARTICLE V
REPRESENTATIONS AND WARRANTIES

The Borrower represents and warrants to the Lender as follows:

SECTION 5.1 CORPORATE EXISTENCE AND POWER; NAME; CHIEF EXECUTIVE OFFICE; INVENTORY AND EQUIPMENT LOCATIONS; TAX IDENTIFICATION NUMBER. The Borrower is a corporation, duly organized, validly existing and in good standing under the laws of the State of Delaware and is duly licensed or qualified to transact business in all jurisdictions where the character of the property owned or leased or the nature of the business transacted by it makes such licensing or qualification necessary. The Borrower has all requisite power and authority, corporate or otherwise, to conduct its business, to own its properties and to execute and deliver, and to perform all of its obligations under, the Loan Documents. During its existence, the Borrower has done business solely under the names set forth in Schedule 5.1 hereto. The Borrower's chief executive office and principal place of business is located at the address set forth in Schedule 5.1 hereto, and all of the Borrower's records relating to its business or the

Collateral are kept at that location. All Inventory and Equipment is located at that location or at one of the other locations set forth in Schedule 5.1 hereto. The Borrower's tax identification number is correctly set forth in Section 3.6 hereto.

SECTION 5.2 AUTHORIZATION OF BORROWING; NO CONFLICT AS TO LAW OR AGREEMENTS. The execution, delivery and performance by the Borrower of the Loan Documents and the borrowings from time to time hereunder have been duly authorized by all necessary corporate action and do not and will not (i) require any consent or approval of the Borrower's stockholders; (ii) require any authorization, consent or approval by, or registration, declaration or filing with, or notice to, any governmental department, commission, board, bureau, agency or instrumentality, domestic or foreign, or any third party, except such

authorization, consent, approval, registration, declaration, filing or notice as has been obtained, accomplished or given prior to the date hereof; (iii) violate any provision of any law, rule or regulation (including, without limitation, Regulation X of the Board of Governors of the Federal Reserve System) or of any order, writ, injunction or decree presently in effect having applicability to the Borrower or of the Borrower's articles of incorporation or bylaws; (iv) result in a breach of or constitute a default under any indenture or loan or credit agreement or any other material agreement, lease or instrument to which the Borrower is a party or by which it or its properties may be bound or affected; or (v) result in, or require, the creation or imposition of any mortgage, deed of trust, pledge, lien, security interest or other charge or encumbrance of any nature (other than the Security Interest) upon or with respect to any of the properties now owned or hereafter acquired by the Borrower.

SECTION 5.3 LEGAL AGREEMENTS. This Agreement constitutes and, upon due execution by the Borrower, the other Loan Documents will constitute the legal, valid and binding obligations of the Borrower, enforceable against the Borrower in accordance with their respective terms.

SECTION 5.4 SUBSIDIARIES. Except as set forth in Schedule 5.4, the Borrower has no Subsidiaries.

SECTION 5.5 FINANCIAL CONDITION; NO ADVERSE CHANGE. The Borrower has heretofore furnished to the Lender unaudited financial statements of the Borrower for the fiscal year ended December 31, 1999, and those statements fairly present the Borrower's financial condition on the dates thereof and the results of its operations and cash flows for the periods then ended and were prepared in accordance with generally accepted accounting principles. Since the date of the most recent financial statements, there has been no material adverse change in the Borrower's business, properties or condition (financial or otherwise).

SECTION 5.6 LITIGATION. Except as disclosed on Schedule 5.6, there are no actions, suits or proceedings pending or, to the Borrower's knowledge, threatened against or affecting the Borrower or any of its Affiliates or the properties of the Borrower or any of its Affiliates before any court or governmental department, commission, board, bureau, agency or instrumentality, domestic or foreign, which, if determined adversely to the Borrower or any of its Affiliates, would have a material adverse effect on the financial condition, properties or operations of the Borrower or any of its Affiliates.

SECTION 5.7 REGULATION U. The Borrower is not engaged in the business of extending credit for the purpose of purchasing or carrying margin stock (within the meaning of Regulation U of the Board of Governors of the Federal Reserve System), and no part of the proceeds of any Advance will be used to purchase or carry any margin stock or to extend credit to others for the purpose of purchasing or carrying any margin stock.

SECTION 5.8 TAXES. The Borrower and its Affiliates have paid or caused to be paid to the proper authorities when due all federal, state and local taxes required to be withheld by each of them. The Borrower and its Affiliates have filed all federal, state and local tax returns which to the knowledge of the officers of the Borrower or any Affiliate, as the case may be, are required to be filed, and the Borrower and its Affiliates have paid or caused to be paid to the respective taxing authorities all taxes as shown on said returns or on any assessment received by any of them to the extent such taxes have become due.

SECTION 5.9 TITLES AND LIENS. The Borrower has good and absolute title to all Collateral described in the collateral reports provided to the Lender and all other Collateral, properties and assets reflected in the latest financial statements referred to in Section 5.5 and all proceeds thereof, free and clear of all mortgages, security interests, liens and encumbrances, except for Permitted Liens. No financing statement naming the Borrower as debtor is on file in any office except to perfect only Permitted Liens.

SECTION 5.10 PLANS. Except as disclosed to the Lender in writing prior to the date hereof, neither the Borrower nor any of its Affiliates maintains or has maintained any Plan. Neither the Borrower nor any Affiliate has received any notice or has any knowledge to the effect that it is not in full compliance with any of the requirements of ERISA. No Reportable Event or other fact or circumstance which may have an adverse effect on the Plan's tax qualified status exists in connection with any Plan. Neither the Borrower nor any of its Affiliates has:

(a) Any accumulated funding deficiency within the meaning of ERISA; or

(b) Any liability or knows of any fact or circumstances which could result in any liability to the Pension Benefit Guaranty Corporation, the Internal Revenue Service, the Department of Labor or any participant in connection with any Plan (other than accrued benefits which or which may become payable to participants or beneficiaries of any such Plan).

SECTION 5.11 DEFAULT. The Borrower is in compliance with all provisions of all agreements, instruments, decrees and orders to which it is a party or by which it or its property is bound or affected, the breach or default of which could have a material adverse effect on the Borrower's financial condition, properties or operations.

SECTION 5.12 ENVIRONMENTAL MATTERS.

(a) DEFINITIONS. As used in this Agreement, the following terms shall have the following meanings:

(i) "Environmental Law" means any federal, state, local or other governmental statute, regulation, law or ordinance dealing with the protection of human health and the environment.

(ii) "Hazardous Substances" means pollutants, contaminants, hazardous substances, hazardous wastes, petroleum and fractions thereof, and all other chemicals, wastes, substances and materials listed in, regulated by or identified in any Environmental Law.

(b) To the Borrower's best knowledge, there are not present in, on or under the Premises any Hazardous Substances in such form or quantity as to create any liability or obligation for either the Borrower or the Lender under common law of any jurisdiction or under any Environmental Law, and to the best of Borrower's knowledge no Hazardous Substances have been stored, buried, spilled, leaked, discharged, emitted or released in, on or under the Premises during Borrower's occupancy of the Premises in such a way as to create any such liability.

(c) To the Borrower's best knowledge, the Borrower has not disposed of Hazardous Substances in such a manner as to create any liability under any Environmental Law.

(d) There are not and there never have been, during Borrower's occupancy of the Premises to the best of Borrower's knowledge, any requests, claims, notices, investigations, demands, administrative proceedings, hearings or litigation, relating in any way to the Premises or the Borrower, alleging liability under, violation of, or noncompliance with any Environmental Law or any license, permit or other authorization issued pursuant thereto. To the Borrower's best knowledge, no such matter is threatened or impending.

(e) To the Borrower's best knowledge, the Borrower's businesses are and have in the past always been conducted in accordance with all Environmental Laws and all licenses, permits and other authorizations required pursuant to any Environmental Law and necessary for the lawful and efficient operation of such businesses are in the Borrower's possession and are in full force and effect. No permit required under any Environmental Law is scheduled to expire within 12 months and there is no threat that any such permit will be withdrawn, terminated, limited or materially changed.

(f) To the Borrower's best knowledge, the Premises are not and never have been, during Borrower's occupancy of the Premises, listed on the National Priorities List, the Comprehensive Environmental Response, Compensation and Liability Information System or any similar federal, state or local list, schedule, log, inventory or database.

(g) The Borrower has delivered to Lender all environmental assessments, audits, reports, permits, licenses and other documents describing or relating in any way to the Premises or Borrower's businesses.

SECTION 5.13 SUBMISSIONS TO LENDER. All financial and other information provided to the Lender by or on behalf of the Borrower in connection with the Borrower's request for the credit facilities contemplated hereby is true and correct in all material respects and, as to projections, valuations or proforma financial statements, present a good faith opinion as to such projections, valuations and proforma condition and results.

SECTION 5.14 FINANCING STATEMENTS. The Borrower has provided to the Lender signed financing statements sufficient when filed to perfect the Security Interest and the other security interests created by the Security Documents.

When such financing statements are filed in the offices noted therein, the Lender will have a valid and perfected security interest in all Collateral and all other collateral described in the Security Documents which is capable of being perfected by filing financing statements. None of the Collateral or other collateral covered by the Security Documents is or will become a fixture on real estate, unless a sufficient fixture filing is in effect with respect thereto.

SECTION 5.15 RIGHTS TO PAYMENT. Each right to payment and each instrument, document, chattel paper and other agreement constituting or evidencing Collateral or other collateral covered by the Security Documents is (or, in the case of all future Collateral or such other collateral, will be when arising or issued) the valid, genuine and legally enforceable obligation, subject to no defense, setoff or counterclaim, of the account debtor or other obligor named therein or in the Borrower's records pertaining thereto as being obligated to pay such obligation.

SECTION 5.16 FINANCIAL SOLVENCY. Both before and after giving effect to the transactions contemplated in the Loan Documents, none of the Borrower or its Affiliates:

(a) was or will be insolvent, as that term is used and defined in Section 101(32) of the United States Bankruptcy Code and Section 2 of the Uniform Fraudulent Transfer Act;

(b) has unreasonably small capital or is engaged or about to engage in a business or a transaction for which any remaining assets of the Borrower or such Affiliate are unreasonably small;

(c) by executing, delivering or performing its obligations under the Loan Documents or other documents to which it is a party or by taking any action with respect thereto, intends to, nor believes that it will, incur debts beyond its ability to pay them as they mature;

(d) by executing, delivering or performing its obligations under the Loan Documents or other documents to which it is a party or by taking any action with respect thereto, intends to hinder, delay or defraud either its present or future creditors; and

(e) at this time contemplates filing a petition in bankruptcy or for an arrangement or reorganization or similar proceeding under any law any jurisdiction, nor, to the best knowledge of the Borrower, is the subject of any actual, pending or threatened bankruptcy, insolvency or similar proceedings under any law of any jurisdiction.

ARTICLE VI
BORROWER'S AFFIRMATIVE COVENANTS

So long as the Obligations shall remain unpaid, or the Credit Facility shall remain outstanding, the Borrower will comply with the following requirements, unless the Lender shall otherwise consent in writing:

SECTION 6.1 REPORTING REQUIREMENTS. The Borrower will deliver, or cause to be delivered, to the Lender each of the following, which shall be in form and detail acceptable to the Lender (provided that in the case of matters due on a date certain pursuant to the terms of this Section 6.1, it shall not be a Default so long as the reporting requirement shall be satisfied by Borrower within 10 days after such due date):

(a) as soon as available, and in any event within 90 days after the end of each fiscal year of the Borrower, the Borrower's audited financial statements with the unqualified opinion of independent certified public accountants selected by the Borrower and acceptable to the Lender, which annual financial statements shall include the Borrower's balance sheet as of the end of such fiscal year and the related statements of the Borrower's income, retained earnings and cash flows for the fiscal year then ended, prepared, if the Lender so requests, on a consolidating and consolidated basis to include any Affiliates, all in reasonable detail and prepared in accordance with GAAP, together with (i) copies of all management letters prepared by such accountants; (ii) a report signed by such accountants stating that in making the investigations necessary for said opinion they obtained no knowledge, except as specifically stated, of any Default or Event of Default hereunder and all relevant facts in reasonable detail to evidence, and the computations as to, whether or not the Borrower is in compliance with the requirements set forth in Sections 6.12 through 6.14, and 7.10; and (iii) a certificate of the Borrower's chief financial officer stating that such financial statements have been prepared in accordance with GAAP and whether or not such officer has knowledge of the occurrence of any Default or Event of Default hereunder and, if so, stating in reasonable detail the facts with respect thereto;

(b) as soon as available and in any event within 20 days after the end of each month, an unaudited/internal balance sheet and statements of income and retained earnings of the Borrower as at the end of and for such month and for the year to date period then ended, prepared, if the Lender so requests, on a consolidating and consolidated basis to include any Affiliates, in reasonable detail and stating in comparative form the figures for the corresponding date and periods in the previous year, all prepared in accordance with GAAP, subject to year-end audit adjustments; and accompanied by a certificate of the Borrower's chief financial officer, substantially in the form of Exhibit B hereto stating (i) that such financial statements have been prepared in accordance with GAAP, subject to year-end audit adjustments, (ii) whether or not such officer has knowledge of the occurrence of any Default or Event of Default hereunder not theretofore reported and remedied and, if so, stating in reasonable detail the facts with respect thereto, and (iii) all relevant facts

in reasonable detail to evidence, and the computations as to, whether or not the Borrower is in compliance with the requirements set forth in Sections 6.12 through 6.14, and 7.10;

(c) within 20 days after the end of each month or more frequently if the Lender so requires, agings of the Borrower's accounts receivable and its accounts payable, an inventory certification report, and a calculation of the Borrower's Accounts, Eligible Accounts, and Inventory as at the end of such month or shorter time period;

(d) at least 30 days before the beginning of each fiscal year of the Borrower, the projected balance sheets and income statements for each month of such year, each in reasonable detail, representing the Borrower's good faith projections and certified by the Borrower's chief financial officer as being the most accurate projections available and identical to the projections used by the Borrower for internal planning purposes, together with such supporting schedules and information as the Lender may in its discretion require;

(e) immediately after the commencement thereof, notice in writing of all litigation and of all proceedings before any governmental or regulatory agency affecting the Borrower of the type described in Section 5.12 or which seek a monetary recovery against the Borrower in excess of $500,000.00;

(f) as promptly as practicable (but in any event not later than five business days) after an officer of the Borrower obtains knowledge of the occurrence of any event which constitutes a Default or Event of Default hereunder, notice of such occurrence, together with a detailed statement by a responsible officer of the Borrower of the steps being taken by the Borrower to cure the effect of such Default or Event of Default;

(g) as soon as possible and in any event within 30 days after the Borrower knows or has reason to know that any Reportable Event with respect to any Plan has occurred, the statement of the Borrower's chief financial officer setting forth details as to such Reportable Event and the action which the Borrower proposes to take with respect thereto, together with a copy of the notice of such Reportable Event to the Pension Benefit Guaranty Corporation;

(h) as soon as possible, and in any event within 20 days after the Borrower fails to make any quarterly contribution required with respect to any Plan under Section 412(m) of the Internal Revenue Code of 1986, as amended, the statement of the Borrower's chief financial officer setting forth details as to such failure and the action which the Borrower proposes to take with respect thereto, together with a copy of any notice of such failure required to be provided to the Pension Benefit Guaranty Corporation;

(i) on and after the earlier to occur of (i) a Threshold Event, or (ii) a Default, promptly upon knowledge thereof, notice of (i) any dispute or claim by the Borrower's customers which exceeds $25,000.00; (ii) credit memos; (iii) any goods returned to or recovered by the Borrower; and (iv) any change in

the persons constituting the Borrower's officers and directors;

(j) promptly upon knowledge thereof, notice of any loss of or material damage to the Collateral or other collateral covered by the Security Documents or of any substantial adverse change in the Collateral or such other collateral or the prospect of payment thereof;

(k) promptly upon their distribution, copies of all financial statements, reports and proxy statements which the Borrower shall have sent to its stockholders;

(l) promptly after the sending or filing thereof, copies of all regular and periodic reports which the Borrower shall file with the Securities and Exchange Commission or any national securities exchange;

(m) promptly upon knowledge thereof, notice of the Borrower's violation of any law, rule or regulation, the non-compliance with which could materially and adversely affect the Borrower's business or its financial condition; and

(n) within 20 days after the end of each month until such time as a Threshold Event shall occur and then thereafter from time to time with such frequency as shall be required by Lender, with reasonable promptness, any and all receivables schedules, collection reports, deposit records, equipment

schedules, copies of invoices to account debtors, shipment documents and delivery receipts for goods sold, and such other material, reports, records or information as the Lender may request.

SECTION 6.2 BOOKS AND RECORDS; INSPECTION AND EXAMINATION. The Borrower will keep accurate books of record and account for itself pertaining to the Collateral and pertaining to the Borrower's business and financial condition and such other matters as the Lender may from time to time request in which true and complete entries will be made in accordance with GAAP and, upon the Lender's request, will permit any officer, employee, attorney or accountant for the Lender to audit, review, make extracts from or copy any and all corporate and financial books and records of the Borrower at all times during ordinary business hours, to send and discuss with account debtors and other obligors requests for verification of amounts owed to the Borrower, and to discuss the Borrower's affairs with any of its directors, officers, employees or agents. The Borrower will permit the Lender, or its employees, accountants, attorneys or agents, to examine and inspect any Collateral, other collateral covered by the Security Documents or any other property of the Borrower at any time during ordinary business hours.

SECTION 6.3 ACCOUNT VERIFICATION. The Lender may at any time and from time to time send or require the Borrower to send requests for verification of accounts or notices of assignment to account debtors and other obligors. The Lender may also at any time and from time to time telephone account debtors and

other obligors to verify accounts.

SECTION 6.4 COMPLIANCE WITH LAWS.

(a) The Borrower will (i) comply with the requirements of applicable laws and regulations, the non-compliance with which would materially and adversely affect its business or its financial condition and (ii) use and keep the Collateral, and require that others use and keep the Collateral, only for lawful purposes, without violation of any federal, state or local law, statute or ordinance.

(b) Without limiting the foregoing undertakings, the Borrower specifically agrees that it will comply with all applicable Environmental Laws and obtain and comply with all permits, licenses and similar approvals required by any Environmental Laws, and will not generate, use, transport, treat, store or dispose of any Hazardous Substances in such a manner as to create any liability or obligation under the common law of any jurisdiction or any Environmental Law.

SECTION 6.5 PAYMENT OF TAXES AND OTHER CLAIMS. The Borrower will pay or discharge, when due, (a) all taxes, assessments and governmental charges levied or imposed upon it or upon its income or profits, upon any properties belonging to it (including, without limitation, the Collateral) or upon or against the creation, perfection or continuance of the Security Interest, prior to the date on which penalties attach thereto, (b) all federal, state and local taxes required to be withheld by it, and (c) all lawful claims for labor, materials and supplies which, if unpaid, might by law become a lien or charge upon any properties of the Borrower; provided, that the Borrower shall not be required to pay any such tax, assessment, charge or claim whose amount, applicability or validity is being contested in good faith by appropriate proceedings and for which proper reserves have been made.

SECTION 6.6 MAINTENANCE OF PROPERTIES.

(a) The Borrower will keep and maintain the Collateral, the other collateral covered by the Security Documents and all of its other properties necessary or useful in its business in good condition, repair and working order (normal wear and tear excepted) and will from time to time replace or repair any worn, defective or broken parts; provided, however, that nothing in this Section 6.6 shall prevent the Borrower from discontinuing the operation and maintenance of any of its properties if such discontinuance is, in the Lender's judgment, desirable in the conduct of the Borrower's business and not disadvantageous in any material respect to the Lender.

(b) The Borrower will defend the Collateral against all claims or demands of all persons (other than the Lender and Permitted Liens) claiming the Collateral or any interest therein.

(c) The Borrower will keep all Collateral and other collateral covered

by the Security Documents free and clear of all security interests, liens and encumbrances except Permitted Liens. SECTION 6.7 INSURANCE. The Borrower will obtain and at all times maintain insurance with insurers believed by the Borrower to be responsible and reputable, in such amounts and against such risks as may from time to time be required by the Lender, but in all events in such amounts and against such risks as is usually carried by companies engaged in similar business and owning similar properties in the same general areas in which the Borrower operates. Without limiting the generality of the foregoing, the Borrower will at all times maintain business interruption insurance including coverage for force majeure and keep all tangible Collateral insured against risks of fire (including so-called extended coverage), theft, collision (for Collateral consisting of motor vehicles) and such other risks and in such amounts as the Lender may reasonably request, with any loss payable to the Lender to the extent of its interest, and all policies of such insurance shall contain a lender's loss payable endorsement for the Lender's benefit acceptable to the Lender. All policies of liability insurance required hereunder shall name the Lender as an additional insured.

SECTION 6.8 PRESERVATION OF EXISTENCE. The Borrower will preserve and maintain its existence and all of its rights, privileges and franchises necessary or desirable in the normal conduct of its business and shall conduct its business in an orderly, efficient and regular manner.

SECTION 6.9 DELIVERY OF INSTRUMENTS, ETC. Upon request by the Lender, the Borrower will promptly deliver to the Lender in pledge all instruments, documents and chattel papers constituting Collateral, duly endorsed or assigned by the Borrower.

SECTION 6.10 LOCKBOX AGREEMENTS AND COLLECTION ACCOUNT.

(a) As of the date of this Agreement, the Borrower maintains a lockbox under the "Existing Lockbox Agreement" with Silicon Valley Bank. At such time as a Threshold Event may occur, Borrower shall irrevocably and permanently ensure that all Receivables deposited in the lockbox under the Existing Lockbox Agreement shall be deposited directly to the Collection Account.

(b) After the date of this Agreement, but in any event not later than the earlier to occur of, (i) a Threshold Event, or (ii) 18 months from the date of this Agreement, Borrower shall have entered into the Lockbox Agreement with Lender, Wells Fargo Bank, N.A. and Regulus West, LLC pursuant to an agreement with terms and conditions satisfactory to Lender (the "Lockbox Agreement"). As each account debtor's contract is renewed, Borrower shall direct that all Receivables thereafter be directed to the lockbox established under the Lockbox Agreement. The following provisions shall apply to the Lockbox Agreement:

(i) The Lockbox Agreement will require all payments on Receivables to be deposited in the Collection Account so long as any Revolving Advance remains outstanding after the occurrence of a Threshold Event. If the Borrower receives any payments on Receivables after the occurrence of a

Threshold Event and while any Revolving Advance is outstanding, the Borrower shall deposit such payments into the Collection Account. Until so deposited, the Borrower shall hold all such payments in trust for and as the property of the Lender and shall not commingle such payments with any of its other funds or property.

(ii) Amounts deposited in the Collection Account shall not bear interest and shall not be subject to withdrawal by the Borrower, except after full payment and discharge of all Obligations.

(iii) All deposits in the Collection Account shall constitute proceeds of Collateral and shall not constitute payment of the Obligations. The Lender from time to time at its discretion may, apply deposited funds in the Collection Account to the payment of the Obligations, in any order or manner of application satisfactory to the Lender, by transferring such funds to the Lender's general account.

(iv) All items deposited in the Collection Account shall be subject to final payment. If any such item is returned uncollected, the Borrower will immediately pay the Lender, or, for items deposited in the Collection Account, the bank maintaining such account, the amount of that item, or such bank at its discretion may charge any uncollected item to the Borrower's commercial account or other account. The Borrower shall be liable as an endorser on all items deposited in the Collection Account, whether or not in fact endorsed by the Borrower.

(c) Until the earlier to occur of (i) a Default, or (ii) a Threshold Event, Borrower may have monies deposited in any lockbox deposited to its operating account rather than to the Collection Account.

SECTION 6.11 PERFORMANCE BY THE LENDER. If the Borrower at any time fails to perform or observe any of the foregoing covenants contained in this Article VI or elsewhere herein, and if such failure shall continue for a period of ten calendar days after the Lender gives the Borrower written notice thereof (or in the case of the agreements contained in Sections 6.5, 6.7 and 6.10, immediately upon the occurrence of such failure, without notice or lapse of time), the Lender may, but need not, perform or observe such covenant on behalf and in the name, place and stead of the Borrower (or, at the Lender's option, in the Lender's name) and may, but need not, take any and all other actions which the Lender may reasonably deem necessary to cure or correct such failure (including, without limitation, the payment of taxes, the satisfaction of security interests, liens or encumbrances, the performance of obligations owed to account debtors or other obligors, the procurement and maintenance of insurance, the execution of assignments, security agreements and financing statements, and the

endorsement of instruments); and the Borrower shall thereupon pay to the Lender on demand the amount of all monies expended and all costs and expenses (including reasonable attorneys' fees and legal expenses) incurred by the Lender in connection with or as a result of the performance or observance of such

agreements or the taking of such action by the Lender, together with interest thereon from the date expended or incurred at the Floating Rate. To facilitate the Lender's performance or observance of such covenants of the Borrower, the Borrower hereby irrevocably appoints the Lender, or the Lender's delegate, acting alone, as the Borrower's attorney in fact (which appointment is coupled with an interest) with the right (but not the duty) from time to time to create, prepare, complete, execute, deliver, endorse or file in the name and on behalf of the Borrower any and all instruments, documents, assignments, security agreements, financing statements, applications for insurance and other agreements and writings required to be obtained, executed, delivered or endorsed by the Borrower under this Section 6.12.

SECTION 6.12 TANGIBLE NET WORTH. The Borrower covenants that as of the date of this Agreement, the Borrower has a Tangible Net Worth of not less than $43,000,000.00. The Borrower covenants that commencing with the month ending January 31, 2000 and continuing each month thereafter, the Borrower's Tangible Net Worth as of the last day of each month shall be not less than $43,000,000.00.

SECTION 6.13 QUICK RATIO. The Borrower covenants that commencing with the month ending January 31, 2000 and continuing each month thereafter, the Borrower will maintain during each month a Quick Ratio of not less than 2.0 to 1.0 as determined at the end of each month.

SECTION 6.14 DEBT TO TANGIBLE NET WORTH. The Borrower covenants that commencing with the month ending January 31, 2000 and continuing each month thereafter, the Borrower will maintain during each month a Debt to Tangible Net Worth Ratio of not less than 0.50 to 1.00 as determined at the end of each month.

ARTICLE VII
NEGATIVE COVENANTS

So long as the Obligations shall remain unpaid, or the Credit Facility shall remain outstanding, the Borrower agrees that, without the Lender's prior written consent:

SECTION 7.1 LIENS. The Borrower will not create, incur or suffer to exist any mortgage, deed of trust, pledge, lien, security interest, assignment or transfer upon or of any of its assets (including, without limitation, the Patents), now owned or hereafter acquired, to secure any indebtedness; EXCLUDING, HOWEVER, from the operation of the foregoing, the following (collectively, "Permitted Liens"):

(a) in the case of any of the Borrower's property which is not Collateral or other collateral described in the Security Documents, covenants, restrictions, rights, easements and minor irregularities in title which do not materially interfere with the Borrower's business or operations as presently conducted;

(b) mortgages, deeds of trust, pledges, liens, security interests, capital leases and assignments listed in Schedule 7.1 hereto, securing indebtedness for borrowed money permitted under Section 7.2;

(c) the Security Interest and liens and security interests created by the Security Documents; and

(d) purchase money security interests relating to the acquisition of machinery and equipment of the Borrower not exceeding the cost or fair market value thereof and so long as no Default Period is then in existence and none would exist immediately after such acquisition.

SECTION 7.2 INDEBTEDNESS. The Borrower will not incur, create, assume or permit to exist any indebtedness or liability on account of deposits or advances or any indebtedness for borrowed money or letters of credit issued on the Borrower's behalf, or any other indebtedness or liability evidenced by notes, bonds, debentures or similar obligations, except:

(a) indebtedness arising hereunder;

(b) indebtedness of the Borrower in existence on the date hereof and listed in Schedule 7.2 hereto; and

(c) indebtedness relating to liens permitted in accordance with Section 7.1.

SECTION 7.3 GUARANTIES. The Borrower will not assume, guarantee, endorse or otherwise become directly or contingently liable in connection with any obligations of any other Person, except:

(a) the endorsement of negotiable instruments by the Borrower for deposit or collection or similar transactions in the ordinary course of business; and

(b) guaranties, endorsements and other direct or contingent liabilities in connection with the obligations of other Persons, in existence on the date hereof and listed in Schedule 7.2 hereto.

SECTION 7.4 INVESTMENTS AND SUBSIDIARIES.

(a) The Borrower will not purchase or hold beneficially any stock or other securities or evidences of indebtedness of, make or permit to exist any loans or advances to, or make any investment or acquire any interest whatsoever in, any other Person, including specifically but without limitation any partnership or joint venture, except:

(i) investments in direct obligations of the United States of America or any agency or instrumentality thereof whose obligations constitute full faith and credit obligations of the United States of America having a maturity of one year or less, commercial paper issued by U.S. corporations rated "A-1" or "A-2" by Standard & Poors Corporation or "P-1" or "P-2" by Moody's

Investors Service or certificates of deposit or bankers' acceptances having a maturity of one year or less issued by members of the Federal Reserve System

having deposits in excess of $100,000,000.00 (which certificates of deposit or bankers' acceptances are fully insured by the Federal Deposit Insurance Corporation); and

(ii) travel advances or loans to the Borrower's officers and employees; and

(iii) advances in the form of progress payments, prepaid rent not exceeding three (3) months or security deposits; and

(iv) the Allowed Investments;

(b) The Borrower will not create or permit to exist any Subsidiary other than the Subsidiary shown on Schedule 5.4.

SECTION 7.5 DIVIDENDS. The Borrower will not declare or pay any dividends (other than dividends payable solely in stock of the Borrower) on any class of its common stock or make any payment on account of the purchase, redemption or other retirement of any shares of such stock or make any distribution in respect thereof, either directly or indirectly (provided that, except during a Default Period, Borrower may pay dividends on its common shares, or redeem or retire shares of such stock, so long as all such dividends or payments for redemption or retirement in any fiscal year of Borrower shall not exceed, in the aggregate, the lesser of (i) 10% of Borrower's total assets, or (ii) 10% of Borrower's total sales for such period.

SECTION 7.6 SALE OR TRANSFER OF ASSETS; SUSPENSION OF BUSINESS OPERATIONS. The Borrower will not sell, lease, assign, transfer or otherwise dispose of (i) the stock of any Subsidiary, (ii) all or a substantial part of its assets, or (iii) any Collateral or any interest therein (whether in one transaction or in a series of transactions) to any other Person other than the sale of Inventory in the ordinary course of business and will not liquidate, dissolve or suspend business operations. The Borrower will not in any manner transfer any property without prior or present receipt of full and adequate consideration.

SECTION 7.7 CONSOLIDATION AND MERGER; ASSET ACQUISITIONS. The Borrower will not consolidate with or merge into any Person, or permit any other Person to merge into it, or acquire (in a transaction analogous in purpose or effect to a consolidation or merger) all or substantially all the assets of any other Person.

SECTION 7.8 SALE AND LEASEBACK. The Borrower will not enter into any arrangement, directly or indirectly, with any other Person whereby the Borrower shall sell or transfer any real or personal property, whether now owned or hereafter acquired, and then or thereafter rent or lease as lessee such property or any part thereof or any other property which the Borrower intends to use for

substantially the same purpose or purposes as the property being sold or transferred.

SECTION 7.9 RESTRICTIONS ON NATURE OF BUSINESS. The Borrower will not engage in any line of business materially different from that presently engaged in by the Borrower and will not purchase, lease or otherwise acquire assets not related to its business.

SECTION 7.10 CAPITAL EXPENDITURES. The Borrower will not incur or contract to incur Capital Expenditures of more than (i) $4,000,000.00 in the aggregate during any fiscal year applicable to Borrower's rental fleet, or (ii) more than $3,000,000.00 in the aggregate during any fiscal year which are not applicable to Borrower's rental fleet.

SECTION 7.11 ACCOUNTING. The Borrower will not adopt any material change in accounting principles other than as required by GAAP. The Borrower will not adopt, permit or consent to any change in its fiscal year.

SECTION 7.12 DISCOUNTS, ETC. The Borrower will not, after notice from the Lender, grant any discount, credit or allowance to any customer of the Borrower outside the ordinary course of Borrower's business or accept any return of goods sold, or at any time (whether before or after notice from the Lender) modify, amend, subordinate, cancel or terminate the obligation of any account debtor or other obligor of the Borrower.

SECTION 7.13 DEFINED BENEFIT PENSION PLANS. The Borrower will not adopt, create, assume or become a party to any defined benefit pension plan, unless disclosed to the Lender pursuant to Section 5.10.

SECTION 7.14 OTHER DEFAULTS. The Borrower will not permit any breach or default (beyond any applicable notice and cure period) or event of default to occur under any note, loan agreement, indenture, lease, mortgage, contract for deed, security agreement or other contractual obligation binding upon the Borrower.

SECTION 7.15 PLACE OF BUSINESS; NAME. The Borrower will not transfer its chief executive office or principal place of business, or move, relocate, close or sell any business location. The Borrower will not permit any tangible Collateral or any records pertaining to the Collateral to be located in any state or area in which, in the event of such location, a financing statement covering such Collateral would be required to be, but has not in fact been, filed in order to perfect the Security Interest. The Borrower will not change its name.

SECTION 7.16 ORGANIZATIONAL DOCUMENTS; S CORPORATION STATUS. The Borrower will not amend its certificate of incorporation, articles of incorporation or bylaws in any material manner or in any manner adverse to the interests of Lender hereunder. The Borrower will not become an S Corporation.

ARTICLE VIII
EVENTS OF DEFAULT, RIGHTS AND REMEDIES

SECTION 8.1 EVENTS OF DEFAULT. "Event of Default", wherever used herein, means any one of the following events:

(a) Default in the payment of the Obligations when they become due and payable;

(b) Default in the payment of any fees, commissions, costs or expenses required to be paid by the Borrower under this Agreement;

(c) Default in the performance, or breach, of any covenant or agreement of the Borrower contained in this Agreement;

(d) The Borrower shall be or become insolvent, or admit in writing its inability to pay its debts as they mature, or make an assignment for the benefit of creditors; or the Borrower shall apply for or consent to the appointment of any receiver, trustee, or similar officer for it or for all or any substantial part of its property; or such receiver, trustee or similar officer shall be appointed without the application or consent of the Borrower (and in the case of such appointment without the consent of Borrower, such appointment order shall not be vacated or reversed within 60 days after such appointment); or the Borrower shall institute (by petition, application, answer, consent or otherwise) any bankruptcy, insolvency, reorganization, arrangement, readjustment of debt, dissolution, liquidation or similar proceeding relating to it under the laws of any jurisdiction; or any such proceeding shall be instituted (by petition, application or otherwise) against the Borrower (provided, however, that in the case of such proceeding being instituted against the Borrower without the Borrower's consent, such proceeding shall not have been dismissed within 60 days after the filing thereof); or any judgment, writ, warrant of attachment or execution or similar process shall be issued or levied against a substantial part of the property of the Borrower;

(e) A petition shall be filed by or against the Borrower under the United States Bankruptcy Code naming the Borrower as debtor (provided, however, that in the event of an involuntary filing Borrower shall fail to have the same dismissed within 60 days after the filing thereof);

(f) Any representation or warranty made by the Borrower in this Agreement, or by the Borrower (or any of its officers) in any agreement, certificate, instrument or financial statement or other statement contemplated by or made or delivered pursuant to or in connection with this Agreement or any such guaranty shall prove to have been incorrect in any material respect when deemed to be effective;

(g) The rendering against the Borrower of a final judgment, decree or order for the payment of money in excess of $250,000.00 and the continuance of such judgment, decree or order unsatisfied and in effect for any period of 30

consecutive days without a stay of execution;

(h) A default under any bond, debenture, note or other evidence of indebtedness of the Borrower owed to any Person other than the Lender, or under any indenture or other instrument under which any such evidence of indebtedness has been issued or by which it is governed, or under any lease of any of the Principal Premises, and the expiration of the applicable period of grace, if any, specified in such evidence of indebtedness, indenture, other instrument or lease;

(i) Any Reportable Event, which the Lender determines in good faith might constitute grounds for the termination of any Plan or for the appointment by the appropriate United States District Court of a trustee to administer any Plan, shall have occurred and be continuing 30 days after written notice to such effect shall have been given to the Borrower by the Lender; or a trustee shall have been appointed by an appropriate United States District Court to administer any Plan; or the Pension Benefit Guaranty Corporation shall have instituted proceedings to terminate any Plan or to appoint a trustee to administer any Plan; or the Borrower shall have filed for a distress termination of any Plan under Title IV of ERISA; or the Borrower shall have failed to make any quarterly contribution required with respect to any Plan under Section 412(m) of the Internal Revenue Code of 1986, as amended, which the Lender determines in good

faith may by itself, or in combination with any such failures that the Lender may determine are likely to occur in the future, result in the imposition of a lien on the Borrower's assets in favor of the Plan;

(j) An event of default shall occur under any Security Document or under any other security agreement, mortgage, deed of trust, assignment or other instrument or agreement securing any obligations of the Borrower hereunder or under any note evidencing any obligations of the Borrower hereunder;

(k) The Borrower shall liquidate, dissolve, terminate or suspend its business operations or otherwise fail to operate its business in the ordinary course, or sell all or substantially all of its assets, without the Lender's prior written consent;

(l) The Borrower shall fail to pay, withhold, collect or remit any tax or tax deficiency in excess of $150,000.00 when assessed or due (other than any tax deficiency which is being contested in good faith and by proper proceedings and for which it shall have set aside on its books adequate reserves therefor) or notice of any state or federal tax liens shall be filed or issued;

(m) Default in the payment of any amount owed by the Borrower to the Lender other than any indebtedness arising hereunder;

(n) Any breach, default or event of default by or attributable to any Affiliate under any agreement between such Affiliate and the Lender.

SECTION 8.2 RIGHTS AND REMEDIES. During any Default Period, the Lender may exercise any or all of the following rights and remedies:

(a) the Lender may, by notice to the Borrower, declare the Commitment to be terminated, whereupon the same shall forthwith terminate;

(b) the Lender may, by notice to the Borrower, declare the Obligations to be forthwith due and payable, whereupon all Obligations shall become and be forthwith due and payable, without presentment, notice of dishonor, protest or further notice of any kind, all of which the Borrower hereby expressly waives;

(c) the Lender may, without notice to the Borrower and without further action, apply any and all money owing by the Lender to the Borrower to the payment of the Obligations;

(d) the Lender may exercise and enforce any and all rights and remedies available upon default to a secured party under the UCC, including, without limitation, the right to take possession of Collateral, or any evidence thereof, proceeding without judicial process or by judicial process (without a prior hearing or notice thereof, which the Borrower hereby expressly waives) and the right to sell, lease or otherwise dispose of any or all of the Collateral, and, in connection therewith, the Borrower will on demand assemble the Collateral and make it available to the Lender at a place to be designated by the Lender which is reasonably convenient to both parties;

(e) the Lender may exercise and enforce its rights and remedies under the Loan Documents; and

(f) the Lender may exercise any other rights and remedies available to it by law or agreement.

Notwithstanding the foregoing, upon the occurrence of an Event of Default described in subsections (d) or (e) of Section 8.1, the Obligations shall be immediately due and payable automatically without presentment, demand, protest or notice of any kind.

SECTION 8.3 INTELLECTUAL PROPERTY. In addition to the rights and remedies set forth in Section 8.2 above, upon the occurrence of an Event of Default, the Borrower shall, upon the request of Lender, immediately execute and deliver to Lender a Patent and Trademark Security Agreement, in form and substance satisfactory to the Lender, covering all of the Borrower's Patents, and trademarks, and creating a first and prior lien thereon in favor of Lender.

SECTION 8.4 CERTAIN NOTICES. If notice to the Borrower of any intended disposition of Collateral or any other intended action is required by law in a particular instance, such notice shall be deemed commercially reasonable if given (in the manner specified in Section 9.3) at least ten calendar days before the date of intended disposition or other action.

ARTICLE IX
MISCELLANEOUS

SECTION 9.1 NO WAIVER; CUMULATIVE REMEDIES. No failure or delay by the Lender in exercising any right, power or remedy under the Loan Documents shall operate as a waiver thereof; nor shall any single or partial exercise of any such right, power or remedy preclude any other or further exercise thereof or the exercise of any other right, power or remedy under the Loan Documents. The remedies provided in the Loan Documents are cumulative and not exclusive of any remedies provided by law.

SECTION 9.2 AMENDMENTS, ETC. No amendment, modification, termination or waiver of any provision of any Loan Document or consent to any departure by the Borrower therefrom or any release of a Security Interest shall be effective unless the same shall be in writing and signed by the Lender, and then such waiver or consent shall be effective only in the specific instance and for the specific purpose for which given. No notice to or demand on the Borrower in any case shall entitle the Borrower to any other or further notice or demand in similar or other circumstances.

SECTION 9.3 ADDRESSES FOR NOTICES, ETC. Except as otherwise expressly provided herein, all notices, requests, demands and other communications provided for under the Loan Documents shall be in writing and shall be (a) personally delivered, (b) sent by first class United States mail, (c) sent by overnight courier of national reputation, or (d) transmitted by telecopy, in each case addressed or telecopied to the party to whom notice is being given at its address or telecopier number as set forth below:

If to the Borrower:

OrthoLogic Corp.
1275 West Washington Street
Tempe, AZ 85281
Telecopier: 602/937-5520
Attention: Terry D. Meier

With a copy to (provided such copy shall not be required to effect official notice to Borrower):

Quarles & Brady LLP
One East Camelback, Suite 400
Phoenix, AZ 85012-1659
Telecopier: 602/230-5598
Attention: P. Robert Moya

If to the Lender:

Wells Fargo Business Credit, Inc.
100 West Washington Street, 7th Floor

MAC S4101-076
Phoenix, AZ 85003
Telecopier: 602/378-6215
Attention: Sanat Amladi

or, as to each party, at such other address or telecopier number as may hereafter be designated by such party in a written notice to the other party complying as to delivery with the terms of this Section. All such notices, requests, demands and other communications shall be deemed to have been given on (a) the date received if personally delivered, (b) when deposited in the mail if delivered by mail, (c) the date sent if sent by overnight courier, or (d) the date of transmission if delivered by telecopy, except that notices or requests to the Lender pursuant to any of the provisions of Article II shall not be effective until received by the Lender.

SECTION 9.4 FURTHER DOCUMENTS. The Borrower will from time to time execute and deliver or endorse any and all instruments, documents, conveyances, assignments, security agreements, financing statements and other agreements and writings that the Lender may reasonably request in order to secure, protect, perfect or enforce the Security Interest or the Lender's rights under the Loan Documents (but any failure to request or assure that the Borrower executes, delivers or endorses any such item shall not affect or impair the validity, sufficiency or enforceability of the Loan Documents and the Security Interest, regardless of whether any such item was or was not executed, delivered or endorsed in a similar context or on a prior occasion).

SECTION 9.5 COLLATERAL. This Agreement does not contemplate a sale of accounts, contract rights or chattel paper, and, as provided by law, the Borrower is entitled to any surplus and shall remain liable for any deficiency. The Lender's duty of care with respect to Collateral in its possession (as imposed by law) shall be deemed fulfilled if it exercises reasonable care in physically keeping such Collateral, or in the case of Collateral in the custody or possession of a bailee or other third person, exercises reasonable care in the selection of the bailee or other third person, and the Lender need not

otherwise preserve, protect, insure or care for any Collateral. The Lender shall not be obligated to preserve any rights the Borrower may have against prior parties, to realize on the Collateral at all or in any particular manner or order or to apply any cash proceeds of the Collateral in any particular order of application.

SECTION 9.6 COSTS AND EXPENSES. The Borrower agrees to pay on demand all costs and expenses, including (without limitation) attorneys' fees, incurred by the Lender in connection with the Obligations, this Agreement, the Loan Documents, and any other document or agreement related hereto or thereto, and the transactions contemplated hereby, including without limitation all such costs, expenses and fees incurred in connection with the negotiation, preparation, execution, amendment, administration, performance, collection and enforcement of the Obligations and all such documents and agreements and the

creation, perfection, protection, satisfaction, foreclosure or enforcement of the Security Interest.

SECTION 9.7 INDEMNITY. In addition to the payment of expenses pursuant to Section 9.6, the Borrower agrees to indemnify, defend and hold harmless the Lender, and any of its participants, parent corporations, subsidiary corporations, affiliated corporations, successor corporations, and all present and future officers, directors, employees, attorneys and agents of the foregoing (the "Indemnitees") from and against any of the following (collectively, "Indemnified Liabilities"):

(a) any and all transfer taxes, documentary taxes, assessments or charges made by any governmental authority by reason of the execution and delivery of the Loan Documents or the making of the Advances;

(b) any claims, loss or damage to which any Indemnitee may be subjected if any representation or warranty contained in Section 5.12 proves to be incorrect in any respect or as a result of any violation of the covenant contained in Section 6.4(b); and

(c) any and all other liabilities, losses, damages, penalties, judgments, suits, claims, costs and expenses of any kind or nature whatsoever (including, without limitation, the reasonable fees and disbursements of counsel) in connection with the foregoing and any other investigative, administrative or judicial proceedings, whether or not such Indemnitee shall be designated a party thereto, which may be imposed on, incurred by or asserted against any such Indemnitee, in any manner related to or arising out of or in connection with the making of the Advances and the Loan Documents or the use or intended use of the proceeds of the Advances except to the extent the same arise out of the gross negligence or willful misconduct of Indemnitees.

If any investigative, judicial or administrative proceeding arising from any of the foregoing is brought against any Indemnitee, upon such Indemnitee's request, the Borrower, or counsel designated by the Borrower and satisfactory to the Indemnitee, will resist and defend such action, suit or proceeding to the extent and in the manner directed by the Indemnitee, at the Borrower's sole costs and expense. Each Indemnitee will use its best efforts to cooperate in the defense of any such action, suit or proceeding. If the foregoing undertaking to indemnify, defend and hold harmless may be held to be unenforceable because it violates any law or public policy, the Borrower shall nevertheless make the maximum contribution to the payment and satisfaction of each of the Indemnified Liabilities which is permissible under applicable law. The Borrower's obligation under this Section 9.7 shall survive the termination of this Agreement and the discharge of the Borrower's other obligations hereunder.

SECTION 9.8 PARTICIPANTS. The Lender and its participants, if any, are not partners or joint venturers, and the Lender shall not have any liability or responsibility for any obligation, act or omission of any of its participants. All rights and powers specifically conferred upon the Lender may be transferred

or delegated to any of the Lender's participants, successors or assigns.

SECTION 9.9 EXECUTION IN COUNTERPARTS. This Agreement and other Loan Documents may be executed in any number of counterparts, each of which when so executed and delivered shall be deemed to be an original and all of which counterparts, taken together, shall constitute but one and the same instrument.

SECTION 9.10 BINDING EFFECT; ASSIGNMENT; COMPLETE AGREEMENT; EXCHANGING INFORMATION. The Loan Documents shall be binding upon and inure to the benefit of the Borrower and the Lender and their respective successors and assigns, except that the Borrower shall not have the right to assign its rights thereunder or any interest therein without the Lender's prior written consent. This Agreement, together with the Loan Documents, comprises the complete and integrated agreement of the parties on the subject matter hereof and supersedes all prior agreements, written or oral, on the subject matter hereof. Without limiting the Lender's right to share information regarding the Borrower and its Affiliates with the Lender's participants, accountants, lawyers and other advisors, the Lender, Wells Fargo Bank, N.A. or Norwest Corporation, and all direct and indirect subsidiaries of Wells Fargo Bank, N.A. or Norwest Corporation, may exchange any and all information they may have in their possession regarding the Borrower and its Affiliates, and the Borrower waives any right of confidentiality it may have with respect to such exchange of such information.

SECTION 9.11 SEVERABILITY OF PROVISIONS. Any provision of this Agreement which is prohibited or unenforceable shall be ineffective to the extent of such prohibition or unenforceability without invalidating the remaining provisions hereof.

SECTION 9.12 HEADINGS. Article and Section headings in this Agreement are included herein for convenience of reference only and shall not constitute a part of this Agreement for any other purpose.

SECTION 9.13 GOVERNING LAW; JURISDICTION; VENUE; WAIVER OF JURY TRIAL. The Loan Documents shall be governed by and construed in accordance with the substantive laws (other than conflict laws) of the State of California. The parties hereto hereby (i) consents to the personal jurisdiction of the state and federal courts located in the State of California in connection with any controversy related to this Agreement; (ii) waives any argument that venue in any such forum is not convenient, (iii) agrees that any litigation initiated by the Lender or the Borrower in connection with this Agreement or the other Loan Documents shall be venued in either the Superior Court of Los Angeles County, or the Central District Court of California; and (iv) agrees that a final judgment in any such suit, action or proceeding shall be conclusive and may be enforced in other jurisdictions by suit on the judgment or in any other manner provided by law. THE PARTIES WAIVE ANY RIGHT TO TRIAL BY JURY IN ANY ACTION OR PROCEEDING BASED ON OR PERTAINING TO THIS AGREEMENT.

IN WITNESS WHEREOF, the parties hereto have caused this Agreement to be executed by their respective officers thereunto duly authorized as of the date first above written.

ORTHOLOGIC CORP., a Delaware corporation

By _____

Its _____

WELLS FARGO BUSINESS CREDIT, INC.

By _____

Its _____

Table of Exhibits and Schedules

Exhibit A	Form of Revolving Note
Exhibit B	Compliance Certificate
Exhibit C	Premises
Schedule 5.1	Trade Names, Chief Executive Office, Principal Place of Business, and Locations of Collateral
Schedule 5.4	Subsidiary
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Schedule 7.1	Permitted Liens
Schedule 7.2	Permitted Indebtedness and Guaranties

Exhibit A to Credit and Security Agreement

REVOLVING NOTE

$10,000,000.00 _____, _____

_____, 2000

For value received, the undersigned, OrthoLogic Corp., a Delaware corporation (the "Borrower"), hereby promises to pay on the Termination Date under the Credit Agreement (defined below), to the order of Wells Fargo Business Credit, Inc., a Minnesota corporation (the "Lender"), at its main office in Phoenix, Arizona, or at any other place designated at any time by the holder hereof, in lawful money of the United States of America and in immediately available funds, the principal sum of TEN MILLION DOLLARS ($10,000,000.00) or, if less, the aggregate unpaid principal amount of all Revolving Advances made by the Lender to the Borrower under the Credit Agreement (defined below) together with interest on the principal amount hereunder remaining unpaid from time to time, computed on the basis of the actual number of days elapsed and a 360-day year, from the date hereof until this Note is fully paid at the rate from time to time in effect under the Credit and Security Agreement of even date herewith (as the same may hereafter be amended, supplemented or restated from time to time, the "Credit Agreement") by and between the Lender and the Borrower. The principal hereof and interest accruing thereon shall be due and payable as provided in the Credit Agreement. This Note may be prepaid only in accordance with the Credit Agreement.

This Note is issued pursuant, and is subject, to the Credit Agreement, which provides, among other things, for acceleration hereof. This Note is the Revolving Note referred to in the Credit Agreement. This Note is secured, among other things, pursuant to the Credit Agreement and the Security Documents as therein defined, and may now or hereafter be secured by one or more other security agreements, mortgages, deeds of trust, assignments or other instruments or agreements.

The Borrower hereby agrees to pay all costs of collection, including attorneys' fees and legal expenses in the event this Note is not paid when due, whether or not legal proceedings are commenced.

Presentment or other demand for payment, notice of dishonor and protest are expressly waived.

ORTHOLOGIC CORP., a Delaware corporation

By ----------

Its ----------

EXHIBIT A

Exhibit B to Credit and Security Agreement

COMPLIANCE CERTIFICATE

To: _____

Wells Fargo Business Credit, Inc.

Date: _____, _____

Subject: OrthoLogic Corp.
Financial Statements

In accordance with our Credit and Security Agreement dated as of _____, 2000 (the "Credit Agreement"), attached are the financial statements of OrthoLogic Corp., a Delaware corporation (the "Borrower") as of and for _____, 2000 (the "Reporting Date") and the year-to-date period then ended (the "Current Financials"). All terms used in this certificate have the meanings given in the Credit Agreement.

I certify that the Current Financials have been prepared in accordance with GAAP, subject to year-end audit adjustments, and fairly present the Borrower's financial condition and the results of its operations as of the date thereof.

EVENTS OF DEFAULT. (Check one):

[ ] The undersigned does not have knowledge of the occurrence of a Default or Event of Default under the Credit Agreement.

[ ] The undersigned has knowledge of the occurrence of a Default or Event of Default under the Credit Agreement and attached hereto is a statement of the facts with respect to thereto.

I hereby certify to the Lender as follows:

[ ] The Reporting Date does not mark the end of one of the Borrower's fiscal quarters, hence I am completing only paragraph __ below.

[ ] The Reporting Date marks the end of one of the Borrower's fiscal quarters, hence I am completing all paragraphs below except paragraph __.

[ ] The Reporting Date marks the end of the Borrower's fiscal year, hence I am completing all paragraphs below.

[TO COME]

EXHIBIT B

Exhibit C to Credit and Security Agreement

PREMISES

The Premises referred to in the Credit and Security Agreement are legally described as follows:

(See attached 3 pages)

EXHIBIT C

Schedule 5.1 to Credit and Security Agreement

Trade Names, Chief Executive Office, Principal Place of Business, and Locations of Collateral

TRADE NAMES:

Iatromed Inc., a Delaware corporation, which changed its name to OrthoLogic Corp. on June 28, 1991.

CHIEF EXECUTIVE OFFICE/PRINCIPAL PLACE OF BUSINESS:

1275 West Washington Street
Tempe, AZ 85281

OTHER INVENTORY AND EQUIPMENT LOCATIONS:

Most of the collateral is located at the principal place of business, however, the Company keeps some equipment at the various sales peoples' sites throughout the country.

SCHEDULE 5.1

Schedule 5.4 to Credit and Security Agreement

SUBSIDIARY

OrthoLogic Canada (previously Toronto Medical Corp.)

SCHEDULE 5.4

Schedule 5.6 to Credit and Security Agreement

Pending Litigation

Case Number:	Name:	Location:
96 CV 01514	Chan v. OrthoLogic Corp.	Arizona Dist. Ct.
96 CV 01520	Boren v. Weinstein	Arizona Dist. Ct.

96 CV 01563	Silveira v. Weinstein	Arizona Dist. Ct.
96 CV 01615	Cohen v. OrthoLogic Corp.	Arizona Dist. Ct.
96 CV 01643	Barton v. Weinstein	Arizona Dist. Ct.
96 CV 01667	Draker v. Weinstein	Arizona Dist. Ct.
96 CV 01678	Rutkin v. Weinstein	Arizona Dist. Ct.
96 CV 01713	DeFelice v. OrthoLogic Corp.	Arizona Dist. Ct.
96 CV 01891	Longacre v. Weinstein	Arizona Dist. Ct.
96 CV 01910	Bailey v. Weinstein	Arizona Dist. Ct.
96 CV 01937	Kyser v. OrthoLogic Corp.	Arizona Dist. Ct.
96 CV 02451	Rapport v. Weinstein	Arizona Dist. Ct.
98 CV 00621	OrthoLogic Corp. v. Freeman	Arizona Dist. Ct.
96 CV 01668	Katz, et al. v. OrthoLogic Corp.	Arizona Dist. Ct.
TJ97-01248	OrthoLogic Corp./Clemente Ranch HOA	Maricopa County Sup. Ct.
CV96-10799	Cooper v. Weinstein	Maricopa County Sup. Ct.
CV99-12910	Elizabeth Worley v. Samaritan Health System/OrthoLogic Corp.	Maricopa County Sup. Ct.

SCHEDULE 5.6

Schedule 7.1 to Credit and Security Agreement

Permitted Liens

Creditor:	Collateral:
CAPITAL LIENS:	
Norstan Financial Services, Inc.	Telephone Equipment
Associates Leasing, Inc.	Equipment
The CIT Group	Computer Equipment
The CIT Group	Computer Software
Pitney Bowes Credit	Equipment
The CIT Group	Equipment
The CIT Group	Equipment
T&W Funding Company II, LLC	Flooring Equipment
CURRENT CREDIT FACILITY:	
Silicon Valley Bank	

SCHEDULE 7.1

Schedule 7.2 to Credit and Security Agreement

Permitted Indebtedness and Guaranties

Creditor:	Collateral:
CAPITAL LIENS:	

Norstan Financial Services, Inc.	Telephone Equipment
Associates Leasing, Inc.	Equipment
The CIT Group	Computer Equipment
The CIT Group	Computer Software
Pitney Bowes Credit	Equipment
The CIT Group	Equipment
The CIT Group	Equipment
T&W Funding Company II, LLC	Flooring Equipment

CURRENT CREDIT FACILITY:

Silicon Valley Bank

SCHEDULE 7.2

EXHIBIT 10.19

LEASE EXTENSION AND AMENDMENT AGREEMENT

THIS AGREEMENT made the 29th day of September, 1998.

BETWEEN:

TMC (HERITAGE) CORP.
(the "Landlord")

OF THE FIRST PART

- and -

ORTHOLOGIC CANADA LTD.
(the "Tenant")

OF THE SECOND PART

- and -

ORTHOLOGIC CORP.
(the "Idemnifier")

OF THE THIRD PART

WHEREAS by an indenture of lease made the 1st day of March, 1997 (the "Lease") between Toronto Medical Corp. (the "Prior Landlord") and the Tenant (then known as Toronto Medical Orthpaedics Ltd.) the Prior Landlord leased to the Tenant the Premises (as defined in the Lease) upon and subject to the terms and conditions contained in the Lease.

AND WHEREAS subsequent to the execution of the Lease by the Prior Landlord, the Prior Landlord changed its corporate name to Saringer Investments Ltd.;

AND WHEREAS subsequent to the execution of the Lease by the Tenant, the Tenant changed its corporate name to Orthologic Canada Ltd.;

AND WHEREAS on November 14, 1997 the Prior Landlord assigned its interest in the Lease to the Landlord, notice of which was provided to the Tenant;

AND WHEREAS section 9.1 of the Lease granted the Tenant the right to renew the Term of the Lease for a further five (5) year term (the "First Renewal Term");

AND WHEREAS the Landlord and the Tenant have agreed that;

1 the First Renewal Term shall be reduced to a three (3) year term, and

2 the Base Rent for the First Renewal Term shall be the same Base Rent paid by the Tenant under the Lease for the Term.

AND WHEREAS pursuant to an Indemnity Agreement dated March 1, 1997 (the "Indemnity"), the Indemnifier agreed that throughout the Term of the Lease and any extension or renewal the Indemnifier will:

1 promptly pay all Base Rent, Additional Rent and any other amount payable by the Tenant under the Lease, whether to the Landlord or anyone else; and

2 promptly perform each and every obligation of the Tenant under the Lease, pursuant to the terms and conditions contained in the Indemnity.

NOW THEREFORE THIS AGREEMENT WITNESSETH that in consideration of the premises and the terms and conditions hereinafter set forth, other good and valuable consideration and the sum of Two Dollars ($2.00) now paid by each party to the other (the receipt and sufficiency of which is hereby acknowledged), the parties agree as follows:

1 The parties hereby acknowledge, confirm and agree that the foregoing recitals are true in substance and in fact.

2 Where used herein, all capitalized terms and expressions have the same meaning as they have in the Lease, unless a contrary expression is expressed herein.

3 Subject to paragraph 6 hereof, the Landlord and the Tenant agree, subject to the terms of the Lease as amended hereby, to renew the Lease for the First Renewal Term. The First Renewal Term shall be for a term of three (3) years from March 1, 1999 until February 28, 2002, and section 9.1 of the Lease shall be amended accordingly by deleting the word "five (5)" appearing in the tenth line of the first paragraph and replacing it with the word "three (3)".

4 The Base Rent for the First Renewal Term shall be the same Base Rent that was paid by the Tenant during the Term, being the annual sum of One Hundred and Forty Two Thousand Two Hundred and Eighty Five Dollars ($142,285.00) of lawful money of Canada, such amount payable in twelve (12) equal monthly installments of Eleven Thousand Eight Hundred and Fifty Seven Dollars ($11,857.00) in advance on the first day of each and every month during the First Renewal Term commencing March 1, 1999.

5 Pursuant to section 12.2(a) of the Lease, the Landlord's address for the service shall be amended to read as follows:

"TMC" Heritage Corp.
65 Proctor Avenue
Thornhill, Ontario
L3T 1M6
Attention: Mr. JP. Scheidegger

Facsimile: (905) 882-6678

With a copy to:
Koskie Minsky
Barristers and Solicitors
Suite 900, Box 52
20 Queen Street West
Toronto, Ontorio
MSH 3R3
Attention: Mr. George P. Dzuro
Facsimile: (416) 977-3316

6 The renewal of the Lease for the First Renewal Term is subject to and conditional upon compliance by the Tenant with the provisions of section 9.1 of the Lease and, in particular, that: the Tenant has not been in default under the terms of the Lease on more than two (2) occasions in any consecutive twelve (12) month period occurring prior to the commencement date of the First Renewal Term; or the Tenant is not in default under the terms of the Lease on the last day of the Term.

If the foregoing condition has not been performed at or prior to the commencement date of the First Renewal Term, the Landlord may, by written notice to the Tenant, terminate all of its obligations with respect to the First Renewal Term and the Landlord shall be released from all of its obligations under the Lease, as amended hereby, with respect to the First Renewal Term. The foregoing condition may be waived be by the Landlord by notice in writing, without prejudice to any of the Landlord's rights to renew the Lease for the First Renewal Term and pursue any and all other legal remedies the Landlord may have, under the Lease or otherwise, with respect to any default by the Tenant under the terms of the Lease.

The Indemnifier acknowledges, confirms and agrees that the Indemnity shall continue in full force and effect in favour of the Landlord pursuant to its terms and conditions with respect to the Lease and the obligations of the Tenant thereunder, as amended and renewed pursuant to this agreement.

2 Save and except as provided for herein, the parties hereto acknowledge and agree that all of The terms and conditions of the Lease shall continue in full force and effect, save and except as amended hereby.

3 This agreement shall ensure to the benefit of and be binding upon the parties hereto and their respective successors and assigns.

4 This agreement may be executed in several counterparts each of which so executed shall be deemed to be an original and such counterparts together shall constitute one and the same agreement. This agreement may be executed by one or more of the parties hereto by way of telecopying device and such execution shall be accepted as though signatures thereof were signed originals and in the event of such method of execution each party agrees to

provide the other parties with copies of this agreement bearing original signatures within a reasonable time after execution.

IN WITNESS WHEREOF the parties hereto have duly executed this agreement on the date first above written.

TMC (HERITAGE) CORP.

Per:

(Authorized Signing Officer)

ORTHOLOGIC CANADA LTD.

Per:

(Authorized Signing Officer)

OTHOLOGIC CORP.

Per:

(Authorized Signing Officer)

OrthoLogic, Corp.
Statement of Computation of Net Loss per Weighted Average
Number of Common Shares Outstanding
(in thousands, except per share amounts)

	Years Ended December 31,		
	1999	1998	1997
Net loss	$ (586)	$(17,838)	$(17,714)
Common shares outstanding at end of period	27,638	25,302	25,255
Adjustment to reflect weighted average for shares issued during the period	(1,560)	(11)	(139)
Weighted average number of common shares outstanding	26,078	25,291	25,116
Net loss per weighted average number of common shares outstanding	(0.02)	(0.71)	(0.71)

GENERAL

The goal of OrthoLogic Corp. ("the Company") is to become the worldwide leader in fracture healing and orthopedic rehabilitation. OrthoLogic develops, manufactures, and distributes products that support physicians and hospitals improve the quality of life for their patients. OrthoLogic is committed to providing technologically advanced, superior products to customers at affordable costs.

OrthoLogic was founded in July 1987. Through August 1996, the Company was engaged primarily in the commercialization of the Company's proprietary BioLogicTM technology in order to develop products that stimulate the healing of bone fractures and spinal fusions. The Company expanded its product base to include continuous passive motion ("CPM") products on August 30, 1996 by acquiring Sutter Corporation. The Company completed two additional CPM related acquisitions in March 1997. These acquisitions allowed the Company to develop, manufacture and market orthopedic rehabilitation products and services. During the first quarter of 1998, the Company completed the integration of all the CPM administrative and service related operations from these acquisitions into one Phoenix based headquarters.

OrthoLogic periodically discusses with third parties the possible acquisition of technology, product lines, and businesses in the orthopedic health care market. It has previously entered into letters of intent that provides the Company with an exclusivity period during which it considers possible acquisitions.

MARKET OVERVIEW

Sales in the orthopedic market are in excess of $10 billion with an average annual growth rate for the last five years of 6.8%. The average annual growth rate for the next five years is projected to be 8%. The key driver for most of this growth rate is the age segment of the population between 45 and 64. This age segment favorably impacts the demand for fracture healing, spine and osteoarthitis products.

OrthoLogic competes in three segments of the orthopedic market; fracture healing, rehabilitation and injectable products. The fracture healing product line consists of electronic bone growth stimulators for long bones and a new device, SpinaLogic. The recently FDA approved SpinaLogic provides stimulation for the lumbar lower portion of the spine. The fracture healing market for the long bone has been growing at an average annual rate of 8% over the last five years. The market growth for spine stimulation has been growing at an average annual rate of 12%. The rehabilitation product line consists of continuous passive motion devices for both the lower and upper extremities and the ancillary products such as braces and cryotherapy equipment. The rehabilitation market has been growing at a rate of 5.4% for the past five years. The injectable product line consists of the Hyalgan(R) brand of hyaluronic acid for pain relief of the osteoarthritis of the knee. The orthopedic market for injectable hyaluronic acid was established in 1997. Retail sales for this product during 1999 were approximately $140 million.

PRODUCT OVERVIEW
BONE GROWTH STIMULATION

OrthoLogic competes in the market for long bone stimulation with the OL-1000, OL-1000 Single Coil and custom curve coil products.

Bone growth stimulation devices are noninvasive physician prescribed magnetic field bone growth stimulators designed for home treatment of patients with a non-union fracture. Market growth for fractures of the long bone is dependent on manufactures' continuing to demonstrate the economic and patient benefits of using bone growth stimulation prior to moving forward with more expensive surgical alternatives. During November 1999, a Decision Memorandum issued by the Health Care Financing Administration (HCFA) changed the acceptance criteria for Medicare patients who qualify for treatment with a bone growth stimulator. The new criteria broaden the potential patient population by removing the six-month

period required to determine the existence of a non-union fracture. Due to HCFA's Y2K policy, the new guideline was not formally implemented until April 1, 2000. Over the past few years, both the United States Food and Drug Administration (FDA) and HCFA have changed both the definitions of a non-union fracture and the reimbursement guidelines for using a bone growth stimulator. The new HCFA reimbursement guidelines have defined a non-union fracture as being established when at least 90 days have passed and healing has ceased. This new definition allows for non-unions to be treated with the Company's OL-1000 product as soon as 90 days post-injury. The OrthoFrame(R) and the OrthoFrame/Mayo(R) products are external fixation devices used in conjunction with surgical procedures.

The FDA approved SpinaLogic in December of 1999. SpinaLogic is a technologically advanced medical device that can be used as an adjunct to spinal fusion surgery to improve the probability of a successful fusion. SpinaLogic is a non-invasive externally worn device, that delivers a unique, patented magnetic signal to the surgical site and requires only a 30-minute daily treatment cycle. There are currently only two other approved noninvasive spine bone growth stimulators on the market. The Company began commercial distribution of SpinaLogic during the last few business days of December. To enhance market penetration, the Company plans to supplement the distribution of the product using a combination of its own direct sales force and regional spine product distributors. Full distribution in the United States will occur in early fiscal year 2000, with distribution for Europe planned for late third quarter.

The main call point for fracture healing product sales is the physician office. Orthopedic surgeons, spine surgeons, neurosurgeons and podiatrists prescribe bone growth stimulators. They are placed on patients in the physician's office or the home. Strong relationships with the physician, reimbursement coverage, product efficacy and prompt customer service are the most important factors in the sale process.

Fracture healing products are placed on to patients upon receipt of a written prescription. The Company submits a bill to the patient's insurance carrier for reimbursement. The Company recognizes revenue at the time the product is placed on the patient. The OrthoFrame(R) and the OrthoFrame/Mayo(R) products are sold to hospitals. The revenue is recognized on these products at the point a purchase order is received and the product is sent to the hospital.

REHABILITATION PRODUCTS

CPM devices provide controlled, continuous movement to joints and limbs without requiring the patient to exert muscular effort and is intended to be applied immediately following the orthopedic trauma or surgery. The products are designed to reduce swelling, increase joint range of motion, reduce the length of hospital stay, reduce the incidence of post-trauma, and post surgical complication. OrthoLogic competes in the rehabilitation market with a complete line of lower and upper extremity CPM devices and ancillary products such as knee braces, splints and cryotherapy products. Lower extremity CPM is an accepted treatment modality for knee surgical procedures such as total knee replacement (TKR) and anterior cruciate ligament reconstruction (ACL). Due to the wide acceptance of lower extremity CPM and the number of companies competing for this business, managed care companies have been decreasing their reimbursement rates. Upper extremity CPM for the shoulder, elbow, wrist and hand are continuing to gain acceptance in the rehabilitation market. No outcomes based on clinical studies have been completed supporting the efficacy of upper extremity CPM. As a result, there is no Medicare reimbursement to date for this treatment. The majority of the reimbursement payments for upper extremity are Worker's Compensation related. This segment of the market is expected to experience some growth as upper extremity CPM becomes accepted as a standard treatment modality. Cryotherapy is used to cool the operative or injured site in order to prevent pain and swelling. The Company produces its own cryotherapy device, the Blue Arctic.

The main call points for the rehabilitation market are hospitals, orthopedic surgeons, plastic surgeons, physical therapists and hand therapists. Rehabilitation products are sold and rented to hospital customers and rented directly to patients in the home. The length of use in the hospital rental business continues to decline because of shorter hospital stays. Historically, rehabilitation product sales were based on strong customer relationships and a high level of customer service. Due to cost cutting initiatives by managed care companies, price has become a major factor with the orthopedic surgeon having

less impact on the choice of rehabilitation providers.

The Company maintains a fleet of CPM devices that are rented to patients upon receipt of a written prescription. The Company recognizes rental revenue daily during the period of usage. Revenue on ancillary products is recognized when the patient receives the product. A bill is sent to the patient's insurance carrier for reimbursement.

HYALGAN(R)

The Company began marketing Hyalgan(R) to orthopedic surgeons during July 1997 under a Co-Promotion Agreement (the "Co-Promotion Agreement") with Sanofi Pharmaceuticals, Inc. Hyalgan(R) is used for relief of pain from osteoarthritis of the knee for those patients who have failed to respond adequately to simple analgesics.

In January 2000, the FDA approved new labeling for Hyalgan(R). The labeling states that Hyalgan(R) can produce pain relief beyond 26 weeks. This labeling will allow the Company to use published clinical papers exhibiting up to 12 months of pain relief with a single course of therapy. In addition, the revised label allows the Company to promote Hyalgan(R) for repeated cycles of treatment.

Short-term market growth for Hyalgan(R) is dependent on orthopedic surgeons using hyaluronic acid early in the continuum of care as a replacement for non-steroidal anti-inflammatory drugs (NSAIDs) and steroidals. Longer-term market growth will depend in part on expanded applications for Hyalgan(R) use beyond osteoarthritis of the knee.

The Company recognizes fee revenue when the product is shipped from the distributor to the orthopedic surgeon under a purchase order. The fee revenue is based upon the number of units sold at the wholesale acquisition cost less amounts for distribution costs, discounts, rebates, returns, product transfer price, overhead factor and a royalty factor.

CHRYSALIN

In January 1998, the Company acquired a minority interest in a biotech firm, Chrysalis Bio Technology, Inc., for $750,000. Chrysalin is a synthetically manufactured peptide that has shown potential in preclinical animal studies to accelerate fracture healing. Chrysalin represents a portion of the receptor-binding domain of the human thrombin molecule, which is actively involved in the healing process for both soft tissue and bone. By mimicking specific attributes of the thrombin molecule, Chrysalin stimulates the body's natural healing processes, resulting in accelerated tissue repair. On January 12, 2000, the Company began enrolling patients in an FDA authorized combined

Phase I/II clinical trial for Chrysalin. The trial consists of a prospective, randomized double-blind study of 90 patients in three to five clinical centers to evaluate the safety and preliminary efficacy of Chrysalin. Patients will receive one injection of Chrysalin or placebo (saline solution) at the time the fracture is set and will be monitored weekly to evaluate healing. Depending on the rate of patient enrollment, the trial could be completed by the end of fiscal year 2000.

OTHER

The Company reported a net loss attributable to common shareholders of $586,000 during 1999 with an accumulated deficit as of December 31, 1999 of $52.0 million. As of December 31, 1999, the Company had approximately $33.6 million in net operating loss carryforwards for federal tax purposes. The Company's ability to utilize its net operating loss carryforwards may be subject to annual limitations in future years pursuant to the "change in ownership rules" under Section 382 of the Internal Revenue Code of 1986, as amended, and is dependent on the Company's future profitability.

Future operating results will depend on numerous factors including, but not limited to, demand for the Company's products, the timing, cost and acceptance of product introductions and enhancements made by the Company or others, level of third party payment, alternate treatments which currently exist or may be introduced in the future, practice patterns, competitive conditions in the industry, general economic conditions and other factors influencing the orthopedic market in the United States or other countries in which the Company

operates or expands. In addition, efforts to reform the health care systems and contain health care expenditures in the United States could adversely affect the Company's revenues and results of operations. Furthermore, the Company's products are subject to regulation by the FDA, and FDA regulations may adversely affect the marketing and sales of the Company's products. The Company cannot determine the effect such trends and regulations will have on its operations, if any.

RESULTS OF OPERATIONS YEARS ENDED
DECEMBER 31, 1997, 1998 AND 1999

REVENUES. OrthoLogic's total revenues increased 10% from $75.4 million in 1998 to $83.2 million in 1999. OrthoLogic's revenues consist of net sales of the bone growth stimulator for long bone and spine, fracture fixation devices, orthopedic rehabilitation equipment and ancillary products, net rentals of CPM equipment and fee revenues from the co-promotion agreement. The Company recognizes fee revenue for the distribution of Hyalgan(R). Net sales increased by 10% to $32.6 million during 1999. The growth in net sales is primarily attributed to an increased demand for orthopedic rehabilitation products. Sales recorded for the OL1000 product were relatively constant over the two-year period. The Company recorded its first sale of SpinaLogic units after receiving FDA approval in late December 1999. Net rentals for CPM equipment increased by $5.2 million in 1999 or 14% over 1998 rental revenue. Fee revenue from Hyalgan(R) decreased from 1998 to 1999 by $440,000 or 5%.

Total revenues decreased 2% from $77.0 million in 1997 to $75.4 million in 1998. The decrease in net sales of 18% or $6.6 million is primarily attributable to the Company restructuring its sales force, marketing and managed care operations. Prior to 1998, the primary source of sales for the OL-1000 product was through distributor sales teams. As a result of the change in the sales structure, sales of the OL-1000 fell during 1998. Net rentals of CPM equipment stayed fairly constant between 1997 and 1998. Fee revenue was recorded for Hyalgan(R) over twelve months of 1998, after launching the distribution of the product during 1997.

GROSS PROFIT. Gross profit increased 12% from $57.7 million in 1998 to $64.7 million in 1999. The gross profit on net sales was 65% in 1999 compared to 64% in 1998. The overall improvement in the margin is attributable to 14% growth in net rentals. The cost of rentals as a percent of net rentals decreased from 19% in 1998 to 17% in 1999. For future margins, the recent launch of SpinaLogic in late 1999 is anticipated to allow the Company economies of scale in the current manufacturing process by adding the production of an additional product in future periods. Overall, gross profit decreased by 2% in 1998 from 1997. The decrease in gross profit is reflective of the overall decrease in total revenues during 1998. The cost of goods sold increased as a percent of net sales to 36% in 1998 from 28% in 1997. The increase in cost of goods sold is due to the change in the mix of the products sold. The decrease in the net sales of OL-1000 was partially offset by increased sales of CPM equipment and ancillary products for rehabilitation, which have lower margins.

SELLING, GENERAL AND ADMINISTRATIVE ("SG&A") EXPENSES. SG&A expenses decreased from $72.0 million during 1998 to $61.9 million during 1999, a 14% decrease. A significant portion of the decrease in cost is directly related to bad debt of approximately $9.3 million recorded during the first quarter of 1998. The increase was a result of management's decision to focus resources on the collection of current sales and on re-engineering the overall process of billing and collections. The increased sales recorded in 1999 have related variable costs associated with the increased revenues, such as commissions and bad debt reserve. Despite the increase in variable costs associated with the higher revenues, SG&A costs decreased from 1998 to 1999. Excluding the first quarter

increase in bad debt expense in 1998, SG&A expenses would have been 83% of total revenues, compared to 74% in 1999. SG&A costs during 1997 were 80% of sales.

RESEARCH AND DEVELOPMENT EXPENSES. Research and development expenses decreased slightly in 1999 from 1998. R&D costs were increased in the third quarter of 1998, when the Company paid an additional fee of $750,000 for the initial license of Chrysalin.

As part of the transaction, OrthoLogic was awarded various options to license orthopedic applications of Chrysalin. In January of 1999, OrthoLogic exercised the option to acquire the rights to Chrysalin for fracture indications for the

U.S. market. As part of the license agreement, and in conjunction to FDA clearance to begin human clinical trials, OrthoLogic made a $500,000 milestone payment to Chrysalis Biotechnology in the fourth quarter of 1999.

RESTRUCTURING AND OTHER CHARGES. During the third quarter of 1997, the Company restructured its sales, marketing and managed care groups. As a result of their restructuring and a second consecutive quarter of declining sales of the OrthoLogic 1000 in the third quarter of 1997, the Company determined that certain dealer intangibles acquired in the transition to a direct sales force had been impaired. The Company recorded a restructuring charge of $13.8 million in the third quarter, composed of a $10.0 million write-off of its dealer intangibles and $3.8 million in severance, facility closing and related costs. During 1999 and 1998, $216,000 and $399,000 of the 1997 restructuring charge was reversed.

NET INCOME (LOSS). Net income in 1999 of $238,000 consists of an operating profit of $148,000 and other income. Net loss during 1998 consists of an operating loss of $16.9 million offset by other income of $354,000. Net loss during 1997 is composed of an operating loss of $19 million offset by other income of $1.5 million, consisting primarily of interest income of $1.4 million.

LIQUIDITY AND CAPITAL RESOURCES

The Company has financed its operations through the public and private sales of equity securities and product revenues.

In July 1998, the Company completed a private equity placement with two investors, an affiliate of Credit Suisse First Boston Corp. and Capital Ventures International. Under the terms of the Purchase Agreement, OrthoLogic sold 15,000 shares of Series B convertible Preferred Stock for $15 million (before costs). The Series B Convertible Preferred Stock is convertible into shares of Common Stock and will automatically convert, to the extent not previously converted, into Common Stock four years following the date of issuance. Each share of Series B convertible Preferred Stock is convertible into Common Stock at a per share price equal to the lesser of the average of the 10 lowest closing bids during the 30 days prior to conversion, or $3.0353. In the event of certain Mandatory Redemption Events, each holder of Series B Preferred Shares will have the right to require the Company to redeem those shares for cash at the Mandatory Redemption Price. Mandatory Redemption Events include, but are not limited to: the failure of the Company to timely deliver Common Shares as required under the terms of the Series B Preferred Shares, or Warrants; the Company's failure to satisfy registration requirements applicable to such securities; the failure of the Company's stockholders to approve the transactions contemplated by the Securities Purchase Agreement related to the issuance of the Series B Preferred Shares; the failure by the company to maintain the listing of its Common Stock on NASDAQ or another national securities exchange; and certain transactions involving the sale of assets or business combinations involving the Company. In the event of any liquidation, dissolution or winding up of the Company, holders of the Series B Shares are entitled to receive, prior and in preference to any distribution of any assets of the Company to the holders of Common Stock, the Stated Value for each Series B Preferred Shares outstanding at that time. The Purchase Agreement contains strict covenants that protect against hedging and short-selling of OrthoLogic Common Stock while the purchaser holds shares of the Series B Convertible Preferred Stock.

In connection with the private placement of the Series B Convertible Preferred Stock, OrthoLogic issued to the purchasers warrants to purchase 40 shares of Common Stock for each share of Series B Convertible Preferred Stock, exercisable at $5.50. These warrants expire in 2008. The warrants were valued at $1,093,980. Additional costs of the private placement were approximately $966,000. Both the value of the warrants and the cost of the equity offering were recognized over the 10 month conversion period as an "accretion of non-cash Preferred Stock Dividends" for the amount of $617,994 per quarter. The Company filed a registration statement covering the underlying Common Stock.

Proceeds from the private placement were used to fund new product opportunities, including SpinaLogic, Chrysalin and Hyalgan(R), as well as to complete the re-engineering of the Company's key business processes.

At the close of business on December 31, 1999, 4,820 shares of Series B Convertible Preferred Stock had been converted into 2,053,003 shares of Common Stock.

From the inception of the Company through December 31, 1999, equity financing has resulted in net proceeds of $134.4 million. At December 31, 1999, the

Company had cash and cash equivalents of $6.0 million and short term investments of $250,000. Working capital increased 5% from $38.8 million at December 31, 1998 to $40.9 million at December 31, 1999.

Through December 31, 1999, the Company had secured a $7.5 million accounts receivable revolving line of credit and a $2.5 million revolving term loan from a bank. The maximum amount that may be borrowed under this agreement is $10 million. The Company may borrow up to 70% of the eligible accounts receivable under the accounts receivable revolving line of credit and 50% of the net book value of CPM rental fleet under the revolving term loan. The accounts receivable revolving line of credit matures December 3, 2000 and the revolving term loan on November 30, 2000. Interest is payable monthly on the accounts receivable revolving line of credit and amortized principal and interest are due monthly on the revolving term loan. The interest rate is prime plus 0.65% for the accounts receivable line of credit, and prime plus 1.05% for the revolving term loan. There are certain financial covenants and reporting requirements associated with the loans. In connection with these loans, the Company issued a warrant to purchase 10,000 shares of Common Stock at a price equal to the average fair market value for five days prior to the closing of the loans.

On February 28, 2000, the Company obtained a new $10 million accounts receivable revolving line of credit with a different bank. The Company may borrow up to 75% of the eligible accounts receivable. The interest rate is at prime for the revolving line of credit. Interest accruing on the note and a monthly administration fee is due in arrears on the first day of each month. The revolving note matures February 28, 2003. There are certain financial covenants and reporting requirements associated with the loan. Included in the financial covenants are (1) tangible net worth of not less than $43 million, (2) a quick ratio of not less than 2.0 to 1.0, (3) a debt to tangible net worth ration of not less than 0.50 to 1.0, and (4) capital expenditures will not exceed more than $7.0 million dollars during any fiscal year.

The Company anticipates that its cash on hand and the funds available from the line of credit will be sufficient to meet the Company's presently projected cash and working capital requirements for the next 12 months. There can be no assurance, however, that this will prove to be the case. The timing and amounts of cash used will depend on many factors, including the Company's ability to continue to increase revenues, reduce and control its expenditures, become profitable and collect amounts due from third party payers. Additional funds may be required if the Company is not successful in any of these areas. The Company's ability to continue funding its planned operations beyond the next 12 months is dependant upon its ability to generate sufficient cash flow to meet its obligations on a timely basis, or to obtain additional funds through equity or debt financing, or from other sources of financing, as may be required.

Net cash provided by operations during 1999 was $4.7 million. This improvement in operating cash flow was primarily a result of (1) net income of $237,901, (2) a decrease in inventories of $2.7 million and depreciation/amortization of $6.8 million, partially offset by an increase in accounts receivable of $3.4 million. Net cash used in operations during 1998 was $10 million, an increase of 108% over the cash used in operations of $4.8 million in 1997. The 1998 amount was primarily due to (1) a net loss of $16.6 million, (2) a decrease in accrued and other current liabilities of $4.5 million, and (3) an increase in inventories of $1.4 million, which was offset by a decrease in accounts receivable of $5.7 million and depreciation/amortization of $6.5 million. The 1997 amount was primarily due to (1) a net loss of $17.7 million, (2) an increase in accounts receivable of $2.8 million and (3) an increase in inventories of $1.5 million, which was offset by a non-cash restructuring charge of $13.8 million and depreciation/amortization of $5.5 million.

As discussed in greater detail in Note 13 to the Consolidated Financial Statements the Company has been named as a defendant in certain lawsuits. Management believes that the allegations are without merit and will vigorously defend them. No costs related to the potential outcome of these actions have been accrued.

MARKET RISKS

The Company has exposure to foreign exchange rates through its manufacturing subsidiary in Canada.

The Company does not use foreign currency exchange forward contracts or commodity contracts to limit its exposure. The Company is not currently

vulnerable to a material extent to fluctuations in interest rates and commodity prices.

YEAR 2000 COMPLIANCE

The Company did not experience any material Year 2000 computer problems on its primary computer systems. The Company's computer systems functioned properly into the year 2000. As a result, the Company was able to service its customers, communicate with its suppliers, and submit billings to third party payers without disruption. The Company, however, continues to monitor its systems, suppliers, and customers for any unanticipated issues that have yet to surface.

ORTHOLOGIC SELECTED FINANCIAL DATA

The selected financial data for each of the five years in the period ended December 31, 1999 are derived from audited financial statements of the Company. The selected financial data should be read in conjunction with the Financial Statements and related Notes thereto and other financial information appearing elsewhere herein and the discussion in "Management's Discussion and Analysis of Financial Condition and Results of Operations." As discussed in Note 2 of the notes, the Company completed two acquisitions in March 1997 and one in August 1996.

<TABLE>
<CAPTION>

	Years Ending December 31,				
(in thousands)	1999	1998	1997	1996	1995
<S>	<C>	<C>	<C>	<C>	<C>
STATEMENTS OF OPERATIONS DATA:					
Total revenues	$ 83,232	$ 75,369	$ 77,049	$ 41,884	$ 14,678
Total cost of revenues	18,504	17,693	18,369	8,299	3,065
Operating expenses:					
Selling, general, and administrative	61,936	72,011	61,484	31,901	11,304
Research and development	2,860	2,920	2,320	2,169	2,132
Restructuring and other charges [Note 1]	(216)	(399)	13,844	--	--
Total operating expenses	64,580	74,532	77,648	34,070	13,436
Operating profit (loss)	148	(16,856)	(18,968)	(485)	(1,823)
Other income	148	354	1,466	3,023	471
Income Taxes	(58)	(100)	(212)	--	--
Net income (loss)	238	(16,602)	(17,714)	2,538	(1,352)
Accretion of non-cash preferred stock dividend	(824)	(1,236)	--	--	--
Net income (loss) applicable to common stockholders	$ (586)	$(17,838)	$(17,714)	$ 2,538	$ (1,352)
Net income (loss) per common share					
Basic [Note 1]	$ (0.02)	$ (0.71)	$ (0.71)	$ 0.11	$ (0.09)
Net income (loss) per common share					
Diluted [Note 1]	$ (0.02)	$ (0.71)	$ (0.71)	$ 0.11	$ (0.09)
Basic shares outstanding	26,078	25,291	25,116	23,275	15,549
Equivalent shares and stock options	--	--	869	--	
Diluted shares outstanding	26,078	25,291	25,116	24,114	15,549

</TABLE>

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1. Net income was affected in 1997 by a one-time charge for restructuring and other costs, applicable to the impairment of dealer intangibles acquired in the transition to a direct sales force and expenses related to severance, facility closing and related costs. The effect on earnings per share from the restructuring and other changes is a loss of .55 cents per share.

<TABLE>
<CAPTION>

	Years Ended December 31,				
(in thousands)	1999	1998	1997	1996	1995

<S>	<C>	<C>	<C>	<C>	<C>
BALANCE SHEET DATA:					
Working capital	$ 40,865	$ 38,817	$ 44,418	$ 74,985	$ 23,518
Total assets	92,203	93,980	103,103	113,026	27,490
Long-term debt, less current maturities	209	196	1,631	280	--
Stockholders' equity	73,054	68,225	84,737	101,927	24,437

</TABLE>

STOCKHOLDER INFORMATION

Market Information. The Company's Common Stock commenced trading on the NASDAQ National Market on January 28, 1993 under the symbol "OLGC." The bid price information [adjusted for a 2-for-1 stock split effected as a stock dividend in June 1996] included herein is derived from the NASDAQ Monthly Statistical Report, represents quotations by dealers, may not reflect applicable markups, markdowns or commissions and does not necessarily represent actual transactions.

	1999		1998	
	High	Low	High	Low
First Quarter	$4 3/16	$2 3/4	$7 9/16	$5 1/2
Second Quarter	3 7/8	2 5/16	7 1/2	4 3/4
Third Quarter	3 1/8	2 1/4	5	2 1/2
Fourth Quarter	3 1/16	2 1/4	4 3/8	2 15/16

As of January 31, 2000, there were 29,126,456 shares outstanding of the Common Stock of the Company held by approximately 275 stockholders of record.

DIVIDENDS. The Company has never paid a cash dividend on its Common Stock. The Board of Directors currently anticipates that all the Company's earnings, if any, will be retained for use in its business and does not intend to pay any cash dividends on its Common Stock in the foreseeable future.

ORTHOLOGIC CONSOLIDATED BALANCE SHEETS

<TABLE>
<CAPTION>

	December 31,	
	1999	1998
<S>	<C>	<C>
ASSETS		
Current assets:		
Cash and cash equivalents	$ 6,023,263	$ 1,713,966
Short-term investments [Note 7]	250,000	6,052,469
Accounts receivable, less allowance for doubtful accounts of $15,502,720 and $19,317,823 [Note 12]	30,428,564	27,030,755
Inventories, net [Note 8]	9,306,455	11,960,071
Prepaids and other current assets	986,753	799,350
Deferred income taxes [Note 10]	2,630,659	2,642,909
Total current assets	49,625,694	50,199,520
Rental fleet, equipment & furniture, net [Note 9 and 12]	13,061,771	12,867,391
Deposits and other assets	766,586	344,915
Goodwill, net of accumulated amortization of $4,645,793 and $2,918,116 [Note 2]	24,643,822	26,195,846
Other Intangibles, net [Notes 3,15, and 16]	4,105,574	4,372,238
Total assets	$ 92,203,447	$ 93,979,910
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current liabilities:		
Accounts payable	$ 2,568,805	$ 3,038,684
Loan payable	--	500,000
Accrued compensation	2,852,631	1,458,849
Deferred credits	138,813	1,542,393
Accrued royalties [Note 6]	37,040	166,457
Accrued restructuring expenses [Note 3]	150,086	762,151
Obligations under co-promotion agreement [Note 15]	--	1,000,000
Sales and property taxes payable	1,908,904	1,185,190
Accrued expenses	1,104,475	1,729,207

Total current liabilities	8,760,754	11,382,931
Deferred rent and capital leases	209,138	196,192
Total liabilities	8,969,892	11,579,123
Commitments and contingencies [Notes 6,12,13,14,15 and 16]		
Series B Convertible Preferred Stock, $1,000 par value; 10,180 and 15,000 shares issued and outstanding; liquidation preference, $10,180,000 and $15,000,000 [Note 11]	10,180,000	14,176,008
STOCKHOLDERS' EQUITY [NOTE 11]		
Common Stock, $.0005 par value; 50,000,000 shares authorized; and 27,637,593 and 25,302,190 shares issued and outstanding	13,818	12,649
Additional paid in capital	125,206,621	119,658,836
Deficit	(51,992,079)	(51,405,989)
Comprehensive income (loss)	(174,805)	(40,717)
Total stockholders' equity	73,053,555	68,224,779
Total liabilities and stockholders' equity	$ 92,203,447	$ 93,979,910

</TABLE>

See notes to consolidated financial statements

ORTHOLOGIC CONSOLIDATED STATEMENTS OF OPERATIONS

<TABLE>
<CAPTION>

	Years Ending December 31,		
	1999	1998	1997
<S>	<C>	<C>	<C>
REVENUES			
Net sales	$ 32,578,511	$ 29,491,932	$ 36,043,169
Net rentals	42,356,168	37,138,960	37,362,446
Fee revenue from co-promotion agreement [Note 15]	8,296,844	8,737,325	3,643,618
Total revenues	83,231,523	75,368,217	77,049,233
COST OF REVENUES			
Cost of goods sold	11,303,309	10,591,924	10,224,397
Cost of rentals	7,200,549	7,100,706	8,144,806
Total cost of revenues	18,503,858	17,692,630	18,369,203
Gross Profit	64,727,665	57,675,587	58,680,030
OPERATING EXPENSES			
Selling, general and administrative	61,936,094	72,010,982	61,484,418
Research and development	2,860,159	2,919,857	2,319,640
Restructuring and other charges [Note 3]	(216,211)	(398,943)	13,843,591
Total operating expenses	64,580,042	74,531,896	77,647,649
Operating Profit (Loss)	147,623	(16,856,309)	(18,967,619)
OTHER INCOME (EXPENSE)			
Grant/other revenue	1,306	103,861	147,263
Interest income	224,139	350,858	1,384,133
Interest expense	(77,281)	(101,100)	(65,884)
Total other income	148,164	353,619	1,465,512
Income (Loss) Before Income Taxes	295,787	(16,502,690)	(17,502,107)
Provision for income taxes [Note 8]	(57,886)	(99,804)	(211,560)
Net Income (Loss)	237,901	(16,602,494)	(17,713,667)
Accretion on non-cash preferred stock dividend	(823,991)	(1,235,988)	--
Net loss applicable to common stockholder	$ (586,090)	$(17,838,482)	$(17,713,667)
Net loss per common share-basic	$ (0.02)	$ (0.71)	$ (0.71)

Net loss per common share-diluted	$ (0.02)	$ (0.71)	$ (0.71)
Basic and diluted shares outstanding	26,078,058	25,290,784	25,116,164

OrthoLogic Consolidated Statements of Comprehensive Income (Loss)

	Years Ending December 31,		
	1999	1998	1997
Net loss applicable to common stockholders	$ (586,091)	$(17,838,482)	$(17,713,667)
Foreign translation adjustment	(134,088)	(18,136)	(22,581)
Comprehensive loss applicable to common stockholders	$ (720,179)	$(17,856,618)	$(17,736,248)

</TABLE>
See notes to consolidated financial statements

ORTHOLOGIC CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY

<TABLE>
<CAPTION>

	Shares	Amount	Paid in Capital	Comprehensive Income	Deficit	Total
<S>	<C>	<C>	<C>	<C>	<C>	<C>
Balance, December 31, 1996	25,022,346	$ 12,510	$118,832,040	--	$(16,917,616)	$ 101,926,934
Exercise of common stock options at prices ranging from $.16 to $4.78 per share	232,844	116	496,593	--	--	496,709
Stock option compensation	--	--	84,577	--	--	84,577
Other	--	--	--	$(22,581)	(34,511)	(57,092)
Net loss	--	--	--	--	(17,713,667)	(17,713,667)
Balance, December 31,1997	25,255,190	12,626	119,413,210	(22,581)	(34,665,794)	84,737,461
Exercise of common stock options at prices ranging from $.50 to $4.55 per share	47,000	23	158,754	--	--	158,777
Stock option compensation	--	--	25,622	--	--	25,622
Series B Preferred Convertible Stock	--	--	1,093,980	--	1,093,980	
Accretion of Non-cash Preferred Stock	--	--	(1,093,980)	--	(142,008)	(1,235,988)
Other	--	--	61,250	--	4,307	65,557
Foreign translation adjustment	--	--	--	(18,136)	--	(18,136)
Net Loss	--	--	--	--	(16,602,494)	(16,602,494)
Balance December 31, 1998	25,302,190	12,649	119,658,836	(40,717)	(51,405,989)	68,224,779
Accretion of non-cash preferred stock dividend	00	00	00	00	(823,991)	(823,991)
Exercise of common options at prices ranging from $2.03 to $2.88 per share	282,400	142	728,812	00	00	728,954
Conversion of Preferred Stock	2,053,003	1,027	4,818,973	00	00	4,820,000
Foreign translation adjustment	(134,088)	(134,088)				
Net Income	00	00	00	00	237,901	237,901
Balance December 31, 1999	27,637,593	$ 13,818	$125,206,621	$(174,805)	$(51,992,079)	$73,053,555

</TABLE>

See notes to consolidated financial statements

ORTHOLOGIC CONSOLIDATED STATEMENTS OF CASH FLOW

<TABLE>
<CAPTION>

	Years Ending December 31,		
	1999	1998	1997
<S>	<C>	<C>	<C>
OPERATING ACTIVITIES			
Net income (loss)	$ 237,901	$(16,602,494)	$(17,713,667)
Adjustments to reconcile net income (loss) to net cash used in operating activities:			
Depreciation and amortization	6,758,663	6,473,000	5,510,251
Restructuring and other charges	(216,211)	(399,000)	13,843,591
Other	--	--	(438,504)
Change in operating assets and liabilities, excluding acquisitions:			
Accounts receivable	(3,415,663)	5,682,834	(2,759,187)
Inventories	2,653,616	(1,411,898)	(1,494,096)
Prepaids and other current assets	(175,153)	280,065	(23,215)
Deposits and other assets	(421,671)	186,870	(438,447)
Accounts payable	(469,879)	242,628	(871,546)
Accrued and other current liabilities	(263,944)	(4,466,299)	(437,934)
Net cash provided (used) in operating activities	4,687,659	(10,014,294)	(4,822,754)
INVESTING ACTIVITIES			
Expenditures for rental fleet, equipment and furniture	(4,958,701)	(5,423,652)	(5,128,159)
Intangibles from dealer transactions	--	--	(704,966)
Officer note receivable, net	(157,800)	--	200,000
Acquisitions, net of cash acquired	--	--	(24,886,134)
Investments in Chrysalin	--	(750,000)	
(Purchase) sale of short-term investments	5,802,469	(1,484,943)	30,738,463
Net cash (used) provided in investing activities	685,968	(7,658,595)	219,204
FINANCING ACTIVITIES			
Payments under long-term debt and capital lease obligations	(159,197)	(157,984)	(233,756)
Payments on loan payable	(500,000)	(500,000)	(420,084)
Payments under co-promotion agreement	(1,000,000)	(2,000,000)	(1,000,000)
Net proceeds from stock options exercised and other	594,867	227,490	546,886
Net proceeds from issuance of convertible preferred stock and warrants	--	14,034,000	--
Net cash (used in) provided by financing activities	(1,064,330)	11,603,506	(1,106,954)
NET (DECREASE) INCREASE IN CASH AND CASH EQUIVALENTS	4,309,297	(6,069,383)	(5,710,504)
CASH AND CASH EQUIVALENTS, BEGINNING OF YEAR	1,713,966	7,783,349	13,493,853
CASH AND CASH EQUIVALENTS, END OF YEAR	$ 6,023,263	$ 1,713,966	$ 7,783,349
Supplemental schedule of non-cash investing and financing activities:			
Stock option compensation	--	$ 25,622	$ 84,577
SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION			
Acquisition of intangible asset through obligation for product distribution rights [Note 15]	--	--	$ 4,000,000
Conversion of series B preferred stock for common stock	$ 4,820,000	--	--
Accretion of non-cash preferred stock dividend	$ 823,992	$ 1,235,988	--
Purchase of property and equiupment with capital leases	--	$ 493,289	--
Purchase price adjustment related to preacquisition contingencies	$ 175,653	$ 1,816,362	--
Cash paid during the year for interest	$ 50,510	$ 101,100	$ 65,844
Cash paid during the year for income taxes	$ 3,295	$ 350,000	$ 400,000

</TABLE>

See notes to consolidated financial statements.

OrthoLogic Notes to Consolidated Financial Statements

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Organization. OrthoLogic Corp. was incorporated on July 30, 1987 (date of inception) and commenced operations in September 1987. On August 30, 1996 OrthoLogic Corp. acquired all of the outstanding capital stock of Sutter Corporation ("Sutter") which became a wholly-owned subsidiary of OrthoLogic (collectively the "Company" or "OrthoLogic"). On March 9, 1997 and March 12, 1997, the Company acquired certain assets and assumed certain liabilities of Toronto Medical Corp. ("Toronto") and Danninger Medical Technology, Inc. ("DMTI "). Concurrent with the acquisition of Toronto the Company formed a wholly owned Canadian subsidiary, now known as OrthoLogic Canada Ltd.

Description of the business. OrthoLogic develops manufactures and markets proprietary technologically advanced orthopedic products and packaged services for the orthopedic health care market including bone growth stimulation, orthopedic rehabilitation products and injectable products primarily in the United States. OrthoLogic's products are designed to enhance the healing of diseased, damaged, degenerated or recently repaired musculo skeletal tissue. The Company's products focus on improving the clinical outcomes and cost-effectiveness of orthopedic procedures that are characterized by compromised healing, high-cost, potential for complication and long recuperation time. On January 14, 1999 the Company exercised its option to license the United States development, marketing, and distribution rights for the fresh fracture indications for Chrysalin, a new tissue repair synthetic peptide. On January 12, 2000, the Company began enrolling patients in the combined Phase I/II clinical trials for Chrysalin.

During the year ended December 31, 1999 and 1998, the Company reported net income of $237,901 and a loss of $16.6 million, respectively. In addition, the Company provided cash from operating activities of $4.7 million and used cash of $10.0 million for the years ending December 31, 1999 and 1998, respectively. The Company anticipates that its cash and short-term investments on hand, cash from operations and the funds available from the revolving line of credit (Note 12) will be sufficient to meet the Company's presently projected cash and working capital requirements for the next 12 months. There can be no assurance, however, that this will prove to be the case. The timing and amounts of cash used will depend on many factors, including the Company's ability to continue to increase revenues, reduce and control expenditures, maintain profitability and collect amounts due from third party payers. Additional funds may be required if the Company is not successful in any of these areas. The Company's ability to continue funding its planned operations beyond the next 12 months is dependent on its ability to generate sufficient cash flow to meet its obligations on a timely basis, or to obtain additional funds through equity and debt financing, or from other sources of financing, as may be required.

PRINCIPLES OF CONSOLIDATION. The consolidated financial statements include the accounts of OrthoLogic Corp. since its inception, Sutter since its acquisition on August 30, 1996, Toronto, and DMTI, since their acquisition in March 1997. All material intercompany accounts and transactions have been eliminated. The following briefly describes the significant accounting policies used in the preparation of the financial statement of the Company:

A. INVENTORIES are stated at the lower of cost (first in, first out method) or market.

B. RENTAL FLEET, EQUIPMENT AND FURNITURE are stated at cost or, in the case of leased assets under capital leases, at the present value of future lease payments at inception of the lease. Depreciation is calculated on a straight-line basis over the estimated useful lives of the various assets, which range from three to seven years. Leasehold improvements and leased assets under capital leases are amortized over the life of the asset or the period of the respective lease using the straight-line method, whichever is the shortest.

C. REVENUE is recognized for sales of the Orthologic 1000 and SpinaLogic products at the time the product is placed on the patient. If the sale of either product is to a commercial buyer, revenue is recognized at the time of shipment. The Orthoframe(R) and the OrthoFrame/Mayo are typically held on consignment at hospitals and revenue is recognized at the point a purchase order is received from the hospital. Rental revenue for CPM products is recorded daily during the period of usage. Revenue on rehabilitative ancillary products is generally recognized at the time of shipment. Fee revenue for Hylagan(R) is based upon the number of units sold at the wholesale acquisition cost less amounts for distribution costs, discounts, rebates, returns, product transfer price, overhead factor and a royalty factor. Grant revenue is recorded as earned in accordance with the terms of the grant contracts.

D. RESEARCH AND DEVELOPMENT represent both costs incurred internally for research and development activities, as well as costs incurred by the Company to

fund the activities of the various research groups which the Company has contracted. All research and development costs are expensed when incurred.

E. CASH AND CASH EQUIVALENTS consist of cash on hand and cash deposited with financial institutions, including money market accounts, and commercial paper purchased with an original maturity of three months or less.

F. INCOME (LOSS) PER COMMON SHARES is computed on the weighted average number of common or common and common equivalent shares outstanding during each year. Basic EPS is computed as net income (loss) applicable to common stockholders divided by the weighted average number of common shares outstanding for the period. Diluted EPS reflects the potential dilution that could occur from common shares issuable through stock options, warrants, and other convertible securities when the effect would be dilutive.

G. CERTAIN RECLASSIFICATIONS have been made to the 1998 and 1997 financial statements to conform to the 1999 presentation.

H. INTANGIBLE ASSETS. Goodwill from the acquisition of Sutter, Toronto and DMTI is capitalized and amortized on a straight-line basis over the estimated useful life of the related assets (15-20 years). The intangible relating to the product distribution rights for Hyalgan(R) acquired in the co-promotion agreement is being amortized over 15 years. The investment in Chrysalis continues to be carried at cost.

I. LONG-LIVED ASSETS. In accordance with Statement of Financial Accounting Standards ("SFAS") No. 121, the Company reviews the carrying values of its long lived assets and identifiable intangibles for possible impairment whenever events or changes in circumstances indicate that the carrying amount of assets to be held and used may not be recoverable.

J. STOCK BASED COMPENSATION. The Company accounts for its stock based compensation plan based on accounting Principles Board ("APB") Opinion No. 25. In October 1995, the Financial Accounting Standards Board issued SFAS No. 123, Accounting for Stock-Based Compensation. The Company has determined that it will not change to the fair value method and will continue to use APB Opinion No. 25 for measurement and recognition of employee stock based transactions (Note 11).

K. USE OF ESTIMATES. The preparation of the financial statements in conformity with generally accepted accounting principles necessarily requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenue and expenses during the reporting period. Significant estimates include the allowance for doubtful accounts ($15,502,720 and $19,317,823 at December 31, 1999 and 1998, respectively), which is based primarily on trends in historical collection statistics, consideration of events, payer mix and other considerations. In addition, the Company derives a significant amount of its revenues in the United States from third-party health insurance plans, including Medicare. Amounts paid under these plans are generally based on fixed or allowable reimbursement rates. Revenues are recorded at the expected or preauthorized reimbursement rates when billed. Some billings are subject to review by such third party payers and may be subject to adjustments. In the opinion of management, adequate allowances have been provided for doubtful accounts and contractual adjustments. Any differences between estimated reimbursement and final determinations are reflected in the year finalized.

L. NEW ACCOUNTING PRONOUNCEMENT. In June 1998, the FASB issued SFAS No. 133, Accounting for Derivative Instruments and Hedging Activities. SFAS No. 133 requires that an enterprise recognizes all derivatives as either assets or liabilities in the statement of financial position and measure those instruments at fair value. The statement is effective, as ammended, in the first quarter of 2001. The Company has not completed evaluating the impact of implementing the provisions of SFAS No. 133.

2. ACQUISITIONS

On March 3, 1997 and March 12, 1997, the Company acquired certain assets and assumed certain liabilities of Toronto and DMTI . After paying certain of the assumed liabilities, the net cash outlay was approximately $7.5 million for Toronto and $10.7 million for DMTI . Both acquisitions were accounted for as purchases under the purchase method of accounting, which resulted in goodwill of $5.5 million for Toronto and $10.6 million for DMTI . The goodwill is being amortized over 20 years. The Company has substantially completed its integration of operations related to these acquisitions. The following unaudited pro forma summary combines the consolidated results of operations of OrthoLogic, Toronto

and DMTI as if the acquisitions had occurred January 1, 1997 after giving effect to certain adjustments including amortization of goodwill, interest income and income taxes. This pro forma summary is not necessarily indicative of the results of operations that would have occurred if OrthoLogic, Sutter, Toronto, and DMTI had been combined for all of 1997.

	Year Ending December 31,
(in thousands, except per share data)	1997
Net revenues	$ 80,332
Income (loss) from continuing Operations	(17,725)
Net income (loss) per common share	$ (.71)

3. RESTRUCTURING AND OTHER CHARGES

During the third quarter of 1997, the Company restructured its sales, marketing and managed care groups. As a result of their restructuring and a second consecutive quarter of declining sales of the OrthoLogic 1000 bone growth stimulator, the Company determined that certain dealer intangibles acquired in

the transition to a direct sales force in 1996 had been impaired. The Company recorded a restructuring charge of $13.8 million in the third quarter, composed of a $10.0 million write-off its dealer intangibles, $2.3 million in severance, $1.2 million in facility closing and $300,000 of related costs. There was a reversal of 1997 restructuring expenses of $216,000 during 1999 and $399,000 during 1998. The remaining $150,000 balance of the restructuring reserve on December 31, 1999 primarily relates to severance.

4. SELLING, GENERAL AND ADMINISTRATIVE EXPENSES

During the first quarter of 1998, the Company recorded a charge of approximately $9.3 million for additional bad debt expense. The charge was a result of a management decision during the first quarter of 1998 to focus proportionately more resources on collection of current sales and on re-engineering the overall process of billing and collections. Management determined it was no longer considered to be cost effective to expend significant resources on the collection of the older receivables as has been done in the past.

5. LEGAL SETTLEMENT

The Company settled a false claims matter with the U.S. Department of Justice in a case that was filed in December 1996 under qui tam provisions of the Federal False Claims Act. The allegations included the submission of claims for reimbursement for a small number of custom medical devices to various federal care programs including Medicare, TRICARE (formerly known as CHAMPUS) and various state Medicaid programs.

OrthoLogic denies any wrongdoing or liability with respect to the allegations in this matter. Nevertheless, in effort to avoid the expense, burden and uncertainty of litigation in this case as well as the potential distraction this case could have on the Company's management, the Company agreed to settle this matter. Under the terms of the definitive settlement agreement, OrthoLogic paid to the U.S. Department of Justice, on behalf of several federal health care programs including Medicare, TRICARE, and various state Medicaid programs, the amount of $1,000,000. In return, the U.S. Department of Justice released the Company's officers, employees, and directors from any causes of actions for civil damages or civil penalties for the various allegations being settled in this matter. The original complaint was dismissed with prejudice.

6. RESEARCH, PRODUCT DEVELOPMENT AND LICENSE AGREEMENTS

The Company has committed to pay royalties on the sale of products or components of products developed under certain product developing and licensing agreements. The royalty percentages vary but generally range from 7% to 0.5% of the sales amount for licensed products. The royalty percentage under the different agreements decrease when either a certain sales dollar amount is reached or royalty amount is paid. Royalty expense under these agreements totaled $126,179, $258,456 and $360,110 in 1999, 1998 and 1997 respectively.

7. INVESTMENTS

The Company has implemented SFAS No. 115 "Accounting for Certain Investments in Debt and Equity Securities." At December 31, 1999, marketable securities were composed of municipal bonds and were managed as part of the Company's cash

management program and were classified as held-to-maturity securities. All such securities were purchased with original maturities less than one year. Such classification requires these securities to be reported at amortized cost.

A summary of the fair market value and unrealized gains and losses on these securities is as follows:

	Years Ending December 31,	
	1999	1998
Amortized cost	$ 250,000	$ 6,052,469
Gross unrealized gains	-	665
Gross unrealized losses	-	(17,205)
Fair value	$ 250,000	$ 6,035,929

8. INVENTORIES

Inventories consisted of the following:

	Years Ending December 31,	
	1999	1998
Raw materials	$ 7,083,159	$ 8,484,773
Work-in-process	92,584	122,371
Finished goods	3,110,514	4,101,325
	10,286,257	12,708,469
Less allowance for obsolescene	(979,802)	(748,398)
Total	$ 9,306,455	$ 11,960,071

9. RENTAL FLEET, EQUIPMENT AND FURNITURE

Rental fleet, equipment and furniture consisted of the following:

	Years Ending December 31,	
	1999	1998
Rental fleet	$ 17,827,501	$ 14,373,674
Machinery and equipment	2,243,657	2,383,562
Computer equipment	4,760,501	3,708,812
Furniture and fixtures	1,495,054	767,661
Leasehold and improvements	744,896	727,996
	27,071,609	21,961,705
Less accumulated depreciation and amortization	(14,009,838)	(9,094,314)
Total	$ 13,061,771	$ 12,867,391

10. INCOME TAXES

At December 31,1999, the Company has accumulated approximately $33.6 million in net operating loss carryforwards expiring from 2002 through 2017 for federal

income tax purposes. Stock issuances, as discussed in Note 11, may cause a change in ownership under the provisions of Internal Revenue Code Section 382; accordingly, the utilization of the Company's net operating loss carryforwards may be subject to annual limitations.

Management has evaluated the available evidence about future taxable income and other possible sources of realization of deferred tax assets. The valuation allowance reduces deferred tax assets to an amount that management believes will more likely than not be realized. The components of deferred income taxes at December 31 are as follows:

	1999	1998

Allowance for bad debts	$ 6,201,000	$ 7,779,000
Other accruals and reserves	886,659	1,263,909
Valuation allowance	(4,457,000)	(6,400,000)
Total current	2,630,659	2,642,909
Net operating loss carryforwards	14,064,000	12,207,000
Difference in basis of fixed assets	(1,517,000)	(1,100,000)
Nondeductible accruals and reserves	159,000	159,000
Amortization of intangibles and other	430,000	90,000
Difference in basis of dealer intangible	3,581,000	3,889,000
Valuation allowance	(16,717,000)	(15,245,000)
Total noncurrent	--	--
Total deferred income taxes	$ 2,630,659	$ 2,642,909

The provision for income taxes are as follows:

	1999	1998	1997
Current	$ 45,636	$ 146,327	$ 407,000
Deferred	$ 12,250	$ (46,523)	$(195,440)
Income Tax Provision	$ 57,886	$ 99,804	$ 211,560

A reconciliation of the difference between the provision (benefit) for income taxes and income taxes at the statutory U.S. federal income tax rate is as follows for the years ending December 31:

	1999	1998	1997
Income taxes at statutory rate	$ 80,000	$(5,611,000)	$(5,950,000)
State income taxes	28,000	(990,000)	(1,024,000)
Change in valuation allowance	(471,000)	6,403,000	6,558,000
Other	420,886	297,804	627,560
Net Provision	$ 57,886	$ 99,804	$ 211,560

11. STOCKHOLDERS' EQUITY AND SERIES B

CONVERTIBLE PREFERRED STOCK

In October 1987, the stockholders adopted a Stock Option Plan (the "1987 Option Plan") which was amended in September 1996, and approved by shareholders in May 1997, to increase the number of common shares reserved for issuance under the 1987 Option Plan to 4,160,000 shares. This plan expired during October 1997. In May 1997, the Stockholders adopted a new Stock Option Plan (the "1997 Option Plan") which replaced the 1987 Option Plan. The 1997 Option Plan reserved for issuance 1,040,000 shares of common stock and was amended in 1998 to increase the number of shares of common stock by 275,000 shares. Two types of options may be granted under the 1997 Option Plan: options intended to qualify as incentive stock options under Section 422 of the Internal Revenue Code ("Code") and other options not specifically authorized or qualified for favorable income tax treatment by the Code. All eligible employees may receive more than one type of option. Any director or consultant who is not an employee of the Company shall be eligible to receive only nonqualified stock options under the 1997 Option Plan. Included in the stock granted in 1999 are 300,000 options granted to an employee exclusive of the 1987 and 1997 stock option plan.

In October 1989, the Board of Directors (the "Board") approved that in the event of a takeover or merger of the company in which 100% of the equity of the company is purchased, 75% of all unvested employee options will vest, with the balance vesting equally over the ensuing 12 months, or according to the individual's vesting schedule, whichever is earlier. If an employee or holder of stock options is terminated as a result of or subsequent to the acquisition,

100% of that individual's stock option will vest immediately upon employment termination. These provisions are also included in the 1997 Option Plan.

Options are granted at prices, which are equal to the current fair value of the Company's common stock at the date of grant. The vesting period is generally related to length of employment and all vested options lapse upon termination of employment if not exercised within a 90-day period (or one year after death or disability or the date of termination if terminated for cause).

A summary of the status of the Option Plans as of December 31, 1999, 1998 and 1997, and changes during the years then ended is:

<TABLE>
<CAPTION>

	1999		1998		1997	
	Shares	Weighted-Average Exercise price	Shares	Weighted-Average Exercise price	Shares	Weighted-Average Exercise price
<S>	<C>	<C>	<C>	<C>	<C>	<C>
Fixed options outstanding at beginning of year	3,384,825	$5.66	2,535,450	$6.07	2,509,644	$7.31
Granted	688,850	3.12	1,024,000	4.79	1,132,150	5.54
Exercised	(282,400)	2.58	(47,000)	3.92	(232,844)	2.37
Forfeited	(302,362)	7.83	(127,625)	7.48	(873,500)	9.59
Outstanding at end of year	3,488,913	5.24	3,384,825	5.66	2,535,450	6.07
Options exercisble at year-end	2,357,717		1,744,357		1,072,975	

</TABLE>

The following table summarizes information about fixed stock options outstanding at December 31, 1999:

<TABLE>
<CAPTION>

	Outstanding			Exercisable	
Range of Exercise Prices	Number Outstanding as of 12/31/99	Weighted-Average Remaining Contractual Life	Weighted-Average Exercised Price	Number Exercisable as of 12/31/99	Weighted-Average Exercised Price
<S> <C>	<C>	<C>	<C>	<C>	<C>
$1.8100 - $ 2.5000	397,863	4.18	$2.1569	300,054	$2.0451
$2.5310 - $ 3.0000	172,100	9.47	$2.6195	128,434	$2.5318
$3.2500 - $ 3.2500	405,000	8.77	$3.2500	243,333	$3.2500
$3.3440 - $ 5.0000	469,250	8.29	$4.4152	238,250	$4.7848
$5.0630 - $ 5.4380	419,750	7.91	$5.3677	313,875	$5.3543
$5.5000 - $ 5.5310	351,400	8.33	$5.5018	168,002	$5.5037
$5.5630 - $ 5.5630	100,000	8.01	$5.5630	50,000	$5.5630
$5.6250 - $ 5.6250	381,000	7.76	$5.6250	208,083	$5.6250
$5.8125 - $ 6.5625	114,850	7.49	$6.2769	66,236	$6.2780
$6.7800 - $17.3800	677,700	4.69	$8.8305	641,450	$8.8097
$1.8100 - $17.3800	3,488,913	7.10	$5.2418	2,357,717	$5.5097

</TABLE>

The Company applies APB Opinion No. 25 and related interpretations in accounting for its Option Plans. Accordingly, no compensation cost has been recognized for its Option Plans. Had compensation cost been computed based on the fair value of awards on the date of grant, utilization the Black-Scholes option-pricing model, consistent with the method stipulated by SFAS No. 123, the Company's net earnings and earnings per share for the years ended December 31, 1999, 1998 and 1997 would have been reduced to the pro forma amounts indicated below, followed by the model assumptions used:

<TABLE>
<CAPTION>

	1999	1998	1997

<S>	<C>	<C>	<C>
Estimated weighted-average fair value of options granted during the year	$ 1.61	$ 2.26	$ 3.02
Net income (loss) attributable to common stockholders:			
As reported (in thousands)	$ (586)	$(17,838)	$(17,714)
Pro forma (in thousands)	$(2,525)	$(20,351)	$(20,371)
Basic and Diluted Net income (loss) per-share:			
As reported	$ (0.02)	$ (0.71)	$ (0.71)
Pro forma	$ (0.10)	$ (0.80)	$ (0.81)
Black- scholes model assumptions:			
Risk free interest rate	6.00%	6.00%	6.00%
Expected volatility	0.6	0.4	0.6
Expected term	5 Years	5 Years	5 Years
Dividend yield	0%	0%	0%

</TABLE>

In July 1998, the Company completed a private equity placement with two investors, an affiliate of Credit Suisse First Boston Corp. and Capital Ventures International. Under the terms of the Purchase Agreement, OrthoLogic sold 15,000 shares of Series B convertible Preferred Stock for $15 million (before costs). The Series B Convertible Preferred Stock is convertible into shares of Common Stock and will automatically convert, to the extent not previously converted, into Common Stock four years following the date of issuance. Each share of Series B convertible Preferred Stock is convertible into Common Stock at a per share price equal to the lesser of the average of the 10 lowest closing bids during the 30 days prior to conversion or $3.0353. In the event of certain Mandatory Redemption Events, each holder of Series B Preferred Shares will have the right to require the Company to redeem those shares for cash at the Mandatory Redemption Price. Mandatory Redemption Events include, but are not limited to: the failure of the Company to timely deliver Common Shares as required under the terms of the Series B Preferred Shares, or Warrants; the Company's failure to satisfy registration requirements applicable to such securities; the failure of the Company's stockholders to approve the transactions contemplated by the Securities Purchase Agreement related to the issuance of the Series B Preferred Shares; the failure by the company to maintain the listing of its Common Stock on NASDAQ or another national securities exchange; and certain transactions involving the sale of assets or business combinations involving the Company. In the event of any liquidation, dissolution or winding up of the Company, holders of the Series B Shares are entitled to receive, prior and in preference to any distribution of any assets of the Company to the holders of Common Stock, the States Value for each Series B Preferred Shares outstanding at that time. The Purchase Agreement contains strict covenants that protect against hedging and short-selling of OrthoLogic Common Stock while the purchaser holds shares of the Series B Convertible Preferred Stock.

In connection with the private placement of the Series B Convertible Preferred Stock, OrthoLogic issued to the purchasers warrants to purchase 40 shares of Common Stock for each share of Series B Convertible Preferred Stock, exercisable at $5.50. These warrants expire in 2008. The warrants were valued at $1,093,980. Additional costs of the private placement were approximately $966,000. Both the value of the warrants and the cost of the equity offering were recognized over the 10 month conversion period as an "accretion of non-cash Preferred Stock Dividends" for the amount of $617,994 per quarter. The Company filed a registration statement covering the underlying Common Stock.

Proceeds from the private placement were used to fund new product opportunities, including SpinaLogic, Chrysalin and Hyalgan(R), as well as to complete the re-engineering of the Company's key business processes.

At the close of business on December 31, 1999, 4,820 shares of Series B Convertible Preferred Stock had been converted into 2,053,003 shares of Common Stock.

At the closing of the Company's IPO on January 28, 1993 all convertible Series D Preferred Stock, totaling 4,173,002 shares, was converted into an equal amount of common stock. At December 31, 1998, there were 2,000,000 shares of preferred stock authorized.

12. COMMITMENTS

The Company is obligated under non-cancelable operating lease agreements for its office, manufacturing and research facilities. Rent expense for the years ended December 31, 1999, 1998 and 1997 was $1,998,000, $1,716,000, and $594,000

respectively.

Future lease payments for fiscal years 2000,2001,2002, 2003, 2004 and beyond 2004 are $1,819,000, $1,135,000, $1,011,000, $1,130,000, $1,130,000 and $3,486,000 respectively.

Through December 31, 1999, the Company had secured a $7.5 million accounts receivable revolving line of credit and a $2.5 million revolving term loan from a bank. The maximum amount that may be borrowed under this agreement is $10 million. The Company may borrow up to 70% of the eligible accounts receivable under the accounts receivable revolving line of credit and 50% of the net book value of CPM rental fleet under the revolving term loan. The accounts receivable revolving line of credit matures December 3, 2000 and the revolving term loan on November 30, 2000. Interest is payable monthly on the accounts receivable revolving line of credit and amortized principal and interest are due monthly on the revolving term loan. The interest rate is prime plus .65% for the accounts receivable line of credit, and prime plus 1.05% for the revolving term loan. There are certain financial covenants and reporting requirements associated with the loans. In connection with these loans, the Company issued a warrant to purchase 10,000 shares of Common Stock at a price equal to the average fair market value for five days prior to the closing of the loans.

On February 28, 2000, the Company attained a new $10 million accounts receivable revolving line of credit with a different lending institution. The Company may borrow up to 75% of the eligible accounts receivable. The interest rate is at prime for the revolving note. Interest accruing on the note and a monthly administration fee is due in arrears on the first day of each month. The revolving note matures February 28, 2003. There are certain financial covenants

and reporting requirements associated with the loan. Included in the financial covenants are (1) tangible net worth of not less than $43 million, (2) a quick ratio of not less than 2.0 to 1.0, (3) a debt to tangible net worth ration of not less than 0.50 to 1.0, and (4) capital expenditures will not exceed more than $7.0 million dollars during any fiscal year.

13. LITIGATION

During 1996, certain class action lawsuits were filed in the United States District Court for the District of Arizona against the Company and certain officers and directors alleging violations of Section 10(b) of the Securities Exchange Act of 1934 and SEC Rule 10b-6 promulgated thereunder.

Plaintiffs in these actions allege that correspondence received by the Company from the U.S. Food and Drug Administration (the "FDA") pertaining principally to the promotion of the Company's Orthologic 1000 Bone Growth Stimulator was material and undisclosed, leading to an artificially inflated stock price. Plaintiffs further allege practices referenced in the correspondence operated as a fraud against plaintiffs. Plaintiffs further allege that once the FDA letter became known, a material decline in the stock price of the Company occurred, causing damage to the plaintiffs.

The actions were consolidated for all purposes in the United States District Court for the District of Arizona and lead plaintiffs and counsel were appointed. On March 31, 1999, the judge in the consolidated case before the United States District Court granted the Company's Motion to Dismiss and entered an order dismissing all claims in the suit against the Company and two individual officers/directors. The judge allowed certain narrow claims based on insider trading theories to proceed against certain individual defendants. On December 21, 1999, the District Court granted plaintiffs' motion for class certification to include purchasers of common stock between June 4 through June 18, 1996, inclusive. Discovery is proceeding in the case.

In addition, the Company has been served with a substantially similar action filed in Arizona state court alleging state law causes of action grounded in the same set of facts. The Company filed a Motion to Dismiss the Complaint in Arizona State Court in May 1999. The Court denied the motion in July 1999 and granted the plaintiffs' motion for the class certification on November 24, 1999. The Company has appealed the state court's class certification and the appeal is now pending in the Arizona Supreme Court.

In addition, a shareholder derivative complaint, alleging, among other things, breach of fiduciary duty in connection with the conduct alleged in the federal and state court class actions have also been filed in Arizona state court. The Company filed a Motion to Dismiss the Complaint which was granted on December 13, 1999.

Management believes that the allegations in the remaining federal and state cases are without merit and will vigorously defend them.

As of December, 31, 1999, in addition to other matters disclosed above, the Company is involved in other various legal proceedings that arose in the ordinary course of business.

The costs associated with defending the above allegations and potential outcome cannot be determined at this time and accordingly, no estimate for such costs have been included in the accompanying Financial Statements. In management's opinion, the ultimate resolution of the above proceedings will not have a material effect on the financial position of the Company

14. 401(k) PLAN

The Company adopted a 401(k) plan (the "Plan") for its employees on July 1, 1993. The Company may make matching contributions to the Plan on behalf of all Plan participants, the amount of which is determined by the Board of Directors. The Company did not make any matching contributions to the Plan in 1998 and 1997. The Company matched $97,980 in 1999, which represented a 10% match of 1999 employee contributions to the plan.

15. CO-PROMOTION AGREEMENT

The Company entered into an exclusive co-promotion agreement (the "agreement") with Sanofi Pharmaceuticals Inc. ("Sanofi") at a cost of $4 million on June 23, 1997 for purpose of marketing Hyalgan(R), a hyaluronic acid sodium salt, to orthopedic surgeons in the United States for the treatment of pain in patients with osteoarthtitis of the knee. The initial term of the agreement ends on December 31, 2002. Upon the expiration of the initial term, Sanofi may terminate the agreement, extend the agreement for an additional one-year period, or enter into a revised agreement with the Company. Upon termination of the agreement, Sanofi must pay the Company an amount equal to 50% of the gross compensation paid to the Company for the immediately preceding year, provided the Company met all contractual obligations pursuant to the agreement.

The Company's sales force began to promote Hyalgan(R) in the third quarter of 1997. Fee revenue of $8.3, $8.7 and $3.6 million was recognized during 1999, 1998 and 1997, respectively.

16. LICENSING AGREEMENT

The Company announced in January 1998 that it had acquired a minority equity interest in a biotech firm, Chrysalis Bio Technology, Inc. for $750,000. As part of the transaction, the Company was awarded a nine-month world-wide exclusive option to license the orthopedic applications of Chrysalin, a patented 23-amino acid pep-tide that has shown promise in accelerating the healing process and has completed an extensive pre-clinical safety and efficacy profile of the product. In pre-clinical animal studies, Chrysalin was also shown to double the rate of fracture healing with a single injection into the fresh fracture gap. The Company's agreement with Chrysalis contains provisions for the Company to continue and expand its option to license Chrysalin contingent upon regulatory approvals, successful preclinical trials, and certain trials and certain milestone payments to Chrysalis by the Company. As part of the equity investment, OrthoLogic acquired options to license Chrysalin for orthopedic applications. An additional fee of $750,000 for the initial license was expensed in the third quarter of 1998 and the Agreement was extended to January 1999. In January 1999, the Company exercised its option to license the U. S. development, marketing and distribution rights for Chrysalin, for fresh fracture indications. As part of the license agreement, and in conjunction to FDA clearance to begin human clinical trials, OrthoLogic made a $500,000 milestone payment to Chrysalis Biotechnology in the fourth quarter of 1999. In January 2000, the Company began enrolling patients in the combined Phase I/II clinical trial for Chrysalin. The Company has elected not to exercise its option to license worldwide (excluding US) development, marketing and distribution rights for Chrysalin for fracture and orthopedic applications that expired on June 30, 1999.

The Company projects that Chrysalis could receive all the necessary FDA approvals and be introduced in the market during 2004 There can be no assurance, however, that the clinical trials will result in favorable data or that FDA approvals, if sought, will be obtained. Significant additional costs will be necessary to complete development of this product.

17. RELATED PARTIES

In the second quarter of 1999, the Company extended the maturity date on a loan

of $157,800 to an officer of the Company to February 15, 2000. On January 27, 2000, the loan was extended to a maturity date of February 29, 2000. An additional loan of $81,200 was entered into with the same officer on January 27, 2000, with a maturity date of February 29, 2000. The principal and interest of both loans were paid in full subsequent to year end.

INDEPENDENT AUDITORS' CONSENT

We consent to the incorporation by reference in Registration Statements No. 33-79010, No. 333-1268, No. 333-09785, No. 333-35507 and No. 333-35505 of OrthoLogic Corp. on Form S-8 and Registration Statements No. 33-82050, No. 333-1558 and No. 333-62321 of OrthoLogic Corp. on Form S-3 of our reports dated January 26, 2000, except for the last paragraph of Note 12, as to which the date is February 28, 2000, appearing in and incorporated by reference in the Annual Report on Form 10-K of OrthoLogic Corp. for the year ended December 31, 1999.

/s/ DELOITTE & TOUCHE LLP
Phoenix, Arizona
March 28, 2000

INDEPENDENT AUDITORS' REPORT

To the Board of Directors and Stockholders of
OrthoLogic Corporation
Tempe, Arizona

We have audited the consolidated financial statements of OrthoLogic Corporation as of December 31, 1999 and 1998, and for each of the three years in the period ended December 31, 1999, and have issued our report thereon dated January 26, 2000, except for the last paragraph of Note 12 as to which the date is February 28, 2000; such consolidated financial statements and report are included in your 1999 Annual Report to Stockholders and are incorporated herein by reference. Our audits also included the financial statement schedule of OrthoLogic Corporation, listed in Item 14. This financial statement schedule is the responsibility of the Corporation's management. Our responsibility is to express an opinion based on our audits. In our opinion, such 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.

DELOITTE & TOUCHE LLP

Phoenix, Arizona
January 26, 2000

<TABLE> <S> <C>

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THIS SCHEDULE CONTAINS SUMMARY FINANCIAL INFORMATION EXTRACTED FROM THE FINANCIAL STATEMENTS IN ORTHOLOGIC CORP'S REPORT ON FORM 10-K FOR THE YEAR ENDED DECEMBER 31, 1999 AND IS QUALIFIED IN ITS ENTIRETY BY REFERENCE TO SUCH FINANCIAL STATEMENTS.
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