Abatix Corp.

2009 Annual Report

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ABATIX Est. 1983

EXPERIENCE THE DIFFERENCE.

To Our Fellow Stockholders:

With respect to 2009, we are especially grateful for the loyalty of our customers and the reliability of our suppliers. In addition, we are thankful for the confidence in our Company from our stockholders and the support we receive from the communities in which we operate.

Although we remained profitable in 2009 when compared to 2008, both sales and profitability were negatively impacted by the following items.

- There were no significant weather related events in 2009.
- The recession in the U.S. economy.

During 2008, there were floods in the Midwest as well as a hurricane that made landfall in South Texas and another hurricane that made landfall in Galveston, Texas. These events provided a major source of revenue for the Company, as we assisted in the clean up and restoration process. During 2009, there were no major events to provide an equal level of revenue.

The current recession in the U.S. caused many manufacturers to reduce their production levels and layoff staff. The economic slowdown also caused delays or cancellation of many commercial construction projects.

As a result of the lower revenue levels, we carefully evaluated our company expenses early in 2009. As a result of that evaluation, we made the difficult decision to reduce our level of staff, however; we also made great strides in reducing other expenses so that our current expense levels are better aligned with our current revenue levels. We do not anticipate any improvement in the commercial construction market during 2010.

Our conservative approach throughout the years has kept our debt levels manageable. This management philosophy, combined with our profitability in 2008, afforded us the opportunity to reduce our debt significantly in 2009, in spite of the economic downturn. The reduction of debt has provided us with the financial flexibility and the opportunity to expand our operations. In September 2009, we added a new facility in San Diego, California. In December 2009, we acquired a small business in Jacksonville, Florida. Both of these efforts provide us with the opportunity to better serve our customers.

Because revenues have stabilized, our expenses have been reduced and our debt level remains low, the Board approved the repurchase of up to $500,000 of stock during 2010. These purchases can be made in open market or privately negotiated transactions.

Although our overall outlook for 2010 remains neutral, we are having some success attacking new markets and will continue to actively pursue new customers in both historical and new markets.

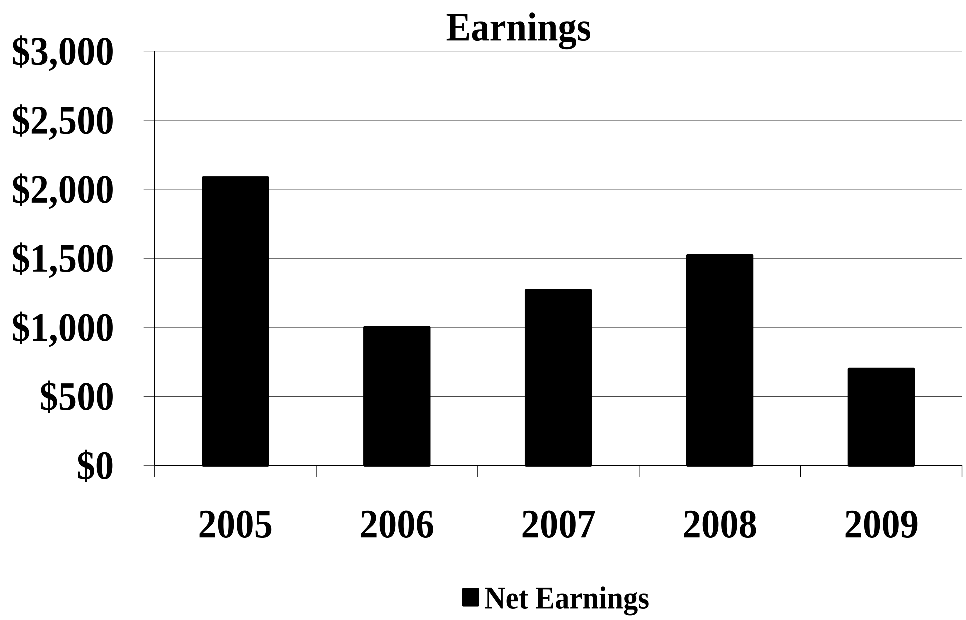
We believe 2010 will provide some opportunities as well as some challenges. Rest assured, that we are prepared to face these challenges and are confident that with the help of our long term investors, customers, suppliers and employees, we will be a stronger company going forward.

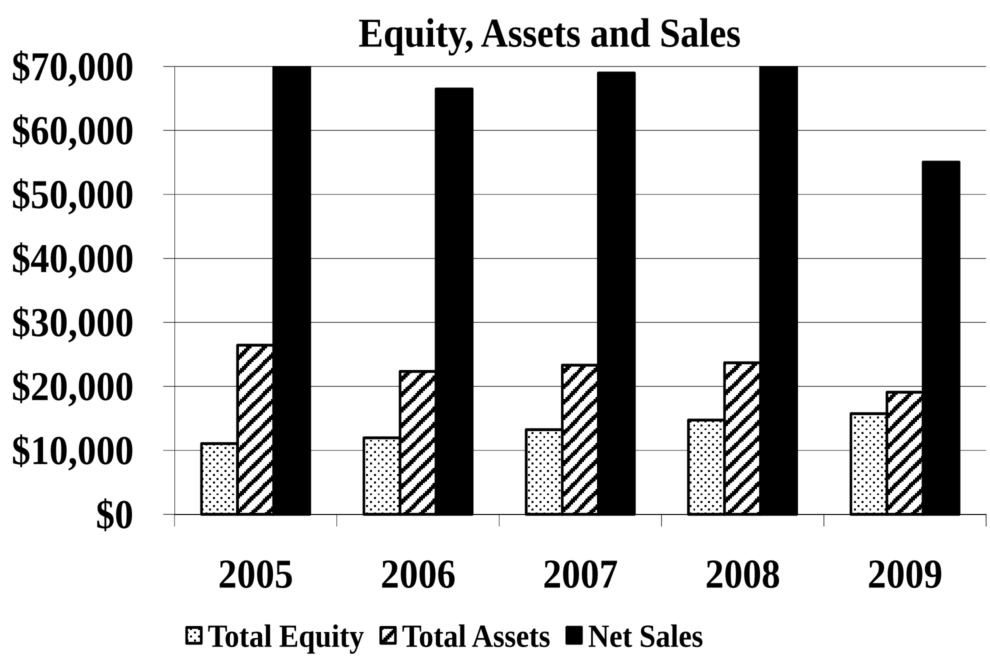
Thank you for your continued support.

Terry W. Shaver	Gary L. Cox
President, CEO	Senior Executive VP
and Stockholder	and Stockholder

Abatix Corp.
Financial Information

(Dollars in thousands)





ABATIX CORP. AND SUBSIDIARY

Index to Consolidated Financial Statements

KPMG LLP
Suite 3100
717 North Harwood Street
Dallas, TX 75201-6585

Independent Auditors' Report

The Board of Directors
Abatix Corp.:

We have audited the accompanying consolidated balance sheets of Abatix Corp. and subsidiary (the Company) as of December 31, 2009 and 2008, and the related consolidated statements of operations, stockholders' equity, and cash flows for each of the years in the three-year period ended December 31, 2009. These consolidated financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

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

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Abatix Corp. and subsidiary as of December 31, 2009 and 2008, and the results of their operations and their cash flows for the years in the three-year period ended December 31, 2009, in conformity with U.S. generally accepted accounting principles.

KPMG LLP

Dallas, Texas
April 6, 2010

ABATIX CORP. AND SUBSIDIARY

Consolidated Balance Sheets
December 31, 2009 and 2008

Assets	2009	2008
Current assets:		
Cash	$ 210,140	$ 154,372
Trade accounts receivable, net of allowance for doubtful accounts of $503,859 in 2009 and $540,389 in 2008	6,444,270	9,269,095
Inventories, net	9,769,591	10,668,181
Prepaid expenses and other assets	838,059	1,272,615
Deferred income taxes (note 6)	720,149	682,929
Income taxes receivable	-	388,928
Total current assets	17,982,209	22,436,120
Property and equipment, net (note 4)	767,120	982,153
Deferred income taxes (note 6)	149,536	169,191
Intangible assets, net of accumulated amortization of $2,764 in 2009 and $75,000 in 2008 (note 3)	63,567	-
Other assets	126,497	105,977
	$ 19,088,929	$ 23,693,441

Liabilities and Stockholders' Equity	2009	2008
Current liabilities:		
Notes payable (note 5)	$ -	$ 4,301,236
Accounts payable	2,160,518	2,807,607
Accrued compensation	233,765	883,615
Other accrued expenses	947,052	950,139
Total current liabilities	3,341,335	8,942,597
Long term debt	-	-
Total liabilities	3,341,335	8,942,597
Stockholders' equity:		
Preferred stock - $1 par value, 500,000 shares authorized; none issued	-	-
Common stock - $.001 par value, 5,000,000 shares authorized; 2,437,314 shares issued in 2009 and 2008	2,437	2,437
Additional paid-in capital	2,622,665	2,574,560
Retained earnings	15,127,939	14,431,189
Treasury stock at cost, 626,166 common shares in 2009 and 726,166 common shares in 2008	(2,005,447)	(2,257,342)
Total stockholders' equity	15,747,594	14,750,844
	$ 19,088,929	$ 23,693,441

See accompanying notes to consolidated financial statements.

ABATIX CORP. AND SUBSIDIARY

Consolidated Statements of Operations
Years ended December 31, 2009, 2008 and 2007

	2009	2008	2007
Net sales	$ 55,018,031	$ 78,641,845	$ 68,956,190
Cost of sales	(38,296,153)	(56,172,780)	(48,997,180)
Gross profit	16,721,878	22,469,065	19,959,010
Selling, general and administrative expenses	(15,587,140)	(19,672,837)	(17,487,768)
Operating profit	1,134,738	2,796,228	2,471,242
Other income (expense):			
Interest expense	(48,530)	(283,062)	(412,805)
Other, net	27,225	744	11,720
Earnings before income taxes	1,113,433	2,513,910	2,070,157
Income tax expense (note 6)	(416,683)	(994,498)	(803,900)
Net earnings	$ 696,750	$ 1,519,412	$ 1,266,257
Basic and diluted net earnings per common share	$ .38	$ .88	$ .74
Basic and diluted weighted average shares outstanding (note 2)	1,811,148	1,719,481	1,711,148

See accompanying notes to consolidated financial statements.

ABATIX CORP. AND SUBSIDIARY

Consolidated Statements of Stockholders' Equity
Years ended December 31, 2009, 2008 and 2007

	Common Stock		Additional		Treasury Stock		
	Shares Issued	Amount	Paid-in Capital	Retained Earnings	Shares	Amount	Total Equity
Balance at December 31, 2006	2,437,314	$ 2,437	$ 2,574,560	$ 11,645,520	726,166	$ (2,257,342)	$ 11,965,175
Net earnings	-	-	-	1,266,257	-	-	1,266,257
Balance at December 31, 2007	2,437,314	2,437	2,574,560	12,911,777	726,166	(2,257,342)	13,231,432
Net earnings	-	-	-	1,519,412	-	-	1,519,412
Balance at December 31, 2008	2,437,314	2,437	2,574,560	14,431,189	726,166	(2,257,342)	14,750,844
Issuance of treasury stock to the Employee Stock Ownership Plan (note 7)	-	-	48,105	-	(100,000)	251,895	300,000
Net earnings	-	-	-	696,750	-	-	696,750
Balance at December 31, 2009	2,437,314	$ 2,437	$ 2,622,665	$ 15,127,939	626,166	$ (2,005,447)	$ 15,747,594

See accompanying notes to consolidated financial statements.

ABATIX CORP. AND SUBSIDIARY

Consolidated Statements of Cash Flows
Years ended December 31, 2009, 2008 and 2007

	2009	2008	2007
Cash flows from operating activities:			
Net earnings	$ 696,750	$ 1,519,412	$ 1,266,257
Adjustments to reconcile net earnings to net cash provided by operating activities:			
Depreciation and amortization	399,416	503,324	525,633
Deferred income taxes	(17,565)	64,014	45,366
Amortization of intangible assets	2,764	64,555	10,445
Provision for losses on receivables	182,903	111,050	78,081
Provision for obsolescence of inventory	130,522	129,986	221,781
ESOP contribution payable in common stock	-	300,000	-
(Gain) loss on disposal of assets	(11,749)	2,550	2,882
Changes in operating assets and liabilities:			
Receivables	2,784,112	(372,198)	296,681
Inventories	857,581	(71,353)	(1,175,261)
Prepaid expenses and other assets	439,379	(447,923)	(201,783)
Other assets	(7,520)	-	5,457
Income taxes receivable	388,928	(251,774)	(137,154)
Accounts payable	(647,089)	117,652	(833,894)
Accrued expenses	(352,937)	180,005	127,856
Net cash provided by operating activities	4,845,495	1,849,300	232,347
Cash flows from investing activities:			
Purchase of property and equipment	(192,177)	(331,380)	(298,107)
Proceeds from the disposal of fixed assets	23,103	-	46,129
Business acquisitions, net of cash acquired (note 3)	(301,594)	-	-
Purchase of intangible assets (note 3)	-	-	(75,000)
Investment in insurance captive	(13,000)	-	-
Advances to employees	(14,663)	(8,000)	(10,070)
Collection of advances to employees	9,840	14,202	7,945
Net cash used in investing activities	(488,491)	(325,178)	(329,103)
Cash flows from financing activities:			
Borrowings on notes payable	13,896,809	26,988,166	22,146,479
Repayments on notes payable and long-term debt	(18,198,045)	(28,718,302)	(21,744,298)
Net cash (used in) provided by financing activities	(4,301,236)	(1,730,136)	402,181
Net increase (decrease) in cash	55,768	(206,014)	305,425
Cash at beginning of year	154,372	360,386	54,961
Cash at end of year	$ 210,140	$ 154,372	$ 360,386
Supplemental information:			
Cash paid for interest	$ 59,557	$ 303,179	$ 416,791
Cash paid for income taxes	$ 447,538	$ 1,336,015	$ 837,797

See accompanying notes to consolidated financial statements.

(1) General Information

Abatix Corp. (“Abatix”) and subsidiary (collectively, the “Company”) market and distribute personal protection and safety equipment, and durable and nondurable supplies to the environmental industry, the industrial safety industry and, combined with tools and tool supplies, the construction industry. At December 31, 2009, the Company operated nine sales and distribution centers in six states with the addition of the San Diego location in September 2009. In response to flooding in the summer of 2008, Abatix operated a temporary facility in Cedar Rapids, Iowa from June 2008 until August 2008. The effects of hurricanes and other natural disasters that occur in the U.S. have created an opportunity for the Company to improve revenue and profitability and increase our customer base. However, this revenue is non-recurring and may cause volatility in our revenues and profits.

Abatix’s wholly-owned subsidiary, International Enviroguard Systems, Inc. (“IESI”) imports disposable protective clothing products sold through Abatix’s distribution channels and through other distributors.

(2) Summary of Significant Accounting Policies

The preparation of financial statements in conformity with generally accepted accounting principles in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of expenses during the reporting period. Actual results could differ from those estimates.

The accompanying consolidated financial statements include the accounts of Abatix and IESI. All significant intercompany accounts and transactions have been eliminated in consolidation. Certain prior year amounts have been reclassified for consistency in presentation including the reclassification between cash and trade accounts receivable for credit card receivables.

(a) Accounts Receivable

Accounts receivable consist of sales, on terms, to customers that have been deemed to be creditworthy. The Company establishes reserves for customer accounts that are potentially uncollectible. Management’s methodology used to estimate the allowance is based on many factors including economic conditions that may affect a specific industry, geographic region or specific customer, historical trends, the age of the receivables and payment history of specific customers. A write-off occurs when management deems the Company will not collect the receivable. Actual write-offs could be materially different than the reserves.

(b) Inventories

Inventories consist of materials and equipment for resale and are stated at the lower of cost or market. Cost is determined by the first-in, first-out method. The Company establishes reserves for lower of cost or market and obsolescence issues. Management's methodology used to estimate the allowance is based on many factors including economic conditions, competitive products, historical trends and the age of the inventory, which is based on number of days since the item was last sold. A write-off occurs when Management deems the Company will not sell an inventory item or product line. Actual write-offs could be materially different than the reserves.

(c) Vendor Consideration

The Company has numerous programs to promote its vendors' products, including catalogs, the Internet and other marketing and advertising programs. Most of these programs support multiple vendors. To the extent funds received from vendors are associated with marketing programs, those funds are included in selling, general and administrative (advertising) expenses as a reduction to the cost of the program.

Rebates earned from vendors that are based on purchases reduce cost of sales. However, the Company calculates the amount of rebates that should be applied to ending inventory in each reporting period based on inventory turnover and capitalizes that estimate into inventory.

(d) Intangible Assets

Intangible assets with finite lives are amortized on a straight-line basis over their estimated useful lives. The estimated remaining useful lives are evaluated and adjusted, if appropriate, at each reporting period. In addition, the intangible assets are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. An impairment loss would be indicated when estimated undiscounted future cash flows from the use of the asset are less than its carrying amount. An impairment loss would be measured as the difference between the fair value (based on discounted future cash flows) and the carrying amount of the asset. See note 3 for further information.

(e) Property and Equipment

Property and equipment are stated at cost. Depreciation is provided by the straight-line method over the estimated useful lives of the assets. Leasehold improvements are depreciated over the initial term of the respective lease. See note 4 for further information.

(f) Impairment of Long-Lived Assets and Long-Lived Assets to Be Disposed Of

The Company reviews long-lived assets for impairment whenever events or changes in circumstances indicate the carrying amount of an asset may not be recoverable. Recoverability of assets to be held and used is measured by a comparison of the carrying amount of an asset to future net cash flows expected to be generated by the asset. If such assets are considered to be impaired, the impairment to be recognized is measured by the amount by which the carrying value of the assets exceeds the fair value of the assets. Assets to be disposed of are reported at the lower of the carrying amount or fair value less costs to sell.

(g) Revenue Recognition

As the Company's standard shipping terms are FOB shipping point, revenue is recognized when the goods are shipped. Sales are reported net of returns, allowances and customer rebates. Shipping fees billed to customers are included in net sales. The costs related to these shipping fees, which are included in selling, general and administrative expense, were $1,330,000, $1,804,000, and $1,763,000 for the years ended December 31, 2009, 2008 and 2007, respectively.

Taxes assessed by governmental agencies based on the value of the sale, which are billed to customers, and ultimately remitted to such governmental agencies are not recorded as revenue in the Company's Consolidated Statements of Operations.

(h) Lease Costs

The Company has operating leases for all of its facilities. The Company factors the known terms that will occur during the term of the lease and applies the straight-line method to determine rent expense. Known factors include such items as rent increases, if determinable, rent holidays or rent concessions.

(i) Advertising Costs

Advertising costs are expensed as incurred. Advertising expense was $160,000, $287,000, and $283,000 in 2009, 2008 and 2007, respectively.

(j) Retained Insurance Reserves

The Company funds all health care related costs below certain limits, after which, the Company has traditional insurance that covers catastrophic claims. The accrued liabilities for incurred but not reported events are based upon historical loss patterns, specific events that the Company may become aware of and management's judgment. Retained insurance reserves were $47,000, $44,000, and $48,000 at December 31, 2009, 2008 and 2007, respectively.

(k) Earnings per Share

Basic earnings per share is calculated using the weighted average number of common shares outstanding during each year, while diluted earnings per share includes the effects of all dilutive potential common shares. As of December 31, 2009, 2008 and 2007, there were no dilutive securities outstanding. Therefore, the weighted average number of common shares outstanding is the same for basic and diluted earnings per share for each period presented.

As shares are committed to be released for allocation to Employee Stock Ownership Plan ("ESOP") participants, the shares become outstanding for basic and diluted earnings per share computations. Such shares will be weighted according to the portion of the year they are outstanding. However, these shares have no impact on the Consolidated Statement of Shareholder's Equity or the Stockholders' Equity section of the Consolidated Balance Sheet until the shares are issued to the trustee.

In December 2008, 100,000 shares of common stock were committed to be released to the ESOP, although these shares were not delivered to the trustee until February 2009. The 100,000 shares committed to be released are included in the 2008 earnings per share computation on a weighted average basis. See note 7 for further details of the ESOP.

(l) Income Taxes

The Company accounts for income taxes using the asset and liability method. Under this method the Company records deferred income taxes for the temporary differences between the financial reporting basis and the tax basis of assets and liabilities at enacted tax rates expected to be in effect when such amounts are realized or settled. The resulting deferred tax liabilities and assets are adjusted to reflect changes in tax laws or rates in the period that includes the enactment date. If the Company determines that future earnings will not be sufficient to realize the benefit of deferred tax assets, a valuation allowance would be established.

The Company accrues for interest and penalties associated with income tax liabilities in accordance with applicable tax laws. Any charges for interest and penalties related to income tax liabilities are recorded in the income tax expense on the Consolidated Statements of Operations.

Effective January 1, 2007, the Company adopted the provisions of Financial Accounting Standards Board ("FASB") Interpretation Number 48, which is now included in Accounting Standards Codification Topic ("FASB ASC Topic") 740, *Income Taxes*. FASB ASC Topic 740 clarifies the accounting for income taxes by prescribing a minimum recognition threshold tax benefits are required to meet before being recognized in the financial statements. The purpose of FASB ASC Topic 740 is to clarify and set forth consistent accounting rules for uncertain tax positions. The impact of the adoption of FASB ASC Topic 740 was not material to the consolidated financial statements. See note 6 for further information.

(m) Recent Accounting Standards

In June 2009, the FASB issued Statement of Financial Accounting Standards ("SFAS") 168, *The FASB Accounting Standards Codification and the Hierarchy of Generally Accepted Accounting Principles — a replacement of FAS 162* ("SFAS 168"), which created FASB ASC Subtopic 105-10. FASB ASC Subtopic 105-10 identifies the sources of accounting principles and the framework for selecting principles used in the preparation of financial statements of nongovernmental entities that are presented in conformity with US Generally Accepted Accounting Principles ("GAAP"). The Statement makes the Codification effective for interim and annual periods ending after September 15, 2009. On the effective date, the Codification will supersede existing non-SEC accounting and reporting standards. From the effective date of the Codification, there will no longer be levels of authoritative GAAP, all content within the Codification carries the same level of authority.

While the guidance was not intended to change GAAP, it did change the way the Company references these accounting principles in the Notes to the Consolidated Financial Statements. The Company adopted FASB ASC Subtopic 105-10 beginning October 1, 2009.

In May 2009, the FASB issued SFAS 165, *Subsequent Events* ("SFAS 165"), codified in FASB ASC Subtopic 855-10, which establishes accounting and disclosure standards for events that occur after the balance sheet date, but before financial statements are issued or are available to be issued for interim or annual financial periods ending after June 15, 2009. This guidance was effective for interim or annual financial periods ending after June 15, 2009. It defines financial statements as available to be issued, requiring the disclosure of the date through which an entity has evaluated subsequent events and the basis for that date, whether it be the date the financial statements were issued or the date they were available to be issued. The Company adopted SFAS 165 upon issuance.

In April 2009, the FASB issued FSP 141(R)-1, *Accounting for Assets Acquired and Liabilities Assumed in a Business Combination That Arise from Contingencies* ("FSP 141(R)-1"). FSP 141(R)-1, which is included in FASB ASC Topic 805, *Business Combinations*, addresses application issues related to the measurement, accounting and disclosure of assets and liabilities arising from contingencies in a business combination. This guidance was effective on or after the beginning of the first annual reporting period on or after December 15, 2008. The Company adopted FASB ASC Topic 805 upon issuance. This standard did not have an impact on the Company's consolidated financial statements.

In December 2007, the FASB issued Statement No. 141(R), "*Business Combinations*." Statement No. 141(R), which is now codified as FASB ASC Topic 805, establishes principles and requirements for how an acquirer recognizes and measures in its financial statements the identifiable assets acquired, the liabilities assumed, any noncontrolling interest in the acquiree and the goodwill acquired. FASB ASC Topic 805 also establishes disclosure requirements to enable the evaluation of the nature and financial effects of the business combination. FASB ASC Topic 805 was effective for fiscal years beginning after December 15, 2008. The impact of adoption of FASB ASC Topic 805 was that immaterial transaction costs were included in selling, general and administrative costs for the year ended December 31, 2009. See note 3 for further information.

(3) Intangible Assets and Acquisitions

Effective December 17, 2009, the Company consummated an asset purchase agreement with Golden Triangle Imports Inc. ("Golden Triangle"), an industrial safety supply distributor based in Jacksonville, Florida. The estimated fair value of the assets acquired was approximately $302,000. The aggregate purchase price was settled in cash without the assumption of any liabilities. This acquisition has been accounted for using the Acquisition method of accounting and, accordingly, the results of Golden Triangle's operations are included in the Company's consolidated financial statements since the acquisition date. No goodwill was created in the acquisition. Purchased intangible assets of $66,331 are being amortized on a straight-line basis over two years. The accumulated amortization of the intangible assets recorded as of December 31, 2009 was $2,764.

In May 2007, IESI entered into an Exclusive Marketing and Sales Agreement and Joint Venture Letter of Intent ("Agreement"). This Agreement licensed the right for IESI to sell a certain fabric for a period of three years, provided that the obligations defined in the agreement were met. In accordance with the Agreement, IESI paid the $75,000 in licensing fees ("License Fees"). The information available at the time indicated a residual value of zero. At December 31, 2007, due to difficulties with the licensor, the Company estimated the remaining useful life of the License Fees to be one year. Therefore, the License Fees were fully amortized as of December 31, 2008.

(4) Property and Equipment

Property and equipment consists of the following at December 31, 2009 and 2008:

	Estimated Useful Life	2009	2008
Furniture and equipment	3 - 5 years	$ 3,324,926	$ 3,575,708
Transportation equipment	3 - 5 years	498,956	490,979
Leasehold improvements	3 - 10 years	507,636	495,457
		4,331,518	4,562,144
Less accumulated depreciation and amortization		(3,564,398)	(3,579,991)
Net property and equipment		$ 767,120	$ 982,153

(5) Notes Payable

The Company amended its credit agreement in September 2009. At December 31, 2009 the Company has a $5,000,000 working capital line of credit and a $500,000 capital equipment facility with its financial institution. The working capital facility allows the Company to borrow up to 80% of the book value of eligible trade receivables plus the lesser of 40% of eligible inventory or $2,500,000, up to a maximum of $5,000,000. The capital equipment facility provides for individual borrowings at 80% of the purchased equipment's cost. These credit facilities require the Company to maintain a minimum level of trailing twelve months earnings before interest, taxes, depreciation and amortization and a debt to equity level that the Company is not to exceed. These credit facilities are secured by accounts receivable, inventories and equipment.

- Based on the borrowing formula calculated as of December 31, 2009 the Company had the capacity to borrow up to a maximum of $5,000,000 on its working capital line.
- As of December 31, 2009, there were no advances outstanding on either loan facility. As of December 31, 2008, there was $4,227,538 outstanding on the working capital facility and $73,698 outstanding on the capital equipment facility.
- The Company's rate of interest on these facilities was:
  - December 31, 2009 – 3.25%
  - December 31, 2008 – 2.75%
  - December 31, 2007 – 6.75%
  - Subsequent to September 9, 2009, both credit facilities bear a variable rate of interest tied to the LIBOR rate.
- Both credit facilities expire in September 2010. The Company believes it will be able to extend our credit facilities or obtain financing from another source as substantially similar amounts, terms and conditions.
- Although the Company has relationships with three financial institutions, all of the Company's credit facilities are currently at one financial institution.

(6) Income Taxes

Income tax expense (benefit) for the years ended December 31, 2009, 2008 and 2007 consists of:

	2009	2008	2007
Current:			
Federal	$ 392,373	$ 817,671	$ 665,038
State	41,875	112,813	93,496
Total current expense	434,248	930,484	758,534
Deferred:			
Federal	(16,101)	63,021	42,549
State	(1,464)	993	2,817
Total deferred (benefit) expense	(17,565)	64,014	45,366
Total income tax expense	$ 416,683	$ 994,498	$ 803,900

A reconciliation of expected federal income tax expense to actual income tax expense for the years ended December 31, 2009, 2008 and 2007 follows:

	2009	2008	2007
Expected income tax expense	$ 378,567	$ 854,729	$ 703,853
State income taxes, net of related federal tax benefit	26,671	75,112	63,567
Nondeductible meals, entertainment expense	25,054	57,252	30,775
Other	(13,609)	7,405	5,705
Actual income tax expense	$ 416,683	$ 994,498	$ 803,900

The effective tax rate is greater than the Federal statutory rate because it includes items that are not deductible for Federal income taxes, as well as state income taxes.

The income tax effects of temporary differences that gave rise to the deferred tax assets and liabilities at December 31, 2009 and 2008 are as follows:

	2009	2008
Deferred tax assets:		
Allowance for doubtful accounts	$ 181,389	$ 194,540
Inventory	530,297	460,330
Goodwill	128,217	157,531
Property and equipment, principally due to differences in depreciation	20,457	11,659
Accrued compensation	1,416	124,983
Deferred rent	68,632	80,347
Intangible assets	862	-
Total gross deferred tax assets	931,270	1,029,390
Deferred tax liabilities:		
Retained insurance reserves	(8,412)	(9,974)
Prepaid expenses	(53,173)	(167,296)
Total gross deferred tax liabilities	(61,585)	(177,270)
Net deferred tax assets	$ 869,685	$ 852,120

The net deferred tax assets are classified as follows:		
Current assets	$ 720,149	$ 682,929
Noncurrent assets	149,536	169,191
Net deferred tax assets	$ 869,685	$ 852,120

Management has determined, based on the Company’s prior operating earnings, prior taxable income and its expectations for the future, that earnings will more likely than not be sufficient to realize the benefit of the deferred tax assets. Accordingly, the Company has not provided a valuation allowance for deferred tax assets in any period presented.

The Company records liabilities in current income taxes for potential assessments resulting from tax audits. Any accruals related to uncertain tax positions, in potentially a variety of taxing jurisdictions, are based on what management believes will be the ultimate resolution of these positions. These liabilities may be affected by changing interpretations of laws, rulings by tax authorities, or the expiration of the statute of limitations. The Company has analyzed all filing positions in federal and state tax jurisdictions where it is required to file income tax returns. Major tax jurisdictions of the Company include the federal jurisdiction and the states of Texas and California.

The Company's U.S. federal income tax returns have been audited through 2005 and all federal assessments of additional taxes, interest and penalties have been paid. State tax returns are open to examination for years 2006 through 2008. The Company believes that it is more likely than not that all income tax positions and deductions will be sustained on audit. Accordingly, no reserves for uncertain income tax positions have been recorded in the financial statements. There are no unrecognized tax benefits as of December 31, 2009, no change in the balance during the year for new positions, tax positions from prior years, settlements or lapse of statute of limitations, nor does the Company anticipate any change in its unrecognized tax benefits during the next twelve months.

The Company recognizes accrued interest and penalties related to income taxes in income tax expense. During the years ended December 31, 2009 and 2008, the Company did not recognized any amount for these interest and penalties, while during the year ended December 31, 2007, the Company recognized a net cost of approximately $3,000. In addition, related to these interest and penalties, there were no amounts accrued for in the Consolidated Balance Sheets at December 31, 2009 and 2008.

(7) Benefit Plans

The Company has a 401(k) profit sharing plan, under which eligible employees may request the Company deduct and contribute a portion of their compensation to the plan. The Company, at its discretion, may match a portion of employee contributions to the plan. Contributions by the Company to the 401(k) plan aggregated $27,273, $121,362 and $93,485 during 2009, 2008 and 2007, respectively.

In an effort to better align the long-term interests of all employees with the long-term interests of the stockholders, the Company established an ESOP, a qualified plan, effective January 1, 2008. All eligible employees who were employed as of April 29, 2008, the date the plan document was executed, were automatically participants in the ESOP. Other employees must meet certain eligibility requirements, which are primarily being employed by the Company for one year and attaining 21 years of age. Participants must be employed on the last day of the plan year to participate in that year's allocation of any contribution made by the Company. The allocation of assets in the ESOP to individual participants is based on a formula that weighs compensation and tenure with the Company equally. Participants vest based on the years of service from the effective date of the ESOP according to the following table.

Years of Service	Vesting Percentage
Less than 1	0%
1	20%
2	40%
3	60%
4	80%
5 or more	100%

The amount of the Company's discretionary contribution to the ESOP is determined by the Board of Directors ("Board"). The Company recognizes contributions to the ESOP as compensation cost in the year which they occur. Compensation cost is determined as the fair market value of the shares contributed to the plan or as the amount of cash that is contributed to the ESOP.

In December 2009, the Board committed to contribute $60,000 to the ESOP for the 2009 plan year. The cash was delivered to the Trustee in January 2010 for investment in outstanding Abatix stock to be allocated to the participant accounts. Therefore, the Company recognized an accrued compensation liability on the Consolidated Balance Sheet as of December 31, 2009 in the amount of $60,000 with a corresponding compensation expense in the Consolidated Statement of Operations for the year ended December 31, 2009.

In December 2008, the Board committed to release 100,000 shares from treasury stock to the ESOP for the 2008 plan year. All 100,000 shares were delivered to the ESOP custodian in February 2009 for allocation to the participant accounts. Therefore, the Company recognized an accrued compensation liability on the Consolidated Balance Sheet as of December 31, 2008 in the amount of $300,000 with a corresponding compensation expense in the Consolidated Statement of Operations for the year ended December 31, 2008.

The Company used quoted prices in active markets for identical assets (Level 1) as inputs in the market approach to determine the fair value measurement of the stock contribution to the ESOP as of December 31, 2008 as shown in the table below.

		Fair Value Measurements at Reporting Date Using		
Description	**December 31, 2008**	**Quoted Prices in Active Markets for Identical Assets (Level 1)**	**Significant Other Observable Inputs (Level 2)**	**Significant Unobservable Inputs (Level 3)**
Accrued stock compensation	$300,000	$300,000	-	-

In accordance with the provisions of the ESOP, only the vested amount will be distributed to a terminated participant. Depending on factors like vested account balance and reason for termination, the distribution will occur no later than the fifth plan year after the participant separated from service. As long as the Company’s shares are publicly traded, the Company has the option to distribute the vested balance in Company shares, cash or partly in each. As of December 31, 2009 the Company is under no obligation to repurchase shares distributed to any terminated participant.

(8) Fair Value of Financial Instruments

The reported amounts of financial instruments such as cash, accounts receivable, accounts payable and accrued expenses approximate fair value because of their short maturity. The carrying value of notes payable to bank approximates fair value because these instruments bear interest at current market rates.

(9) Segment Information

Identification of operating segments is based principally upon differences in the types and distribution channel of products. The Company's reportable segments consist of Abatix and IESI. The Abatix operating segment includes the Company's corporate operations and the aggregated operating locations (including any temporary facilities), which are principally engaged in distributing environmental, safety and construction equipment and supplies to contractors and industrial manufacturing facilities in the Western, Southwestern and Southeastern portions of the United States. The IESI operating segment, which consists of the Company's wholly-owned subsidiary, International Enviroguard Systems, Inc., is engaged in the wholesale distribution of disposable protective clothing to companies similar to, and including, Abatix. The IESI operating segment distributes products primarily throughout the United States.

The accounting policies are consistent in each operating segment as described in note 2 of the Notes to Consolidated Financial Statements. The Company evaluates the performance of its operating segments based on operating profit after a charge for the carrying value of inventory and accounts receivable. Intersegment sales are at agreed upon pricing and intersegment profits are eliminated in consolidation.

Summarized financial information concerning the Company's reportable segments is shown in the following table. There are no significant noncash items.

	Abatix	IESI	Total
2009			
Sales from external customers	$50,283,751	$ 4,734,280	$55,018,031
Intersegment sales	50,672	2,254,968	2,305,640
Interest expense	48,530	-	48,530
Depreciation and amortization	368,083	34,097	402,180
Segment profit	434,864	866,044	1,300,908
Segment assets	16,471,411	3,036,518	19,507,929
Capital expenditures	187,042	5,135	192,177
2008			
Sales from external customers	$74,679,916	$ 3,961,929	$78,641,845
Intersegment sales	396	2,145,951	2,146,347
Interest expense	283,062	-	283,062
Depreciation and amortization	465,844	102,035	567,879
Segment profit	2,628,519	136,526	2,765,045
Segment assets	20,920,763	2,915,607	23,836,370
Capital expenditures	327,949	3,431	331,380
2007			
Sales from external customers	$65,393,606	$ 3,562,584	$68,956,190
Intersegment sales	1,047	1,606,474	1,607,521
Interest expense	412,805	-	412,805
Depreciation and amortization	491,064	45,014	536,078
Segment profit	2,312,954	234,926	2,547,880
Segment assets	21,048,149	2,528,592	23,576,741
Capital expenditures	267,218	30,889	298,107

Below is a reconciliation of (i) total segment profit to operating profit on the Consolidated Statements of Operations, and (ii) total segment assets to total assets on the Consolidated Balance Sheets for all periods presented. The sales from external customers represent the net sales on the Consolidated Statements of Operations.

	2009	2008	2007
Profit for reportable segments	$ 1,300,908	$ 2,765,045	$ 2,547,880
Elimination of intersegment profits	(166,170)	31,183	(76,638)
Operating profit	$ 1,134,738	$ 2,796,228	$ 2,471,242
Total assets for reportable segments	$19,507,929	$23,836,370	$23,576,741
Elimination of intersegment assets	(419,000)	(142,929)	(270,233)
Total assets	$19,088,929	$23,693,441	$23,306,508

The Company's sales, substantially all of which are on an unsecured credit basis, are to various customers from its permanent distribution centers in Texas, California, Arizona, Washington, Nevada and Florida and its temporary facilities, if any. The Company evaluates credit risks on an individual basis before extending credit to its customers and it believes the allowance for doubtful accounts adequately provides for loss on uncollectible accounts. During 2009 and 2008, no single customer accounted for more than 10% of net sales, although sales to environmental contractors were approximately 38% and 46%, respectively.

The receivables balance is comprised of more than 1,600 accounts. The largest customer receivable represented approximately 7% and 9% of the total receivables balance as of December 31, 2009 and 2008, respectively. The top ten companies owing money represented approximately 24% and 35% as of December 31, 2009 and 2008, respectively. While most of these accounts have been customers of the Company for more than four years, with several being customers of the Company for more than ten years, non-payment by any one of these accounts would have a significant negative impact on the cash flows of the Company. During times of disasters, as was the case in 2008, the concentration of balances in a few customers could be significantly larger.

In 2009, one vendor, a manufacturer of disposable clothing, represented 10% of the Company's sales. No one vendor accounted for more than 10% of the Company's sales in 2008 or 2007. The top ten vendors represented 42%, 38% and 36% of sales for 2009, 2008 and 2007, respectively. In addition, two product classes (groupings of similar products) accounted for greater than 10% of sales for 2009, 2008 or 2007.

- The first product class, plastic sheeting and bags, accounted for approximately 18%, 17% and 18% of net sales in 2009, 2008 and 2007, respectively. A major component of these products is petroleum. Volatility in oil prices or shortages in supply could significantly impact sales and the Company's ability to supply its customers with certain products at a reasonable price.
- The second product class, disposable clothing, accounted for approximately 19%, 14% and 14% of net sales in 2009, 2008 and 2007, respectively. A majority of these products are produced internationally, predominantly in China. Changes in the political or economic climates or other events (e.g., Swine Flu, Avian Bird Flu, SARS, etc.) could impact our ability to obtain these products from our current sources.

(10) Commitments and Contingencies

The Company leases warehouses, office facilities and certain office equipment under long-term noncancelable operating leases and has other noncancelable agreements expiring at various dates through April 2017. These leases and other agreements generally contain standard terms and conditions. The following is a schedule of future minimum lease payments and other agreement payments as of December 31, 2009:

2010	$ 1,023,000
2011	690,000
2012	481,000
2013	466,000
2014	453,000
Thereafter	1,004,000
	$ 4,117,000

Rental expense under operating leases for the years ended December 31, 2009, 2008 and 2007 was $1,369,598, $1,347,212 and $1,251,649, respectively.

The Company has employment agreements with three officers (expiring at the end of 2010) and a key employee (expiring December 17, 2011). The agreements provide for combined minimum annual compensation of $764,200 and $106,700 in 2010 and 2011, respectively.

Currently the Company is not a party to any material legal proceedings but from time to time the Company may be involved with various legal proceedings arising in the normal course of business.

(11) Subsequent Events

On January 12, 2010 the Company announced the Board of Directors authorized the repurchase of up to $500,000 of the Company's common stock.

Stock repurchases under this program may be made in the open market or through privately negotiated transactions during 2010. This program could be suspended and restarted at any time without prior notice. The timing and actual number of shares repurchased will depend upon market conditions and other factors.

Material subsequent events have been evaluated and disclosed through the audit report date.

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Certain product, event and financial information are available on these sites.

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Senior Executive Vice President and
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Chairman of the Board, President
and Chief Executive Officer

Gary L. Cox
Senior Executive Vice President and
Chief Operating Officer

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STOCK LISTING
Abatix Corp.'s Common Stock trades on the Pink Sheets market under the symbol "ABIX.PK".

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