



November 23, 2015

Dear Stockholder

I am pleased to provide you with the fourth update on PharmChem, Inc. (the “Company”) as well as the Company’s results for the year ending December 31, 2014.

As discussed in last year’s update, the Company has shifted its customer base from those customers who are federally directed to state-funded Drug Court monitoring programs, including rehabilitation facilities. In concert with this shift, the Company further committed and fashioned its marketing efforts to demonstrate that its PharmChek® Sweat Patch would provide valuable assistance in the monitoring of offenders on probation or seeking help.

This commitment has been further emphasized by the Company’s hiring of Kerri S. Wagner as President of the PharmChek® Sweat Patch Division. In this position, Ms. Wagner is responsible for sales, customer service, marketing, and training, as well as managing the Company’s growth and expansion efforts. Ms. Wagner began a 13-year career as a Police Officer in South Dakota in 1992, before transferring in 2005 to the South Dakota Department of Corrections. In 2006, Ms. Wagner was charged with the management and oversight of the Department’s 24/7 Sobriety Program, where the Sweat Patch technology is actively utilized. In 2013, she was promoted to Senior Parole Agent for the Department of Corrections. Ms. Wagner has provided consulting, training and related services to the Company since 2011.

The Company estimates that the number of Drug Courts (as well as those dealing with DWI/DUI’s and the treatment of veterans) now number approximately 2,900. The Company estimates that these Drug Courts receive approximately \$104 million in federal funding and \$260 million in state funding. This funding, complemented by the requirement of participants to provide financial assistance for their treatment, has accelerated the use of the Sweat Patch when drugs of abuse are a concern.

The Company’s 2014 results reflect the successes it has experienced by building upon the shift in its customer base, thereby improving financial results and growing market share.

Some of the Company’s accomplishments include: sales were \$2,522,857, an increase over 2013 of 42%; operating income more than tripled to \$471,809; net income grew to \$433,995; and cash and cash equivalents increased \$563,906. Over the past two years, we’ve secured 133 new customers and, in 2014, we sold our product and related services in 42 states and six foreign countries—the latter related mainly to research.

Also, the Company completed an audit of its 2014 financial statements as well as an independent FDA compliance review.



Attached are summary financial statements for 2014 and 2013.

As previously discussed, merger and acquisition activity remains one of the Company's highest priorities. The Company is not waiting for an exit opportunity to arise; rather, it is proactively seeking to present PharmChem, Inc. and its strategic value to the few larger entities that can benefit from acquiring the Company at the appropriate valuation. However, the industry's appetite for acquisitions has dampened—particularly for those which are priced fairly.

Going forward, certain risk factors and challenges remain. The Company needs a sizeable investment for further research and development in order to keep abreast of current trends and heavily regulated protocols to which the Company's business continues to be subjected. Also, new FDA regulations relating to recalls and serialization may affect the Company's performance. The Company will also likely need new screening assays in the near future. Moreover, PharmChem continues to monitor certain contractual disputes inherited by the Company years ago. Finally, the Company must continue to address the dilemma of developing other certified laboratories capable of testing its Sweat Patch.

Potential buyers likely view these regulatory and risk factors as impediments to acquiring the Company. However, given the Company's sales growth of 8% in 2013, 42% in 2014, and an expected double-digit increase in 2015, it is believed that the Company's franchise has an inherent value not yet reflected in the market.

I appreciate your continued support. Future updates will be made as conditions warrant.

Joseph W. Halligan  
President & Chief Executive Officer  
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In 2003, the Company filed Form 15 with the Securities and Exchange Commission effectively terminating its registration under the Securities Exchange Act of 1934. The Company has no plans to revoke this filing.

The Company does not believe that it is subject to the Securities Exchange Commission's reporting requirements. Nonetheless, this letter contains forward-looking statements within the meaning of Section 21E of the Securities Exchange Act of 1934 and Section 27A of the Securities Act of 1933 ("Forward-looking Statements"), which are subject to the "safe harbor"



created by these Sections. Forward-looking statements are statements about future financial results, future products or services and other events that have not yet occurred. These forward-looking statements contain words such as, but not limited to, “expect”, “anticipate”, “estimate”, “believe”, “will”, “may” or “might”. Investors should be aware that actual results may differ materially from our expressed expectations because of risks and uncertainties about the future. We will not necessarily update the information in this letter if any forward-looking statement later turns out to be inaccurate.”



PharmChem, Inc.  
Summary Balance Sheets  
December 31, 2014 and 2013

	2014 <u>(Audited)</u>	2013 <u>(Unaudited)</u>
Cash & Cash Equivalents	\$ 1,620,866	\$ 1,056,960
Short-Term Securities	57,028	127,482
Receivables, Net	303,331	240,537
Other Current Assets	88,462	91,135
	<u>2,069,687</u>	<u>1,516,114</u>
Property and Equipment	6,776	7,652
Total Assets	<u>\$ 2,076,463</u>	<u>\$ 1,523,766</u>
Accounts Payable	\$ 180,193	\$ 103,372
Accrued Expenses	201,049	159,168
Total Liabilities	<u>381,242</u>	<u>262,540</u>
Stockholders' Equity	<u>1,695,221</u>	<u>1,261,226</u>
	<u>\$ 2,076,463</u>	<u>\$ 1,523,766</u>

Certain restatements and reclassifications to prior year amounts have been made to conform to the current year's presentation.



PharmChem, Inc.  
Summary Statements of Operations  
For The Twelve Months Ending December 31, 2014 and 2013

	2014 <u>(Audited)</u>	2013 <u>Unaudited)</u>
Net Sales	\$ 2,522,857	\$ 1,775,230
Cost of Goods Sold	<u>949,704</u>	<u>651,554</u>
Gross Profit	1,573,153	1,123,676
Selling, General & Administrative Expenses	<u>1,101,344</u>	<u>1,000,884</u>
Operating Income	471,809	122,792
Dividend Income and Realized and Unrealized Loss on Securities, Net	<u>(32,502)</u>	<u>14,807</u>
Net Profit Before Taxes	439,307	137,599
Provisions for (Benefit) From Taxes	<u>5,312</u>	<u>(7,520)</u>
Net Income	<u>\$ 433,995</u>	<u>\$ 145,119</u>

Certain restatements and reclassifications to prior year amounts have been made to conform to the current year's presentation.