Lifevantage Corp
Form 10-Q
May 06, 2014

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

Form 10-Q

ý QUARTERLY REPORT UNDER SECTION 13 OR 15 (d) OF THE SECURITIES EXCHANGE ACT OF 1934
FOR THE QUARTERLY PERIOD ENDED MARCH 31, 2014

¨ TRANSITION REPORT PURSUANT TO SECTION 13 OR 15 (d) OF THE SECURITIES EXCHANGE ACT OF 1934
FOR THE TRANSITION PERIOD FROM TO
Commission file number 001-35647

LIFEVANTAGE CORPORATION
(Exact name of Registrant as specified in its charter)

COLORADO	90-0224471
(State or other jurisdiction of incorporation or organization)	(IRS Employer Identification No.)

9785 S. Monroe Street, Ste 300, Sandy, UT 84070
(Address of principal executive offices)
(801) 432-9000
(Registrant’s telephone number)
9815 S. Monroe Street, Suite 100, Sandy, UT 84070
(Former name, former address and former fiscal year, if changed since last report)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15 (d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes ý No ¨
Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes ý No ¨
Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of “large accelerated filer,” “accelerated filer” and “smaller reporting company” in Rule 12b-2 of the Exchange Act.

Large accelerated filer	¨	Accelerated filer	ý
Non-accelerated filer	¨ (Do not check if a smaller reporting company)	Smaller reporting company	¨

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes ¨ No ý
The number of shares outstanding of the issuer’s common stock, par value $0.001 per share, as of May 01, 2014 was 103,701,792.

CAUTIONARY NOTE REGARDING FORWARD-LOOKING STATEMENTS

This quarterly report on Form 10-Q, in particular "Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations," and the information incorporated by reference herein contains “forward-looking statements” (as such term is defined in Section 27A of the Securities Act of 1933, as amended and Section 21E of the Securities Exchange Act of 1934, as amended). These statements, which involve risks and uncertainties, reflect our current expectations, intentions, or strategies regarding our possible future results of operations, performance, and achievements. Forward-looking statements include, without limitation: statements regarding future products or product development; statements regarding future selling, general and administrative costs and research and development spending; statements regarding the future performance of our network marketing efforts; statements regarding our expectations regarding ongoing litigation; and statements regarding future financial performance, results of operations, capital expenditures and sufficiency of capital resources to fund our operating requirements. These forward-looking statements are made pursuant to the safe harbor provisions of the Private Securities Litigation Reform Act of 1995 and applicable rules of the Securities and Exchange Commission and common law.

These forward-looking statements may be identified in this report and the information incorporated by reference by words such as “anticipate”, “believe”, “could”, “estimate”, “expect”, “intend”, “plan”, “predict”, “project”, “should” and simila expressions, including references to assumptions and strategies. These statements reflect our current beliefs and are based on information currently available to us. Accordingly, these statements are subject to certain risks, uncertainties, and contingencies, which could cause our actual results, performance, or achievements to differ materially from those expressed in, or implied by, such statements.

The following factors are among those that may cause actual results to differ materially from our forward-looking statements:

- We may not succeed in expanding our operations;
- Inability to conform to government regulations in existing markets;
- We may not succeed in growing existing markets or opening new international markets;
- Inability to manage our growth and expansion;
- Disruptions in our information technology systems;
- Claims against us as a result of our independent distributors failing to comply with our policies and procedures;
- Inability of new products to gain distributor and market acceptance;
- International trade or foreign exchange restrictions, increased tariffs, foreign currency exchange;
- Deterioration of global economic conditions;
- Inability to maintain appropriate level of internal control over financial reporting;
- We may be unable to raise additional capital if needed;
- Exposure to environmental liabilities stemming from past operations and property ownership;
- Significant dependence upon a single product;
- The impact of our debt service obligations and restrictive debt covenants;
- Our inability to obtain high quality raw material for our products;
- Improper actions by our independent distributors that violate laws or regulations;
- Our inability to retain independent distributors or to attract new independent distributors on an ongoing basis;
- We may be subject to a product recall;
- Our dependence on third parties to manufacture our products;
- Significant government regulations on network marketing activities;
- Third party and governmental actions involving our network marketing sales activities;
- Our direct selling program could be found to not be in compliance with current or newly adopted laws or regulations;

- Unfavorable publicity on our business or products;
- Legal proceedings may be expensive and time consuming;
- Regulations governing the production or marketing of our products;
- Our business is subject to strict government regulations;
- We are subject to the risk of investigatory and enforcement action by the federal trade commission;
- Government authorities may question our tax positions or transfer pricing policies or change their laws in a manner that could increase our effective tax rate or otherwise harm our business;
- Failure to comply with anti-corruption laws;
- Loss of key personnel;
- Competition in the dietary supplement market;
- Our inability to protect our intellectual property rights;
- Third party claims that we infringe on their intellectual property;
- Product liability claims against us;
- Economic, political, foreign exchange and other risks associated with international operations;
- Significant dilution of outstanding voting shares if holders of our existing warrants and options exercise their securities for shares of common stock;
- Volatility of the market price of our common stock;
- We have not paid dividends on our capital stock, and we do not currently anticipate paying dividends in the foreseeable future; and
- Other factors not specifically described above, including the other risks, uncertainties, and contingencies described under “Part II. Item 1A — Risk Factors” of this Quarterly Report on Form 10-Q or under “Business”, “Risk Factors” and “Management’s Discussion and Analysis of Financial Condition and Results of Operations” in Items 1, 1A and 7 of our Annual Report on Form 10-K for the year ended June 30, 2013.

When considering these forward-looking statements, you should keep in mind the cautionary statements in this report and the documents incorporated by reference. We have no obligation and, except as required by law, do not undertake to update or revise any such forward-looking statements to reflect events or circumstances after the date of this report.

LIFEVANTAGE CORPORATION
INDEX

PART I Financial Information

Item 1. Financial Statements

LIFEVANTAGE CORPORATION AND SUBSIDIARIES

CONDENSED CONSOLIDATED BALANCE SHEETS

(Unaudited)

	As of, March 31, 2014	June 30, 2013
(In thousands, except per share data)		
ASSETS		
Current assets		
Cash and cash equivalents	$35,681	$26,299
Accounts receivable	2,606	1,789
Income tax receivable	1,511	2,150
Inventory	8,576	10,524
Current deferred income tax asset	2,885	2,885
Prepaid expenses and deposits	4,999	2,294
Total current assets	56,258	45,941
Property and equipment, net	7,183	5,692
Intangible assets, net	1,697	1,747
Deferred debt offering costs, net	1,413	—
Long-term deferred income tax asset	730	730
Other long-term assets	3,021	1,374
TOTAL ASSETS	$70,302	$55,484
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current liabilities		
Accounts payable	$2,641	$5,171
Commissions payable	9,595	7,564
Other accrued expenses	8,369	7,831
Short-term portion of debt	4,700	—
Total current liabilities	25,305	20,566
Long-term debt		
Principal amount	41,125	—
Less: unamortized discount	(1,098)	—
Long-term debt, net of unamortized discount	40,027	—
Other long-term liabilities	2,243	973
Total liabilities	67,575	21,539
Commitments and contingencies		
Stockholders' equity		
Preferred stock — par value $0.001 per share, 50,000 shares authorized, no shares issued or outstanding	—	—
Common stock — par value $0.001 per share, 250,000 shares authorized and 104,024 and 117,088 issued and outstanding as of March 31, 2014 and June 30, 2013, respectively	104	121
Additional paid-in capital	113,692	110,413
Accumulated deficit	(110,593)	(76,476)
Accumulated other comprehensive loss	(476)	(113)
Total stockholders' equity	2,727	33,945

TOTAL LIABILITIES AND STOCKHOLDERS’ EQUITY	$70,302	$55,484

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

LIFEVANTAGE CORPORATION AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS AND OTHER COMPREHENSIVE INCOME (LOSS)
(Unaudited)

	For the Three Months Ended March 31,		For the Nine Months Ended March 31,	
	2014	2013	2014	2013
(In thousands, except per share data)				
Sales, net	$55,064	$50,370	$157,930	$156,667
Cost of sales	8,459	7,330	24,212	23,936
Product recall costs	—	(461)	—	5,418
Gross profit	46,605	43,501	133,718	127,313
Operating expenses:				
Sales and marketing	32,483	29,844	92,510	88,976
General and administrative	8,470	8,370	23,432	23,227
Research and development	655	848	1,546	2,105
Depreciation and amortization	530	499	1,527	1,180
Total operating expenses	42,138	39,561	119,015	115,488
Operating income	4,467	3,940	14,703	11,825
Other income (expense), net:				
Interest and other income (expense), net	(1,278)	122	(1,605)	(426)
Total other income (expense)	(1,278)	122	(1,605)	(426)
Net income before income taxes	3,189	4,062	13,098	11,399
Income tax expense	(695)	(646)	(4,066)	(3,609)
Net income	$2,494	$3,416	$9,032	$7,790
Net income per share:				
Basic	$0.02	$0.03	$0.08	$0.07
Diluted	$0.02	$0.03	$0.08	$0.06
Weighted average shares outstanding:				
Basic	101,594	112,806	107,385	112,203
Diluted	106,578	124,985	113,717	125,371
Other comprehensive income (loss), net of tax:				
Foreign currency translation adjustment	103	(87)	(363)	(24)
Other comprehensive income (loss), net of tax:	$103	$(87)	$(363)	$(24)
Comprehensive income	$2,597	$3,329	$8,669	$7,766

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

LIFEVANTAGE CORPORATION AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENT OF STOCKHOLDERS' EQUITY
(Unaudited)

	Common stock		Additional paid-in capital	Accumulated deficit	Accumulated other comprehensive loss	Total
	Shares	Amount				
(In thousands)						
Balances, June 30, 2013	117,088	$121	$110,413	$(76,476)	$(113)	$33,945
Stock-based compensation	—	—	2,044	—	—	2,044
Exercise of options and warrants	4,654	4	1,235	—	—	1,239
Issuance of shares related to restricted stock	225	—	—	—	—	—
Shares canceled or surrendered as payment of tax withholding	(453)	—	—	—	—	—
Repurchase of company stock	(17,490)	(21)	—	(43,149)	—	(43,170)
Currency translation adjustment	—	—	—	—	(363)	(363)
Net income	—	—	—	9,032	—	9,032
Balances, March 31, 2014	104,024	$104	$113,692	$(110,593)	$(476)	$2,727

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

7

LIFEVANTAGE CORPORATION AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(Unaudited)

	For the Nine Months Ended March 31, 2014		2013	
(In thousands)				
Cash Flows from Operating Activities:				
Net income	$9,032		$7,790	
Adjustments to reconcile net income to net cash provided by operating activities:				
Depreciation and amortization	1,527		1,180	
Stock-based compensation	2,169		1,635	
Amortization of deferred financing fees	99		—	
Amortization of debt discount	76		—	
Impairment of inventory	—		4,155	
Changes in operating assets and liabilities:				
Increase in accounts receivable	(189	)	(1,048	)
Decrease/(increase) in inventory	1,858		(827	)
Increase in prepaid expenses and deposits	(2,719	)	(4,735	)
Increase in other long-term assets	(1,645	)	(1,077	)
Increase/(decrease) in accounts payable	(2,527	)	993	
Increase in accrued expenses	2,596		1,559	
Increase/(decrease) in other long-term liabilities	(100	)	442	
Net Cash Provided by Operating Activities	10,177		10,067	
Cash Flows from Investing Activities:				
Purchase of equipment	(1,671	)	(4,625	)
Net Cash Used in Investing Activities	(1,671	)	(4,625	)
Cash Flows from Financing Activities:				
Proceeds from term loan	45,825		—	
Payment of deferred financing fees	(1,511	)	—	
Repurchase of company stock	(43,170	)	(4,893	)
Payment on term loan	(1,175	)	—	
Exercise of options and warrants	1,239		2,066	
Net Cash Provided by (Used in) Financing Activities	1,208		(2,827	)
Foreign Currency Effect on Cash	(332	)	(24	)
Increase in Cash and Cash Equivalents:	9,382		2,591	
Cash and Cash Equivalents — beginning of period	26,299		24,648	
Cash and Cash Equivalents — end of period	$35,681		$27,239	
Non Cash Investing and Financing Activities:				
Increase in property and equipment/other long-term liabilities	$1,386		$376	
SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION				
Cash paid for interest expense	$1,821		$—	
Cash paid for income taxes	$3,461		$6,370	

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

8

LIFEVANTAGE CORPORATION AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)

These unaudited Condensed Consolidated Financial Statements and Notes should be read in conjunction with the audited financial statements and notes of LifeVantage Corporation (the “Company”) as of and for the year ended June 30, 2013 included in our Annual Report on Form 10-K filed with the Securities and Exchange Commission (“SEC”) on September 12, 2013.

Note 1 — Organization and Basis of Presentation

The condensed consolidated financial statements included herein have been prepared by the Company’s management, without audit, pursuant to the rules and regulations of the SEC. In the opinion of the Company’s management, these interim Financial Statements include all adjustments, consisting of normal recurring adjustments, that are considered necessary for a fair presentation of its financial position as of March 31, 2014, and the results of operations for the three and nine months ended March 31, 2014 and 2013 and the cash flows for the nine months ended March 31, 2014 and 2013. Interim results are not necessarily indicative of results for a full year or for any future period.

The condensed consolidated financial statements and notes included herein are presented as required by Form 10-Q, and do not contain certain information included in the Company’s audited financial statements and notes for the fiscal year ended June 30, 2013 pursuant to the rules and regulations of the SEC. For further information, refer to the financial statements and notes thereto as of and for the year ended June 30, 2013, and included in the Annual Report on Form 10-K on file with the SEC.

Note 2 — Summary of Significant Accounting Policies

Consolidation

The consolidated financial statements include the accounts of the Company and its wholly-owned subsidiaries. All significant intercompany accounts and transactions are eliminated in consolidation.

Use of Estimates

Management has made a number of estimates and assumptions relating to the reporting of revenues, expenses, assets and liabilities and the disclosure of contingent assets and liabilities to prepare these consolidated financial statements. Actual results could differ from those estimates.

Translation of Foreign Currency Statements

A portion of the Company’s business operations occurs outside the United States. The local currency of each of the Company’s subsidiaries is generally its functional currency. All assets and liabilities are translated into U.S. dollars at exchange rates existing at the balance sheet dates, revenue and expenses are translated at weighted average exchange rates and stockholders’ equity is recorded at historical exchange rates. The resulting foreign currency translation adjustments are recorded as a separate component of stockholders’ equity in the consolidated balance sheets and transaction gains and losses are included in interest and other income (expense), net in the consolidated financial statements.

Currency translation gains and losses on intercompany balances denominated in a foreign currency are recorded as other income (expense), net. A net foreign currency gain of $121,000 and a loss of $213,000 is recorded in other income (expense), net for the three and nine months ended March 31, 2014.

Derivative Instruments and Hedging Activities

The Company's subsidiaries enter into transactions with each other which may not be denominated in the respective subsidiaries' functional currencies. The Company seeks to reduce its exposure to fluctuations in foreign exchange rates through the use of derivatives. The Company does not use such derivative financial instruments for trading or speculative purposes.

To hedge risks associated with the foreign-currency-denominated intercompany transactions the Company entered into forward foreign exchange contracts which were settled in March 2014 and were not designated for hedge accounting. For the three and nine months ended March 31, 2014, a realized loss of $176,000 and a gain of $8,000, related to forward contracts, is recorded in other income (expense), net. The Company did not hold any derivative instruments at March 31, 2014.

9

Cash and Cash Equivalents

The Company considers only its monetary liquid assets with original maturities of three months or less as cash and cash equivalents.

Concentration of Credit Risk

The Company discloses significant concentrations of credit risk regardless of the degree of such risk. Financial instruments with significant credit risk include cash and investments. At March 31, 2014, the Company had $30.8 million in cash accounts that were held primarily at one financial institution and $4.8 million in accounts at other financial institutions. As of March 31, 2014 and June 30, 2013 the Company's cash balances exceeded federally insured limits.

Accounts Receivable

The Company's accounts receivable as of March 31, 2014 and June 30, 2013 consist primarily of credit card receivables. Based on the Company's verification process for customer credit cards and historical information available, management has determined that an allowance for doubtful accounts on credit card sales related to its customer sales as of March 31, 2014 is not necessary. No bad debt expense has been recorded for the periods ended March 31, 2014 and March 31, 2013.

Inventory

Inventory is stated at the lower of cost or market value. Cost is determined using the first-in, first-out method. The Company has capitalized payments to its contract product manufacturer for the acquisition of raw materials and commencement of the manufacturing, bottling and labeling of its product. As of March 31, 2014 and June 30, 2013, inventory consisted of (in thousands):

	March 31, 2014	June 30, 2013
Finished goods	$5,208	$5,273
Raw materials	3,368	5,251
Total inventory	$8,576	$10,524

Revenue Recognition

The Company ships the majority of its product directly to the consumer and receives substantially all payment for these sales in the form of credit card receipts. Revenue from direct product sales to customers is recognized upon passage of title and risk of loss. Estimated returns are recorded when product is shipped. The Company's return policy is to provide a full refund for product returned within 30 days if the returned product is unopened or defective. After 30 days, the Company generally does not issue refunds to direct sales customers for returned product. The Company allows terminating distributors to return unopened, unexpired product that they have purchased within the prior twelve months, subject to certain consumption limitations, for a full refund, less a 10% restocking fee. The Company establishes the returns reserve based on historical experience. The returns reserve is evaluated on a quarterly basis. As of March 31, 2014 and June 30, 2013, the Company's reserve balance for returns and allowances was approximately $0.6 million and $0.6 million, respectively.

Shipping and Handling

Shipping and handling costs associated with inbound freight and freight out to customers, including independent distributors, are included in cost of sales. Shipping and handling fees charged to all customers are included in sales.

Research and Development Costs

The Company expenses all costs related to research and development activities as incurred. Research and development expenses for the nine months ended March 31, 2014 and 2013 were approximately $1.5 million and $2.1 million, respectively.

Stock-Based Compensation

The Company recognizes stock-based compensation by measuring the cost of services to be rendered based on the grant date fair value of the equity award. The Company recognizes stock-based compensation, net of any estimated forfeitures, over the period an employee is required to provide service in exchange for the award, generally referred to as the requisite service period.

The Black-Scholes option pricing model is used to estimate the fair value of stock options. The determination of the fair value of stock options is affected by the Company's stock price and a number of assumptions, including expected volatility, expected life, risk-free interest rate and expected dividends. The Company uses historical volatility as the expected volatility assumption required in the Black-Scholes model. The Company utilizes a simplified method for estimating the expected life of the options. The Company uses this method because it believes that it provides a better estimate than the Company’s historical data as post vesting exercises have been limited. The risk-free interest rate assumption is based on observed interest rates appropriate for the expected terms of the stock options.

The fair value of restricted stock grants is based on the closing market price of the Company's stock on the date of grant less the Company's expected dividend yield. The fair value of performance-based awards to be paid in cash, accounted for as liabilities, is remeasured at the end of each reporting period and is based on the closing market price of the Company’s stock on the last day of the reporting period. The Company recognizes compensation costs for awards with performance conditions when it concludes it is probable that the performance conditions will be achieved. The Company reassesses the probability of vesting at each balance sheet date and adjusts compensation.

Income Taxes

Income taxes are accounted for under the asset and liability method. Deferred tax assets and liabilities are recognized for the future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases and operating loss and tax credit carry-forwards. Deferred tax assets and liabilities are measured using statutory tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. The effect on deferred tax assets and liabilities from a change in tax rates is recognized in income in the period that includes the effective date of the change.

For the nine months ended March 31, 2014 and 2013 the Company has recognized income tax expense of $4.1 million and $3.6 million, respectively, which is the Company’s estimated federal, state and foreign income tax liability. Realization of deferred tax assets is dependent upon future earnings in specific tax jurisdictions, the timing and amount of which are uncertain. The Company continues to evaluate the realizability of the deferred tax asset based upon achieved and estimated future results. The difference between the nine months ended March 31, 2014 effective rate of 31.0% and the Federal statutory rate of 35.0% is due to state income taxes (net of federal benefit) and certain permanent differences between taxable and book income as well as a one-time tax benefit from a tax return true-up recognized during the three months ended March 31, 2014.

Income Per Share

Basic income per common share is computed by dividing the net income or loss by the weighted average number of common shares outstanding during the period, less unvested restricted stock awards. Diluted income per common share is computed by dividing net income by the weighted average number of common shares and potentially dilutive common share equivalents using the treasury stock method.

For the three and nine months ended March 31, 2014 the effects of approximately 0.7 million and 0.2 million common shares, respectively, issuable upon exercise of options and non-vested shares of restricted stock granted pursuant to the Company’s 2007 and 2010 Long-Term Incentive Plans are not included in computations because their effect was anti-dilutive. For the three and nine months ended March 31, 2013 the effects of approximately 0.7 million common shares, respectively, issuable upon exercise of options granted pursuant to the Company’s 2007 and 2010 Long-Term Incentive Plans are not included in computations because their effect was anti-dilutive.

The following is a reconciliation of earnings per share and the weighted average common shares outstanding for purposes of computing basic and diluted net income per share (in thousands except per share amounts):

	Three Months Ended March 31,		Nine Months Ended March 31,	
	2014	2013	2014	2013
Numerator:				
Net income	$2,494	$3,416	$9,032	$7,790
Denominator:				
Basic weighted average common shares outstanding	101,594	112,806	107,385	112,203
Effect of dilutive securities:				
Stock awards and options	1,974	3,802	2,929	4,586
Warrants	3,010	8,377	3,403	8,582
Diluted weighted average common shares outstanding	106,578	124,985	113,717	125,371
Net income per share, basic	$0.02	$0.03	$0.08	$0.07
Net income per share, diluted	$0.02	$0.03	$0.08	$0.06

Segment Information

The Company operates in a single operating segment by selling products to a global network of independent distributors that operates in an integrated manner from market to market. Selling expenses are the Company's largest expense comprised of the commissions paid to its worldwide independent distributors. The Company manages its business primarily by managing its global network of independent distributors. The Company reports revenue in two geographic regions: Americas and Asia/Pacific. Revenues by geographic area are as follows (in thousands):

	Three Months Ended March 31,		Nine Months Ended March 31,	
	2014	2013	2014	2013
Americas	$32,641	$33,098	$101,557	$97,720
Asia/Pacific	22,423	17,272	56,373	58,947
Total revenues	$55,064	$50,370	$157,930	$156,667

Additional information as to the Company's revenue from operations in the most significant geographical areas is set forth below (in thousands):

	Three Months Ended March 31,		Nine Months Ended March 31,	
	2014	2013	2014	2013
United States	$31,619	$32,721	$98,415	$96,779
Japan	$19,202	$15,284	$48,122	$55,080

As of March 31, 2014 long-lived assets were $9.9 million in the U.S. and $2.5 million in Japan. As of June 30, 2013 long-lived assets were $4.8 million in the U.S. and $3.0 million in Japan.

Effect of New Accounting Pronouncements

The Company has reviewed recently issued, but not yet effective, accounting pronouncements and does not believe any such pronouncements will have a material impact on its financial statements.

Note 3 — Long-Term Debt

On October 18, 2013 the Company entered into a Financing Agreement providing for a term loan facility in an aggregate principal amount of $47 million (the "Term Loan") and a delayed draw term loan facility in an aggregate principal amount not to exceed $20 million (the "Delayed Draw Term Loan" and collectively with the Term Loan, the "Credit Facility"). The Delayed Draw Term Loan is available for borrowing in specified minimum amounts from time to time beginning after the effective date (as defined in the Financing Agreement) until October 18, 2014 or until the Delayed Draw Term Loan is reduced to zero, if earlier. As of March 31, 2014 the Company had not borrowed any amounts under the Delayed Draw Term Loan.

The principal amount of the Term Loan is payable in consecutive quarterly installments beginning with the calendar quarter ended March 31, 2014 and matures on the earlier of October 18, 2018 or such date as the outstanding loans become payable in accordance with the terms of the Financing Agreement (the "Final Maturity Date"). In the event the Company borrows under the Delayed Draw Term Loan, the outstanding principal will be payable in consecutive quarterly installments beginning with the calendar quarter ending December 31, 2014 through the Final Maturity Date. Each of the loans will bear interest at a rate equal to 7.5% per annum plus the greater of (i) 1.25% or (ii) LIBOR, or at the Company's option, a reference rate (as defined in the Financing Agreement) plus 6.5% per annum, with such interest payable monthly. For the nine months ended March 31, 2014 the interest rate was 8.75%.

The Company's obligations under the Credit Facility are secured by a security interest in substantially all of the Company's assets. Loans outstanding under the Credit Facility (1) must be prepaid based on certain cash flow metrics and with any net proceeds of certain permitted asset sales and (2) may be prepaid in whole or in part at any time, with any prepayments made prior to the first anniversary of the effective date subject to a prepayment premium. Any principal amount of the loans which is prepaid or repaid may not be re-borrowed.

The Credit Facility contains customary negative covenants that, among other things, restrict the Company from undertaking specified corporate actions such as, creation of liens, incurrence of additional indebtedness, making certain investments with affiliates, changes of control, having excess foreign cash, issuance of equity, repurchasing the Company's equity securities, and making certain restricted payments, including dividends, without prior approval from the lender. The Credit Facility also contains various financial covenants that require the Company to maintain a certain consolidated EBITDA, certain leverage and fixed charges ratios as well as a minimum level of liquidity. Additionally, the Credit Facility contains cross-default provisions, whereby a default pursuant to the terms and conditions of certain indebtedness will cause a default on the remaining indebtedness under the Credit Facility. At March 31, 2014, the Company was not in compliance with the non-financial covenant restricting it from having excess foreign cash. The Company's foreign cash balance exceeded the covenant limit of $5.5 million. On April 7, 2014 the Company obtained a waiver of the violation from the lender. The Company was in compliance with all other financial and non-financial covenants under the Credit Facility.

The Company incurred transaction costs associated with the Credit Facility totaling $2.7 million, of which $175,000 was recorded in interest expense during the nine months ended March 31, 2014. The remaining $2.5 million consists of unamortized deferred debt offering costs and debt discount included in the accompanying consolidated balance sheet and are amortized to interest expense using the interest method.

The Company's book value for the Credit Facility approximates the fair value. Aggregate future principal payments required in accordance with the terms of the Credit Facility are as follows (in thousands):

Year Ending June 30,	Amount
2014 (remaining three months ending June 30, 2014)	$1,175
2015	4,700
2016	4,700
2017	4,700
2018	4,700
Thereafter	25,850
	$45,825

Note 4 — Stockholders' Equity

During the three and nine months ended March 31, 2014 the Company issued 100,000 and 225,000 shares, respectively, of restricted stock and 0.4 million and 4.7 million shares, respectively, of common stock upon the exercise of warrants and options. During the three and nine months ended March 31, 2014, 351,000 and 453,000 shares, respectively, of restricted stock were canceled or surrendered as payment of tax withholding upon vesting.

On March 11, 2014 the Company announced a share repurchase program authorizing it to repurchase up to $3 million of shares of the Company's common stock. As part of that repurchase program, the Company entered into a pre-arranged stock repurchase plan that operated in accordance with guidelines specified under Rule 10b5-1 of the Securities Exchange Act of 1934. As of March 31, 2014, the Company had not purchased any shares under this repurchase program.

On November 1, 2013, the Company accepted for payment an aggregate of 16.3 million shares of its common stock at an aggregate purchase price of $40 million as a result of its modified Dutch auction tender offer (the "Tender Offer") that expired October 25, 2013. The Company incurred transaction costs of $0.3 million related to the Tender Offer. The Company entered into the Credit Facility to finance this repurchase, (see Note 3).

On March 22, 2013 the Company announced a share repurchase program authorizing it to repurchase up to $5 million of shares of the Company's common stock. As part of that repurchase program, the Company entered into a pre-arranged stock repurchase plan that operated in accordance with guidelines specified under Rule 10b5-1 of the Securities Exchange Act of 1934. During July 2013 the Company repurchased 1.2 million shares under this repurchase authorization. As of March 31, 2014, the Company had purchased the full $5 million in shares authorized under this repurchase program.

The Company’s Articles of Incorporation authorize the issuance of preferred shares. However, as of March 31, 2014, none have been issued nor have any rights or preferences been assigned to the preferred shares by the Company’s Board of Directors.

Note 5 — Share-based Compensation

Long-Term Incentive Plans

The Company adopted and the shareholders approved the 2007 Long-Term Incentive Plan (the “2007 Plan”), effective November 21, 2006, to provide incentives to certain eligible employees, directors and consultants. A maximum of 10.0 million shares of the Company's common stock can be issued under the 2007 Plan in connection with the grant of awards. Awards to purchase common stock have been granted pursuant to the 2007 Plan and are outstanding to various employees, officers, directors, Scientific Advisory Board members and independent distributors at prices between $0.21 and $1.50 per share, with initial vesting periods of one to three years. Awards expire in accordance with the terms of each award and the shares subject to the award are added back to the 2007 Plan upon expiration of the award. The contractual term of stock options granted is generally ten years. As of March 31, 2014 there were awards outstanding, net of awards expired, for the purchase in aggregate of 2.5 million shares of the Company's common stock.

The Company adopted and the shareholders approved the 2010 Long-Term Incentive Plan (the “2010 Plan”), effective September 27, 2010, as amended on January 10, 2012, to provide incentives to eligible employees, directors and consultants who contribute to the strategic and long-term performance objectives and growth of the Company. A maximum of 6.9 million shares of the Company’s common stock can be issued under the 2010 Plan in connection with the grant of awards. Awards to purchase common stock have been granted pursuant to the 2010 Plan and are outstanding to various employees, officers and directors. Outstanding stock options awarded under the 2010 Plan have exercise prices between $0.63 and $3.53 per share, and vest over one to four year vesting periods. Awards expire in accordance with the terms of each award and the shares subject to the award are added back to the 2010 Plan upon expiration of the award. The contractual term of stock options granted is generally ten years. As of March 31, 2014 there were awards outstanding, net of awards expired, for an aggregate of 3.3 million shares of the Company’s common stock.

The Company adopted a Performance Incentive Plan (the “Performance Plan”), effective July 1, 2013, to provide selected employees an opportunity to earn performance-based cash bonuses whose value is based upon the Company’s stock value and to encourage such employees to provide services to the Company and to attract new individuals with outstanding qualifications. The Performance Plan seeks to achieve this purpose by providing for awards in the form of performance share units (the “Units”). No shares will be issued under the Performance Plan. Awards may be settled only with cash and will be paid subsequent to award vesting. The fair value of share-based compensation awards, that include performance shares, are accounted for as liabilities. Vesting for the Units is subject to achievement of both service-based and performance-based vesting requirements. Performance-based vesting occurs in three installments if the Company meets certain performance criteria generally set for each year of a three-year performance period. The service-based vesting criteria occurs in three annual installments which are achieved at the end of a given fiscal year only if the participant has continuously remained in service from the date of award through the end of that fiscal year. The fair value of these awards is based on the trading price of our common stock and is remeasured at each reporting period date until settlement.

Stock-Based Compensation

In accordance with accounting guidance for stock-based compensation, payments in equity instruments for goods or services are accounted for under the fair value method. For the three and nine months ended March 31, 2014, stock-based compensation of $0.6 million and $2.0 million was reflected as an increase to additional paid in capital, all of which was employee related and $103,000 and $125,000 was reflected as an increase to other accrued expenses. For the three and nine months ended March 31, 2013, stock-based compensation of $0.6 million and $1.6 million, was reflected as an increase to additional paid in capital, all of which was employee related.

For the nine months ended March 31, 2014, no stock options were awarded. For the nine months ended March 31, 2013, the fair value of stock option awards was estimated using the Black-Scholes option-pricing model with the following assumptions and weighted average fair values:

	Nine Months Ended March 31,		
	2014	2013	
Risk-free interest rate	N/A	0.46% - 1.19%	
Dividend yield	N/A	—	%
Expected life in years	N/A	3.0 - 6.0	
Expected volatility	N/A	113% - 127%	

Note 6 — Contingencies

The Company is occasionally involved in lawsuits and disputes arising in the normal course of business. In the opinion of management, based upon advice of counsel, the likelihood of an adverse outcome in any litigation currently pending against the Company is remote. As such, management currently believes that the ultimate outcome of these lawsuits will not have a material impact on the Company's financial position or results of operations.

Item 2. Management’s Discussion and Analysis of Financial Condition and Results of Operations

Overview

We are a company dedicated to helping people achieve their health, wellness and financial independence goals. We provide quality, scientifically-validated products and a financially rewarding network marketing business opportunity to preferred customers and independent distributors who seek a healthy lifestyle and financial freedom. We sell our products in the United States, Japan, Hong Kong, Australia, Canada, Philippines, and Mexico primarily through a network of independent distributors, and to our preferred customers.

We engage in the identification, research, development and distribution of advanced nutraceutical dietary supplements and skin care products, including, Protandim®, our scientifically-validated dietary supplement, LifeVantage TrueScience® , our anti-aging skin care product, and Canine Health®, our companion pet supplement formulated to fight oxidative stress in dogs. We currently focus our internal research efforts on oxidative stress solutions, particularly the activation of Nuclear factor (erythroid-derived 2)-like 2, also known as Nrf2, as it relates to health-related disorders. We also evaluate healthy living products developed by third party research companies that we believe are scientifically-validated and compatible with our current product offerings.

Our Products

Our products are Protandim®, a full-line of LifeVantage TrueScience® skin care products and Canine Health®. Protandim® contains a proprietary blend of ingredients and has been shown to combat oxidative stress by increasing the body’s natural antioxidant protection at the genetic level, inducing the production of naturally-occurring protective antioxidant enzymes including superoxide dismutase, catalase, and glutathione synthase. Our full-line of LifeVantage TrueScience® skin care products was introduced in April 2014 and consists of TrueScience Ultra Gentle Facial Cleanser, TrueScience Perfecting Lotion, TrueScience Eye Corrector Serum, and an enhanced version of our LifeVantage TrueScience® anti-aging skin care lotion. Canine Health® is a supplement formulated to combat oxidative stress in dogs through Nrf2 activation.

We sell our Protandim®, LifeVantage TrueScience® and Canine Health® products through a direct selling model to independent distributors and to our preferred customers.

Customers

Because we utilize a direct selling model for the distribution of our products, the success and growth of our business is primarily based on our ability to attract new and retain existing independent distributors. Changes in our product sales are typically the result of variations in product sales volume relating to fluctuations in the number of active independent distributors and preferred customers purchasing our products. The number of active independent distributors and preferred customers is, therefore, used by management as a key non-financial measure.

15

The following tables summarize the changes in our active customer base by geographic region. These numbers have been rounded to the nearest thousand as of the dates indicated. For purposes of this report, we only count as active customers those independent distributors and preferred customers who have purchased from us at any time during the most recent three-month period, either for personal use or for resale.

	Active Independent Distributors By Region March 31,									
	2014			2013			Change from Prior Year		Percent Change	
Americas	43,000	58.9	%	38,000	60.3	%	5,000		13.2	%
Asia/Pacific	30,000	41.1	%	25,000	39.7	%	5,000		20.0	%
	73,000	100.0	%	63,000	100.0	%	10,000		15.9	%

	Active Preferred Customers By Region March 31,									
	2014			2013			Change from Prior Year		Percent Change	
Americas	106,000	79.1	%	115,000	82.1	%	(9,000	)	(7.8	)%
Asia/Pacific	28,000	20.9	%	25,000	17.9	%	3,000		12.0	%
	134,000	100.0	%	140,000	100.0	%	(6,000	)	(4.3	)%

Three and Nine months Ended March 31, 2014 Compared to Three and Nine months Ended March 31, 2013

Revenue. We generated net revenue of $55.1 million and $50.4 million during the three months ended March 31, 2014 and 2013, respectively. We generated net revenue of $157.9 million and $156.7 million during the nine months ended March 31, 2014 and 2013, respectively. Foreign currency fluctuations negatively impacted our revenue $2.3 million or 4.6% and $9.8 million or 6.2% during the three and nine months ended March 31, 2014, respectively.

Americas. The following table sets forth revenue for the three and nine months ended March 31, 2014 and 2013 for the Americas region (in thousands):

	Three Months Ended March 31,				Nine Months Ended March 31,			
	2014	2013	% Change		2014	2013	% Change	
United States	$31,619	$32,721	(3.37	)%	$98,415	$96,779	1.7	%
Other	1,022	377	171.09	%	3,142	941	233.9	%
Americas Total	$32,641	$33,098	(1.4	)%	$101,557	$97,720	3.9	%

Revenue in the Americas region for the three and nine months ended March 31, 2014 decreased $0.5 million or 1.4% and increased $3.8 million or 3.9% from the three and nine months ended March 31, 2013, respectively. The decrease in revenue during the three months ended March 31, 2014 is due to lower volume of product sales in the United States partially offset by increased volume in Canada as compared to the prior year same period. The increase in revenue during the nine months ended March 31, 2014 is due to higher volume of product sales in the United States as well as Canada as compared to the prior year same period.

Asia/Pacific. The following table sets forth revenue for the three and nine months ended March 31, 2014 and 2013 for the Asia/Pacific region and its principal markets (in thousands):

	Three Months Ended March 31,			Nine Months Ended March 31,		
	2014	2013	% Change	2014	2013	% Change
Japan	$19,202	$15,284	25.6 %	$48,122	$55,080	(12.6)%
Hong Kong	2,278	1,203	89.4 %	5,872	1,203	