

Lifevantage Corp
Form 10-Q
November 04, 2015

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

Form 10-Q

QUARTERLY REPORT UNDER SECTION 13 OR 15 (d) OF THE SECURITIES EXCHANGE ACT OF 1934
FOR THE QUARTERLY PERIOD ENDED SEPTEMBER 30, 2015

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 (IRS Employer
incorporation or organization) Identification No.)
9785 S. Monroe Street, Ste 300, Sandy, UT 84070
(Address of principal executive offices)
(801) 432-9000
(Registrant's telephone number)

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

Indicate by check mark 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 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
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

The number of shares outstanding of the issuer's common stock, par value \$0.001 per share, as of October 30, 2015 was 13,996,906.

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; statements regarding international growth; 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 similar 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:

- Inability to strengthen our business and properly manage distractions among our distributors in Japan;
- Inability to manage existing markets, open new international markets or expand our operations;
- Inability of new products to gain distributor or market acceptance;
- Our inability to execute our product launch process due to increased pressure on our supply chain, information systems and management;
- Disruptions in our information technology systems;
- Inability to comply with financial covenants imposed by our credit facility;
- Inability to protect against cyber security risks and to maintain the integrity of data;
- The impact of our debt service obligations and restrictive debt covenants;
- Claims against us as a result of our independent distributors failing to comply with applicable legal requirements or our policies and procedures;
- 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;
- Inability to raise additional capital if needed;
- Exposure to environmental liabilities stemming from past operations and property ownership;
- Significant dependence upon a few products for revenue;
- Inability to retain independent distributors or to attract new independent distributors on an ongoing basis;
- High quality material for our products may become difficult to obtain or expensive;
- Improper actions by our independent distributors that violate laws or regulations;
- Dependence on third parties to manufacture our products;
- Disruptions to the transportation channels used to distribute our products;

• We may be subject to a product recall;

• Government regulations on direct selling activities may prohibit or severely restrict our business model;

• Unfavorable publicity on our business or products;

• Our direct selling program could be found to not be in compliance with current or newly adopted laws or regulations;

• Legal proceedings may be expensive and time consuming;

• Strict government regulations on our business;

• Regulations governing the production or marketing of our products;

- 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;

• Inability to build and integrate our new management team could harm our business;

• Loss of, or inability to attract, key personnel;

• We could be held responsible for certain taxes or assessments relating to the activity of our independent distributors;

• 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;

• Volatility of the market price of our common stock;

• Substantial sales of shares may negatively impact the market price of our common stock;

• Significant dilution of outstanding voting shares if holders of our existing warrants and options exercise their securities for shares of 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 "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, 2015 and under "Risk Factors" in Part II, Item 1A of this Quarterly Report on Form 10-Q.

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

	PAGE
<u>PART I. Financial Information</u>	<u>5</u>
Item 1. <u>Financial Statements:</u>	<u>5</u>
<u>Condensed Consolidated Balance Sheets (unaudited)</u>	<u>5</u>
<u>Condensed Consolidated Statements of Operations and Comprehensive Income (unaudited)</u>	<u>6</u>
<u>Condensed Consolidated Statement of Stockholders' Equity (unaudited)</u>	<u>7</u>
<u>Condensed Consolidated Statements of Cash Flows (unaudited)</u>	<u>8</u>
<u>Notes to Condensed Consolidated Financial Statements (unaudited)</u>	<u>9</u>
Item 2. <u>Management's Discussion and Analysis of Financial Condition and Results of Operations</u>	<u>15</u>
Item 3. <u>Quantitative and Qualitative Disclosures About Market Risk</u>	<u>22</u>
Item 4. <u>Controls and Procedures</u>	<u>22</u>
 <u>PART II. Other Information</u>	 <u>23</u>
Item 1. <u>Legal Proceedings</u>	<u>23</u>
Item 1A. <u>Risk Factors</u>	<u>23</u>
Item 2. <u>Unregistered Sales of Equity Securities and Use of Proceeds</u>	<u>23</u>
Item 3. <u>Defaults Upon Senior Securities</u>	<u>23</u>
Item 4. <u>Mine Safety Disclosures</u>	<u>23</u>
Item 5. <u>Other Information</u>	<u>23</u>
Item 6. <u>Exhibits</u>	<u>23</u>
<u>Signatures</u>	<u>24</u>

PART I Financial Information

Item 1. Financial Statements

LIFEVANTAGE CORPORATION AND SUBSIDIARIES

CONDENSED CONSOLIDATED BALANCE SHEETS

(Unaudited)

	As of, September 30, 2015	June 30, 2015
(In thousands, except per share data)		
ASSETS		
Current assets		
Cash and cash equivalents	\$ 13,686	\$ 13,905
Accounts receivable	1,144	1,031
Income tax receivable	2,811	2,179
Inventory	8,538	9,248
Current deferred income tax asset	1,086	1,117
Prepaid expenses and deposits	3,596	2,995
Total current assets	30,861	30,475
Property and equipment, net	5,267	5,759
Intangible assets, net	1,845	1,879
Long-term deferred income tax asset	229	235
Other long-term assets	1,400	1,433
TOTAL ASSETS	\$39,602	\$39,781
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current liabilities		
Accounts payable	\$2,502	\$2,614
Commissions payable	6,450	6,505
Other accrued expenses	7,280	5,600
Current portion of long-term debt	11,723	11,141
Total current liabilities	27,955	25,860
Long-term debt		
Principal amount	6,786	10,484
Less: unamortized discount and deferred offering costs	(1,767)	(1,951)
Long-term debt, net of unamortized discount and deferred offering costs	5,019	8,533
Other long-term liabilities	2,051	2,063
Total liabilities	35,025	36,456
Commitments and contingencies - Note 6		
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 13,981 and 13,958 issued and outstanding as of September 30, 2015 and June 30, 2015, respectively	14	14
Additional paid-in capital	117,826	117,657
Accumulated deficit	(113,029)	(114,095)
Accumulated other comprehensive loss	(234)	(251)
Total stockholders' equity	4,577	3,325

Edgar Filing: Lifevantage Corp - Form 10-Q

TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY	\$39,602	\$39,781
--------------------------------------------	----------	----------

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

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

	For the Three Months Ended September 30,	
	2015	2014
(In thousands, except per share data)		
Revenue, net	\$45,352	\$51,633
Cost of sales	6,975	5,679
Gross profit	38,377	45,954
Operating expenses:		
Commissions and incentives	22,043	24,574
Selling, general and administrative	13,663	13,615
Total operating expenses	35,706	38,189
Operating income	2,671	7,765
Other income (expense):		
Interest expense	(749)	(808)
Other income (expense), net	(216)	203
Total other income (expense)	(965)	(605)
Income before income taxes	1,706	7,160
Income tax expense	(640)	(2,444)
Net income	\$1,066	\$4,716
Net income per share:		
Basic	\$0.08	\$0.33
Diluted	\$0.08	\$0.32
Weighted-average shares outstanding:		
Basic	13,709	14,228
Diluted	13,830	14,837
Other comprehensive income, net of tax:		
Foreign currency translation adjustment	17	57
Other comprehensive income, net of tax	17	57
Comprehensive income	\$1,083	\$4,773
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, 2015	13,958	\$14	\$117,657	\$(114,095)	\$(251)	\$3,325
Stock-based compensation	—	—	188	—	—	188
Exercise of options and warrants	—	—	(19)	—	—	(19)
Issuance of shares related to restricted stock	43	—	—	—	—	—
Shares canceled or surrendered as payment of tax withholding	(20)	—	—	—	—	—
Currency translation adjustment	—	—	—	—	17	17
Net income	—	—	—	1,066	—	1,066
Balances, September 30, 2015	13,981	\$14	\$117,826	\$(113,029)	\$(234)	\$4,577

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

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

	For the Three Months Ended September 30,		
	2015	2014	
(In thousands)			
Cash Flows from Operating Activities:			
Net income	\$1,066	\$4,716	
Adjustments to reconcile net income to net cash provided by operating activities:			
Depreciation and amortization	531	585	
Stock-based compensation	192	474	
Amortization of deferred financing fees	104	61	
Amortization of debt discount	81	48	
Deferred income tax	37	—	
Changes in operating assets and liabilities:			
Decrease / (increase) in receivables	(739) 1,469	
Decrease / (increase) in inventory	657	(2,379)
Increase in prepaid expenses and deposits	(606) (1,467)
Decrease in long-term assets	50	563	
Increase / (decrease) in accounts payable	(109) 1,392	
Increase / (decrease) in accrued expenses	1,304	(379)
Increase / (decrease) in other long-term liabilities	273	(21)
Net Cash Provided by Operating Activities	2,841	5,062	
Cash Flows from Investing Activities:			
Purchase of equipment	(3) (236)
Net Cash Used in Investing Activities	(3) (236)
Cash Flows from Financing Activities:			
Excess tax benefit from stock-based compensation	(19) —	
Repurchase of company stock	—	(2,000)
Payment on term loan	(3,116) (1,175)
Exercise of options and warrants	—	35	
Net Cash Used in Financing Activities	(3,135) (3,140)
Foreign Currency Effect on Cash	78	62	
(Decrease) Increase in Cash and Cash Equivalents:	(219) 1,748	
Cash and Cash Equivalents — beginning of period	13,905	20,387	
Cash and Cash Equivalents — end of period	\$13,686	\$22,135	
SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION			
Cash paid for interest	\$559	\$699	
Cash paid for income taxes	\$1,207	\$372	

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

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, 2015 included in our Annual Report on Form 10-K filed with the Securities and Exchange Commission (“SEC”) on September 1, 2015.

Note 1 — Organization and Basis of Presentation

LifeVantage Corporation is a company dedicated to helping people achieve their health, wellness and financial independence goals. We provide quality, scientifically-validated products and a financially rewarding direct sales business opportunity to customers and independent distributors who seek a healthy lifestyle and financial freedom. We sell our products to preferred customers, retail customers and independent distributors located in the United States, Japan, Hong Kong, Australia, Canada, Philippines, Mexico and Thailand.

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 line of anti-aging skin care products, Canine Health®, our companion pet supplement formulated to combat oxidative stress in dogs, and Axio®, our energy drink mixes.

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 September 30, 2015, and the results of operations for the three months ended September 30, 2015 and 2014 and the cash flows for the three months ended September 30, 2015 and 2014. Interim results are not necessarily indicative of results for a full year or for any future period. Certain amounts in the prior year financial statements have been reclassified for comparative purposes in order to conform with current year presentation.

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, 2015 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, 2015, 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

We prepare our consolidated financial statements and related disclosures in conformity with accounting principles generally accepted in the United States of America (GAAP). In preparing these statements, we are required to use 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 revenues and expenses during the reporting period. Actual results could differ materially from those estimates and assumptions. On an ongoing basis, we review our estimates, including those related to inventory obsolescence, sales returns, income taxes and tax valuation reserves, share-based compensation, and loss contingencies.

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 condensed consolidated balance sheets and as a component of comprehensive income. Transaction gains and losses and currency translation gains and losses

on intercompany balances denominated in a foreign currency are included in other income (expense), net in the condensed consolidated statements of

9

operations and comprehensive income. Net foreign currency losses of \$0.2 million and \$0.1 million are recorded in other income (expense), net for the three months ended September 30, 2015 and 2014, respectively.

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 September 2015 and were not designated for hedge accounting. For the three months ended September 30, 2015 and 2014, the Company realized a loss of \$9,000 and a gain of \$0.3 million, respectively, related to forward contracts which is recorded in other income (expense), net. The Company did not hold any derivative instruments at September 30, 2015.

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

Accounting guidance for financial instruments requires disclosure of significant concentrations of credit risk regardless of the degree of such risk. Financial instruments with significant credit risk include cash and investments. At September 30, 2015, the Company had \$11.2 million in cash accounts that were held primarily at one financial institution and \$2.5 million in accounts at other financial institutions. As of September 30, 2015 and June 30, 2015, and during the periods then ended, the Company's cash balances exceeded federally insured limits.

Accounts Receivable

The Company's accounts receivable as of September 30, 2015 and June 30, 2015 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 as of September 30, 2015 is not necessary. No bad debt expense has been recorded for the periods ended September 30, 2015 and September 30, 2014.

Inventory

As of September 30, 2015 and June 30, 2015, inventory consisted of (in thousands):

	September 30, 2015	June 30, 2015
Finished goods	\$4,283	\$5,783
Raw materials	4,255	3,465
Total inventory	\$8,538	\$9,248

Inventories are carried and depicted above at the lower of cost or net realizable value, using the first-in, first-out method, which includes a reduction in inventory values of \$0.2 million and \$0.3 million at September 30, 2015 and June 30, 2015, respectively, related to obsolete and slow-moving inventory.

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. Subject to some exceptions based on local regulations, 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 up to 30% of unopened, unexpired product that they have purchased within the prior twelve months 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 September 30, 2015 and June 30, 2015, the Company's reserve balance for returns and allowances was approximately \$0.1 million and \$0.1 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 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 three months ended September 30, 2015 and 2014 were approximately \$0.2 million and \$0.5 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. For awards with market based performance conditions, the cost of the awards is recognized as the requisite service is rendered by employees, regardless of when, if ever, the market based performance conditions are satisfied.

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 stock units that include market based performance conditions is based on the closing market price of the Company's stock on the date of grant less the Company's expected dividend yield, with further adjustments made to reflect the market conditions that must be satisfied in order for the units to vest by using a Monte-Carlo simulation model. Key assumptions for the Monte-Carlo simulation model include the risk-free rate, expected volatility, expected dividends and the correlation coefficient. The fair value of cash-settled performance based awards, 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 costs accordingly.

Reverse Stock Split

In October 2015, following approval of the Company's shareholders, the Company's board of directors approved the filing of an amendment to the Company's amended and restated articles of incorporation to effectuate a reverse split of the issued and outstanding shares of the Company's common stock on a one-for-seven basis. The reverse stock split was effective on October 19, 2015. The par value and authorized number of shares of common stock were not adjusted as a result of the reverse split. All fractional shares resulting from the reverse stock split were rounded up. All issued and outstanding common stock and per share amounts contained within the Company's consolidated financial statements and footnotes have been retroactively adjusted to reflect this reverse stock split for all periods presented.

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.

Edgar Filing: Lifevantage Corp - Form 10-Q

For the three months ended September 30, 2015 and 2014, the Company recognized income tax expense of \$0.6 million and \$2.4 million, respectively, which is reflective of the Company's current estimated federal, state and foreign effective tax rate. 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 three months ended September 30, 2015 effective rate of 37.5% and the Federal statutory rate of 35.0% is due primarily to the effect of state taxes and certain permanent differences.

Income Per Share

Basic income per common share is computed by dividing the net income 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 common shares and potentially dilutive common share equivalents using the treasury stock method.

For the three months ended September 30, 2015 the effects of approximately 0.5 million common shares 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 months ended September 30, 2014 the effects of approximately 0.3 million common shares issuable upon exercise of options granted pursuant to the Company's 2007 and 2010 Long-Term Incentive Plans were not included in computations because their effect was anti-dilutive.

The following is a reconciliation of net income 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):

	For the Three Months Ended September 30,	
	2015	2014
Numerator:		
Net income	\$ 1,066	\$ 4,716
Denominator:		
Basic weighted-average common shares outstanding	13,709	14,228
Effect of dilutive securities:		
Stock awards and options	59	228
Warrants	62	381
Diluted weighted-average common shares outstanding	13,830	14,837
Net income per share, basic	\$0.08	\$0.33
Net income per share, diluted	\$0.08	\$0.32

Segment Information

The Company operates in a single operating segment by selling products to an international network of independent distributors that operates in an integrated manner from market to market. Commissions and incentives 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 international network of independent distributors. The Company does not use profitability reports on a regional or divisional basis for making business decisions. However, the Company does report revenue in two geographic regions: Americas and Asia/Pacific. Revenues by geographic area are as follows (in thousands):

	For the Three Months Ended September 30,	
	2015	2014
Americas	\$34,726	\$36,456
Asia/Pacific	10,626	15,177
Total revenues	\$45,352	\$51,633

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

	For the Three Months Ended September 30,	
	2015	2014
United States	\$33,496	\$35,009
Japan	\$8,593	\$12,194

As of September 30, 2015 long-lived assets were \$6.1 million in the United States and \$1.4 million in Japan. As of June 30, 2015 long-lived assets were \$6.5 million in the United States and \$1.5 million in Japan.

Effect of New Accounting Pronouncements

In April 2015, FASB issued ASU No. 2015-03, Interest - Imputation of Interest (Subtopic 825-30): Simplifying the Presentation of Debt Issuance Costs. This guidance requires that debt issuance costs related to a recognized debt liability be presented in the balance sheet as a direct deduction from the carrying amount of that debt liability, consistent with debt discounts. The Company adopted this updated standard in the current year during the interim period ended September 30, 2015 by reclassifying the debt issue costs from long-term assets to a direct reduction from the related debt, consistent with the debt discount. All prior period balances have been retrospectively adjusted.

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 was 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. The Company did not borrow any amounts under the Delayed Draw Term Loan.

On May 1, 2015 the Company entered into an Amendment No. 1 to Financing Agreement ("Amendment No. 1"). Amendment No. 1 revised the March 31, 2015 and June 30, 2015 consolidated EBITDA covenants from \$20.6 million and \$21.3 million, respectively, to \$17.0 million for each quarter end. Amendment No. 1 also revised the minimum unrestricted cash and cash equivalents that the Company is required to hold from \$10.0 million to \$8.0 million for the reporting periods ended March 31, 2015 and June 30, 2015. In addition, Amendment No. 1 required that the Company make certain accelerated principal payments on the Term Loan totaling \$4.5 million during the fourth quarter of fiscal year 2015.

On August 27, 2015 the Company entered into an Amendment No. 2 to Financing Agreement ("Amendment No. 2" and collectively, with the Term Loan, as previously amended by Amendment No. 1, the "Credit Facility"). Amendment No. 2 revised the covenants related to minimum consolidated EBITDA (as defined in the amended Financing Agreement) for the four consecutive fiscal quarters ending September 30, 2015, December 31, 2015, March 31, 2016 and June 30, 2016 from \$22.2 million, \$23.1 million, \$24.4 million and \$25.6 million, respectively, to \$14.5 million, \$15.0 million, \$17.0 million and \$17.5 million, respectively. In addition, Amendment No. 2 requires that the Company make additional monthly accelerated principal payments on the Term Loan in the amount of \$0.5 million commencing on October 15, 2015 and continuing until the Term Loan has been paid in full. Amendment No. 2 also requires that the Company make additional accelerated payments at the end of each fiscal quarter in the amount of all unrestricted cash on hand as of the close of business on the last day for the quarter in excess of \$12.5 million. 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"). The Term loan bears 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 three months ended September 30, 2015 the average 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 the 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. As of September 30, 2015, the Company was in compliance with all applicable covenants including those under the amended Credit Facility.

During the three months ended September 30, 2015, the Company recorded interest expense of \$0.2 million related to transaction costs associated with the 2013 Credit Facility. At September 30, 2015, the Company had unamortized transaction costs totaling \$1.8 million included in the consolidated balance sheet. The remaining balance will be 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
2015 (remaining nine months ending June 30, 2016)	\$9,048
2016	9,461
	\$18,509

Note 4 — Stockholders' Equity

During the three months ended September 30, 2015 the Company issued 43,000 shares of restricted stock and no shares of common stock upon the exercise of warrants and options. During the three months ended September 30, 2015, 20,000 shares of restricted stock were canceled or surrendered as payment of tax withholding upon vesting. The Company's Articles of Incorporation authorize the issuance of preferred shares. However, as of September 30, 2015, 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 — Stock-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 1.4 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 \$1.47 and \$10.50 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 September 30, 2015 there were awards outstanding, net of awards expired, for the purchase in aggregate of 0.3 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 August 21, 2014, 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 1.5 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 \$4.41 and \$24.71 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 September 30, 2015 there were awards outstanding, net of awards expired, for an aggregate of 0.1 million shares of the Company's common stock.

The Company adopted a Performance Incentive Plan effective July 1, 2013 (the "Fiscal 2014 Performance Plan"). The Fiscal 2014 Performance Plan is intended 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 Fiscal 2014 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 Fiscal 2014 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. The Company adopted a separate Performance Incentive Plan effective July 1, 2014 (the "Fiscal 2015 Performance Plan"). The Fiscal 2015 Performance Plan is substantially similar to the Fiscal 2014 Performance Plan except that the service-based vesting criteria occurs in a single installment and is achieved at the end of the third fiscal year after the award is granted if the participant has continuously remained in service from the date of the award through the end of the third fiscal year.

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 months ended September 30, 2015, stock-based compensation of \$0.2 million was reflected as an increase to additional paid-in capital and an increase of \$4,000 was included in other accrued expenses, all of which was employee related. For the three months ended September 30, 2014, stock-based compensation of \$0.4 million was reflected as an increase to additional paid-in capital, all of which was employee related.

Note 6 — Commitments and Contingencies

From time to time, the Company is involved in lawsuits and disputes arising in the normal course of business. The Company regularly reviews all pending litigation matters in which it is involved and establishes accruals deemed appropriate by management for these litigation matters when a probable loss estimate can be made. In the opinion of management, the amounts accrued for as of September 30, 2015 are appropriate based on the probable outcome of currently pending matters.

Note 7 — Subsequent Events

On October 19, 2015 the Company effected a 1 for 7 reverse stock split as approved by the Company's shareholders and Board of Directors. All issued and outstanding common stock and per share amounts contained within the Company's consolidated financial statements and footnotes have been retroactively adjusted to reflect this reverse stock split for all periods presented.

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 sell quality, scientifically validated products and provide a financially rewarding direct sales business opportunity to preferred customers, retail customers and independent distributors who seek a healthy lifestyle and financial freedom. We engage in the identification, research, development and distribution of advanced nutraceutical dietary supplements and skin care products. We sell our products to preferred customers and independent distributors in two geographic regions: Americas and Asia/Pacific.

Our revenue depends on the number and productivity of our independent distributors and the number of our retail and preferred customers. When we are successful in attracting and retaining independent distributors and preferred customers, it is largely because of:

- Our scientifically-validated products, including Protandim®, LifeVantage TrueScience®, Canine Health® and Axio®;
- Our compensation plan and other sales initiatives; and
- Our delivery of superior customer service.

As a result, it is vital to our success that we leverage our product development resources to develop and introduce innovative products and provide opportunities for our independent distributors to sell these products in a variety of markets.

We have begun selling our products and attracting new independent distributors and preferred customers in several new markets since the beginning of our direct selling activities in 2009, including Japan, Australia, Canada, Mexico, Hong Kong, Thailand and, on a limited basis, the Philippines. Entering a new market requires a considerable amount of time, resources and continued support. If we are unable to properly support an existing or new market, our revenue growth will be negatively impacted.

Our Products

Our products are Protandim®, the LifeVantage TrueScience® skin care regimen, Canine Health®, and Axio®.

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 LifeVantage TrueScience® skin care regimen includes TrueScience® Ultra Gentle Facial Cleanser, TrueScience® Perfecting Lotion, TrueScience® Eye Corrector Serum, and our

enhanced TrueScience® Anti-Aging Cream. Axio® is our energy drink mix formulated to promote alertness and support mental performance. Canine Health® is a supplement specially formulated to combat oxidative stress in dogs through Nrf2 activation.

We currently have additional products in development. Any delays or difficulties in introducing compelling products or attractive initiatives or tools into our markets may have a negative impact on our revenue and our ability to attract new preferred customers and independent distributors.

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 the effectiveness of our independent distributors in selling our products and 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.

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 Preferred Customers By Region September 30,

	2015		2014		Change from Prior Year		Percent Change	
Americas	93,000	81.6 %	104,000	82.5 %	(11,000)		(10.6)	%
Asia/Pacific	21,000	18.4 %	22,000	17.5 %	(1,000)		(4.5)	%
	114,000	100.0 %	126,000	100.0 %	(12,000)		(9.5)	%

Active Independent Distributors By Region September 30,

	2015		2014		Change from Prior Year		Percent Change	
Americas	44,000	68.7 %	44,000	64.7 %	—		—	%
Asia/Pacific	20,000	31.3 %	24,000	35.3 %	(4,000)		(16.7)	%
	64,000	100.0 %	68,000	100.0 %	(4,000)		(5.9)	%

Three months Ended September 30, 2015 Compared to the Three months Ended September 30, 2014

Revenue. We generated net revenue of \$45.4 million and \$51.6 million during the three months ended September 30, 2015 and 2014, respectively. Foreign currency fluctuations negatively impacted our revenue in the amount of \$1.9 million or 3.7% during the three months ended September 30, 2015.

Americas. The following table sets forth revenue for the three months ended September 30, 2015 and 2014 for the Americas region (in thousands):

	For the Three Months Ended September 30,		
	2015	2014	% Change
United States	\$33,496	\$35,009	(4.3) %
Other	1,230	1,447	(15.0) %
Americas Total	\$34,726	\$36,456	(4.7) %

Revenue in the Americas region for the three months ended September 30, 2015 decreased \$1.7 million or 4.7% from the prior year same period. The decrease in revenue is due to lower volume of product sales in the United States and Canada, partially offset by an increase in Mexico sales as compared to the prior year same periods.

Asia/Pacific. The following table sets forth revenue for the three months ended September 30, 2015 and 2014 for the Asia/Pacific region and its principal markets (in thousands):

	For the Three Months Ended September 30,		
	2015	2014	% Change
Japan	\$8,593	\$12,194	(29.5)%
Hong Kong	1,179	1,624	(27.4)%
Other	854	1,359	(37.2)%
Asia/Pacific Total	\$10,626	\$15,177	(30.0)%

Revenue in the Asia/Pacific region for the three months ended September 30, 2015 was negatively impacted approximately \$1.7 million or 10.9% by foreign currency exchange rate fluctuations.

During the three months ended September 30, 2015 the Japanese yen continued to weaken against the U.S. dollar, negatively impacting our revenue in this market by \$1.5 million or 12.5%. In addition to the negative impact of foreign currency fluctuations, product sales volume decreased in Japan, Hong Kong, Australia and the Philippines. All of our sales and marketing efforts continue to be directed toward building our network marketing sales. We expect increased revenue in the Americas region as we continue to focus on our growth initiatives, specifically product development and sales and marketing. We expect revenue in Australia, Hong Kong, and the Philippines to remain consistent with the revenue generated in those countries for the three months ended September 30, 2015 as we continue to provide similar levels of support as previous periods.

We continue to face significant challenges in our Japan market, with our biggest challenge being the contraction in revenue. We believe that continued attempts by former distributors, including two previous lead distributors, who terminated their distributorships in June 2014 after being suspended for ongoing violations of our policies and procedures, to recruit our distributors to another network marketing company has continued to be a distraction in that market.

While there continues to be uncertainty regarding the full impact these distractions will have on future revenue, we have taken actions to mitigate the impact and we continue to monitor the progress of these actions. During fiscal year 2015 we commenced, and during fiscal year 2016 we are continuing to take, legal action against the company to which some of our former distributor leaders have moved, but anticipate that will take time to complete. In addition, we are working to unify our Japan distributor base, starting with our distributor leaders in the market. During fiscal year 2015 we restructured our Japan field advisory board, with the intended effect to streamline the partnership process and focus leaders on positive in-country distributor activities. In addition to promoting greater leadership and unity in the market, we continue to be focused on creating country-specific marketing tools and materials that we believe will be of significant benefit to our distributors as they build their businesses. We expect Japan revenue to stabilize beginning in the second fiscal quarter of 2016.

Gross Margin. Our gross profit percentage for the three months ended September 30, 2015 and 2014 was 84.6% and 89.0%, respectively.

As a percentage of total revenues, cost of sales for the three months ended September 30, 2015 increased to 15.4% from 11.0% for the three months ended September 30, 2014. The increase in cost of sales for the three months ended September 30, 2015, as compared to the prior year period, is due primarily to benefits associated with the rework of previously recalled inventory as well as cost recoveries from insurance of approximately \$2.0 million that were recognized in the prior year, reducing cost of sales in that period.

Operating Expenses. Total operating expenses during the three months ended September 30, 2015 were \$35.7 million as compared to operating expenses of \$38.2 million during the three months ended September 30, 2014. Operating expenses consist of commissions and incentives expenses and selling, general and administrative expenses.

Operating expenses as a percentage of revenue increased to 78.7% for the three months ended September 30, 2015 from 74.0% for the three months ended September 30, 2014. The increase is due primarily to a higher rate of decline

in revenue relative to the rate of decline in selling, general administrative expenses during the three months ended September 30, 2015 as compared to the prior year period.

Commissions and Incentives. Commissions and incentives expenses during the three months ended September 30, 2015 were \$22.0 million as compared to commissions and incentives expenses of \$24.6 million for the three months ended September 30, 2014.

The decrease in commissions and incentives expenses for the three months ended September 30, 2015 was due primarily to decreased commission expenses related to the lower revenues realized during the quarter as compared to the prior year period.

We expect our commissions and incentives expenses to increase slightly during the remainder of fiscal 2016, as compared to the same period in fiscal 2015, as we continue to focus our efforts on increasing revenue through growth and retention of our distributors and preferred customers, both domestically and internationally.

Selling, General and Administrative. Selling, general and administrative expenses during the three months ended September 30, 2015 were \$13.7 million as compared to selling, general and administrative expenses of \$13.6 million for the three months ended September 30, 2014.

The increase in selling, general and administrative expenses during the three months ended September 30, 2015, compared to the prior year same period, was due primarily to increases in other general and administrative expenses. These increases were partially offset by decreases in sales and marketing expenses.

Other general and administrative expenses increased primarily as a result of increased expenses associated with executive severance and recruiting expenses incurred during the three months ended September 30, 2015 related to the separation and subsequent hiring of our Chief Financial Officer and Chief Sales Officer positions.

Sales and marketing expenses for the three months ended September 30, 2015 were lower primarily as a result of fewer events being held in anticipation of our 2015 convention and Japan elite academy which will take place during our second quarter of fiscal year 2016.

We expect our sales and marketing expenses to remain consistent as we remain focused on investing in our strategic initiatives of new product innovation, investing in and strengthening our sales and marketing efforts, and strengthening and expanding our geographic reach.

Total Other Income (Expense). During the three months ended September 30, 2015 we recognized net other expenses of \$1.0 million as compared to net other expenses of \$0.6 million for the three months ended September 30, 2014.

Total other income (expense) for the three months ended September 30, 2015 consisted primarily of interest expense and net currency losses.

The following table sets forth interest expense for the three months ended September 30, 2015 and 2014 (in thousands):

	For the Three Months Ended September 30,	
	2015	2014
Contractual interest expense:		
2013 Term Loan	\$559	\$699
Amortization of deferred financing fees:		
2013 Term Loan	104	61
Amortization of debt discount:		
2013 Term Loan	81	48
Other	5	—
Total interest expense	\$749	\$808

Income Tax Expense. We recognized income tax expense of \$0.6 million for the three months ended September 30, 2015 as compared to income tax expense of \$2.4 million for the three months ended September 30, 2014.

The effective tax rate was 37.5% of pre-tax income during the three months ended September 30, 2015, compared to 34.1% for the same prior year period. The increase in the effective tax rate for the three months ended September 30, 2015 consisted primarily of the effect of current year permanent differences.

Liquidity and Capital Resources

Liquidity

Our primary liquidity and capital resource requirements are to service our debt and finance the cost of our planned operating expenses and working capital (principally inventory purchases), as well as capital expenditures. We have generally relied on cash flow from operations to fund operating activities and we have, at times, incurred long-term debt in order to fund stock repurchases and strategic transactions.

As of September 30, 2015, our available liquidity was \$13.7 million, including available cash and cash equivalents. This represented a decrease of \$0.2 million from the \$13.9 million in cash and cash equivalents as of June 30, 2015. During the three months ended September 30, 2015, our net cash provided by operating activities was \$2.8 million as compared to net cash provided by operating activities of \$5.1 million during the three months ended September 30, 2014.

During the three months ended September 30, 2015, our net cash used in investing activities was \$3,000, as a result of the purchase of fixed assets. During the three months ended September 30, 2014, our net cash used in investing activities was \$0.2 million, as a result of the purchase of fixed assets.

Cash used in financing activities during the three months ended September 30, 2015 was \$3.1 million compared to cash used in financing activities of \$3.1 million during the three months ended September 30, 2014. Cash used in financing activities during the three months ended September 30, 2015 was comprised of \$3.1 million in principal payments on the Term Loan entered into in October 2013. Cash used in financing activities during the three months ended September 30, 2014 was comprised primarily of \$1.2 million in principal payments on the Term Loan and \$2.0 million for the repurchase of shares of our common stock.

At September 30, 2015 and June 30, 2015, the total amount of our foreign subsidiary cash was \$4.2 million and \$5.2 million, respectively. For earnings considered to be indefinitely reinvested, we have not accrued taxes. If we were to remit the cash and cash equivalents from our foreign subsidiaries to our U.S. consolidated group for the purpose of repatriation of undistributed earnings, we would need to accrue and pay taxes. As of September 30, 2015, our U.S. consolidated group had approximately \$0.1 million of permanently reinvested unremitted earnings from our subsidiaries, and if these earnings were remitted, the impact of any tax consequences on our overall liquidity position would not be material. We do not have any plans to repatriate these unremitted earnings to our parent; therefore, we do not have any liquidity concerns relating to these unremitted earnings and related cash and cash equivalents.

At September 30, 2015, we had working capital (current assets minus current liabilities) of \$2.9 million, compared to working capital of \$4.6 million at June 30, 2015. We believe that our cash and cash equivalents balances and our ongoing cash flow from operations will be sufficient to satisfy our cash requirements for at least the next 12 months. The majority of our historical expenses have been variable in nature and as such, a potential reduction in the level of revenue would reduce our cash flow needs. In the event that our current cash balances and future cash flow from operations are not sufficient to meet our obligations or strategic needs, we would consider raising additional funds, which may not be available on terms that are acceptable to us, or at all. Our credit facility, however, contains covenants that restrict our ability to raise additional funds in the debt or equity markets and repurchase our equity securities without prior approval from the lender. Additionally, we would consider realigning our strategic plans including a reduction in capital spending and expenses.

Capital Resources

On October 18, 2013, we 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"). The Delayed Draw Term Loan was 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 was reduced to zero, if earlier. We did not borrow any amounts under the Delayed Draw Term Loan.

On May 1, 2015 we entered into an Amendment No. 1 to Financing Agreement ("Amendment No. 1"). Amendment No. 1 revised the covenants relating to minimum consolidated EBITDA (as defined in the Financing Agreement) for the four consecutive fiscal quarters ending March 31, 2015 and June 30, 2015 from \$20.6 million and \$21.3 million, respectively, to \$17.0 million for each quarter end. Amendment No. 1 also revised the minimum unrestricted cash and

cash equivalents that we are required to hold from \$10.0 million to \$8.0 million for the reporting periods ended March 31, 2015 and June 30, 2015. In addition, Amendment No. 1 required that we make certain accelerated principal payments on the Term Loan totaling \$4.5 million during our fourth quarter of fiscal year 2015.

On August 27, 2015 we entered into an Amendment No. 2 to Financing Agreement ("Amendment No. 2" and collectively with the Term Loan, as previously amended by Amendment No. 1, the "Credit Facility"). Amendment No. 2 revised the covenants related to minimum consolidated EBITDA (as defined in the amended Financing Agreement) for the four consecutive fiscal quarters ending September 30, 2015, December 31, 2015, March 31, 2016 and June 30, 2016 from \$22.2 million, \$23.1 million, \$24.4 million and \$25.6 million, respectively, to \$14.5 million, \$15.0 million, \$17.0 million and \$17.5 million, respectively. In addition, Amendment No. 2 requires that we make additional monthly accelerated principal payments on the Term Loan in the amount of \$0.5 million commencing on October 15, 2015 and continuing until the Term Loan has been paid in full. Amendment No. 2 also requires that we make additional accelerated payments at the end of each calendar quarter in the amount of all unrestricted cash on hand as of the close of business on the last day of the quarter in excess of \$12.5 million.

The Credit Facility contains customary negative covenants that, among other things, restrict us from undertaking specified corporate actions such as the creation of liens, incurrence of additional indebtedness, making certain investments with affiliates, changes of control, having excess foreign cash, issuance of equity, repurchasing our equity securities, and making certain restricted payments, including dividends, without prior approval from the lender. As of September 30, 2015, we were in compliance with the applicable non-financial and restrictive covenants under the Credit Facility. Additionally, management anticipates that in the normal course of operations, we will be in compliance with the non-financial and restrictive covenants during the ensuing year.

The Credit Facility also contains various financial covenants that require us to maintain a certain consolidated EBITDA, certain leverage and fixed charges ratios as well as a minimum level of liquidity. Specifically, after giving effect to Amendment No. 2, we must:

- Have a consolidated EBITDA (as defined in the Financing Agreement) of at least \$14.5 million for the four consecutive fiscal quarters ending September 30, 2015. Our consolidated EBITDA requirement increases over time to \$25.6 million for the four consecutive fiscal quarters ending September 30, 2016 and each period of four consecutive fiscal quarters ending each December 31, March 31, June 30, and September 30 thereafter;

- Have a total leverage ratio (as defined in the Credit Facility) of less than 1.50 to 1.00 for the quarter ended September 30, 2015. Our leverage ratio requirement decreases over time to 1.25 to 1.00 for the quarter ended June 30, 2016, and remains level thereafter;

- Have a fixed charge ratio (as defined in the Credit Facility) of greater than 1.25 to 1.00 for the four consecutive fiscal quarters ending September 30, 2015; and

- For the fiscal quarter ending September 30, 2015 have no less than \$7.0 million in unrestricted cash and cash equivalents at any time when the total leverage ratio is greater than 1.25 to 1.00, and for all fiscal quarters ending subsequent to September 30, 2015 have no less than \$8.0 million in unrestricted cash and cash equivalents at any time when the total leverage ratio is greater than 1.25 to 1.00.

As of September 30, 2015 the Company was in compliance with all applicable financial covenants including those under the amended Credit Facility. We anticipate that in the absence of a significant increase to our consolidated EBITDA we likely will not meet our consolidated EBITDA covenants for the reporting periods subsequent to June 30, 2016. We intend to work with our lender to further revise our financial covenants under the Credit Facility as needed. While we expect to be successful in negotiating with our lender to revise the consolidated EBITDA covenant to a level that will be achievable in light of our current business, it is possible that these negotiations will be unsuccessful.

Off-Balance Sheet Arrangements

As of September 30, 2015, we did not have any off-balance sheet arrangements.

Critical Accounting Policies

We prepare our financial statements in conformity with accounting principles generally accepted in the United States of America. As such, we are required to make certain estimates, judgments, and assumptions that we believe are reasonable based upon the information available. These estimates and assumptions affect the reported amounts of assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the periods presented. Actual results could differ from these estimates. Our significant accounting policies are described in Note 2 to our financial statements. Certain of these significant accounting policies require us to make difficult, subjective, or complex judgments or estimates. We consider an accounting estimate to be critical if (1) the

accounting estimate requires us to make assumptions about matters that were highly uncertain at the time the accounting estimate was made, and (2) changes in the estimate that are reasonably likely

to occur from period to period, or use of different estimates that we reasonably could have used in the current period, would have a material impact on our financial condition or results of operations.

There are other items within our financial statements that require estimation, but are not deemed critical as defined above. Changes in estimates used in these and other items could have a material impact on our financial statements. Management has discussed the development and selection of these critical accounting estimates with our board of directors, and the audit committee has reviewed the disclosures noted below.

Allowances for Product Returns

We record allowances for product returns at the time we ship the product based on estimated return rates. Subject to some exceptions based on local regulations, customers may return unopened product to us within 30 days of purchase for a refund of the purchase price less shipping and handling. As of September 30, 2015, our shipment of products sold totaling \$14.4 million were subject to the return policy. In addition, we allow terminating distributors to return up to 30% of unopened, unexpired product they purchased within the prior 12 months.

We monitor our return estimate on an ongoing basis and may revise the allowances to reflect our experience. Our allowance for product returns was \$0.1 million at September 30, 2015, compared with \$0.1 million at June 30, 2015. To date, product expiration dates have not played any role in product returns, and we do not expect that they will in the future as it is unlikely that we will ship product with an expiration date earlier than the latest allowable product return date.

Inventory Valuation

We value our inventory at the lower of cost or net realizable value on a first-in first-out basis. Accordingly, we reduce our inventories for the diminution of value resulting from product obsolescence, damage or other issues affecting marketability equal to the difference between the cost of the inventory and its estimated net realizable value. Factors utilized in the determination of estimated net realizable value include (i) current sales data and historical return rates, (ii) estimates of future demand, (iii) competitive pricing pressures, (iv) new production introductions, (v) product expiration dates, and (vi) component and packaging obsolescence. We have recorded \$4,000 of obsolescence costs for the three months ended September 30, 2015.

Revenue Recognition

We ship the majority of our product directly to the consumer and receive 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.

Stock-Based Compensation

We use the fair value approach to account for stock-based compensation in accordance with current accounting guidance. We recognize compensation costs for awards with performance conditions when we conclude it is probable that the performance conditions will be achieved. We reassess the probability of vesting at each balance sheet date and adjust compensation costs based on our probability assessment. For awards with market based performance conditions, the cost of the awards is recognized as the requisite service is rendered by employees, regardless of when, if ever, the market based performance conditions are satisfied.

Research and Development Costs

We expense all of our payments related to research and development activities as incurred.

Commitments and Obligations

The following table summarizes our contractual payment obligations and commitments as of September 30, 2015 (in thousands):

Contractual Obligations	Total	Payments due by period			
		Less than 1 year	1-3 years	3-5 years	Thereafter
Long-term debt obligations	\$18,509	\$11,723	\$6,786	\$—	\$—
Interest on long-term debt obligations	1,427	1,172	255	—	—
Operating lease obligations	13,257	2,449	4,732	4,037	2,039
Total	\$33,193	\$15,344	\$11,773	\$4,037	\$2,039

Recently Issued Accounting Standards

See Note 2 to our unaudited condensed consolidated financial statements for a discussion of recently issued accounting standards.

Item 3. Quantitative and Qualitative Disclosures About Market Risk

We conduct business in several countries and intend to continue to grow our international operations. Net revenue, operating income and net income are affected by fluctuations in currency exchange rates and other uncertainties in doing business and selling products in more than one currency. In addition, our operations are exposed to risks associated with changes in social, political and economic conditions inherent in international operations, including changes in the laws and policies that govern international investment in countries where we have operations, as well as, to a lesser extent, changes in U.S. laws and regulations relating to international trade and investment.

Foreign Currency Risk

During the three months ended September 30, 2015, approximately 26.1% of our net revenue was realized outside of the United States. The local currency of each international subsidiary is generally the functional currency. All revenues and expenses are translated at weighted-average exchange rates for the periods reported. Therefore, our reported revenue and earnings will be positively impacted by a weakening of the U.S. dollar and will be negatively impacted by a strengthening of the U.S. dollar. Currency fluctuations, however, have the opposite effect on our expenses incurred outside the United States. Given the large portion of our business derived from Japan, any weakening of the Japanese Yen will negatively impact our reported revenue and profits, whereas a strengthening of the Japanese Yen will positively impact our reported revenue and profits. Because of the uncertainty of exchange rate fluctuations, it is difficult to predict the effect of these fluctuations on our future business, product pricing and results of operations or financial condition. Changes in various currency exchange rates affect the relative prices at which we sell our products. We regularly monitor our foreign currency risks and periodically take measures to reduce the risk of foreign exchange rate fluctuations on our operating results. Additionally, we may seek to reduce our exposure to fluctuations in foreign currency exchange rates through the use of foreign currency exchange contracts. We do not use derivative financial instruments for trading or speculative purposes. At September 30, 2015 we did not have any derivative instruments. A 10% strengthening of the U.S. Dollar compared to all of the foreign currencies in which we transact business would have resulted in a 2.4% decrease of our three months ended September 30, 2015 revenue, in the amount of \$1.1 million.

Interest Rate Risks

As of September 30, 2015, we had \$18.5 million in variable rate debt issued pursuant to the Financing Agreement we entered into in October 2013. Based on the amount of our variable debt as of September 30, 2015, a hypothetical 100 basis point increase or decrease in interest rates on our variable rate debt would increase or decrease our annual interest expense by approximately \$0.1 million. This market risk exposure was driven by our borrowings in connection with our repurchase of shares of our common stock under the November 2013 Dutch auction tender offer in which we accepted for payment an aggregate of 16.3 million shares of our common stock at an aggregate purchase price of \$40.0 million.

Item 4. Controls and Procedures

Disclosure Controls and Procedures

We maintain disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) of the Exchange Act) that are designed to ensure that the information required to be disclosed in the reports we file or submit under the Exchange Act is (a) recorded, processed, summarized and reported within the time periods specified in the rules and forms of the SEC and (b) accumulated and communicated to management, including our Chief Executive Officer (“CEO”) and Chief Financial Officer (“CFO”), as appropriate, to allow timely decisions regarding required disclosure. As of the end of the period covered by this Quarterly Report on Form 10-Q, we carried out an evaluation, under the supervision and with the participation of our management, including our CEO and CFO, of the effectiveness and design and operation of such disclosure controls and procedures, as defined in Rules 13a-15(e) and 15d-15(e) under the Exchange Act. Based on this evaluation, our CEO and CFO concluded that our disclosure controls and procedures were effective as of September 30, 2015.

Changes in Internal Control Over Financial Reporting

An evaluation required by paragraph (d) of Rules 13a-15 and 15d-15 of the Exchange Act was also performed under the supervision and with the participation of our management, including our CEO and CFO, of any change in our internal control over financial reporting that occurred during our last fiscal quarter. That evaluation did not identify any changes in our internal control over financial reporting during the three months ended September 30, 2015 that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

PART II Other Information

Item 1. Legal Proceedings

None.

Item 1A. Risk Factors

The following description of risk factors includes any material changes to, and, if applicable, supersedes the description of, risk factors associated with our business previously disclosed in "Part I. Item 1A — Risk Factors" in our Annual Report on Form 10-K for the fiscal year ended June 30, 2015, and should be read in conjunction with the detailed discussion of risks associated with our business in our recent SEC filings, including the risk factors discussed in "Part I. Item 1A — Risk Factors" in our Annual Report on Form 10-K for the fiscal year ended June 30, 2015.

We may not be able to comply with the financial covenants set forth in the Financing Agreement.

The Financing Agreement we entered into in October 2013 contains financial covenants that require us to maintain specified financial ratios and satisfy certain financial condition tests. For example, the Financing Agreement originally required us to have a minimum consolidated EBITDA for the four consecutive fiscal quarters ended March 31, 2015 of at least \$20.6 million. We were not in compliance with this financial covenant at March 31, 2015 and we entered into Amendment No. 1 to Financing Agreement on May 1, 2015 (the "Amendment") to remedy our noncompliance and to establish a lower EBITDA covenant for the four consecutive fiscal quarters ending March 31, 2015 and June 30, 2015. The Amendment, however, did not revise the required minimum consolidated EBITDA for periods subsequent to June 30, 2015.

On August 27, 2015 we entered into an Amendment No. 2 to Financing Agreement ("Amendment No. 2").

Amendment No. 2 revised the covenants related to minimum consolidated EBITDA (as defined in the amended Financing Agreement) for the four consecutive fiscal quarters ending September 30, 2015, December 31, 2015, March 31, 2016 and June 30, 2016 from \$22.2 million, \$23.1 million, \$24.4 million and \$25.6 million, respectively, to \$14.5 million, \$15.0 million, \$17.0 million and \$17.5 million, respectively. In addition, Amendment No. 2 requires that we make additional monthly accelerated principal payments on our outstanding term loan in the amount of \$0.5 million commencing on October 15, 2015 and continuing until the term loan has been paid in full. Amendment No. 2 also requires that we make additional accelerated payments at the end of each calendar quarter in the amount of all unrestricted cash on hand as of the close of business on the last day of the quarter in excess of \$12.5 million. If we are unable to further amend the Financing Agreement or significantly increase our revenue and manage our expenses, our consolidated EBITDA may not exceed the minimum consolidated EBITDA required by the Financing Agreement and, as a result, an event of default would exist under the Financing Agreement for which our lender could accelerate our repayment of the indebtedness.

Item 2. Unregistered Sales of Equity Securities and Use of Proceeds

There were no shares of our common stock issued during the three months ended September 30, 2015 due to the exercise of warrants.

We did not purchase any shares of our common stock during the quarter ended September 30, 2015.

During the quarter ended September 30, 2015, we withheld 922 shares to satisfy tax withholding obligations in connection with the partial vesting of restricted stock awards.

Item 3. Defaults Upon Senior Securities

None.

Item 4. Mine Safety Disclosures

Not applicable.

Item 5. Other Information

None.

Item 6. Exhibits

See the exhibit index immediately following the signature page of this report.

SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the Registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

LIFEVANTAGE CORPORATION

Date: November 4, 2015

/s/ Darren Jensen
Darren Jensen
Chief Executive Officer
(Principal Executive Officer)

Date: November 4, 2015

/s/ Mark Jaggi
Mark Jaggi
Chief Financial Officer
(Principal Financial Officer)

Edgar Filing: Lifevantage Corp - Form 10-Q

Exhibit Index

Exhibit No.	Document Description	Filed Herewith or Incorporate by Reference From
3.1(a)	Amended and Restated Articles of Incorporation and Statement of Correction to Amended and Restated Articles of Incorporation	Exhibit to 4.1 to Registration Statement on Form S-8 (File No. 333-200363) filed on November 19, 2014
3.1(b)	Articles of Amendment to the Amended and Restated Articles of Incorporation	Filed herewith
31.1	Certification of principal executive officer pursuant to Rule 13a-14(a)/15d-14(a)	Filed herewith
31.2	Certification of principal financial officer pursuant to Rule 13a-14(a)/15d-14(a)	Filed herewith
32.1*	Certification of principal executive officer pursuant to 18 U.S.C. 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002	Filed herewith
32.2*	Certification of principal financial officer pursuant to 18 U.S.C. 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002	Filed herewith

101	The following financial information from the Company's Quarterly Report on Form 10-Q for the quarter ended September 30, 2015 formatted in XBRL (extensible Business Reporting Language): (i) Unaudited Condensed Consolidated Balance Sheets at September 30, 2015 and June 30, 2015; (ii) Unaudited Condensed Consolidated Statements of Operations and Other Comprehensive Income for the three months ended September 30, 2015 and 2014; (iii) Unaudited Condensed Consolidated Statement of Stockholders' Deficit for the three months ended September 30, 2015; (iv) Unaudited Condensed Consolidated Statements of Cash Flows for the three months ended September 30, 2015 and 2014; and (v) Notes to Unaudited Condensed Consolidated Financial Statements, tagged as blocks of text	Filed herewith
-----	-----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------	----------------

* This certification is being furnished solely to accompany this report pursuant to 18 U.S.C. 1350, and is not being filed for purposes of Section 18 of the Exchange Act and is not to be incorporated by reference into any filing of the registrant, whether made before or after the date hereof, regardless of any general incorporation language in such filing