

NATURES SUNSHINE PRODUCTS INC
Form 10-K
October 07, 2008
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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-K

x Annual report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934 for the fiscal year ended December 31, 2007

OR

o Transition report under Section 13 or 15(d) of the Securities Exchange Act of 1934 for the transition period from to .

Commission file number 0-8707

NATURE S SUNSHINE PRODUCTS, INC.

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(Exact name of Registrant as specified in its charter)

Utah
(State or other jurisdiction of
incorporation or organization)

87-0327982
(IRS Employer
Identification No.)

75 East 1700 South
Provo, Utah 84606

(Address of principal executive offices and zip code)

(801) 342-4300

(Registrant's telephone number, including area code)

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

None

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

Common Stock, no par value.

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes No .

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act. Yes No .

Indicate by check mark whether the registrant has (1) 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 if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K.

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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 Act). Yes No .

The aggregate market value of the voting stock held by non-affiliates of the registrant on June 30, 2008 was approximately \$82,797,216 based on the closing price of \$6.75 as quoted by the National Quotation Bureau's Pink Sheets on June 30, 2008

The number of shares of Common Stock, no par value, outstanding on June 30, 2008 is 15,510,159 shares.

Documents Incorporated by Reference: For items incorporated by reference, see List of Exhibits in Item 15 of this Form 10-K.

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CAUTIONARY NOTE REGARDING FORWARD-LOOKING STATEMENTS

Certain information included or incorporated by reference in this report may be deemed to be forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995. Forward-looking statements may include, but are not limited to, statements relating to our objectives, plans and strategies. All statements (other than statements of historical fact) that address activities, events or developments that we intend, expect, project, believe or anticipate will or may occur in the future are forward-looking statements. These statements are often characterized by terminology such as believe, hope, may, anticipate, should, intend, plan, will, expect, estimate, project, similar expressions, and are based on assumptions and assessments made by management in light of their experience and their perception of historical trends, current conditions, expected future developments and other factors they believe to be appropriate. Forward-looking statements are not guarantees of future performance and are subject to risks and uncertainties. Important factors that could cause actual results, developments and business decisions to differ materially from forward-looking statements are described in this report, including the risks set forth under Risk Factors in Item 1A.

Throughout this report, we refer to Nature's Sunshine Products, Inc., together with its subsidiaries, as we, us, our Company or the Company.

EXPLANATORY NOTE

Internal Investigation

As previously announced, in October 2005, the Audit Committee of our Board of Directors (our Audit Committee) commenced an internal investigation regarding certain sales and commission activities involving certain of our foreign operations. The investigation was subsequently expanded to include other matters related to our consolidated financial statements. The Audit Committee engaged a nationally-recognized independent law firm to assist in the investigation and the law firm, in turn, engaged a nationally-recognized independent public accounting firm to provide further assistance. The internal investigation was overseen by a Special Committee comprised of one independent member of the Audit Committee and an outside independent consultant, who later became a director and independent member of the Audit Committee. On March 15, 2006, the Audit Committee received an oral preliminary report on the findings of the investigation through that date (the Preliminary Report). Based on issues raised in the Preliminary Report, on March 15, 2006, the Audit Committee determined that the financial statements filed with the SEC in connection with the following previously issued reports of the Company should not be relied upon:

- (i) Quarterly Reports on Form 10-Q for each of the first three fiscal quarters of 2005;
- (ii) Annual Report on Form 10-K for the fiscal year ended December 31, 2004 (which includes financial statements as of December 31, 2004 and 2003 and for the fiscal years ended December 31, 2004, 2003 and 2002); and
- (iii) Quarterly Reports on Form 10-Q for each of the first three fiscal quarters of 2004, 2003 and 2002.

Change in Certifying Accountant

As previously announced, on March 31, 2006, we received a letter from KPMG LLP (KPMG) pursuant to which KPMG resigned as our independent registered public accounting firm. Following KPMG 's resignation, we began the process of obtaining a new independent registered public accounting firm. On February 2, 2007, our Audit Committee engaged Deloitte & Touche LLP (Deloitte) to serve as our independent registered public accounting firm.

Failure to Report and Delisting

Due primarily to the dedication of a substantial amount of our resources to the review and assessment of information we received in the course of the internal investigation described above, we have been unable to prepare and file periodic reports for periods ending on or after December 31, 2005 as required by the Exchange Act. As a result of

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our inability to file such reports, on April 5, 2006, the Nasdaq Listing Qualifications Panel determined to delist our common stock from The Nasdaq National Market.

Since April 2006, our common stock has been listed on the Pink Sheets. We intend to seek to be re-listed on a securities exchange when we become current in our financial reporting. There can be no assurance regarding our ability to satisfy the standards for listing on an exchange or that an exchange will approve our listing. Nor can there be any assurance at this time when the re-listing would occur. Continuing to be quoted only on Pink Sheets could adversely affect the trading market and potentially the market price of our common stock.

Preceding the filing of this report, we filed the Annual Report on Form 10-K for the fiscal year ended December 31, 2006. We are currently preparing and expect to file the following reports with the SEC subsequent to the filing of this Report: Quarterly Reports on Form 10-Q for the quarterly periods ended March 31, and June 30, 2008.

Legal Proceedings

On July 12, 2007, we announced that the SEC had instituted an administrative proceeding pursuant to Section 12(j) of the Securities Exchange Act of 1934, as amended (the Exchange Act), to suspend or revoke the registration of our common stock under Section 12 of the Exchange Act. On November 8, 2007, an administrative law judge in an administrative proceeding issued an Initial Decision to revoke the registration of our common stock because of our failure to file required periodic reports. Shortly thereafter, we filed a petition for review with the SEC. On December 5, 2007, the SEC granted our petition for review. The SEC had scheduled oral argument regarding the Company's petition on October 1, 2008. The SEC has now rescheduled the oral argument for an unspecified future date. We cannot predict the outcome of such review at this time. The Initial Decision of the administrative law judge will not become effective prior to the completion of the SEC's review. We cannot predict what, if any, impact the SEC's ultimate determination may have on our financial statements or the materiality of such impact, if any. If a final order is issued by the SEC revoking the registration of our common stock, broker-dealers would not be permitted to effect transactions in shares of our common stock until we file a new registration with the SEC under the Exchange Act and that registration is made effective.

Given the significant delay in the filing of our annual report on Form 10-K for 2007, certain amounts and discussions, as indicated, have been updated to include relevant 2008 and current information as far as practicable to do so.

Restatement of Previously Issued Financial Statements

On October 6, 2008, the Company restated its previously filed consolidated financial statements for the year ended December 31, 2004 and its previously reported December 31, 2003 consolidated common stock, treasury stock, retained earnings, and accumulated other comprehensive loss to recognize corrected items that relate to periods prior to January 1, 2004. The restatement of our 2004 financial statements reflect changes resulting from errors identified from Management's comprehensive review of its accounting policies, practices, and financial records, including matters identified by the independent investigation, as discussed above. The Company used all available information in determining the impact of adjustments identified as a result of Management's review. The restatement is discussed

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in greater detail in the Company's Annual Report on Form 10-K for the year ended December 31, 2006, filed on October 6, 2008.

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PART 1

Item 1. Business

The Company

Nature's Sunshine Products, Inc., founded in 1972 and incorporated in Utah in 1976, together with our subsidiaries, is primarily engaged in the manufacturing and marketing of nutritional and personal care products. We sell our products worldwide to a sales force of independent Distributors who use the products themselves or resell them to other Distributors or consumers.

Our operations are conducted in the United States as well as in various other countries. Our subsidiaries are located in Mexico, Central America, Canada, Venezuela, Dominican Republic, Japan, Ecuador, the United Kingdom, Colombia, Peru, Israel, Russia, Ukraine, Latvia, Lithuania, Kazakhstan, Mongolia, Belarus, China, Poland and Brazil. We export our products to several other countries, including Argentina, Australia, Chile, New Zealand and Norway.

We also sell our products through a separate division, Synergy Worldwide. Synergy Worldwide sells products in the United States, Japan, South Korea, Singapore, Thailand, Taiwan, Malaysia, Hong Kong, Philippines, Indonesia, the United Kingdom, Germany, Austria, the Netherlands and Australia.

Our principal executive office is located at 75 East 1700 South, Provo, Utah 84606. Our telephone number is (801) 342-4300 and our Internet website address is <http://www.natr.com>. We make available free of charge on our website our Annual Reports on Form 10-K, our Quarterly Reports on Form 10-Q, our Current Reports on Form 8-K, and amendments to those reports, filed or furnished pursuant to Section 13(a) of the Securities Exchange Act of 1934 as soon as practicable after we electronically file these documents with, or furnish them to, the Securities and Exchange Commission (the "SEC").

Financial Information by Business Segment

We are principally engaged in one line of business; namely, manufacturing and marketing nutritional and personal care products. We conduct our business through three operating business segments. Two of the operating business segments operate under the *Nature's Sunshine Products* name and are based on geographic operations: a United States segment ("NSP United States") and an international segment ("NSP International"). Our third operating business segment is *Synergy Worldwide*, a division that was acquired in 2000. Synergy Worldwide offers products with formulations different from those of the Nature's Sunshine Products offerings. In addition, Synergy Worldwide's marketing and Distributor compensation plans are sufficiently different from those of Nature's Sunshine Products. Information by business segment for each of our last three fiscal years for sales revenue and operating income, and information by business segment as of the end of our last two fiscal years for identifiable assets, are set forth in Note 14 of the Notes to Consolidated Financial Statements set forth in Item 8 of this Report.

Products and Manufacturing

Our line of over 700 products includes herbal products, vitamins and mineral supplements, personal care, nutritional drinks, and miscellaneous other products. We purchase herbs and other raw materials in bulk and, after quality control testing, formulate, encapsulate, tablet or concentrate, and package them for shipment. Most of our products are manufactured at our facility in Spanish Fork, Utah. Contract manufacturers produce some of our personal care and other miscellaneous products for us in accordance with our specifications and standards. We have implemented stringent quality control procedures to verify that the contract manufacturers have complied with our specifications and standards. Our product lines are described below.

Herbal Products

We manufacture a wide selection of herbal products, which are sold in the form of capsules or tablets. These capsules or tablets contain herb powder or a combination of two or more herb powders. We also produce both single

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herbs and herb combinations in the form of liquid herbs and extracts. Liquid herbs are manufactured by concentrating herb constituents in a vegetable glycerin base. Extracts are created by dissolving powdered herbs into liquid solvents that separate the key elements of the herbs from the fibrous plant material. For the years ended December 31, 2007, 2006, and 2005, herbal products accounted for approximately 52.9, 54.0, and 53.7 percent of net sales revenue, respectively.

Vitamins and Mineral Supplements

We manufacture a wide variety of single vitamins, which are sold in the form of chewable or non-chewable tablets. We also manufacture several multiple vitamins and mineral supplements, including a line containing natural antioxidants. Generally, mineral supplements are sold in the form of tablets; however, certain minerals are offered only in liquid form. For the years ended December 31, 2007, 2006, and 2005, vitamin and mineral supplements accounted for approximately 41.6, 40.3, and 40.5 percent of net sales revenue, respectively.

Personal Care Products

We manufacture or contract with independent manufacturers to supply a variety of personal care products for external use, including oils and lotions, aloe vera gel, herbal shampoo, herbal skin treatment, toothpaste, and skin cleanser. For the years ended December 31, 2007, 2006, and 2005, personal care products accounted for approximately 2.3, 2.4, and 2.5 percent of net sales revenue, respectively.

Other Products

We manufacture or contract with independent manufacturers to supply a variety of other products, including a variety of nutritional drinks, homeopathic products, and powders. For the years ended December 31, 2007, 2006, and 2005, other products accounted for approximately 3.2, 3.3, and 3.3 percent of net sales revenue, respectively.

Distribution and Marketing

Our independent Distributors (as hereinafter defined) market our products to consumers through direct-selling techniques, as well as sponsor other Distributors. We seek to motivate and provide incentives to our independent Distributors by offering high quality products and providing our Distributors with product support, training seminars, sales conventions, travel programs, and financial benefits.

Our products sold in the United States are shipped directly from our manufacturing and warehouse facilities located in Spanish Fork, Utah, as well as from our regional warehouses located in Columbus, Ohio; Dallas, Texas; and Atlanta, Georgia. Each international operation maintains warehouse facilities with inventory to supply its customers.

Demand for our products is created primarily from our independent Distributors. As of June 30, 2008, we had approximately 718,500 active Distributors worldwide, which included approximately 227,000 Distributors in the United States. A person who joins our independent sales force begins as a Distributor. An individual can become a Distributor by signing up under the sponsorship of someone who is already a Distributor. Each Distributor is required to renew his/her distributorship on a yearly basis; our experience indicates that approximately 45 percent of our Distributors renew annually. Many Distributors sell our products on a part-time basis to friends or associates or use the products themselves. A Distributor interested in earning additional income by committing more time and effort to selling our products may earn Manager status. Manager status is contingent upon attaining certain purchase volume levels, recruiting additional Distributors, and demonstrating leadership abilities. We had approximately 26,800 Managers worldwide as of June 30, 2008, including approximately 7,600 Managers in the United States. Managers resell our products to Distributors within their sales group, sell our products directly to consumers, or use the products themselves. Historically, approximately 60 percent of Distributors appointed as Managers have continued to maintain that status annually.

In the United States, we generally sell our products on a cash or credit card basis. From time to time, our United States operation extends short-term credit associated with product promotions. For certain of our international operations, we use independent distribution centers and offer credit terms which are generally consistent with industry standards within each respective country.

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We pay sales commissions (Volume Incentives) to our Managers and Distributors based upon the amount of sales group product purchases. Generally, a portion of these Volume Incentives are paid to the applicable Manager as a rebate for product purchases made by the Manager and the Manager's down-line Distributors. The remaining portion of these Volume Incentives is paid in the form of commissions for purchases made by the Manager's down-line Distributors. The amounts of Volume Incentives that we paid during the years ended December 31, 2007, 2006, and 2005 are set forth in our Consolidated Financial Statements in Item 8 of this report. In addition to the opportunity to receive Volume Incentives, Managers who qualify by attaining certain levels of monthly product purchases are eligible for additional incentive programs including automobile allowances, sales convention privileges, and travel.

Source and Availability of Raw Materials

Raw materials used in the manufacture of our products are generally available from a number of suppliers. To date, we have not experienced any major difficulty in obtaining adequate sources of supply. We attempt to ensure the availability of many of our raw materials by contracting, in advance, for our annual requirements. In the past, we have found alternative sources of raw materials when needed. Although there can be no assurance we will be successful in locating such sources in the future, we believe we will be able to do so.

Trademarks and Trade Names

We have obtained trademark registrations of our basic trademark, Nature's Sunshine, and the landscape logo for all of our Nature's Sunshine product lines. We have also obtained trademark registrations for Synergy for all of our Synergy product lines. We hold trademark registrations in the United States and in many other countries. Our customers' recognition and association of our brands and trademarks with quality is an important element of our operating strategy.

Seasonality

Our business does not reflect significant seasonality.

Inventories

In order to provide a high level of product availability to our independent Distributors and Managers, we maintain a considerable inventory of raw materials in the United States and of finished goods in every country in which we sell our products. Due to different regulatory requirements across the countries in which we sell our products, our finished goods inventories reflect product labels and sometimes product formulations specific for each country. Our inventories are subject to obsolescence due to finite shelf lives.

Dependence Upon Customers

We are not dependent upon a single customer or a few customers, the loss of which we believe would have a material adverse effect on our business.

Backlog

We typically ship orders for our products within 24 hours after receipt. As a result, we have not historically experienced significant backlogs.

Competition

Our products are sold in competition with other companies, some of which have greater sales volumes and financial resources than we do, and which sell brands that are, through advertising and promotions, better known to consumers. We compete in the nutritional and personal care industry against companies which sell through retail stores as well as against other direct selling companies. For example, we compete against manufacturers and retailers of nutritional and personal care products, which are distributed through supermarkets, drug stores, health food stores, discount stores, etc. In addition to competition with these manufacturers and retailers, we compete for product sales and independent Distributors with many other direct sales companies, including Herbalife, Pharmanex (NuSkin), USANA, Shaklee,

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Mannatech and Amway. The principal competitors in the retail encapsulated and tableted herbal products market include Nature's Way, NOW, Rexall Sundown, and Nutraceuticals. We believe that the principal components of competition in the direct sales marketing of nutritional and personal care products are quality, price, and brand recognition. In addition, the recruitment, training, travel, and financial incentives for the independent sales force are important factors.

Research and Development

We conduct research and development activities at our manufacturing facility located in Spanish Fork, Utah. Our principal emphasis in our research and development activities is the development of new products and the enhancement of existing products. The amount, excluding capital expenditures, spent on research and development activities was approximately \$1.9 million in 2007 and 2006, and \$1.8 million in 2005, respectively. During the three years in the period ended December 31, 2007, we did not contract for any third-party research and development.

Compliance with Environmental Laws and Regulations

The nature of our business has not required any material capital expenditures to comply with federal, state, or local provisions enacted or adopted regulating the discharge of materials into the environment. No material expenditures to meet such provisions are anticipated. Such regulatory provisions have not had any material effect upon our results of operations or competitive position.

Regulation

The formulation, manufacturing, packaging, labeling, advertising, distribution and sale of each of our major product groups are subject to regulation by one or more governmental agencies. The most active of these is the Food and Drug Administration (FDA), which regulates our products under the Federal Food, Drug and Cosmetic Act (FDCA) and regulations promulgated thereunder. The FDCA defines the terms "food" and "dietary supplement" and sets forth various conditions that unless complied with may constitute adulteration or misbranding of such products. The FDCA has been amended several times with respect to dietary supplements, most recently by the Nutrition Labeling and Education Act of 1990 (the NLEA) and the Dietary Supplement Health and Education Act of 1994 (the DSHEA).

FDA regulations relating specifically to foods and dietary supplements for human use are set forth in Title 21 of the Code of Federal Regulations. These regulations include basic labeling requirements for both foods and dietary supplements. Additionally, Good Manufacturing Practices (GMPs) exist for both foods and dietary supplements. The GMPs for dietary supplements became effective August 27, 2007 with a phase-in compliance date of June 2008 for companies with more than 500 employees.

Our products are also regulated by the Federal Trade Commission (FTC), the Consumer Product Safety Commission (CPSC), the United States Department of Agriculture (USDA), and the Environmental Protection Agency (EPA). Our activities, including our multi-level distribution activities, are also regulated by various agencies of the states, localities, and foreign countries in which our products are sold.

Employees

The number of individuals we employed as of June 30, 2008 was 1,177. We believe that our relations with our employees are satisfactory.

International Operations

A significant portion of our net sales are concentrated within the United States, which represents 41.7 percent of net sales in 2007. Outside of the United States, Japan continues to be our largest market, representing 12.4 percent of net sales during 2007. As we continue to expand internationally, our operating results will likely become more sensitive to economic and political conditions in foreign markets, as well as to foreign currency fluctuations.

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Year Ended December 31,	2007		2006		2005	
Sales Revenue:						
United States	\$	152,943	41.7%	\$	157,132	43.4%
Foreign						
Japan		45,554	12.4		52,301	14.4
Russia		34,314	9.4		28,394	7.8
Other		133,836	36.5		124,395	34.4
Total Foreign		213,704	58.3		114,382	32.5