

MANNATECH INC  
Form 10-Q  
November 04, 2010

September 2010

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

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FORM 10-Q  
(Mark One)

QUARTERLY REPORT PURSUANT TO SECTION 13 OR  
15(d) OF THE SECURITIES EXCHANGE ACT OF 1934  
For the quarterly period ended: September 30, 2010

OR

TRANSITION REPORT PURSUANT TO SECTION 13 OR  
15(d) OF THE SECURITIES EXCHANGE ACT OF 1934  
For the transition period from \_\_\_\_\_ to \_\_\_\_\_.

Commission File No. 000-24657

MANNATECH, INCORPORATED  
(Exact Name of Registrant as Specified in its Charter)

Texas	75-2508900
(State or other Jurisdiction of Incorporation or Organization)	(I.R.S. Employer Identification No.)
600 S. Royal Lane, Suite 200, Coppell, Texas	75019
(Address of Principal Executive Offices)	(Zip Code)

Registrant's Telephone Number, including Area Code: (972) 471-7400

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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

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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 definitions of “accelerated filer”, “large accelerated filer” and “smaller reporting company” in Rule 12b-2 of the Exchange Act.

Large accelerated filer       Accelerated filer       Non-accelerated filer       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

As of November 1, 2010, the number of shares outstanding of the registrant’s sole class of common stock, par value \$0.0001 per share, was 26,490,466.

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Special Note Regarding Forward-Looking Statements

Certain disclosures and analysis in this Form 10-Q, including information incorporated by reference, may include forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended, or the Securities Act, Section 21E of the Securities Exchange Act of 1934, as amended, or the Exchange Act, and the Private Securities Litigation Reform Act of 1995 that are subject to various risks and uncertainties. Opinions, forecasts, projections, guidance, or other statements other than statements of historical fact are considered forward-looking statements and reflect only current views about future events and financial performance. Some of these forward-looking statements include statements regarding:

- § management's plans and objectives for future operations;
- § existing cash flows being adequate to fund future operational needs;
- § future plans related to budgets, future capital requirements, market share growth, and anticipated capital projects and obligations;
- § the realization of net deferred tax assets;
- § the ability to curtail operating expenditures;
- § global statutory tax rates remaining unchanged;
- § the impact of future market changes due to exposure to foreign currency translations;
- § the possibility of certain policies, procedures, and internal processes minimizing exposure to market risk;
- § the impact of new accounting pronouncements on financial condition, results of operations, or cash flows;
- § the outcome of new or existing litigation matters;
- § the outcome of new or existing regulatory inquiries or investigations; and
- § other assumptions described in this report underlying such forward-looking statements.

Although we believe that the expectations included in these forward-looking statements are reasonable, these forward-looking statements are subject to certain events, risks, assumptions, and uncertainties, including those discussed below and in the "Risk Factors" section in Item 1A of this Form 10-Q, and elsewhere in this Form 10-Q and the documents incorporated by reference herein. If one or more of these risks or uncertainties materialize, or if our underlying assumptions prove to be incorrect, actual results and developments could materially differ from those expressed in or implied by such forward-looking statements. For example, any of the following factors could cause actual results to vary materially from our projections:

- § overall growth or lack of growth in the nutritional supplements industry;
- § plans for expected future product development;

- § changes in manufacturing costs;
- § shifts in the mix of packs and products;
- § the future impact of any changes to global associate career and compensation plans or incentives;
- § the ability to attract and retain independent associates and members;
- § new regulatory changes that could affect operations and/or products;
- § the competitive nature of our business with respect to products and pricing;
- § publicity related to our products or network-marketing; and
- § the political, social, and economic climate.

Forward-looking statements generally can be identified by use of phrases or terminology such as “may,” “will,” “should,” “could,” “would,” “expects,” “plans,” “intends,” “anticipates,” “believes,” “estimates,” “approximates,” “predicts,” “projects,” “continues” or other similar words or the negative of such terms and other comparable terminology. Similarly, descriptions of Mannatech’s objectives, strategies, plans, goals, or targets contained herein are also considered forward-looking statements. Readers are cautioned when considering these forward-looking statements to keep in mind these risks, assumptions, and uncertainties and any other cautionary statements in this report, as all of the forward-looking statements contained herein speak only as of the date of this report.

Unless stated otherwise, all financial information throughout this report and in the Consolidated Financial Statements and related Notes include Mannatech, Incorporated and all of its subsidiaries on a consolidated basis and may be referred to herein as “Mannatech,” “the Company,” “its,” “we,” “our,” or “their.”

Our products are not intended to diagnose, cure, treat, or prevent any disease and any statements about our products contained in this report have not been evaluated by the Food and Drug Administration, also referred to herein as the FDA.

## PART I – FINANCIAL INFORMATION

## Item 1. Financial Statements

## MANNATECH, INCORPORATED AND SUBSIDIARIES

## CONSOLIDATED BALANCE SHEETS

(in thousands, except share and per share amounts)

	September 30, 2010	December 31, 2009
ASSETS		
Cash and cash equivalents	\$ 21,680	\$ 17,367
Restricted cash	1,282	1,288
Accounts receivable, net of allowance of \$14 and \$17 in 2010 and 2009, respectively	163	664
Income tax receivable	999	8,075
Inventories, net	25,389	31,290
Prepaid expenses and other current assets	3,515	3,139
Deferred tax assets	2,823	2,662
Total current assets	55,851	64,485
Property and equipment, net	19,963	27,144
Construction in progress	1,507	317
Long-term restricted cash	5,632	7,201
Other assets	2,162	2,503
Long-term deferred tax assets	693	652
Total assets	\$ 85,808	\$ 102,302
LIABILITIES AND SHAREHOLDERS' EQUITY		
Current portion of capital leases	\$ 1,197	\$ 847
Accounts payable	5,309	11,319
Accrued expenses	13,271	14,231
Commissions and incentives payable	7,097	10,624
Taxes payable	3,265	2,577
Current deferred tax liability	423	274
Deferred revenue	2,881	2,807
Total current liabilities	33,443	42,679
Capital leases, excluding current portion	1,402	1,068
Long-term deferred tax liabilities	1,736	3,923
Other long-term liabilities	5,189	3,348
Total liabilities	41,770	51,018
Commitments and contingencies		
Shareholders' equity:		
Preferred stock, \$0.01 par value, 1,000,000 shares authorized, no shares issued or outstanding	—	—
Common stock, \$0.0001 par value, 99,000,000 shares authorized,	3	3

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27,697,560 shares issued and 26,490,466 shares outstanding in 2010 and 27,687,882 shares issued and 26,480,788 shares outstanding in 2009

Additional paid-in capital	41,934	41,442
Retained earnings	17,869	25,743
Accumulated other comprehensive loss	(977)	(1,113)
Less treasury stock, at cost, 1,207,094 shares in 2010 and 2009	(14,791)	(14,791)
Total shareholders' equity	44,038	51,284
Total liabilities and shareholders' equity	\$ 85,808	\$ 102,302

See accompanying notes to unaudited consolidated financial statements.

MANNATECH, INCORPORATED AND SUBSIDIARIES  
CONSOLIDATED STATEMENTS OF OPERATIONS – (UNAUDITED)  
(in thousands, except per share information)

	Three months ended		Nine months ended	
	September 30,		September 30,	
	2010	2009	2010	2009
Net sales	\$ 54,866	\$ 71,295	\$ 173,137	\$ 219,640
Cost of sales	7,924	11,923	24,640	35,944
Commissions and incentives	23,109	35,268	74,617	115,413
	31,033	47,191	99,257	151,357
Gross profit	23,833	24,104	73,880	68,283
Operating expenses:				
Selling and administrative	15,811	17,748	47,579	53,403
Depreciation and amortization	2,772	3,085	8,691	9,357
Other operating costs	8,911	11,842	26,292	30,831
Total operating expenses	27,494	32,675	82,562	93,591
Loss from operations	(3,661)	(8,571)	(8,682)	(25,308)
Interest income	20	39	1	182
Other income (expense), net	400	859	(175)	822
Loss before income taxes	(3,241)	(7,673)	(8,856)	(24,304)
(Provision) benefit for income taxes	1,963	(1,534)	982	4,785
Net loss	\$ (1,278)	\$ (9,207)	\$ (7,874)	\$ (19,519)
Net loss per share:				
Basic	\$ (0.05)	\$ (0.35)	\$ (0.30)	\$ (0.74)
Diluted	\$ (0.05)	\$ (0.35)	\$ (0.30)	\$ (0.74)
Weighted-average common shares outstanding:				
Basic	26,490	26,464	26,487	26,462
Diluted	26,490	26,464	26,487	26,462



See accompanying notes to unaudited consolidated financial statements.

MANNATECH, INCORPORATED AND SUBSIDIARIES  
CONSOLIDATED STATEMENTS OF SHAREHOLDERS' EQUITY  
AND COMPREHENSIVE INCOME (LOSS) – (UNAUDITED)  
(in thousands, except per share information)

	Common stock outstanding	Par value	Additional paid in capital	Retained earnings	Accumulated other comprehensive loss	Treasury stock Shares	Treasury stock Amounts	Total shareholders' equity
Balance at December 31, 2009	26,481	\$ 3	\$ 41,442	\$ 25,743	\$ (1,113)	1,207	\$ (14,791)	\$ 51,284
Charge related to stock-based compensation	—	—	464	—	—	—	—	464
Proceeds from stock options exercised	9	—	28	—	—	—	—	28
Components of comprehensive loss:								
Foreign currency translations	—	—	—	—	136	—	—	136
Net loss	—	—	—	(7,874)	—	—	—	(7,874)
Total comprehensive loss								(7,738)
Balance at September 30, 2010	26,490	\$ 3	\$ 41,934	\$ 17,869	\$ (977)	1,207	\$ (14,791)	\$ 44,038

See accompanying notes to unaudited consolidated financial statements.

MANNATECH, INCORPORATED ALL SUBSIDIARIES  
CONSOLIDATED STATEMENTS OF CASH FLOWS – (UNAUDITED)  
(in thousands)

	Nine months ended September 30,	
	2010	2009
<b>CASH FLOWS FROM OPERATING ACTIVITIES:</b>		
Net loss	\$ (7,874)	\$ (19,519)
Adjustments to reconcile net loss to net cash provided by (used) in operating activities:		
Depreciation and amortization	8,691	9,357
Provision for doubtful accounts	28	(7)
Provision for inventory losses	1,538	821
Loss on disposal of assets	61	94
Accounting charge related to stock-based compensation expense	464	437
Deferred income taxes	(2,024)	(1,556)
Changes in operating assets and liabilities:		
Accounts receivable	478	12
Income tax receivable	7,079	517
Inventories	4,411	1,265
Prepaid expenses and other current assets	53	2,220
Other assets	428	(1,022)
Accounts payable	(6,062)	1,630
Accrued expenses	592	(2,635)
Taxes payable	699	774
Commissions and incentives payable	(3,697)	2,505
Deferred revenue	72	399
Net cash provided by (used in) operating activities	4,937	(4,708)
<b>CASH FLOWS FROM INVESTING ACTIVITIES:</b>		
Purchases of property and equipment	(1,529)	(2,500)
Change in restricted cash	1,687	389
Net cash provided by (used in) investing activities	158	(2,111)
<b>CASH FLOWS FROM FINANCING ACTIVITIES:</b>		
Payment of cash dividends	—	(1,058)
Proceeds from stock options exercised	28	66
Repayment of capital lease obligations	(917)	(273)
Net cash used in financing activities	(889)	(1,265)
Effect of currency exchange rate changes on cash and cash equivalents	107	(284)
Net increase (decrease) in cash and cash equivalents	4,313	(8,368)
Cash and cash equivalents at the beginning of period	17,367	30,945
Cash and cash equivalents at the end of period	\$ 21,680	\$ 22,577
<b>SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION:</b>		
Income taxes received, net	\$ 7,228	\$ 2,721

Interest paid on capital leases	\$	69	\$	29
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See accompanying notes to unaudited consolidated financial statements.

MANNATECH, INCORPORATED AND SUBSIDIARIES

NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

NOTE 1: ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Mannatech, Incorporated (together with its subsidiaries, the “Company”), headquartered in Coppel, Texas, was incorporated in the state of Texas on November 4, 1993 and is listed on the NASDAQ Global Select Market under the symbol “MTEX”. The Company develops, markets, and sells high-quality, proprietary nutritional supplements, topical and skin care products, and weight-management products that are primarily sold to independent associates and members located in the United States, Canada, Australia, the United Kingdom, Japan, New Zealand, the Republic of Korea, Taiwan, Denmark, Germany, South Africa, Singapore, Austria, the Netherlands, Norway, and Sweden.

Independent associates purchase the Company’s products at published wholesale prices to either sell to retail customers or consume personally. Members purchase the Company’s products at a discount from published retail prices primarily for personal consumption. The Company cannot distinguish its personal consumption sales from its other sales because it has no involvement in its products after delivery, other than usual and customary product warranties and returns. Only independent associates are eligible to earn commissions and incentives.

The accompanying unaudited consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America for interim financial information and with instructions for Form 10-Q and Rule 10-01 of Regulation S-X. Accordingly, the Company’s consolidated financial statements and footnotes contained herein do not include all of the information and footnotes required by accounting principles generally accepted in the United States of America (“GAAP”) to be considered “complete financial statements”. However, in the opinion of the Company’s management, the accompanying unaudited consolidated financial statements and footnotes contain all adjustments, including normal recurring adjustments, considered necessary for a fair presentation of the Company’s consolidated financial information as of, and for, the periods presented. The Company cautions that its consolidated results of operations for an interim period are not necessarily indicative of its consolidated results of operations to be expected for its fiscal year. The December 31, 2009 consolidated balance sheet was included in the audited consolidated financial statements in the Company’s annual report on Form 10-K for the year ended December 31, 2009 and filed with the United States Securities and Exchange Commission on March 11, 2010 (the “2009 Annual Report”), which includes all disclosures required by GAAP. Therefore, these unaudited consolidated financial statements should be read in conjunction with the consolidated financial statements of the Company included in the 2009 Annual Report.

Principles of Consolidation

The consolidated financial statements and footnotes include the accounts of the Company and its wholly-owned subsidiaries. All intercompany balances and transactions have been eliminated in consolidation.

Use of Estimates

The preparation of the Company’s consolidated financial statements in accordance with GAAP requires the use of estimates that affect the reported value of assets, liabilities, revenues and expenses. These estimates are based on historical experience and various other factors. The Company continually evaluates the information used to make

these estimates as the business and economic environment changes. Historically, actual results have not varied materially from the Company's estimates and the Company does not currently anticipate a significant change in its assumptions related to these estimates. Actual results may differ from these estimates under different assumptions or conditions.

The use of estimates is pervasive throughout the consolidated financial statements, but the accounting policies and estimates considered to be the most significant are described in this note to the consolidated financial statements, Organization and Summary of Significant Accounting Policies.

#### Cash and Cash Equivalents

The Company considers all highly liquid investments with original maturities of three months or less to be cash equivalents. The Company includes in its cash and cash equivalents credit card receivables due from its credit card processor, as the cash proceeds from credit card receivables are generally received within 24 to 72 hours. As of September 30, 2010 and December 31, 2009, credit card receivables were \$3.6 million and \$2.8 million, respectively. Additionally, as of September 30, 2010 and December 31, 2009, cash and cash equivalents held in bank accounts in foreign countries totaled \$10.5 million and \$10.2 million, respectively.

### Restricted Cash

The Company is required to restrict cash for (i) direct selling insurance premiums and credit card sales in the Republic of Korea, (ii) a reserve on credit card sales in the United States and Canada, and (iii) collateral for its Australia building lease. As of September 30, 2010 and December 31, 2009, our total restricted cash was \$6.9 million and \$8.5 million, respectively. The decrease in restricted cash was primarily related to the partial refund of direct selling insurance premiums in Korea.

### Accounts Receivable

Accounts receivable are carried at their estimated collectible amounts. Receivables are created upon shipment of an order if the credit card payment is rejected or does not match the order total. Receivables consist primarily of amounts due from members and independent associates. The Company periodically evaluates its receivables for collectability based on historical experience, recent account activities, and the length of time they are past due, and writes-off receivables when they become uncollectible. At September 30, 2010 and December 31, 2009, the Company held an allowance for doubtful accounts of less than \$0.1 million.

### Inventories

Inventories consist of raw materials, finished goods, and promotional materials that are stated at the lower of cost (using standard costs that approximate average costs) or market. The Company periodically reviews inventories for obsolescence and any inventories identified as obsolete are reserved or written off.

### Other Assets

As of September 30, 2010 and December 31, 2009, other assets of \$2.2 million and \$2.5 million primarily consisted of deposits for building leases in various locations and certain intangible assets.

### Commissions and Incentives

Independent associates earn commissions and incentives based on their direct and indirect commissionable net sales over 13 business periods. Each business period equals 28 days. The Company accrues commissions and incentives when earned by independent associates and pays commissions on product sales three weeks following the business period end and pays commissions on its pack sales five weeks following the business period end.

### Other Long-Term Liabilities

In August 2003, the Company entered into a Long-Term Post-Employment Royalty Agreement with Dr. Bill McAnalley, the Company's former Chief Science Officer, pursuant to which the Company is required to pay Dr. McAnalley, or his heirs, royalties for ten years beginning September 2005 and continuing through August 2015. Quarterly payments related to this Long-Term Post-Employment Royalty Agreement are based on certain applicable annual global product sales by the Company in excess of \$105.4 million. At the time the Company entered into this royalty agreement, it was considered a post-employment benefit and the Company was required to measure and accrue the present value of the estimated future royalty payments related to this benefit, and recognize it over the life of Dr. McAnalley's employment agreement, which was two years. As of September 30, 2010, the Company's liability related to this royalty agreement was \$1.3 million, of which \$0.3 million was currently due and included in accrued expenses. As of December 31, 2009, the Company's long-term liability related to this royalty agreement was \$1.6 million, of which \$0.3 million was currently due and included in accrued expenses.



Certain operating leases for the Company's regional office facilities contain a restoration clause that requires the Company to restore the premises to its original condition. As of September 30, 2010 and December 31, 2009, accrued restoration costs related to these leases amounted to \$0.4 million. At September 30, 2010 and December 31, 2009, the Company also recorded a long-term liability for an estimated deferred benefit obligation related to a deferred benefit plan for its Japan operations of \$1.1 million and \$0.8 million, respectively.

## MANNATECH, INCORPORATED AND SUBSIDIARIES

## NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

## Comprehensive Income (loss) and Accumulated Other Comprehensive Income (loss)

Comprehensive income (loss) is defined as the change in equity of a business enterprise during a period from transactions and other events and circumstances from non-owner sources and includes all changes in equity during a period except those resulting from investments by owners and distributions to owners. The Company's comprehensive income (loss) consists of the Company's net income (loss), foreign currency translation adjustments from its Japan, Republic of Korea, Taiwan, Norway, and Sweden operations, and changes in the pension obligation for its Japanese employees.

## Revenue Recognition

The Company's revenue is derived from sales of individual products, sales of its starter and renewal packs, and shipping fees. Substantially all of the Company's product and pack sales are made to independent associates at published wholesale prices and to members at discounted published retail prices. The Company records revenue net of any sales taxes and records a reserve for expected sales returns based on its historical experience.

The Company recognizes revenue from shipped packs and products upon receipt by the customer. Corporate-sponsored event revenue is recognized when the event is held. The Company defers certain components of its revenue. At September 30, 2010 and December 31, 2009, the Company's deferred revenue was \$2.9 million and \$2.8 million, respectively, and consisted primarily of revenue received from: (i) sales of packs and products shipped but not received by the customers by period end; and (ii) prepaid registration fees from customers planning to attend a future corporate-sponsored event.

We estimate a sales return reserve for expected sales refunds based on our historical experience over a rolling six-month period. If actual results differ from our estimated sales return reserve due to various factors, the amount of revenue recorded each period could be materially affected. Historically, our sales returns have not materially changed through the years, as the majority of our customers who return their merchandise do so within the first 90 days after the original sale. Sales returns have averaged 1.5% or less of our gross sales. For the nine months ended September 30, 2010 our sales return reserve was composed of the following (in thousands):

	September 30, 2010
Sales reserve as of January 1, 2010	\$ 595
Provision related to sales made in current period	1,591
Provision related to sales made in prior periods	112
Actual returns or credits related to current period	(1,128)
Actual returns or credits related to prior periods	(710)
Sales reserve as of September 30, 2010	\$ 460

## Shipping and Handling Costs

The Company records freight and shipping fees collected from its customers as revenue. The Company records inbound freight as cost of sales and records shipping and handling costs associated with shipping products to customers as selling and administrative expenses. Total shipping and handling costs included in selling and administrative expenses were approximately \$2.7 million and \$3.6 million for the three months ended September 30, 2010 and 2009, respectively, and \$8.8 million and \$10.6 million for the nine months ended September 30, 2010 and 2009, respectively.

#### Reclassifications

Certain reclassifications have been made to the financial statements for prior periods to conform to the current period presentation.

## MANNATECH, INCORPORATED AND SUBSIDIARIES

## NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

## NOTE 2: INVENTORIES

Inventories consist of raw materials and finished goods, including promotional materials. The Company provides an allowance for any slow-moving or obsolete inventories. Inventories at September 30, 2010 and December 31, 2009, consisted of the following (in thousands):

	September 30, 2010	December 31, 2009
Raw materials	\$ 9,223	\$ 10,819
Finished goods	18,156	21,844
Inventory reserves for obsolescence	(1,990)	(1,373)
	\$ 25,389	\$ 31,290

## NOTE 3: INCOME TAXES

For the three months ended September 30, 2010, the Company recognized a tax benefit of approximately \$1.9 million. This was the result of changes to management's estimates for 2010 annual operating results, including the mix of income between tax jurisdictions, the change in the valuation allowances associated with certain deferred tax assets, and the change in reserves related to uncertain income tax positions. For the nine months ended September 30, 2010 the Company recognized a \$0.9 million tax benefit. For the three and nine months ended September 30, 2009, the Company's effective tax rate was (20.0)% and 19.7%, respectively. For the three and nine months ended September 30, 2010 and 2009, the Company's effective income tax rate was determined based on the estimated annual effective income tax rate.

The effective tax rate for the nine months ended September 30, 2010 was lower than what would have been expected if the federal statutory rate were applied to income before taxes. Items reducing the effective income tax rate included reductions due to changes to management's estimates for 2010 annual operating results, including the mix of income between tax jurisdictions, the change in the valuation allowances associated with certain deferred tax assets, and the change in reserves related to uncertain income tax positions. The effective tax rate for the three months ended September 30, 2010 was higher than what would have been expected if the federal statutory rate were applied to income before taxes due to changes in management's estimates during the quarter for 2010 annual operating results, including the mix of income between tax jurisdictions.

## NOTE 4: LOSS PER SHARE

Basic Earnings (Loss) Per Share ("EPS") calculations are based on the weighted-average number of the Company's common shares outstanding during the period. Diluted EPS calculations are based on the calculated weighted-average number of common shares and dilutive common share equivalents outstanding during each period.

The following data shows the amounts used in computing the Company's EPS and their effect on the Company's weighted-average number of common shares and dilutive common share equivalents for the three months ended

September 30, 2010 and 2009. For the three months ended September 30, 2010, approximately 1.6 million shares of the Company's common stock subject to options were excluded from diluted EPS calculations using an average closing price of \$2.41 per share, as their effect was antidilutive. For the three months ended September 30, 2009, approximately 1.6 million shares of the Company's common stock subject to options were excluded from diluted EPS calculations using an average close price of \$3.73 per share, as their effect was antidilutive. The amounts below are rounded to the nearest thousands, except for per share amounts.

## MANNATECH, INCORPORATED AND SUBSIDIARIES

## NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

	For the three months ended September 30, 2010		Per share amount	For the three months ended September 30, 2009		Per share amount
	Loss (numerator)	Shares (denominator)		Loss (numerator)	Shares (denominator)	
<b>Basic EPS:</b>						
Net loss available to common shareholders	\$ (1,278)	26,490	\$ (0.05)	\$ (9,207)	26,464	\$ (0.35)
Effect of dilutive securities:						
Stock options	—	—	—	—	—	—
<b>Diluted EPS:</b>						
Net loss available to common shareholders plus assumed conversions	\$ (1,278)	26,490	\$ (0.05)	\$ (9,207)	26,464	\$ (0.35)

The following data shows the amounts used in computing the Company's EPS and their effect on the Company's weighted-average number of common shares and dilutive common share equivalents for the nine months ended September 30, 2010 and 2009. For the nine months ended September 30, 2010, approximately 1.6 million shares of the Company's common stock subject to options were excluded from diluted EPS calculations using an average close price of \$2.93 per share, as their effect was antidilutive. For the nine months ended September 30, 2009, approximately 1.5 million shares of the Company's common stock subject to options were excluded from diluted EPS calculations using an average close price of \$3.48 per share, as their effect was antidilutive. The amounts below are rounded to the nearest thousands, except for per share amounts.

	For the nine months ended September 30, 2010		Per share amount	For the nine months ended September 30, 2009		Per share amount
	Loss (numerator)	Shares (denominator)		Loss (numerator)	Shares (denominator)	
<b>Basic EPS:</b>						
Net loss available to	\$ (7,874)	26,487	\$ (0.30)	\$ (19,519)	26,462	\$ (0.74)

common shareholders						
Effect of dilutive securities:						
Stock options	—	—	—	—	—	—
Diluted EPS:						
Net loss available to common shareholders plus assumed conversions	\$(7,874)	26,487	\$(0.30)	\$(19,519)	26,462	\$(0.74)

NOTE 5: STOCK-BASED COMPENSATION

The Company currently has one active stock-based compensation plan, which was approved by shareholders. The Company generally grants stock options to employees, consultants, and board members at the fair market value of its common stock, on the date of grant, with a term no greater than ten years. The stock options generally vest over two or three years. Shareholders who own 10% or more of the Company’s outstanding stock are granted incentive stock options at an exercise price that may not be less than 110% of the fair market value of the Company’s common stock on the date of grant and have a term no greater than five years.

In February 2008, the Company’s Board of Directors approved the Mannatech, Incorporated 2008 Stock Incentive Plan (the “2008 Plan”), which reserved, for issuance of stock options and restricted stock to employees, board members, and consultants, up to 1,000,000 shares of common stock plus any shares reserved under the Company’s then-existing, unexpired stock plan for which options had not yet been issued plus any shares underlying outstanding options under the then-existing stock option plan that terminate without having been exercised in full. The 2008 Plan was approved by the Company’s shareholders at the 2008 Annual Shareholders’ Meeting. As of September 30, 2010, the 2008 Plan had 321,088 stock options available for grant before the plan expires on February 20, 2018.

At the 2010 Annual Shareholders' Meeting the Company obtained approval from the Company's shareholders for an amendment to the 2008 Plan to permit a one-time stock option exchange program (the "Exchange Offer"). On July 16, 2010, the Company commenced the option exchange program (the "Exchange Program") whereby employees (including officers), directors and consultants were able to elect to exchange their "out of the money" stock options for fewer options at a lower exercise price. The Exchange Program expired on August 13, 2010.

The Company filed with the Securities and Exchange Commission (the "SEC") the Tender Offer Statement on Schedule TO on July 16, 2010, (as amended, the "Schedule TO"), and the Offer to Exchange filed with the Schedule TO as Exhibit (a)(1)(A), (as amended, the "Offer to Exchange").

Pursuant to the Exchange Program, an aggregate of 784,930 eligible options were tendered and accepted by the Company in exchange for the grant of an aggregate of 440,558 replacement options.

All of the replacement options that were granted on August 16, 2010 have an exercise price of \$2.46 and were granted under the 2008 Plan, as amended. Each replacement option vests annually in installments starting one year from the grant date and has a term of 10 years. Incremental stock option expense resulting from the exchange was minimal because the fair value of the replacement options was approximately equal to the fair value of the surrendered options they replaced. The foregoing description of the Exchange Program is qualified in its entirety by reference to the Schedule TO and the Offer to Exchange.

The Company records stock-based compensation expense related to granting stock options as selling and administrative expenses. During the three months ended September 30, 2010, the Company granted 465,558 stock options, of which 440,558 were a result of the Exchange Program. During the three months ended September 30, 2009, the Company granted 30,000 stock options. During the nine months ended September 30, 2010, the Company granted 772,194 stock options, of which 440,558 were a result of the Exchange Program. During the nine months ended September 30, 2009, the Company granted 305,000 stock options. The fair value of stock options granted during the three months ended September 30, 2010 ranged from \$1.26 to \$1.40 per share. The fair value of stock options granted during the three months ended September 30, 2009 was \$2.01 per share. The fair value of stock options granted during the nine months ended September 30, 2010 ranged from \$1.18 to \$2.03 per share. The fair values of stock options granted during the nine months ended September 30, 2009 ranged from \$1.24 to \$2.01 per share. The Company recognized compensation expense as follows for the periods ended September 30 (in thousands):

	Three months		Nine months	
	2010	2009	2010	2009
Total gross compensation expense	\$ 123	\$ 125	\$ 514	\$ 437
Total tax benefit associated with compensation expense	10	24	67	97
Total net compensation expense	\$ 113	\$ 101	\$ 447	\$ 340

As of September 30, 2010, the Company expects to record compensation expense in the future as follows:

	Three months ending December 31, 2010	Year ending December 31, 2011	2012	2013
Total gross unrecognized compensation expense	\$ 112	\$ 375	\$ 184	\$ 71
	16	49	20	6



Tax benefit associated with unrecognized  
compensation expense

Total net unrecognized compensation expense	\$	96	\$ 326	\$ 164	\$ 65
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## NOTE 6: SHAREHOLDER'S EQUITY

On September 16, 2010, the Company entered into an Investment Agreement (the "Investment Agreement") with Dutchess Opportunity Fund, II, LP, a Delaware limited partnership (the "Investor"). Pursuant to the Investment Agreement, the Investor committed to purchase, subject to certain restrictions and conditions, up to \$10,000,000 of the Company's common stock, over a period of 36 months from the first trading day following the effectiveness of the registration statement registering the resale of shares purchased by the Investor pursuant to the Investment Agreement (the "Equity Line"). The aggregate number of shares of common stock issuable by the Company and purchasable by the Investor under the Investment Agreement is 5,000,000.

The Company may draw on the Equity Line from time to time, as and when it determines appropriate in accordance with the terms and conditions of the Investment Agreement. The maximum amount that the Company is entitled to put to the Investor in any one draw down notice is the greater of (i) 200% of the average lowest daily volume of the Company's common stock traded on the NASDAQ Global Market for the 3 trading days prior to the date of delivery of the applicable draw down notice, multiplied by the average of the closing prices for such trading days or (ii) \$500,000. The purchase price shall be set at 96% of the lowest daily volume weighted average price (VWAP) of the Company's common stock during the 5 consecutive trading day period beginning on the date of delivery of the applicable draw down notice. Before the closing of an exercised put, the Company (not the Investor) has the right to withdraw all or any portion of the put; provided that the Company may not withdraw any portion of a put that the Investor has already committed to resell to a third party. There are put restrictions applied on days between the draw down notice date and the closing date with respect to that particular put. During such time, the Company shall not be entitled to deliver another draw down notice. In addition, the Investor will not be entitled to purchase shares if the Investor's total number of shares beneficially held at that time would exceed 4.99% of the number of shares of the Company's common stock as determined in accordance with Rule 13d-1(j) of the Securities Exchange Act of 1934, as amended. In addition, the Company is not permitted to draw on the Equity Line unless there is an effective registration statement (as further explained below) to cover the resale of the shares.

The Investment Agreement further provides that the Company and the Investor are each entitled to customary indemnification from the other for, among other things, any losses or liabilities they may suffer as a result of any breach by the other party of any provisions of the Investment Agreement or Registration Rights Agreement (as defined below), or as a result of any lawsuit brought by a third-party arising out of or resulting from the other party's execution, delivery, performance or enforcement of the Investment Agreement or the Registration Rights Agreement.

The Investment Agreement also contains customary representations and warranties of each of the parties. Investors should read the Investment Agreement together with the other information concerning the Company that the Company publicly files in reports and statements with the SEC.

Pursuant to the terms of a Registration Rights Agreement dated September 16, 2010 between the Company and the Investor (the "Registration Rights Agreement"), the Company is obligated to file one or more registration statements with the SEC to register the resale by Investor of the shares of common stock issued or issuable under the Investment Agreement. On October 28, 2010, the SEC declared effective the Company's Registration Statement on Form S-3 (File No. 333-169774), which registers up to 5,000,000 shares of common stock that may be resold by the Investor pursuant to the Investment Agreement. As of November 3, 2010, no shares of common stock have been issued pursuant to the Investment Agreement.

In connection with the preparation of the Investment Agreement and the Registration Rights Agreement, the Company paid the Investor a document preparation fee in the amount of \$15,000.

## NOTE 7: LITIGATION

Patent Infringement Litigation

Mannatech, Inc. v. Country Life, LLC, et al., No. 3:10-cv-00533-O, United States District Court, Northern District of Texas, Dallas Division

On March 16, 2010, Mannatech, Inc. filed a patent infringement lawsuit against Country Life, LLC; Country Life Manufacturing, LLC; EvenBetterNow, LLC; Micro Health Solutions, LLC; New Sun, Inc.; Oasis Advanced Wellness, LLC; Roex, Inc.; VDF FutureCeuticals, Inc.; and John Does 1-20, alleging the defendants infringe United States Patent Nos. 6,929,807, 7,157,431, 7,196,064, 7,199,104, and 7,202,220, all entitled “Compositions of Plant Carbohydrates as Dietary Supplements” (“Patents-in-Suit”), and seeking to stop their manufacture, offer, and sale of infringing glyconutritional dietary supplement products. On May 14, 2010, Mannatech amended its complaint to add patent infringement claims against Angel Care USA, Inc.; Florida Nutri Labs, LLC; and Wy’s Enterprises of Springfield, Inc.

Agreed Judgments have been entered against seven of the eleven defendants: EvenBetterNow, Oasis Advanced Wellness, Micro Health Solutions, Wy's Enterprises of Springfield, Florida Nutri Labs, Angel Care, USA, and New Sun. In each of the Agreed Judgments, the defendant is enjoined, for the term of the Patents-in-Suit, from making, using, offering to sell, or otherwise distributing the accused infringing products or colorable imitations thereof (the "Enjoined Products"); inducing infringement of the patents by encouraging or assisting others in selling the Enjoined Products; or supplying or causing to be supplied all or a substantial portion of the components of the Enjoined Products.

On June 25, 2010, Mannatech filed an unopposed motion to drop defendant Country Life Manufacturing, LLC because Mannatech discovered that Country Life Manufacturing was no longer active or associated with Country Life, LLC. On June 29, Mannatech's motion was granted and Country Life Manufacturing, LLC was dismissed from the lawsuit without prejudice.

The lawsuit is now proceeding against the remaining three defendants: Country Life, Roex, and VDF FutureCeuticals. All three have filed answers, and two of the defendants, Roex and VDF FutureCeuticals, have filed counterclaims challenging the validity of Mannatech's patents and seeking recovery of their attorneys' fees. In addition, on June 25, 2010, Roex filed a motion to sever and motion to transfer venue to its home district of the Central District of California. On July 16, Mannatech filed its response in opposition, after which VDF FutureCeuticals filed a motion to join Roex's motion to transfer. On July 21, Mannatech filed a motion to strike VDF's improper joinder. On July 26, 2010, the Court denied Roex's motion.

On July 16, 2010, the court entered a Scheduling Order, setting trial for November 1, 2011. In order to permit the parties to engage in direct settlement discussions, the parties have twice filed joint motions seeking extensions of the Scheduling Order deadlines. The court granted both motions and the current Second Amended Scheduling Order, issued on October 12, 2010, reset the trial date for December 5, 2011. Mannatech intends to vigorously prosecute this matter in the event settlement cannot be reached, as this lawsuit continues Mannatech's enforcement of its patent rights. Based on the previous successful patent infringement lawsuits against Glycobiotics International, Inc., Techmedica Health, Inc., IonX Holdings, Inc., Boston Mountain Laboratories, Inc., Green Life, LLC, and Xiong Lo, Mannatech believes it could obtain permanent injunctions against the manufacture and sale of any infringing products for the duration of Mannatech's Patents-in-Suit.

#### Business Arbitration and Litigation

Marinova Pty. Limited v. Mannatech, Incorporated & Mannatech (International) Limited, Case No. 50-122-T-00635-09, International Centre for Dispute Resolution, a division of the American Arbitration Association

On December 10, 2009, Marinova Pty. Limited ("Marinova"), a company duly organized and operating under the laws of Australia, filed a Notice of Arbitration and Statement of Claim with the International Centre for Dispute Resolution, which is a division of the American Arbitration Association, against Mannatech Incorporated and Mannatech (International) Limited (collectively, "Mannatech"). Marinova's claims stem from the parties' April 27, 2007 Purchase Agreement, which was entered into between Marinova and Mannatech (International) Limited and executed by Marinova and Mannatech, Incorporated. Through the Purchase Agreement, Marinova agreed to sell and Mannatech agreed to buy set quantities of glyconutrient powder that Mannatech uses in the manufacturing of some its products. Marinova claims that Mannatech breached the Purchase Agreement by not buying certain quantities of Marinova's product. Marinova alternatively claims that Mannatech, Incorporated tortiously interfered with the Purchase Agreement. Finally, Marinova claims that Mannatech, Incorporated made fraudulent representations to Marinova upon which Marinova claims it relied in executing the Purchase Agreement. Marinova claims that Mannatech's actions have caused them over \$5,000,000 in damages, as well as attorneys' fees and costs.



On January 15, 2010, Mannatech filed its Answering Statement and Counterclaims, through which Mannatech asserted affirmative defenses in response to Marinova's claims, including that Marinova's own actions or omissions contributed to or caused Marinova's alleged injury. Mannatech also filed a counterclaim for breach of contract, through which Mannatech alleges that Marinova sold Mannatech non-conforming powder and then refused to reimburse Mannatech the amount it paid for the non-conforming powder, thereby breaching the Purchase Agreement. Mannatech further alleges that Marinova separately breached the Purchase Agreement by marketing its powder to one or more of Mannatech's competitors in violation of an amendment to the Purchase Agreement's exclusivity clause. Finally, Mannatech requested declaratory judgments from the arbitration panel, including a judgment that Mannatech is not obligated to purchase any additional product from Marinova because Marinova breached the Purchase Agreement. Mannatech is seeking damages in the amount it paid for the non-conforming product, as well as damages from Marinova's breach of the parties' exclusivity agreement, attorneys' fees, and costs.

On August 25, 2010, the panel of three arbitrators held their preliminary hearing, during which Mannatech requested the opportunity to brief a motion to strike certain portions of Marinova's Statement of Claims that Mannatech thought were brought solely for the purposes of prejudicing the panel against Mannatech. Those portions of Marinova's Statement of Claims related to lawsuits filed against Mannatech several years ago, all of which have now settled and bear no relation to Marinova's claims. The panel granted Mannatech leave to file a motion to strike.

In response, Marinova sought leave and was granted the opportunity to re-plead its Statement of Claims. On August 31, 2010, Marinova filed its Amended Statement of Claims, in which it claims that, in addition to its other claims against Mannatech, Mannatech breached the Purchase Agreement because Mannatech allegedly falsely warranted that it was not the subject of any lawsuits or investigations. Accordingly, on September 15, 2010, Mannatech filed its Motion to Dismiss and Strike, through which it seeks to strike Marinova's newly-added claim because (a) Marinova never raised the claim prior to its re-pleading; (b) Marinova accepted millions of dollars from Mannatech after it became aware of Mannatech's alleged breach; and (c) Marinova is asserting its claim solely in an attempt to prejudice the panel. Marinova subsequently filed a response and Mannatech filed a reply in support of its Motion to Dismiss and Strike on October 12, 2010. The panel has not yet ruled on the Motion to Dismiss and Strike.

Mannatech intends to vigorously defend against Marinova's claims and prosecute its counterclaim.

#### Litigation in General

The Company has several pending claims incurred in the normal course of business. In the Company's opinion, such claims can be resolved without any material adverse effect on its consolidated financial position, results of operations, or cash flows.

The Company maintains certain liability insurance; however, certain costs of defending lawsuits, such as those below the insurance deductible amount, are not covered by or only partially covered by its insurance policies. Additionally, insurance carriers could refuse to cover certain of these claims in whole or in part. The Company accrues costs to defend itself from litigation as incurred or as they become determinable.

The outcome of litigation may not be assured, and despite management's views of the merits of any litigation, or the reasonableness of the Company's estimates and reserves, the Company's financial statements could nonetheless be materially affected by an adverse judgment. The Company believes it has adequately reserved for the contingencies arising from the above legal matters where an outcome was deemed to be probable, and the loss amount could be reasonably estimated. While it is not possible to predict with certainty what liability or damages the Company might incur in connection with any of the above-described lawsuits, based on the advice of counsel and a management review of the existing facts and circumstances related to these lawsuits, and related legal fees, the Company has accrued \$0.5 million as of September 30, 2010 for these matters, which is included in accrued expenses in its Consolidated Balance Sheet.



MANNATECH, INCORPORATED AND SUBSIDIARIES

NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

NOTE 8: RECENT ACCOUNTING PRONOUNCEMENTS

In October 2009, the FASB issued Accounting Standards Update No. 2009-13, “Revenue Recognition—Multiple Deliverable Revenue Arrangements” (“ASU 2009-13”). ASU 2009-13 updates the existing multiple-element revenue arrangements guidance currently included in FASB ASC 605-25. The revised guidance provides for two significant changes to the existing multiple element revenue arrangements guidance. The first change relates to the determination of when the individual deliverables included in a multiple-element arrangement may be treated as separate units of accounting. The second change modifies the manner in which the transaction consideration is allocated across the separately identified deliverables. The revised guidance also expands the disclosures required for multiple-element revenue arrangements. The revised multiple-element revenue arrangements guidance will be effective for the first annual reporting period beginning on or after June 15, 2010. The adoption of ASU 2009-13 is not expected to have a material impact on the Company’s financial position or results of operations.

In January 2009, the Securities and Exchange Commission issued Release No. 33-9002, “Interactive Data to Improve Financial Reporting.” The final rule requires companies to provide their financial statements and financial statement schedules to the Securities and Exchange Commission in interactive data format using the eXtensible Business Reporting Language (“XBRL”). The rule was adopted by the Securities and Exchange Commission to improve the ability of financial statement users to access and analyze financial data. The Securities and Exchange Commission adopted a phase-in schedule indicating when registrants must furnish interactive data. Under this schedule, the Company will be required to submit filings with financial statement information using XBRL commencing with our June 30, 2011 quarterly report on Form 10-Q. We began furnishing financial information in XBRL format starting with our quarterly report on Form 10-Q for the period ended September 30, 2009. As an early XBRL adopter, the Company may choose to discontinue furnishing XBRL data in the future until the required compliance date of June 30, 2011.

NOTE 9: FAIR VALUE

Fair Value Measurements and Disclosure Topic of the FASB ASC establishes a fair value hierarchy that requires the use of observable market data, when available, and prioritizes the inputs to valuation techniques used to measure fair value in the following categories:

- Level 1 – Quoted unadjusted prices for identical instruments in active markets.
- Level 2 – Quoted prices for similar instruments in active markets, quoted prices for identical or similar instruments in markets that are not active and model-derived valuations in which all observable inputs and significant value drivers are observable in active markets.
- Level 3 – Model-derived valuations in which one or more significant inputs or significant value drivers are unobservable, including assumptions developed by the Company.



The primary objective of the Company's investment activities is to preserve principal while maximizing yields without significantly increasing risk. The investment instruments held by the Company are money market funds and interest bearing deposits for which quoted market prices are readily available. The Company considers these highly liquid investments to be cash equivalents. These investments are classified within Level 1 of the fair value hierarchy because they are valued based on quoted market prices in active markets. The table below presents the recorded amount of financial assets measured at fair value (in thousands) on a recurring basis as of September 30, 2010. The Company does not have any material financial liabilities that were required to be measured at fair value on a recurring basis at September 30, 2010.

## MANNATECH, INCORPORATED AND SUBSIDIARIES

## NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

Asset	Level 1	Level 2	Level 3	Total
Money Market Funds – Fidelity, US	\$ 6,029	\$ —	\$ —	6,029
Interest bearing deposits – various banks, Korea	4,969	—	—	4,969
Total assets	\$ 10,998	\$ —	\$ —	10,998
Amounts included in:				
Cash and cash equivalents	\$ 6,345	\$ —	\$ —	6,345
Long-term restricted cash	4,653	—	—	4,653
Total	\$ 10,998	\$ —	\$ —	10,998

## NOTE 10: SEGMENT INFORMATION

The Company conducts its business as a single operating segment, consolidating all of its business units into a single reportable entity, as a seller of proprietary nutritional supplements, topical and skin care products, and weight-management products through its network marketing distribution channels operating in sixteen countries. Each of the Company's business units sells similar packs and products and possesses similar economic characteristics, such as selling prices and gross margins. In each country, the Company markets its products and pays commissions and incentives in similar market environments. The Company's management reviews its financial performance by country and analyzes consolidated revenues by packs and product sales. The Company sells its products through its independent associates and distributes its products through similar distribution channels in each country. No single independent associate has ever accounted for more than 10% of the Company's consolidated net sales.

The Company operates in nine physical locations and sells products in sixteen different countries around the world. The nine physical locations are the United States, Canada, Switzerland, Australia, the United Kingdom, Japan, the Republic of Korea (South Korea), Taiwan, and South Africa. Each of the Company's physical locations services different geographic areas. The United States, Canada, Australia, United Kingdom, Japan, and South Africa offices provide administrative support to their respective local markets and serve as meeting locations for independent associates. The United States location processes orders for the United States, Canada, and South Africa. The Australian location processes orders for Australia, New Zealand, and Singapore. The United Kingdom location processes orders for the United Kingdom, Denmark, Germany, Austria, the Netherlands, Norway, and Sweden. The Japan, Republic of Korea, and Taiwan locations process orders for their local markets only. The Switzerland office was created to manage certain day-to-day business needs of our international markets.

Consolidated net sales shipped to customers in these locations, along with pack and product information for the three and nine months ended September 30, 2010 and 2009 are as follows (in millions, except percentages):

Country	Three months				Nine months			
	2010		2009		2010		2009	
United States	\$ 23.9	43.5%	\$ 34.0	47.7%	\$ 77.7	44.9%	\$ 109.7	49.9%
Japan	8.9	16.2%	9.9	13.9%	25.8	14.9%	31.4	14.3%
Republic of Korea	5.1	9.3%	6.9	9.7%	16.2	9.4%	19.2	8.8%
Canada	4.6	8.4%	5.8	8.1%	14.0	8.1%	17.5	8.0%
Australia	4.7	8.6%	5.7	8.0%	14.8	8.6%	16.7	7.6%
South Africa	3.0	5.5%	3.9	5.5%	9.0	5.2%	9.4	4.2%
Taiwan	1.4	2.6%	1.4	2.0%	5.0	2.9%	4.8	2.2%
New Zealand	0.7	1.3%	1.1	1.5%	2.5	1.4%	3.3	1.5%
Germany	0.6	1.1%	0.9	1.3%	1.8	1.0%	2.6	1.2%
United Kingdom	0.4	0.7%	0.8	1.0%	1.6	0.9%	2.5	1.1%
Denmark	0.1	0.2%	0.5	0.7%	0.4	0.2%	1.5	0.7%
Singapore	0.5	0.9%	0.4	0.6%	1.5	0.9%	1.0	0.5%
Austria(1)	0.2	0.3%	—	—	0.9	0.5%	—	—
Norway(1)	0.5	0.9%	—	—	1.2	0.7%	—	—
The Netherlands(1)	0.2	0.3%	—	—	0.4	0.2%	—	—
Sweden(1)	0.1	0.2%	—	—	0.3	0.2%	—	—
Totals	\$ 54.9	100%	\$ 71.3	100%	\$ 173.1	100%	\$ 219.6	100%

(1) Austria, Norway, the Netherlands, and Sweden began operations in September 2009, and had a combined total net sales of \$0.1 million for the period ended September 30, 2009.

	Three months		Nine months	
	2010	2009	2010	2009
Consolidated product sales	\$ 45.5	\$ 52.3	\$ 140.8	\$ 159.1
Consolidated pack sales	7.0	15.5	25.1	50.2
Consolidated other, including freight	2.4	3.5	7.2	10.3
Consolidated total net sales	\$ 54.9	\$ 71.3	\$ 173.1	\$ 219.6

Long-lived assets, which include property and equipment and construction in progress for the Company and its subsidiaries, reside in the following countries (in millions):

Country	September 30,	December
	2010	31, 2009
Australia	\$ 0.3	\$ 0.3
Canada	0.1	0.1
Japan	0.2	0.3
Republic of Korea	0.9	0.6
Switzerland	0.4	0.5
Taiwan	0.1	0.1
South Africa	0.1	—
United Kingdom	0.1	0.1
United States	19.3	25.5
Totals	\$ 21.5	\$ 27.5



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

The following discussion is intended to assist in the understanding of our consolidated financial position and results of operations for the nine months ended September 30, 2010 as compared to the same period in 2009, and should be read in conjunction with Item I "Financial Statements" in Part I of this quarterly report on Form 10-Q. Unless stated otherwise, all financial information presented below, throughout this report, and in the consolidated financial statements and related notes includes Mannatech, Incorporated and all of our subsidiaries on a consolidated basis.

### COMPANY OVERVIEW

Since November 1993, we have continued to develop innovative, high-quality, proprietary nutritional supplements, topical and skin care products, and weight-management products that are sold through a global network marketing system operating in the United States, Canada, Australia, the United Kingdom, Japan, New Zealand, the Republic of Korea, Taiwan, Denmark, Germany, South Africa, Singapore, Austria, the Netherlands, Norway, and Sweden. The United States, Canada, Australia, United Kingdom Japan, and South Africa offices provide administrative support to its local markets and act as meeting locations for independent associates. The United States location processes orders for the United States, Canada, and South Africa. The Australian location processes orders for Australia, New Zealand, and Singapore. The United Kingdom location processes orders for the United Kingdom, Denmark, Germany, Austria, the Netherlands, Norway, and Sweden. The Japan, Republic of Korea, and Taiwan locations process orders for their local markets only. The Switzerland office was created to manage certain day-to-day business needs of our international markets. We review and analyze net sales by geographical location and by packs and products on a consolidated basis. Each subsidiary sells the same type of products and exhibits similar economic characteristics, such as selling prices and gross margins.

We conduct our business as a single operating segment and primarily sell our products through a network of approximately 422,000 independent associates and members who have purchased our products and/or packs within the last 12 months, which we refer to as current independent associates and members. New recruits and pack sales are regarded as leading indicators for the long-term success of our business. New recruits include new independent associates and members purchasing our packs and products for the first time.

Because we sell our products through network marketing distribution channels, the opportunities and challenges that affect us most are: recruitment of new and retention of existing independent associates and members, entry into new markets and growth of existing markets, niche market development, new product introduction, maintaining competitive compensation plans, and investment in our infrastructure.

During calendar year 2008, the U.S. and foreign economies slowed dramatically because of the global financial crisis. The difficult conditions affecting the overall macro-economic environment continued to impact our business in 2009 and 2010. Significant reduction in consumers' disposable income impacted our customers' spending practices, causing a decline in our revenues.

During 2008 and 2009, in response to adverse market conditions, we implemented various initiatives to reduce expenses, including the temporary suspension of matching contributions under our 401(k) employee savings plan, reduction in our workforce, and reduction in other discretionary costs such as outside services, travel and overtime. We also suspended our quarterly cash dividend in August of 2009. By establishing a culture of expense control and accountability, we achieved a decrease in operating expenses and maintained that level of expense control through 2010. Our intent is to systematically review all expenditures with the goal of prudently managing our business. At the same time, we remain committed to our strategic plan of developing new, innovative, and scientifically-validated products, international expansion, strengthening financial results, and adding value to our shareholders and

independent associates.

We continue expansion into new international markets and are scheduled to begin selling products in Mexico in early 2011. Our expansion into Mexico will complement our existing presence in North America while highlighting our continued focus on global expansion.

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We continue to focus on new product development. In the first quarter of 2010, we launched the Simply Delicious snack bar. The Simply Delicious bar is USDA (United States Department of Agriculture) Organic certified and is offered in two flavors – cherry pie and chocolate raspberry truffle. In late September 2010, we launched our exclusive, age-defying product line, the Mannatech LIFT™ skin care system. The Mannatech LIFT™ skin care line is an innovative system formulated to reduce the signs of aging and improve the youthful radiance of skin in three easy steps. The line is paraben-free and features the company's Jeunesse 7™ proprietary blend – a combination of Mannatech's signature glyconutrients and a French green clay. These features collectively make the Mannatech LIFT™ line a natural, age-defying skin care system unique to the industry. The easy-to-use system is formulated with more than 30 natural and botanical ingredients and is currently available throughout the United States and Canada.

In addition to our innovative product development, we continue to invest in research for our existing products. Recent results of a randomized, double-blind, placebo-controlled study validated that Ambrotose® has beneficial effects on cognitive functioning. Additional preclinical studies suggest that Ambrotose® can exert positive effects on the immune system and the digestive tract. Ambrotose®, a glyconutrient product originally launched in 1996, is still our best-selling product.

MannaRelief and Mannatech have partnered together to launch the new Give for RealSM program. This “donation-through-consumption” initiative was designed to allow consumers and associates to help undernourished children around the world. For every purchase on an automatic order containing Ambrotose® complex powder, Advanced Ambrotose® powder, MannaBears™ gummies, PhytoMatrix® caplets, PhytoBurst® nutritional chews or Optimal Support Packets, a donation of Mannatech's nutritional supplements is provided through MannaRelief to children in need worldwide. For the three months ended September 30, 2010, Mannatech has provided an additional \$90,000 in donations to MannaRelief as a result of the Give For RealSM program. MannaRelief and Mannatech's goal is to connect one million sponsors to one million undernourished children.

Subsequent to the end of the second quarter 2010, the board of directors of the International Sport Karate Association (ISKA) certified Mannatech as its official dietary supplement provider. Several of our products will feature the “ISKA Certified for Elite Athletes” seal on the label, which will be the only health supplements on the market to feature this seal on its packaging. The certification program was developed by ISKA to recognize high-quality dietary supplements. ISKA and Mannatech's exclusive initial partnership will last until 2012, with an option to renew.

We believe our aggressive cost reduction, new product introduction, international expansion, and financial discipline will enable us to effectively manage through the challenging economy. We believe these recent changes will position us to support future long-term profitable growth.

## RESULTS OF OPERATIONS

The table below summarizes our consolidated operating results in dollars and as a percentage of net sales for the three months ended September 30, 2010 and 2009 (in thousands, except percentages).

	2010		2009		Change from 2010 to 2009	
	Total dollars	% of net sales	Total dollars	% of net sales	Dollar	Percentage
Net sales	\$ 54,866	100%	\$ 71,295	100%	\$ (16,429)	(23.0)%
Cost of sales	7,924	14.4%	11,923	16.7%	(3,999)	(33.5)%
Commissions and incentives	23,109	42.1%	35,268	49.6%	(12,159)	(34.5)%
	31,033	56.6%	47,191	66.2%	(16,158)	(34.2)%
Gross profit	23,833	43.4%	24,104	33.8%	(271)	(1.1)%
<b>Operating expenses:</b>						
Selling and administrative expenses	15,811	28.8%	17,748	24.9%	(1,937)	(10.9)%
Depreciation and amortization	2,772	5.1%	3,085	4.3%	(313)	(10.1)%
Other operating costs	8,911	16.2%	11,842	16.6%	(2,931)	(24.8)%
Total operating expenses	27,494	50.1%	32,675	45.8%	(5,181)	(15.9)%
Loss from operations	(3,661)	(6.7)%	(8,571)	(12.0)%	4,910	57.3%
Interest income	20	0.0%	39	0.1%	(19)	(48.7)%
Other income, net	400	0.7%	859	1.2%	(459)	(53.4)%
Loss before income taxes	(3,241)	(5.9)%	(7,673)	(10.8)%	4,432	57.8%
(Provision) benefit for income taxes	1,963	3.6%	(1,534)	(2.2)%	3,497	228.0%
Net loss	\$ (1,278)	(2.3)%	\$ (9,207)	(12.8)%	\$ 7,929	86.1%



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The table below summarizes our consolidated operating results in dollars and as a percentage of net sales for the nine months ended September 30, 2010 and 2009 (in thousands, except percentages).

	2010		2009		Change from 2010 to 2009	
	Total dollars	% of net sales	Total dollars	% of net sales	Dollar	Percentage
Net sales	\$ 173,137	100%	\$ 219,640	100%	\$(46,503)	(21.2)%
Cost of sales	24,640	14.2%	35,944	16.4%	(11,304)	(31.4)%
Commissions and incentives	74,617	43.1%	115,413	52.5%	(40,796)	(35.3)%
	99,257	57.3%	151,357	68.9%	(52,100)	(34.4)%
Gross profit	73,880	42.7%	68,283	31.1%	5,597	8.2%
<b>Operating expenses:</b>						
Selling and administrative expenses	47,579	27.5%	53,403	24.3%	(5,824)	(10.9)%
Depreciation and amortization	8,691	5.0%	9,357	4.3%	(666)	(7.1)%
Other operating costs	26,292	15.2%	30,831	14.0%	(4,539)	(14.7)%
Total operating expenses	82,562	47.7%	93,591	42.6%	(11,029)	(11.8)%
Loss from operations	(8,682)	(5.0)%	(25,308)	(11.5)%	16,626	65.7%
Interest income	1	0.0%	182	0.1%	(181)	(99.5)%
Other income (expense), net	(175)	(0.1)%	822	0.4%	(997)	(121.3)%
Loss before income taxes	(8,856)	(5.1)%	(24,304)	(11.1)%	15,448	63.6%
Benefit for income taxes	982	0.6%	4,785	2.2%	(3,803)	(79.5)%
Net loss	\$ (7,874)	(4.5)%	\$ (19,519)	(8.9)%	\$ 11,645	59.7%

Consolidated net sales shipped to customers by location for the three months ended September 30, 2010 and 2009 were as follows (in millions, except percentages):

Net Sales in Dollars and as a Percentage of Consolidated Net Sales

Country	2010		2009	
United States	\$ 23.9	43.5%	\$ 34.0	47.7%
Japan	8.9	16.2%	9.9	13.9%
Republic of Korea	5.1	9.3%	6.9	9.7%
Canada	4.6	8.4%	5.8	8.1%
Australia	4.7	8.6%	5.7	8.0%
South Africa	3.0	5.5%	3.9	5.5%
Taiwan	1.4	2.6%	1.4	2.0%
New Zealand	0.7	1.3%	1.1	1.5%
Germany	0.6	1.1%	0.9	1.3%

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United Kingdom	0.4	0.7%	0.8	1.0%
Denmark	0.1	0.2%	0.5	0.7%
Singapore	0.5	0.9%	0.4	0.6%
Austria(1)	0.2	0.3%	—	—
Norway(1)	0.5	0.9%	—	—
The Netherlands(1)	0.2	0.3%	—	—
Sweden(1)	0.1	0.2%	—	—
Totals	\$ 54.9	100%	\$ 71.3	100%

(1) Austria, Norway, the Netherlands, and Sweden began operations in September 2009, and had a combined total net sales of \$0.1 million for the period ended September 30, 2009.

Consolidated net sales shipped to customers by location for the nine months ended September 30, 2010 and 2009 were as follows (in millions, except percentages):

Country	2010		2009	
	\$	%	\$	%
United States	77.7	44.9%	109.7	49.9%
Japan	25.8	14.9%	31.4	14.3%
Republic of Korea	16.2	9.4%	19.2	8.8%
Canada	14.0	8.1%	17.5	8.0%
Australia	14.8	8.6%	16.7	7.6%
South Africa	9.0	5.2%	9.4	4.2%
Taiwan	5.0	2.9%	4.8	2.2%
New Zealand	2.5	1.4%	3.3	1.5%
Germany	1.8	1.0%	2.6	1.2%
United Kingdom	1.6	0.9%	2.5	1.1%
Denmark	0.4	0.2%	1.5	0.7%
Singapore	1.5	0.9%	1.0	0.5%
Austria(1)	0.9	0.5%	—	—
Norway(1)	1.2	0.7%	—	—
The Netherlands(1)	0.4	0.2%	—	—
Sweden(1)	0.3	0.2%	—	—
Totals	\$ 173.1	100%	\$ 219.6	100%

(1) Austria, Norway, the Netherlands, and Sweden began operations in September 2009, and had a combined total net sales of \$0.1 million for the period ended September 30, 2009.

## Net Sales

For the three and nine months ended September 30, 2010, our operations outside of the United States accounted for approximately 56.5% and 55.1%, respectively, of our consolidated net sales, whereas in the same period in 2009, our operations outside of the United States accounted for approximately 52.3% and 50.1%, respectively, of our consolidated net sales.

Consolidated net sales for the three months ended September 30, 2010 decreased by \$16.4 million, or 23.0%, as compared to the same period in 2009. This change in consolidated net sales was comprised of a decrease in domestic sales of \$10.1 million and a decrease in international sales of \$6.3 million.

Consolidated net sales for the nine months ended September 30, 2010 decreased by \$46.5 million, or 21.2%, as compared to the same period in 2009. This change in consolidated net sales was comprised of a decrease in domestic sales of \$32.0 million and a decrease of international sales of \$14.5 million.

The global financial crisis continues to be a major factor for the decline in both our domestic and international sales and recruiting. Sales in domestic and international markets have also been adversely affected as a result of direct competition.

Fluctuation in foreign currency exchange rates had an overall favorable impact on our net sales of approximately \$1.5 million and \$7.4 million for the three and nine months ended September 30, 2010, respectively. The net sales impact is calculated as the difference between (1) the current period's net sales in USD and (2) the current period's net sales in local currencies converted to USD by applying average exchange rates for the same periods ended September 30,

2009.

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Net sales by country in local currency for the three and nine months ended September 30, 2010 and 2009 are as follows (in millions, except percentages):

Country	Currency	Three months		Change	
		2010	2009	Local currency	Percentage
Australia and Singapore	AUD	5.8	7.4	(1.6)	(21.6)%
Austria(1), Germany, the Netherlands(1)	EUR	0.7	0.6	0.1	16.7%
Denmark	DKK	0.6	2.4	(1.8)	(75.0)%
Japan	JPY	753.5	921.0	(167.5)	(18.2)%
Republic of Korea	KRW	6,032.8	8,540.1	(2,507.3)	(29.4)%
New Zealand	NZD	1.0	1.6	(0.6)	(37.5)%
Norway(1)	NOK	2.1	0.2	1.9	950.0%
South Africa	ZAR	21.8	30.2	(8.4)	(27.8)%
Sweden(1)	SEK	0.7	0.1	0.6	600.0%
Taiwan	TWD	43.5	46.1	(2.6)	(5.6)%
United Kingdom	GBP	0.4	0.5	(0.1)	(20.0)%

(1) Austria, the Netherlands, Norway, and Sweden began operations in September 2009. Austria and the Netherlands had net sales of less than \$.01 million Euros for the period ended September 30, 2009.

Country	Currency	Nine months		Change	
		2010	2009	Local currency	Percentage
Australia and Singapore	AUD	18.2	23.7	(5.5)	(23.2)%
Austria(1), Germany, the Netherlands(1)	EUR	2.2	1.9	0.3	15.8%
Denmark	DKK	2.4	7.6	(5.2)	(68.4)%
Japan	JPY	2,279.9	2,945.3	(665.4)	(22.6)%
Republic of Korea	KRW	18,849.1	25,012.7	(6,163.6)	(24.6)%
New Zealand	NZD	3.5	5.5	(2.0)	(36.4)%
Norway(1)	NOK	5.8	0.2	5.6	2,800.0%
South Africa	ZAR	67.2	80.7	(13.5)	(16.7)%
Sweden(1)	SEK	2.1	0.1	2.0	2,000.0%
Taiwan	TWD	157.8	159.0	(1.2)	(0.8)%
United Kingdom	GBP	1.3	1.6	(0.3)	(18.8)%

(1) Austria, the Netherlands, Norway, and Sweden began operations in September 2009. Austria and the Netherlands had net sales of less than \$.01 million Euros for the period ended September 30, 2009.

Our total sales and sales mix can be influenced by any of the following:

- changes in our sales prices;

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- changes in consumer demand;
  - changes in the number of independent associates and members;
    - changes in competitors' products;
    - changes in economic conditions;
      - changes in regulations;
  - announcements of new scientific studies and breakthroughs;
    - introduction of new products;
    - discontinuation of existing products;
      - adverse publicity;
  - changes in our commissions and incentives programs;
    - direct competition; and
  - fluctuations in foreign currency exchange rates.
-

Our sales mix for the three and nine months ended September 30, was as follows (in millions, except percentages):

	Three Months		Change	
	2010	2009	Dollar	Percentage
Product sales	\$ 45.5	\$ 52.3	\$ (6.8)	(13.0)%
Pack sales	7.0	15.5	(8.5)	(54.8)%
Other, including freight	2.4	3.5	(1.1)	(31.4)%
Total net sales	\$ 54.9	\$ 71.3	\$ (16.4)	(23.0)%

	Nine Months		Change	
	2010	2009	Dollar	Percentage
Product sales	\$ 140.8	\$ 159.1	\$ (18.3)	(11.5)%
Pack sales	25.1	50.2	(25.1)	(50.0)%
Other, including freight	7.2	10.3	(3.1)	(30.1)%
Total net sales	\$ 173.1	\$ 219.6	\$ (46.5)	(21.2)%

For the three and nine months ended September 30, 2010 compared to the same periods in 2009, the decrease in our pack sales was primarily a result of fewer new associates. Pack sales generally correlate to new independent associates who purchase starter packs and continuing independent associates who purchase upgrade or renewal packs. However, there is no direct correlation between product sales and the number of new and continuing independent associates and members because independent associates and members utilize products at different volumes.

#### Product Sales

In order to evaluate new product sales as compared to existing product sales, we calculate our product sales that are either (i) newly developed products, or (ii) existing products that are newly introduced to a country within the last twelve months as of quarter end. We then compare this total to our existing product line, or products that have been available in a country over twelve months. This analysis is a valuable tool to help determine the success of our new products, as well as the timely expansion of our existing products.

Product sales for the three months ended September 30, 2010 decreased \$6.8 million, or 13.0%, as compared to the same period in 2009. This change in product sales was comprised of a decrease of new product sales of \$1.7 million and a decrease of existing product sales of \$5.1 million.

Product sales for the nine months ended September 30, 2010 decreased \$18.3 million, or 11.5%, as compared to the same period in 2009. This change in product sales was comprised of a decrease of new product sales of \$5.0 million and a decrease of existing product sales of \$13.3 million.

We implemented a 2-5% price increase in most countries in late January 2010. We believe the decrease in product sales for the third quarter ended September 30, 2010 as compared to the same period in 2009 was largely due to several factors, including macro-economics and competition, which directly impacts our company.

We have introduced the following new products since September 30, 2009:

- Simply Delicious™ Snack Bars in the United States and Canada;
- Essential Source™ Omega 3 in the United States and all of our international markets;
- PhytoBurst® Nutritional Chews in the United States, Canada, Japan, Taiwan, and South Africa;
- Health Solutions Starter packs in several international markets;
  - GlycoSlim® drink mix in certain international markets;
  - BounceBack® capsules in Japan and Taiwan;
  - GI-Pro Balance™ powder in South Korea;
  - Mannatech LIFT™ products in United States and Canada;
- Immunostart® tablets in the United Kingdom, Germany, Denmark, New Zealand, Australia, Austria, the Netherlands, Norway, Sweden;
  - Various promotional packages in the United States and international markets; and
  - Various Optimal Health, Weight and Fitness products in Austria, the Netherlands, Norway and Sweden.

#### Pack Sales

Packs may be purchased by our independent associates who wish to build a Mannatech business. These packs are offered to our independent associates at a discount from published retail prices. There are several pack options available to our independent associates. In certain markets, pack sales are concluded during the associate registration process and can provide new independent associates with valuable training and promotional materials, as well as products for resale to retail customers, demonstration purposes, and personal consumption. Business-building independent associates can also choose to purchase an upgrade pack, which provides the associate with additional promotional materials and eligibility for additional commissions and incentives. Many of our business-building independent associates also choose to purchase renewal packs to satisfy annual renewal requirements to continue to earn various commissions.

Pack sales associated with the number of independent associates and members can be further analyzed as follows, for the three and nine months ended September 30 (in millions, except percentages):

	2010		2009		Change	
	Dollar	Percentage	Dollar	Percentage	Dollar	Percentage
New	\$ 5.1		\$ 11.0		\$ (5.9)	(53.6)%
Continuing	1.9		4.5		(2.6)	(57.8)%
Total	\$ 7.0		\$ 15.5		\$ (8.5)	(54.8)%

#### Nine Months

Change



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	2010	2009	Dollar	Percentage
New	\$ 17.2	\$ 32.1	\$ (14.9)	(46.4)%
Continuing	7.9	18.1	(10.2)	(56.4)%
Total	\$ 25.1	\$ 50.2	\$ (25.1)	(50.0)%

Total pack sales for the three months ended September 30, 2010 decreased by \$8.5 million, or 54.8%, as compared to the same period in 2009. This reduction in pack sales was comprised of a decrease of \$5.9 million related to fewer new independent associates purchasing starter packs, and a decrease of \$2.6 million related to a decline in the number of continuing associates purchasing renewal and upgrade packs.

Total pack sales for the nine months ended September 30, 2010 decreased by \$25.1 million, or 50.0%, as compared to the same period in 2009. This reduction in pack sales was comprised of a decrease of \$14.9 million related to fewer new independent associates purchasing starter packs, and a decrease of \$10.2 million related to a decline in the number of continuing associates purchasing renewal and upgrade packs.

The number of new and continuing independent associates and members who purchased our packs or products during the twelve months ended September 30, 2010 and 2009 were as follows:

	2010		2009	
New	93,000	22.0%	151,000	28.3%
Continuing	329,000	78.0%	383,000	71.7%
Total	422,000	100%	534,000	100%

There was an overall decrease of 112,000 associates and members for the twelve months ended September 30, 2010. We are experiencing increased competition in certain domestic and international markets where competitors have launched operations, and in some cases have attracted some of our independent associate field leaders. We will continue to address new independent associate recruiting and associate retainment through additional incentives, new promotional support materials, and cause-related charitable activities.

During 2009 and 2010, we took the following actions to help increase the number of, and retain our existing, independent associates and members:

- registered our most popular products with the appropriate regulatory agencies in all countries of operations;
  - focused on new product development;
  - explored new international markets;
  - launched an aggressive marketing and educational campaign;
  - strengthened compliance initiatives;
- concentrated on publishing results of research studies and clinical trials related to our products;
  - initiated additional incentives;
  - explored new advertising and educational tools to broaden name recognition;
  - implemented changes to our global associate career and compensation plan;
    - introduced new products in many of our global markets;
- introduced the \$499 Premium-All-Star pack into United States, Canada, and South Africa in January 2009;
  - introduced similar All-Star Packs into all other markets in January 2010;
  - expanded into four new international markets in early fall of 2009;
    - revamped our website to increase user-friendliness; and

- launched three new effective online tools (MannacastSM, which includes StoryCastTM, Mannapages®, and Success Tracker) in the United States and Canada that offer support to our independent associates in managing and expanding their business.

#### Other Sales

Other sales consisted of (i) sales of promotional materials; (ii) training and event registration fees; (iii) monthly fees collected for the SuccessTracker tool, a customized electronic business-building and educational materials database for our independent associates that helps stimulate product sales and provide business management; (iv) freight revenue charged to our independent associates and members; and (v) a reserve for estimated sales refunds and returns.

Other sales for the three months ended September 30, 2010 decreased by \$1.1 million to \$2.4 million as compared to \$3.5 million for the same period in 2009. Other sales for the nine months ended September 30, 2010 decreased by \$3.1 million to \$7.2 million as compared to \$10.3 million for the same period in 2009. The decrease in both periods was primarily due to a decrease in freight fees for product and pack shipments.

#### Gross Profit

Gross profit for the three months ended September 30, 2010 decreased by \$0.3 million, or 1.1%, to \$23.8 million as compared to \$24.1 million for the same period in 2009. Gross profit as a percentage of net sales increased to 43.4% as compared to 33.8% for the same period in 2009. The increase in gross profit as a percentage of net sales was due to lower commissions and incentives for the period.

Gross profit for the nine months ended September 30, 2010 increased by \$5.6 million, or 8.2%, to \$73.9 million as compared to \$68.3 million for the same period in 2009. Gross profit as a percentage of net sales increased to 42.7% as compared to 31.1% for the same period in 2009. The increase in gross profit for the nine months ended September 30, 2010 compared to the same period in 2009 was primarily due to the modification of our bonus structure associated with the \$499 Premium-All Star pack. This alteration in the bonus structure allowed commission and incentive rates to return to more historical levels.

Cost of sales during the three months ended September 30, 2010 decreased by \$4.0 million, or 33.5%, to \$7.9 million as compared to \$11.9 million for the same period in 2009. Cost of sales as a percentage of net sales for the three months ended September 30, 2010 decreased to 14.4% as compared to 16.7% for the same period in 2009.

Cost of sales during the nine months ended September 30, 2010 decreased \$11.3 million, or 31.4%, to \$24.6 million as compared to \$35.9 million for the same period in 2009. Cost of sales as a percentage of net sales for the nine months ended September 30, 2010 decreased to 14.2 % as compared to 16.4% for the same period in 2009.

The decrease in cost of sales, and cost of sales as a percentage of net sales, for the three and nine months ended September 30, 2010 compared to the same periods in 2009 was primarily due to improved economics associated with pack sales, including a reduction in the cost of packs and modification of bonus and pack components, as well as a decrease in the cost of finished products sold.

Commission costs for the three months ended September 30, 2010 decreased by 34.6%, or \$11.9 million, to \$22.5 million as compared to \$34.4 million for the same period in 2009. Commissions as a percentage of net sales for the three months ended September 30, 2010 decreased to 41.0% from 48.2% for the same period in 2009.

Commission costs for the nine months ended September 30, 2010 decreased by 33.6%, or \$36.2 million, to \$71.6 million as compared to \$107.8 million for the same period in 2009. Commissions as a percentage of net sales for the nine months ended September 30, 2010 decreased to 41.4% from 49.1% for the same period in 2009.

Incentive costs for the three months ended September 30, 2010 decreased by 33.3%, or \$0.3 million, to \$0.6 million as compared to \$0.9 million for the same period in 2009. The costs of incentives as a percentage of net sales for the three months ended September 30, 2010 decreased to 1.1% from 1.3% for the same period in 2009.

Incentive costs for the nine months ended September 30, 2010 decreased by 60.5%, or \$4.6 million, to \$3.0 million as compared to \$7.6 million for the same period in 2009. The costs of incentives as a percentage of net sales for the nine months ended September 30, 2010 decreased to 1.7% from 3.5 % for the same period in 2009.

The decrease in commission and incentive costs for the three and nine months ended September 30, 2010 compared to the same periods in 2009 was due to modification of our pack bonus structure and commission rates, as well as a

decrease in the number of new and continuing independent associates and members who purchased our packs or products. As a result, there was a decrease in the number of independent associates who qualified for the annual incentives to 715 as compared to 2,374 in 2009. The alteration in the bonus structure allowed commission and incentive rates to return to more historical levels.

## Selling and Administrative Expenses

Selling and administrative expenses include a combination of both fixed and variable expenses. These expenses consist of compensation and benefits for employees, temporary and contract labor, outbound shipping and freight expenses, and marketing-related expenses, such as monthly magazine development costs and costs related to hosting our corporate-sponsored events.

Selling and administrative expenses for the three months ended September 30, 2010 decreased by \$1.9 million, or 10.9%, to \$15.8 million as compared to \$17.8 million for the same period in 2009. The decrease in selling and administrative expenses consisted primarily of a \$1.3 million decrease in contract labor, payroll and payroll-related costs and a \$0.8 million decrease in freight costs, partially offset by an increase of \$0.2 million in marketing costs and costs related to corporate-sponsored events. As a percentage of net sales, selling and administrative expenses increased to 28.8% from 24.9% for the same period in 2009.

Selling and administrative expenses for the nine months ended September 30, 2010 decreased by \$5.8 million, or 10.9%, to \$47.6 million as compared to \$53.4 million for the same period in 2009. The decrease in selling and administrative expenses consisted primarily of a \$3.3 million decrease in contract labor, payroll and payroll-related costs, a \$0.7 million decrease in marketing costs and costs related to corporate-sponsored events, and a \$1.8 million decrease in freight costs. As a percentage of net sales, selling and administrative expenses increased to 27.5% from 24.3% for the same period in 2009.

## Depreciation and Amortization Expense

Depreciation and amortization expense for the three months ended September 30, 2010 decreased by 10.1%, or \$0.3 million, to \$2.8 million as compared to \$3.1 million for the same period in 2009. As a percentage of net sales, depreciation and amortization expense increased to 5.1% from 4.3% for the same period in 2009.

Depreciation and amortization expense for the nine months ended September 30, 2010 decreased by 7.1%, or \$0.7 million, to \$8.7 million as compared to \$9.4 million for the same period in 2009. As a percentage of net sales, depreciation and amortization expense increased slightly to 5.0% from 4.3% for the same period in 2009.

## Other Operating Costs

Other operating costs generally include travel, accounting/legal/consulting fees, royalties, credit card processing fees, banking fees, off-site storage fees, utilities, and other miscellaneous operating expenses. Generally, changes in other operating costs are associated with changes in our net sales.

Other operating costs for the three months ended September 30, 2010 decreased by \$2.9 million, or 24.8%, to \$8.9 million as compared to \$11.8 million for the same period in 2009. This decrease was due to a \$1.5 million reduction in legal expenses, a \$0.4 million reduction in credit card fees, a \$0.3 million reduction in accounting/consulting fees, a \$0.2 million reduction in travel expenses, a \$0.2 million reduction in research and development costs, a \$0.2 million in miscellaneous operating costs, such as mailing services, office supplies, telephone, insurance, and lease/rental costs, and a \$0.1 million in repairs and maintenance fees. As a percentage of net sales, other operating costs decreased slightly to 16.2% from 16.6% for the same period in 2009.

Other operating costs for the nine months ended September 30, 2010 decreased by \$4.5 million, or 14.7%, to \$26.3 million as compared to \$30.8 million for the same period in 2009. This decrease was due to a \$1.2 million reduction in credit card fees, \$1.2 million reduction in accounting/consulting fees, a \$0.7 million reduction in legal fees, a \$0.5

million reduction in travel expenses, a \$0.5 million reduction in miscellaneous expenses, a \$0.3 million reduction in research and development costs, and a \$0.1 million reduction in repairs and maintenance. As a percentage of net sales, other operating costs increased to 15.2% from 14.0% for the same period in 2009.

Other Income (Expense), Net

Other income (expense), net primarily consists of foreign currency gains and losses related to translating our foreign subsidiaries' assets, liabilities, revenues, and expenses to the United States dollar and revaluing monetary accounts in United States, Switzerland, Japan, and the Republic of Korea, using current and weighted-average currency exchange rates. Net foreign currency transaction gains and losses are the result of the United States dollar fluctuating in value against foreign currencies.

Other income, net for the three months ended September 30, 2010 was \$0.4 million, as compared to \$0.8 million for the same period in 2009.

Other expense, net for the nine months ended September 30, 2010 was \$0.2 million, as compared to other income, net of \$0.8 million for the same period in 2009.

(Provision) Benefit for Income Taxes

(Provision) benefit for income taxes includes current and deferred income taxes for both our domestic and foreign operations. Our statutory income tax rates by jurisdiction are as follows, for the three and nine months ended September 30:

Country	2010	2009
Australia	30.0%	30.0%
Canada	30.0%	33.0%
Denmark	25.0%	25.0%
Japan	42.0%	42.0%
Mexico	30.0%	—
Norway	28.0%	28.0%
Republic of Korea	22.0%	24.2%
Singapore	17.0%	17.0%
South Africa	28.0%	28.0%
Sweden	26.3%	26.3%
Switzerland	16.2%	16.2%
Taiwan	17.0%	25.0%
United Kingdom	28.0%	28.0%
United States	37.5%	37.5%

Income from our international operations is subject to taxation in the countries in which we operate. Although we may receive foreign income tax credits that would reduce the total amount of income taxes owed in the United States, we may not be able to fully utilize our foreign income tax credits in the United States.

We use the recognition and measurement provisions of FASB ASC Topic 740, Income Taxes, to account for income taxes. The provisions of the Income Tax Topic require a company to record a valuation allowance when the “more likely than not” criterion for realizing net deferred tax assets cannot be met. Furthermore, the weight given to the potential effect of such evidence should be commensurate with the extent to which it can be objectively verified. As a result, we reviewed the operating results, as well as all of the positive and negative evidence related to realization of such deferred tax assets to evaluate the need for a valuation allowance in each tax jurisdiction. As of September 30, 2010 and December 31, 2009, we maintained our valuation allowance for deferred tax assets totaling \$3.6 million and \$2.3 million, respectively, as we believe the “more likely than not” criterion for recognition and realization purposes, as defined in FASB ASC Topic 740, cannot be met.



Country	September 30, 2010	December 31, 2009
Mexico	\$ 0.6	\$ —
Norway	0.1	0.0
Sweden	0.1	0.0
Switzerland	0.6	0.3
Taiwan	0.9	0.9
United States	1.3	1.1
Total	\$ 3.6	\$ 2.3

For the three months ended September 30, 2010, the Company recognized a tax benefit of approximately \$1.9 million. This was the result of changes to management's estimates for 2010 annual operating results, including the mix of income between tax jurisdictions, the change in the valuation allowances associated with certain deferred tax assets, and the change in reserves related to uncertain income tax positions. For the nine months ended September 30, 2010 the Company recognized a \$0.9 million tax benefit. For the three and nine months ended September 30, 2009, the Company's effective tax rate was (20.0)% and 19.7%, respectively. For the three and nine months ended September 30, 2010 and 2009, the Company's effective income tax rate was determined based on the estimated annual effective income tax rate.

The effective tax rate for the nine months ended September 30, 2010 was lower than what would have been expected if the federal statutory rate were applied to income before taxes. Items reducing the effective income tax rate included reductions due to changes to management's estimates for 2010 annual operating results, including the mix of income between tax jurisdictions, the change in the valuation allowances associated with certain deferred tax assets, and the change in reserves related to uncertain income tax positions. The effective tax rate for the three months ended September 30, 2010 was higher than what would have been expected if the federal statutory rate were applied to income before taxes due to changes in management's estimates during the quarter for 2010 annual operating results, including the mix of income between tax jurisdictions.

## LIQUIDITY AND CAPITAL RESOURCES

Our principal use of cash is to pay for operating expenses, including commissions and incentives, capital assets, inventory purchases, international expansion, and to pay quarterly cash dividends. In August 2009, the quarterly cash dividend was suspended and remained suspended as of September 30, 2010. At September 30, 2010, we had \$21.7 million in cash and cash equivalents that can be used, along with normal cash flows from operations, to fund any unanticipated shortfalls in future cash flows. Although our cash has been impacted by net losses for most of 2009 and 2010, we saw our costs, particularly commissions and incentives, return to more historical levels. Although we are contemplating alternative liquidity sources, remaining at these historical cost levels will be a key factor in our ability to generate sufficient cash from operations. In addition, in April 2010, we received a federal income tax refund of \$8.1 million.

### Cash and Cash Equivalents and Investments

As of September 30, 2010, our cash and cash equivalents increased by 24.8%, or \$4.3 million, to \$21.7 million from \$17.4 million as of December 31, 2009. The increase in cash and cash equivalents is related to the federal income tax refund of \$8.1 million we received in April 2010 which is offset by the current period loss, adjusted for noncash items, purchases of property and equipment, and decreases of payables due to the timing of payments.

## Working Capital

Working capital represents total current assets less total current liabilities. At September 30, 2010, our working capital increased by \$0.6 million, or 2.8%, to \$22.4 million from \$21.8 million at December 31, 2009. The change in working capital primarily relates to an increase in cash and cash equivalents, a decrease in short-term tax accounts, a decrease in inventories, partially offset by a decrease in operating liabilities.

## Net Cash Flows

Our net consolidated cash flows consisted of the following, for the nine months ended September 30 (in millions):

Provided by (used in):	2010	2009
Operating activities	\$ 4.9	\$ (4.7)
Investing activities	\$ 0.2	\$ (2.1)
Financing activities	\$ (0.9)	\$ (1.3)

## Operating Activities

For the nine months ended September 30, 2010, our operating activities provided cash of \$4.9 million compared to using cash of \$4.7 million for the same period in 2009. This increase in cash is due to the \$8.1 million federal income tax refund received in April 2010, as well as the significant decrease in operating costs that we achieved through establishing a culture of expense control and accountability.

We entered into an Investment Agreement with the Investor on September 16, 2010. The Investor committed to purchase, subject to certain restrictions and conditions, up to \$10 million of our common stock, over a period of 36 months from the first trading following the effectiveness of the registration statement, which was October 28, 2010. We may draw funds from the Equity Line by selling shares of common stock to the Investor from time to time. We will not receive any proceeds from the resale of these shares of common stock offered by the Investor. We will, however, receive proceeds from the sale of shares to the Investor pursuant to the Equity Line. The proceeds will be used for general working capital needs and for other general corporate purposes.

We expect that our net operating cash flows in 2010 will be sufficient to fund our current operations. There can be no assurance, however, that we will continue to generate cash flows at or above current levels. Certain events, such as the uncertainty of the worldwide economic environment, could impact our available cash or our ability to generate cash flows from operations.

## Investing Activities

For the nine months ended September 30, 2010, our net investing activities provided cash of \$0.2 million compared to using cash of \$2.1 million for the same period of 2009. For the nine months ended September 30, 2010, we used cash of \$1.5 million to purchase capital assets as compared to purchasing \$2.5 million in capital assets for the same period in 2009. In 2010, we had a decrease in restricted cash of \$1.7 million as compared to a decrease of \$0.4 million for the same period in 2009.

## Financing Activities

For the nine months ended September 30, 2010, we used cash of \$0.9 million for repayment of capital lease obligations as compared to \$1.1 million to fund the payment of cash dividends to our shareholders for the same period in 2009. In August 2009, the quarterly cash dividend was suspended. See “Risk Factors—We are not required to pay dividends, and our Board of Directors could decide not to declare a dividend or could reduce the amount of the dividend at any time” in item 1A of our annual report on Form 10-K for the year ended December 31, 2009, for further discussion related to future payment of dividends.

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Our quarterly cash dividends were \$0.02 per share for the first and second quarters of 2009. In 2009, we declared and paid the following dividends:

Declared date	Date of record	Date paid	Total amount of dividends	Dollar amount paid per common share
May 20, 2009	June 3, 2009	June 29, 2009	\$ 0.5million	\$ 0.02
February 18, 2009	March 9, 2009	March 26, 2009	\$ 0.5million	\$ 0.02

## General Liquidity and Cash Flows

We believe our existing liquidity and cash flows from operations are adequate to fund our normal expected future business operations and possible international expansion costs for the next 12 to 24 months. However, if our existing capital resources or cash flows become insufficient to meet current business plans, projections, and existing capital requirements, we may be required to raise additional funds, which may not be available on favorable terms, if at all.

Contractual Obligations. The following summarizes our future commitments and obligations associated with various agreements and contracts as of September 30, 2010, for the years ending December 31 (in thousands):

	Remaining							
	2010	2011	2012	2013	2014	2015	Thereafter	Total
Capital lease obligations	\$ 440	\$ 1,154	\$ 711	\$ 344	\$ 239	\$ 1	\$ —	\$ 2,889
Purchase obligations(1)(2)	8,766	4,956	2,535	1,050	1,050	1,050	—	19,407
Operating leases	799	2,174	2,036	1,572	897	815	955	9,248
Post-employment royalty	152	492	492	492	369	—	—	1,997
Employment agreements	584	1,379	—	—	—	—	—	1,963
Total commitments and obligations	\$ 10,741	\$ 10,155	\$ 5,774	\$ 3,458	\$ 2,555	\$ 1,866	\$ 955	\$ 35,504

(1) Purchase obligations for the years 2010, 2011, and 2012 include \$4.7 million, \$2.1 million, and \$1.5 million, respectively, of purchase commitments under a contract terminated by the Company for an asserted breach. Pursuant to the terms of the contract, we are engaged in the arbitration process with the supplier.

(2) Purchase obligations for the remainder of 2010 include \$0.2 million of purchase commitments under a contract terminated effective December 31, 2010, by the supplier. The Company is negotiating a new agreement with this supplier.

We have maintained purchase commitments with certain raw material suppliers to purchase minimum quantities and to ensure exclusivity of our raw materials and the proprietary nature of our products. Currently, we have four supply agreements that require minimum purchase commitments. We terminated one of these contracts for an asserted breach in 2009 and are now engaged in the arbitration process with the supplier. We also maintain other supply agreements and manufacturing agreements to protect our products, regulate product costs, and help ensure quality control standards. These agreements do not require us to purchase any set minimums. We have no present commitments or agreements with respect to acquisitions or purchases of any manufacturing facilities; however, management from time to time explores the possibility of the benefits of purchasing a raw material manufacturing facility to help control costs of our raw materials and help ensure quality control standards.

## Off-Balance Sheet Arrangements

We do not have any special-purpose entity arrangements, nor do we have any off-balance sheet arrangements.

## CRITICAL ACCOUNTING POLICIES AND ESTIMATES

Our consolidated financial statements are prepared in accordance with accounting principles generally accepted in the United States of America ("GAAP"). The application of GAAP requires us to make estimates and assumptions that

affect the reported values of assets and liabilities at the date of our financial statements, the reported amounts of revenues and expenses during the reporting period, and the related disclosures of contingent assets and liabilities. We use estimates throughout our financial statements, which are influenced by management's judgment and uncertainties. Our estimates are based on historical trends, industry standards, and various other assumptions that we believe are applicable and reasonable under the circumstances at the time the consolidated financial statements are prepared. Our Audit Committee reviews our critical accounting policies and estimates. We continually evaluate and review our policies related to the portrayal of our consolidated financial position and consolidated results of operations that require the application of significant judgment by our management. We also analyze the need for certain estimates, including the need for such items as allowance for doubtful accounts, inventory reserves, long-lived fixed assets and capitalization of internal-use software development costs, reserve for uncertain income tax positions and tax valuation allowances, revenue recognition, sales returns, and deferred revenues, accounting for stock-based compensation, and contingencies and litigation. Historically, actual results have not materially deviated from our estimates. However, we caution readers that actual results could differ from our estimates and assumptions applied in the preparation of our consolidated financial statements. If circumstances change relating to the various assumptions or conditions used in our estimates, we could experience an adverse effect on our financial position, results of operations, and cash flows. We have identified the following applicable critical accounting policies and estimates as of September 30, 2010:

## Inventory Reserves

Inventory consists of raw materials, finished goods, and promotional materials that are stated at the lower of cost (using standard costs that approximate average costs) or market. We record the amounts charged by vendors as the costs of inventory. Typically, the net realizable value of our inventory is higher than the aggregate cost. Determination of net realizable value can be complex and, therefore, requires a high degree of judgment. In order for management to make the appropriate determination of net realizable value, the following items are considered: inventory turnover statistics, current selling prices, seasonality factors, consumer demand, regulatory changes, competitive pricing, and performance of similar products. If we determine the carrying value of inventory is in excess of estimated net realizable value, we write down the value of inventory to the estimated net realizable value.

We also review inventory for obsolescence in a similar manner and any inventory identified as obsolete is reserved or written off. Our determination of obsolescence is based on assumptions about the demand for our products, product expiration dates, estimated future sales, and general future plans. We monitor actual sales compared to original projections, and if actual sales are less favorable than those originally projected by us, we record an additional inventory reserve or write-down. Historically, our estimates have been close to our actual reported amounts. However, if our estimates regarding fair market value or obsolescence are inaccurate or consumer demand for our products changes in an unforeseen manner, we may be exposed to additional material losses or gains in excess of our established estimated inventory reserves.

## Long Lived Fixed Assets and Capitalization of Software Development Costs

In addition to capitalizing long lived fixed asset costs, we also capitalize costs associated with internally-developed software projects (collectively “fixed assets”) and amortize such costs over the estimated useful lives of such fixed assets. Fixed assets are carried at cost, less accumulated depreciation computed using the straight-line method over the assets’ estimated useful lives. Leasehold improvements are amortized over the shorter of the remaining lease terms or the estimated useful lives of the improvements. Expenditures for maintenance and repairs are charged to operations as incurred. If a fixed asset is sold or otherwise retired or disposed of, the cost of the fixed asset and the related accumulated depreciation or amortization is written off and any resulting gain or loss is recorded in other operating costs in our consolidated statement of operations.

We review our fixed assets for impairment whenever an event or change in circumstances indicates the carrying amount of an asset or group of assets may not be recoverable, such as plans to dispose of an asset before the end of its previously estimated useful life. Our impairment review includes a comparison of future projected cash flows generated by the asset, or group of assets, with its associated net carrying value. If the net carrying value of the asset or group of assets exceeds expected cash flows (undiscounted and without interest charges), an impairment loss is recognized to the extent the carrying amount exceeds the fair value. The fair value is determined by calculating the discounted expected future cash flows using an estimated risk-free rate of interest. Any identified impairment losses are recorded in the period in which the impairment occurs. The carrying value of the fixed asset is adjusted to the new carrying value and any subsequent increases in fair value of the fixed asset are not recorded. In addition, if we determine the estimated remaining useful life of the asset should be reduced from our original estimate, at that time the periodic depreciation expense is adjusted prospectively, based on the new remaining useful life of the fixed asset.

The impairment calculation requires us to apply judgment and estimates concerning future cash flows, strategic plans, useful lives, and discount rates. If actual results are not consistent with our estimates and assumptions, we may be exposed to an additional impairment charge, which could be material to our results of operations. In addition, if accounting standards change, or if fixed assets become obsolete, we may be required to write off any unamortized costs of fixed assets; or if estimated useful lives change, we would be required to accelerate depreciation or amortization periods and recognize additional depreciation expense in our consolidated statement of operations.





Historically, our estimates and assumptions related to the carrying value and the estimated useful lives of our fixed assets have not materially deviated from actual results. As of September 30, 2010, the estimated useful lives and net carrying values of fixed assets were as follows:

	Estimated useful life	Net carrying value at September 30, 2010
Office furniture and equipment	5 to 7 years	\$ 2.0million
Computer hardware	3 to 5 years	4.0million
Computer software	3 to 5 years	10.7million
Automobiles	3 to 5 years	0.1million
Leasehold improvements	2 to 10 years(1)	3.2million
Construction in progress	2 to 10 years(2)	1.5million
Total net carrying value at September 30, 2010		\$ 21.5million

(1) We amortize leasehold improvements over the shorter of the useful estimated life of the leased asset or the lease term.

(2) Construction in progress includes leasehold improvements and internally-developed software costs. Once placed in service, leasehold improvements will be amortized over the shorter of an asset's useful life or the remaining lease term. Once the internally-developed software is placed in service, it will be amortized over three to five years.

The net carrying costs of fixed assets and construction in progress are exposed to impairment losses if our assumptions and estimates of their carrying values change, there is a change in estimated future cash flow, or there is a change in the estimated useful life of the fixed asset. We determined that no impairment indicators existed for the nine months ended September 30, 2010.

#### Uncertain Income Tax Positions and Tax Valuation Allowances

As of September 30, 2010, we recorded \$2.1 million in other long-term liabilities on our consolidated balance sheet related to uncertain income tax positions. As required by FASB ASC Topic 740, Income Taxes, we use judgments and make estimates and assumptions related to evaluating the probability of uncertain income tax positions. We base our estimates and assumptions on the potential liability related to an assessment of whether the income tax position will "more likely than not" be sustained in an income tax audit. We are also subject to periodic audits from multiple domestic and foreign tax authorities related to income tax and other forms of taxation. These audits examine our tax positions, timing of income and deductions, and allocation procedures across multiple jurisdictions. As part of our evaluation of these tax issues, we establish reserves in our consolidated financial statements based on our estimate of current probable tax exposures. Depending on the nature of the tax issue, we could be subject to audit over several years. Therefore, our estimated reserve balances and liability related to uncertain income tax positions may exist for multiple years before the applicable statute of limitations expires or before an issue is resolved by the taxing authority. We believe our tax liabilities related to uncertain tax positions are based upon reasonable judgment and estimates; however, if actual results materially differ, our effective income tax rate and cash flows could be affected in the period of discovery or resolution.

We also review the estimates and assumptions used in evaluating the probability of realizing the future benefits of our deferred tax assets and record a valuation allowance when we believe that a portion or all of the deferred tax assets may not be realized. If we are unable to realize the expected future benefits of our deferred tax assets, we are required to provide a valuation allowance. We use our past history and experience, overall profitability, future management plans, and current economic information to evaluate the amount of valuation allowance to record. As of September 30, 2010, we maintained a valuation allowance for deferred tax assets arising from our operations in various jurisdictions because they did not meet the "more likely than not" criteria as defined by the recognition and measurement provisions of FASB ASC Topic 740, Income Taxes. In addition, as of September 30, 2010, we had deferred tax assets, after

valuation allowance, totaling \$5.3 million, which may not be realized if our assumptions and estimates change, which would affect our effective income tax rate and cash flows in the period of discovery or resolution.

#### Revenue Recognition and Deferred Revenue

We derive revenues from sales of our products, sales of our starter and renewal packs, shipping fees, and corporate-sponsored events. Substantially all of our product and pack sales are made to independent associates at published wholesale prices. We also sell products to independent members at discounted published retail prices. We record revenue net of any transaction taxes. We recognize revenue from shipped packs and products upon receipt by the customer. We recognize revenue related to future corporate-sponsored events when the event is held. Our deferred revenue primarily consists of (i) revenue received from sales of packs and products shipped but not received by the customers at period end; and (ii) revenue received from prepaid registration fees from customers planning to attend a future corporate-sponsored event. At September 30, 2010, total deferred revenue was \$2.9 million. Significant changes in our shipping methods could result in additional revenue deferrals.

## Product Return Policy

We stand behind our packs and products and believe we offer a reasonable and industry-standard product return policy to all of our customers. We do not resell returned product. Refunds are not processed until proper approval is obtained. All refunds must be processed and returned in the same form of payment that was originally used in the sale. Each country in which we operate has specific product return guidelines. However, we generally allow our independent associates and members to exchange products as long as the products are unopened and in good condition. In addition, in August 2007, we changed our sales return policy from 90% to a 100% satisfaction guarantee policy. Our return policies for our retail customers and our independent associates and members are as follows:

- **Retail Customer Product Return Policy.** This policy allows a retail customer to return any of our products to the original independent associate who sold the product and receive a full cash refund by the independent associate for the first 180 days following the product's purchase if located in the United States, Canada, and South Africa, and for the first 90 days following the product's purchase for the remaining countries. The independent associate may then return or exchange the product based on the independent associate product return policy.
- **Independent Associate and Member Product Return Policy.** This policy allows the independent associate or member to return an order within one year of the purchase date upon terminating their account. If an independent associate or member returns a product unopened and in good condition, he/she may receive a full refund minus a 10% restocking fee. We may also allow the independent associate or member to receive a full Satisfaction Guarantee refund if they have tried the product and are not satisfied for any reason, excluding promotional materials. This Satisfaction Guarantee refund applies in the United States, Canada, and South Africa only for the first 180 days following the product's purchase, and applies to the remaining countries for the first 90 days following the product's purchase; however, any commissions earned by an independent associate will be deducted from the refund. If we discover abuse of the refund policy, we may terminate the independent associate's or member's account.

Historically, sales returns estimates have not materially deviated from actual sales returns. Based upon our return policies, we estimate a sales return reserve for expected sales refunds based on our historical experience over a rolling six-month period. If actual results differ from our estimated sales returns reserves due to various factors, the amount of revenue recorded each period could be materially affected. Historically, our sales returns have not materially changed through the years, as the majority of our customers who return their merchandise do so within the first 90 days after the original sale. Sales returns have averaged 1.5% or less of our gross sales.

## Accounting for Stock-Based Compensation

We grant stock options to our employees and board members. At the date of grant, we determine the fair value of a stock option award and recognize compensation expense over the requisite service period, which is generally two to four years – the vesting period of such stock option award. The fair value of the stock option award is calculated using the Black-Scholes option-pricing model, (“calculated fair value”). The Black-Scholes option-pricing model requires us to apply judgment and use highly subjective assumptions, including expected stock option life, expected volatility, expected average risk-free interest rates, and expected forfeiture rates. For the nine months ended September 30, 2010, our assumptions and estimates used for the calculated fair value of stock options granted in 2010 were as follows:

	February 2010 grant	May 2010 grant	June 2010 grant #1	June 2010 grant #2	September 2010 Grant #1	September 2010 Grant #2
Estimated fair value per share of options granted:	\$ 2.03	\$ 1.86	\$ 1.23	\$ 1.18	\$ 1.26	\$ 1.40
Assumptions:						
Annualized dividend yield	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%
Risk-free rate of return	2.16%	2.07%	1.91%	1.91%	1.91%	1.24%
Common stock price volatility	71.1%	70.8%	71.5%	71.5%	72.40%	72.3%
Expected average life of stock options (in years)	4.5	4.5	4.5	4.5	4.5	4.5

The assumptions we use are based on our best estimates and involve inherent uncertainties based on market conditions that are outside of our control. Therefore, the stock-based compensation expense reported in our consolidated financial statements may not be representative of the actual economic cost of stock-based compensation. For example, if actual employee forfeitures significantly differ from our estimated forfeitures, we may be required to make an adjustment to our consolidated financial statements in future periods. As of September 30, 2010, using our current assumptions and estimates, we anticipate recognizing \$0.7 million in gross compensation expense through 2013 related to unvested stock options outstanding.

If we grant additional stock options in the future, we would be required to recognize additional compensation expense over the vesting period of such stock options in our consolidated statement of operations. Gross compensation expense would equal the calculated fair value of such stock options, which is dependent on the assumptions used to calculate such fair value, but generally ranges between 34% to 69% of the exercise price multiplied by the number of stock options awarded. As of September 30, 2010, we had 321,088 shares available for grant in the future.

#### Contingencies and Litigation

Each quarter, we evaluate the need to establish a reserve for any legal claims or assessments. We base our evaluation on our best estimates of the potential liability in such matters. The legal reserve includes an estimated amount for any damages and the probability of losing any threatened legal claims or assessments. The legal reserve is developed in consultation with our general and outside counsel and is based upon a combination of litigation and settlement strategies. Although we believe that our legal reserves and accruals are based on reasonable judgments and estimates, actual results could differ, which may expose us to material gains or losses in future periods. If actual results differ, if circumstances change, or if we experience an unanticipated adverse outcome of any legal action, including any claim or assessment, we would be required to recognize the estimated amount which could reduce net income, earnings per share, and cash flows.

#### RECENT ACCOUNTING PRONOUNCEMENTS

See “Recent Accounting Pronouncements” in Note 8 of the Notes to our Consolidated Financial Statements, which is incorporated herein by reference.

#### Item 3. Quantitative and Qualitative Disclosures About Market Risk

We do not engage in trading market risk sensitive instruments and do not purchase investments as hedges or for purposes “other than trading” that are likely to expose us to certain types of market risk, including interest rate, commodity price, or equity price risk. Although we have investments, we believe there has been no material change in our exposure to interest rate risk. We have not issued any debt instruments, entered into any forward or futures contracts, purchased any options, or entered into any swap agreements.

We are exposed, however, to other market risks, including changes in currency exchange rates as measured against the United States dollar. Because the change in value of the United States dollar measured against foreign currency may affect our consolidated financial results, changes in foreign currency exchange rates could positively or negatively affect our results as expressed in United States dollars. For example, when the United States dollar strengthens against foreign currencies in which our products are sold or weakens against foreign currencies in which we may incur costs, our consolidated net sales or related costs and expenses could be adversely affected.

We believe inflation has not had a material impact on our consolidated operations or profitability. We expanded into Canada in 1996, into Australia in 1998, into the United Kingdom in 1999, into Japan in 2000, into New Zealand in 2002, into the Republic of Korea in 2004, into Taiwan and Denmark in 2005, into Germany in 2006, into South Africa and Singapore in 2008, and into Austria, the Netherlands, Norway, and Sweden in September 2009. Our United States location processes orders for the United States, Canada, and South Africa. The Australian location processes orders for Australia, New Zealand, and Singapore. The United Kingdom location processes orders for the United Kingdom, Denmark, Germany, Austria, the Netherlands, Norway, and Sweden. The Japan, Republic of Korea, and Taiwan locations process orders for their local markets only. We translate our revenues and expenses in foreign markets using an average rate.

We maintain policies, procedures, and internal processes in an effort to help monitor any significant market risks and we do not use any financial instruments to manage our exposure to such risks. We assess the anticipated foreign currency working capital requirements of our foreign operations and maintain a portion of our cash and cash equivalents denominated in foreign currencies sufficient to satisfy most of these anticipated requirements.

We caution that we cannot predict with any certainty our future exposure to such currency exchange rate fluctuations or the impact, if any, such fluctuations may have on our future business, product pricing, operating expenses, and on our consolidated financial position, results of operations, or cash flows. However, to combat such market risk, we closely monitor our exposure to currency fluctuations. The foreign currencies in which we currently have exposure to foreign currency exchange rate risk include the currencies of Canada, Australia, the United Kingdom, Japan, New Zealand, the Republic of Korea, Taiwan, Denmark, Germany, South Africa, Singapore, Austria, the Netherlands, Norway, and Sweden. The current (spot) rate, average currency exchange rates, and the low and high of such currency exchange rates as compared to the United States dollar, for each of these countries as of and for the nine months ended September 30, 2010 were as follows:

Country (foreign currency name)	Low	High	Average	Spot
Australia (Dollar)	0.81520	0.97010	0.89710	0.97010
Austria, Germany, the Netherlands (Euro)	1.19440	1.45130	1.31694	1.36120
Canada (Dollar)	0.92880	1.00340	0.96556	0.97190
Denmark (Krone)	0.16060	0.19520	0.17687	0.18270
Japan (Yen)	0.01057	0.01202	0.01118	0.01196
New Zealand (Dollar)	0.66310	0.74190	0.70967	0.73860
Norway (Krone)	0.14970	0.17800	0.16471	0.17100
Republic of Korea (Won)	0.00080	0.00092	0.00086	0.00088
Singapore (Dollar)	0.70340	0.75990	0.72309	0.75990
South Africa (Rand)	0.12600	0.14390	0.13451	0.14390
Sweden (Krona)	0.12370	0.14870	0.13638	0.14870
Switzerland (Franc)	0.86000	1.02450	0.93956	1.02450
Taiwan (Dollar)	0.03074	0.03225	0.03136	0.03189
United Kingdom (British Pound)	1.43380	1.63820	1.53432	1.58090

#### Item 4. Controls and Procedures

##### Evaluation of Disclosure Controls and Procedures

Our management, with the participation of our Co-Chief Executive Officers (principal executive officer) and our Chief Financial Officer (principal financial officer), have concluded, based on their evaluation as of the end of the period covered by this report, that our disclosure controls and procedures are effective to ensure that information required to be disclosed by us in reports filed or submitted under the Securities Exchange Act of 1934, as amended (as defined in Exchange Act Rules 13(a) and 15(d)-15(e)), is recorded, processed, summarized, and reported within the time periods specified in the Securities and Exchange Commission's rules and forms and include controls and procedures designed to ensure that information required to be disclosed by us in such reports is accumulated and communicated to our management, including our principal executive and financial officers, as appropriate, to allow timely decisions regarding required disclosure.

##### Changes in Internal Control over Financial Reporting

During the quarter ended September 30, 2010, there were no changes in our internal control over our financial reporting that we believe materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

PART II - OTHER INFORMATION

Item 1. Legal Proceedings

See “Litigation” in Note 7 of the Notes to our Unaudited Consolidated Financial Statement, which is incorporated herein by reference.

Item 1A. Risk Factors

In addition to the other information set forth in this report, you should carefully consider the factors discussed in Part I, “Item 1A. Risk Factors” in our Annual Report on Form 10-K for the year ended December 31, 2009, which could materially affect our business or our consolidated financial position, results of operations, and cash flows. The risks described in our Annual Report on Form 10-K are not the only risks we face. Additional risks and uncertainties not currently known to us or that we currently deem to be insignificant also may become materially adverse or may affect our business in the future or our consolidated financial position, results of operations, or cash flows.

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

None.

Item 3. Defaults Upon Senior Securities

None.

Item 4. Removed and Reserved

Item 5. Other Information

None.

Item 6. Exhibits

See Index to Exhibits following the signature page of this Quarterly Report on Form 10-Q.



SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) 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.

Mannatech, Incorporated

Dated: November 4, 2010

By: /s/ Stephen D. Fenstermacher  
Stephen D. Fenstermacher  
Co-Chief Executive Officer and  
Chief Financial Officer  
(principal financial and  
accounting officer)

Dated: November 4, 2010

By: /s/ Robert A. Sinnott  
Robert A. Sinnott  
Co-Chief Executive Officer and  
Chief Science Officer  
(principal executive officer)

## INDEX TO EXHIBITS

Exhibit Number	Exhibit Description	Incorporated by Reference			
		Form	File No.	Exhibit (s)	Filing Date
3.1	Amended and Restated Articles of Incorporation of Mannatech, dated May 19, 1998.	S-1	333-63133	3.1	October 28, 1998
3.2	Fourth Amended and Restated Bylaws of Mannatech, dated August 8, 2001 (Corrected).	10-K	000-24657	3.2	March 16, 2007
3.3	First Amendment to the Fourth Amended and Restated Bylaws of Mannatech, effective November 30, 2007.	8-K	000-24657	3.1	December 6, 2007
4.1	Specimen Certificate representing Mannatech's common stock, par value \$0.0001 per share.	S-1	333-63133	4.1	October 28, 1998
10.1	Investment Agreement by and between Mannatech, Incorporated and Dutchess Opportunity Fund, II, LP, dated September 16, 2010	8-K	000-24657	10.1	September 21, 2010
10.2	Registration Rights Agreement by and between Mannatech, Incorporated and Dutchess Opportunity Fund, II, LP, dated September 16, 2010	8-K	000-24657	10.2	September 21, 2010
10.3	Amendment to Investment Agreement, by and between Mannatech, Incorporated and Dutchess Opportunity Fund, II, LP, dated October 4, 2010	8-K	000-24657	10.1	October 5, 2010
10.4	Form of Indemnification Agreement between Mannatech and each of the following directors: J. Stanley Fredrick, Patricia Weir, Alan D. Kennedy, Gerald E. Gilbert, Marlin Ray Robbins, Larry A. Jobe, and Robert A. Toth	*	*	*	*
31.1*	Certification pursuant to Section 302 of the Sarbanes-Oxley Act of 2002, of the Co-Chief Executive Officer of Mannatech.	*	*	*	*
31.2*	Certification pursuant to Section 302 of the Sarbanes-Oxley Act of 2002, of the Co-Chief Executive Officer of Mannatech.	*	*	*	*

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32.1*	Certification pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, of the Co-Chief Executive Officer of Mannatech.	*	*	*	*
32.2*	Certification pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, of the Co-Chief Executive Officer of Mannatech.	*	*	*	*
101.INS**	XBRL Instance Document	**	**	**	**
101.SCH**	XBRL Taxonomy Extension Schema Document	**	**	**	**
101.CAL**	XBRL Taxonomy Extension Calculation Linkbase Document	**	**	**	**
101.LAB**	XBRL Taxonomy Extension Label Linkbase Document	**	**	**	**
101.PRE**	XBRL Taxonomy Extension Presentation Linkbase Document	**	**	**	**
101.DEF**	XBRL Taxonomy Extension Definition Linkbase Document	**	**	**	**

\* Filed herewith.

\*\* Furnished herewith. In accordance with Rule 406T of Regulation S-T, the information in these exhibits shall not be deemed to be “filed” for purposes of Section 18 of the Securities Exchange Act of 1934, or otherwise subject to liability under that section, and shall not be incorporated by reference into any registration statement or other document filed under the Securities Act of 1933, as amended, except as expressly set forth by specific reference in such filing.

