

NATURAL HEALTH TRENDS CORP
Form 10-K
March 06, 2015

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-K

(Mark One)

ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the fiscal year ended December 31, 2014

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 number: 0-26272

NATURAL HEALTH TRENDS CORP.

(Exact name of registrant as specified in its charter)

Delaware 59-2705336
(State or other jurisdiction of (I.R.S. Employer
incorporation or organization) Identification No.)

4514 Cole Avenue

Suite 1400

Dallas, Texas 75205

(Address of principal executive offices, including zip code)

Registrant's telephone number, including area code: (972) 241-4080

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

Title of each class	Name of each exchange on which registered
Common Stock, par value \$0.001 per share	The NASDAQ Stock Market LLC

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

None

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

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

Indicate by check mark whether the registrant: (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 Website, 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

Edgar Filing: NATURAL HEALTH TRENDS CORP - Form 10-K

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K (§229.405 of this chapter) is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K.

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of "large accelerated filer," "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act.

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

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Act). Yes No

The aggregate market value of the voting and non-voting common equity held by non-affiliates computed by reference to the closing price of such common equity on June 30, 2014: \$48,917,062

At February 27, 2015, the number of shares outstanding of the registrant's common stock was 12,482,356 shares.

DOCUMENTS INCORPORATED BY REFERENCE

Portions of the registrant's definitive proxy statement to be filed with the United States Securities and Exchange Commission no later than 120 days after the end of the registrant's fiscal year end to which this report relates are incorporated by reference into Part III of this Annual Report on Form 10-K where indicated.

NATURAL HEALTH TRENDS CORP.
Annual Report on Form 10-K
December 31, 2014

TABLE OF CONTENTS

	Page
PART I	
Item 1. Business	1
Item 1A. Risk Factors	9
Item 1B. Unresolved Staff Comments	19
Item 2. Properties	20
Item 3. Legal Proceedings	20
Item 4. Mine Safety Disclosures	20
PART II	
Item 5. Market for Registrant's Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities	21
Item 6. Selected Financial Data	23
Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations	24
Item 7A. Quantitative and Qualitative Disclosures About Market Risk	31
Item 8. Financial Statements and Supplementary Data	32
Item 9. Changes In and Disagreements with Accountants on Accounting and Financial Disclosure	54
Item 9A. Controls and Procedures	54
Item 9B. Other Information	55
PART III	
Item 10. Directors, Executive Officers and Corporate Governance	55
Item 11. Executive Compensation	55
Item 12. Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters	55
Item 13. Certain Relationships and Related Transactions, and Director Independence	55
Item 14. Principal Accounting Fees and Services	55
PART IV	
Item 15. Exhibits and Financial Statement Schedules	55
Signatures	56

FORWARD-LOOKING STATEMENTS

This Annual Report on Form 10-K, in particular “Item 7. Management’s Discussion and Analysis of Financial Condition and Results of Operations,” and “Item 1. Business,” include “forward-looking statements” within the meaning of Section 21E of the Securities Exchange Act of 1934, as amended (the “Exchange Act”). When used in this report, the words or phrases “will likely result,” “expect,” “intend,” “will continue,” “anticipate,” “estimate,” “project,” “believe” and similar expressions are intended to identify “forward-looking statements” within the meaning of the Exchange Act. These statements represent our expectations or beliefs concerning, among other things, future revenue, earnings, growth strategies, new products and initiatives, future operations and operating results, and future business and market opportunities.

Forward-looking statements in this report speak only as of the date hereof, and forward-looking statements in documents incorporated by reference speak only as of the date of those documents. We undertake no obligation to publicly update or revise any forward-looking statement, whether as a result of new information, future events or otherwise, except as required by law. We caution and advise readers that these statements are based on certain assumptions that may not be realized and involve risks and uncertainties that could cause actual results to differ materially from the expectations and beliefs contained herein.

For a summary of certain risks related to our business, see “Item 1A. Risk Factors” in this report. Additional factors that could cause actual results to differ materially from our forward-looking statements are set forth in this report, including under the heading “Management’s Discussion and Analysis of Financial Condition and Results of Operations” and in our financial statements and the related notes.

Unless otherwise noted, the terms “we,” “our,” “us,” and “Company,” refer to Natural Health Trends Corp. and its subsidiaries. References to “dollars” and “\$” are to United States dollars.

Part I

Item 1. BUSINESS

Overview of Business

Natural Health Trends Corp. is an international direct-selling and e-commerce company headquartered in Dallas, Texas. Subsidiaries controlled by the Company sell personal care, wellness, and “quality of life” products under the “NHT Global” brand. In most markets, we sell our products to a network of consumers or business builders that either uses the products themselves or resells them to consumers.

Our wholly-owned subsidiaries have an active physical presence in the following markets: North America; Greater China, which consists of Hong Kong, Taiwan and China; South Korea; Japan; and Europe, which consists of Italy and Slovenia. We also operate within certain Commonwealth of Independent States (Russia, Kazakhstan and Ukraine) through our engagement with a local service provider.

We seek to sell our products into many markets, primarily through our network marketing operations. The exception is China, where we sell directly to consumers through an e-commerce platform. Our objectives are to enrich the lives of the users of our products and enable our distributors to benefit financially from the sale of our products.

We were originally incorporated as a Florida corporation in 1988. We merged into one of our subsidiaries and re-incorporated in Delaware effective June 29, 2005.

Our common stock is currently traded on the NASDAQ Capital Market under the symbol “NHTC.”

Available Information

We maintain executive offices at 4514 Cole Avenue, Suite 1400, Dallas, Texas 75205 and our telephone number is (972) 241-4080. Our website is located at www.naturalhealthtrends.com. Our Annual Reports on Form 10-K, Quarterly Reports on Form 10-Q, Current Reports on Form 8-K, and amendments to such reports are available, free of

charge, on our website as soon as reasonably practicable after we file electronically such material with, or furnish it to, the United States Securities and Exchange Commission, or SEC. The information provided on our website should not be considered part of this report. The public may read and copy any materials we file with the SEC at the SEC's Public Reference Room at 100 F Street, N.E., Room 1580, Washington, DC 20549. The public may obtain information on the operation of the Public Reference Room by calling the SEC at 1-800-SEC-0330. The SEC maintains an internet website at <http://www.sec.gov> that contains reports, proxy and information statements, and other information regarding issuers that file electronically with the SEC.

Our Principal Products

We offer a line of "NHT Global" branded products in three distinct categories: wellness, beauty and lifestyle. These product categories, along with the business opportunity we offer in most of our markets, provide our members a platform to further their goal of achieving and maintaining healthy, quality lifestyles complete with product supplementation and the opportunity for financial rewards.

The following table summarizes our product offering by category:

Product Category	Description	Products
<i>Wellness</i>		
Products formulated and designed to meet specific wellness goals of our customers. Includes targeted nutrition such as joint health, antioxidant support, digestive health, heart health, immune support and cellular health.	Liquid, encapsulated, tableted and powder dietary and nutritional supplements, herbal supplements, vitamins, minerals	Premium Noni Juice™, Triotein™, Cluster X2™, Children's Chewable MultiVitamin™, ReStor™ Silver, ReStor™ Vital, HerBalance™, Trifusion Max™, Glucosamine 2200™, FibeRich™, Energin™, Essential Probiotics™, LivaPro™, Cordyceps Mycelia CS-4™, Purus™, and our recently launched Omega 3 Essential Fatty Acids
<i>Beauty</i>		
Products to help improve skin health and bring an appearance of youthful vibrancy. This product line includes anti-aging and hydrating cleansers, creams, lotions, serums and toners to moisturize, protect and improve the appearance of skin.	Facial skin care and body care	Skindulgence™ 30-Minute Non-Surgical Facelift System, Time Restore™ Eye Cream and Essence, BioCell™ Mask, 24K Renaissance Rejuvenation Serum™, Soothe™, Floraeda Hydrating Series™
<i>Lifestyle</i>		
Products uniquely formulated to improve overall quality of life and to support active, physical and healthy lifestyles including weight management, intimacy support and energy enhancing supplements.	Supplements and topical gels for improved vitality	Alura™ by NHT Global, Valura™, LaVie™ Vibrant Energy drink, Twin Slim Diet Jelly™

We continuously source unique, proprietary and immediate impact products to offer to our members and customers. Our product development is an ongoing process that is fueled by marketplace trends and new scientific findings and research.

Working closely with raw material manufacturers and leading domestic and international contract manufacturers, our mission is to co-develop and bring to market the highest quality products. Our manufacturers are primarily located in the United States, as well as a few in South Korea, Hong Kong and China. Our raw materials (including botanical ingredients) are sourced from reputable suppliers around the world. In addition, raw material Certificates of Analysis are reviewed in our effort to assure that the appropriate testing has been performed and are within ingredient specification requirements.

Operations of the Business

Operating Strategy

Our objective is to help our members succeed in achieving their life objectives; be it personal health, beauty, happiness or financial security. The Company consists of professionals who focus on assisting our members in attaining their goals.

We believe that, since early 2010, we have completely changed our corporate identity and are building a competitive business model applicable to the markets in which we operate based on six key competencies:

Our field leaders are experienced and culturally coherent. They work effectively with the Company's management, implementing our strategies and providing continuous feedback to improve the Company's services.

The Company has implemented a commission structure that makes it as easy as possible to join the Company's business, while giving existing members a chance to start making money as quickly as possible in multiple ways.

We have developed and rolled out a comprehensive training system that provides a complete career path appropriate for our members. Our training material covers the needs of all of our members, be they prospects, new recruits, product evangelists, sales leaders or dream builders.

The continuously improving mentality and methodology in our customer services have not only distinguished us as an organization, but have also given us a constant flow of information as to how we can do better to service our members.

We have developed a year-round, multi-faceted promotional plan that targets different segments of our membership and has proven most effective in the last few years.

Last, a discipline and capability has been established to continue launching high-quality consumer products that are designed to facilitate the accomplishment of our corporate objective.

Sourcing of Products

Our corporate staff works with research and development personnel of our manufacturers and other prospective vendors to create product concepts and develop the product ideas into actual products. We then may enter into supply agreements with the vendors pursuant to which we obtain rights to sell the products under private labels (or trademarks) that are owned by us. Because our current main products all came to us originally as proposals from our vendors, we have incurred minimal “out-of-pocket” research and development costs through December 31, 2014. In addition, some of our local markets introduce their own products from time to time and these products are sometimes adopted by our other markets.

We or certain of our subsidiaries generally purchase finished goods from manufacturers and sell them to our distributors for their resale or personal consumption. We believe that in the event we are unable to source products from our current or alternate suppliers, our revenue, income and cash flow could be adversely and materially impacted. We have a contract with Two Harbors Trading Company (for *Premium Noni Juice*TM) through December 2017 with automatic renewal rights and a contract with 40Js LLC (for *Alura*TM) through July 2016.

Marketing and Distribution

We distribute our products internationally primarily through a network marketing system, which is a form of person-to-person direct selling. Under this system, distributors primarily refer our products to prospective consumers or they may buy at wholesale prices for resale to consumers and for personal consumption. The concept of network marketing is based on the strength of personal recommendations that frequently come from friends, neighbors, relatives, and close acquaintances. We believe that network marketing is an effective way to distribute our products because it allows person-to-person product education and testimonials as well as higher levels of customer service, all of which are not as readily available through other distribution channels. In this document, we generically use the term “distributor” to refer to distributors who purchase for their own consumption or for resale, or both, as well as to members who only sign up to consume our products.

Our distributors are independent full-time or part-time contractors who purchase products directly from our subsidiaries via the internet for resale to retail consumers (other than in China and certain other markets) or for their own personal consumption. Purchasers of our products in China and certain other markets may purchase only for their own personal consumption and not for resale.

The following table sets forth the number of active distributors by market for the time periods indicated. We consider a distributor “active” if they have placed at least one product order with us during the preceding year.

	December 31,	
	2013	2014
North America	1,720	1,660
Hong Kong	20,190	46,710
Taiwan	1,710	2,370
South Korea	510	450
Japan	150	130
Russia, Kazakhstan and Ukraine	2,970	2,600
Europe	270	440
Total	27,520	54,360

NHT Global distributors must agree to the terms and conditions of our distributor agreement posted on our website and generally pay an annual enrollment fee. The distributor agreement sets forth our policies and procedures, and we may elect to terminate a distributor for non-compliance.

We pay commissions to eligible NHT Global distributors based on product purchases by such distributors' down-line distributors during a given commission period. To be eligible to receive commissions, distributors in some countries may be required to make nominal monthly or other periodic purchases of products. See "Working with Distributors."

Distributors generally place orders through the internet and pay by credit card prior to shipment. Accordingly, we carry minimal accounts receivable and credit losses are historically minimal.

We sponsor promotional meetings and motivational training events for current and potential NHT Global distributors. These events are designed to inform prospective and existing distributors about both existing and new product lines, our latest marketing and promotional plans, and new services improvements. These events also serve as a venue for recognition of distributor accomplishments. Distributors typically share their experiences in using our products and developing their business at these events. We are continually developing or updating our marketing strategies and programs to motivate our distributors.

Management Information Systems

The NHT Global business uses a proprietary web-based system to process orders and to communicate bonus volume activity and commissions to distributors. Other than this proprietary system, we have not fully automated and integrated other critical business processes such as inventory management. We have automated a substantial amount of our financial reporting processes through implementation of Oracle's E-Business Suite.

Employees

At December 31, 2014, we employed 113 total full-time employees worldwide, of which 14 were located in North America, 79 in Greater China (Hong Kong, China, and Taiwan), 13 in Commonwealth of Independent States (Russia, Kazakhstan and Ukraine), three in South Korea, three in Europe, and one in Japan.

Seasonality

From quarter to quarter, we are somewhat impacted by seasonal factors and trends such as major cultural events and vacation patterns. For example, most Asian markets celebrate their respective local New Year in the first quarter, which generally has a significant impact on that quarter. We believe that net sales are also generally negatively impacted during the third quarter, when many of our distributors traditionally take time off for vacations. In addition, the national holidays in Hong Kong, China and Taiwan in early October tend to have an adverse effect on sales in those markets.

Our spending is materially affected by the major events planned at different times of the year. A major promotional event could significantly increase the reported expenses during the quarter in which the event actually takes place, while the revenue that might be generated by the event may not occur in the same reporting period.

Intellectual Property

Most of our products are packaged under a "private label" arrangement. We have obtained or applied for trademark registration for certain names, logos and various product names in several countries in which we are doing business or considering expanding. We also rely on common law trademark rights to protect our unregistered trademarks. These common law trademark rights do not provide us with the same level of protection as afforded by a United States federal trademark. Common law trademark rights are limited to the geographic area in which the trademark is actually utilized, while a United States federal registration of a trademark enables the registrant to discontinue the unauthorized use of the trademark by a third party anywhere in the United States even if the registrant has never used the trademark in the geographic area where the trademark is being used; provided, however, that the unauthorized third party user has not, prior to the registration date, perfected its common law rights in the trademark within that geographic area.

We have a foreign holding and operating company structure for our non-United States businesses, which involves the division of our United States and non-United States operations. Under this structure, we and some of our United States subsidiaries have granted an exclusive license to some of our non-United States subsidiaries to use outside of the United States all of their intangible property, including trademarks, trade secrets and other proprietary information.

Working with Distributors

Sponsorship

Sponsoring new distributors creates multiple levels in the direct selling structure of NHT Global. The persons that a distributor sponsors within the network are referred to as "sponsored" distributors, who may purchase solely for their own personal consumption, for resale, or both. Persons newly recruited are assigned by sponsoring distributors into network positions that can be "under" other distributors, thus they can be called "down-line" distributors. If down-line distributors also sponsor new distributors, they create additional levels within the structure, but their down-line distributors remain in the same down-line network as their original sponsoring distributor.

While we provide product samples, brochures and other sales materials, distributors are primarily responsible for recruiting and educating their new distributors with respect to products, the compensation plan and how to build a successful distributorship network.

Distributors are not required to sponsor other distributors as their down-line, and we do not pay any commissions for sponsoring new distributors. However, because of the financial incentives provided to those who succeed in building a distributor network that consumes and resells products, we believe that many of our distributors attempt, with varying degrees of effort and success, to sponsor additional distributors. Because they are seeking new opportunities for income, people are often attracted to become distributors after using our products or after attending introductory seminars. Once a person becomes a distributor, he or she is able to purchase products directly from us at wholesale prices via the internet. The distributor is also entitled to sponsor other distributors in order to build a network of distributors and product users.

Compensation Plans

NHT Global employs what is commonly referred to as a binary compensation plan, enhanced with certain unilevel features. Under the NHT Global compensation plan, distributors are paid weekly commissions for product purchases by their down-line distributor network across all geographic markets, except China, where we maintain an e-commerce retail platform and do not pay any commissions. This "seamless" compensation plan enables a distributor located in one country to sponsor other distributors located in other countries. Currently, there are basically two ways in which NHT Global distributors can earn income:

Through retail markups on sales of products purchased by distributors at wholesale prices (in some markets, sales are for personal consumption only and income may not be earned through retail mark-ups on sales in that market); and Through commissions paid on product purchases made by their down-line distributors.

Each of our products is designated a specified number of bonus volume points. Commissions are based on total personal and group bonus volume points per sales period. Bonus volume points are essentially a percentage of a product's wholesale price. As the distributor's business expands, the distributor receives higher commissions from purchases made by an expanding down-line network. To be eligible to receive commissions, a distributor may be required to make nominal monthly or other periodic purchases of our products. Certain of our subsidiaries do not require these nominal purchases for a distributor to be eligible to receive commissions. In determining commissions, the number of levels of down-line distributors included within the distributor's commissionable group increases as the number of distributorships directly below the distributor increases. Under our current compensation plan, certain of our commission payout may be limited to a hard cap dollar amount per week or a specific percentage of the total product sales. In some markets, commissions may be further limited.

In some markets, we also pay certain bonuses on purchases by up to three generations of personally sponsored distributors, as well as bonuses on commissions earned by up to three generations of personally sponsored distributors. Distributors can also earn income, trips and other prizes in specific time-limited promotions and contests we hold from time to time.

From time to time we make modifications and enhancements to our compensation plan to help motivate distributors, which can have an impact on distributor commissions. From time to time we also enter into agreements for business or market development, which may result in additional compensation to specific distributors.

Distributor Support

We are committed to providing a high level of support services tailored to the needs of our distributors in each marketplace we are serving. We attempt to meet the needs and build the loyalty of distributors by providing personalized distributor services and by maintaining a generous product return policy (see "Product Warranties and Returns"). We believe that maximizing a distributor's efforts by providing effective distributor support has been, and could continue to be, important to our success.

Through product training meetings, regular conventions, web-based messages, distributor focus groups, regular telephone conference calls and other personal contacts with distributors, we seek to understand and satisfy the needs of our distributors. Via our websites, we provide product fulfillment and tracking services that result in user-friendly and timely product distribution.

To help maintain communication with our distributors, we offer the following support programs:

Teleconferences – we hold teleconferences with associate field leadership on various subjects such as technical product discussions, distributor organization building and management techniques.

Internet – we maintain a website at www.nhtglobal.com. On this website, the user can read company news, learn more about various products, sign up to be a distributor, place orders, and track the fulfillment and delivery of their orders.

Product Literature – we offer a variety of literature to distributors, including product catalogs, informational brochures, pamphlets and posters for individual products.

Broadcast E-mail and Text Messages – we send announcements via e-mail and/or text messages to all active distributors.

Social Media tools – in some countries we maintain country-specific social media sites to foster a community environment around our product offering and business opportunity.

Technology and Internet Initiatives

We believe that the internet is important to our business as more consumers communicate online and purchase products over the internet as opposed to traditional retail and direct sales channels. As a result, we have committed significant resources to our e-commerce capabilities and the abilities of our distributors to take advantage of the internet. Substantially all of our sales take place via the internet. NHT Global offers a global web page that allows a distributor to have a personalized website through which he or she can sell products in all of the countries in which we do business. Links to these websites can be found at our main website for distributors at www.nhtglobal.com. The information provided on these websites should not be considered part of this report.

Rules Affecting Distributors

Our distributor policies and procedures establish the rules that distributors must follow in each market. We also monitor distributor activity in an attempt to provide our distributors with a “level playing field” so that one distributor may not be disadvantaged by the activities of another. We require our distributors to present products and business opportunities in an ethical and professional manner. Distributors further agree that their presentations to customers must be consistent with, and limited to, the product claims and representations made in our literature.

We require that we produce or pre-approve all sales aids used by distributors such as videotapes, audiotapes, brochures and promotional clothing. Further, distributors may not use any form of media advertising to promote products unless it is pre-approved by us. Products may be promoted only by personal contact or by literature produced or approved by us. Distributors are not entitled to use our trademarks or other intellectual property without our prior consent.

Our compliance department reviews reports of alleged distributor misbehavior. If we determine that a distributor has violated our distributor policies or procedures, we may terminate the distributor’s rights completely. Alternatively, we may impose sanctions, such as warnings, probation, withdrawal or denial of an award, suspension of privileges of the distributorship, fines, withholding commissions, until specified conditions are satisfied or other appropriate injunctive relief. Our distributors are independent contractors, not employees, and may act independently of us. Further, our distributors may resign or terminate their distributorship at any time without notice. See “Item 1A. Risk Factors.”

Government Regulations

Direct Selling Activities

Direct selling, or multi-level marketing, activities are regulated by various federal, state and local governmental agencies in the United States and other countries. These laws and regulations are generally intended to prevent fraudulent or deceptive schemes, often referred to as “pyramid” schemes, which compensate participants for recruiting additional participants irrespective of product sales, use high-pressure recruiting methods and/or do not involve legitimate products. The laws and regulations in our current markets often:

- impose cancellation/product return, inventory buy-backs and cooling-off rights for consumers and distributors;
- require us or our distributors to register with governmental agencies;
- impose reporting requirements; and
- impose upon us requirements, such as requiring distributors to maintain levels of retail sales to qualify to receive commissions, to ensure that distributors are being compensated for sales of products and not for recruiting new distributors.

The laws and regulations governing direct selling are modified from time to time, and, like other direct selling companies, we are subject from time to time to government investigations in our various markets related to our direct selling activities. This can require us to make changes to our business model and aspects of our global compensation plan in the markets impacted by such changes and investigations.

Based on advice of our engaged outside professionals in existing markets, the nature and scope of inquiries from government regulatory authorities and our history of operations in those markets to date, we believe our method of distribution complies in all material respects with the laws and regulations related to direct selling of the countries in which we currently operate.

As a result of restrictions in China on direct selling activities, we are not conducting direct selling in China. Consumers and members purchase the Company’s products via our Hong Kong-based website or our e-commerce platform in China. The regulatory environment in China is complex. Because we operate a direct selling model outside of China, our operations in China have received regulatory and media attention. At the end of 2005, China adopted new direct selling and anti-pyramiding regulations that are restrictive and contain various limitations, including a restriction on the ability to pay multi-level compensation to independent distributors. Regulations are subject to discretionary interpretation by municipal and provincial level regulators. Interpretations of what constitutes permissible activities by regulators can vary from province to province and can change from time to time because of the lack of clearly defined rules regarding direct selling activities.

Because of the Chinese government's significant concerns about direct selling activities and its adoption of direct selling and anti-pyramiding regulations, it scrutinizes very closely activities of direct selling companies. Our business continues to be subject to reviews and investigations by municipal and provincial level regulators. At times, investigations and related actions by government regulators have caused an obstruction to our members' activities in certain locations, and have resulted in a few cases of enforcement actions. In each of these cases, we helped our members with their defense in the legality of their conduct. So far, no material changes to our business model have been required. We expect to receive continued guidance and direction as we work with regulators to address our business model and any changes that need to be made to comply with the direct selling regulations.

To augment our business in China, our Chinese subsidiary applied for a direct selling license first in 2005, provided a revised version in June 2006, and then updated again our application in November 2007. After the approval from the municipal and the provincial authorities, the application did not progress further with the central government. Eventually, the information contained in our most recent application became stale and we withdrew the license application in February 2009 with the intention of filing an updated application in the future.

Regulation of Our Products

Our products and related promotional and marketing activities are subject to extensive governmental regulation by numerous governmental agencies and authorities in the United States, including the U.S. Food and Drug Administration (the "FDA"), the Federal Trade Commission (the "FTC"), the Consumer Product Safety Commission, the United States Department of Agriculture, State Attorneys General and other state regulatory agencies. In our foreign markets, the products are generally regulated by similar government agencies.

Our personal care products are subject to various laws and regulations that regulate cosmetic products and set forth regulations for determining whether a product can be marketed as a “cosmetic” or requires further approval as an over-the-counter drug. In the United States, regulation of cosmetics is under the jurisdiction of the FDA. The Food, Drug and Cosmetic Act defines cosmetics by their intended use, as “articles intended to be rubbed, poured, sprinkled, or sprayed on, introduced into, or otherwise applied to the human body . . . for cleansing, beautifying, promoting attractiveness, or altering the appearance.” Among the products included in this definition are skin moisturizers, eye and facial makeup preparations, perfumes, lipsticks, fingernail polishes, shampoos, permanent waves, hair colors, toothpastes and deodorants, as well as any material intended for use as a component of a cosmetic product. Conversely, a product will not be considered a cosmetic, but may be considered a drug if it is intended for use in the diagnosis, cure, mitigation, treatment, or prevention of disease, or is intended to affect the structure or any function of the body. A product’s intended use can be inferred from marketing or product claims. The other markets in which we operate have similar regulations. In Japan, the Ministry of Health, Labour and Welfare regulates the sale and distribution of cosmetics and requires us to have an import business license and to register each personal care product imported into Japan. In Taiwan, all “medicated” cosmetic products require registration. In China, personal care products are placed into one of two categories, “general” and “drug.” Products in both categories require submission of formulas and other information with the health authorities, and drug products require human clinical studies. The product registration process in China for these products can take from nine to more than 18 months or longer. Such regulations in any given market can limit our ability to import products and can delay product launches as we go through the registration and approval process for those products. The sale of cosmetic products is regulated in the European Union under the European Union Cosmetics Directive, which requires a uniform application for foreign companies making personal care product sales.

The markets in which we operate all have varied regulations that distinguish foods and nutritional health supplements from “drugs” or “pharmaceutical products.” Because of the varied regulations, some products or ingredients that are recognized as a “food” in certain markets may be treated as a “pharmaceutical” in other markets. These regulations may require us to either modify a product or refrain from selling the product in a given market. As a result, we must often modify the ingredients and/or the levels of ingredients in our products for certain markets. In some circumstances, the regulations in foreign markets may require us to obtain regulatory approval prior to introduction of a new product or limit our uses of certain ingredients altogether. Because of negative publicity associated with some supplements, there has been an increased movement in the United States and other markets to expand the regulation of dietary supplements, which could impose additional restrictions or requirements in the future. In general, the regulatory environment is becoming more complex with increasingly strict regulations each year.

FDA regulations require current good manufacturing practices (cGMP) for dietary supplements. The regulations ensure that dietary supplements are produced in a quality manner, do not contain contaminants or impurities, and are accurately labeled. The regulations include requirements for establishing quality control procedures for us and our vendors and suppliers, designing and constructing manufacturing plants, and testing ingredients and finished products. The regulations also include requirements for record keeping and handling consumer product complaints. If dietary supplements contain contaminants or do not contain the type or quantity of dietary ingredient they are represented to contain, the FDA would consider those products to be adulterated or misbranded.

Our business is subject to additional FDA regulations, such as those implementing an adverse event reporting system (“AER’s”), which requires us to document and track adverse events and report serious adverse events, which are events involving hospitalization or death, associated with consumers’ use of our products.

Most of our major markets also regulate advertising and product claims regarding the efficacy of products. This is particularly true with respect to our dietary supplements because we typically market them as foods or health foods. For example, in the United States, we are unable to claim that any of our nutritional supplements will diagnose, cure, mitigate, treat or prevent disease. In the United States, the Dietary Supplement Health and Education Act, however, permits substantiated, truthful and non-misleading statements of nutritional support to be made in labeling, such as statements describing general well-being resulting from consumption of a dietary ingredient or the role of a nutrient or dietary ingredient in affecting or maintaining a structure or a function of the body. Most of the other markets in which we operate have not adopted similar legislation, although we may be subject to more restrictive limitations on the claims we can make about our products in these markets.

Other Regulatory Issues

As a United States entity operating through subsidiaries in foreign jurisdictions, we are subject to foreign exchange control, transfer pricing and custom laws that regulate the flow of funds between our subsidiaries and us for product purchases, management services and contractual obligations, such as the payment of distributor commissions. As is the case with most companies that operate in our product categories, we might receive inquiries from time to time from government regulatory authorities regarding the nature of our business and other issues, such as compliance with local direct selling, transfer pricing, customs, taxation, foreign exchange control, securities and other laws.

Product Warranties and Returns

NHT Global refund policies and procedures closely follow industry and country-specific standards, which vary greatly by country. For example, in the United States, the Direct Selling Association recommends that direct sellers permit returns during the twelve-month period following the sale, while in Hong Kong the standard return policy is 14 days following the sale. Our return policies typically conform to local laws or the recommendation of the local direct selling association. In most cases, distributors who timely return unopened product that is in resalable condition may receive a refund. The amount of the refund may be dependent on the country in which the sale occurred, the timeliness of the return, and any applicable re-stocking fee. NHT Global must be notified of the return in writing and such written requests would be considered a termination notice of the distributorship. From time to time, we may alter our return policy in response to special circumstances.

Our Industry

We are engaged in the direct selling industry, selling lifestyle enhancement products, cosmetics, personal care and dietary supplements. More specifically, we are engaged in what is called network marketing or multi-level marketing. This type of organizational structure and approach to marketing and sales include companies selling lifestyle enhancement products, cosmetics and dietary supplements, or selling other types of consumer products. Generally, direct selling is based upon an organizational structure in which independent distributors of a company's products are compensated for sales made directly to consumers.

NHT Global distributors are compensated based on sales generated by distributors they have recruited and all subsequent distributors recruited by their "down-line" network of distributors. The experience of the direct selling industry has been that once a sizeable network of distributors is established, new and alternative products and services can be offered to those distributors for sale to consumers and additional distributors.

Competition

The network marketing industry is very diverse, with giant multinational corporations as well as smaller, local operators. Big network marketing companies include Nu Skin Enterprises, Inc., USANA Health Sciences, Inc., Mannatech, Incorporated., Reliv' International, Inc, and Herbalife, Ltd, which have much greater name recognition and financial resources than we do and also have many more distributors. They are publicly traded and therefore serve as informational benchmarks. But we don't overlap with them in terms of marketplace or product range. On the other hand, many medium- and small-sized privately held Chinese, Taiwanese and Hong Kong companies are fierce competitors and are much closer to directly competing with us. Also, a number of our former employees and distributors now work for competitors, and sometimes try to use relationships and knowledge obtained to compete

with us.

Our ability to compete with other network marketing companies depends, in significant part, on our success in attracting and retaining distributors. There can be no assurance that our programs for attracting and retaining distributors will be successful. The pool of individuals interested in network marketing is limited in each market and is reduced to the extent other network marketing companies successfully attract these individuals into their businesses. Although we believe that we offer an attractive opportunity for our distributors, there can be no assurance that other network marketing companies will not be able to recruit our existing distributors or deplete the pool of potential distributors in a given market.

The direct selling channel tends to sell products at a higher price compared to traditional retailers, which poses a degree of competitive risk. There is no assurance that we would continue to compete effectively against retail stores, internet-based retailers or other direct sellers.

Item 1A. RISK FACTORS

We are exposed to a variety of risks that are present in our business and industry. The following are some of the more significant factors that could affect our business, results of operations and financial condition.

We could be adversely affected by management changes or an inability to attract and retain key management, directors and consultants.

We incur a low level of overhead and are run by a small number of executives, who rely on a small group of employees. Our future success depends to a significant degree on the skills, experience and efforts of our top management and directors. We also depend on the ability of our executive officers and other members of senior management to work effectively as a team. The loss of one or more of our executive officers, members of our senior management or directors could have a material adverse effect on our business, results of operations and financial condition. Moreover, as our business evolves, we may require additional or different management members, directors or consultants, and there can be no assurance that we will be able to locate, attract and retain them if and when they are needed.

Because our Hong Kong operations account for a majority of our overall business, and most of our Hong Kong business is derived from the sale of products to members in China, any material adverse change in our business relating to either Hong Kong or China would likely have a material adverse impact on our overall business.

In 2013 and 2014, approximately 77% and 89% of our revenue, respectively, was generated in Hong Kong. Most of our Hong Kong revenues are derived from the sale of products that are delivered to members in China. This geographic concentration in our business means that events or conditions that could negatively impact this geographic region or our operations in this region would have a greater adverse impact upon our overall business and financial results than would be the case with a company having greater geographic diversification.

In contrast to our operations in other parts of the world, we have not implemented a direct sales model in China. The Chinese government permits direct selling only by organizations that have a license that we do not have, and has also adopted anti-multilevel marketing legislation. We operate an e-commerce direct selling model in Hong Kong and recognize the revenue derived from sales to both Hong Kong and Chinese members as being generated in Hong Kong. Products purchased by members in China are delivered to third parties that act as the importers of record under agreements to pay applicable duties. In addition, through a Chinese entity, we sell products in China using an e-commerce retail model. The Chinese entity operates separately from the Hong Kong entity, although a Chinese member may elect to participate separately or in both.

We believe that the laws and regulations in China regarding direct selling and multi-level marketing are not specifically applicable to our Hong Kong-based e-commerce activity, and that our Chinese entity is operating in compliance with applicable Chinese laws. However, there can be no assurance that the Chinese authorities will agree with our interpretations of applicable laws and regulations or that China will not adopt new laws or regulations. Should the Chinese government determine that our e-commerce activity violates China's direct selling or anti-multilevel marketing legislation, or should new laws or regulations be adopted, there could be a material adverse effect on our business, financial condition and results of operations.

Because of the Chinese government's significant concerns about direct selling activities, it scrutinizes very closely activities of direct selling companies. At times, investigations and related actions by government regulators have resulted in a few cases where we have paid substantial fines. In each of these cases, we have been allowed to recommence operations after the government's investigation, and no material changes to our business model were required in connection with these fines and impediments.

Although we attempt to work closely with both national and local Chinese governmental agencies in conducting our business, our efforts to comply with national and local laws may be harmed by a rapidly evolving regulatory climate, concerns about activities resembling violations of direct selling or anti-multi-level marketing legislation, subjective interpretations of laws and regulations, and activities by individual distributors that may violate laws notwithstanding our strict policies prohibiting such activities. Any determination that our operations or activities, or the activities of

our individual distributors or employee sales representatives, or importers of record are not in compliance with applicable laws and regulations could result in the imposition of substantial fines, extended interruptions of business, restrictions on our future ability to obtain business licenses or expand into new locations, changes to our business model, the termination of required licenses to conduct business, or other actions, any of which could materially harm our business, financial condition and results of operations.

Various other factors could harm our business in Hong Kong and China, such as worsening economic conditions in Hong Kong or China, adverse local publicity or other events that may be out of our control. For example, we were advised to voluntarily suspend marketing activities in China during the third quarter of 2007 when the Chinese government was expected to impose a more intense enforcement program against illegal chain sales activities. We did not want to run the risk of being inadvertently entangled in the government enforcement actions and voluntarily withdrew all marketing activities from China during that period. It may be necessary or advisable to repeat this or similar actions from time to time in the future, and such periods of reduced activity could have a material adverse effect on our business.

Our failure to maintain and expand our distributor relationships could adversely affect our business.

We distribute our products through independent distributors, and we depend upon them directly for all of our sales in most of our markets. Accordingly, our success depends in significant part upon our ability to attract, retain and motivate a large base of distributors. Our direct selling organization is headed by a relatively small number of key distributors. The loss of a significant number of distributors, especially key distributors, could materially and adversely affect sales of our products and could impair our ability to attract new distributors. Moreover, the replacement of distributors could be difficult because, in our efforts to attract and retain distributors, we compete with other direct selling organizations, including but not limited to those in the personal care, cosmetic product and nutritional supplement industries. Our distributors may terminate their services with us at any time and, in fact, like most direct selling organizations, we have a high rate of attrition.

The number of active distributors or their productivity may not increase and could decline in the future. We cannot accurately predict any fluctuation in the number and productivity of distributors because we primarily rely upon existing distributors to sponsor and train new distributors and to motivate new and existing distributors. Operating results could be adversely affected if our existing and new business opportunities and products do not generate sufficient economic incentive or interest to retain existing distributors and to attract new distributors.

The number and productivity of our distributors could be harmed by several factors, including:

- adverse publicity or negative perceptions regarding us, our products, our method of distribution or our competitors;
- lack of interest in, or the technical failure of, existing or new products;
- lack of interest in our existing compensation plan for distributors or in enhancements or other changes to that compensation plan;
- our actions to enforce our policies and procedures;
- regulatory actions or charges or private actions against us or others in our industry;
- general economic and business conditions;
 - changes in management or the loss of one or more key distributor leaders;
- entry of new competitors, or new products or compensation plan enhancements by existing competitors, in our markets; and
- potential saturation or maturity levels in a given country or market which could negatively impact our ability to attract and retain distributors in such market.

The high level of competition in our industry could adversely affect our business.

The business of marketing personal care, cosmetic, nutritional supplements, and lifestyle enhancement products is highly competitive. This market segment includes numerous manufacturers, distributors, marketers, and retailers that actively compete for the business of consumers both in the United States and abroad. The market is highly sensitive to the introduction of new products, which may rapidly capture a significant share of the market. Sales of similar products by competitors may materially and adversely affect our business, financial condition and results of operations.

We are subject to significant competition for the recruitment of distributors from other direct selling organizations, including those that market similar products. Many of our competitors are substantially larger than we are, offer a wider array of products, have far greater financial resources and many more active distributors than we have. Even more numerous are those medium- and small-sized, all privately held Chinese, Taiwanese and Hong Kong companies that are fierce competitors and are much closer to directly competing with us. Our ability to remain competitive depends, in significant part, on our success in recruiting and retaining distributors with our products, attractive compensation plan and other incentives. We believe that we have an attractive product line and that our compensation and incentive programs provide our distributors with significant earning potential. However, we cannot be sure that

our programs for recruitment and retention of distributors would be successful.

Some of our competitors have employed or otherwise contracted for the services of our former officers, employees, consultants, and distributors, who may try to use information and contacts obtained while under contract with us for competitive advantage. While we seek to protect our information through contractual and other means, there can be no assurance that we will timely learn of such activity, have the resources to attempt to stop it, or have adequate remedies available to us.

An increase in the amount of compensation paid to distributors would reduce profitability.

A significant expense is the payment of compensation to our distributors, which represented approximately 46% of net sales during each of 2013 and 2014. We compensate our distributors by paying commissions, bonuses, and certain awards and prizes. Factors impacting the overall commission payout include the growth and depth of the distributor network, the distributor retention rate, the level of promotions, local promotional programs and business development agreements. Any increase in compensation payments to distributors as a percentage of net sales will reduce our profitability.

Our compensation plan includes a cap that may be enforced on distributor compensation paid out on a weekly dollar limit or as a percentage of product sales. There can be no assurance that enforcement of this cap will ensure profitability (which depends on many other factors). Moreover, enforcement of this cap could cause key distributors affected by the cap to leave and join other companies.

Failure of new products to gain distributor and market acceptance could harm our business.

An important component of our business is our ability to develop new products that create enthusiasm among our distributor force. If we fail to introduce new products on a timely basis, our distributor productivity could be harmed. In addition, if any new products fail to gain market acceptance, are restricted by regulatory requirements, or have quality problems, this would harm our results of operations. Factors that could affect our ability to continue to introduce new products include, among others, limited capital and human resources, government regulations, proprietary protections of competitors that may limit our ability to offer comparable products and any failure to anticipate changes in consumer tastes and buying preferences.

Direct-selling laws and regulations may prohibit or severely restrict our direct sales efforts and cause our revenue and profitability to decline, and regulators could adopt new regulations that harm our business.

Our direct selling system is subject to extensive laws, governmental regulations, administrative determinations, court decisions and similar constraints. These laws and regulations are generally intended to prevent fraudulent or deceptive schemes, often referred to as “pyramid” schemes, which compensate participants for recruiting additional participants irrespective of product sales, use high pressure recruiting methods and/or do not involve legitimate products.

Complying with these widely varying and sometimes inconsistent rules and regulations can be difficult and may require the devotion of significant resources on our part. There can be no assurance that we or our distributors are in compliance with all of these regulations. Our failure or our distributors’ failure to comply with these regulations or new regulations could lead to the imposition of significant penalties or claims and could negatively impact our business. If we are unable to continue business in existing markets or commence operations in new markets because of these laws, our revenue and profitability may decline.

We are also subject to the risk that new laws or regulations might be implemented or that current laws or regulations might change, which could require us to change or modify the way we conduct our business in certain markets. This could be particularly detrimental to us if we have to change or modify the way we conduct business in markets that represent a significant percentage of our revenue. For example, the Federal Trade Commission (the “FTC”) released a proposed New Business Opportunity Rule in April 2006. As initially drafted, the proposed rule would have required

pre-sale disclosures for all business opportunities, which may have included network marketing compensation plans such as ours. However, in November 2011, the FTC issued a final rule that does not apply to multi-level marketing companies that do not represent that they or another designated person will do any of the following: (a) provide locations for the operation of equipment, displays, vending machines or similar devices owned, leased, controlled or paid for by the purchaser of the opportunity; (b) provide outlets, accounts, or customers (including but not limited to internet outlets, accounts, or customers) for the purchaser's goods or services (advertising and general advice about business development and training is not considered as "providing locations, outlets, accounts, or customers"); or (c) buy back any or all of the goods or services that the purchaser makes or provides. As we understand the final regulation, the Company does not make any of these representations and therefore is not covered by the final rule, which took effect on March 1, 2012.

Challenges by third parties to the form of our business model could harm our business.

We are also subject to the risk of private party challenges to the legality of our direct selling system. The regulatory requirements concerning direct selling systems do not include "bright line" rules and are inherently fact-based and subject to judicial interpretation. An adverse judicial determination against us with respect to our direct selling system, or in proceedings not involving us directly but which challenge the legality of other direct selling marketing systems, could have a material adverse effect on our business. There is also risk that challenges and settlements involving other parties could provide incentives for similar actions by distributors against us and other direct selling companies. Moreover, challenges to our business system and operations in important markets may come from short sellers, hedge funds and other investors. Other companies in our industry have recently faced such challenges. Any challenges regarding us or others in our industry could harm our business if such challenges result in the investigation of our business model and operations or the imposition of any fines or damages on our business, create adverse publicity, increase scrutiny of our industry, detrimentally affect our efforts to recruit or motivate distributors and attract customers, or interpret laws in a manner inconsistent with our current business practices.

Our products and related activities are subject to extensive government regulation, which could delay, limit or prevent the sale of some of our products in some markets.

The formulation, manufacturing, packaging, labeling, importation, advertising, distribution, sale and storage of certain of our products are subject to extensive regulation by various federal agencies, including the Food and Drug Administration (the “FDA”), the FTC, the Consumer Product Safety Commission and the United States Department of Agriculture and by various agencies of the states, localities and foreign countries in which our products are manufactured, distributed and sold. For example, the FDA requires us and our suppliers to meet relevant current good manufacturing practice (cGMP) regulations for the preparation, packing and storage of foods and over-the-counter (OTC) drugs. We are also now required to report serious adverse events associated with consumer use of certain of our products. Other laws and regulations govern or restrict the claims that may be made about our products and the information that must be included and excluded on labels.

In markets outside the United States, prior to commencing operations or marketing new products, we may be required to obtain approvals, licenses, or certifications from a ministry of health or a comparable agency. Moreover, a foreign jurisdiction may pass laws that would prohibit the use of certain ingredients in their particular market. Compliance with these regulations can create delays and added expense in introducing new products to certain markets.

Failure by our distributors or us to comply with those regulations could lead to the imposition of significant penalties or claims and could materially and adversely affect our business. If we are not able to satisfy the various regulations, then we would have to cease sales of that product in that market. In addition, the adoption of new regulations or changes in the interpretation of existing regulations may result in significant compliance costs or discontinuation of product sales and may adversely affect the marketing of our products, resulting in significant loss of revenues.

We cannot predict the nature of any future laws, regulations, interpretations, or applications, nor can we determine what effect additional governmental regulations or administrative orders, when and if promulgated, could have on our business. These potential effects could include, however, requirements for the reformulation of certain products to meet new standards, the recall or discontinuance of certain products, additional recordkeeping and reporting requirements, expanded documentation of the properties of certain products, expanded or different labeling, or additional scientific substantiation. Any or all of these requirements could have a material adverse effect on our business, financial condition, or results of operations.

New regulations governing the marketing and sale of nutritional supplements could harm our business.

There has been an increasing movement in the United States and other markets to increase the regulation of dietary supplements, which could impose additional restrictions or requirements in the future. In the United States, for

example, some legislators and industry critics continue to push for increased regulatory authority by the FDA over nutritional supplements. Our business could be harmed if more restrictive legislation is successfully introduced and adopted in the future. In particular, the adoption of legislation requiring FDA approval of supplements or ingredients could delay or inhibit our ability to introduce new supplements. We face similar pressures in our other markets. In the United States, effective December 1, 2009, the FTC approved revisions to its Guides Concerning the Use of Endorsements and Testimonials in Advertising (“Guides”) that require disclosure of material connections between an endorser and the company they are endorsing and do not allow marketing using atypical results. The requirements and restrictions of the revised Guides may diminish the impact of our marketing efforts and negatively impact our sales results. If we or our distributors fail to comply with these Guides, the FTC could bring an enforcement action against us and we could be fined and/or forced to alter our operations. Our operations also could be harmed if new laws or regulations are enacted that restrict our ability to market or distribute nutritional supplements or impose additional burdens or requirements on nutritional supplement companies or require us to reformulate our products.

Regulations governing the production and marketing of our personal care products could harm our business.

Our personal care products are subject to various domestic and foreign laws and regulations that regulate cosmetic products and set forth regulations for determining whether a product can be marketed as a “cosmetic” or requires further approval as an over-the-counter drug. A determination that our cosmetic products impact the structure or function of the human body, or improper marketing claims by our distributors, may lead to a determination that such products require pre-market approval as a drug. Such regulations in any given market can limit our ability to import products and can delay product launches as we go through the registration and approval process for those products. Furthermore, if we fail to comply with these regulations, we could face enforcement action against us and we could be fined, forced to alter or stop selling our products and/or required to adjust our operations. Our operations also could be harmed if new laws or regulations are enacted that restrict our ability to market or distribute our personal care products or impose additional burdens or requirements on the contents of our personal care products or require us to reformulate our products.

If we are found not to be in compliance with good manufacturing practices our operations could be harmed.

FDA regulations on good manufacturing practices and adverse event reporting requirements for the nutritional supplement industry are in effect and require good manufacturing processes for us and our vendors, including stringent vendor qualifications, ingredient identification, manufacturing controls and record keeping. We are also now required to report serious adverse events associated with consumer use of our products. Our operations could be harmed if regulatory authorities make determinations that we or our vendors are not in compliance with the new regulations. A finding of noncompliance may result in administrative warnings, penalties or actions impacting our ability to continue selling certain of our products. In addition, compliance with these regulations has increased and may further increase the cost of manufacturing certain of our products as we work with our vendors to assure they are qualified and in compliance.

Failure to comply with domestic and foreign laws and regulations governing product claims and advertising could harm our business.

Our failure to comply with FTC or state regulations, or with regulations in foreign markets that cover our product claims and advertising, including direct claims and advertising by us, as well as claims and advertising by distributors for which we may be held responsible, may result in enforcement actions and imposition of penalties or otherwise materially and adversely affect the distribution and sale of our products. Distributor activities in our existing markets that violate applicable governmental laws or regulations could result in governmental or private actions against us in markets where we operate. Given the size of our distributor force, we cannot ensure that our distributors would comply with applicable legal requirements.

Although our distributors are independent contractors, improper distributor actions that violate laws or regulations could harm our business.

Our distributors are independent contractors and, accordingly, we are not in a position to directly provide the same direction, motivation and oversight as we would if distributors were our own employees. As a result, there can be no assurance that our distributors will participate in our marketing strategies or plans, accept our introduction of new products, or comply with our distributor policies and procedures. Extensive federal, state and local laws regulate our business, our products and our network marketing program. Because we have expanded into foreign countries, our policies and procedures for our distributors differ due to the different legal requirements of each country in which we do business. While we have implemented distributor policies and procedures designed to govern distributor conduct and to protect the goodwill associated with our trademarks and trade names, it can be difficult to enforce these policies and procedures because of the large number of distributors and their independent status.

Given the size and diversity of our distributor force, we experience problems with distributors from time to time, especially with respect to our distributors in foreign markets. Distributors often desire to enter a market, before we have received approval to do business, to gain an advantage in the marketplace. Improper distributor activity in new geographic markets could result in adverse publicity and can be particularly harmful to our ability to ultimately enter these markets. Violations by our distributors of applicable law or of our policies and procedures in dealing with customers could reflect negatively on our products and operations, and harm our business reputation. In addition, it is possible that a court could hold us civilly or criminally accountable based on vicarious liability because of the actions of our distributors. If any of these events occur, our business, financial condition, or results of operations could be materially adversely affected.

Adverse publicity associated with our products, ingredients or network marketing program, or those of similar companies, could harm our financial condition and operating results.

Adverse publicity concerning any actual or claimed failure by us or our distributors to comply with applicable laws and regulations regarding product claims and advertising, good manufacturing practices, the regulation of our network marketing program, the licensing of our products for sale in our target markets or other aspects of our business, whether or not resulting in enforcement actions or the imposition of penalties, could have an adverse effect on our goodwill and could negatively affect our ability to attract, motivate and retain distributors, which would negatively impact our ability to generate revenue. We cannot ensure that all distributors will comply with applicable legal requirements relating to the advertising, labeling, licensing or distribution of our products.

In addition, our distributors' and consumers' perception of the safety and quality of our products and ingredients, as well as similar products and ingredients distributed by other companies, can be significantly influenced by national media attention, publicized scientific research or findings, widespread product liability claims and other publicity concerning our products or ingredients or similar products and ingredients distributed by other companies. Adverse publicity, whether or not accurate or resulting from consumers' use or misuse of our products, that associates consumption of our products or ingredients or any similar products or ingredients with illness or other adverse effects, questions the benefits of our or similar products or claims that any such products are ineffective, inappropriately labeled or have inaccurate instructions as to their use, could negatively impact our reputation or the market demand for our products.

We have a limited product line.

We offer a limited number of products under our NHT Global brand. Our *Premium Noni Juice*[™] product accounts for a significant portion of our total revenue. If demand decreases significantly, government regulation restricts its sale, we are unable to adequately source or deliver the product, or we cease offering the product for any reason without a suitable replacement, our business, financial condition and results of operations could be materially and adversely affected.

We rely on a limited number of independent third parties to manufacture and supply our products.

All of our products are manufactured by a limited number of independent third parties. There is no assurance that our current manufacturers will continue to reliably supply products to us at the level of quality we require. If a key manufacturer suffers liquidity or experiences operational problems assisting with our products, our results could suffer. In the event any of our third-party manufacturers become unable or unwilling to continue to provide the products in required volumes and quality levels at acceptable prices, we will be required to identify and obtain acceptable replacement manufacturing sources or replacement products. There is no assurance that we will be able to obtain alternative manufacturing sources or products or be able to do so on a timely basis. An extended interruption in the supply of certain of our products may result in a substantial loss of revenue. In addition, any actual or perceived degradation of product quality as a result of our reliance on third party manufacturers may have an adverse effect on revenue or result in increased product returns.

Growth may be impeded by the political and economic risks of entering and operating foreign markets.

Our ability to achieve future growth is dependent, in part, on our ability to continue our international expansion efforts. However, there can be no assurance that we would be able to grow in our existing international markets, enter new international markets on a timely basis, or that new markets would be profitable. We must overcome significant regulatory and legal barriers before we can begin marketing in any foreign market.

Also, it is difficult to assess the extent to which our products and sales techniques would be accepted or successful in any given country. In addition to significant regulatory barriers, we may also encounter problems conducting operations in new markets with different cultures and legal systems from those elsewhere. We may be required to reformulate certain of our products before commencing sales in a given country. Once we have entered a market, we must adhere to the regulatory and legal requirements of that market. No assurance can be given that we would be able to successfully reformulate our products in any of our current or potential international markets to meet local regulatory requirements or attract local customers. The failure to do so could have a material adverse effect on our business, financial condition, and results of operations. There can be no assurance that we would be able to obtain and

retain necessary permits and approvals.

In many markets, other direct selling companies already have significant market penetration, the effect of which could be to desensitize the local distributor population to a new opportunity or to make it more difficult for us to recruit qualified distributors. There can be no assurance that, even if we are able to commence operations in foreign countries, there would be a sufficiently large population of potential distributors inclined to participate in a direct selling system offered by us. We believe our future success could depend in part on our ability to seamlessly integrate our business methods, including distributor compensation plan, across all markets in which our products are sold. There can be no assurance that we would be able to further develop and maintain a seamless compensation program.

Currency exchange rate fluctuations could lower our revenue and net income.

In 2014, approximately 98% of our revenue was recorded by subsidiaries located outside of North America. Revenue transactions and related commission payments, as well as other incurred expenses, are typically denominated in the local currency. Accordingly, our international subsidiaries use the local currency as their functional currency. The results of operations of our international subsidiaries are exposed to foreign currency exchange rate fluctuations during consolidation since we translate into U.S. dollars using the average exchanges rates for the period. As exchange rates vary, revenue and other operating results may differ materially from our expectations. Additionally, we may record significant gains or losses related to foreign-denominated cash and cash equivalents and the re-measurement of inter-company balances.

We believe that our foreign currency exchange rate exposure is somewhat limited since the Hong Kong dollar is pegged to the U.S. dollar. We also purchase a significant majority of inventories in U.S. dollars. Our foreign currency exchange rate exposure, mainly to South Korean won, Taiwan dollar, Japanese yen, Chinese yuan, Russian ruble, Kazakhstani tenge, Ukrainian hryvnia and European euro, represented approximately 18% and 9% of our revenue in 2013 and 2014, respectively. Our foreign currency exchange rate exposure may increase in the near future as we intend to develop opportunities in Southeast Asia, Canada and Europe. Additionally, our foreign currency exchange rate exposure would significantly increase if the Hong Kong dollar were no longer pegged to the U.S. dollar.

Given our inability to predict the degree of exchange rate fluctuations, we cannot estimate the effect these fluctuations may have upon future reported results, product pricing or our overall financial condition. Further, to date we have not attempted to reduce our exposure to short-term exchange rate fluctuations by using foreign currency exchange contracts.

Changes in tax or duty laws, and unanticipated tax or duty liabilities, could adversely affect our net income.

In the course of doing business we may be subject to various taxes, such as sales and use, value-added, and franchise. We are also subject to income taxes in the United States and numerous foreign jurisdictions. We earn a substantial portion of our income in foreign jurisdictions. If our capital or financing needs in the United States require us to repatriate earnings from foreign jurisdictions above our current levels, our effective income tax rates for the affected periods could be negatively impacted. Economic and political conditions make tax rules in any jurisdiction, including the United States, subject to significant change. There have been proposals to reform U.S. and foreign tax laws that could significantly impact how U.S. multinational corporations are taxed on foreign earnings. Although we cannot predict whether or in what form these proposals will pass, several of the proposals considered, if enacted into law, could have an adverse impact on our income tax expense and cash flows.

Our principal domicile is the United States. Under tax treaties, we are eligible to receive foreign tax credits in the United States for taxes paid abroad. Taxes paid to foreign taxing authorities may exceed the credits available to us, resulting in the payment of a higher overall effective tax rate on our worldwide operations.

Our effective income tax rate in the future could be adversely affected by a number of factors, including changes in the mix of earnings in countries with differing statutory tax rates, changes in the valuation of deferred tax assets and liabilities, changes in tax laws, the outcome of income tax audits in various jurisdictions around the world, and any repatriation of non-U.S. earnings for which we have not previously provided for U.S. taxes.

We may also be subject to examinations of our tax returns and other tax matters by the Internal Revenue Service and other tax authorities and governmental bodies. We regularly assess the likelihood of an adverse outcome resulting from these examinations to determine the adequacy of our provision for taxes, which is subject to significant discretion. There can be no assurance as to the outcome of these examinations. If our effective tax rates were to increase, particularly in the U.S., or if the ultimate determination of taxes owed is for an amount in excess of amounts previously accrued, our financial results or operations could be adversely affected.

In addition, our operations are subject to regulations designed to ensure that appropriate levels of customs duties are assessed on the importation of our products. The failure to properly calculate, report and pay such duties when we are subject to them could have a material adverse effect on our financial condition and results of operations. Any change

in the laws or regulations regarding such duties, or any interpretation thereof, could result in an increase in the cost of doing business.

Transfer pricing regulations affect our business and results of operations.

In many countries, including the United States, we are subject to transfer pricing and other tax regulations designed to ensure that appropriate levels of income are reported as earned by our United States or local entities and are taxed accordingly. We have adopted transfer pricing agreements with our subsidiaries to regulate inter-company transfers, which agreements are subject to transfer pricing laws that regulate the flow of funds between the subsidiaries and the parent corporation for product purchases, management services, and contractual obligations, such as the payment of distributor compensation. We believe that we operate in compliance with all applicable transfer pricing laws, and we intend to continue to operate in compliance with such laws. However, there can be no assurance that we will continue to be found to be operating in compliance with transfer pricing laws, or that those laws would not be modified, which, as a result, may require changes in our operating procedures or otherwise may have a material adverse effect on our financial results or operations.

We may be held responsible for certain taxes or assessments relating to the activities of our distributors, which could harm our financial condition and operating results.

Our distributors are subject to taxation, and in some instances, legislation or governmental agencies impose an obligation on us to collect the taxes, such as value added taxes, and to maintain appropriate records. In addition, we are subject to the risk in some jurisdictions of being responsible for social security and similar taxes with respect to our distributors.

We may face litigation that could harm our business.

We have been a party to lawsuits and other proceedings in the past. Prosecuting and defending potential litigation and other governmental proceedings may require significant expense and attention of our management. There can be no assurance that the significant money, time and effort spent will not adversely affect our business, financial condition and results of operations.

We may be unable to protect or use our intellectual property rights.

We rely on trade secret, copyright and trademark laws and confidentiality agreements with employees and third parties, all of which offer only limited protection of our confidential information and trademarks. Moreover, the laws of some countries in which we market our products may afford little or no effective protection of our intellectual property rights. The unauthorized copying, use or other misappropriation of our confidential information, trademarks and other intellectual property could enable third parties to benefit from such property without paying us for it. This could have a material adverse effect on our business, operating results and financial condition. If we resort to legal proceedings to enforce our intellectual property rights, the proceedings could be burdensome, expensive and result in inadequate remedies. It is also possible that our use of our intellectual property rights could be found to infringe on prior rights of others and, in that event, we could be compelled to stop or modify the infringing use, which could be burdensome and expensive.

We do not have product liability insurance and product liability claims could hurt our business.

Currently, we do not have product liability insurance, although the insurance carried by our suppliers may cover certain product liability claims against us. As a marketer of dietary supplements, cosmetics and other products that are ingested by consumers or applied to their bodies, we may become subjected to various product liability claims, including that:

- our products contain contaminants or unsafe ingredients;
- our products include inadequate instructions as to their uses; or
- our products include inadequate warnings concerning side effects and interactions with other substances.

If our suppliers' product liability insurance fails to cover product liability claims or other product liability claims, or any product liability claims exceeds the amount of coverage provided by such policies or if we are unsuccessful in any third party claim against the manufacturer or if we are unsuccessful in collecting any judgment that may be recovered by us against the manufacturer, we could be required to pay substantial monetary damages which could materially

harm our business, financial condition and results of operations. As a result, we may become required to pay high premiums and accept high deductibles in order to secure adequate insurance coverage in the future. Especially since we do not have direct product liability insurance, it is possible that product liability claims and the resulting adverse publicity could negatively affect our business.

Our internal controls and accounting methods may require modification.

We continue to review and develop controls and procedures sufficient to accurately report our financial performance on a timely basis. If we do not develop and implement effective controls and procedures, we may not be able to report our financial performance on a timely basis and our business and stock price would be adversely affected.

If we fail to achieve and maintain an effective system of internal controls in the future, we may not be able to accurately report our financial results or prevent fraud. As a result, investors may lose confidence in our financial reporting.

The Sarbanes-Oxley Act of 2002 requires that we report annually on the effectiveness of our internal control over financial reporting. Among other things, we must perform systems and processes evaluation and testing. We must also conduct an assessment of our internal controls to allow management to report on our assessment of our internal control over financial reporting, as required by Section 404 of the Sarbanes-Oxley Act. We are required to provide management's assessment of internal controls in conjunction with the filing of our Annual Report on Form 10-K. As disclosed under Item 9A of this report, our management concluded that our internal control over financial reporting was effective at December 31, 2014. In the future, our continued assessment, or the assessment by our independent registered public accounting firm, could reveal significant deficiencies or material weaknesses in our internal controls, which may need to be disclosed in future Annual Reports on Form 10-K. We believe, at the current time, that we are taking appropriate steps to mitigate these risks. However, disclosures of this type can cause investors to lose confidence in our financial reporting and may negatively affect the price of our common stock. Moreover, effective internal controls are necessary to produce reliable financial reports and to prevent fraud. Deficiencies in our internal controls over financial reporting may negatively impact our business and operations.

We rely on and are subject to risks associated with our reliance upon information technology systems.

Our success is dependent on the accuracy, reliability, and proper use of information processing systems and management information technology. Our information technology systems are designed and selected to facilitate order entry and customer billing, maintain distributor records, accurately track purchases and distributor compensation payments, manage accounting operations, generate reports, and provide customer service and technical support. Any interruption in these systems could have a material adverse effect on our business, financial condition, and results of operations.

Although we believe that the members of our software development team have the qualifications, know-how and experience to perform the necessary software development and other information technology services, there can be no assurance that there will not be delays or interruptions in these services. An interruption or delay in availability of these services could, if it lasted long enough, prevent us from accepting orders, cause distributors to leave our business, or otherwise materially adversely affect our business.

System failures and attacks could harm our business.

Because of our diverse geographic operations and our internationally applicable distributor compensation plans, our business is highly dependent on the efficient functioning of our information technology systems and operations, which are vulnerable to damage or interruption from fires, earthquakes, telecommunications failures, computer viruses and worms, hacking, denial of service attacks, software defects and other events. They are also subject to break-ins, sabotage, acts of vandalism and similar misconduct, as well as human error. Despite precautions implemented by our information technology staff, problems could result in interruptions in services and materially and adversely affect our business, financial condition and results of operations.

Moreover, hackers could attack our system seeking to retrieve personal or confidential information of ours or of third parties, such as credit card information used to purchase our products on-line. Although we take steps to prevent such loss of information, there can be no assurance that our system will not be successfully hacked. Laws in the United States and other jurisdictions where we do business require prompt notice of any such loss of information. Failure to comply with those reporting obligations could result in material penalties. In addition, if our system were hacked, we could incur material costs in investigating the incidents and could be liable for damages. Any such damages may or may not be covered by insurance.

Terrorist attacks, cyber-attacks, acts of war, epidemics or other communicable diseases or any other natural disasters may seriously harm our business.

Terrorist attacks, cyber-attacks, or acts of war or natural disasters may cause damage or disruption to us, our employees, our facilities and our distributors and customers, which could impact our revenues, expenses and financial condition. The potential for future terrorist attacks, the national and international responses to terrorist attacks, and other acts of war or hostility, such as the Chinese objection to the Taiwan independence movement and its resultant tension in the Taiwan Strait, could materially and adversely affect our business, results of operations, and financial condition in ways that we currently cannot predict. Additionally, natural disasters less severe than the Indian Ocean tsunami that occurred in December 2004 may adversely affect our business, financial condition and results of operations.

Because our systems, software and data reside on third-party servers, our access could be temporarily or permanently interrupted.

Beginning in 2012, most of our systems, software and data reside in the “cloud” on third-party servers to which we have contractual access. Cyber-attacks or hacking on these servers unrelated to us, or system or hardware failures experienced by the third party vendor, could result in disclosure of or damage to our systems, software and data. Moreover, any delay or failure in payment of the third party vendors, disputes with such vendors, or business interruption or failure of the third party vendors could result in loss of or interruption in access to our systems, software or data. It is possible that our systems, software and data could in the future be moved to servers of different third parties or to our own servers. Any such move could result in temporary or permanent loss of access to our systems, software or data. Any protracted loss of such access would materially and adversely affect our business, financial condition and results of operations.

We may experience substantial negative cash flows, which may have a significant adverse effect on our business and could threaten our solvency.

We experienced substantial negative cash flows during the years ended December 31, 2008 and 2009, primarily due to declines in our revenues greater than the decreases in expenditures we could manage. If we again experience negative cash flows, any resulting decreasing cash balance could impair our ability to support our operations and, eventually, threaten our solvency, which would have a material adverse effect on our business, results of operations and financial condition, as well as our stock price. Negative cash flows and the related adverse market perception associated therewith may have negatively affected, and may in the future negatively affect, our ability to attract new distributors and/or sell our products. There can be no assurance that we will be successful in maintaining an adequate level of cash resources and we could be forced to act more aggressively in the area of expense reduction in order to conserve cash resources as we look for alternative solutions.

If we experience negative cash flows, we may need to seek additional debt or equity financing, which may not be available on acceptable terms or at all. If available, it could have a highly dilutive effect on the holdings of existing stockholders.

Unless we are able to at least maintain revenues, control expenses and achieve positive cash flows, our ability to support our obligations could be impaired and our liquidity could be adversely affected and our solvency and our ability to repay our debts when they come due could be threatened. We may need to seek additional debt or equity financing on acceptable terms in order to improve our liquidity. However, we may not be able to obtain additional debt or equity financing on satisfactory terms, or at all, and any new financing could have a dilutive effect to our existing stockholders.

Disappointing quarterly revenue or operating results could cause the price of our common stock to fall.

Our quarterly revenue and operating results are difficult to predict and may fluctuate significantly from quarter to quarter. If our quarterly revenue or operating results fall below the expectations of investors or securities analysts, the price of our common stock could fall substantially.

Our common stock is particularly subject to volatility because of the industry in which we operate.

The market prices of securities of direct selling companies have been extremely volatile, and have experienced fluctuations that have often been unrelated or disproportionate to the operating performance of such

companies. These broad market fluctuations could adversely affect the market price of our common stock.

The historic price of our common stock has been volatile and the future market price of our common stock is likely to continue to be volatile. Further, the limited trading volume in our common stock has, and in the future may, contribute significantly to the high volatility in the market price of our common stock. This may make it more difficult for holders of our common stock to sell shares when they want and at prices they find attractive.

The public market for our common stock has historically been very volatile. Prior to February 17, 2015, our common stock was quoted on the OTCQB tier of the OTC Market and, like many other stocks quoted on the OTCQB, trading in our common stock was often thin and characterized by wide fluctuations in trading prices. Although we are hopeful that the transition to trading our common stock on the NASDAQ Capital Market will reduce the historical volatility in our common stock, it is likely that our common stock will continue to experience volatility for some time. There are a number of factors that may contribute to this volatility, but the limited trading volume in our common stock has, and in the future may, contribute significantly to volatility. This volatility may make it more difficult for holders of our common stock to sell shares when they want and at prices they find attractive. There can be no assurance that a larger or more liquid market will be developed or maintained for our common stock.

Future sales by us or our existing stockholders could depress the market price of our common stock.

If we or our existing stockholders sell a large number of shares of our common stock, the market price of our common stock could decline significantly. Further, even the perception in the public market that we or our existing stockholders might sell shares of common stock could depress the market price of the common stock.

Item 1B. UNRESOLVED STAFF COMMENTS

Not applicable.

Item 2. PROPERTIES

We lease 3,800 square feet of office space in Dallas, Texas for our corporate headquarters. In January 2015, we entered into a lease for 3,700 square feet of office space in Rolling Hills Estates, California with the intention of relocating some Dallas-based employees and hiring additional staff. The California location will make traveling to and communicating with Asia easier. In addition, we are intending to execute a lease for 2,400 square foot of retail space in Monterrey Park, California to help further develop the Chinese-American market in Southern California. Outside the United States, we lease office space in Hong Kong, China, Japan, Taiwan, South Korea and Singapore. We also lease a multi-purposed facility in Zhongshan, China that serves the needs of Chinese consumers. We contract with third parties for fulfillment and distribution operations in most of our international markets. Through a local service provider, we maintain marketing and distributor centers in Almaty, Kazakhstan, and Odessa, Ukraine. We believe that our existing office space is in good condition, suitable and adequate for the conduct of our business.

Item 3. LEGAL PROCEEDINGS

None.

Item 4. MINE SAFETY DISCLOSURES

Not applicable.

Part II

Item MARKET FOR REGISTRANT'S COMMON EQUITY, RELATED STOCKHOLDER MATTERS AND 5. ISSUER PURCHASES OF EQUITY SECURITIES

Market Information

Our common stock is currently traded on the NASDAQ Capital Market ("Nasdaq") under the symbol "NHTC." Prior to February 17, 2015, our common stock was quoted under the trading symbol "NHTC" on the OTCQB tier of the OTC Market. The following table sets forth the range of the high and low bid quotations of our common stock as reported by the OTC Markets Group, Inc. The bid quotations reflect inter-dealer prices, without retail mark-up, mark-down or commission and may not necessarily represent actual transactions.

	2013		2014	
	High	Low	High	Low
First quarter	\$1.44	\$1.01	\$4.95	\$2.81
Second quarter	1.30	0.80	7.50	4.80
Third quarter	2.20	0.93	19.85	6.76
Fourth quarter	3.40	1.86	13.80	8.05

On February 27, 2015, the closing price of our common stock as reported by Nasdaq was \$13.05 per share.

Holders of Record

At February 27, 2015, there were approximately 160 record holders of our common stock (although we believe that the number of beneficial owners of our common stock is substantially greater).

Dividends

No dividends were ever declared or paid on our common stock prior to 2014. At December 31, 2013, we had accrued unpaid dividends of \$98,000 with respect to outstanding shares of Series A preferred stock, but such dividends had not

been declared and we were under no obligation to pay such accrued dividends except in certain extraordinary circumstances. On March 7, 2014, the Board of Directors declared a dividend on each share of outstanding Series A preferred stock in the amount of \$0.81507 per share representing the accrued unpaid dividends from May 4, 2007 through March 7, 2014. All outstanding shares of Series A preferred stock were converted into common stock during 2014. The following table summarizes all cash dividend activity during 2014 (in thousands, except per share data):

Declaration Date	Dividends Per Share		Amount	Date Payable
	Preferred	Common		
March 7, 2014	\$0.815	\$ 0.005	\$ 159	April 8, 2014
May 6, 2014	0.020	0.005	62	June 4, 2014
July 29, 2014	0.027	0.010	127	August 27, 2014
November 4, 2014	0.032	0.010	128	December 3, 2014
Total	\$0.894	\$ 0.030	\$ 476	

Additionally, on February 27, 2015, the Board of Directors declared a dividend of \$0.02 on each share of common stock outstanding. Such dividends are payable in cash on March 27, 2015 to stockholders of record on March 17, 2015. Payment of any future dividends on shares of common stock will be at the discretion of the Company's Board of Directors.

Equity Compensation Plan Information

The following table sets forth information regarding all compensation plans under which Company equity securities are authorized for issuance as of December 31, 2014:

Plan Category	Number of securities to be issued upon exercise of outstanding options, warrants and rights (a)	Weighted-average exercise price of outstanding options, warrants and rights (b)	Number of securities remaining available for future issuance under equity compensation plans (excluding securities reflected in column (a)) (c)	
Equity compensation plans approved by security holders	—	\$ —	—	1,083
Equity compensation plans not approved by security holders	—	\$ —	—	—
Total	—	\$ —	—	1,083

Purchases of Equity Securities by the Issuer and Affiliated Purchasers

A summary of the Company's purchases of shares of its common stock during the quarter ended December 31, 2014 is as follows:

Period	Total Number of Shares Purchased (a)	Average Price Paid Per Share	Total Number of Shares Purchased as Part of Publicly Announced Plans or	Maximum Number (or Approximate Dollar Value) of Shares that May Yet Be Purchased Under the
--------	---	------------------------------	---	--

Edgar Filing: NATURAL HEALTH TRENDS CORP - Form 10-K

			Programs ^(b)	Plans or Programs ^(c)
October 1–31, 2014	2,100	\$ 9.98	53,835	\$ 262,015
November 1—30, 2014	216,737	\$ 12.26	270,572	\$ 2,148,200
December 1—31, 2014	146,927	\$ 12.82	417,499	\$ 235,100

^(a) The shares were purchased in open market transactions as described in footnote (b) below, except for those shares purchased under the Stock Repurchase Agreement also described in footnote (b) below.

On August 13, 2012, the Company disclosed in its Quarterly Report on Form 10-Q that its Board of Directors had, on that day, authorized the Company, acting as trustee for certain of its employees, to execute a Rule 10b5-1 plan to purchase 100,000 shares of its common stock in accordance with guidelines specified under Rule 10b5-1 of the Exchange Act and the Company's policies regarding stock transactions (the “Employee Plan”). The Company may ^(b) terminate the plan at any time. The employees for whom the Company will purchase stock as trustee under the plan will receive the stock as incentive compensation in quarterly increments over three years beginning March 15, 2013, provided that they are employees of the Company on the date of the distribution. Any stock that is purchased under the plan that is forfeited by an employee whose employment terminates will be delivered to the Company and held by it as treasury stock.

On November 4, 2014, the Board of Directors approved a special, stock repurchase program of up to \$5 million of the Company's outstanding shares of common stock (the “Repurchase Plan”). In connection therewith, the Company was advised by George K. Broady, a director of the Company and owner of more than 5% of its outstanding common stock, that Mr. Broady desired to participate in the Repurchase Plan on a basis roughly proportional to his ownership interest, with an estimate of generating approximately \$1.5 million through the sale of a portion of the shares of the Company's common stock held by him. After noting Mr. Broady's participation interest, the Company authorized its broker to proceed with the purchase of shares of the Company's common stock in the open market for a total purchase price of \$3.0 million in accordance with Rules 10b5-1 and 10b-18 under the Exchange Act.

On November 14, 2014, the Company entered into a Stock Repurchase Agreement (the “Stock Repurchase Agreement”) with Mr. Broady in accordance with Rule 10b5-1 under the Exchange Act. The Stock Repurchase Agreement provided for the Company's purchase from Mr. Broady of one-half of the number of shares of common stock purchased by the Company's broker in the open market under the Repurchase Plan approved by the Company's Board of Directors on November 4, 2014. The Stock Repurchase Agreement with Mr. Broady required that the Company report to Mr. Broady on a weekly basis information regarding the broker's open market purchases, and that the Company purchase from Mr. Broady on a weekly basis at a per share purchase price equal to the weighted average price per share paid by the Company's broker to purchase shares in the open market.

The Company, as Trustee, began purchasing under the Employee Plan in December 2012. Under the initial 10b5-1 plan executed by the Company, as Trustee, with the Board's authorization, the Company would not purchase more than 2,800 shares per month. That 10b5-1 plan was replaced by a new 10b5-1 plan effective November 11, 2013, which was amended on May 13, 2014 and again on October 23, 2014. The latest 10b5-1 plan terminated in November 2014, and the Company, as Trustee, has not entered into a new 10b5-1 plan.

The Repurchase Plan was completed on December 17, 2014, and resulted in the Company purchasing an aggregate of 359,840 shares of its common stock for a purchase price of \$4.5 million, plus transaction costs. Of that total, the Company purchased 119,947 shares from Mr. Broady under the Stock Repurchase Agreement for an aggregate purchase price of \$1.5 million.

Item 6. SELECTED FINANCIAL DATA

Not applicable under smaller reporting company disclosure rules.

Item 7. MANAGEMENT’S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

Business Overview

We are an international direct-selling and e-commerce company. Subsidiaries controlled by us sell personal care, wellness, and “quality of life” products under the “NHT Global” brand. In most markets, we sell our products to an independent distributor network that either uses the products themselves or resells them to consumers. Our wholly-owned subsidiaries have an active physical presence in the following markets: North America; Greater China, which consists of Hong Kong, Taiwan and China; Commonwealth of Independent States, which consists of Russia, Kazakhstan and Ukraine; South Korea; Japan; and Europe, which consists of Italy and Slovenia.

Our distributor network operates in a seamless manner from market to market, except for the Chinese market, where we sell to consumers through an e-commerce platform. We believe that all of our operating segments should be aggregated into a single reportable segment as they have similar economic characteristics. Additionally, we believe that all of the operating segments are similar in the nature of the products sold, the product acquisition process, the types of customers products are sold to, the methods used to distribute the products, and the nature of the regulatory environment. Our e-commerce retail business in China does not require a direct selling license and allows for discounts on volume purchases. There is no separate segment manager who is held accountable by our chief operating decision-makers, or anyone else, for operations, operating results and planning for the Chinese market on a stand-alone basis. Accordingly, we consider ourselves to be in a single reporting segment and operating unit structure.

As of December 31, 2014, we were conducting business through 54,360 active distributors. We consider a distributor “active” if they have placed at least one product order with us during the preceding year. Our priority is to focus our resources in our most promising markets, which we consider to be Greater China and countries where our existing members have the connections to recruit prospects and sell our products, such as Southeast Asia. Up to \$10.0 million of our available cash may be invested in our Mainland China entity within the next 18 months for such purposes as establishing China-based manufacturing capabilities, opening additional Healthy Lifestyle Centers or branch offices, and ultimately, funding the mandated deposit and other requirements for a China direct selling license application. We also may evaluate product or distribution opportunities to diversify from our current Greater China concentration.

We generate approximately 98% of our net sales from subsidiaries located outside North America, with sales in Hong Kong representing 89% of net sales in the latest fiscal year. Because of the size of our foreign operations, operating results can be impacted negatively or positively by factors such as foreign currency fluctuations, and economic, political and business conditions around the world. In addition, our business is subject to various laws and regulations, in particular regulations related to direct selling activities that create certain risks for our business, including improper claims or activities by our distributors and potential inability to obtain necessary product registrations.

China has been and continues to be our most important business development project. In June 2004, we obtained a general business license in China. Direct selling is prohibited in China without a direct selling license which we do not have. In December 2005, we submitted a preliminary application for a direct selling license. In June 2006, we submitted a revised application package in accordance with new requirements issued by the Chinese government. In June 2007, we launched a new e-commerce retail platform in China that does not require a direct selling license. We believe this model, which offers discounts based on volume purchases, will encourage repeat purchases of our products for personal consumption in the Chinese market. The platform is designed to be in compliance with our understanding of current laws and regulations in China. In November 2007, we filed a new, revised direct selling application incorporating a name change, our new e-commerce model and other developments. These direct selling applications were not approved or rejected by the pertinent authorities, but did not appear to materially progress. By 2009, the information contained in the most recent application was stale. The Company applied to temporarily withdraw the license application in February 2009 to furnish new information and intends to amend its application with the goal to re-apply in the future. We are unable to predict whether we will be successful in obtaining a direct selling license to operate in China, and if we are successful, when we will be permitted to enhance our e-commerce retail platform with direct selling operations.

Most of our Hong Kong revenue is derived from the sale of products that are delivered to members in China. After consulting with outside professionals, we believe that our Hong Kong e-commerce business does not violate any applicable laws in China even though it is used for the internet purchase of our products by buyers in China. But the government in China could, in the future, officially interpret its laws and regulations – or adopt new laws and regulations – to prohibit some or all of our e-commerce activities with China and, if our members engage in illegal activities in China, those actions could be attributed to us. In addition, other Chinese laws regarding how and when members may assemble and the activities that they may conduct, or the conditions under which the activities may be conducted, in China are subject to interpretations and enforcement attitudes that sometimes vary from province to province, among different levels of government, and from time to time. Members sometimes violate one or more of the laws regulating these activities, notwithstanding training that we attempt to provide. Enforcement measures regarding these violations, which can include arrests, raise the uncertainty and perceived risk associated with conducting this business, especially among those who are aware of the enforcement actions but not the specific activities leading to the enforcement action. We believe that this has led some existing members in China – who are signed up as distributors in Hong Kong – to leave the business or curtail their selling activities and has led some potential members to choose not to participate. Among other things, we are combating this with more training and public relations efforts that are designed, among other things, to distinguish the Company from businesses that make no attempt to comply with the law. This environment creates uncertainty about the future of doing this type of business in China generally and under our business model, specifically. See “Item 1A. Risk Factors—Because our Hong Kong operations account for a majority of our overall business....”

Income Statement Presentation

We mainly derive revenue from sales of products, enrollment packages, and shipping charges. Substantially all of our product sales are to independent distributors at published wholesale prices. Product sales are recorded when the products are shipped and title passes to independent distributors, which generally is upon our delivery to the carrier that completes delivery to the distributors. We estimate and accrue a reserve for product returns based on our return policies and historical experience. Enrollment package revenue, including any nonrefundable set-up fees, is deferred and recognized over the term of the arrangement, generally twelve months.

Cost of sales consists primarily of products purchased from third-party manufacturers, freight cost for transporting products to our foreign subsidiaries and shipping products to distributors, import duties, packing materials, product royalties, costs of promotional materials sold to the Company's distributors at or near cost, and provisions for slow moving or obsolete inventories. Cost of sales also includes purchasing costs, receiving costs, inspection costs and warehousing costs.

Distributor commissions are typically our most significant expense and are classified as an operating expense. Under our compensation plan, distributors are paid weekly commissions, generally in their home country currency, for product purchases by their down-line distributor network across all geographic markets, except China, where we launched an e-commerce retail platform and do not pay any commissions. This "seamless" compensation plan enables a distributor located in one country to sponsor other distributors located in other countries where we are authorized to conduct our business. Currently, there are basically two ways in which our distributors can earn income:

Through retail markups on sales of products purchased by distributors at wholesale prices (in some markets, sales are for personal consumption only and income may not be earned through retail mark-ups on sales in that market); and Through commissions paid on product purchases made by their down-line distributors.

Each of our products is designated a specified number of bonus volume points. Commissions are based on total personal and group bonus volume points per sales period. Bonus volume points are essentially a percentage of a product's wholesale cost. As the distributor's business expands from successfully sponsoring other distributors who in turn expand their own businesses by sponsoring other distributors, the distributor receives higher commissions from purchases made by an expanding down-line network. To be eligible to receive commissions, a distributor may be required to make nominal monthly or other periodic purchases of our products. Certain of our subsidiaries do not require these nominal purchases for a distributor to be eligible to receive commissions. In determining commissions, the number of levels of down-line distributors included within the distributor's commissionable group increases as the number of distributorships directly below the distributor increases. Under our current compensation plan, certain of our commission payouts may be limited to a hard cap dollar amount per week or a specific percentage of total product sales. In some markets, commissions may be further limited. In some markets, we also pay certain bonuses on purchases by up to three generations of personally sponsored distributors, as well as bonuses on commissions earned by up to three generations of personally sponsored distributors. Distributors can also earn income, trips and other

prizes in specific time-limited promotions and contests we hold from time to time. Distributor commissions are dependent on the sales mix and, for each of fiscal 2013 and 2014, represented 46% of net sales. From time to time we make modifications and enhancements to our compensation plan to help motivate distributors, which can have an impact on distributor commissions. From time to time we also enter into agreements for business or market development, which may result in additional compensation to specific distributors.

Selling, general and administrative expenses consist of administrative compensation and benefits (including stock-based compensation), travel, credit card fees and assessments, professional fees, certain occupancy costs, and other corporate administrative expenses. In addition, this category includes selling, marketing, and promotion expenses including costs of distributor training events and conventions, which are designed to increase both product awareness and distributor recruitment. Because our various distributor conventions are not always held at the same time each year, interim period comparisons will be impacted accordingly.

The functional currency of our international subsidiaries is generally their local currency. Local currency assets and liabilities are translated at the rates of exchange on the balance sheet date, and local currency revenues and expenses are translated at average rates of exchange during the period. Equity accounts are translated at historical rates. The resulting translation adjustments are recorded directly into a separate component of stockholders' equity and represent the only component of accumulated other comprehensive income.

Sales by our foreign subsidiaries are transacted in the respective local currencies and are translated into U.S. dollars using average rates of exchange for each monthly accounting period to which they relate. Most of our product purchases from third-party manufacturers are transacted in U.S. dollars. Consequently, our sales and net earnings are affected by changes in currency exchange rates, with sales and earnings generally increasing with a weakening U.S. dollar and decreasing with a strengthening U.S. dollar.

Results of Operations

The following table sets forth our operating results as a percentage of net sales for the periods indicated.

	Year Ended December 31,	
	2013	2014
Net sales	100.0%	100.0%
Cost of sales	23.9	21.7
Gross profit	76.1	78.3
Operating expenses:		
Distributor commissions	45.8	45.7
Selling, general and administrative expenses	22.2	15.8
Depreciation and amortization	0.1	0.1
Total operating expenses	68.1	61.6
Income from operations	8.0	16.7
Other expense, net	—	(0.2)
Income before income taxes	8.0	16.5
Income tax provision	0.2	0.2
Net income	7.8 %	16.3 %

Net Sales

The following table sets forth revenue by market for the periods indicated (in thousands):

	Year Ended December 31,					
	2013			2014		
North America	\$2,361	4.5	%	\$2,812	2.3	%
Hong Kong	40,585	77.3		111,028	89.1	
China	791	1.5		1,538	1.2	
Taiwan	3,387	6.4		4,628	3.7	
South Korea	702	1.3		1,009	0.8	
Japan	106	0.2		89	0.1	
Russia, Kazakhstan and Ukraine	4,354	8.3		3,113	2.5	
Europe	241	0.5		373	0.3	
Total	\$52,527	100.0%		\$124,590	100.0%	

Net sales were \$124.6 million for the year ended December 31, 2014 compared with \$52.5 million a year ago, an increase of \$72.1 million, or 137%. Hong Kong net sales increased \$70.4 million, or 174%, over the prior year. The sales increase was primarily due to a substantial increase in product sale volumes attributable to the effectiveness of the Company's leadership development, promotional programs, incentives, events, new products, training, commission plans and services.

Outside of our Hong Kong business, net sales in our Commonwealth of Independent States ("CIS") market were negatively impacted in 2014 by the political unrest in the region and decreased \$1.2 million, or 29%, over the prior year. Elsewhere, net sales increased \$2.9 million, or 38%, over the prior year, resulting in a total net sales increase in 2014 outside of our Hong Kong business of \$1.7 million, or 14%, over the prior year.

As of December 31, 2014, our operating subsidiaries had 54,360 active distributors, compared with 27,520 active distributors at December 31, 2013. Hong Kong experienced an increase of 26,520 active distributors, or 131%, from December 31, 2013 to December 31, 2014. This substantial increase in the number of active distributors is attributable to the same factors that contributed to the increase in net sales and product sale volumes on a year-over-year basis.

As of December 31, 2014, deferred revenue was \$2.7 million, which primarily consisted of \$1.2 million pertaining to unshipped product orders, \$815,000 pertaining to auto ship advances and \$222,000 pertaining to unamortized enrollment package revenue.

Gross Profit

Gross profit was 78.3% of net sales for the year ended December 31, 2014 compared with 76.1% of net sales for the year ended December 31, 2013. The gross profit margin percentage increase is primarily attributable to lower fees paid to our third-party service provider in the CIS market and less importation costs as a percentage of overall net sales, which occurs when sales from the CIS market comprise a lower percentage of our overall net sales. Additionally, the increase is attributable to higher product margins in Hong Kong due to a more favorable product mix. The margin increase is somewhat offset by a cost increase assessed by one of our Hong Kong third-party logistics service providers effective in the fourth quarter of 2013.

Distributor Commissions

Distributor commissions were 45.7% of net sales for the year ended December 31, 2014 compared with 45.8% of net sales for the year ended December 31, 2013. Though overall commissions as a percentage of net sales were flat year over year, there was a change in the composition. During 2014, commissions earned on a weekly basis increased 1%, mainly in Hong Kong; but that increase was offset by a comparable decrease in incentive program costs during 2014, primarily the Supreme Bonus Plan, which is tied to our international recognition program.

Selling, General and Administrative Expenses

Selling, general and administrative expenses were \$19.7 million for the year ended December 31, 2014 compared with \$11.6 million for the year ended December 31, 2013. Selling, general and administrative expenses increased by \$8.1 million, or 69%, mainly due to an increase in employee-related costs and incentive program accruals, as well as an increase in credit card fees and assessments due to higher net sales as compared to the same period in the prior year.

Other Expense, Net

Loss on foreign exchange was \$202,000 for the year ended December 31, 2014 primarily due to the impact of CIS market currency devaluation (against the U.S. dollar) on inter-company balances, namely the Ukrainian hryvnia, the Russian ruble and the Kazakhstani tenge. A loss on foreign exchange totaling \$32,000 was recognized for the year ended December 31, 2013.

Income Taxes

An income tax provision of \$266,000 was recognized for the year ended December 31, 2014 compared with \$102,000 for the year ended December 31, 2013. The increase is due to increased profitability of our operations both domestically and internationally. The Company did not recognize a tax benefit for U.S. tax purposes in 2013 due to uncertainty that the benefit will be realized.

Liquidity and Capital Resources

At December 31, 2014, the Company's cash and cash equivalents totaled \$44.8 million. Total cash and cash equivalents increased by \$10.3 million and \$30.3 million during 2013 and 2014, respectively.

At December 31, 2014, the ratio of current assets to current liabilities was 2.03 to 1.00 and the Company had \$25.2 million of working capital. Current liabilities included deferred revenue of \$2.7 million that consisted primarily of unshipped product orders, auto ship advances and unamortized enrollment package revenues. The ratio of current assets to current liabilities excluding deferred revenue was 2.28 to 1.00. Working capital as of December 31, 2014 increased \$21.8 million compared to the Company's working capital as of December 31, 2013, due to cash generated from operations.

Cash provided by operations during 2014 was \$30.6 million compared to \$10.7 million during 2013. The increase in operating cash flows results primarily from the net sales increase year over year. Additionally, the timing difference of cash outlays associated with both distributor and employee incentive programs contributed to the increase as the current year expenses were greater than those recognized in the prior year.

Cash flows used in investing activities totaled \$339,000 during 2014, primarily the result of buildout costs incurred at the multi-purposed facility in Zhongshan, China and renovations in the Taipei, Taiwan office. Cash flows used in investing activities totaled \$292,000 during 2013, of which \$210,000 were purchases of property and equipment. The buildout of the multi-purposed facility in Zhongshan, China began in November 2013 and such costs totaled \$102,000 during 2013. Also, as a result of increased sales in South Korea during 2013, additional cash deposits in the amount of \$82,000 were required to be held by a certain South Korean credit card processing company.

Cash flows used in financing activities during 2014 totaled \$189,000. Warrants to purchase 1,407,855 shares of common stock were exercised during 2014 at exercise prices ranging from \$3.5108 to \$3.52 per share for total proceeds of \$4.9 million. Offsetting this amount, on November 4, 2014, the Board of Directors approved a special stock repurchase program of up to \$5.0 million of the Company's outstanding shares of common stock. The stock repurchase program was completed on December 17, 2014 and resulted in stock repurchases totaling \$4.5 million, plus transaction costs. George K. Broady, a director and an owner of more than 5% of the Company's outstanding common stock, participated in the Company's repurchase program on a basis roughly proportional to his ownership interest, selling approximately \$1.5 million of the Company's common stock held by him (see Note 8 of the Notes to Consolidated Financial Statements in Item 8 of this report). Additionally, other financing cash outflows included cash dividend payments of \$476,000 and the repurchase of shares of common stock pursuant to Rule 10b5-1 under a program authorized by the Board of Directors for the Company to purchase 100,000 shares, acting as Trustee for certain of its non-officer, overseas employees. Such repurchases totaled \$159,000 and \$52,000 during 2014 and 2013, respectively. No additional financing activities occurred during 2013.

The following table summarizes the Company's cash dividend activity during 2014 (in thousands, except per share data):

Declaration Date	Dividends Per Share		Amount	Date Payable
	Preferred	Common		
March 7, 2014	\$0.815	\$ 0.005	\$ 159	April 8, 2014
May 6, 2014	0.020	0.005	62	June 4, 2014
July 29, 2014	0.027	0.010	127	August 27, 2014
November 4, 2014	0.032	0.010	128	December 3, 2014
Total	\$0.894	\$ 0.030	\$ 476	

On February 27, 2015, the Board of Directors declared a cash dividend of \$0.02 on each share of common stock outstanding. Such dividends are payable on March 27, 2015 to stockholders of record on March 17, 2015. Payment of any future dividends on shares of common stock will be at the discretion of the Company's Board of Directors.

The Company believes that its existing internal liquidity, supported by cash on hand and cash flows from operations should be adequate to fund normal business operations and address its financial commitments for at least the next 12 months, assuming no significant unforeseen expense or revenue decline. If the Company's foregoing beliefs or assumptions prove to be incorrect, however, the Company's business, results of operations and financial condition could be materially adversely affected. See "Item 1A. Risk Factors."

The Company does not have any significant unused sources of liquid assets. If necessary, the Company may attempt to generate more funding from the capital markets, but currently does not believe that will be necessary.

On October 19, 2007, the Company issued warrants to purchase 3,141,499 shares of common stock in connection with a convertible debentures financing. The warrants consisted of seven-year warrants to purchase 1,495,952 shares of common stock, one-year warrants to purchase 1,495,952 shares of common stock, and five-year warrants to purchase 149,595 shares of common stock. The term for each of the warrants began six months and one day after their respective issuance and each had an exercise price of \$3.52 per share. Such one-year warrants expired unexercised on April 21, 2009 and such five-year warrants expired unexercised on April 21, 2013. Of the seven-year warrants to purchase 1,495,952 shares of common stock, as of February 27, 2015, warrants to purchase 88,097 shares of common stock remain outstanding with an exercise price of \$3.5082 per share. Such exercise price was adjusted as a result of cash dividends declared during 2014 on each share of outstanding common stock in accordance with the terms of the related warrant agreement. The exercise price per share may be further adjusted on March 17, 2015, the record date for the dividends declared on February 27, 2015. The unexercised warrants expire April 21, 2015 if not previously exercised.

Our priority is to focus our resources in our most important markets, which we consider to be Greater China and countries where our existing members may have the connections to recruit prospects and sell our products, such as Southeast Asia. Up to \$10.0 million of our available cash may be invested in our Mainland China entity within the next 18 months for such purposes as establishing China-based manufacturing capabilities, opening additional Healthy Lifestyle Centers or branch offices, and ultimately, funding the required deposit for a China direct selling license application. We also may evaluate product or distribution opportunities to diversify from our current Greater China concentration.

The Company has entered into non-cancelable operating lease agreements for locations within the United States and for its international subsidiaries, with expirations through March 2018.

In May 2013, the Company entered into an exclusive distribution agreement with one of its suppliers to purchase its product through July 2016. To maintain exclusivity, the Company is required to purchase a minimum of \$40,000 of product per month until the termination date. As of December 31, 2014, the Company was in compliance with the exclusivity provision.

In December 2014, the Company amended a supply agreement with one of its suppliers to obtain worldwide exclusivity in return for purchasing a minimum of \$3.3 million of product annually. If the Company does not purchase the minimum product as required, then a Cure Payment, as defined, will be due to the supplier. The term of the agreement is three years commencing on January 1, 2015 and shall automatically renew for successive three year terms unless notice of termination is provided by either party.

The Company has employment agreements with certain members of its management team that can be terminated by either the employee or the Company upon four weeks' notice. The employment agreements entered into with the management team contain provisions that guarantee the payments of specified amounts in the event of a change in control, as defined, or if the employee is terminated without cause, as defined, or terminates employment for good reason, as defined. In addition, the Company has an employment agreement with another employee that can be terminated at will by either the employee or the Company, provided that the Company must pay a specified amount if it terminates the agreement without cause, as defined, or the employee terminates the agreement with good reason, as defined. Accrued severance totaling \$12,000 as of December 31, 2014 was paid in January 2015.

Critical Accounting Policies and Estimates

A summary of our significant accounting policies is provided in Note 1 of the Notes to Consolidated Financial Statements in Item 8 of this report. The preparation of financial statements in accordance with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that

affect the reported amounts of assets and liabilities and the disclosure of contingent assets and liabilities at the date of the consolidated financial statements and the reported amounts of revenues and expenses during the reported period. The process of determining significant estimates is fact specific and takes into account historical experience and current and expected economic conditions. To the extent that there are material differences between the estimates and actual results, future results of operations will be affected.

Critical accounting policies and estimates are defined as both those that are material to the portrayal of our financial condition and results of operations and as those that require management's most subjective judgments. Management believes the Company's critical accounting policies and estimates are those related to obsolete inventory and the fair value of acquired intangible assets, including goodwill, revenue recognition, as well as those used in the determination of liabilities related to sales returns, distributor commissions and income taxes.

Inventory Valuation. The Company reviews its inventory carrying value and compares it to the net realizable value of its inventory and any inventory value in excess of net realizable value is written down. In addition, the Company reviews its inventory for obsolescence and any inventory identified as obsolete is reserved or written off. The Company's determination of obsolescence is based on assumptions about the demand for its products, product expiration dates, estimated future sales, and management's future plans. Also, if actual sales or management plans are less favorable than those originally projected by management, additional inventory reserves or write-downs may be required. At December 31, 2013 and 2014, the Company's inventory value was \$1.8 million and \$3.8 million, respectively, net of reserves of zero and \$18,000, respectively. No significant provision was recorded during the periods presented.

Valuation of Goodwill. The Company assesses qualitative factors in order to determine whether it is more likely than not that the fair value of a reporting unit is less than its carrying amount. If, through this qualitative assessment, the conclusion is made that it is more likely than not that a reporting unit's fair value is less than its carrying amount, a two-step impairment test is performed. The Company's policy is to test for impairment annually during the fourth quarter. At December 31, 2013 and 2014, goodwill of \$1.8 million was reflected on the Company's balance sheet. No impairment of goodwill was recognized during the periods presented.

Allowance for Sales Returns. An allowance for sales returns is provided during the period the product is shipped. The allowance is based upon the return policy of each country, which varies from 14 days to one year, and their historical return rates, which range from 1% to 7% of sales. Sales returns were 1% and 2% of sales for the years ended December 31, 2013 and 2014, respectively. The allowance for sales returns was \$504,000 and \$654,000 at December 31, 2013 and 2014, respectively. No material changes in estimates have been recognized during the periods presented.

Revenue Recognition. Product sales are recorded when the products are shipped and title passes to independent distributors. Product sales to distributors are made pursuant to a distributor agreement that provides for transfer of both title and risk of loss upon our delivery to the carrier that completes delivery to the distributors, which is commonly referred to as “F.O.B. Shipping Point.” The Company primarily receives payment by credit card at the time distributors place orders. The Company’s sales arrangements do not contain right of inspection or customer acceptance provisions other than general rights of return. Amounts received for unshipped product are recorded as deferred revenue. Such amounts totaled \$1.9 million and \$1.2 million at December 31, 2013 and 2014, respectively. Shipping charges billed to distributors are included in net sales. Costs associated with shipments are included in cost of sales.

Enrollment package revenue, including any nonrefundable set-up fees, is deferred and recognized over the term of the arrangement, generally twelve months. Enrollment packages provide distributors access to both a personalized marketing website and a business management system. No upfront costs are deferred as the amount is nominal. At December 31, 2013 and 2014, enrollment package revenue totaling \$182,000 and \$222,000 was deferred, respectively. Although the Company has no immediate plans to significantly change the terms or conditions of enrollment packages, any changes in the future could result in additional revenue deferrals or could cause us to recognize the deferred revenue over a longer period of time. Additionally, deferred revenue includes advances for auto ship orders. In certain markets, when a distributor’s cumulative commission income reaches a certain threshold, a percentage of the distributor’s weekly commission is held back as an advance and applied to an auto ship order once the accumulated amount of the advances is sufficient to pay for the pre-selected auto ship package of the distributor. Such advances were \$449,000 and \$815,000 at December 31, 2013 and 2014, respectively.

Distributor Commissions. Independent distributors earn commissions based on total personal and group bonus volume points per weekly sales period. Each of our products are designated a specified number of bonus volume points, which is essentially a percentage of the product’s wholesale price. The Company accrues commissions when earned and pays commissions on product sales generally two weeks following the end of the weekly sales period.

In some markets, we also pay certain bonuses on purchases by up to three generations of personally sponsored distributors, as well as bonuses on commissions earned by up to three generations of personally sponsored distributors. Independent distributors may also earn incentives based on meeting certain qualifications during a designated incentive period, which may range from several weeks to up to a year. These incentives may be both monetary and non-monetary in nature. The Company estimates and accrues the costs associated with incentives over the duration of the qualification period based on distributor achievement of the qualification requirements. Accrued commissions, including the estimated cost of our international recognition incentive program and other supplemental programs, totaled \$4.0 million and \$8.9 million at December 31, 2013 and 2014, respectively.

Tax Valuation Allowance. The Company evaluates the probability of realizing the future benefits of any of its deferred tax assets and records a valuation allowance when it believes a portion or all of its deferred tax assets may not be realized. The Company increased the valuation allowance to equal its net deferred tax assets during 2005 due to the uncertainty of future operating results. The valuation allowance will be reduced at such time as management believes it is more likely than not that the deferred tax assets will be realized. During 2013 and 2014, no such reduction in the valuation allowance occurred. Any reductions in the valuation allowance will reduce future income tax provisions.

Provision for income taxes depends on the statutory tax rates in each of the jurisdictions in which we operate. We believe that we operate in compliance with all applicable transfer pricing laws and we intend to continue to operate in compliance with such laws. However, there can be no assurance that we will continue to be found to be operating in compliance with transfer pricing laws, or that those laws would not be modified, which, as a result, may require changes in our operating procedures. If the United States Internal Revenue Service or the taxing authorities of any other jurisdiction were to successfully challenge these agreements, plans, or arrangements, or require changes in our transfer pricing practices, we could be required to pay higher taxes, interest and penalties, and our earnings would be adversely affected.

Item 7A. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

Not applicable under smaller reporting company disclosure rules.

Item 8. FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA

NATURAL HEALTH TRENDS CORP.

INDEX TO CONSOLIDATED FINANCIAL STATEMENTS

	<u>Page</u>
Report of Lane Gorman Trubitt, PLLC, Independent Registered Public Accounting Firm	33
Consolidated Balance Sheets	34
Consolidated Statements of Operations	35
Consolidated Statements of Comprehensive Income	36
Consolidated Statements of Stockholders' Equity	37
Consolidated Statements of Cash Flows	38
Notes to Consolidated Financial Statements	39

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

Board of Directors and Stockholders

Natural Health Trends Corp.

Dallas, Texas

We have audited the accompanying consolidated balance sheets of Natural Health Trends Corp. (the “Company”) as of December 31, 2014 and 2013, and the related consolidated statements of operations, comprehensive income, stockholders’ equity, and cash flows for each of the years in the two-year period ended December 31, 2014. The Company’s management is responsible for these financial statements. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free of material misstatement. The Company is not required to have, nor were we engaged to perform, an audit of its internal control over financial reporting. Our audit included consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company’s internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the consolidated financial position of Natural Health Trends Corp. as of December 31, 2014 and 2013, and the results of its operations and its cash flows for each of the years in the two-year period ended December 31, 2014, in conformity with accounting principles generally accepted in the United States of America.

/s/ Lane Gorman Trubitt, PLLC

Dallas, Texas

March 6, 2015

33

NATURAL HEALTH TRENDS CORP.

CONSOLIDATED BALANCE SHEETS

(In Thousands, Except Share Data)

	December 31,	
	2013	2014
ASSETS		
Current assets:		
Cash and cash equivalents	\$14,550	\$44,816
Accounts receivable	134	107
Inventories, net	1,828	3,760
Other current assets	658	930
Total current assets	17,170	49,613
Property and equipment, net	265	476
Goodwill	1,764	1,764
Restricted cash	328	315
Other assets	300	372
Total assets	\$19,827	\$52,540
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current liabilities:		
Accounts payable	\$3,058	\$2,232
Income taxes payable	25	268
Accrued distributor commissions	3,962	8,853
Other accrued expenses	3,146	6,743
Deferred revenue	2,569	2,687
Deferred tax liability	108	65
Amounts held in distributor eWallets	—	2,064
Other current liabilities	882	1,513
Total current liabilities	13,750	24,425
Long-term incentive	—	1,665
Total liabilities	13,750	26,090
Commitments and contingencies		
Stockholders' equity:		
Preferred stock, \$0.001 par value; 5,000,000 shares authorized; 1,761,900 shares designated Series A convertible preferred stock at December 31, 2013, 123,693 shares issued and outstanding at December 31, 2013	111	—
Common stock, \$0.001 par value; 50,000,000 shares authorized; 11,359,769 and 12,891,317 shares issued at December 31, 2013 and 2014, respectively	11	13
Additional paid-in capital	80,690	85,750

Edgar Filing: NATURAL HEALTH TRENDS CORP - Form 10-K

Accumulated deficit	(74,619)	(54,799)
Accumulated other comprehensive income (loss):		
Foreign currency translation adjustments	(81)	62
Treasury stock, at cost; 26,998 and 384,220 shares at December 31, 2013 and 2014, respectively	(35)	(4,576)
Total stockholders' equity	6,077	26,450
Total liabilities and stockholders' equity	\$ 19,827	\$ 52,540

See accompanying notes to consolidated financial statements.

NATURAL HEALTH TRENDS CORP.

CONSOLIDATED STATEMENTS OF OPERATIONS

(In Thousands, Except Per Share Data)

	Year Ended December 31,	
	2013	2014
Net sales	\$52,527	\$124,590
Cost of sales	12,551	26,981
Gross profit	39,976	97,609
Operating expenses:		
Distributor commissions	24,053	56,997
Selling, general and administrative expenses (including stock-based compensation expense of \$110 and \$49 during 2013 and 2014, respectively)	11,634	19,687
Depreciation and amortization	66	105
Total operating expenses	35,753	76,789
Income from operations	4,223	20,820
Other expense, net	(32)	(184)
Income before income taxes	4,191	20,636
Income tax provision	102	266
Net income	4,089	20,370
Preferred stock dividends	(15)	(10)
Net income available to common stockholders	\$4,074	\$20,360
Income per common share:		
Basic	\$0.36	\$1.67
Diluted	\$0.36	\$1.61
Weighted-average number of common shares outstanding:		
Basic	11,154	12,131
Diluted	11,331	12,600

See accompanying notes to consolidated financial statements.

NATURAL HEALTH TRENDS CORP.

CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

(In Thousands)

	Year Ended December 31,	
	2013	2014
Net income	\$4,089	\$20,370
Other comprehensive income, net of tax:		
Foreign currency translation adjustments	21	143
Comprehensive income	\$4,110	\$20,513

See accompanying notes to consolidated financial statements.

NATURAL HEALTH TRENDS CORP.

CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY

(In Thousands, Except Share Data)

	Preferred Stock Shares	Preferred Stock Amount	Common Stock Shares	Common Stock Amount	Additional Paid-In Capital	Accumulated Deficit	Accumulated Other Comprehensive Loss	treasury Stock Shares	treasury Stock Amount	Total
BALANCE, December 31, 2012	138,400	\$ 124	11,345,062	\$ 11	\$ 80,591	\$(78,708)	\$(102)	(21,014)	\$(7)	\$ 1,909
Net income	—	—	—	—	—	4,089	—	—	—	4,089
Conversion of Series A preferred stock	(14,707)	(13)	14,707	—	13	—	—	—	—	—
Repurchase of common stock	—	—	—	—	—	—	—	(32,660)	(52)	(52)
Shares issued for stock-based compensation awards	—	—	—	—	(24)	—	—	26,676	24	—
Foreign currency translation adjustments	—	—	—	—	—	—	21	—	—	21
Stock-based compensation	—	—	—	—	110	—	—	—	—	110
BALANCE, December 31, 2013	123,693	111	11,359,769	11	80,690	(74,619)	(81)	(26,998)	(35)	6,077
Net income	—	—	—	—	—	20,370	—	—	—	20,370
Conversion of Series A preferred stock	(123,693)	(111)	123,693	—	111	—	—	—	—	—
Exercise of warrants	—	—	1,407,855	2	4,946	—	—	—	—	4,948
Repurchase of common stock	—	—	—	—	—	—	—	(382,564)	(4,661)	(4,661)

Shares issued for stock-based compensation awards	—	—	—	—	(46)	(74)	—	25,342	120	—
Dividends declared	—	—	—	—	—	(476)	—	—	—	(476)
Foreign currency translation adjustments	—	—	—	—	—	—	143	—	—	143
Stock-based compensation	—	—	—	—	49	—	—	—	—	49
BALANCE, December 31, 2014	—	\$—	12,891,317	\$ 13	\$ 85,750	\$(54,799)	\$ 62	(384,220)	\$(4,576)	\$ 26,450

See accompanying notes to consolidated financial statements.

NATURAL HEALTH TRENDS CORP.

CONSOLIDATED STATEMENTS OF CASH FLOWS

(In Thousands)

	Year Ended December 31,	
	2013	2014
CASH FLOWS FROM OPERATING ACTIVITIES:		
Net income	\$4,089	\$20,370
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	66	105
Stock-based compensation	110	49
Deferred income taxes	16	(43)
Changes in assets and liabilities:		
Accounts receivable	(17)	—
Inventories, net	(974)	(2,029)
Other current assets	(35)	(501)
Other assets	(38)	(85)
Accounts payable	1,673	(822)
Income taxes payable	16	243
Accrued distributor commissions	2,679	5,077
Other accrued expenses	1,467	3,706
Deferred revenue	1,738	147
Amounts held in distributor eWallets	—	2,065
Other current liabilities	(104)	666
Long-term incentive	—	1,665
Net cash provided by operating activities	10,686	30,613
CASH FLOWS FROM INVESTING ACTIVITIES:		
Purchases of property and equipment	(210)	(339)
Increase in restricted cash	(82)	—
Net cash used in investing activities	(292)	(339)
CASH FLOWS FROM FINANCING ACTIVITIES:		
Proceeds from exercise of warrants	—	4,948
Repurchase of common stock	(52)	(4,661)
Dividends paid	—	(476)
Net cash used in financing activities	(52)	(189)
Effect of exchange rates on cash and cash equivalents	1	181
Net increase in cash and cash equivalents	10,343	30,266

Edgar Filing: NATURAL HEALTH TRENDS CORP - Form 10-K

CASH AND CASH EQUIVALENTS, beginning of period	4,207	14,550
CASH AND CASH EQUIVALENTS, end of period	\$14,550	\$44,816

See accompanying notes to consolidated financial statements.

NATURAL HEALTH TRENDS CORP.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

1. NATURE OF OPERATIONS AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Nature of Operations

Natural Health Trends Corp. (the “Company”), a Delaware corporation, is an international direct-selling and e-commerce company headquartered in Dallas, Texas. Subsidiaries controlled by the Company sell personal care, wellness, and “quality of life” products under the “NHT Global” brand. In most markets, we sell our products to an independent member network that either uses the products themselves or resells them to consumers.

Our wholly-owned subsidiaries have an active physical presence in the following markets: North America; Greater China, which consists of Hong Kong, Taiwan and China; South Korea; Japan; and Europe, which consists of Italy and Slovenia. We also operate within certain Commonwealth of Independent States (Russia, Kazakhstan and Ukraine) through our engagement with a local service provider.

Principles of Consolidation

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

Use of Estimates

The preparation of financial statements in accordance with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and the disclosure of contingent assets and liabilities at the date of the consolidated financial statements and the reported amounts of revenues and expenses during the reported period.

The most significant accounting estimates inherent in the preparation of the Company's financial statements include estimates associated with obsolete inventory and the fair value of acquired intangible assets, including goodwill, revenue recognition, as well as those used in the determination of liabilities related to sales returns, distributor commissions and income taxes. Various assumptions and other factors prompt the determination of these significant estimates. The process of determining significant estimates is fact specific and takes into account historical experience and current and expected economic conditions. The actual results may differ materially and adversely from the Company's estimates. To the extent that there are material differences between the estimates and actual results, future results of operations will be affected.

Reclassification

Certain equity balances have been reclassified in the prior year consolidated financial statements to conform to current year presentation of treasury stock. No change in total stockholders' equity occurred.

Cash and Cash Equivalents

The Company considers all highly liquid investments with original maturities of three months or less, when purchased, to be cash equivalents. The Company includes credit card receivables due from certain of its credit card processors in its cash and cash equivalents as the cash proceeds are received within two to five days.

The Company maintains certain cash balances at several institutions located in the United States which at times may exceed insured limits. The Company has not experienced any losses in such accounts and believes it is not exposed to any significant credit risk.

Restricted Cash

The Company periodically maintains a cash reserve with certain credit card processing companies to provide for potential uncollectible amounts and chargebacks. Those cash reserves held by credit card processing companies located in South Korea are reflected in noncurrent assets since they require the Company to provide 100% collateral before processing transactions, which must be maintained indefinitely.

Inventories

Inventories consist primarily of finished goods and are stated at the lower of cost or market, using the first-in, first-out method. The Company reviews its inventory for obsolescence and any inventory identified as obsolete is reserved or written off. The Company's determination of obsolescence is based on assumptions about the demand for its products, product expiration dates, estimated future sales, and management's future plans. At December 31, 2014, the reserve for obsolescence totaled \$18,000. No such reserve existed at December 31, 2013.

Property and Equipment

Property and equipment are stated at cost less accumulated depreciation and amortization. Depreciation is computed using the straight-line method over the estimated useful lives of the assets, generally three to five years for office equipment and office software and five to seven years for furniture and fixtures. Leasehold improvements are amortized over the shorter of the lease term or the estimated useful life of the assets. Expenditures for maintenance and repairs are charged to expense as incurred.

The Company reviews property and equipment for impairment whenever events or changes in circumstances indicate the carrying amount of an asset may not be recoverable. Recoverability of these assets is measured by comparison of its carrying amounts to future undiscounted cash flows the assets are expected to generate. If property and equipment are considered to be impaired, the impairment to be recognized equals the amount by which the carrying value of the asset exceeds its fair value.

Goodwill

The Company assesses qualitative factors in order to determine whether it is more likely than not that the fair value of a reporting unit is less than its carrying amount. If, through this qualitative assessment, the conclusion is made that it is more likely than not that a reporting unit's fair value is less than its carrying amount, a two-step impairment test is performed. The Company's policy is to test for impairment annually during the fourth quarter. Considerable management judgment is necessary to measure fair value. We did not recognize any impairment charges for goodwill during the periods presented.

Income Taxes

The Company recognizes income taxes under the liability method of accounting for income taxes. Deferred income taxes are recognized for differences between the financial reporting and tax bases of assets and liabilities at enacted statutory tax rates in effect for the years in which the differences are expected to reverse. Valuation allowances are established when necessary to reduce deferred tax assets to the amounts expected to be ultimately realized. The Company recognizes tax benefits from uncertain tax positions only if it is more likely than not that the tax position will be sustained on examination by the taxing authorities, based on the technical merits of the position. The tax benefits recognized in the financial statements from such a position are measured based on the largest benefit that has a greater than fifty percent likelihood of being realized upon ultimate resolution. The Company recognizes interest and penalties related to unrecognized tax benefits as a component of income tax expense. Deferred taxes are not provided on the portion of undistributed earnings of subsidiaries outside of the United States when these earnings are considered permanently reinvested.

The Company and its subsidiaries file income tax returns in the United States, various states, and foreign jurisdictions. The Company is no longer subject to U.S. federal income tax examinations for years prior to 2011, and is no longer subject to state income tax examinations for years prior to 2010. No jurisdictions are currently examining any income tax returns of the Company or its subsidiaries.

Amounts Held in Distributor eWallets

Commencing in October 2014, the Company requires commission payments of certain distributors in Hong Kong to be first deposited into an electronic wallet (eWallet) account in lieu of being paid out directly to distributors. The eWallet functionality allows distributors to place new product orders utilizing eWallet available funds and/or request commission payout via multiple payment methods. Amounts held in eWallets are reflected on the balance sheet as a current liability.

Long-Term Incentive

Financial rewards earned under the 2014 Long-Term Incentive Plan (the “LTI Plan”) are recognized over the performance period as specified performance or other goals are achieved or exceeded. In accordance with the LTI Plan, fifty percent of any payment earned is payable in cash in thirty-five equal consecutive monthly installments commencing in February of the calendar year immediately following the conclusion of the performance period and the remaining fifty percent of the payment earned is payable in cash in thirty-five equal consecutive monthly installments commencing in February 2021 and ending in December 2023. As such, certain installments to be paid are reflected on the balance sheet as a non-current liability, and the current portion of the installments is reflected in other accrued expenses.

Foreign Currency

The functional currency of the Company’s international subsidiaries is generally their local currency. Local currency assets and liabilities are translated at the rates of exchange on the balance sheet date, and local currency revenues and expenses are translated at average rates of exchange during the period. Equity accounts are translated at historical rates. The resulting translation adjustments are recorded directly into a separate component of stockholders’ equity and represents the only component of accumulated other comprehensive income.

Aggregate transaction gains or losses, including gains or losses related to foreign-denominated cash and cash equivalents and the re-measurement of certain inter-company balances, are included in the statement of operations as other income and expense. Loss on foreign exchange totaling \$32,000 and \$202,000 was recognized during 2013 and 2014, respectively.

Revenue Recognition

Product sales are recorded when the products are shipped and title passes to independent distributors. Product sales to distributors are made pursuant to a distributor agreement that provides for transfer of both title and risk of loss upon our delivery to the carrier that completes delivery to the distributors, which is commonly referred to as “F.O.B. Shipping Point.” The Company primarily receives payment by credit card at the time distributors place orders. Amounts received for unshipped product are recorded as deferred revenue. The Company’s sales arrangements do not contain right of inspection or customer acceptance provisions other than general rights of return.

Actual product returns are recorded as a reduction to net sales. The Company estimates and accrues a reserve for product returns based on its return policies and historical experience.

Enrollment package revenue, including any nonrefundable set-up fees, is deferred and recognized over the term of the arrangement, generally twelve months. Enrollment packages provide distributors access to both a personalized marketing website and a business management system. No upfront costs are deferred as the amount is nominal.

Shipping charges billed to distributors are included in net sales. Costs associated with shipments are included in cost of sales.

Various taxes on the sale of products and enrollment packages to distributors are collected by the Company as an agent and remitted to the respective taxing authority. These taxes are presented on a net basis and recorded as a liability until remitted to the respective taxing authority.

Distributor Commissions

Independent distributors earn commissions based on total personal and group bonus volume points per weekly sales period. Each of our products are designated a specified number of bonus volume points, which is essentially a percentage of the product's wholesale price. The Company accrues commissions when earned and pays commissions on product sales generally two weeks following the end of the weekly sales period.

In some markets, we also pay certain bonuses on purchases by up to three generations of personally sponsored distributors, as well as bonuses on commissions earned by up to three generations of personally sponsored distributors. Independent distributors may also earn incentives based on meeting certain qualifications during a designated incentive period, which may range from several weeks to up to a year. These incentives may be both monetary and non-monetary in nature. The Company estimates and accrues all costs associated with the incentives as the distributors meet the qualification requirements.

From time to time we make modifications and enhancements to our compensation plan to help motivate distributors, which can have an impact on distributor commissions. From time to time we also enter into agreements for business or market development, which may result in additional compensation to specific distributors.

Stock-Based Compensation

Stock-based compensation expense is determined based on the grant date fair value of each award, net of estimated forfeitures which are derived from historical experience, and is recognized on a straight-line basis over the requisite service period for the award.

Income Per Share

Basic income per share is computed via the “two-class” method by dividing net income allocated to common stockholders by the weighted-average number of common shares outstanding during the period. Net income available to common stockholders is allocated to both common stock and participating securities as if all of the income for the period had been distributed. The Company’s Series A convertible preferred stock was a participating security due to its participation rights related to dividends declared by the Company. If dividends were distributed to common stockholders, the Company was also required to pay dividends to the holders of the preferred stock in an amount equal to the greater of (1) the amount of dividends then accrued and not previously paid on such shares of preferred stock or (2) the amount payable if dividends were distributed to the common stockholders on an as-converted basis.

Diluted income per share is determined using the weighted-average number of common shares outstanding during the period, adjusted for the dilutive effect of common stock equivalents. The dilutive effect of non-vested restricted stock and warrants is reflected by application of the treasury stock method. Under the treasury stock method, the amount of compensation cost for future service that the Company has not yet recognized and the amount of tax benefit that would be recorded in additional paid-in capital when the award becomes deductible are assumed to be used to repurchase shares. The dilutive effect of the Company’s Series A convertible preferred stock was calculated using the more dilutive of the “two-class” method and the “if-converted” method, which assumes that the preferred stock was converted into common stock at the beginning of each period presented.

The following table illustrates the computation of basic and diluted income per share for the periods indicated (in thousands, except per share data):

	Year Ended December 31, 2013			2014		
	Income	Shares	Per Share	Income	Shares	Per Share
	(Numerator)	(Denominator)	Amount	(Numerator)	(Denominator)	Amount
Basic EPS:						
Net income available to common stockholders	\$4,074			\$20,360		

Edgar Filing: NATURAL HEALTH TRENDS CORP - Form 10-K

Less: undistributed earnings to participating securities	(31)			(127)		
Net income allocated to common stockholders	\$4,043	11,154	\$ 0.36	\$20,233	12,131	\$ 1.67
Effect of dilutive securities:						
Warrants to purchase common stock	—	—		—	421	
Non-vested restricted stock	—	177		—	48	
Plus: reallocation of undistributed earnings to participating securities	—			5		
Diluted EPS:						
Net income allocated to common stockholders plus assumed conversions	\$4,043	11,331	\$ 0.36	\$20,238	12,600	\$ 1.61

Warrants to purchase 2,234,994 shares of common stock were not included in the computation of diluted income per share for 2013 as their effect is anti-dilutive since the applicable exercise price exceeds the average market price of the related common stock for the period. Warrants to purchase 88,097 shares of common stock were still outstanding at December 31, 2014. Such warrants expire April 21, 2015.

Certain Risks and Concentrations

A substantial portion of the Company's sales are generated in Hong Kong (see Note 10). Most of the Company's Hong Kong revenues are derived from the sale of products that are delivered to members in China. In contrast to the Company's operations in other parts of the world, the Company has not implemented a direct sales model in China. The Chinese government permits direct selling only by organizations that have a license that the Company does not have, and has adopted anti-multilevel marketing legislation. The Company operates an e-commerce direct selling model in Hong Kong and recognizes the revenue derived from sales to both Hong Kong and Chinese members as being generated in Hong Kong. Products purchased by members in China are delivered by the Company to one or more third parties that act as the importers of record under agreements to pay applicable duties. In addition, through a Chinese entity, the Company sells products in China using an e-commerce retail model. The Chinese entity operates separately from the Hong Kong entity, although a Chinese member may elect to participate separately in both.

The Company believes that the laws and regulations in China regarding direct selling and multi-level marketing are not specifically applicable to the Company's Hong Kong based e-commerce activity, and that the Company's Chinese entity is operating in compliance with applicable Chinese laws. However, there can be no assurance that the Chinese authorities will agree with the Company's interpretations of applicable laws and regulations or that China will not adopt new laws or regulations. Should the Chinese government determine that the Company's e-commerce activity violates China's direct selling or anti-multilevel marketing legislation, or should new laws or regulations be adopted, there could be a material adverse effect on the Company's business, financial condition and results of operations.

Although the Company attempts to work closely with both national and local Chinese governmental agencies in conducting the Company's business, the Company's efforts to comply with national and local laws may be harmed by a rapidly evolving regulatory climate, concerns about activities resembling violations of direct selling or anti-multi-level marketing legislation, subjective interpretations of laws and regulations, and activities by individual distributors that may violate laws notwithstanding the Company's strict policies prohibiting such activities. Any determination that the Company's operations or activities, or the activities of the Company's individual distributors or employee sales representatives, or importers of record are not in compliance with applicable laws and regulations could result in the imposition of substantial fines, extended interruptions of business, restrictions on the Company's future ability to obtain business licenses or expand into new locations, changes to the Company's business model, the termination of required licenses to conduct business, or other actions, any of which could materially harm the Company's business, financial condition and results of operations.

The Company's *Premium Noni Juice*TM product accounts for a significant portion of the Company's total revenue. The Company currently sources it from a single supplier. If demand decreases significantly, government regulation restricts its sale, the Company is unable to adequately source or deliver the product, or the Company ceases offering the product for any reason without a suitable replacement, the Company's business, financial condition and results of operations could be materially and adversely affected.

Fair Value of Financial Instruments

The carrying amounts of the Company's financial instruments, including cash and cash equivalents, accounts receivable, accounts payable and accrued expenses, approximate fair value because of their short maturities. The carrying amount of the noncurrent restricted cash approximates fair value since, absent the restrictions, the underlying assets would be included in cash and cash equivalents.

Accounting standards permit companies, at their option, to choose to measure many financial instruments and certain other items at fair value. The Company has elected to not fair value existing eligible items.

Recently Issued and Adopted Accounting Pronouncements

In March 2013, the Financial Accounting Standards Board (“FASB”) issued Accounting Standards Update (“ASU”) No. 2013-05, *Foreign Currency Matters (Topic 830) —Parent’s Accounting for the Cumulative Translation Adjustment upon Derecognition of Certain Subsidiaries or Groups of Assets within a Foreign Entity or of an Investment in a Foreign Entity*, to clarify the guidance for entities that cease to hold a controlling financial interest in a subsidiary or group of assets within a foreign entity when (1) the subsidiary or group of assets is a nonprofit activity or a business (other than a sale of in substance real estate or conveyance of oil and gas mineral rights) and (2) there is a cumulative translation adjustment balance associated with that foreign entity. ASU 2013-05 was effective prospectively for reporting periods, including interim periods, beginning after December 15, 2013. The Company’s adoption of the standard on January 1, 2014 did not have a material impact on its consolidated financial statements.

In July 2013, the FASB issued ASU No. 2013-11, *Income Taxes (Topic 740) — Presentation of an Unrecognized Tax Benefit When A Net Operating Loss Carryforward, a Similar Tax Loss, or a Tax Credit Carryforward Exists*, to provide explicit guidance on the financial statement presentation of an unrecognized tax benefit when a net operating loss carryforward, a similar tax loss, or a tax credit carryforward exists. The amendments in this update were effective for fiscal years, and interim periods within those years, beginning after December 15, 2013 and should be applied prospectively to all tax benefits that exist at the effective date. Retrospective application was permitted. The Company’s adoption of the standard on January 1, 2014 did not have a material impact on its consolidated financial statements.

In May 2014, the FASB issued ASU No. 2014-09, *Revenue From Contracts With Customers*, that outlines a single comprehensive model for entities to use in accounting for revenue arising from contracts with customers and supersedes most current revenue recognition guidance, including industry-specific guidance. ASU 2014-09 is based on the principle that an entity should recognize revenue to depict the transfer of goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. It also requires additional disclosure about the nature, amount, timing and uncertainty of revenue and cash flows arising from customer contracts, including significant judgments and changes in judgments and assets recognized from costs incurred to fulfill a contract. Entities have the option of using either a full retrospective or a modified retrospective approach for the adoption of the new standard. ASU 2014-09 becomes effective for reporting periods, including interim periods, beginning after December 15, 2016. Early adoption is not permitted. The company is currently assessing the impact that this standard will have on its consolidated financial statements.

Other recently issued accounting pronouncements did not or are not believed by management to have a material impact on the Company's present or future financial statements.

2. BALANCE SHEET COMPONENTS

The components of certain balance sheet amounts are as follows (in thousands):

	December 31,	
	2013	2014
Property and equipment:		
Office equipment	\$354	\$391
Office software	533	537
Furniture and fixtures	62	59
Leasehold improvements	256	345
	102	75
Construction in progress		
Property and equipment, at cost	1,307	1,407
Accumulated depreciation and amortization	(1,042)	(931)
	\$265	\$476
Other accrued expenses:		
Sales returns	\$504	\$654
Employee-related expense	1,860	4,620
Warehousing and inventory-related expense	595	987
Other	187	482
	\$3,146	\$6,743
Deferred revenue:		

Unshipped product	\$1,938	\$1,150
Auto ship advances	449	815
Enrollment package revenue	182	222
Market development fees	–	500
	\$2,569	\$2,687

Other current liabilities:

Unclaimed checks	\$674	\$1,266
Other	208	247
	\$882	\$1,513

3. COMMITMENTS AND CONTINGENCIES

Operating Leases

The Company has entered into non-cancelable operating lease agreements for locations within the United States and for its international subsidiaries, with expirations through March 2018. Rent expense in connection with operating leases was \$787,000 and \$777,000 during 2013 and 2014, respectively.

Future minimum lease obligations as of December 31, 2014 are as follows (in thousands):

2015	\$466
2016	178
2017	71
2018	18
2019	—
Total minimum lease obligations	\$733

Purchase Commitments

In May 2013, the Company entered into an exclusive distribution agreement with one of its suppliers to purchase its product through July 2016. To maintain exclusivity, the Company is required to purchase a minimum of \$40,000 of product per month until the termination date. As of December 31, 2014, the Company was in compliance with the exclusivity provision.

In December 2014, the Company amended a supply agreement with one of its suppliers to obtain worldwide exclusivity in return for purchasing a minimum of \$3.3 million of product annually. If the Company does not purchase the minimum product as required, then a Cure Payment, as defined, will be due to the supplier. The term of the agreement is three years commencing on January 1, 2015 and shall automatically renew for successive three year terms unless notice of termination is provided by either party.

Employment Agreements

The Company has employment agreements with certain members of its management team that can be terminated by either the employee or the Company upon four weeks' notice. The employment agreements entered into with the management team contain provisions that guarantee the payments of specified amounts in the event of a change in control, as defined, or if the employee is terminated without cause, as defined, or terminates employment for good reason, as defined. In addition, the Company has an employment agreement with another employee that can be terminated at will by either the employee or the Company, provided that the Company must pay a specified amount if it terminates the agreement without cause, as defined, or the employee terminates the agreement with good reason, as defined. Accrued severance totaling \$12,000 as of December 31, 2014 was paid in January 2015.

Consumer Indemnity

As required by the Door-to-Door Sales Act in South Korea, the Company maintains insurance for consumer indemnity claims with a mutual aid cooperative by possessing a mutual aid contract with Mutual Aid Cooperative & Consumer (the "Cooperative"). The contract secures payment to distributors in the event that the Company is unable to provide refunds to distributors. Typically, requests for refunds are paid directly by the Company according to the Company's normal Korean refund policy, which requires that refund requests be submitted within three months. Accordingly, the Company estimates and accrues a reserve for product returns based on this policy and its historical experience. Depending on the sales volume, the Company may be required to increase or decrease the amount of the contract. The maximum potential amount of future payments the Company could be required to make to address actual distributor claims under the contract is equivalent to three months of rolling sales. At December 31, 2014, non-current other assets include KRW 197 million (USD \$180,000) underlying the contract, which can be utilized by the Cooperative to fund any outstanding distributor claims. The Company believes that the likelihood of utilizing these funds to provide for distributors claims is remote.

Registration Payment Arrangements

Pursuant to a Registration Rights Agreement with the investors in the Company's October 2007 financing of variable rate convertible debentures having an aggregate face amount of \$4,250,000, seven-year warrants to purchase 1,495,952 shares of the Company's common stock, and one-year warrants to purchase 1,495,952 shares of the Company's common stock, the Company was obligated to (i) file a registration statement covering the resale of the maximum number of Registrable Securities (as defined) that is permitted by SEC Guidance (as defined) prior to November 18, 2007, (ii) cause the registration statement to be declared effective within certain specified periods of time and (iii) maintain the effectiveness of the registration statement until all Registrable Securities have been sold, or may be sold without volume restrictions pursuant to Rule 144(k) under the Securities Act. The Company timely filed that registration statement covering the shares of common stock underlying the debentures, which have been redeemed, and the one-year warrants, which have expired. At the time, the 1,495,952 shares of common stock underlying the seven-year warrants were not deemed Registrable Securities and were not included in the Registration Statement. If they are subsequently deemed Registrable Securities at a time when a registration statement covering them is required to be effective under the Registration Rights Agreement, and such registration statement is not then effective, then the warrants may be exercised by means of a cashless exercise. The maximum number of shares that could be required to be issued upon exercise of the warrants (whether on a cashless basis or otherwise) is limited to the number of shares indicated on the face of the warrants. The Company filed a registration statement on November 22, 2013 covering the maximum number of shares that could be required to be issued upon exercise of the warrants,

and such registration statement was declared effective on December 5, 2013. The Company filed a post-effective amendment to that registration statement on June 9, 2014, which was declared effective on June 16, 2014. As of December 31, 2014, no contingent obligations have been recognized under registration payment arrangements.

4. STOCKHOLDERS' EQUITY

Authorized Shares

The Company is authorized to issue two classes of capital stock consisting of up to 5,000,000 shares of preferred stock, \$0.001 par value, and 50,000,000 shares of common stock, \$0.001 par value. On May 4, 2007, the Board of Directors designated up to 1,761,900 shares of preferred stock as Series A preferred stock with the following rights and preferences:

Priority – the Series A preferred stock shall rank, in all respects, including the payment of dividends and upon liquidation, senior and prior to the common stock and other equity of the Company not expressly made senior or pari passu with the Series A preferred stock (collectively, “Junior Securities”).

Dividends –dividends at the rate per annum of \$0.119 per share shall accrue from the date of issuance of any shares of Series A preferred stock, payable upon declaration by the Board of Directors. Accruing dividends shall be cumulative; provided, however, that except as set forth below for the liquidation preference, the Company shall be under no obligation to pay such dividends. No dividends shall be declared on Junior Securities (other than dividends on shares of common stock payable in shares of common stock) unless the holders of the Series A preferred stock then outstanding shall first receive, or simultaneously receive, a dividend on each outstanding share of Series A preferred stock in an amount at least equal to the greater of (i) the amount of the aggregate accrued dividends on such share of Series A preferred stock and not previously paid and (ii) in the case of a dividend on common stock or any class or series of Junior Securities that is convertible into common stock, that dividend per share of Series A preferred stock as would equal the product of (1) the dividend payable on each share as if all shares of such class or series had been converted into common stock and (2) the number of shares of common stock issuable upon conversion of a share of Series A preferred stock.

Liquidation preference – in the event of any voluntary or involuntary liquidation, dissolution or winding up of the affairs of the Company, then, before any distribution or payment shall be made to the holders of any Junior Securities, the holders of the Series A preferred stock then outstanding shall be entitled to be paid in cash out of the assets of the Company available for distribution to its stockholders (on a pari passu basis with the holders of any series of preferred stock ranking on liquidation on a parity with the Series A preferred stock) an amount per share equal to the sum of the Series A Original Issue Price plus any dividends accrued but unpaid thereon, whether or not declared, together with any other dividends declared but unpaid thereon. If the assets of the Company are insufficient to pay the aggregate liquidation preference and the liquidation preference of any series of preferred stock ranking on liquidation on a parity with the Series A preferred stock, the holders of the Series A preferred stock and the holders of any series of preferred stock ranking on liquidation on a parity with the Series A preferred stock shall share ratably with one another in any such distribution or payment in proportion to the full amounts to which they would otherwise be respectively entitled before any distribution shall be made to the holders of the Junior Securities. The “Series A Original Issue Price” shall mean \$1.70 per share, subject to adjustment.

Voting rights – the holders of shares of Series A preferred stock shall be entitled to vote with the holders of the common stock, and with the holders of any other series of preferred stock, voting together as a single class, upon all matters submitted to a vote of stockholders of the Company. Each holder of shares of Series A preferred stock shall be entitled to the number of votes equal to the product (rounded down to the nearest number of whole shares) of 0.729 times the largest number of shares of common stock into which all shares of Series A preferred stock held of record by such holder could then be converted.

Conversion – each share of Series A preferred stock shall be convertible, subject to adjustment only in the event of stock splits, stock dividends, recapitalizations and similar events that would affect all of stockholders, at the option of the holder thereof, at any time and from time to time, into such number of fully paid and nonassessable shares of common stock as determined by dividing the Series A Original Issue Price by the Series A Conversion Price (as defined) in effect at the time of conversion. The “Series A Conversion Price” shall initially be equal to \$1.70. Each share of Series A preferred stock shall automatically be converted into shares of common stock at the then effective conversion price immediately upon such date as the average closing price of the common stock over a consecutive, trailing 6-month period equals or exceeds \$10.00 per share.

On December 3, 2014, the Company filed a Certificate of Elimination of the Series A Convertible Preferred Stock (the “Certificate”) with the Secretary of State of the State of Delaware. The Certificate, which was effective upon filing, canceled the Company’s Series A preferred stock. At the time of filing the Certificate, no shares of Series A preferred stock remained outstanding as a result of the automatic conversion of all outstanding shares into the Company’s common stock due to the fact that the average closing price of the Company’s common stock equaled or exceeded \$10.00 per share over a consecutive, trailing 6-month period that ended November 18, 2014.

Common Stock Purchase Warrants

On October 19, 2007, the Company issued warrants to purchase 3,141,499 shares of common stock in connection with a convertible debentures financing. The warrants consisted of seven-year warrants to purchase 1,495,952 shares of common stock, one-year warrants to purchase 1,495,952 shares of common stock, and five-year warrants to purchase 149,595 shares of common stock. The term for each of the warrants began six months and one day after their respective issuance and each have an exercise price of \$3.52 per share. The exercise price and the number of shares underlying the warrants are subject to adjustment for stock dividends and splits, combinations, and reclassifications, certain rights offerings and distributions to common stockholders, and mergers, consolidations, sales of all or substantially all assets, tender offers, exchange offers, reclassifications or compulsory share exchanges. In addition, subject to certain exceptions, the exercise price and number of shares underlying the warrants are subject to anti-dilution adjustments from time to time if the Company issues its common stock or equivalent securities at below the exercise price for the warrants. If, at any time after the earlier of October 19, 2008 and the completion of the then applicable holding period under Rule 144, there is no effective registration statement for the underlying shares of common stock that are then required to be registered, the warrants may be exercised by means of a cashless exercise. Such one-year warrants expired unexercised on April 21, 2009 and such five-year warrants expired unexercised on April 21, 2013. Seven-year warrants to purchase 1,407,855 shares of common stock were exercised during 2014 at exercise prices ranging from \$3.5108 to \$3.52 per share for total proceeds of \$4.9 million. As a result of the cash dividends declared on each share of outstanding common stock and in accordance with the terms of the related warrant agreement, the exercise price per share for each warrant was adjusted from \$3.52 per share to \$3.5082 per share. The remaining warrants to purchase 88,097 shares of common stock expire April 21, 2015 if not previously exercised.

Dividends

The following table summarizes the Company's cash dividend activity during 2014 (in thousands, except per share data):

Declaration Date	Dividends Per Share		Amount	Date Payable
	Preferred	Common		
March 7, 2014	\$0.815	\$ 0.005	\$ 159	April 8, 2014
May 6, 2014	0.020	0.005	62	June 4, 2014
July 29, 2014	0.027	0.010	127	August 27, 2014
November 4, 2014	0.032	0.010	128	December 3, 2014
Total	\$0.894	\$ 0.030	\$ 476	

Payment of any future dividends on shares of common stock will be at the discretion of the Company's Board of Directors.

Treasury Stock

On August 13, 2012, the Board of Directors authorized the Company, acting as trustee for certain of its non-officer, overseas employees, to execute a Rule 10b5-1 plan to purchase 100,000 shares of its common stock in accordance with guidelines specified under Rule 10b5-1 of the Securities Exchange Act of 1934 (the “Exchange Act”) and the Company's policies regarding stock transactions. Pursuant to this authority, the Company, as Trustee, entered into a 10b5-1 plan and began purchasing shares in December 2012. The latest 10b5-1 plan terminated in November 2014 and the Company, as Trustee, has not entered into a new 10b5-1 plan. See Note 5.

On November 4, 2014, the Board of Directors approved a special, stock repurchase program of up to \$5 million of the Company's outstanding shares of common stock (the “Repurchase Plan”). In connection therewith, the Company was advised by George K. Broady, a director of the Company and owner of more than 5% of its outstanding common stock, that Mr. Broady desired to participate in the Repurchase Plan on a basis roughly proportional to his ownership interest, with an estimate of generating approximately \$1.5 million through the sale of a portion of the shares of the Company's common stock held by him (see Note 8). After noting Mr. Broady's participation interest, the Company authorized its broker to proceed with the purchase of shares of the Company's common stock in the open market for a total purchase price of \$3.0 million in accordance with Rules 10b5-1 and 10b-18 under the Exchange Act. The Repurchase Plan was completed on December 17, 2014. The Repurchase Plan, which included both open market purchases and the purchase of shares from Mr. Broady, resulted in the Company purchasing a total of 359,840 shares of its common stock for an aggregate purchase price of \$4.5 million, plus transaction costs.

5. STOCK-BASED COMPENSATION

On August 18, 2006, the Compensation Committee of Company's Board of Directors approved, subject to stockholder approval, the Natural Health Trends Corp. 2007 Equity Incentive Plan (the “2007 Plan”). Under the 2007 Plan, the Company may grant (i) incentive stock options, (ii) nonqualified stock options, (iii) restricted stock, (iv) restricted stock units, (v) stock appreciation rights either in tandem with an option or alone and unrelated to an option, or SARs, (vi) performance shares, (vii) award shares, or (viii) stock awards. The 2007 Plan was approved by the Company's stockholders on November 17, 2006.

The purpose of the 2007 Plan is to enable the Company to attract and retain employees, officers, directors, consultants and advisors; to provide an incentive for them to assist in achieving long-range performance goals; and to enable them to participate in the long-term growth of the Company. The terms of any particular grant are determined by the Board of Directors or a committee appointed by the Board of Directors. Generally, the grants of restricted stock vest quarterly on a pro rata basis over a three-year period. The maximum number of shares available for issuance under the 2007 Plan was 1,550,000 shares. At the Company's Annual Meeting of Stockholders held on December 30, 2008, the Company's stockholders approved an increase in the maximum number of shares available for issuance under the 2007 Plan by 500,000 shares. As such, the maximum aggregate number of shares available for issuance under the 2007 Plan

totals 2,050,000 shares. As of December 31, 2014, 1,083 shares remain available to be granted under the 2007 Plan.

Valuation and Expense Information under FASB ASC Topic 718

Stock-based compensation expense totaled approximately \$110,000 and \$49,000 for 2013 and 2014, respectively. No tax benefits were attributed to the stock-based compensation because a valuation allowance was maintained for substantially all net deferred tax assets.

A following table summarizes the Company's restricted stock activity under the 2007 Plan:

	Shares	Wtd. Avg. Price at Date of Issuance
Nonvested at December 31, 2012	261,658	\$ 0.37
Vested	(206,672)	0.37
Nonvested at December 31, 2013	54,986	0.37
Vested	(54,986)	0.37
Nonvested at December 31, 2014	—	—

On August 13, 2012, the Board of Directors authorized the Company, acting as trustee for certain of its non-officer, overseas employees, to execute a Rule 10b5-1 plan to purchase 100,000 shares of its common stock in accordance with guidelines specified under Rule 10b5-1 of the Exchange Act and the Company's policies regarding stock transactions. Pursuant to this authority, the Company, as Trustee, entered into a 10b5-1 plan and began purchasing in December 2012. The latest 10b5-1 plan terminated in November 2014, and the Company, as Trustee, has not entered into a new 10b5-1 plan. The employees will receive the stock as incentive compensation in quarterly increments over three years beginning March 15, 2013, provided that they are employees of the Company on the date of the distribution. Any common stock that is forfeited by an employee whose employment terminates will be delivered to the Company and held as treasury stock.

	Shares	Wtd. Avg. Grant-Date Fair Value
Nonvested at December 31, 2012	100,000	\$ 1.37
Vested	(26,676)	1.37
Forfeited	(20,000)	1.37
Nonvested at December 31, 2013	53,324	1.37
Vested	(25,342)	1.37
Forfeited	(3,998)	1.37
Nonvested at December 31, 2014	23,984	1.37

As of December 31, 2014, total unrecognized stock-based compensation expense related to these stock awards was \$31,000, which is expected to be recognized over a weighted-average period of one year.

6. INCOME TAXES

The components of income before income taxes consist of the following (in thousands):

	Year Ended December 31,	
	2013	2014
Domestic	\$ 194	\$4,502
Foreign	3,997	16,134
Income before income taxes	\$4,191	\$20,636

The components of the income tax provision consist of the following (in thousands):

Year Ended
December
31,
2013 2014

Current:

Federal	\$10	\$104
State	–	11
Foreign	76	194
Total current taxes	86	309
Deferred foreign taxes	16	(43)
Income tax provision	\$102	\$266

A reconciliation of the reported income tax provision to the provision that would result from applying the domestic federal statutory tax rate to pretax income is as follows (in thousands):

	Year Ended December 31,	
	2013	2014
Income tax at federal statutory rate	\$1,425	\$7,016
Effect of permanent differences	7	9
Change in valuation allowance	430	(2,070)
Foreign rate differential	(1,218)	(5,240)
Change in enacted tax rates	(597)	38
Expiration of net operating loss carryforward	—	519
Other reconciling items	55	(6)
Income tax provision	\$102	\$266

Deferred income taxes consist of the following (in thousands):

	December 31,	
	2013	2014
Deferred tax assets:		
Net operating losses	\$13,115	\$10,083
Accrued expenses	268	837
Tax credits	512	519
Impairment of long-lived assets	88	69
Other	1	—
Total deferred tax assets	13,984	11,508
Valuation allowance	(13,927)	(11,440)
	57	68
Deferred tax liabilities:		
Intangible assets	(43)	—
Accrued expenses	(107)	(64)
Prepays	(11)	(32)
Other	(4)	(37)
Total deferred tax liabilities	(165)	(133)
Net deferred tax liability	\$(108)	\$(65)

The Company has recorded a valuation allowance equal its net deferred tax assets in the U.S. and certain of its foreign jurisdictions due to the uncertainty of future operating results. The valuation allowance will be reduced at such time as management believes it is more likely than not that the deferred tax assets will be realized. Any reductions in the

valuation allowance will reduce future income tax provisions.

At December 31, 2014, the Company has U.S. federal net operating loss carryforwards of \$27.2 million that begin to expire in 2021, if not utilized. The Company also has foreign net operating loss carryforwards totaling \$3.4 million in various jurisdictions with various expirations, including \$2.0 million in China with expirations from 2015 to 2017. The Company has not provided for U.S. federal and foreign withholding taxes on the undistributed earnings of its foreign subsidiaries as of December 31, 2014. Such earnings are intended to be reinvested indefinitely. Generally, such earnings become subject to U.S. income tax upon the remittance of dividends and under certain other circumstances. At December 31, 2014, it is not practicable to estimate the amount of deferred tax liability on such undistributed earnings.

7. SUPPLEMENTAL CASH FLOW INFORMATION

	Year Ended December 31, 2013 2014 (In Thousands)	
Cash paid during the year for:		
Income taxes, net of refunds	\$ 71	\$ 60
Interest	—	1
Non-cash financing activity:		
Conversion of preferred stock	13	111

8. RELATED PARTY TRANSACTIONS

Product Royalties

In February 2013, the Company entered into a Royalty Agreement and License with Broady Health Sciences, L.L.C., a Texas limited liability company, (“BHS”) regarding the manufacture and sale of a product called *ReStor*™. Under this agreement, the Company agreed to pay BHS a royalty of 2.5% of sales revenue in return for the right to manufacture (or have manufactured), market, import, export and sell this product worldwide, with certain rights being exclusive outside the United States. George K. Broady, a director of the Company and owner of more than 5% of its outstanding common stock, is owner of BHS. The Company recognized royalties of \$48,000 and \$144,000 during 2013 and 2014, respectively. The Company is not required to purchase any product under the agreement, and the agreement may be terminated at any time on 120 days’ notice or, under certain circumstances, with no notice.

The Company is considering entering into another royalty agreement and license with BHS regarding the manufacture and sale of a product called *Soothe*™, which the Company began selling in the fourth quarter of 2012 with the permission of BHS. To continue selling this product, BHS has requested that the Company pay a royalty of 2.5% of sales revenue for this product for 2012 and subsequent years. The Company is considering that proposal and discussing the terms of a definitive agreement. At a royalty of 2.5% of net sales, the Company calculates that royalties through the end of December 2014 would total \$11,700.

Stock Repurchase Agreement

On November 14, 2014, the Company entered into a Stock Repurchase Agreement (the “Stock Repurchase Agreement”) with George K. Broady, a director of the Company and owner of more than 5% of its outstanding common stock, in accordance with Rule 10b5-1 under the Exchange Act. The Stock Repurchase Agreement provided for the Company’s purchase from Mr. Broady of one-half of the number of shares of common stock purchased by the Company’s broker in the open market under the Repurchase Plan approved by the Company’s Board of Directors on November 4, 2014 (see Note 4). The Stock Repurchase Agreement with Mr. Broady required that the Company report to Mr. Broady on a weekly basis information regarding the broker’s open market purchases, and that the Company purchase from Mr. Broady on a weekly basis at a per share purchase price equal to the weighted average price per share paid by the Company’s broker to purchase shares in the open market. The Company’s purchases from Mr. Broady under the Stock Repurchase Agreement, which concluded on December 17, 2014, totaled 119,947 shares of its common stock for an aggregate purchase price of \$1.5 million.

9. EMPLOYEE BENEFIT PLANS

The Company has a 401(k) defined contribution plan which permits participating employees in the United States to defer up to a maximum of 90% of their compensation, subject to limitations established by the Internal Revenue Service. Employees age 21 and older are eligible to contribute to the plan starting the first day of the following month of employment. Participating employees are eligible to receive discretionary matching contributions and profit sharing, subject to certain conditions, from the Company. In 2013 and 2014, the Company matched employee deferral contributions up to 4.5% of salary, which vested 100% immediately. No profit sharing has been paid under the plan. The Company recorded compensation expense of \$62,000 and \$60,000 for 2013 and 2014, respectively, related to its matching contributions to the plan. Certain of the Company’s employees located outside the United States participate in employee benefit plans that are statutory in nature.

10. SEGMENT INFORMATION

The Company sells products to a distributor network that operates in a seamless manner from market to market, except for the Chinese market. The Company believes that all of its operating segments should be aggregated into a single reportable segment as they have similar economic characteristics. In making this determination, the Company believes that all of the operating segments are similar in the nature of the products sold, the product acquisition process, the types of customers products are sold to, the methods used to distribute the products, and the nature of the regulatory environment.

The Company's e-commerce retail business launched in China during June 2007 does not require a direct selling license and allows for discounts on volume purchases. There is no separate segment manager who is held accountable by our chief operating decision-makers, or anyone else, for operations, operating results and planning for the Chinese market on a stand-alone basis. Accordingly, we consider ourselves to be in a single reporting segment and operating unit structure.

The Company's net sales by geographic area are as follows (in thousands):

	Year Ended December 31,	
	2013	2014
Net sales from external customers:		
United States	\$2,289	\$1,438
Canada	72	1,374
Hong Kong	40,585	111,028
China	791	1,538
Taiwan	3,387	4,628
South Korea	702	1,009
Russia, Kazakhstan and Ukraine	4,354	3,113
Other foreign countries	347	462
Total net sales	\$52,527	\$124,590

The Company's net sales by product and service are as follows (in thousands):

	December 31,	
	2013	2014
Net sales by product and service:		
Product sales	\$50,385	\$118,843

Enrollment package revenue, freight and other	2,955	7,927
Less: sales returns	(813)	(2,180)
Total net sales	\$52,527	\$124,590

The Company's long-lived assets by geographic area are as follows (in thousands):

	December 31, 2013 2014	
Long-lived assets:		
United States	\$35	\$31
China	137	241
Other foreign countries	93	204
Total long-lived assets	\$265	\$476

11. SUBSEQUENT EVENTS

On January 20, 2015, the Company's Board of Directors granted 60,960 shares of restricted common stock to certain employees and its outside directors for the purpose of further aligning their interest with those of its stockholders and, as to the employee shares, settling fiscal 2014 performance incentives. The shares vest on a quarterly basis over the next three years and are subject to forfeiture in the event of their termination of service to the Company under specified circumstances.

On January 22, 2015, the Company entered into a Stock Repurchase Agreement with George K. Broady, a director of the Company and owner of more than 5% of its outstanding common stock. The agreement provided for the Company's purchase from Mr. Broady in off-the-market, private transactions of a total of 91,817 shares of the Company's common stock, which would be purchased at the rate of 5,000 shares each trading day following the date of the agreement until all of such shares were purchased. The shares would be purchased at a per share price equal to the closing price per share of the Company's common stock on the preceding trading day, as reported on the primary market in which the Company's common stock is publicly traded. The Company's purchases concluded on February 19, 2015, and resulted in an aggregate purchase price of \$1.1 million.

On February 11, 2015, the Board of Directors voted to expand its size to provide for five directors and, in accordance with the Company's bylaws, elected Christopher R. O'Brien and Kin Y. Chung to fill the newly-created directorships. At the time of their election, Messrs. O'Brien and Chung, together with Randall A. Mason (an existing director), were also appointed to the Board's Audit Committee, and Messrs. O'Brien and Mason were also appointed to the Board's Compensation Committee and Nominating and Corporate Governance Committee. The Board determined that each of Messrs. O'Brien and Chung is an "independent director," as such term is defined in Rule 5605 of The Nasdaq Stock Market Rules; in addition, each such newly-elected director qualifies as an "independent director," as defined in Rule 10A-3(b), as promulgated under the Exchange Act.

Upon their election and in their capacity as non-employee directors of the Company, each of Messrs. O'Brien and Chung received \$25,000 cash and 3,058 shares of restricted common stock, which shares vest on a quarterly basis over the next three years and are subject to forfeiture in the event of their termination of service to the Company under specified circumstances.

Also on February 11, 2015, the Company entered into an indemnification agreement ("Indemnification Agreement") with each of its two recently elected directors, Messrs. O'Brien and Chung, as well as its existing directors and executive officers. The Indemnification Agreement confirms the Company's obligation to indemnify its directors and executive officers against liability arising out of the performance of their duties. The Indemnification Agreement provides mandatory indemnification, on the terms and conditions set forth in the agreement, for expenses and losses actually and reasonably incurred by directors and executive officers in defending legal proceedings in which they are parties by reason of their service to the Company or other entities to which they provide services at the Company's request or on its behalf. Pursuant to the Indemnification Agreement, the Company will advance reasonable expenses incurred by directors and executive officers in defending these legal proceedings, on the terms and conditions set forth in the Indemnification Agreement, and subject to repayment in the event of a determination that a director or executive officer is not entitled to indemnification for those expenses.

On February 12, 2015, the Company announced that its common stock had been approved for listing on The NASDAQ Capital Market and began trading under the ticker symbol NHTC on February 17, 2015.

On February 27, 2015, the Board of Directors declared a cash dividend of \$0.02 on each share of common stock outstanding. Such dividends are payable on March 27, 2015 to stockholders of record on March 17, 2015. Payment of any future dividends on shares of common stock will be at the discretion of the Company's Board of Directors.

Item 9. CHANGES IN AND DISAGREEMENTS WITH ACCOUNTANTS ON ACCOUNTING AND FINANCIAL DISCLOSURE

Not applicable.

Item 9A. CONTROLS AND PROCEDURES

Disclosure Controls and Procedures

Management, with the participation of the Company's principal executive officer and principal financial officer, evaluated the effectiveness of the design and operation of the Company's disclosure controls and procedures (as defined in Rule 13a-15(e) of the Exchange Act) as of December 31, 2014. The Company's disclosure controls and procedures are designed to ensure that information required to be disclosed by the Company in the reports that it files or submits under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in the Securities and Exchange Commission rules and forms, and that such information is accumulated and communicated to management, including the Company's principal executive officer and principal financial officer, as appropriate, to allow timely decisions regarding required disclosure. Based on this evaluation, the principal executive officer and principal financial officer concluded that, as of December 31, 2014, the Company's disclosure controls and procedures were effective.

Management's Annual Report on Internal Control over Financial Reporting

Management is responsible for establishing and maintaining adequate internal control over financial reporting. Internal control over financial reporting is a process designed by, or under the supervision of, the Company's principal executive and principal financial officers and effected by the Company's Board of Directors, management and other personnel to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles and includes those policies and procedures that:

pertain to the maintenance of records that in reasonable detail accurately and fairly reflect the transactions and dispositions of the assets of the Company;

provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the Company are being made only in accordance with authorizations of management and directors of the Company; and

provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use or disposition of the Company's assets that could have a material effect on the financial statements.

Because of inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Projections of any evaluation of effectiveness to future periods are subject to the risks that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

Management evaluates the effectiveness of the Company's internal control over financial reporting by using the criteria established in Internal Control – Integrated Framework (2013), issued by the Committee of Sponsoring Organizations of the Treadway Commission ("COSO "). Based on this criteria, management concluded that the Company's internal control over financial reporting as of December 31, 2014 was effective.

This Annual Report does not include an attestation report of the Company's independent registered public accounting firm regarding internal control over financial reporting. Management's report was not subject to attestation by the Company's independent registered public accounting firm pursuant to rules of the Securities and Exchange Commission that permit the Company to provide only management's report in this Annual Report.

Changes in Internal Control over Financial Reporting

There were no changes in internal control over financial reporting that occurred during the fiscal quarter ended December 31, 2014 that have materially affected, or are reasonably likely to materially affect, internal control over financial reporting.

Item 9B. OTHER INFORMATION

None.

Part III

Item 10. DIRECTORS, EXECUTIVE OFFICERS AND CORPORATE GOVERNANCE

The information required by this Item is incorporated by reference from the definitive proxy statement to be filed with the SEC within 120 days after December 31, 2014.

**Item 11. EXECUTIVE
COMPENSATION**

The information required by this Item is incorporated by reference from the definitive proxy statement to be filed with the SEC within 120 days after December 31, 2014.

**Item 12. SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT AND
RELATED STOCKHOLDER MATTERS**

The information required by this Item is incorporated by reference from the definitive proxy statement to be filed with the SEC within 120 days after December 31, 2014.

**Item 13. CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS, AND DIRECTOR
INDEPENDENCE**

The information required by this Item is incorporated by reference from the definitive proxy statement to be filed with the SEC within 120 days after December 31, 2014.

Item 14. PRINCIPAL ACCOUNTING FEES AND SERVICES

The information required by this Item is incorporated by reference from the definitive proxy statement to be filed with the SEC within 120 days after December 31, 2014.

Part IV

Item 15. EXHIBITS AND FINANCIAL STATEMENT SCHEDULES

Documents filed as part of this Form 10-K:

1. Financial Statements. See Index to Consolidated Financial Statements under Item 8 of Part II.
2. Financial Statement Schedules. Financial statement schedules have been omitted because they are not required, not applicable, or because the required information is shown in the financial statements or notes thereto.
3. Exhibits. The exhibits listed on the accompanying Exhibit Index are filed as a part of, and are incorporated by reference into, this report.

SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the registrant has duly caused this Annual Report on Form 10-K to be signed on its behalf by the undersigned, thereunto duly authorized.

NATURAL HEALTH TRENDS CORP.

Date: March 6, 2015

/s/ Chris T. Sharng
Chris T. Sharng
President
(Principal Executive Officer)

POWER OF ATTORNEY

KNOW ALL MEN BY THESE PRESENTS that each of Natural Health Trends Corp., a Delaware corporation, and the undersigned directors and officers of Natural Health Trends Corp., hereby constitutes and appoints Chris T. Sharng and Timothy S. Davidson, or any one of them, its, his or her true and lawful attorney-in-fact and agent, for it, him or her and in its, his or her name, place and stead, in any and all capacities, with full power to act alone, to sign any and all amendments to this report, and to file each such amendment to the report, with all exhibits thereto, and any and all other documents in connection therewith, with the Securities and Exchange Commission, hereby granting unto said attorney-in-fact and agent full power and authority to do and perform any and all acts and things requisite and necessary to be done in and about the premises as fully to all intents and purposes as it, he or she might or could do in person, hereby ratifying and confirming all that said attorney-in-fact and agent may lawfully do or cause to be done by virtue hereof.

Pursuant to the requirements of the Securities Act of 1934, this report has been signed below by the following persons on behalf of the registrant and in the capacities and on the dates indicated.

Signature	Title	Date
/s/ Chris T. Sharng Chris T. Sharng	President and Director (Principal Executive Officer)	March 6, 2015
/s/ Timothy S. Davidson Timothy S. Davidson	Senior Vice President and Chief Financial Officer (Principal Financial and Accounting Officer)	March 6, 2015

Edgar Filing: NATURAL HEALTH TRENDS CORP - Form 10-K

/s/ Randall A. Mason Randall A. Mason	Chairman of the Board and Director	March 6, 2015
/s/ George K. Broady George K. Broady	Director	March 6, 2015
/s/ Christopher R. O'Brien Christopher R. O'Brien	Director	March 6, 2015
/s/ Kin Y. Chung Kin Y. Chung	Director	March 6, 2015

EXHIBIT INDEX

(Pursuant to Item 601 of Regulation S-K)

Exhibit

Number	Exhibit Description
3.1	Certificate of Incorporation of Natural Health Trends Corp. (incorporated by reference to Exhibit 3.01 to Current Report on Form 8-K filed on July 12, 2005).
3.3	By-Laws of Natural Health Trends Corp. (incorporated by reference to Exhibit 3.02 to Current Report on Form 8-K filed on July 12, 2005).
4.1	Specimen Certificate for shares of common stock, \$.001 par value per share, of Natural Health Trends Corp. (incorporated by reference to Exhibit 4.01 to Annual Report on Form 10-K filed on May 8, 2006).
10.1	Form of Seven Year Warrants to Purchase Shares of Common Stock of the Company issued by the Company to certain purchasers (incorporated by reference to Exhibit 10.4 to Current Report on Form 8-K filed on October 22, 2007).
+10.2	2007 Annual Incentive Plan (incorporated by reference to Appendix A to Definitive Proxy Statement filed on October 20, 2006).
+10.3	2007 Equity Incentive Plan, as amended and restated as of November 13, 2008 (incorporated by reference to Appendix A to Definitive Proxy Statement filed on November 25, 2008).
+10.4	Form of Notice of Restricted Stock Grant and Restricted Stock Agreement under the Company's 2007 Equity Incentive Plan (incorporated by reference to Exhibit 10.5 to Quarterly Report on Form 10-Q filed on May 11, 2007).
+10.5	Natural Health Trends Corp. Annual Incentive Plan (incorporated by reference to Exhibit 10.1 to Current Report on Form 8-K filed on April 8, 2014).
+10.6	Natural Health Trends Corp. 2014 Long-Term Incentive Plan (incorporated by reference to Exhibit 10.2 to Current Report on Form 8-K filed on April 8, 2014).
+10.7	Employment Agreement (including form of Non-Competition and Proprietary Rights Assignment Agreement) for Chris T. Sharng, dated April 23, 2007 (incorporated by reference to Exhibit 10.1 to Current Report on Form 8-K filed on April 26, 2007).
+10.8	Employment Agreement (including form of Non-Competition and Proprietary Rights Assignment Agreement) for Timothy S. Davidson dated April 23, 2007 (incorporated by reference to Exhibit 10.2 to Current Report on Form 8-K filed on April 26, 2007).
+10.9	Form of Restricted Stock Notice of Grant and Award Agreement for shares of restricted stock granted on (1) January 20, 2015 to each of Chris T. Sharng, Timothy S. Davidson, Randall A. Mason any George K. Broady, and (2) February 11, 2015 to each of Christopher R. O'Brien and Kin Y. Chung (filed herewith).
+10.10	Form of Indemnification Agreement dated February 11, 2015, between Natural Health Trends Corp. and each of its directors (incorporated by reference to Exhibit 10.1 to Current Report on Form 8-K filed on February 12, 2015).
10.11	Stock Repurchase Agreement dated November 14, 2014 by and between Natural Health Trends Corp. and George K. Broady (incorporated by reference to Exhibit 10.1 to Current Report on Form 8-K filed November 17, 2014).
10.12	Stock Repurchase Agreement dated January 22, 2015 by and between Natural Health Trends Corp. and George K. Broady (incorporated by reference to Exhibit 10.1 to Current Report on Form 8-K filed January 26, 2015).
14.1	

Edgar Filing: NATURAL HEALTH TRENDS CORP - Form 10-K

Worldwide Code of Business Conduct, as revised on February 11, 2015 (incorporated by reference to Exhibit 14.1 to Current Report on Form 8-K filed on February 12, 2015).

21.1 Subsidiaries of the Company (filed herewith).

24.1 Power of Attorney (see signature page).

31.1 Certification of Principal Executive Officer pursuant to Exchange Act Rules 13a-14(a) and 15d-14(a), as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 (filed herewith).

31.2 Certification of Principal Financial Officer pursuant to Exchange Act Rules 13a-14(a) and 15d-14(a), as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 (filed herewith).

32.1 Certifications of Principal Executive Officer and Principal Financial Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 (filed herewith).

101.INS XBRL Instance

101.SCH XBRL Taxonomy Extension Schema

101.CAL XBRL Taxonomy Extension Calculation

101.DEF XBRL Taxonomy Extension Definition

101.LAB XBRL Taxonomy Extension Labels

101.PRE XBRL Taxonomy Extension Presentation

+ Management contract or compensatory plan