GNC HOLDINGS, INC.
Form 10-Q
October 27, 2016
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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

Form 10-Q

(Mark one)

[X] QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the quarterly period ended September 30, 2016

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

For the transition period from to .

Commission File Number: 001-35113

GNC Holdings, Inc.
(Exact name of registrant as specified in its charter)

Delaware	20-8536244
(State or other jurisdiction of Incorporation or organization)	(I.R.S. Employer Identification No.)
300 Sixth Avenue Pittsburgh, Pennsylvania (Address of principal executive offices)	15222 (Zip Code)

Registrant's telephone number, including area code: (412) 288-4600

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. [X] Yes [ ] No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files).
[X] Yes [ ] No

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

Large accelerated filer [X] Accelerated filer [ ] Non-accelerated filer [ ] Smaller reporting company [ ]

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

As of October 25, 2016, there were 68,399,989 outstanding shares of Class A common stock, par value $0.001 per share (the “common stock”), of GNC Holdings, Inc.

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PART I - FINANCIAL INFORMATION

Item 1. Financial Statements

GNC HOLDINGS, INC. AND SUBSIDIARIES
Consolidated Balance Sheets
(unaudited)
(in thousands)

	September 30, 2016	December 31, 2015
Current assets:		
Cash and cash equivalents	$37,203	$56,462
Receivables, net	143,494	142,486
Inventory (Note 3)	621,865	555,885
Deferred income taxes	10,925	10,916
Prepaid and other current assets	32,553	27,114
Total current assets	846,040	792,863
Long-term assets:		
Goodwill (Note 5)	647,806	649,892
Brands (Note 5)	720,000	720,000
Other intangible assets, net (Note 5)	113,197	119,204
Property, plant and equipment, net (Note 5)	221,775	230,535
Deferred income taxes	3,358	3,358
Other long-term assets	32,472	38,555
Total long-term assets	1,738,608	1,761,544
Total assets	$2,584,648	$2,554,407
Current liabilities:		
Accounts payable	$185,286	$152,099
Current portion of long-term debt (Note 6)	4,550	4,550
Deferred revenue and other current liabilities	133,023	121,062
Total current liabilities	322,859	277,711
Long-term liabilities:		
Long-term debt (Note 6)	1,544,038	1,444,628
Deferred income taxes	307,921	304,491
Other long-term liabilities	57,251	59,016
Total long-term liabilities	1,909,210	1,808,135
Total liabilities	2,232,069	2,085,846
Contingencies (Note 8)		
Stockholders' equity:		
Common stock	114	114
Additional paid-in capital	921,794	916,128
Retained earnings	1,163,406	1,058,148
Treasury stock, at cost	(1,725,349)	(1,496,180)
Accumulated other comprehensive loss	(7,386)	(9,649)
Total stockholders' equity	352,579	468,561
Total liabilities and stockholders' equity	$2,584,648	$2,554,407

The accompanying notes are an integral part of the consolidated financial statements.

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GNC HOLDINGS, INC. AND SUBSIDIARIES
Consolidated Statements of Income
(unaudited)
(in thousands, except per share amounts)

	Three months ended September 30,		Nine months ended September 30,	
	2016	2015	2016	2015
Revenue	$627,964	$683,358	$1,970,087	$2,054,187
Cost of sales, including warehousing, distribution and occupancy	412,556	432,714	1,280,136	1,297,778
Gross profit	215,408	250,644	689,951	756,409
Selling, general, and administrative	148,392	141,155	430,448	421,013
Gains on refranchising (Note 4)	(383)	(945)	(18,283)	(2,436)
Long-lived asset impairments (Note 5)	3,045	28,333	3,045	28,333
Other (income) loss, net	(539)	(49)	(441)	106
Operating income	64,893	82,150	275,182	309,393
Interest expense, net (Note 6)	15,360	13,753	45,078	36,912
Income before income taxes	49,533	68,397	230,104	272,481
Income tax expense (Note 12)	17,179	22,647	82,907	96,104
Net income	$32,354	$45,750	$147,197	$176,377
Earnings per share (Note 9):				
Basic	$0.47	$0.55	$2.11	$2.06
Diluted	$0.47	$0.54	$2.10	$2.05
Weighted average common shares outstanding (Note 9):				
Basic	68,190	83,669	69,808	85,663
Diluted	68,315	83,958	69,939	85,930
Dividends declared per share	$0.20	$0.18	$0.60	$0.54

The accompanying notes are an integral part of the consolidated financial statements.

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GNC HOLDINGS, INC. AND SUBSIDIARIES
Consolidated Statements of Comprehensive Income
(unaudited)
(in thousands)

	Three months ended September 30,		Nine months ended September 30,	
	2016	2015	2016	2015
Net income	$32,354	$45,750	$147,197	$176,377
Other comprehensive (loss) income:				
Foreign currency translation (loss) gain	(592)	(3,406)	2,263	(6,568)
Comprehensive income	$31,762	$42,344	$149,460	$169,809

The accompanying notes are an integral part of the consolidated financial statements.

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GNC HOLDINGS, INC. AND SUBSIDIARIES
Consolidated Statements of Stockholders' Equity
(unaudited)
(in thousands)

	Common Stock Class A		Treasury Stock	Paid-in Capital	Retained Earnings	Accumulated Other Comprehensive Loss	Total Stockholders' Equity
	Shares	Dollars					
Balance at December 31, 2015	76,276	$ 114	$ (1,496,180)	$ 916,128	$ 1,058,148	$ (9,649)	$ 468,561
Comprehensive income	—	—	—	—	147,197	2,263	149,460
Purchase of treasury stock	(7,926)	—	(229,169)	—	—	—	(229,169)
Dividends declared	—	—	—	—	(41,939)	—	(41,939)
Exercise of stock options	23	—	—	343	—	—	343
Restricted stock awards	72	—	—	—	—	—	—
Minimum tax withholding requirements	(47)	—	—	(1,126)	—	—	(1,126)
Net excess tax benefits from stock-based compensation	—	—	—	(742)	—	—	(742)
Stock-based compensation	—	—	—	7,191	—	—	7,191
Balance at September 30, 2016	68,398	$ 114	$ (1,725,349)	$ 921,794	$ 1,163,406	$ (7,386)	$ 352,579
Balance at December 31, 2014	88,335	$ 113	$ (1,016,381)	$ 877,566	$ 898,574	$ (3,829)	$ 756,043
Comprehensive income (loss)	—	—	—	—	176,377	(6,568)	169,809
Purchase of treasury stock	(6,012)	—	(279,798)	—	—	—	(279,798)
Dividends declared	—	—	—	—	(45,986)	—	(45,986)
Exercise of stock options	71	1	—	1,597	—	—	1,598
Restricted stock awards	239	—	—	—	—	—	—
Minimum tax withholding requirements	(7)	—	—	(381)	—	—	(381)
Net excess tax benefits from stock-based compensation	—	—	—	597	—	—	597
Stock-based compensation	—	—	—	4,747	—	—	4,747
Issuance of convertible notes, net (Note 6)	—	—	—	30,509	—	—	30,509
Balance at September 30, 2015	82,626	$ 114	$ (1,296,179)	$ 914,635	$ 1,028,965	$ (10,397)	$ 637,138

The accompanying notes are an integral part of the consolidated financial statements.

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GNC HOLDINGS, INC. AND SUBSIDIARIES
Consolidated Statements of Cash Flows
(unaudited)
(in thousands)

	Nine months ended September 30, 2016			2015		
Cash flows from operating activities:						
Net income	$	147,197		$	176,377	
Adjustments to reconcile net income to net cash provided by operating activities:						
Depreciation and amortization expense	43,547			43,100		
Amortization of debt costs	9,419			3,538		
Stock-based compensation	7,191			4,747		
Long-lived asset impairments	3,045			28,333		
Gains on refranchising	(18,283		)	(2,436		)
Changes in assets and liabilities:						
Decrease (increase) in receivables	3,519			(6,275		)
(Increase) decrease in inventory	(71,760		)	12,037		
(Increase) in prepaid and other current assets	(5,342		)	(9,084		)
Increase in accounts payable	35,700			14,691		
Increase in deferred revenue and accrued liabilities	13,515			11,635		
Other operating activities	1,999			(1,924		)
Net cash provided by operating activities	169,747			274,739		
Cash flows from investing activities:						
Capital expenditures	(35,368		)	(30,432		)
Refranchising proceeds	30,306			1,888		
Store acquisition costs	(1,918		)	(2,607		)
	(6,980		)	(31,151		)

Net cash used in investing activities		
Cash flows from financing activities:		
Borrowings under revolving credit facility	197,000	—
Payments on revolving credit facility	(103,000)	—
Payments on term loan facility	(3,412)	(167,901)
Proceeds from issuance of convertible senior notes	—	287,500
Debt issuance costs	(1,712)	(8,225)
Proceeds from exercise of stock options	343	1,597
Gross excess tax benefits from stock-based compensation	162	597
Minimum tax withholding requirements	(1,126)	(381)
Cash paid for treasury stock	(229,169)	(279,798)
Dividends paid to shareholders	(41,613)	(45,904)
Net cash used in financing activities	(182,527)	(212,515)
Effect of exchange rate changes on cash and cash equivalents	501	(833)
Net (decrease) increase in cash and cash equivalents	(19,259)	30,240
Beginning balance, cash and cash equivalents	56,462	133,834
Ending balance, cash and cash equivalents	$ 37,203	$ 164,074

The accompanying notes are an integral part of the consolidated financial statements.

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GNC HOLDINGS, INC. AND SUBSIDIARIES
Supplemental Cash Flow Information
(unaudited)
(in thousands)

	As of September 30,	
	2016	2015
Non-cash investing activities:		
Accrued capital expenditures	$3,432	$2,117

The accompanying notes are an integral part of the consolidated financial statements.

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GNC HOLDINGS, INC. AND SUBSIDIARIES
Condensed Notes to the Unaudited Consolidated Financial Statements

NOTE 1. NATURE OF BUSINESS

GNC Holdings, Inc., a Delaware corporation ("Holdings," and collectively with its subsidiaries and, unless the context requires otherwise, its and their respective predecessors, the "Company"), is a global specialty retailer of health, wellness and performance products, including protein, performance supplements, weight management supplements, vitamins, herbs and greens, wellness supplements, health and beauty, food and drink and other general merchandise.

The Company is vertically integrated as its operations consist of purchasing raw materials, formulating and manufacturing products and selling the finished products through its three reportable segments, which effective in the second quarter of 2016 include U.S. and Canada, International, and Manufacturing / Wholesale (refer to Note 11, "Segments" for more information). Corporate retail store operations are located in the United States, Canada, Puerto Rico, China and, beginning with the acquisition of THSD d/b/a The Health Store ("The Health Store") in 2014, Ireland. In addition, the Company offers products on the Internet through its websites, GNC.com and LuckyVitamin.com. The Company also offered product on the Internet through its 2013 acquisition of A1 Sports Limited d/b/a Discount Supplements ("Discount Supplements") up to and including December 31, 2015 when the assets of Discount Supplements were sold and operations were ceased. Franchise locations exist in the United States and approximately 50 other countries. The Company operates its primary manufacturing facilities in South Carolina and distribution centers in Arizona, Indiana, Pennsylvania and South Carolina. The Company manufactures the majority of its branded products, but also merchandises various third-party products. Additionally, the Company licenses the use of its trademarks and trade names.

The processing, formulation, packaging, labeling and advertising of the Company's products are subject to regulation by various federal agencies, including the Food and Drug Administration, the Federal Trade Commission, the Consumer Product Safety Commission, the United States Department of Agriculture and the Environmental Protection Agency. These activities are also regulated by various agencies of the states and localities in which the Company's products are sold.

NOTE 2. BASIS OF PRESENTATION

The accompanying unaudited consolidated financial statements, which have been prepared in accordance with the applicable rules of the Securities and Exchange Commission, include all adjustments (consisting of a normal and recurring nature) that management considers necessary to fairly state the Company's results of operations, financial position and cash flows. The December 31, 2015 consolidated balance sheet was derived from audited financial statements, but does not include all disclosures required by accounting principles generally accepted in the United States of America ("U.S. GAAP"). These interim consolidated financial statements should be read in conjunction with the consolidated financial statements and notes included in the Company's audited financial statements in its Annual Report on Form 10-K for the year ended December 31, 2015 ("2015 10-K"). Interim results are not necessarily indicative of the results that may be expected for the remainder of the year ending December 31, 2016.

Revision for Sublease Rent Income

The Company revised its presentation of sublease income received from its franchisees for prior year periods to conform to the current period's presentation with no impact on previously reported gross profit, operating income, net income, shareholders' equity or cash flow from operations. The Company is the primary obligor of the leases for the majority of its franchise store locations and makes rental payments directly to the landlord and separately bills the franchisee for reimbursement. Accordingly, beginning in the first quarter of 2016, sublease rental income received from franchisees is appropriately presented as “Revenue” compared with the previous presentation as a reduction to occupancy expense in “Cost of sales, including warehousing, distribution, and occupancy" on the consolidated statements of income. In addition, the deferred rent asset associated with recognizing sublease rental income for lease agreements that contain escalation clauses, which are fixed and determinable, on a straight-line basis is now appropriately presented in “Other long-term assets” compared with the previous presentation as a reduction to the deferred rent liability in “Other long-term liabilities" on the consolidated balance sheets. This revision is not material to prior periods.

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The following table includes the revisions to the 2015 consolidated statements of income:

	Three months ended September 30	Nine months ended September 30
Revenue:	(in thousands)	
Prior to revision	$672,244	$2,021,011
Revision	11,114	33,176
As Revised	$683,358	$2,054,187
Cost of sales, including warehousing, distribution and occupancy:		
Prior to revision	$421,600	$1,264,602
Revision	11,114	33,176
As Revised	$432,714	$1,297,778

The following table includes the revision to the consolidated balance sheet:

	December 31, 2015
Other long-term assets:	(in thousands)
Prior to revision (*)	$ 32,891
Revision	5,664
As Revised	$ 38,555
Other long-term liabilities:	
Prior to revision	$ 53,352
Revision	5,664
As Revised	$ 59,016

(*) Includes the adoption of ASU 2015-03 and 2015-15 relating to the presentation of deferred financing fees as described below, which reclassified $3.3 million of debt issuance costs from "Other long-term assets" to "Long-term debt" at December 31, 2015 on the consolidated balance sheet.

Correction of Prior Year Immaterial Error

During the quarter ended March 31, 2015, the Company identified a $2.8 million error relating to prior periods in the calculation of the portion of the accrued payroll liability relating to certain amounts paid to store employees. The impact of this error was not material to any prior period. Consequently, the Company corrected the error in the first quarter of 2015 by increasing "Selling, general and administrative" expense on the consolidated statement of income and "Deferred revenue and other current liabilities" on the consolidated balance sheet by $2.8 million. The impact to net income was a decrease of $1.8 million for the nine months ended September 30, 2015. This correction had no impact on cash flows from operations for the prior year nine-month period.

Recently Adopted Accounting Pronouncements

In April 2015, the Financial Accounting Standards Board ("FASB") issued Accounting Standard Update ("ASU") 2015-03, which requires an entity to present debt issuance costs related to a recognized debt liability as a direct reduction from the carrying amount of that debt liability, consistent with the treatment of debt discounts. This standard does not affect the recognition and measurement guidance for debt issuance costs. In August 2015, the FASB subsequently issued ASU 2015-15, which clarifies that ASU 2015-03 does not address the presentation of debt issuance costs related to line-of-credit arrangements. This standard is effective for fiscal years beginning after December 15, 2015. Accordingly, the Company adopted these standards during the first quarter of fiscal 2016, with retrospective application. Net debt issuance costs in the amount of $3.3 million, which were previously classified as "Other long-term assets" at December 31, 2015, were reclassified as a reduction to "Long-term debt" on the Company's consolidated balance sheet to conform to the current year presentation.

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Recently Issued Accounting Pronouncements

In March 2016, the FASB issued ASU 2016-09, which includes multiple provisions intended to simplify various aspects of accounting and reporting for share-based payments. Currently, the difference between the deduction for tax purposes and the compensation cost of a share-based payment award results in either an excess tax benefit or deficiency. These excess tax benefits are recognized in additional paid-in capital and tax deficiencies (to the extent there are previous tax benefits) are recognized as an offset to accumulated excess tax benefits. If no previous tax benefit exists, the deficiencies are recognized in the income statement. The changes require all excess tax benefits and tax deficiencies related to share-based payments be recognized as income tax expense or benefit in the income statement as opposed to equity. The excess tax benefit in the cash flow statement will also change from its current presentation as a financing activity to being classified with other income tax as an operating activity. This standard is effective for annual reporting periods, and interim periods therein, beginning after December 15, 2016. The Company does not expect the impact of this guidance to have a material impact on the consolidated financial statements.

In February 2016, the FASB issued ASU 2016-02, which requires lessees to recognize a right-of-use asset and a lease liability, initially measured at the present value of the lease payments for all leases with a term greater than 12 months. This standard is effective for annual reporting periods, and interim periods therein, beginning after December 15, 2018 and is required to be applied using a modified retrospective approach for all leases existing at, or entered into after, the beginning of the earliest comparative period presented. The Company has a significant number of leases, and as a result, expects this guidance to have a material impact on its consolidated balance sheet, the impact of which is currently being evaluated.

In November 2015, the FASB issued ASU 2015-17, which requires an entity to classify deferred tax assets and liabilities as noncurrent on the balance sheet. This standard is effective for annual reporting periods, and interim periods therein, beginning after December 15, 2016. The Company does not believe the adoption of this guidance will have a material effect on the consolidated financial statements.

In July 2015, the FASB issued ASU 2015-11, which requires an entity that determines the cost of inventory by methods other than last-in, first-out and the retail inventory method to measure inventory at the lower of cost and net realizable value. This standard is effective for annual reporting periods, and interim periods therein, beginning after December 15, 2016. The Company does not believe the adoption of this guidance will have a material effect on the Company's consolidated financial statements.

In May 2014, the FASB issued ASU 2014-09, which updates revenue recognition guidance relating to contracts with customers. This standard states that an entity should recognize revenue to depict the transfer of promised 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. In August 2015, the FASB subsequently issued ASU 2015-14, which approved a one year deferral of ASU 2014-09 for annual reporting periods beginning after December 15, 2017, including interim periods within that reporting period. The Company is currently evaluating the impact this guidance will have on the consolidated financial statements.

Other Revisions

In addition to the sublease rent revision and the adoption of ASU 2015-03 as explained above, certain amounts in the consolidated financial statements for prior year periods have been revised to conform to the current period's presentation. The impact to prior periods of these revisions was not significant with no impact on previously reported operating income, net income, cash flows from operations or stockholders' equity.

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NOTE 3. INVENTORY

The net realizable value of inventory consisted of the following:

	September 30, 2016	December 31, 2015
	(in thousands)	
Finished product ready for sale	$557,076	$487,075
Work-in-process, bulk product and raw materials	58,993	62,242
Packaging supplies	5,796	6,568
Total inventory	$621,865	$555,885

NOTE 4. REFRANCHISING

Gains on Refranchising

The Company has begun to execute its previously announced refranchising strategy, which includes increasing the proportion of its domestic stores that are franchise locations. During the nine months ended September 30, 2016, the Company refranchised 96 of its company-owned stores, including six refranchised during the three months ended September 30, 2016 and recorded refranchising gains of $18.3 million, of which $0.4 million related to the current quarter. The Company refranchised five and 12 stores, respectively, during the three and nine months ended September 30, 2015 and recorded refranchising gains of $0.9 million and $2.4 million during the respective periods.

Refranchising gains are calculated by subtracting the carrying value of applicable assets disposed of from the sales proceeds. In addition, the initial franchise fee received is included in the gain along with any other costs incurred by the Company to get the underlying assets ready for sale. The Company recognizes gains on refranchising after the asset purchase agreement is signed, the franchisee has taken possession of the store and management is satisfied that the franchisee can meet its financial obligations.

During the nine months ended September 30, 2016, the Company completed the refranchising of 84 stores to one franchisee for $28.6 million of net proceeds resulting in a gain of $16.5 million. The Company provided a short term promissory note as bridge financing while the franchisee secured third party bank loans. The demand note of $23.0 million was paid in July 2016, and together with a $0.5 million deposit and $5.1 million primarily related to inventory, resulted in a $28.6 million investing cash inflow in the nine months ending September 30, 2016.

Held for Sale

The Company classifies assets as held for sale when it commits to a plan to dispose of the assets by refranchising specific stores in their current condition at a price that is reasonable and the Company believes completing the sale within one year is probable without significant changes. Assets held for sale are recorded at the lower of their carrying value or fair value, less costs to sell and depreciation is ceased on assets at the time they are classified as held for sale. During the quarter ended September 30, 2016, the Company reclassified $1.8 million of the applicable assets of 10 company-owned stores previously presented as held for sale within “Prepaid and other current assets” to "Inventory," "Goodwill" and "Property, plant and equipment, net" in the accompanying consolidated balance sheet as the Company no longer expects to sell these assets during the next 12 months.

Goodwill

In connection with the Company's change in reportable segments described in Note 11, "Segments," the Company's Domestic Retail and Domestic Franchise reporting units were combined into one Domestic Stores reporting unit, consistent with how the segment manager now reviews this business effective in the second quarter of 2016. The amount of goodwill derecognized in a refranchising is determined by a fraction (the numerator of which is the fair value of the portion of the reporting unit being sold and the denominator of which is the fair value of the Domestic Stores reporting unit) that is applied to the total goodwill balance of the Domestic Stores reporting unit. The fair value of the portion of the reporting unit sold is determined by the sales price, which is generally based on the discounted future cash flows expected to be generated by the franchisee. Appropriate adjustments are made to the fair value determinations if such franchise agreement is determined to not be at prevailing market rates. In connection with the

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sale of 96 company-owned stores to franchisees during the nine months ended September 30, 2016, the Company derecognized $3.6 million of goodwill that was included in the carrying value of the assets sold.

NOTE 5. GOODWILL AND OTHER LONG-LIVED ASSETS

Interim Impairment Test

Based on the Company's continued decline in operating results coupled with the sustained decrease in share price through September 30, 2016, management concluded a triggering event occurred in the current quarter requiring an interim goodwill impairment test for all of its reporting units as of September 30, 2016. Based on the results of this interim test, management concluded that all of the Company's reporting units had fair values in excess of their respective carrying values. Approximately $12 million of goodwill associated with the Lucky Vitamin reporting unit had an estimated fair value that exceeded its carrying value by less than 15% consistent with the 2015 annual test performed. If actual market conditions are less favorable than those projected, or if events occur or circumstances change that would reduce the fair value of the Lucky Vitamin reporting unit below its carrying value, an impairment charge may be recognized in a future period. Management estimated the fair value of its reporting units using the discounted cash flow method (income approach). Management also performed a quantitative impairment test for its indefinite-lived brand intangible assets and concluded that the fair values were in excess of their respective carrying values. The relief from royalty method (income approach) was used to calculate the fair value of the Retail brand and the excess earnings method (income approach) was used to calculate the fair value of the Franchise brand.

Management also evaluated its definite-long-lived assets consisting of property, equipment and other intangible assets. This impairment test resulted in a $3.0 million charge related to certain of the Company's under-performing stores in the three months ended September 30, 2016 presented as "Long-lived asset impairments" in the accompanying statement of income within the U.S. and Canada segment. For individual under-performing stores and those stores with expected future losses, the impairment test was performed at the individual store level as this is the lowest level which identifiable cash flows are largely independent of other groups of assets and liabilities. This test was performed by comparing estimated future undiscounted cash flows expected to result from the long-lived assets to the carrying value of the asset group, consisting of fixed assets and inventory. Under-performing stores were generally defined as those with historical and expected future losses. If the undiscounted estimated cash flows are less than the carrying value of the asset group, an impairment charge is calculated by subtracting the estimated fair value of property and equipment from its carrying value. Fair value is estimated using a discounted cash flow method (income approach) utilizing the undiscounted cash flows computed in the first step of the test.

Discount Supplements

During the third quarter of 2015, due to the declining financial performance and the Company’s decision to review strategic options for the business a triggering event occurred requiring an interim goodwill impairment review of the Discount Supplements reporting unit as of September 30, 2015. The Company determined the fair value of the Discount Supplements reporting unit at September 30, 2015 using a discounted cash flow method (income approach). As a result of the review, the Company concluded that the carrying value of the Discount Supplements reporting unit exceeded its fair value and proceeded to step two of the impairment analysis. Based on the results of step two, the Company concluded that this reporting unit was fully impaired; as a result, a goodwill impairment charge of $23.3 million was recorded in the third quarter of 2015.

As a result of the impairment indicators, the Company also performed an impairment analysis with respect to the definite-long-lived assets of Discount Supplements, consisting of trade name and website intangibles and property and equipment. The fair value of these assets were determined using various income approaches. Based on the results of the analyses, the Company recorded impairment charges of $4.4 million on the trade name and website intangible assets and $0.6 million on property and equipment. All of the aforementioned charges totaling $28.3 million were recorded in "Long-lived asset impairments" in the consolidated statement of income for the nine months ended September 30, 2015.

The Company sold Discount Supplements in the fourth quarter of 2015.

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Goodwill

The following table summarizes the Company's goodwill activity:

	U.S. and Canada	International	Manufacturing/ Wholesale	Total
	(in thousands)			
Balance at December 31, 2015	$403,874	$ 43,177	$ 202,841	$649,892
Acquired franchise stores	1,391	—	—	1,391
Translation effect of exchange rates	21	151	—	172
Franchise conversions	(3,649)	—	—	(3,649)
Balance at September 30, 2016	$401,637	$ 43,328	$ 202,841	$647,806

Intangible Assets

Intangible assets other than goodwill consisted of the following:

	Retail Brand	Franchise Brand	Operating Agreements	Other Intangibles	Total
	(in thousands)				
Balance at December 31, 2015	$500,000	$220,000	$ 112,359	$ 6,845	$839,204
Acquired franchise stores	—	—	—	280	280
Amortization expense	—	—	(4,990)	(1,309)	(6,299)
Translation effect of exchange rates	—	—	—	12	12
Balance at September 30, 2016	$500,000	$220,000	$ 107,369	$ 5,828	$833,197

The following table reflects the gross carrying amount and accumulated amortization for each major intangible asset:

	Weighted-Average Life	September 30, 2016			December 31, 2015		
		Cost	Accumulated Amortization	Carrying Amount	Cost	Accumulated Amortization	Carrying Amount
		(in thousands)					
Brands - retail	Indefinite	$500,000	$ —	$500,000	$500,000	$ —	$500,000
Brands - franchise	Indefinite	220,000	—	220,000	220,000	—	220,000
Retail agreements	30.3	31,000	(10,197)	20,803	31,000	(9,407)	21,593
Franchise agreements	25.0	70,000	(26,717)	43,283	70,000	(24,617)	45,383
Manufacturing agreements	25.0	70,000	(26,717)	43,283	70,000	(24,617)	45,383
Other intangibles	11.8	10,239	(5,347)	4,892	10,222	(4,560)	5,662
Franchise rights	3.0	7,486	(6,550)	936	7,206	(6,023)	1,183
Total		$908,725	$ (75,528)	$833,197	$908,428	$ (69,224)	$839,204

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The following table represents future estimated amortization expense of intangible assets with finite lives at September 30, 2016:

Years ending December 31,	Estimated amortization expense (in thousands)
2016 (remainder)	$ 1,946
2017	7,627
2018	7,426
2019	7,286
2020	7,223
Thereafter	81,689
Total	$ 113,197

NOTE 6. LONG-TERM DEBT

Long-term debt consisted of the following:

	September 30, 2016	December 31, 2015
	(in thousands)	
Term Loan Facility (net of $1.7 million and $2.2 million discount)	$1,171,457	$1,174,369
Revolving Credit Facility	137,000	43,000
Notes	242,675	235,085
Debt issuance costs	(2,544)	(3,276)
Total debt	1,548,588	1,449,178
Less: current maturities	(4,550)	(4,550)
Long-term debt	$1,544,038	$1,444,628

The Company maintains a $1.2 billion term loan facility (the “Term Loan Facility”) that matures in March 2019. The Company also maintains a $300.0 million revolving credit facility (the “Revolving Credit Facility” and, together with the Term Loan Facility, the “Senior Credit Facility”) that matures in September 2018 as described in more detail below.

At September 30, 2016 and December 31, 2015, the interest rate under the Term Loan Facility was 3.25%. The Revolving Credit Facility had a weighted average interest rate of 2.7% and 2.6% at September 30, 2016 and December 31, 2015, respectively. At September 30, 2016 and December 31, 2015, the commitment fee on the undrawn portion of the Revolving Credit Facility was 0.5%, and the fee on outstanding letters of credit was 2.50%.

Refinancing of Revolving Credit Facility

The Company amended the Revolving Credit Facility on March 4, 2016, to extend its maturity from March 2017 to September 2018 and increase total availability from $130.0 million to $300.0 million. In connection with this transaction, the Company incurred $1.7 million of costs, which were capitalized as deferred financing fees within "Other long-term assets" and will be amortized to interest expense over the new term of the Revolving Credit Facility. At September 30, 2016, the Company had $157.4 million available under the Revolving Credit Facility, after giving effect to $137.0 million of borrowings outstanding and $5.6 million utilized to secure letters of credit.

Convertible Debt

Summary of Terms. On August 10, 2015, the Company issued $287.5 million principal amount of 1.5% convertible senior notes due 2020 (the “Notes”) in a private offering. The Notes are governed by the terms of an indenture between the Company and BNY Mellon Trust Company, N.A., as the Trustee (the "Indenture"). The Notes will mature on August 15, 2020, unless earlier purchased by the Company or converted. The Notes will bear interest at a rate of 1.5% per annum, and additionally will be subject to special interest in connection with any failure of the Company to perform certain of its obligations under the Indenture.

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The Notes are unsecured obligations and do not contain any financial covenants or restrictions on the payments of dividends, the incurrence of indebtedness or the issuance or repurchase of securities by the Company or any of its subsidiaries. Certain events are considered “events of default” under the Notes, which may result in the acceleration of the maturity of the Notes, as described in the indenture governing the Notes. The Notes are fully and unconditionally guaranteed by certain operating subsidiaries of the Company (“Subsidiary Guarantors”) and are subordinated to the Subsidiary Guarantors obligations from time to time with respect to the Senior Credit Facility and ranks equal in right of payment with respect to the Subsidiary Guarantor’s other obligations.

The initial conversion rate applicable to the Notes is 15.1156 shares of common stock per $1,000 principal amount of Notes, which is equivalent to an initial conversion price of approximately $66.16 per share. The conversion rate will be subject to adjustment upon the occurrence of certain specified events, but will not be adjusted for any accrued and unpaid special interest. In addition, upon the occurrence of a “make-whole fundamental change" as defined in the Indenture, the Company will, in certain circumstances, increase the conversion rate by a number of additional shares for a holder that elects to convert its Notes in connection with such make-whole fundamental change.

Prior to May 15, 2020, the Notes will be convertible only under the following circumstances: (1) during any calendar quarter commencing after September 30, 2015, if, for at least 20 trading days (whether or not consecutive) during the 30 consecutive trading day period ending on the last trading day of the immediately preceding calendar quarter, the last reported sale price of the Company’s common stock on such trading day is greater than or equal to 130% of the applicable conversion price on such trading day; (2) during the 5 consecutive business day period after any 10 consecutive trading day period in which, for each day of that period, the trading price per $1,000 principal amount of Notes for such trading day was less than 98% of the product of the last reported sale price of the Company’s common stock and the applicable conversion rate on such trading day; or (3) upon the occurrence of specified corporate transactions. On and after May 15, 2020, until the close of business on the second scheduled trading day immediately preceding the maturity date, holders may convert all or a portion of their Notes at any time, regardless of the foregoing circumstances. Upon conversion, the Notes will be settled, at the Company’s election, in cash, shares of the Company’s common stock, or a combination of cash and shares of the Company’s common stock. If the Company has not delivered a notice of its election of settlement method prior to the final conversion period it will be deemed to have elected combination settlement with a dollar amount per note to be received upon conversion of $1,000.

The Notes consist of the following components:

	September 30, 2016	December 31, 2015
	(in thousands)	
Liability component		
Principal	$287,500	$287,500
Conversion feature	(39,493)	(46,271)
Discount related to debt issuance costs	(5,332)	(6,144)
Net carrying amount	$242,675	$235,085
Equity component		
Conversion feature	$49,680	$49,680
Debt issuance costs	(1,421)	(1,421)
Deferred taxes	(17,750)	(17,750)
Net amount recorded in additional paid-in capital	$30,509	$30,509

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Interest Expense

Interest expense consisted of the following:

	Three months ended September 30,		Nine months ended September 30,	
	2016	2015	2016	2015
	(in thousands)			
Senior Credit Facility:				
Term Loan Facility coupon	$9,753	$10,390	$29,076	$32,366
Revolver	1,359	172	3,420	510
Amortization of discount and debt issuance costs	591	1,243	1,775	2,168
Total Senior Credit Facility	11,703	11,805	34,271	35,044
Notes:				
Coupon	1,078	623	3,234	623
Amortization of conversion feature	2,294	1,218	6,778	1,218
Amortization of discount and debt issuance costs	290	147	845	147
Total Notes	3,662	1,988	10,857	1,988
Interest income and other	(5)	(40)	(50)	(120)
Interest expense, net	$15,360	$13,753	$45,078	$36,912

NOTE 7. FAIR VALUE MEASUREMENTS AND FINANCIAL INSTRUMENTS

Accounting Standards Codification 820, Fair Value Measurements and Disclosures defines fair value as a market-based measurement that should be determined based on the assumptions that marketplace participants would use in pricing an asset or liability. As a basis for considering such assumptions, the standard establishes a three-tier fair value hierarchy which prioritizes the inputs used in measuring fair value as follows:

Level 1 — observable inputs such as quoted prices in active markets for identical assets and liabilities;

Level 2 — observable inputs such as quoted prices for similar assets or liabilities in active markets, quoted prices for identical or similar assets or liabilities in markets that are not active, other inputs that are observable, or can be corroborated by observable market data; and

Level 3 — unobservable inputs for which there are little or no market data, which require the reporting entity to develop its own assumptions.

The carrying amounts of cash and cash equivalents, receivables, accounts payable, accrued liabilities and the Revolving Credit Facility approximate their respective fair values. Based on the interest rates currently available and their underlying risk, the carrying value of franchise notes receivable recorded in "Other long-term assets" approximates its fair value.

The carrying value and estimated fair value of the Term Loan Facility and Notes (excluding the equity component classified in stockholders' equity) were as follows:

	September 30, 2016		December 31, 2015	
	Carrying Amount	Fair Value	Carrying Amount	Fair Value
	(in thousands)			
Term Loan Facility	$1,171,457	$1,172,921	$1,174,369	$1,145,010
Notes	242,675	213,491	235,085	188,940

The fair value of the Term Loan Facility was determined using the instrument's trading value in markets that are not active, which are considered Level 2 inputs. The fair value of the Notes was determined based on quoted market prices and bond terms and conditions, which are considered Level 2 inputs.

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As described in Note 5, "Goodwill and Other Long-Lived Assets," the Company recorded asset impairments in the three months ended September 30, 2016 and 2015. This resulted in property and equipment at certain of the Company's corporate stores at September 30, 2016 and goodwill and definite-long-lived assets of Discount Supplements (which was sold in the fourth quarter of 2015) at September 30, 2015 being measured at fair value on a non-recurring basis using Level 3 inputs.

NOTE 8. CONTINGENCIES

The Company is engaged in various legal actions, claims and proceedings arising in the normal course of business, including claims related to breach of contracts, product liabilities, intellectual property matters and employment-related matters resulting from the Company's business activities.

The Company records accruals for outstanding legal matters when it believes it is probable that a loss will be incurred and the amount of such loss can be reasonably estimated. The Company evaluates, on a quarterly basis, developments in legal matters that could affect the amount of any accrual and developments that would make a loss contingency both probable and reasonably estimable. If a loss contingency is not both probable and estimable, the Company does not establish an accrued liability. During the three months ended September 30, 2016, the Company recorded $5.1 million in legal-related charges associated with a Pennsylvania fluctuating workweek wage issue, the Jason Olive case and a government regulation matter, the amounts of which were individually immaterial. These items are explained in more detail below. If the Company ultimately is required to make additional payments in connection with an adverse outcome in any of the matters discussed below, it is possible that it could have a material adverse effect on the Company's business, financial condition, results of operations or cash flows.

The Company's contingencies are subject to substantial uncertainties, including for each such contingency the following, among other factors: (i) the procedural status of the case; (ii) whether the case has or may be certified as a class action suit; (iii) the outcome of preliminary motions; (iv) the impact of discovery; (v) whether there are significant factual issues to be determined or resolved; (vi) whether the proceedings involve a large number of parties and/or parties and claims in multiple jurisdictions or jurisdictions in which the relevant laws are complex or unclear; (vii) the extent of potential damages, which are often unspecified or indeterminate; and (viii) the status of settlement discussions, if any, and the settlement posture of the parties. Consequently, except as otherwise noted below with regard to a particular matter, the Company cannot predict with any reasonable certainty the timing or outcome of the legal matters described below, and the Company is unable to estimate a possible loss or range of loss.

As a manufacturer and retailer of nutritional supplements and other consumer products that are ingested by consumers or applied to their bodies, the Company has been and is currently subjected to various product liability claims. Although the effects of these claims to date have not been material to the Company, it is possible that current and future product liability claims could have a material adverse effect on its business or financial condition, results of operations or cash flows. The Company currently maintains product liability insurance with a deductible/retention of $4.0 million per claim with an aggregate cap on retained loss of $10.0 million. The Company typically seeks and has obtained contractual indemnification from most parties that supply raw materials for its products or that manufacture or market products it sells. The Company also typically seeks to be added, and has been added, as an additional insured under most of such parties' insurance policies. The Company is also entitled to indemnification by Numico for certain losses arising from claims related to products containing ephedra or Kava Kava sold prior to December 5, 2003. However, any such indemnification or insurance is limited by its terms and any such indemnification, as a practical matter, is limited to the creditworthiness of the indemnifying party and its insurer, and the absence of significant defenses by the insurers. Consequently, the Company may incur material product liability claims, which could increase its costs and adversely affect its reputation, revenue and operating income.

Litigation

DMAA / Aegeline Claims. Prior to December 2013, the Company sold products manufactured by third parties that contained derivatives from geranium known as 1.3-dimethylpentylamine/dimethylamylamine/13-dimethylamylamine, or "DMAA," which were recalled from the Company's stores in November 2013, and/or Aegeline, a compound extracted from bael trees. As of September 30, 2016, the Company was named in 30 personal injury lawsuits involving products containing DMAA and/or Aegeline.

As a general matter, the proceedings associated with these personal injury cases, which generally seek indeterminate money damages, are in the early stages, and any losses that may arise from these matters are not probable or reasonably estimable at this time.

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The Company is contractually entitled to indemnification by its third-party vendors with regard to these matters, although the Company's ability to obtain full recovery in respect of any such claims against it is dependent upon the creditworthiness of the vendors and/or their insurance coverage and the absence of any significant defenses available to its insurer.

California Wage and Break Claims. In July 2011, Charles Brewer, on behalf of himself and all others similarly situated, sued General Nutrition Corporation in federal court, alleging state and federal wage and hour claims. In October 2011, plaintiff filed an eight-count amended complaint alleging, among other matters, meal, rest break and overtime violations on behalf of sales associates and store managers. In January 2013, the Court conditionally certified a Fair Labor Standards Act ("FLSA") class with respect to one of Plaintiff's claims, and in November 2014, the Court granted in part and denied in part the plaintiff's motion to certify a California class and granted the Company's motion for decertification of the FLSA class. In May 2015, plaintiffs filed a motion for partial summary judgment as to the Company's alleged liability for non-compliant wage statements, which was granted in part and denied in part in September 2015. On February 5, 2016, the Company and attorneys representing the putative class agreed to class-wide settlements of the Brewer case and an additional, immaterial case raising similar claims, pursuant to which the Company agreed to pay up to $9.5 million in the aggregate, including attorneys' fees and costs. Following a hearing on August 23, 2016, the Court approved the settlement agreement and dismissed the case with prejudice. As a result of this settlement, the Company recorded a charge of $6.3 million in the fourth quarter of 2015, in addition to $3.2 million previously accrued in the first quarter of 2015.

On February 29, 2012, former Senior Store Manager, Elizabeth Naranjo, individually and on behalf of all others similarly situated, sued General Nutrition Corporation in the Superior Court of the State of California for the County of Alameda. The complaint contains eight causes of action, alleging, among other matters, meal, rest break and overtime violations. As of September 30, 2016, an immaterial liability has been accrued in the accompanying financial statements.

Pennsylvania Fluctuating Workweek. On September 18, 2013, Tawny Chevalier and Andrew Hiller commenced a class action in the Court of Common Pleas of Allegheny County, Pennsylvania. Plaintiff asserted a claim against the Company for a purported violation of the Pennsylvania Minimum Wage Act (PMWA), challenging the Company's utilization of the "fluctuating workweek" method to calculate overtime compensation, on behalf of all employees who worked for the Company in Pennsylvania and who were paid according to the fluctuating workweek method. In October 2014, the Court entered an order holding that the use of the fluctuating workweek method violated the PMWA. In September 2016, the Court entered judgment in favor of Plaintiffs and the class in an immaterial amount, which has been recorded as a charge in the quarter ended September 30, 2016 in the accompanying consolidated financial statements. Plaintiffs subsequently filed a petition for an award of attorney's fees, costs and incentive payments; that petition is pending. The Company appealed from the adverse judgment; the appeal is pending.

Jason Olive v. General Nutrition Corp. In April 2012, Jason Olive filed a complaint in the Superior Court of California, County of Los Angeles, for misappropriation of likeness in which he alleges that the Company continued to use his image in stores after the expiration of the license to do so in violation of common law and California statutes. Mr. Olive is seeking compensatory, punitive and statutory damages and attorneys' fees and costs. The trial in this matter began on July 20, 2016 and concluded on August 8, 2016. The jury awarded plaintiff immaterial amounts for actual damages and emotional distress damages, which are accrued in the Company's accompanying financial statements. The jury refused to award plaintiff any of the profits he sought to disgorge, or punitive damages. The court has not yet entered judgment in the case. In addition to the verdict, the Company expects Mr. Olive to seek attorneys' fees and other costs in a total amount as yet unknown to the Company; because this amount cannot be reasonably estimated at this time, no amount has been accrued in the financial statements.

Oregon Attorney General. On October 22, 2015, the Attorney General for the State of Oregon sued General Nutrition Corporation in Multnomah County Circuit Court for alleged violations of Oregon's Unlawful Trade Practices Act, in connection with its sale in Oregon of certain third-party products, which was amended on September 19, 2016 to add allegations related to products containing DMAA and oxilofrine. The Company intends to continue to vigorously defend against all of these allegations. As any losses that may arise from this matter are not probable or reasonably estimable at this time, no liability has been accrued in the accompanying interim consolidated financial statements. Moreover, the Company does not anticipate that any such losses are likely to have a material impact on the Company, its business or results of operations. The Company is contractually entitled to indemnification and defense by its third-party vendors. Ultimately, however, the Company's ability to obtain full recovery in respect of any such claims against it is dependent upon the creditworthiness of its vendors and/or their insurance coverage and the absence of any significant defenses available to their insurers.

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Government Regulation

In November 2013, the Company received a subpoena from the U.S. Department of Justice (“DOJ”) for information related to its investigation of a third party product vendor, USP Labs, LLC. GNC fully cooperated with the investigation of the vendor and the related products, all of which were discontinued by GNC in 2013. In October 2016, the Company reached agreement in principle with DOJ in connection with the Company’s cooperation; which agreement would acknowledge GNC relied on the representations and written guarantees of USP Labs and GNC’s representation that it did not knowingly sell products not in compliance with the FDCA. Under the agreement, which would include an immaterial payment to the federal government, GNC will take a number of actions to broaden industry-wide knowledge of prohibited ingredients and improve compliance by vendors of third party products. These actions are in keeping with the leadership role GNC has taken in setting industry quality and compliance standards, and GNC’s commitment over the course of the agreement (60 months) to support a combination of GNC and industry initiatives.

Environmental Compliance

In March 2008, the South Carolina Department of Health and Environmental Control (the "DHEC") requested that the Company investigate contamination associated with historical activities at its South Carolina facility. These investigations have identified chlorinated solvent impacts in soils and groundwater that extend offsite from the facility. The Company entered into a Voluntary Cleanup Contract with the DHEC regarding the matter on September 24, 2012. Pursuant to such contract, the Company is completing additional investigations with the DHEC's approval. The Company installed and began operating a pilot vapor extraction system under a portion of the facility in the second half of 2016, which was an immaterial cost to the Company, with DHEC’s approval to assess the effectiveness of such a remedial system. At this stage of the investigation, however, it is not possible to estimate the timing and extent of any additional remedial action that may be required, the ultimate cost of remediation, or the amount of the Company's potential liability, therefore no liability is recorded.

In addition to the foregoing, the Company is subject to numerous federal, state, local and foreign environmental and health and safety laws and regulations governing its operations, including the handling, transportation and disposal of the Company's non-hazardous and hazardous substances and wastes, as well as emissions and discharges from its operations into the environment, including discharges to air, surface water and groundwater. Failure to comply with such laws and regulations could result in costs for remedial actions, penalties or the imposition of other liabilities. New laws, changes in existing laws or the interpretation thereof, or the development of new facts or changes in their processes could also cause the Company to incur additional capital and operating expenditures to maintain compliance with environmental laws and regulations and environmental permits. The Company is also subject to laws and regulations that impose liability and cleanup responsibility for releases of hazardous substances into the environment without regard to fault or knowledge about the condition or action causing the liability. Under certain of these laws and regulations, such liabilities can be imposed for cleanup of previously owned or operated properties, or for properties to which substances or wastes that were sent in connection with current or former operations at its facilities. The presence of contamination from such substances or wastes could also adversely affect the Company's ability to sell or lease its properties, or to use them as collateral for financing. From time to time, the Company has incurred costs and obligations for correcting environmental and health and safety noncompliance matters and for remedia