

GNC HOLDINGS, INC.  
Form 10-Q  
November 01, 2012

# UNITED STATES SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

## Form 10-Q

(Mark one)

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

For the quarterly period ended **September 30, 2012**

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**  
(State or other jurisdiction of  
Incorporation or organization)

**300 Sixth Avenue**  
**Pittsburgh, Pennsylvania**  
(Address of principal executive offices)

**20-8536244**  
(I.R.S. Employer  
Identification No.)

**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.  Yes  No

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

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

Large accelerated filer       Accelerated filer       Non-accelerated filer       Smaller reporting company

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

As of October 26, 2012, there were 99,298,280 outstanding shares of Class A common stock, par value \$0.001 per share (the Class A common stock), of GNC Holdings, Inc.

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**TABLE OF CONTENTS**

|                                       | <b>PAGE</b>   |
|---------------------------------------|---|
| <b>PART I - FINANCIAL INFORMATION</b> |   |
| <b>Item 1.</b>                        | <b>Financial Statements</b>   |
|                                       | Consolidated Balance Sheets as of September 30, 2012 (unaudited) and December 31, 2011                                    |
|                                       | 1   |
|                                       | Unaudited Consolidated Statements of Income for the three and nine months ended September 30, 2012 and 2011               |
|                                       | 2   |
|                                       | Unaudited Consolidated Statements of Comprehensive Income for the three and nine months ended September 30, 2012 and 2011 |
|                                       | 2   |
|                                       | Unaudited Consolidated Statements of Stockholders' Equity for the nine months ended September 30, 2012 and 2011           |
|                                       | 3   |
|                                       | Unaudited Consolidated Statements of Cash Flows for the nine months ended September 30, 2012 and 2011                     |
|                                       | 4   |
|                                       | Summarized Notes to Unaudited Consolidated Financial Statements   |
|                                       | 5   |
| <b>Item 2.</b>                        | <b>Management's Discussion and Analysis of Financial Condition and Results of Operations</b>                              |
|                                       | 17  |
| <b>Item 3.</b>                        | <b>Quantitative and Qualitative Disclosures About Market Risk</b>   |
|                                       | 28  |
| <b>Item 4.</b>                        | <b>Controls and Procedures</b>  |
|                                       | 28  |
| <b>PART II - OTHER INFORMATION</b>    |   |
| <b>Item 1.</b>                        | <b>Legal Proceedings</b>  |
|                                       | 29  |
| <b>Item 1A.</b>                       | <b>Risk Factors</b>   |
|                                       | 30  |
| <b>Item 2.</b>                        | <b>Unregistered Sales of Equity Securities and Use of Proceeds</b>  |
|                                       | 32  |
| <b>Item 3.</b>                        | <b>Defaults Upon Senior Securities</b>  |
|                                       | 32  |
| <b>Item 4.</b>                        | <b>Mine Safety Disclosures</b>  |
|                                       | 32  |
| <b>Item 5.</b>                        | <b>Other Information</b>  |
|                                       | 32  |
| <b>Item 6.</b>                        | <b>Exhibits</b>   |
|                                       | 32  |
| <b>Signatures</b>                     | 33  |

**PART I - FINANCIAL INFORMATION****Item 1. Financial Statements****GNC HOLDINGS, INC. AND SUBSIDIARIES****Consolidated Balance Sheets****(in thousands, including share data)**

|   | <b>September 30,<br/>2012<br/>(unaudited)</b> | <b>December 31,<br/>2011</b> |
|---|---|------------------------------|
| Current assets:   |   |                              |
| Cash and cash equivalents   | \$ 96,795                                     | \$ 128,438                   |
| Receivables, net  | 134,585                                       | 114,190                      |
| Inventories (Note 3)  | 496,069                                       | 423,610                      |
| Prepays and other current assets  | 43,397  | 38,777                       |
| Total current assets  | 770,846                                       | 705,015                      |
| Long-term assets:   |   |                              |
| Goodwill (Note 4)   | 639,765                                       | 637,877                      |
| Brands (Note 4)   | 720,000                                       | 720,000                      |
| Other intangible assets, net (Note 4)   | 143,745                                       | 149,589                      |
| Property, plant and equipment, net  | 198,405                                       | 198,171                      |
| Other long-term assets  | 29,702  | 18,935                       |
| Total long-term assets  | 1,731,617                                     | 1,724,572                    |
| Total assets  | \$ 2,502,463                                  | \$ 2,429,587                 |
| Current liabilities:  |   |                              |
| Accounts payable  | 116,472                                       | 124,416                      |
| Current portion, long-term debt (Note 5)  | 3,788   | 1,592                        |
| Deferred revenue and other current liabilities  | 120,147                                       | 104,525                      |
| Total current liabilities   | 240,407                                       | 230,533                      |
| Long-term liabilities:  |   |                              |
| Long-term debt (Note 5)   | 1,095,291                                     | 899,950                      |
| Deferred tax liabilities, net   | 285,331                                       | 283,403                      |
| Other long-term liabilities   | 42,937  | 37,239                       |
| Total long-term liabilities   | 1,423,559                                     | 1,220,592                    |
| Total liabilities   | 1,663,966                                     | 1,451,125                    |
| Stockholders' equity:   |   |                              |
| Common stock, \$0.001 par value, 150,000 shares authorized:   |   |                              |
| Class A, 111,525 shares issued and 99,073 shares outstanding and 12,452 shares held in treasury at September 30, 2012 and 105,988 shares issued and 102,985 shares outstanding and 3,004 shares held in treasury at December 31, 2011 | 111   | 105                          |
| Class B, 0 and 2,060 shares issued and outstanding at September 30, 2012 and December 31, 2011, respectively  | -   | 2                            |
| Paid-in-capital   | 802,703                                       | 741,848                      |
| Retained earnings   | 456,237                                       | 298,831                      |
| Treasury stock, at cost   | (423,900)                                     | (65,048)                     |
| Accumulated other comprehensive income  | 3,346   | 2,724                        |
| Total stockholders' equity  | 838,497                                       | 978,462                      |

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|  |    |           |    |           |
|--|----|-----------|----|-----------|
| Total liabilities and stockholders' equity | \$ | 2,502,463 | \$ | 2,429,587 |
|--|----|-----------|----|-----------|

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

## GNC HOLDINGS, INC. AND SUBSIDIARIES

## Consolidated Statements of Income

(unaudited)

(in thousands, except per share data)

|  | Three months ended September 30, |            | Nine months ended September 30, |              |
|--|----------------------------------|------------|---------------------------------|--------------|
|  | 2012                             | 2011       | 2012                            | 2011         |
| Revenue  | \$ 621,607                       | \$ 538,028 | \$ 1,864,961                    | \$ 1,562,571 |
| Cost of sales, including cost of warehousing, distribution and occupancy | 386,393                          | 343,129    | 1,149,600                       | 992,908      |
| Gross profit   | 235,214                          | 194,899    | 715,361                         | 569,663      |
| Compensation and related benefits  | 78,707                           | 72,375     | 237,126                         | 219,011      |
| Advertising and promotion  | 15,697                           | 12,433     | 45,327                          | 40,031       |
| Other selling, general and administrative                                | 28,717                           | 26,629     | 91,075                          | 84,530       |
| Foreign currency (loss) gain   | (8)                              | 225        | (84)                            | 106          |
| Transaction related costs  | 924                              | 637        | 1,610                           | 12,999       |
| Operating income   | 111,177                          | 82,600     | 340,307                         | 212,986      |
| Interest expense, net (Note 5)   | 12,080                           | 10,418     | 32,958                          | 64,517       |
| Income before income taxes   | 99,097                           | 72,182     | 307,349                         | 148,469      |
| Income tax expense (Note 10)   | 36,868                           | 23,519     | 114,592                         | 53,879       |
| Net income   | \$ 62,229                        | \$ 48,663  | \$ 192,757                      | \$ 94,590    |
| <b>Income per share - Basic and Diluted:</b>                             |                                  |            |                                 |              |
| Net income   | \$ 62,229                        | \$ 48,663  | \$ 192,757                      | \$ 94,590    |
| Preferred stock dividends  | -                                | -          | -                               | (4,726)      |
| Net income available to common shareholders                              | \$ 62,229                        | \$ 48,663  | \$ 192,757                      | \$ 89,864    |
| Earnings per share:  |                                  |            |                                 |              |
| Basic  | \$ 0.61                          | \$ 0.47    | \$ 1.84                         | \$ 0.91      |
| Diluted  | \$ 0.60                          | \$ 0.45    | \$ 1.81                         | \$ 0.89      |
| Weighted average common shares outstanding:                              |                                  |            |                                 |              |
| Basic  | 102,541                          | 104,390    | 104,946                         | 98,223       |
| Diluted  | 103,721                          | 107,351    | 106,515                         | 100,858      |
| Dividends declared per share:  | \$ 0.11                          | -          | \$ 0.33                         | -            |

## Consolidated Statements of Comprehensive Income

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(unaudited)

(in thousands)

|  | Three months ended September 30, |           | Nine months ended September 30, |           |
|--|----------------------------------|-----------|---------------------------------|-----------|
|  | 2012                             | 2011      | 2012                            | 2011      |
| Net income   | \$ 62,229                        | \$ 48,663 | \$ 192,757                      | \$ 94,590 |
| <i>Other comprehensive income:</i>   |                                  |           |                                 |           |
| Unrealized gains on derivatives and qualified as cash flow hedges, net of tax of \$2,718 | -                                | -         | -                               | 4,751     |
| Foreign currency translation adjustments   | 848                              | (2,397)   | 622                             | (1,277)   |
| Other comprehensive income   | 848                              | (2,397)   | 622                             | 3,474     |
| Comprehensive income   | \$ 63,077                        | \$ 46,266 | \$ 193,379                      | \$ 98,064 |

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

## GNC HOLDINGS, INC. AND SUBSIDIARIES

## Consolidated Statements of Stockholders Equity

(unaudited)

(in thousands, including per share data)

|  | Common Stock   |                 |                |                 | Treasury Stock      | Paid-in-Capital  | Retained Earnings | Accumulated Other Comprehensive Income/(Loss) | Total Stockholders Equity |
|--|----------------|-----------------|----------------|-----------------|---------------------|------------------|-------------------|---|---------------------------|
|  | Class A Shares | Class A Dollars | Class B Shares | Class B Dollars |                     |                  |                   |   |                           |
| <b>Balance at December 31, 2011</b>              | <b>102,985</b> | <b>\$ 105</b>   | <b>2,060</b>   | <b>\$ 2</b>     | <b>\$ (65,048)</b>  | <b>\$741,848</b> | <b>\$298,831</b>  | <b>\$ 2,724</b>                               | <b>\$ 978,462</b>         |
| Comprehensive Income                             | -              | -               | -              | -               | -                   | -                | 192,757           | 622   | 193,379                   |
| Conversion of Class B stock to Class A stock     | 2,060          | 2               | (2,060)        | (2)             | -                   | -                | -                 | -   | -                         |
| Purchase of treasury stock                       | (9,477)        | -               | -              | -               | (358,852)           | -                | -                 | -   | (358,852)                 |
| Common stock dividends                           | -              | -               | -              | -               | -                   | -                | (34,300)          | -   | (34,300)                  |
| Conversions to common stock                      | 3,505          | 4               | -              | -               | -                   | 57,246           | -                 | -   | 57,250                    |
| Non-cash stock-based compensation                | -              | -               | -              | -               | -                   | 3,609            | -                 | -   | 3,609                     |
| Other  | -              | -               | -              | -               | -                   | -                | (1,051)           | -   | (1,051)                   |
| <b>Balance at September 30, 2012 (unaudited)</b> | <b>99,073</b>  | <b>\$ 111</b>   | <b>-</b>       | <b>\$ -</b>     | <b>\$ (423,900)</b> | <b>\$802,703</b> | <b>\$456,237</b>  | <b>\$ 3,346</b>                               | <b>\$ 838,497</b>         |
| <b>Balance at December 31, 2010</b>              | <b>59,199</b>  | <b>\$ 60</b>    | <b>28,169</b>  | <b>\$ 28</b>    | <b>\$ (2,277)</b>   | <b>\$451,728</b> | <b>\$171,224</b>  | <b>\$ (1,280)</b>                             | <b>\$ 619,483</b>         |
| Comprehensive Income                             | -              | -               | -              | -               | -                   | -                | 94,590            | 3,474   | 98,064                    |
| Issuance of common stock                         | 16,000         | 16              | -              | -               | -                   | 237,237          | -                 | -   | 237,253                   |
| Conversion of Class B stock to Class A stock     | 14,387         | 14              | (14,387)       | (14)            | -                   | -                | -                 | -   | -                         |
| Preferred stock dividends                        | -              | -               | -              | -               | -                   | -                | (4,726)           | -   | (4,726)                   |
| Conversions to common stock                      | 1,572          | 1               | -              | -               | -                   | 18,620           | -                 | -   | 18,621                    |
| Non-cash stock-based compensation                | -              | -               | -              | -               | -                   | 2,895            | -                 | -   | 2,895                     |
| <b>Balance at September 30, 2011 (unaudited)</b> | <b>91,158</b>  | <b>\$ 91</b>    | <b>13,782</b>  | <b>\$ 14</b>    | <b>\$ (2,277)</b>   | <b>\$710,480</b> | <b>\$261,088</b>  | <b>\$ 2,194</b>                               | <b>\$ 971,590</b>         |

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



## GNC HOLDINGS, INC. AND SUBSIDIARIES

## Consolidated Statements of Cash Flows

(unaudited)

(in thousands)

|   | Nine Months Ended September 30, |                  |
|---|---------------------------------|------------------|
|   | 2012                            | 2011             |
| <b><u>CASH FLOWS FROM OPERATING ACTIVITIES:</u></b>                               |                                 |                  |
| Net income  | \$ 192,757                      | \$ 94,590        |
| Adjustments to reconcile net income to net cash provided by operating activities: |                                 |                  |
| Loss on early extinguishment of debt  | -                               | 19,855           |
| Depreciation and amortization expense   | 36,476                          | 34,344           |
| Amortization of debt costs  | 1,811                           | 2,195            |
| Increase in provision for inventory losses  | 8,902                           | 14,582           |
| Increase in receivables   | (23,273)                        | (15,205)         |
| Increase in inventory   | (78,193)                        | (46,418)         |
| Decrease in prepaids and other current assets                                     | 4,568                           | 2,452            |
| (Decrease) increase in accounts payable   | (7,855)                         | 36,155           |
| Increase in deferred revenue and other current liabilities                        | 8,721                           | 1,371            |
| Other operating activities  | (1,962)                         | 2,459            |
| <b>Net cash provided by operating activities</b>                                  | <b>141,952</b>                  | <b>146,380</b>   |
| <b><u>CASH FLOWS FROM INVESTING ACTIVITIES:</u></b>                               |                                 |                  |
| Capital expenditures  | (29,856)                        | (27,808)         |
| Acquisition of LuckyVitamin.com, net of cash required                             | -                               | (20,998)         |
| Other investing activities  | (1,966)                         | (1,437)          |
| <b>Net cash used in investing activities</b>                                      | <b>(31,822)</b>                 | <b>(50,243)</b>  |
| <b><u>CASH FLOWS FROM FINANCING ACTIVITIES:</u></b>                               |                                 |                  |
| Payments on long-term debt  | (1,757)                         | (1,355,566)      |
| Dividends paid to shareholders  | (34,300)                        | -                |
| Proceeds from exercised stock options   | 23,840                          | 11,125           |
| Repurchase of treasury stock  | (359,990)                       | -                |
| Tax benefit from exercise of stock options  | 35,605                          | 8,379            |
| Repurchase of Series A preferred stock  | -                               | (223,107)        |
| Net proceeds from sale of Class A common stock                                    | -                               | 237,253          |
| Proceeds from issuance of long-term debt  | 199,000                         | 1,196,200        |
| Deferred financing fees   | (1,148)                         | (17,346)         |
| Other financing activities  | (2,500)                         | -                |
| <b>Net cash used in financing activities</b>                                      | <b>(141,250)</b>                | <b>(143,062)</b> |
| Effect of exchange rate on cash and cash equivalents                              | (523)                           | (870)            |
| Decrease in cash and cash equivalents   | (31,643)                        | (47,795)         |
| Beginning balance, cash and cash equivalents                                      | 128,438                         | 193,902          |
| Ending balance, cash and cash equivalents   | \$ 96,795                       | \$ 146,107       |

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

## NOTE 1. NATURE OF BUSINESS

**General Nature of Business.** GNC Holdings, Inc., formerly GNC Acquisition 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 and wellness products, which include: vitamins, minerals and herbal supplements, sports nutrition products, diet products and other wellness products.

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 primary segments: Retail, Franchising and Manufacturing/Wholesale. Corporate retail store operations are located in the United States, Canada and Puerto Rico, and in addition the Company offers products domestically through GNC.com, www.drugstore.com, and since September 2011, LuckyVitamin.com. Franchise stores are located in the United States and 55 international countries (including distribution centers where retail sales are made). The Company operates its primary manufacturing facilities in South Carolina and distribution centers in Arizona, 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 one or more federal agencies, including the Food and Drug Administration (the FDA ), Federal Trade Commission, Consumer Product Safety Commission, 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.

**Recent Significant Transactions.** In March 2011, General Nutrition Centers, Inc. ( Centers ), a wholly owned subsidiary of Holdings, entered into a senior credit facility, consisting of a \$1.2 billion term loan facility (the Term Loan Facility ) and an \$80.0 million revolving credit facility (the Revolving Credit Facility ) and, together with the Term Loan Facility, the Senior Credit Facility ), and utilized the proceeds to repay all outstanding indebtedness under the 2007 Senior Credit Facility, the Senior Notes, and the Senior Subordinated Notes (the Refinancing ). Subsequently, the Company completed two amendments to the Term Loan Facility. On August 1, 2012, the Company amended the Term Loan Facility to increase the outstanding borrowings by \$200.0 million (the Incremental Term Loan ). In October 2012, Centers amended the Term Loan Facility to adjust the per annum interest rate to the greater of LIBOR and 1.00%, plus an applicable margin of 2.75%. The Refinancing and these amendments are collectively referred to herein as the Refinancings.

In April 2011, Holdings consummated an initial public offering (the IPO ) of 25.875 million shares of its Class A common stock, par value \$0.001 per share (the Class A common stock ), at an IPO price of \$16.00 per share. The net proceeds from the IPO, together with cash on hand, were used to redeem all outstanding shares of Holdings' Series A preferred stock, par value \$0.001 per share (the Series A preferred stock ), repay approximately \$300.0 million of outstanding borrowings under the Term Loan Facility and pay approximately \$11.1 million to satisfy obligations under the Management Services Agreement (as defined in Note 11, Related Party Transactions ) and Holdings' Class B common stock, par value \$0.001 per share (the Class B common stock ) and, together with the Class A common stock, the common stock ). Subsequent to the IPO, certain of Holdings' stockholders completed the following registered offerings of Class A common stock:

- in October 2011, 23.0 million shares at \$24.75 per share;
- in March 2012, 19.6 million shares at \$33.50 per share; and

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- in August 2012, 10.0 million shares at \$38.42 per share.

In conjunction with the August 2012 offering, the Company repurchased an additional six million shares of Class A common stock from one of its stockholders as part of a share repurchase program. The IPO, the offerings, and the repurchase of the six million shares of Class A common stock are collectively referred to herein as the Offerings.

As of September 30, 2012, the Company had completed its approved share repurchase programs for a total of \$360.0 million of Class A common stock.

**GNC HOLDINGS, INC. AND SUBSIDIARIES**

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)**

On August 31, 2011, the Company acquired substantially all of the assets and assumed certain liabilities of S&G Properties, LLC d/b/a LuckyVitamin.com and What s The Big Deal?, Inc. d/b/a Gary s World of Wellness (collectively referred to as LuckyVitamin.com ), an online retailer of health and wellness products. The aggregate purchase price of LuckyVitamin.com was approximately \$19.8 million.

**NOTE 2. BASIS OF PRESENTATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**

The accompanying unaudited consolidated financial statements have been prepared in accordance with the rules and regulations of the Securities and Exchange Commission. Accordingly, certain information and footnote disclosures normally included in the annual financial statements prepared in accordance with accounting principles generally accepted in the United States ( GAAP ) have been omitted. 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 the Holdings Annual Report on Form 10-K filed for the year ended December 31, 2011. There have been no material changes to the application of critical accounting policies and significant judgments and estimates since December 31, 2011.

The accompanying unaudited consolidated financial statements include all adjustments (consisting of a normal and recurring nature) that management considers necessary for a fair statement of financial information for the interim periods. Interim results are not necessarily indicative of the results that may be expected for the remainder of the year ending December 31, 2012.

**Principles of Consolidation.** The consolidated financial statements include the accounts of Holdings and all of its subsidiaries. All material intercompany transactions have been eliminated in consolidation.

The Company has no relationships with unconsolidated entities or financial partnerships, such as entities often referred to as structured finance or special purpose entities, which would have been established for the purpose of facilitating off balance sheet arrangements, or other contractually narrow or limited purposes.

**Use of Estimates.** The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions. Accordingly, these estimates and assumptions affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements, and the reported amounts of revenues and expenses during the reporting period. Some of the most significant estimates pertaining to the Company include the valuation of inventories, the allowance for doubtful accounts and income taxes. On a regular basis, management reviews its estimates utilizing currently available information, changes in facts and circumstances, historical experience and reasonable assumptions. After such reviews and if deemed appropriate, those estimates are adjusted accordingly. Actual results could differ from those estimates.

**Transaction Related Costs.** The Company recognizes transaction related costs as expenses in the period incurred. For the nine months ended September 30, 2012 and 2011, the Company recognized \$1.6 million and \$13.0 million, respectively, of expenses related to the Offerings and the Refinancings.

### Recent Accounting Pronouncements

In June 2011, the Financial Accounting Standards Board (the FASB ) issued updated guidance on current comprehensive income presentation. This accounting update eliminates the option to present the components of other comprehensive income as part of the statement of stockholders' equity. Instead, the Company must report comprehensive income in either a single continuous statement of comprehensive income that contains two sections, net income and other comprehensive income, or in two separate but consecutive statements. This new guidance is effective for the Company for fiscal years beginning after December 15, 2011, with early adoption permitted. The Company adopted this guidance during the first quarter of 2012. The adoption of this guidance had no material impact on the Company's consolidated financial statements, as it only required a change in the format of presentation.

In May 2011, the FASB issued changes to conform existing guidance regarding fair value measurement and disclosure between GAAP and International Financial Reporting Standards. These changes both clarify the FASB's intent about the application of existing fair value measurement and disclosure requirements and amend certain principles or requirements for measuring fair value or for disclosing information about fair value measurements. The clarifying changes relate to the application of the highest and best use and valuation premise concepts, measuring the fair value of an instrument classified in a reporting entity's stockholders' equity, and

**GNC HOLDINGS, INC. AND SUBSIDIARIES****NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)**

disclosure of quantitative information about unobservable inputs used for Level 3 fair value measurements. The amendments relate to measuring the fair value of financial instruments that are managed within a portfolio; application of premiums and discounts in a fair value measurement; and additional disclosures concerning the valuation processes used and sensitivity of the fair value measurement to changes in unobservable inputs for those items categorized as Level 3, a reporting entity's use of a nonfinancial asset in a way that differs from the asset's highest and best use, and the categorization by level in the fair value hierarchy for items required to be measured at fair value for disclosure purposes only. The Company adopted this guidance during the first quarter of 2012, and it had no material impact on the Company's financial statements.

In July 2012, the FASB issued an accounting standard that simplifies the impairment test for indefinite-lived intangible assets other than goodwill. The new guidance gives the option to first assess qualitative factors to determine if it is more likely than not that the fair value of an indefinite-lived intangible asset is less than its carrying amount as a basis for determining whether it is necessary to perform a quantitative valuation test. The new standard is effective for fiscal years, and interim periods within those fiscal years, beginning on or after September 15, 2012. The Company will adopt this accounting standard in the fourth quarter of 2012 and it does not anticipate that this adoption will have a significant impact on its financial statements.

**NOTE 3. INVENTORIES**

The net carrying value of inventories consisted of the following:

|   | <b>September 30,<br/>2012<br/>(unaudited)</b> | <b>December 31,<br/>2011</b> |
|---|---|------------------------------|
|   | <b>(in thousands)</b>                         |                              |
| Finished product ready for sale                 | \$ 415,259                                    | \$ 354,913                   |
| Work-in-process, bulk product and raw materials | 73,373  | 61,684                       |
| Packaging supplies                              | 7,437   | 7,013                        |
| Total   | \$ 496,069                                    | \$ 423,610                   |

**NOTE 4. GOODWILL AND INTANGIBLE ASSETS, NET**

For the nine months ended September 30, 2012 and 2011, the Company acquired 23 and 22 franchise stores, respectively. These acquisitions were accounted for as business combinations and the Company recorded the acquired inventory, fixed assets, franchise rights and goodwill, with an applicable reduction to receivables and cash. For the nine months ended September 30, 2012 and 2011, the total purchase price associated with these acquisitions was \$3.6 million and \$2.1 million, respectively, of which \$1.8 million and \$0.8 million, respectively, was paid in cash.

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The following table summarizes the Company's goodwill activity:

|  | <b>Retail</b>  | <b>Franchising</b> | <b>Manufacturing/<br/>Wholesale</b> | <b>Total</b> |
|--|----------------|--------------------|-------------------------------------|--------------|
|  | (in thousands) |                    |                                     |              |
| Balance at December 31, 2011                 | \$ 317,733     | \$ 117,303         | \$ 202,841                          | \$ 637,877   |
| Acquired franchise stores                    | 1,888          | -                  | -                                   | 1,888        |
| Balance at September 30, 2012<br>(unaudited) | \$ 319,621     | \$ 117,303         | \$ 202,841                          | \$ 639,765   |

7

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## GNC HOLDINGS, INC. AND SUBSIDIARIES

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

Intangible assets other than goodwill consisted of the following:

|  | <b>Retail<br/>Brand</b> | <b>Franchise<br/>Brand</b> | <b>Operating<br/>Agreements<br/>(in thousands)</b> | <b>Other<br/>Intangibles</b> | <b>Total</b> |
|--|-------------------------|----------------------------|--|------------------------------|--------------|
| Balance at December 31, 2011                 | \$ 500,000              | \$ 220,000                 | \$ 138,970   | \$ 10,619                    | \$ 869,589   |
| Acquired franchise stores                    | -                       | -                          | -  | 548                          | 548          |
| Amortization expense                         | -                       | -                          | (4,990)  | (1,402)                      | (6,392)      |
| Balance at September 30, 2012<br>(unaudited) | \$ 500,000              | \$ 220,000                 | \$ 133,980   | \$ 9,765                     | \$ 863,745   |

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

|                          | <b>Weighted -<br/>Average<br/>Life</b> | <b>Cost</b> | <b>September 30, 2012<br/>Accumulated<br/>Amortization<br/>(unaudited)</b> | <b>Carrying<br/>Amount</b> | <b>Cost</b> | <b>December 31, 2011<br/>Accumulated<br/>Amortization</b> | <b>Carrying<br/>Amount</b> |
|--------------------------|--|-------------|--|----------------------------|-------------|---|----------------------------|
| (in thousands)           |  |             |  |                            |             |   |                            |
| Brands - retail          | -                                      | \$ 500,000  | \$ -   | \$ 500,000                 | \$ 500,000  | \$ -  | \$ 500,000                 |
| Brands - franchise       | -                                      | 220,000     | -  | 220,000                    | 220,000     | -   | 220,000                    |
| Retail agreements        | 30.2                                   | 31,000      | (5,986)  | 25,014                     | 31,000      | (5,196)   | 25,804                     |
| Franchise agreements     | 25.0                                   | 70,000      | (15,517)   | 54,483                     | 70,000      | (13,417)  | 56,583                     |
| Manufacturing agreements | 25.0                                   | 70,000      | (15,517)   | 54,483                     | 70,000      | (13,417)  | 56,583                     |
| Other intangibles        | 11.4                                   | 10,600      | (1,848)  | 8,752                      | 10,600      | (938)   | 9,662                      |
| Franchise rights         | 3.7                                    | 4,981       | (3,968)  | 1,013                      | 4,433       | (3,476)   | 957                        |
| Total                    | 24.5                                   | \$ 906,581  | \$ (42,836)  | \$ 863,745                 | \$ 906,033  | \$ (36,444)   | \$ 869,589                 |

The following table represents future estimated amortization expense of intangible assets with finite lives at September 30, 2012:

| <b>Estimated<br/>amortization<br/>expense<br/>(unaudited)</b> |
|---|
| <b>Years ending December 31,</b>                              |
| <b>(in thousands)</b>   |



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|            |    |         |
|------------|----|---------|
| 2012       | \$ | 2,115   |
| 2013       |    | 8,293   |
| 2014       |    | 8,121   |
| 2015       |    | 7,995   |
| 2016       |    | 7,915   |
| Thereafter |    | 109,306 |
| Total      | \$ | 143,745 |

## GNC HOLDINGS, INC. AND SUBSIDIARIES

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

## NOTE 5. LONG-TERM DEBT / INTEREST EXPENSE

Long-term debt consisted of the following:

|                          | September 30,<br>2012<br>(unaudited) | December 31,<br>2011 |
|--------------------------|--------------------------------------|----------------------|
|                          | (in thousands)                       |                      |
| Senior Credit Facility   | \$ 1,096,191                         | \$ 897,387           |
| Mortgage                 | 2,878                                | 4,135                |
| Capital leases           | 10                                   | 20                   |
| Total debt               | 1,099,079                            | 901,542              |
| Less: current maturities | (3,788)                              | (1,592)              |
| Long-term debt           | \$ 1,095,291                         | \$ 899,950           |

For the nine months ended September 30, 2012, interest expense of \$33.0 million consisted primarily of interest on outstanding borrowings under the Term Loan Facility. Interest under both the Term Loan Facility and the Revolving Credit Facility is based on variable rates. At September 30, 2012 and December 31, 2011, the interest rate under the Term Loan Facility was 5.25% and 4.25%, respectively, and the interest rate under the Revolving Credit Facility was 4.00% and 4.25%, respectively. The Revolving Credit Facility was undrawn and had outstanding letters of credit of \$1.2 million and \$8.0 million at September 30, 2012 and December 31, 2011, respectively. Interest on the letters of credit was 3.00% and 3.25% at September 30, 2012 and December 31, 2011, respectively.

For the nine months ended September 30, 2011, interest expense of \$64.5 million consisted primarily of \$24.1 million on the Senior Credit Facility, \$23.2 million of expenses related to the Refinancing, \$4.9 million of original issue discount and deferred financing fees related to the \$300.0 million repayment of outstanding borrowings under the Term Loan Facility in connection with the IPO, and \$10.3 million of interest expense on former indebtedness prior to the Refinancing. The \$23.2 million of expenses related to the Refinancing consisted of \$5.8 million in interest rate swap termination costs, write-off of \$13.4 million of deferred financing fees of former indebtedness, write-off of \$1.6 million in original issue discount related to former indebtedness and \$2.4 million to defease former indebtedness.

On August 1, 2012, Centers borrowed an additional \$200.0 million under the Incremental Term Loan. After payment of certain fees and expenses, such proceeds were utilized to partially fund the Company's announced share repurchase program. On October 2, 2012, Centers amended the Term Loan Facility to adjust the per annum interest rate to the greater of LIBOR and 1.00%, plus an applicable margin of 2.75%.

As of September 30, 2012, the Company believes that it is in compliance with all covenants under the Senior Credit Facility.

**NOTE 6. FINANCIAL INSTRUMENTS**

At September 30, 2012 and December 31, 2011, the Company's financial instruments consisted of cash and cash equivalents, receivables, franchise notes receivable, accounts payable, certain accrued liabilities and long-term debt. The carrying amount of cash and cash equivalents, receivables, accounts payable and accrued liabilities approximates their respective fair values because of the short maturities of these instruments. Based on the interest rates currently available and their underlying risk, the carrying value of the franchise notes receivable approximates their respective fair values. These fair values are reflected net of reserves for uncollectible amounts. The Company determined the estimated fair values of its debt by using currently available market information. The fair value of debt would be classified as a Level 1 category on the fair value hierarchy, as defined in the Company's Annual Report on Form 10-K for the year ended December 31, 2011. As considerable judgment is required to determine these estimates and assumptions, changes in the assumptions or methodologies may have an effect on these estimates. The actual and estimated fair values of the Company's financial instruments are as follows:

## GNC HOLDINGS, INC. AND SUBSIDIARIES

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

|  | September 30, 2012 |               | December 31, 2011  |               |
|--|--------------------|---------------|--------------------|---------------|
|  | Carrying<br>Amount | Fair<br>Value | Carrying<br>Amount | Fair<br>Value |
|  | (unaudited)        |               |                    |               |
|  | (in thousands)     |               |                    |               |
| Cash and cash equivalents                  | \$ 96,795          | \$ 96,795     | \$ 128,438         | \$ 128,438    |
| Receivables, net                           | 134,585            | 134,585       | 114,190            | 114,190       |
| Franchise notes receivable, net            | 7,024              | 7,024         | 6,510              | 6,510         |
| Accounts payable                           | 116,472            | 116,472       | 124,416            | 124,416       |
| Long-term debt (including current portion) | 1,099,079          | 1,099,079     | 901,542            | 892,526       |

## NOTE 7. COMMITMENTS AND CONTINGENCIES

## Litigation

The Company is engaged in various legal actions, claims and proceedings resulting from the Company's business activities arising in the normal course of business, including claims related to breach of contracts, products liabilities, intellectual property matters and employment-related matters. As with most actions such as these, an estimation of any possible and/or ultimate liability cannot always be determined. The Company continues to assess the requirement to account for additional contingencies in accordance with the standard on contingencies. If the Company is required to make a payment in connection with an adverse outcome in these matters, it could have a material impact on its business, financial condition, operating results and cash flows.

As a manufacturer and retailer of health and wellness products 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 impact on its business, financial condition, operating results or cash flows. The Company currently maintains product liability insurance with a deductible/retention of \$3.0 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 a former owner of the Company 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.

*Hydroxycut Claims.* On May 1, 2009, the FDA issued a warning on several Hydroxycut-branded products manufactured by Iovate Health Sciences U.S.A., Inc. (Iovate). The FDA warning was based on 23 reports of liver injuries from consumers who claimed to have used the products between 2002 and 2009. As a result, Iovate voluntarily recalled 14 Hydroxycut-branded products. Following the recall, the Company was named, among other defendants, in approximately 94 lawsuits related to Hydroxycut-branded

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products in 14 states. lovate previously accepted the Company's tender request for defense and indemnification under its purchasing agreement with the Company and, as such, lovate has accepted the Company's request for defense and indemnification in the Hydroxycut matters. The Company's ability to obtain full recovery under the indemnity is dependent on lovate's insurance coverage, the creditworthiness of its insurer, and the absence of significant defenses by such insurer. To the extent the Company is not fully compensated by lovate's insurer, it can seek recovery directly from lovate. The Company's ability to fully recover such amounts may be limited by the creditworthiness of lovate.

Currently, there are 73 pending lawsuits related to Hydroxycut in which the Company has been named: 67 individual, largely personal injury claims and six putative class action cases, generally inclusive of claims of consumer fraud, misrepresentation, strict liability and breach of warranty. As any liabilities that may arise from these matters are not probable or reasonably estimable at this time, no liability has been accrued in the accompanying financial statements.

**GNC HOLDINGS, INC. AND SUBSIDIARIES**

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)**

By court order dated October 6, 2009, the United States Judicial Panel on Multidistrict Litigation consolidated pretrial proceedings of many of the pending actions in the Southern District of California (In re: Hydroxycut Marketing and Sales Practices Litigation, MDL No. 2087).

*Pro-Hormone/Androstenedione Cases.* The Company is currently defending two lawsuits (the Andro Actions ) in New Jersey and New York relating to the sale by the Company of certain nutritional products between 1999 and 2004, alleged to contain the ingredients commonly known as Androstenedione, Androstenediol, Norandrostenedione, and Norandrostenediol (collectively, Andro Products ). In each of the Andro Actions, plaintiffs sought, or are seeking, to certify a class and obtain damages on behalf of the class representatives and all those similarly-situated who purchased from the Company certain nutritional supplements alleged to contain one or more Andro Products. As any liabilities that may arise from these other Andro Actions are not probable or reasonably estimable at this time, no liability has been accrued in the accompanying financial statements.

**Commitments**

The Company maintains certain purchase commitments with various vendors to ensure its operational needs are fulfilled. As of September 30, 2012, such future purchase commitments consisted of \$4.8 million. Other commitments related to the Company s business operations cover varying periods of time and are not significant. All of these commitments are expected to be fulfilled with no adverse consequences to the Company s operations or financial condition.

**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 its 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 has submitted a plan for additional investigations to the DHEC and is awaiting the DHEC s approval of the plan. After the Company completes the investigations to understand the extent of the chlorinated solvent impacts, the Company will develop appropriate remedial measures for DHEC approval. At this stage of the investigation, however, it is not possible to estimate the timing and extent of any remedial action that may be required, the ultimate cost of remediation, or the amount of the Company s potential liability.

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 operation expenditures to maintain compliance with environmental laws and regulations and environmental permits. The Company also is 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 remediation at or relating to certain of its properties or properties at which its waste has been disposed. The Company believes it has complied with, and is currently complying with, its environmental obligations pursuant to environmental and health and safety laws and regulations and that any liabilities for noncompliance will not have a material adverse effect on its business, financial performance, or cash flows. However, it is difficult to predict future liabilities and obligations, which could be material.

**GNC HOLDINGS, INC. AND SUBSIDIARIES**

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)**

**NOTE 8. STOCK-BASED COMPENSATION PLANS**

The Company has outstanding stock-based compensation awards that were granted by the Compensation Committee (the Compensation Committee ) of the Board of Directors of Holdings (the Board ) under the following two stock-based employee compensation plans:

- the GNC Holdings, Inc. 2011 Stock and Incentive Plan (the 2011 Stock Plan ) adopted in March 2011; and
- the GNC Acquisition Holdings Inc. 2007 Stock Incentive Plan (as amended, the 2007 Stock Plan ) adopted in March 2007.

Both plans have provisions that allow for the granting of stock options, restricted stock and other stock based awards and are available to certain eligible employees, directors, consultants or advisors as determined by the Compensation Committee. Stock options under the plans were granted with exercise prices at or above fair market value on the date of grant, typically vest in equal installments over a four- or five-year period and expire seven or ten years from the date of grant.

Up to 8.5 million shares of Class A common stock may be issued under the 2011 Stock Plan (subject to adjustment to reflect certain transactions and events specified in the 2011 Stock Plan for any award grant). If any award granted under the 2011 Stock Plan expires, terminates or is cancelled without having been exercised in full, the number of shares underlying such unexercised award will again become available for awards under the 2011 Stock Plan. The total number of shares of Class A common stock available for awards under the 2011 Stock Plan will be reduced by (i) the total number of stock options or stock appreciation rights exercised, regardless of whether any of the shares of Class A common stock underlying such awards are not actually issued to the participant as the result of a net settlement, and (ii) any shares of Class A common stock used to pay any exercise price or tax withholding obligation. In addition, the number of shares of Class A common stock that are subject to restricted stock, performance shares or other stock-based awards that are not subject to the appreciation of the value of a share of Class A common stock ( Full Share Awards ) that may be granted under the 2011 Stock Plan is limited by counting shares granted pursuant to such awards against the aggregate share reserve as 1.8 shares for every share granted. If any stock option, stock appreciation right or other stock-based award that is not a Full Share Award is cancelled, expires or terminates unexercised for any reason, the shares covered by such awards will again be available for the grant of awards under the 2011 Stock Plan. If any shares of Class A common stock that are subject to restricted stock, performance shares or other stock-based awards that are Full Share Awards are forfeited for any reason, 1.8 shares of Class A common stock for each Full Share Award forfeited will again be available for the grant of awards under the 2011 Stock Plan.

Upon adoption of the 2011 Stock Plan, the Company determined it will not grant any additional awards under the 2007 Stock Plan. No stock appreciation rights, restricted stock, deferred stock or performance shares were granted under the 2007 Stock Plan.



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The Company utilizes the Black Scholes model to calculate the fair value of options under both the 2011 Stock Plan and the 2007 Stock Plan. The grant-date fair value of the Company's restricted stock awards is based on the stock price on the grant date. The resulting compensation cost is recognized in the Company's financial statements over the option vesting period. The Company recognized \$3.6 million and \$2.9 million of non-cash stock-based compensation expense for the nine months ended September 30, 2012 and 2011, respectively. At September 30, 2012, there was approximately \$13.3 million of total unrecognized compensation cost related to non-vested stock-based compensation for all awards previously made that are expected to be recognized over a weighted average period of approximately 1.8 years.

During the nine months ended September 30, 2012, the total intrinsic value of awards exercised was \$96.8 million and the total amount received by Holdings from the exercise of options was \$23.8 million. The tax impact associated with the exercise of awards for the nine months ended September 30, 2012 was a benefit of \$35.6 million.

## GNC HOLDINGS, INC. AND SUBSIDIARIES

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

The following table sets forth a summary of stock options under all plans for the nine months ended September 30, 2012:

|                                      | Total Options | Weighted<br>Average<br>Exercise<br>Price | Weighted<br>Average<br>Remaining<br>Contractual Term<br>(in years) | Aggregate<br>Intrinsic<br>Value (in<br>thousands) |
|--------------------------------------|---------------|--|--|---|
| Outstanding at December 31, 2011     | 6,673,054     | \$ 11.46                                 |  |   |
| Granted                              | 64,667        | 34.57                                    |  |   |
| Exercised                            | (3,503,728)   | 6.94                                     |  |   |
| Forfeited                            | (69,768)      | 19.96                                    |  |   |
| Outstanding at September 30,<br>2012 | 3,164,225     | \$ 16.75                                 | 6.2  | \$ 70,327   |
| Exercisable at September 30, 2012    | 1,121,500     | \$ 10.68                                 | 5.3  | \$ 31,727   |

The Black Scholes model utilizes the following assumptions in determining a fair value: price of underlying stock, award exercise price, expected term, risk-free interest rate, expected dividend yield and expected stock price volatility over the award's expected term. Due to the utilization of these assumptions, the existing models do not necessarily represent the definitive fair value of awards for future periods. As the IPO occurred during the second quarter of 2011, the option term has been estimated by considering both the vesting period, which typically for both plans has been four or five years, and the contractual term, which historically has been either seven or ten years. Prior to the IPO, the fair value of the Class A common stock was estimated based upon the net enterprise value of the Company, discounted to reflect the lack of liquidity and control associated with the stock. Since the consummation of the IPO, the fair value of the Class A common stock has been based upon the closing price of the Class A common stock as reported on the New York Stock Exchange. Volatility is estimated based upon the Company utilizing its current peer group average to estimate the expected volatility.

The assumptions used in the Company's Black Scholes valuation related to stock option grants made during the nine months ended September 30, 2012 were as follows:

|  |           |
|--|-----------|
| Dividend yield                               | 1.1%-1.4% |
| Expected option life                         | 5.0 years |
| Volatility factor percentage of market price | 40.7%     |
| Discount rate                                | 0.6%-0.9% |

The following table sets forth a summary of restricted stock granted under the 2011 Stock Plan and related information for the nine months ended September 30, 2012:

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|                                   | <b>Restricted<br/>Stock</b> |    | <b>Weighted<br/>Average<br/>Fair Value</b> |
|-----------------------------------|-----------------------------|----|--|
| Outstanding at December 31, 2011  | 138,119                     | \$ | 22.35                                      |
| Granted                           | 14,679                      |    | 33.31                                      |
| Vested                            | (1,545)                     |    | 39.06                                      |
| Forfeited                         | (6,882)                     |    | 21.22                                      |
| Outstanding at September 30, 2012 | 144,371                     | \$ | 23.34                                      |

## GNC HOLDINGS, INC. AND SUBSIDIARIES

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

## NOTE 9. SEGMENTS

The Company has three reportable segments, each of which represents an identifiable component of the Company for which separate financial information is available. This information is utilized by management to assess performance and allocate assets accordingly. The Company's management evaluates segment operating results based on several indicators. The primary key performance indicators are sales and operating income or loss for each segment. Operating income or loss, as evaluated by management, excludes certain items that are managed at the consolidated level, such as distribution and warehousing, impairments and other corporate costs. The following table represents key financial information for each of the Company's reportable segments, identifiable by the distinct operations and management of each: Retail, Franchising, and Manufacturing/Wholesale. The Retail reportable segment includes the Company's corporate store operations in the United States, Canada, Puerto Rico and its GNC.com and LuckyVitamin.com businesses. The Franchise reportable segment represents the Company's franchise operations, both domestically and internationally. The Manufacturing/Wholesale reportable segment represents the Company's manufacturing operations in South Carolina and the Wholesale sales business. This segment supplies the Retail and Franchise segments, along with various third parties, with finished products for sale. The Warehousing and Distribution and Corporate costs represent the Company's administrative expenses. The accounting policies of the segments are the same as those described in the Basis of Presentation and Summary of Significant Accounting Policies.

The following table represents key financial information of the Company's segments:

|  | Three months ended September 30, |                   | Nine months ended September 30, |                     |
|--|----------------------------------|-------------------|---------------------------------|---------------------|
|  | 2012                             | 2011              | 2012                            | 2011                |
|  | (unaudited)<br>(in thousands)    |                   |                                 |                     |
| <b>Revenue:</b>                                |                                  |                   |                                 |                     |
| Retail   | \$ 445,008                       | \$ 385,231        | \$ 1,373,460                    | \$ 1,153,237        |
| Franchise                                      | 108,785                          | 90,884            | 313,809                         | 251,096             |
| Manufacturing/Wholesale:                       |                                  |                   |                                 |                     |
| Intersegment (1)                               | 65,813                           | 58,430            | 202,931                         | 166,271             |
| Third Party                                    | 67,814                           | 61,913            | 177,692                         | 158,238             |
| Subtotal Manufacturing/Wholesale               | 133,627                          | 120,343           | 380,623                         | 324,509             |
| Subtotal segment revenues                      | 687,420                          | 596,458           | 2,067,892                       | 1,728,842           |
| Intersegment elimination (1)                   | (65,813)                         | (58,430)          | (202,931)                       | (166,271)           |
| <b>Total revenue</b>                           | <b>\$ 621,607</b>                | <b>\$ 538,028</b> | <b>\$ 1,864,961</b>             | <b>\$ 1,562,571</b> |
| <b>Operating income:</b>                       |                                  |                   |                                 |                     |
| Retail   | \$ 86,257                        | \$ 62,167         | \$ 277,050                      | \$ 189,173          |
| Franchise                                      | 36,319                           | 31,997            | 103,038                         | 83,291              |
| Manufacturing/Wholesale                        | 26,455                           | 23,385            | 73,150                          | 60,982              |
| Unallocated corporate and other costs:         |                                  |                   |                                 |                     |
| Warehousing and distribution costs             | (16,181)                         | (15,190)          | (47,601)                        | (45,577)            |
| Corporate costs                                | (20,749)                         | (19,122)          | (63,720)                        | (61,884)            |
| Transaction related costs                      | (924)                            | (637)             | (1,610)                         | (12,999)            |
| Subtotal unallocated corporate and other costs | (37,854)                         | (34,949)          | (112,931)                       | (120,460)           |
| <b>Total operating income</b>                  | <b>\$ 111,177</b>                | <b>\$ 82,600</b>  | <b>\$ 340,307</b>               | <b>\$ 212,986</b>   |

(1) Intersegment revenues are eliminated from consolidated revenue.



**GNC HOLDINGS, INC. AND SUBSIDIARIES**

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)**

**NOTE 10. INCOME TAXES**

The Company recognized \$114.6 million of income tax expense (or 37.3% of pre-tax income) during the nine months ended September 30, 2012 compared to \$53.9 million (or 36.3% of pre-tax income) for the same period in 2011. For the nine months ended September 30, 2012 and 2011, income tax expense included \$0.6 million (0.2% of pre-tax income) and \$2.3 million (1.5% of pre-tax income), respectively, related to non-deductible costs incurred in connection with the Offerings. Income tax expense during the nine months ended September 30, 2011 was offset by \$2.6 million (or 1.8% of pre-tax income) related to non-recurring tax credits and incentives.

The Company files a consolidated U.S. federal tax return and various consolidated and separate tax returns as prescribed by the tax laws of the state, local and international jurisdictions in which it operates. The Company has been audited by the Internal Revenue Service (the IRS) through its March 16, 2007 tax year and the Company has been informed that its federal income tax return for 2010 will be audited. The Company has various state, local and international jurisdiction tax years open to examination (the earliest open period is 2003), and is also currently under audit in certain state and local jurisdictions. As of September 30, 2012, the Company believes that it has appropriately reserved for any potential federal, state, local and international income tax exposures.

At each of September 30, 2012 and December 31, 2011, the Company had \$11.8 million and \$10.6 million, respectively, of unrecognized tax benefits. As of September 30, 2012, the Company is not aware of any tax positions for which it is reasonably possible that the amounts of unrecognized tax benefits will significantly increase or decrease within the next 12 months. The amount of unrecognized tax benefits that, if recognized, would affect the effective tax rate is approximately \$11.8 million. The Company recognizes accrued interest and penalties related to unrecognized tax benefits in income tax expense. The Company had accrued approximately \$5.5 million and \$3.5 million for September 30, 2012 and December 31, 2011, respectively, in potential interest and penalties associated with uncertain tax positions. To the extent interest and penalties are not assessed with respect to the ultimate settlement of uncertain tax positions, amounts previously accrued will be reduced and reflected as a reduction of the overall income tax provision.

**NOTE 11. RELATED PARTY TRANSACTIONS**

**Management Services Agreement** On March 16, 2007, the Company entered into a Management Services Agreement (the Management Services Agreement) with ACOF Operating Manager II, L.P. (ACOF Operating Manager), an affiliate of Ares Corporate Opportunities Fund II, L.P. (Ares), which was terminated upon the consummation of the IPO. The Management Services Agreement provided for an annual management fee of \$0.8 million, payable quarterly and in advance to ACOF Operating Manager, on a pro rata basis, until the tenth anniversary from March 16, 2007 plus any one-year extensions (which extensions occurred automatically on each anniversary date of March 16, 2007), as well as reimbursements for ACOF Operating Manager's, and its affiliates', out-of-pocket expenses in connection with the management services provided under the Management Services Agreement. During the first quarter of 2011, \$0.2 million was paid to ACOF Operating Manager in accordance with the terms of the Management Services Agreement.

Upon the consummation of the IPO, the Management Services Agreement was terminated and ACOF Operating Manager received, in lieu of quarterly payments of the annual management fee, an automatic fee equal to the net present value of the aggregate annual management fee that would have been payable to ACOF Operating Manager during the remainder of the term of the Management Services Agreement. The amount of such payment was \$5.6 million, and this amount was accrued and expensed in transaction related costs during the period ended March 31, 2011. No further payments will be made pursuant to the Management Services Agreement.

**Special Dividend** Prior to the consummation of the IPO, Ontario Teachers Pension Plan Board ( OTPP ), as the holder of Class B common stock, was entitled to receive ratably an annual special dividend payment equal to an aggregate amount of \$0.8 million per year when, as and if declared by the Board, for a period of ten years commencing on March 16, 2007 (the Special Dividend Period ). The special dividend was payable in equal quarterly installments on the first day of each quarter commencing on April 1, 2007. During the first quarter of 2011, \$0.2 million was paid to OTPP as a special dividend pursuant to the obligations under the Class B common stock.

Upon the consummation of the IPO, OTPP s right to receive the special dividend payments was terminated and OTPP received, in lieu of quarterly payments of the special dividend payments, an automatic payment equal to the net present value of the aggregate amount of the special dividend payments that would have been payable to OTPP during the remainder of the Special Dividend Period, calculated in good faith by the Board. The amount of such payment was \$5.6 million, and this amount was accrued and expensed in transaction related costs during the period ended March 31, 2011. No further special dividend payments will be made.

**GNC HOLDINGS, INC. AND SUBSIDIARIES**

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)**

**Lease Agreements** At September 30, 2012, General Nutrition Centres Company, the Company's wholly owned subsidiary, was party, as lessee, to 16 lease agreements with Cadillac Fairview Corporation ( Cadillac Fairview ), as lessor, and 1 lease agreement with Ontrea, Inc. ( Ontrea ), as lessor, with respect to properties located in Canada. Each of Cadillac Fairview and Ontrea is a direct wholly owned subsidiary of OTPP. For the nine months ended September 30, 2012 and 2011, the Company paid \$1.9 million and \$2.1 million, respectively, under the lease agreements with Cadillac Fairview, and an immaterial amount for the nine months ended September 30, 2012 under the lease agreement with Ontrea. Each lease was negotiated in the ordinary course of business on an arm's length basis.

**Share Repurchase** On August 9, 2012, in conjunction with the August 2012 Offering, the Company entered into an agreement to repurchase six million shares of common stock directly from Ares at a price of \$38.42 per share. The Company funded this repurchase from borrowings under the Incremental Term Loan, together with cash on hand.

**NOTE 12. SUBSEQUENT EVENTS**

On October 29, 2012, the Board authorized and declared a cash dividend for the fourth quarter of 2012 of \$0.11 per share of Class A common stock, payable on or about December 31, 2012 to stockholders of record as of the close of business on December 14, 2012.



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

The following Management's Discussion and Analysis of Financial Condition and Results of Operations should be read in conjunction with Item 1, Financial Statements in Part I of this Quarterly Report on Form 10-Q.

### Forward-Looking Statements

This Quarterly Report on Form 10-Q and any documents incorporated by reference herein or therein include forward-looking statements within the meaning of federal securities laws. Forward-looking statements include statements that may relate to our plans, objectives, goals, strategies, future events, future revenues or performance, capital expenditures, financing needs and other information that is not historical information. Forward-looking statements can often be identified by the use of terminology such as subject to, believe, anticipate, plan, potential, predict, expect, intend, estimate, project, may, will, should, could, can, think, the negatives thereof, variations thereon and similar expressions, or by discussions of strategy.

All forward-looking statements, including, without limitation, our examination of historical operating trends, are based upon our current expectations and various assumptions. We believe there is a reasonable basis for our expectations and beliefs, but they are inherently uncertain. We may not realize our expectations, and our beliefs may not prove correct. Actual results could differ materially from those described or implied by such forward-looking statements. The following uncertainties and factors, among others (including, but not limited to, those we describe under the caption Risk Factors in our filings with the Securities and Exchange Commission pursuant to Sections 13(a), 14 or 15(d) of the Securities Exchange Act of 1934), could affect future performance and cause actual results to differ materially from those matters expressed in or implied by forward-looking statements:

- significant competition in our industry;
- unfavorable publicity or consumer perception of our products;
- increases in the cost of borrowings and limitations on availability of additional debt or equity capital;
- our debt levels and restrictions in our debt agreements;
- incurrence of material product liability and product recall costs;
- loss or retirement of directors or key members of management;
- costs of compliance and our failure to comply with new and existing governmental regulations including, but not limited to, tax regulations;
- costs of litigation and the failure to successfully defend lawsuits and other claims against us;
- failure of our franchisees to conduct their operations profitably and limitations on our ability to terminate or replace under-performing franchisees;
- economic, political and other risks associated with our international operations;
- failure to keep pace with the demands of our customers for new products and services;
- disruptions in our manufacturing system or losses of manufacturing certifications;

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- disruptions in our distribution network;
- lack of long-term experience with human consumption of ingredients in some of our products;
- increases in the frequency and severity of insurance claims, particularly claims for which we are self-insured;
- failure to adequately protect or enforce our intellectual property rights against competitors;
- changes in raw material costs and pricing of our products;

- failure to successfully execute our growth strategy, including any delays in our planned future growth, any inability to expand our franchise operations or attract new franchisees, or any inability to expand our company-owned retail operations;
- changes in applicable laws relating to our franchise operations;
- damage or interruption to our information systems;
- impact of current economic conditions on our business;
- natural disasters, unusually adverse weather conditions, pandemic outbreaks, boycotts and geo-political events; and
- failure to maintain effective internal controls.

Consequently, forward-looking statements should be regarded solely as our current plans, estimates and beliefs. You should not place undue reliance on forward-looking statements. We cannot guarantee future results, events, levels of activity, performance or achievements. We do not undertake and specifically decline any obligation to update, republish or revise forward-looking statements to reflect future events or circumstances or to reflect the occurrences of unanticipated events.

## Business Overview

We are a global specialty retailer of health and wellness products. We derive our revenues principally from product sales through our company-owned stores and online through GNC.com and LuckyVitamin.com, domestic and international franchise activities and sales of products manufactured in our facilities to third parties. We sell products through a worldwide network of more than 7,900 locations operating under the GNC brand name.

In March 2011, General Nutrition Centers, Inc. ( *Centers* ), a wholly owned subsidiary of Holdings, entered into a senior credit facility, consisting of a \$1.2 billion term loan facility (the *Term Loan Facility* ) and an \$80.0 million revolving credit facility (the *Revolving Credit Facility* ) and, together with the Term Loan Facility, the *Senior Credit Facility* ), and utilized the proceeds to repay all outstanding indebtedness under the 2007 Senior Credit Facility, the Senior Notes, and the Senior Subordinated Notes (the *Refinancing* ). Subsequently, we completed two amendments to the Term Loan Facility. On August 1, 2012, we amended the Term Loan Facility to increase the outstanding borrowings by \$200.0 million (the *Incremental Term Loan* ). In October 2012, we amended the Term Loan Facility to adjust the per annum interest rate to the greater of LIBOR and 1.00%, plus an applicable margin of 2.75%. The Refinancing and these amendments are collectively referred to herein as the *Refinancings*.

In April 2011, we consummated an initial public offering (the *IPO* ) of 25.875 million shares of Holdings' Class A common stock, par value \$0.001 per share (the *Class A common stock* ), at an IPO price of \$16.00 per share. The net proceeds from the IPO, together with cash on hand, were used to redeem all outstanding shares of Holdings' Series A preferred stock, par value \$0.001 per share (the *Series A preferred stock* ), repay approximately \$300.0 million of outstanding borrowings under the Term Loan Facility and pay approximately \$11.1 million to satisfy obligations under the Management Services Agreement (as defined in Note 11, *Related Party Transactions* ) and Holdings' Class B common stock, par value \$0.001 per share (the *Class B common stock* ) and, together with the Class A common stock, the *common stock* ). Subsequent to the IPO, certain of Holdings' stockholders completed the following registered offerings of Class A common stock:

- in October 2011, 23.0 million shares at \$24.75 per share;

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- in March 2012, 19.6 million shares at \$33.50 per share; and
- in August 2012, 10.0 million shares at \$38.42 per share.

In conjunction with the August 2012 offering, we repurchased an additional six million shares of Class A common stock from one of our stockholders as part of a share repurchase program. The IPO, the offerings, and the repurchase of the six million shares of Class A common stock are collectively referred to herein as the Offerings.

As of September 30, 2012, we had completed our approved share repurchase programs for a total of \$360.0 million of Class A common stock.

## Executive Overview

In 2012, we have continued to focus on achieving our five principal corporate goals: growing company-owned domestic retail earnings, growing company-owned domestic retail square footage, growing our international footprint, expanding our e-commerce business and further leveraging the GNC brand. These goals are designed to drive both short-term and long-term financial results. Our efforts led to the following results for the three months ended September 30, 2012 compared to the same period in 2011:

- Our company-owned domestic same store sales increased 9.8%, which included a 20.9% increase in our GNC.com business.
- We increased our company-owned domestic store count by 36 net new stores during the third quarter of 2012.
- Our retail segment sales increased 15.5%, and operating income increased 38.8%.
- Total franchising revenue grew 19.7%, and operating income increased 13.5%.
- Domestic franchising revenue grew 9.9%, and we added 2 net new domestic franchise stores during the third quarter of 2012.
- International franchise revenue grew 35.6%, and we added 60 net new international franchise stores during the third quarter of 2012.
- We increased sales in our wholesale/manufacturing segment by 9.5% through our new wholesale distribution channels and increased third-party sales.
- Consistent with our focus on communicating our core "Live Well" theme in both magazine and print, we expanded our marketing campaign to include a "best in class" theme. The campaign's branding images reflect our core customer: youthful, athletic, aspirational and goal oriented.
- We generated 15.5% of total revenue growth which drove a 34.6% increase in total operating income.

## Revenues and Operating Performance from our Segments

We measure our operating performance primarily through revenues and operating income from our three segments, Retail, Franchise and Manufacturing/Wholesale, and through the management of unallocated costs from our warehousing, distribution and corporate segments, as follows:

- *Retail:* Retail revenues are generated by sales to consumers at our company-owned stores and online through our websites GNC.com and LuckyVitamin.com. Although we believe that our retail and franchise businesses are not seasonal in nature, historically we have experienced, and expect to continue to experience, a variation in our net sales and operating results from quarter to quarter. Our industry is expected to grow at an annual average rate of approximately 6.5% through 2020. As a leader in our industry, we expect our organic retail revenue to grow faster than the projected industry growth as a result of our disproportionate market share, scale economies in purchasing and advertising, strong brand awareness and vertical integration.
- *Franchise:* Franchise revenues are generated primarily by:
  - (1) product sales to our franchisees;

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- (2) royalties on franchise retail sales; and
- (3) franchise fees, which we charge for initial franchise awards, renewals and transfers of franchises.

Although we do not anticipate the number of our domestic franchise stores to grow substantially, we expect to achieve domestic franchise store revenue growth consistent with projected industry growth, which we expect to generate from royalties on franchise retail sales and product sales to our existing franchisees. As a result of our efforts to expand our international presence and provisions in our international franchising agreements requiring franchisees to open additional stores, we have increased our international store base in recent periods and expect to continue to increase the number of our international franchise stores over the next five years. We believe this will result in additional franchise fees associated with new store openings and increased revenues from product sales to, and royalties from, new franchisees. As our existing international franchisees continue to

open additional stores, we also anticipate that franchise revenue from international operations will be driven by increased product sales to, and royalties from, our franchisees. Since our international franchisees pay royalties to us in U.S. dollars, any strengthening of the U.S. dollar relative to our franchisees' local currency may offset some of the growth in royalty revenue.

- *Manufacturing/Wholesale:* Manufacturing/Wholesale revenues are generated by sales of manufactured products to third parties, generally for third-party private label brands; the sale of our proprietary and third-party products to and through Rite Aid and www.drugstore.com; and the sale of our proprietary products to and through PetSmart and Sam's Club. We also record license fee revenue from the opening of franchise store-within-a-store locations within Rite Aid stores in this segment. Our revenues generated by our manufacturing and wholesale operations are subject to our available manufacturing capacity.

A significant portion of our business infrastructure is comprised of fixed operating costs. Our vertically integrated distribution network and manufacturing capacity can support higher sales volume without significant incremental costs. We therefore expect our operating expenses to grow at a lesser rate than our revenues, resulting in positive operating leverage.

The following trends and uncertainties in our industry could affect our operating performance as follows:

- broader consumer awareness of health and wellness issues and rising healthcare costs may increase the use of the products we offer and positively affect our operating performance;
- interest in, and demand for, condition-specific products based on scientific research may positively affect our operating performance if we can timely develop and offer such condition-specific products;
- the effects of favorable and unfavorable publicity on consumer demand with respect to the products we offer may have similarly favorable or unfavorable effects on our operating performance;
- a lack of long-term experience with human consumption of ingredients in some of our products could create uncertainties with respect to the health risks, if any, related to the consumption of such ingredients and negatively affect our operating performance;
- increased costs associated with complying with new and existing governmental regulation may negatively affect our operating performance; and
- a decline in disposable income available to consumers may lead to a reduction in consumer spending and negatively affect our operating performance.

## Results of Operations

The following information presented for the three and nine months ended September 30, 2012 and 2011 was prepared by management, is unaudited and was derived from our unaudited consolidated financial statements and accompanying notes. In the opinion of management, all adjustments necessary for a fair statement of our financial position and operating results for such periods and as of such dates have been included.

As discussed in Note 9, Segments, to our unaudited consolidated financial statements, we evaluate segment operating results based on several indicators. The primary key performance indicators are revenues and operating income or loss for each segment.

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Revenues and operating income or loss, as evaluated by management, exclude certain items that are managed at the consolidated level, such as warehousing and transportation costs, impairments and other corporate costs. The following discussion compares the revenues and the operating income or loss by segment, as well as those items excluded from the segment totals.

Same store sales growth reflects the percentage change in same store sales in the period presented compared to the prior year period. Same store sales are calculated on a daily basis for each store and exclude the net sales of a store for any period if the store was not open during the same period of the prior year. We also include internet sales, as generated only through GNC.com and www.drugstore.com, in our domestic retail company-owned domestic same store sales calculation. When a store's square footage has been changed as a result of reconfiguration or relocation in the same mall or shopping center, the store continues to be treated as a same store. If, during the period presented, a store was closed, relocated to a different mall or shopping center, or converted to a franchise store or a company-owned store, sales from that store up to and including the



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closing day or the day immediately preceding the relocation or conversion are included as same store sales as long as the store was open during the same period of the prior year. We exclude from the calculation sales during the period presented that occurred on or after the date of relocation to a different mall or shopping center or the date of a conversion.

**Results of Operations**

(Dollars in millions and percentages expressed as a percentage of total net revenue)

|  | Three Months Ended September 30, |               |                |               | Nine Months Ended September 30, |               |                |               |
|--|----------------------------------|---------------|----------------|---------------|---------------------------------|---------------|----------------|---------------|
|  | 2012                             |               | 2011           |               | 2012                            |               | 2011           |               |
|  | (unaudited)                      |               |                |               |                                 |               |                |               |
| <b>Revenues:</b>   |                                  |               |                |               |                                 |               |                |               |
| Retail   | \$ 445.0                         | 71.6%         | \$ 385.2       | 71.6%         | \$ 1,373.5                      | 73.7%         | \$ 1,153.3     | 73.8%         |
| Franchise  | 108.8                            | 17.5%         | 90.9           | 16.9%         | 313.8                           | 16.8%         | 251.1          | 16.1%         |
| Manufacturing / Wholesale  | 67.8                             | 10.9%         | 61.9           | 11.5%         | 177.7                           | 9.5%          | 158.2          | 10.1%         |
| <b>Total net revenues</b>  | <b>621.6</b>                     | <b>100.0%</b> | <b>538.0</b>   | <b>100.0%</b> | <b>1,865.0</b>                  | <b>100.0%</b> | <b>1,562.6</b> | <b>100.0%</b> |
| <b>Operating expenses:</b>                                       |                                  |               |                |               |                                 |               |                |               |
| Cost of sales, including warehousing, distribution and occupancy | 386.4                            | 62.2%         | 343.1          | 63.8%         | 1,149.6                         | 61.6%         | 992.9          | 63.5%         |
| Compensation and related benefits                                | 78.7                             | 12.7%         | 72.4           | 13.5%         | 237.1                           | 12.7%         | 219.0          | 14.0%         |
| Advertising and promotion  | 15.7                             | 2.5%          | 12.4           | 2.3%          | 45.3                            | 2.4%          | 40.0           | 2.6%          |
| Other selling, general and administrative                        | 26.6                             | 4.3%          | 24.7           | 4.6%          | 84.8                            | 4.6%          | 78.8           | 5.0%          |
| Transaction related costs  | 0.9                              | 0.1%          | 0.6            | 0.1%          | 1.6                             | 0.1%          | 13.0           | 0.9%          |
| Amortization expense   | 2.1                              | 0.3%          | 2.0            | 0.3%          | 6.4                             | 0.3%          | 5.8            | 0.4%          |
| Foreign currency gain (loss)                                     | -                                | 0.0%          | 0.2            | 0.0%          | (0.1)                           | 0.0%          | 0.1            | 0.0%          |
| <b>Total operating expenses</b>                                  | <b>510.4</b>                     | <b>82.1%</b>  | <b>455.4</b>   | <b>84.6%</b>  | <b>1,524.7</b>                  | <b>81.7%</b>  | <b>1,349.6</b> | <b>86.4%</b>  |
| <b>Operating income:</b>   |                                  |               |                |               |                                 |               |                |               |
| Retail   | 86.3                             | 13.9%         | 62.2           | 11.6%         | 277.0                           | 14.9%         | 189.2          | 12.1%         |
| Franchise.   | 36.3                             | 5.8%          | 32.0           | 6.0%          | 103.0                           | 5.5%          | 83.3           | 5.3%          |
| Manufacturing / Wholesale  | 26.5                             | 4.3%          | 23.4           | 4.3%          | 73.2                            | 3.9%          | 61.0           | 3.9%          |
| Unallocated corporate and other costs:                           |                                  |               |                |               |                                 |               |                |               |
| Warehousing and distribution costs                               | (16.2)                           | -2.7%         | (15.2)         | -2.9%         | (47.6)                          | -2.5%         | (45.6)         | -2.9%         |
| Corporate costs  | (20.8)                           | -3.3%         | (19.2)         | -3.5%         | (63.7)                          | -3.4%         | (61.9)         | -4.0%         |
| Transaction related costs  | (0.9)                            | -0.1%         | (0.6)          | -0.1%         | (1.6)                           | -0.1%         | (13.0)         | -0.8%         |
| Subtotal unallocated corporate and other costs, net              | (37.9)                           | -6.1%         | (35.0)         | -6.5%         | (112.9)                         | -6.0%         | (120.5)        | -7.7%         |
| <b>Total operating income</b>                                    | <b>111.2</b>                     | <b>17.9%</b>  | <b>82.6</b>    | <b>15.4%</b>  | <b>340.3</b>                    | <b>18.3%</b>  | <b>213.0</b>   | <b>13.6%</b>  |
| Interest expense, net  | 12.1                             |               | 10.4           |               | 32.9                            |               | 64.5           |               |
| <b>Income before income taxes</b>                                | <b>99.1</b>                      |               | <b>72.2</b>    |               | <b>307.4</b>                    |               | <b>148.5</b>   |               |
| Income tax expense   | 36.9                             |               | 23.5           |               | 114.6                           |               | 53.9           |               |
| <b>Net income</b>  | <b>\$ 62.2</b>                   |               | <b>\$ 48.7</b> |               | <b>\$ 192.8</b>                 |               | <b>\$ 94.6</b> |               |

**Note:** The numbers in the above table have been rounded to millions. All calculations related to the Results of Operations for the year-over-year comparisons were derived from unrounded data and could occasionally differ immaterially if you were to use the table above for these calculations.

**Comparison of the Three Months Ended September 30, 2012 and 2011**

**Revenues**

Our consolidated net revenues increased \$83.6 million, or 15.5%, to \$621.6 million for the three months ended September 30, 2012 compared to \$538.0 million for the same period in 2011. The increase was the result of increased sales in each of our segments.

*Retail.* Revenue in our Retail segment increased \$59.8 million, or 15.5%, to \$445.0 million for the three months ended September 30, 2012 compared to \$385.2 million for the same period in 2011. Domestic retail revenue increased \$41.7 million due to a 9.8% increase in our same store sales and the opening of new stores. The increase in domestic retail revenue was primarily due to sales increases in the sports nutrition, vitamin and diet categories, and also included an increase in sales from GNC.com of \$4.2 million, or 20.9%, to \$24.2 million for the three months ended September 30, 2012, compared to \$20.0 million for the same period in 2011. Sales from LuckyVitamin.com, acquired on August 31, 2011, contributed \$9.9 million to the increase in revenue. Our

company-owned store base increased by 159 domestic stores to 2,986 at September 30, 2012 compared to 2,827 at September 30, 2011, due to new store openings and franchise store acquisitions. Our Canadian store base decreased by four stores to 165 at September 30, 2012 compared to 169 at September 30, 2011.

*Franchise.* Revenues in our Franchise segment increased \$17.9 million, or 19.7%, to \$108.8 million for the three months ended September 30, 2012 compared to \$90.9 million for the same period in 2011. Domestic franchise revenue increased \$5.5 million primarily due to increases in product sales and royalty income. Our domestic franchisees' same store retail sales increased by 14.3% for the three months ended September 30, 2012 compared to the same period in 2011. There were 935 domestic franchise stores at September 30, 2012 compared to 919 stores at September 30, 2011. International franchise revenue, including China operations, increased \$12.4 million, primarily due to increases in product sales and royalty income. Our international franchise store base increased by 162 stores to 1,711 at September 30, 2012 compared to 1,549 at September 30, 2011.

*Manufacturing/Wholesale.* Revenues in our Manufacturing/Wholesale segment, which includes third party sales from our manufacturing facilities in South Carolina, as well as wholesale sales to Rite Aid, www.drugstore.com, Sam's Club and PetSmart increased \$5.9 million, or 9.5%, to \$67.8 million for the three months ended September 30, 2012 compared to \$61.9 million for the same period in 2011. For the three months ended September 30, 2012, third party contract manufacturing sales from our South Carolina manufacturing plant increased by \$1.2 million, or 3.7%, compared to the same period in 2011. In addition, there was an increase of wholesale revenue due to timing of purchase orders and shipments with key wholesale customers.

#### **Cost of Sales**

Cost of sales, which includes product costs, costs of warehousing and distribution and occupancy costs, increased \$43.4 million, or 12.6%, to \$386.4 million for the three months ended September 30, 2012 compared to \$343.1 million for the same period in 2011. The increase was primarily due to higher sales volumes and store counts. Cost of sales, as a percentage of net revenue, was 62.2% and 63.8% for the three months ended September 30, 2012 and 2011, respectively.

#### **Selling, General and Administrative ( SG&A ) Expenses**

SG&A expenses, including compensation and related benefits, advertising and promotion expense, other SG&A expenses and amortization expense increased \$11.9 million, or 10.7%, to \$124.0 million for the three months ended September 30, 2012 compared to \$112.1 million for the same period in 2011. These expenses, as a percentage of net revenue, were 20.0% for the three months ended September 30, 2012 compared to 20.9% for the three months ended September 30, 2011.

*Compensation and related benefits.* Compensation and related benefits increased \$6.3 million, or 8.7%, to \$78.7 million for the three months ended September 30, 2012 compared to \$72.4 million for the same period in 2011. The increase was primarily due to support for our increased store base and sales volume and payroll tax expense related to the exercise of stock options.

*Advertising and promotion.* Advertising and promotion expenses were \$15.7 million and \$12.4 million for the three months ended September 30, 2012 and 2011, respectively. The increase in advertising expense resulted primarily from an increase in events and promotions.

*Other SG&A.* Other SG&A expenses, including amortization expense, increased \$2.0 million, or 7.5%, to \$28.7 million for the three months ended September 30, 2012 compared to \$26.7 million for the same period in 2011. This increase was due to increased sales in each of our segments.

*Transaction related costs.* For the three months ended September 30, 2012 and 2011, we incurred \$0.9 million and \$0.6 million, respectively, of expenses related to the Offerings and the Refinancings.

### ***Operating Income***

As a result of the foregoing, consolidated operating income increased \$28.6 million, or 34.6%, to \$111.2 million for the three months ended September 30, 2012 compared to \$82.6 million for the same period in 2011. Operating income, as a percentage of net revenue, was 17.9% and 15.4% for the three months ended September 30, 2012 and 2011, respectively.

*Retail.* Operating income increased \$24.1 million, or 38.8%, to \$86.3 million for the three months ended September 30, 2012 compared to \$62.2 million for the same period in 2011. The increase was driven by higher gross margin and expense leverage on the same store sales increase in occupancy and payroll.

*Franchise.* Operating income increased \$4.3 million, or 13.5%, to \$36.3 million for the three months ended September 30, 2012 compared to \$32.0 million for the same period in 2011. The increase was due to higher gross product margin on wholesale sales and franchise royalty income.

*Manufacturing/Wholesale.* Operating income increased \$3.1 million, or 13.1%, to \$26.5 million for the three months ended September 30, 2012 compared to \$23.4 million for the same period in 2011. The increase was driven by a higher gross product margin resulting from improved wholesale margins and increased shipments of proprietary products.

*Warehousing and distribution costs.* Unallocated warehousing and distribution costs increased \$1.0 million, or 6.5%, to \$16.2 million for the three months ended September 30, 2012 compared to \$15.2 million for the three months ended September 30, 2011. The increase was primarily due to higher fuel costs and increased wages to support higher sales volume.

*Corporate costs.* Corporate overhead costs increased \$1.6 million, or 8.3%, to \$20.8 million for the three months ended September 30, 2012 compared to \$19.2 million for the same period in 2011. This increase was due to increases in compensation expenses and health insurance costs.

*Transaction related costs.* For the three months ended September 30, 2012 and 2011, we incurred \$0.9 million and \$0.6 million, respectively, of expenses related to the Offerings and the Refinancings.

### ***Interest Expense***

Interest expense increased \$1.7 million, or 15.9%, to \$12.1 million for the three months ended September 30, 2012 compared to \$10.4 million for the same period in 2011. This increase was primarily due to the borrowings under the \$200.0 million Incremental Term Loan.

### ***Income Tax Expense***

We recognized \$36.9 million of income tax expense (or 37.2% of pre-tax income) during the three months ended September 30, 2012 compared to \$23.5 million (or 32.6% of pre-tax income) for the same period in 2011. For the three months ended September 30, 2011, income tax expense includes \$2.6 million (or 3.0% of pre-tax income) related to non-recurring tax credits and incentives.

**Net Income**

As a result of the foregoing, consolidated net income increased \$13.5 million to \$62.2 million for the three months ended September 30, 2012 compared to \$48.7 million for the same period in 2011. For the three months ended September 30, 2012 and 2011, net income includes \$0.9 million and \$0.4 million, respectively, of transaction related costs, net of tax effect, related to the Offerings and the Refinancings. For the three months ended September 30, 2012, net income excluding these related costs increased \$14.0 million, or 28.7%, to \$63.1 million, from \$49.1 million for the same period in 2011.

**Comparison of the Nine Months Ended September 30, 2012 and 2011**

**Revenues**

Our consolidated net revenues increased \$302.4 million, or 19.4%, to \$1,865.0 million for the nine months ended September 30, 2012 compared to \$1,562.6 million for the same period in 2011. The increase was the result of increased sales in each of our segments.

*Retail.* Revenue in our Retail segment increased \$220.2 million, or 19.1%, to \$1,373.5 million for the nine months ended September 30, 2012 compared to \$1,153.3 million for the same period in 2011. Domestic retail revenue increased \$157.2 million due to a 12.8% increase in our same store sales and the opening of new stores. The increase in domestic retail revenue was primarily due to sales increases in the sports nutrition, vitamin and diet categories, and also included an increase in sales from GNC.com of \$16.5 million, or 27.7%, to \$76.1 million for the nine months ended September 30, 2012 compared to \$59.6 million for the same period in 2011. Sales from LuckyVitamin.com, acquired on August 31, 2011, contributed \$38.5 million to the increase in revenue. Our company-owned store base increased by 159 domestic stores to 2,986 at September 30, 2012 compared to 2,827 at September 30, 2011, due to new store openings and franchise store acquisitions. Our Canadian store base decreased by four stores to 165 at September 30, 2012 compared to 169 at September 30, 2011.

*Franchise.* Revenues in our Franchise segment increased \$62.7 million, or 25.0%, to \$313.8 million for the nine months ended September 30, 2012 compared to \$251.1 million for the same period in 2011. Domestic franchise revenue increased \$29.1 million primarily due to increases in product sales and royalty income. Our domestic franchisees' same store retail sales increased by 16.1% for the nine months ended September 30, 2012 compared to the same period in 2011. There were 935 domestic franchise stores at September 30, 2012 compared to 919 stores at September 30, 2011. International franchise revenue, including China operations, increased \$33.6 million, primarily due to increases in product sales and royalty income. Our international franchise store base increased by 162 stores to 1,711 at September 30, 2012 compared to 1,549 at September 30, 2011.

*Manufacturing/Wholesale.* Revenues in our Manufacturing/Wholesale segment, which includes third-party sales from our manufacturing facilities in South Carolina, as well as wholesale sales to Rite Aid, www.drugstore.com, Sam's Club and PetSmart increased \$19.5 million, or 12.3%, to \$177.7 million for the nine months ended September 30, 2012 compared to \$158.2 million for the same period in 2011. For the nine months ended September 30, 2012, third party contract manufacturing sales from our South Carolina manufacturing plant increased by \$11.9 million, or 14.1%, compared to the same period in 2011.

### **Cost of Sales**

Cost of sales, which includes product costs, costs of warehousing and distribution and occupancy costs, increased \$156.7 million, or 15.8%, to \$1,149.6 million for the nine months ended September 30, 2012 compared to \$992.9 million for the same period in 2011. The increase was primarily due to higher sales volumes and store counts. Cost of sales, as a percentage of net revenue, was 61.6% and 63.5% for the nine months ended September 30, 2012 and 2011, respectively.

### **Selling, General and Administrative ( SG&A ) Expenses**

SG&A expenses, including compensation and related benefits, advertising and promotion expense, other SG&A expenses, amortization expense and transaction related costs increased \$18.6 million, or 5.2%, to \$375.2 million, for the nine months ended September 30, 2012 compared to \$356.6 million for the same period in 2011. These expenses, as a percentage of net revenue, were 20.1% for the nine months ended September 30, 2012 compared to 22.8% for the nine months ended September 30, 2011.

*Compensation and related benefits.* Compensation and related benefits increased \$18.1 million, or 8.3%, to \$237.1 million for the nine months ended September 30, 2012 compared to \$219.0 million for the same period in 2011. The increase was due primarily to support our increased store base and sales volume and payroll tax expense related to the exercise of stock options. The nine months ended September 30, 2011 included \$3.5 million of executive severance.

*Advertising and promotion.* Advertising and promotion expenses increased \$5.3 million, or 13.2%, to \$45.3 million for the nine months ended September 30, 2012 compared to \$40.0 million during the same period in 2011. Advertising expense increased primarily as a result of an increase in media expense, events and promotions.

*Other SG&A.* Other SG&A expenses, including amortization expense, increased \$6.6 million, or 7.7%, to \$91.2 million for the nine months ended September 30, 2012 compared to \$84.6 million for the same period in 2011. This increase was due to increased sales in each of our segments.

*Transaction related costs.* For the nine months ended September 30, 2012 and 2011, we incurred \$1.6 million and \$13.0 million, respectively, of expenses related to the Offerings and the Refinancings. The \$13.0 million of expense for the nine months ended September 30, 2011 primarily consisted of a payment of \$11.1 million for the termination of sponsor-related obligations and other costs of \$1.9 million.

***Operating Income***

As a result of the foregoing, consolidated operating income increased \$127.3 million, or 59.8%, to \$340.3 million for the nine months ended September 30, 2012 compared to \$213.0 million for the same period in 2011. Operating income, as a percentage of net revenue, was 18.3% and 13.6% for the nine months ended September 30, 2012 and 2011, respectively. Excluding transaction related expenses and executive severance, operating income was \$341.9 million and \$229.8 million for the nine months ended September 30, 2012 and 2011, respectively.



*Retail.* Operating income increased \$87.8 million, or 46.5%, to \$277.0 million for the nine months ended September 30, 2012 compared to \$189.2 million for the same period in 2011. The increase was driven by expense leverage on the same store sales increase in occupancy, payroll and marketing.

*Franchise.* Operating income increased \$19.7 million, or 23.7%, to \$103.0 million for the nine months ended September 30, 2012 compared to \$83.3 million for the same period in 2011. The increase was due to higher gross product margin on wholesale sales and franchise royalty income.

*Manufacturing/Wholesale.* Operating income increased \$12.2 million, or 20.0%, to \$73.2 million for the nine months ended September 30, 2012 compared to \$61.0 million for the same period in 2011. The increase was driven by a higher gross product margin rate resulting from improved wholesale margins and increased shipments of proprietary products.

*Warehousing and distribution costs.* Unallocated warehousing and distribution costs increased \$2.0 million, or 4.4%, to \$47.6 million for the nine months ended September 30, 2012 compared to \$45.6 million for the nine months ended September 30, 2011. The increase was primarily due to higher fuel costs and increased wages to support higher sales volume.

*Corporate costs.* Corporate overhead costs increased \$1.8 million, or 2.8%, to \$63.7 million for the nine months ended September 30, 2012 compared to \$61.9 million for the same period in 2011. This increase was due to increases in compensation expenses and health insurance costs.

*Transaction related costs.* For the nine months ended September 30, 2012 and 2011, we incurred \$1.6 million and \$13.0 million, respectively, of expenses related to the Offerings and the Refinancings. The \$13.0 million of expense for the nine months ended September 30, 2011 primarily consisted of a payment of \$11.1 million for the termination of sponsor-related obligations and other costs of \$1.9 million.

### ***Interest Expense***

Interest expense decreased \$31.6 million, or 48.9%, to \$32.9 million for the nine months ended September 30, 2012 compared to \$64.5 million for the same period in 2011. This decrease was primarily due to \$23.2 million of expenses related to the Refinancing, which consisted of: \$5.8 million in interest rate swap termination costs, \$13.4 million of deferred financing fees related to former indebtedness, \$1.6 million in original issue discount related to former indebtedness, and \$2.4 million to defease the former Senior Notes and Senior Toggle Notes. Additionally, \$4.9 million of original issue discount and deferred financing fees were expensed related to the \$300.0 million repayment of outstanding borrowings under the Term Loan Facility in connection with the IPO.

### ***Income Tax Expense***

We recognized \$114.6 million of income tax expense (or 37.2% of pre-tax income) during the nine months ended September 30, 2012 compared to \$53.9 million (or 36.3% of pre-tax income) for the same period in 2011. The 2012 and 2011 income tax expense

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includes \$0.6 million (0.2% of pre-tax income) and \$2.3 million (or 1.5% of pre-tax income), respectively, related to non-deductible costs incurred relating to the transaction related costs. Also, the nine months ended September 30, 2011 was offset by \$2.6 million (or 1.8% of pre-tax income) related to non-recurring tax credits and incentives.

### ***Net Income***

As a result of the foregoing, consolidated net income increased \$98.2 million to \$192.8 million for the nine months ended September 30, 2012 compared to \$94.6 million for the same period in 2011. Net income for the nine months ended September 30, 2012 includes \$1.6 million related to the Offerings and the Refinancings. For the nine months ended September 30, 2011, net income includes \$30.7 million of transaction related costs and executive severance, net of tax effect. For the nine months ended September 30, 2012, net income excluding such transaction related costs, net of tax effect, increased \$69.1 million, or 55.2%, to \$194.4 million from \$125.3 million for the same period in 2011.

### **Liquidity and Capital Resources**

At September 30, 2012, we had \$96.8 million in cash and cash equivalents and \$530.4 million in working capital, compared with \$128.4 million in cash and cash equivalents and \$474.5 million in working capital at December 31, 2011. The \$55.9 million increase in our working capital was primarily driven by an increase in our receivables and inventory levels due to an increase in volume, and a decrease in accounts payable due to timing of payments.

We expect to fund our operations through internally generated cash and, if necessary, from borrowings under the Revolving Credit Facility. At September 30, 2012, we had \$78.8 million available under the Revolving Credit Facility, after giving effect to \$1.2 million utilized to secure letters of credit.

We expect our primary uses of cash in the near future will be for capital expenditures, working capital requirements and funding any quarterly dividends to stockholders that are approved by the Board.

On June 19, 2012, the Board authorized a share repurchase program pursuant to which we repurchased \$300.0 million shares of Class A common stock, which was completed during the third quarter of 2012.

On October 29, 2012, the Board authorized and declared a cash dividend for the fourth quarter of 2012 of \$0.11 per share of Class A common stock, payable on or about December 31, 2012 to stockholders of record as of the close of business on December 14, 2012.

We currently anticipate that cash generated from operations, together with amounts available under the Revolving Credit Facility, will be sufficient for the term of the Revolving Credit Facility, which matures on March 15, 2016, to meet our operating expenses and fund capital expenditures. Under the Incremental Term Loan, we are required to make quarterly payments of \$0.5 million, payable every quarter beginning September 30, 2012 and ending on December 31, 2017. Our ability to make scheduled payments of principal on, to pay interest on or to refinance our debt and to satisfy our other debt obligations will depend on our future operating performance, which will be affected by general economic, financial and other factors beyond our control. We are currently in compliance with our debt covenant reporting and compliance obligations under the 2011 Senior Credit Facility.

#### ***Cash Provided by Operating Activities***

Cash provided by operating activities was \$142.0 million and \$146.4 million for the nine months ended September 30, 2012 and 2011, respectively. The decrease was due primarily to an increase in inventory as a result of increases in finished goods to support increased sales, timing of accounts payable and an increase in accounts receivable due to higher sales volumes offset by an increase in net income of \$98.2 million.

#### ***Cash Used in Investing Activities***

We used cash for investing activities of \$31.8 million and \$50.2 million for the nine months ended September 30, 2012 and 2011, respectively. Capital expenditures, which were primarily for new stores, improvements to our company-owned stores and our South Carolina manufacturing facility and corporate information systems, were \$29.9 million and \$27.8 million for the nine months ended September 30, 2012 and 2011, respectively. Also, during the nine months ended September 30, 2011, we used approximately \$21.0 million for the purchase of LuckyVitamin.com.

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Our capital expenditures typically consist of new stores, certain periodic updates in our company-owned stores and ongoing upgrades and improvements to our manufacturing facilities and information technology systems.

We expect capital expenditures to be approximately \$45 million in 2012, which includes costs associated with growing our domestic square footage. We anticipate funding our 2012 capital requirements with cash flows from operations and, if necessary, borrowings under the Revolving Credit Facility.

### ***Cash Used in Financing Activities***

For the nine months ended September 30, 2012, cash used in financing activities was \$141.3 million, primarily consisting of dividends paid to Holdings' stockholders of \$34.3 million and the repurchase of an aggregate of \$360.0 million shares of Class A common stock under repurchase programs, offset by \$59.4 million of proceeds from exercised stock options, including the associated tax benefit, and \$199.0 million of proceeds from the issuance of long-term debt.

For the nine months ended September 30, 2011, we borrowed \$1,196.2 million under the Senior Credit Facility, and utilized a portion of the funds to repay \$644.4 million under the 2007 Senior Credit Facility, \$300.0 million for the redemption of the Senior Notes, and \$110.0 million for the redemption of the Senior Subordinated

Notes. We received net proceeds from the IPO of \$237.3 million and used these proceeds, together with cash on hand, to redeem all of the outstanding Series A preferred stock and repay \$300.0 million of the Senior Credit Facility. Additionally, we paid \$17.4 million in fees associated with the Refinancing.

### **Contractual Obligations**

There are no material changes in our contractual obligations as disclosed in our Annual Report on Form 10-K for the year ended December 31, 2011.

### **Off Balance Sheet Arrangements**

As of September 30, 2012, we had no relationships with unconsolidated entities or financial partnerships, such as entities often referred to as structured finance or special purpose entities, which would have been established for the purpose of facilitating off balance sheet arrangements, or other contractually narrow or limited purposes. We are, therefore, not materially exposed to any financing, liquidity, market or credit risk that could arise if we had engaged in such relationships.

### **Critical Accounting Estimates**

Our significant accounting policies are described in the notes to our unaudited consolidated financial statements under Note 2, Basis of Presentation and Summary of Significant Accounting Policies . There have been no material changes to the application of critical accounting policies and significant judgments and estimates since those disclosed in our Annual Report on Form 10-K for the year ended December 31, 2011.

### **Recent Accounting Pronouncements**

In June 2011, the FASB issued updated guidance on current comprehensive income presentation, which eliminates the option to present the components of other comprehensive income as part of the statement of stockholders' equity. Instead, we must report comprehensive income in either a single continuous statement of comprehensive income that contains two sections, net income and other comprehensive income, or in two separate but consecutive statements. This new guidance is effective for us for fiscal years beginning after December 15, 2011, with early adoption permitted. We adopted this guidance during the first quarter of 2012. The adoption of this guidance had no material impact on our financial statements, as it only required a change in the format of presentation.

In May 2011, the FASB issued changes to conform existing guidance regarding fair value measurement and disclosure between accounting principles generally accepted in the United States ( GAAP ) and International Financial Reporting Standards. These changes both clarify the FASB's intent about the application of existing fair value measurement and disclosure requirements and amend certain principles or requirements for measuring fair value or for disclosing information about fair value measurements. The

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clarifying changes relate to the application of the highest and best use and valuation premise concepts, measuring the fair value of an instrument classified in a reporting entity's stockholders' equity, and disclosure of quantitative information about unobservable inputs used for Level 3 fair value measurements. The amendments relate to measuring the fair value of financial instruments that are managed within a portfolio; application of premiums and discounts in a fair value measurement; and additional disclosures concerning the valuation processes used and sensitivity of the fair value measurement to changes in unobservable inputs for those items categorized as Level 3, a reporting entity's use of a nonfinancial asset in a way that differs from the asset's highest and best use, and the categorization by level in the fair value hierarchy for items required to be measured at fair value for disclosure purposes only. We adopted this guidance during the first quarter of 2012, and it had no material impact on our financial statements.

In July 2012, the FASB issued an accounting standard that simplifies the impairment test for indefinite-lived intangible assets other than goodwill. The new guidance gives the option to first assess qualitative factors to determine if it is more likely than not that the fair value of an indefinite-lived intangible asset is less than its carrying amount as a basis for determining whether it is necessary to perform a quantitative valuation test. The new standard is effective for fiscal years, and interim periods within those fiscal years, beginning on or after September 15, 2012. We will adopt this accounting standard in the fourth quarter of 2012 and we do not anticipate that this adoption will have a significant impact on our financial statements.

### **Item 3. Quantitative and Qualitative Disclosures about Market Risk**

Market risk represents the risk of changes in the value of market risk sensitive instruments caused by fluctuations in interest rates, foreign exchange rates and commodity prices. Changes in these factors could cause fluctuations in the results of our operations and cash flows. In the ordinary course of business, we are primarily exposed to foreign currency and interest rate risks. We do not use derivative financial instruments in connection with these commodity market risks.

#### ***Foreign Currency Exchange Rate Market Risk***

We are subject to the risk of foreign currency exchange rate changes in the conversion from local currencies to the U.S. dollar of the reported financial position and operating results of our non-U.S. based subsidiaries. We are also subject to foreign currency exchange rate changes for purchases of goods and services that are denominated in currencies other than the U.S. dollar. The primary currencies to which we are exposed to fluctuations are the Canadian Dollar and the Chinese Renminbi. The fair value of our net foreign investments and our foreign denominated payables would not be materially affected by a 10% adverse change in foreign currency exchange rates for the nine months ended September 30, 2012 and 2011.

#### ***Interest Rate Market Risk***

All of Centers' long-term debt is subject to changing interest rates. Although changes in interest rates do not impact our operating income, the changes could affect the fair value of such debt and related interest payments. Based on our variable rate debt balance as of September 30, 2012, a 1% change in interest rates would have no material impact on interest expense due to an interest rate floor that exists on the Senior Credit Facility.

### **Item 4. Controls and Procedures**

#### **Evaluation of Disclosure Controls and Procedures**

Our management, with the participation of our Chief Executive Officer ( CEO ) and Chief Financial Officer ( CFO ), has evaluated the effectiveness of our disclosure controls and procedures (as such term is defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934, as amended (the Exchange Act )) as of the end of the period covered by this report. Disclosure controls and procedures are designed to provide reasonable assurance that the information required to be disclosed in the reports that we file or submit under the Exchange Act has been appropriately recorded, processed, summarized and reported on a timely basis and are effective in ensuring that such information is accumulated and communicated to our management, including our CEO and CFO, as appropriate to allow timely decisions regarding required disclosure. Based on such evaluation, our CEO and CFO have concluded that, as of September 30, 2012, our disclosure controls and procedures are effective at the reasonable assurance level.

**Changes in Internal Control Over Financial Reporting**

There have not been any changes in our internal controls over financial reporting that occurred during the last fiscal quarter, which have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.



## Part II - OTHER INFORMATION

### Item 1. Legal Proceedings

We are engaged in various legal actions, claims and proceedings resulting from our business activities arising in the normal course of business, including claims related to breach of contracts, products liabilities, intellectual property matters and employment-related matters. As with most actions such as these, an estimation of any possible and/or ultimate liability cannot always be determined. We continue to assess the requirement to account for additional contingencies in accordance with the standard on contingencies. If we are required to make a payment in connection with an adverse outcome in these matters, it could have a material impact on our business, financial condition, operating results and cash flows.

As a manufacturer and retailer of health and wellness products and other consumer products that are ingested by consumers or applied to their bodies, we have been and are currently subjected to various product liability claims. Although the effects of these claims to date have not been material to us, it is possible that current and future product liability claims could have a material adverse impact on our business, financial condition, operating results or cash flows. We currently maintain product liability insurance with a deductible/retention of \$3.0 million per claim with an aggregate cap on retained loss of \$10.0 million. We typically seek and have obtained contractual indemnification from most parties that supply raw materials for our products or that manufacture or market products we sell. We also typically seek to be added, and have been added, as an additional insured under most of such parties' insurance policies. We are 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 by the creditworthiness of the indemnifying party and its insurer, and the absence of significant defenses by the insurers.

*Hydroxycut Claims.* On May 1, 2009, the Food and Drug Administration ( FDA ) issued a warning on several Hydroxycut-branded products manufactured by lovate. The FDA warning was based on 23 reports of liver injuries from consumers who claimed to have used the products between 2002 and 2009. As a result, lovate voluntarily recalled 14 Hydroxycut-branded products. Following the recall, we were named, among other defendants, in approximately 94 lawsuits related to Hydroxycut-branded products in 14 states. lovate previously accepted our tender request for defense and indemnification under its purchasing agreement with us and, as such, lovate has accepted our request for defense and indemnification in the Hydroxycut matters. Our ability to obtain full recovery under the indemnity is dependent on lovate's insurance coverage, the creditworthiness of its insurer, and the absence of significant defenses by such insurer. To the extent we are not fully compensated by lovate's insurer, we can seek recovery directly from lovate. Our ability to fully recover such amounts may be limited by the creditworthiness of lovate.

During 2012, we were named in nine new personal injury lawsuits related to Hydroxycut, generally inclusive of claims of consumer fraud, misrepresentation, strict liability and breach of warranty. None of the plaintiffs in these lawsuits asserted specific damages claims. Any liabilities that may arise from these matters are not probable or reasonably estimable at this time.

The following nine personal injury matters were filed during 2012 by individuals claiming injuries from the use and consumption of Hydroxycut-branded products:

- Michael Nunes, et al. v. General Nutrition Centers, Inc., et al., U.S. District Court, Southern District of California, 12CV00915 (filed April 13, 2012);

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- Mark Aguilar, et al. v. General Nutrition Centers, Inc., et al., U.S. District Court, Eastern District of California, 12CV00513 (filed April 13, 2012);
- Clarissa Birdshead, et al. v. General Nutrition Centers, Inc., et al., U.S. District Court, Southern District of California, 12CV00913 (filed April 13, 2012);
- Deloris Blaylock, et al. v. General Nutrition Centers, Inc., et al., U.S. District Court, Eastern District of California, 12CV00988 (filed April 13, 2012);
- Gerard Dure, et al. v. General Nutrition Centers, Inc., et al., U.S. District Court, Eastern District of California, 12CV00987 (filed April 13, 2012);
- Mark Flemings, et al. v. General Nutrition Centers, Inc., et al., U.S. District Court, Eastern District of California, 12CV00982 (filed April 13, 2012);
- Darryl Ingram, et al. v. General Nutrition Centers, Inc., et al., U.S. District Court, Eastern District of California, 12CV00983 (filed April 13, 2012);

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- Darrell Jones, et al. v. General Nutrition Centers, Inc., et al., U.S. District Court, Western District of Oklahoma, 12CV00408 (filed April 13, 2012); and
- Jerry Ruiz v. General Nutrition Corporation, et al., Supreme Court of the State of New York, Nassau County, Index Number 601940/2012 (filed September 26, 2012).

The following ten personal injury matters related to the use and consumption of Hydroxycut-branded products were settled during 2012:

- Kerry and Nadia Donald v. Iovate Health Sciences Group, et al., Court of Common Pleas, Philadelphia County 11-0502384 (filed January 22, 2010);
- Phillip Sims v. GNC Corporation, et al., U.S. District Court, District of New Jersey, 10CV1728 (filed April 5, 2010);
- Donna Natali v. GNC Corporation, et al., Superior Court of New Jersey, Atlantic County, ATL-L-001499-10 (filed April 5, 2010);
- Matthew Carhart v. GNC Corporation, et al., Court of Common Pleas Philadelphia County, 10-0402210 (filed April 15, 2010);
- Michael Brown v. GNC Corporation, et al., Court of Common Pleas Philadelphia County, 10-0402217 (filed April 15, 2010);
- Alan D. Alessio, Jr. v. GNC Corporation, et al., Court of Common Pleas Philadelphia County, 10-0402214 (filed April 15, 2010);
- Carla M. Benson v. GNC Corporation, et al., Court of Common Pleas Philadelphia County, 10-1104602 (filed December 3, 2010);
- Alexander Torres and Jessica Lee Pizarro v. GNC Corporation, et al., Court of Common Pleas Philadelphia County, 11-0403330 (filed May 2, 2011);

- Victor Rendon and Edward Soto v. General Nutrition Centers, Inc., et al. Orange County Superior Court, Case No. 30-2010-00365988-CU-PL-CXC (filed April 23, 2010); and
- Miguel Rivera, et al. v. General Nutrition Centers, Inc., et al. Orange County Superior Court, Case No. 30-2010-00411926-CU-PL-CXC (filed September 27, 2010).

These settlements did not result in any material payment by us.

#### **Item 1A. Risk Factors**

There have been no material changes to the disclosures relating to this item from those set forth in our Annual Report on Form 10-K for the year ended December 31, 2011 except with respect to the risk factor below, which is amended and restated in its entirety as follows:

***We may experience product recalls, which could reduce our sales and margin and adversely affect our results of operations.***

We may be subject to product recalls, withdrawals or seizures if any of the products we formulate, manufacture or sell are believed to cause injury or illness or if we are alleged to have violated governmental regulations in the manufacturing, labeling, promotion, sale or distribution of such products. For example, in May 2009, the FDA warned consumers to stop using Hydroxycut diet products, which are produced by lovate and were sold in our stores. lovate issued a voluntary recall, with which we fully complied. Sales of the recalled Hydroxycut products amounted to approximately \$57.8 million, or 4.7% of our retail sales in 2008, and \$18.8 million, or 4.2% of our retail sales in the first four months of 2009. We provided refunds or gift cards to consumers who returned these products to our stores. In the second quarter of 2009, we experienced a reduction in sales and margin due to this recall as a result of accepting returns of products from customers and a loss of sales as a replacement product was not available. Through December 31, 2011, we estimate that we have refunded approximately \$3.5 million to our retail customers and approximately \$1.6 million to our wholesale customers for Hydroxycut product returns. Our results of operations may continue to be affected by the Hydroxycut recall. Any additional recall, withdrawal or seizure of any of the products we formulate, manufacture or sell would require significant management attention, would likely result in substantial and unexpected expenditures and could

materially and adversely affect our business, financial condition or results of operations. Furthermore, a recall, withdrawal or seizure of any of our products could materially and adversely affect consumer confidence in our brands and decrease demand for our products and the market price of the Class A common stock.

As is common in our industry, we rely on our third-party vendors to ensure that the products they manufacture and sell to us comply with all applicable regulatory and legislative requirements. In general, we seek representations and warranties, indemnification and/or insurance from our vendors. However, even with adequate insurance and indemnification, any claims of non-compliance could significantly damage our reputation and consumer confidence in our products, and materially and adversely affect the market price of the Class A common stock. In addition, the failure of such products to comply with applicable regulatory and legislative requirements could prevent us from marketing the products or require us to recall or remove such products from the market, which in certain cases could materially and adversely affect our business, financial condition and results of operation. For example, products manufactured by third parties that contain derivatives from geranium, known as 1,3-dimethylpentylamine/dimethylamylamine/13-dimethylamylamine ( DMAA ) are popular with our consumers. Although we have received representations from our third-party vendors that these products comply with applicable regulatory and legislative requirements, recent media articles have suggested that DMAA may not comply with the Dietary Supplement Health and Education Act of 1994. In December 2011, the U.S. military asked us to temporarily remove products containing DMAA from our stores on its bases pending the outcome of a precautionary review. That review is still pending. On April 27, 2012, the FDA announced that it had issued warning letters to ten manufacturers and distributors of dietary supplements containing DMAA for allegedly marketing products for which evidence of the safety of the product had not been submitted to FDA. The FDA also indicated that the warning letters advised the companies that the FDA is not aware of evidence or history of use to indicate that DMAA is safe. We expect that the companies will oppose the FDA position. If it is determined that DMAA does not comply with applicable regulatory and legislative requirements, we could be required to recall or remove from the market all products containing DMAA and we could become subject to lawsuits related to any alleged non-compliance, any of which recalls, removals or lawsuits could materially and adversely affect our business, financial condition and results of operations. In the past, due to frequently changing consumer preferences in the dietary supplement space, we have offset losses related to recalls and removals with reformulated or alternative products, which is the strategy we would seek to employ if we were required to remove or recall products containing DMAA; however, there can be no assurance that we would be able to offset all or any portion of losses related to any future removal or recall. As a result of the indeterminable level of product substitution and reformulated product sales, we cannot reliably determine the potential impact of any such recall or removal on our business, financial condition or results of operation.

***Our operations are subject to environmental and health and safety laws and regulations that may increase our cost of operations or expose us to environmental liabilities.***

Our operations are subject to environmental and health and safety laws and regulations, and some of our operations require environmental permits and controls to prevent and limit pollution of the environment. We could incur significant costs as a result of violations of, or liabilities under, environmental laws and regulations, or to maintain compliance with such environmental laws, regulations or permit requirements. For example, in March 2008, the DHEC requested that we investigate contamination associated with historical activities at one of our South Carolina facilities. These investigations have identified chlorinated solvent impacts in soils and groundwater that extend offsite from our facility. We entered into a Voluntary Cleanup Contract with the DHEC regarding the matter on September 24, 2012. Pursuant to such contract, we have submitted a plan for additional investigations to the DHEC and are awaiting the DHEC's approval of the plan. After we complete the investigations to understand the extent of the chlorinated solvent impacts, we will develop appropriate remedial measures for DHEC approval. At this stage of the investigation, however, it is not possible to estimate the timing and extent of any remedial action that may be required, the ultimate cost of remediation, or the amount of our potential liability.

In addition to the foregoing, we are subject to numerous federal, state, local and foreign environmental and health and safety laws and regulations governing our operations, including the handling, transportation and disposal of our 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 us to incur additional capital and operating expenditures to maintain compliance with environmental laws and regulations and environmental permits. We also are 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 our ability to sell or lease our properties, or to use them as collateral for financing.

**Item 2. Unregistered Sales of Equity Securities and Use of Proceeds****Issuer Purchases of Equity Securities**

The following table sets forth information regarding Holdings purchases of shares of Class A common stock during the quarter ended September 30, 2012:

|                                      | <b>Total Number of<br/>Shares Purchased (1)</b> | <b>Average<br/>Price Paid<br/>per Share</b> | <b>Total Number of<br/>Shares Purchased as<br/>Part of Publicly<br/>Announced Plans</b> | <b>Maximum Number (or<br/>Approximate Dollar<br/>Value) of Shares that<br/>May Yet Be Purchased<br/>under the Plans or<br/>Programs</b> |
|--------------------------------------|---|---|---|---|
| July 1 to July 31, 2012              | 653,690   | \$39.00                                     | 653,690   | \$274,503,732   |
| August 1 to August 31,<br>2012.      | 7,158,206                                       | \$38.35                                     | 7,158,206   | -   |
| September 1 to<br>September 30, 2012 | -   | -   | -   | -   |
| <b>Total</b>                         | <b>7,811,896</b>                                | <b>\$38.40</b>                              | <b>7,811,896</b>  |   |

(1) On June 19, 2012, we announced the approval of a share repurchase program pursuant to which we were authorized to purchase up to an aggregate of \$300.0 million shares of Class A common stock during the twelve month period ending July 31, 2013 (the Repurchase Program). We concluded the Repurchase Program in August 2012. Other than purchases in connection with the Repurchase Program as set forth in the table above, we made no purchases of shares of Class A common stock for the quarter ended September 30, 2012.

**Item 3. Defaults Upon Senior Securities**

None.

**Item 4. Mine Safety Disclosures**

Item 4 is not applicable.

**Item 5. Other Information**

None.

**Item 6. Exhibits**

| <u>Exhibit No.</u> | <u>Description</u>   |
|--------------------|--|
| 3.1                | Fifth Amended and Restated Bylaws of Holdings, as currently in effect. (Incorporated by reference to Exhibit 10.1 to Holdings Current Report on Form 8-K (File No. 001-35113)), filed October 23, 2012.) |
| 10.1               | Form of Restricted Stock Unit Award Agreement. (Incorporated by reference to Exhibit 10.1 to Holdings Current Report on Form 8-K (File No. 001-35113)), filed October 23, 2012.)                         |
| 31.1               | Certification of Principal Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.  |
| 31.2               | Certification of Principal Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.  |
| 32.1               | Certification of CEO and CFO Pursuant to 18 U.S.C. Section 1350, as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.   |
| 101.INS            | XBRL Instance Document   |
| 101.SCH            | XBRL Taxonomy Extension Schema   |
| 101.CAL            | XBRL Taxonomy Extension Calculation Linkbase   |
| 101.LAB            | XBRL Taxonomy Extension Label Linkbase   |
| 101.PRE            | XBRL Taxonomy Extension Presentation Linkbase  |
| 101.DEF            | XBRL Taxonomy Extension Definition Linkbase  |



**SIGNATURES**

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

GNC HOLDINGS, INC.  
(Registrant)

Date: November 1, 2012

/s/ Joseph M. Fortunato  
Joseph M. Fortunato  
President and Chief Executive Officer  
(Principal Executive Officer)

Date: November 1, 2012

/s/ Michael M. Nuzzo  
Michael M. Nuzzo  
Chief Financial Officer  
(Principal Financial Officer)

Date: November 1, 2012

/s/ Andrew S. Drexler  
Andrew S. Drexler  
Corporate Controller  
(Principal Accounting Officer)