

USANA HEALTH SCIENCES INC  
Form 10-K  
March 01, 2016

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

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**FORM 10-K**

(Mark One)

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

For the fiscal year ended January 2, 2016

OR

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

For the transition period from \_\_\_\_\_ to \_\_\_\_\_  
Commission file number: 001-35024

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**USANA HEALTH SCIENCES, INC.**

(Exact name of registrant as specified in its charter)

Utah (State or other jurisdiction of incorporation or organization) 87-0500306 (I.R.S. Employer Identification No.)  
3838 West Parkway Blvd., Salt Lake City, Utah 84120 (Address of principal executive offices, Zip Code)

(801) 954-7100 (Registrant's telephone number, including area code)

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

(Title of each class)	(Name of each exchange on which registered)
Common Stock, Par Value \$0.001 Per Share	New York Stock Exchange

**Securities registered pursuant to Section 12(g) of the Act:**  
None

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

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

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Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes  No

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

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

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

Large accelerated filer

Accelerated filer

Non-accelerated filer

Smaller reporting company

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

The aggregate market value of common stock held by non-affiliates of the registrant as of July 2, 2015 was approximately \$832,428,673, based on a closing market price of \$141.74 per share.

There were 11,944,164 shares of the registrant's common stock outstanding as of February 26, 2016.

**Documents incorporated by reference.** The registrant incorporates information required by Part III (Items 10, 11, 12, 13, and 14) of this report by reference to the registrant's definitive proxy statement to be filed pursuant to Regulation 14A for its 2016 Annual Shareholders Meeting.

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*The statements contained in this report on Form 10-K that are not purely historical are considered to be "forward-looking statements" within the meaning of the Private Securities Litigation Reform Act of 1995 and Section 21E of the Securities Exchange Act of 1934, as amended (the "Exchange Act"). These forward-looking statements include, but are not limited to: any projections of net sales, earnings, or other financial items; any statements of the strategies, plans and objectives of management for future operations; any statements concerning proposed new products or developments; any statements regarding future economic conditions or performance; any statements of belief; and any statements of assumptions underlying any of the foregoing. Forward-looking statements may include the words "may," "will," "estimate," "intend," "continue," "believe," "expect" or "anticipate" and any other similar words. These statements represent our expectations, beliefs, anticipations, commitments, intentions, and strategies regarding the future and include, but are not limited to, the risks and uncertainties outlined in Item 1A Risk Factors and Item 7 Management's Discussion and Analysis of Financial Condition and Results of Operations. Readers are cautioned that actual results could differ materially from the anticipated results or other expectations that are expressed in forward-looking statements within this report. The forward-looking statements included in this report speak only as of the date hereof, and we undertake no obligation to publicly update or revise any forward-looking statement, whether as a result of new information, future events or otherwise, except as required by law.*

*In this Annual Report on Form 10-K, unless otherwise expressly indicated, references to "dollars" and "\$" are to United States dollars.*

**PART I**

**Item 1. Business**

**General**

USANA Health Sciences, Inc., a Utah corporation, was founded in 1992 by Myron W. Wentz, Ph.D. We develop and manufacture high-quality, science-based nutritional and personal care products with a primary focus on promoting long-term health and reducing the risk of chronic degenerative disease. In so doing, we are committed to continuous product innovation and sound scientific research. We have operations in 20 markets worldwide, where we distribute and sell our products by way of direct selling. We have chosen this distribution method as we believe it is the most conducive to meeting our vision as a company, which is improving the overall health and nutrition of individuals and families around the world. Our net sales in fiscal year 2015 were \$918.5 million, of which 84.8% were in markets outside of the United States. As a U.S.-based multi-national company with an expanding international presence, our operating results are sensitive to currency fluctuations, as well as economic and political conditions in markets throughout the world. Additionally, we are subject to the various laws and regulations in the United States, China, and the other markets in which we operate with respect to the products that we sell and to our method of distribution.

Our customer base comprises two types of customers: "Associates" and "Preferred Customers." Associates share in our company vision by acting as independent distributors of our products in addition to purchasing our products for their personal use. Preferred Customers purchase our products strictly for personal use and are not permitted to resell or to distribute the products. As of January 2, 2016, we had 421,000 active Associates and 89,000 active Preferred Customers worldwide.

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**Current Focus and Recent Developments**

We have implemented the following strategies and initiatives to increase the number of Associates and Preferred Customers who use our products throughout the world and, thereby, further our company vision:

*Personalization:* Over the last few years, we have focused heavily on personalizing and improving our customers' experience with USANA.

In August 2015, we introduced our new "MySmart™Foods" line of products, which continues our philosophy and strategy of personalization. MySmart™Foods are science-based, healthy nutrition shakes, bars, boosters and flavor optimizers. We made MySmart™Foods available to our Associates for a limited time at our 2015 International Convention only, as a pre-launch opportunity to purchase and try the products. We intend to officially launch MySmart™Foods during the first half of 2016.

We will continue to personalize each of our product lines going forward. In this regard, we have new product and technology launches planned for 2016 and 2017, which we believe will create a new foundation of personalization for USANA to build on as we go forward.

In 2014, we launched an all-new digital marketing suite for our world-wide Associates, which is designed to personalize and simplify conducting a USANA business. This suite provides our Associates with new tools, consisting of a back office hub, personal websites, and advanced communication and marketing tools, all of which enhance our Associates' ability to personalize, manage, promote and build their business in today's demanding e-business environment.

In 2013, we implemented several strategic changes to our business (referred to throughout this report as the "2013 strategic changes"), which were all aimed at promoting customer loyalty, enjoyment and success with USANA. These changes included: (i) simplification of our pricing structure, which included an overall 10% price reduction, while maintaining a price discount on products ordered through our monthly Auto Order program (collectively "price discounts"), (ii) a new reward based on the amount of a customer's initial product order to then be credited on their subsequent two Auto Orders, and (iii) increased payout under and simplification of our Compensation Plan.

We have experienced growth in several business indicators tied to the strategic changes that we implemented in 2013 and continued promoting in 2014 and 2015. These indicators include: active customer counts; world-wide unit volume; percent of sales processed through our Auto Order program; and the number of Associates earning a commission check.

*Market-Specific Strategies:* We have implemented market-specific strategies to facilitate growth and strengthen our business around the world.

In 2015, we continued our strategy to increase our brand-recognition to make it easier for our Associates to introduce USANA to customers. In this regard, we expanded our relationship with Dr. Mehmet Oz and became a Trusted Partner and Sponsor of *The Dr. Oz Show*. Under this partnership, USANA products are regularly featured on *The Dr. Oz Show*. This partnership has helped drive growth in North America and our other regions around the world by increasing awareness and recognition of the USANA brand. Each episode of *The Dr. Oz Show* that features a USANA product is translated into the predominant language of a particular USANA market and made available to Associates in that market via YouTube and other social media outlets for use in promoting the USANA brand. Additionally, viewers of *The Dr. Oz Show* are able to purchase USANA products via a direct link on *The Dr. Oz Show* website. We plan on continuing this partnership in 2016.

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In late 2014, after we passed the anniversary of the 2013 strategic changes, we began offering short-term incentives and promotions for our Associates around the world to generate excitement and additional customer growth. One particular incentive that we offered in late 2014 and early 2015 increased compensation to Associates for sales generated by new Associates and accelerated our sales and customer growth during the fourth quarter of 2014 and the first half of 2015. We plan to continue offering market-specific incentives and promotions going forward to generate excitement in our business.

In 2013, we implemented a price reduction in several of our mature markets to make our products and business opportunity more equitable around the world. Although these price reductions initially had an impact on our net sales on a year-over-year basis, they have been successful in the past helping grow our active customer counts and net sales in these markets, where growth had been declining or flat for several years. We followed this pricing initiative with a new worldwide policy to prohibit cross-border purchasing by our customers. We believe that it is in the best interest of the Company and of our customers to have customers purchase products that are approved and offered in their home market. While this policy had a short-term negative impact on net sales in 2013, these policies have strengthened our underlying business and have improved our opportunity for growth going forward.

*Product Innovation and Information Technology:* Although we originally planned for significant increases in our investment in product and technology innovation to further our Company vision during 2015, much of this investment was delayed as we carefully acquired the necessary human resources. In 2016, we plan to continue to pursue these investment strategies as well as additional investments in our information technology systems and infrastructure to continue to improve our customers' experience with us and to prepare to become a much larger company. These investments will be reflected as both additional SG&A expense and capital expenditures.

*International Development:* Given the significant opportunity that exists in China, we plan to continue focusing significant time and resources on growing this market. Our efforts in this regard include finalizing our new state-of-the-art manufacturing and production facility in Beijing, which we anticipate will become operational during the first half of 2016. We continue to believe that significant growth opportunities exist in new international markets. During the fourth quarter of 2015 we commenced operations in Indonesia. Indonesia is our 20th market and we believe it offers a promising growth opportunity for us.

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**Products**

The following table summarizes our product lines.

<b>Product Line/Category</b>	<b>Description</b>	<b>Percent of Product Sales by Fiscal Year</b>	<b>Product examples</b>
USANA® Nutritionals Essentials	Includes core vitamin and mineral supplements that provide a foundation of advanced total body nutrition for every age group beginning with children 13 months of age.	2013 26%	USANA® Essentials HealthPak 100
		2014 24%	
		2015 22%	
Optimizers	Consists of targeted supplements designed to meet individual health and nutritional needs. These products support needs such as cardiovascular health, skeletal/structural health, and digestive health and are intended to be used in conjunction with the Essentials.	2013 54%	Proflavanol CoQuinone® 30 BiOmega-3
		2014 55%	
		2015 59%	
Foods	Includes low-glycemic meal replacement shakes, snack bars, and other related products that provide optimal macro-nutrition (complex carbohydrates, complete proteins, and beneficial fats) in great tasting and convenient formats. These products can be used along with Essentials and Optimizers to provide a complete and healthy diet and sustained energy throughout the day.	2013 12%	Nutrimeal Fibergy RESET weight-management program and accompanying RESET kit
		2014 13%	
		2015 11%	
Sensé beautiful science®	Includes premium, science-based, personal care products that support healthy skin and hair by providing advanced topical nourishment, moisturization, and protection. These products are designed to complement inner nutrition for the skin provided by the USANA Nutritionals and are manufactured with our patented, self-preserving technology, which uses a unique blend of botanicals, antioxidants, and active ingredients to keep products fresh, without adding traditional chemical preservatives.	2013 6%	Daytime Protective Emulsion Night Renewal Perfecting Essence
		2014 7%	
		2015 7%	
All Other	Includes materials and online tools that are designed to assist our Associates in building their businesses and in marketing our products.	2013 2%	Associate Starter Kit Product Brochures
		2014 1%	
		2015 1%	

In addition to the products described above, we offer products designed specifically for prenatal, infant, and young-child age groups in China. As we continue to increase our focus on personalization and innovation, we will look for innovative product opportunities such as our MyHealthPak product, which is a fully customized, supplement regimen that can include any of our Essentials and Optimizers.

The approximate percentage of total product sales represented by our top-selling products for the last three fiscal years is as follows:

<b>Key Product</b>	<b>Year Ended</b>		
	<b>2013</b>	<b>2014</b>	<b>2015</b>
USANA® Essentials	17%	16%	14%
Proflavanol®	13%	13%	13%
BiOmega-3	8%	10%	12%

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Other top-selling products include our HealthPak 100 and CoQuinone ® 30.

**Geographic Presence**

Our products are distributed and sold in 20 markets. We have organized our markets into two geographic regions: (i) Asia Pacific, which includes three sub-regions, and (ii) Americas and Europe, as noted below.

*Asia Pacific*

Asia Pacific is organized into three sub-regions: Greater China, Southeast Asia Pacific, and North Asia. Markets included in each of these sub-regions are as follows:

Greater China Hong Kong, Taiwan, and China<sup>(1)</sup>

Southeast Asia Pacific Australia, New Zealand, Singapore, Malaysia, the Philippines, Thailand and Indonesia<sup>(2)</sup>

North Asia Japan and South Korea

Asia Pacific has driven our growth the last several years. Our most recent market expansions in this region include our entry into Indonesia in late 2015, Thailand in 2012 and our entry into China in 2010 through our acquisition of BabyCare. Historically, our growth in this region was led by Hong Kong and the Philippines. Since our acquisition of BabyCare, however, our strategy in Asia Pacific has been centered on generating growth in China. Consequently, our growth in Asia Pacific over the last few years has been led by China, and our results in Hong Kong have declined. Our Hong Kong market has now reached our projected size, in terms of customers and sales, and we anticipate modest organic growth for this market going forward. We also anticipate that China and the Philippines will continue to drive our growth in this region going forward, but expect our business to grow in most of our other markets in this region.

*Americas and Europe*

Americas and Europe is our most mature region. Our most recent market expansions in this region include our entry into Colombia in 2013 and France and Belgium in 2012. Americas and Europe has grown modestly over the last several years due to sales and customer growth in Canada and Mexico. Our results in the United States and our newest markets in this region, however, have not paralleled our success in Canada and Mexico. We remain optimistic about our potential to generate growth in the United States and our newest markets and are confident in the growth strategies we have in place. We also anticipate that our growth in Canada and Mexico will continue in 2016.

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(1) Our business in China is that of BabyCare Holdings, Ltd. ("BabyCare"), our wholly-owned subsidiary.

(2) We commenced operations in Indonesia in the fourth quarter of 2015.

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The following table shows net sales by geographic region for our last three fiscal years. We report net sales in a geographic region if a product shipment originates in that geographic region. Additional financial information relating to our geographic regions can be found in Note K to the Consolidated Financial Statements included in this report.

	2013		2014		2015	
	(in thousands)					
<b>Asia Pacific</b>						
Greater China	\$ 271,812	37.9%	\$ 326,134	41.3%	\$ 441,284	48.0%
Southeast Asia Pacific	155,362	21.6%	177,940	22.5%	183,828	20.0%
North Asia	29,319	4.1%	32,667	4.1%	39,751	4.4%
<b>Asia Pacific Total</b>	<b>456,493</b>	<b>63.6%</b>	<b>536,741</b>	<b>67.9%</b>	<b>664,863</b>	<b>72.4%</b>
Americas and Europe	261,682	36.4%	253,730	32.1%	253,636	27.6%
	\$ 718,175	100.0%	\$ 790,471	100.0%	\$ 918,499	100.0%

**Research and Development**

Our research and development efforts are focused on developing and providing high-quality, science-based products that promote long-term health and reduce the risk of chronic degenerative disease. Our research and development activities include developing products that are new to USANA and new to the industry, updating existing USANA brand formulas to keep them current with the latest science, and adapting existing formulas to meet ever-changing regulations in new and existing international markets. In addition, we have an active clinical studies program in place to verify the efficacy of our existing products and our new formulations. Our scientific staff includes experts on human nutrition, cellular biology, biochemistry, natural product chemistry, and clinical research. These experts continually review the latest published research on nutrition, attend scientific conferences, and work with a number of third-party research institutions and researchers to identify possible new products and opportunities and also to reformulate our existing products.

Our in-house research team is working closely with scientists at a number of universities and top research institutes, including the University of Washington, the University of Texas, the University of Colorado Health Sciences Center in Denver, Utah State University, the Linus Pauling Institute at Oregon State University, The Foods for Health Institute at The University of California, Davis, McGill University, in Montreal, Canada, and The Orthopedic Specialty Hospital ("TOSH"), in Salt Lake City, Utah, to maintain our leadership in clinical research in nutrition, oxidative stress, glycemc stress, chronic inflammation and health implications of the microbiome.

We follow pharmaceutical standards established by the U.S. Pharmacopeia and other pharmacopeias in the development and formulation of our products. Our ingredients are selected to meet a number of criteria, including, but not limited to: safety, potency, purity, stability, bio-availability, and efficacy. We control the quality of our products beginning at the formulation stage, and we maintain our quality control through controlled sourcing of raw ingredients, manufacturing, packaging, and labeling. In fiscal years 2013, 2014, and 2015, we expended \$5.1 million, \$5.1 million, and \$6.4 million, respectively, on product research and development activities. Going forward, we expect to increase our spending and resources for research and development in connection with our personalization and product innovation strategies.

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**Manufacturing and Quality Assurance**

We conduct nearly all of the manufacturing, production and quality control operations for our nutritional and personal care products in-house. We have established and maintain a manufacturing and quality control facility in Salt Lake City, Utah. BabyCare manufactures and produces nearly all of its products in-house and maintains manufacturing and quality control facilities in Beijing, China and Tianjin, China. Additional information about our manufacturing, production and quality control operations is set out below.

*Tablet Manufacturing*

Our tablet production process uses automatic and semi-automatic equipment and includes the following activities: auditing and qualifying suppliers of raw materials, acquiring raw materials, analyzing raw material quality, weighing or otherwise measuring raw materials, mixing raw materials into batches, forming mixtures into tablets, coating and sorting the tablets, analyzing tablet quality, packaging finished products, and analyzing finished product quality. We conduct sample testing of raw materials, in-process materials, and finished products for purity, potency, and composition to determine whether our products conform to our internal specifications, and we maintain complete documentation for each of these tests. We employ a qualified staff of professionals to develop, implement and maintain a quality system designed to assure that our products are manufactured to our internal and applicable regulatory agency specifications.

Our Salt Lake City manufacturing facility is registered with the U.S. Food and Drug Administration ("FDA"), Health Canada Natural Health Products Directorate, the Australian Therapeutic Goods Administration ("TGA"), and other governmental agencies, as required. This facility is audited regularly by various organizations and government agencies to assess, among other things, compliance with current Good Manufacturing Practices ("GMPs") and with labeling claims. Additionally, our Salt Lake City manufacturing facility is also certified, through inspection and audits, with the Islamic Foods and Nutrition Counsel of America in compliance with Halal, NSF International in compliance with product testing and GMPs, and the TGA in compliance with the current Therapeutic Goods Act in Australia.

The manufacture of nutritional or dietary supplements and related products in the United States requires compliance with dietary supplement GMPs, which are based on the food-model GMPs and pharmaceutical GMPs, with additional requirements that are specific to dietary supplements. We are audited by the FDA, specifically for dietary supplements, and have been found in full compliance with GMPs for dietary supplements.

*Personal Care Manufacturing*

The production process for personal care products includes identifying and evaluating suppliers of raw materials, acquiring raw materials, analyzing raw material quality, weighing or otherwise measuring the raw materials, mixing raw materials into batches, analyzing liquid batch quality, packaging finished products, and analyzing finished product quality. We conduct sample testing of raw materials, in-process materials, and finished products for purity, potency, and composition to determine whether our products conform to our internal specifications, and we maintain complete documentation for each of these tests.

At our Salt Lake City facility, we have standard technology for producing batches of personal care items, and we have semi-automatic packaging equipment for packaging end products. We employ qualified staff to develop, implement, and maintain a quality system. Although the FDA has not promulgated GMPs for personal care items, it has issued guidelines for manufacturing personal care products. We voluntarily maintain compliance with the guidance established by the FDA and the Personal Care Products Council.

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*Third-Party Suppliers and Manufacturers*

We contract with third-party suppliers and manufacturers for the production of some of our products, which account for approximately 24% of our product sales. These third-party suppliers and manufacturers produce and, in most cases, package these products according to formulations that have been developed by or in conjunction with our in-house product development team. These products include most of our gelatin-capsulated supplements, Rev3 Energy Drink, Probiotic, our powdered drink mixes, nutrition bars, and certain of our personal care products. In particular, we have entered into a strategic relationship with a third-party manufacturer of our nutrition bars. Under this relationship we have extended credit to this supplier in the form of a secured loan to allow the supplier to acquire the necessary equipment to manufacture our bars. This relationship improves our supply chain stability and creates a mutually beneficial relationship between both parties. Products manufactured by third-party suppliers at their locations must also pass through quality control and assurance procedures to ensure they are manufactured in conformance with our specifications. We require products manufactured at these facilities to be shipped to USANA, where a quality inspection and release also takes place.

*Quality Control/Assurance*

We have microbiology and analytical chemistry labs in which we conduct quality control processes. In our microbiology laboratory, scientists test for biological contamination of raw materials and finished goods. In our analytical chemistry laboratory, scientists test for chemical contamination and accurate levels of active ingredients in both raw materials and finished products. Both laboratories conduct stability tests on finished products to determine the shelf life of our products. Our Salt Lake City laboratory staff also performs chemical assays on vitamin and mineral constituents, using U.S. Pharmacopoeia methods and other internally validated methods. In addition to our quality control and clinical laboratories, our headquarters and China facilities also house a laboratory designated for research and development.

*Raw Materials*

Most of the raw ingredients that are used in the manufacture of our products are available from a number of suppliers. We have not generally experienced difficulty in obtaining necessary quantities of raw ingredients. When supplies of certain raw materials have tightened, we have been able to find alternative sources of raw materials, and believe we will be able to do so in the future, if the need arises. Our raw material suppliers must demonstrate stringent process and quality control before we use their products in our manufacturing process.

**Distribution and Marketing**

*General*

We distribute our products internationally through a network marketing system, which is a form of person-to-person direct selling. Under this system, distributors purchase products at wholesale prices from the manufacturer for resale to consumers and for personal consumption. The concept of network marketing is based on the strength of personal recommendations that frequently come from friends, neighbors, relatives, and close acquaintances. We believe that network marketing is an effective way to distribute our products because it allows person-to-person product education and testimonials, as well as higher levels of customer service, all of which are not as readily available through other distribution channels.

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*Structure of Network Marketing Program*

*Associates.* A person who wishes to sell USANA products must join our independent sales force as an Associate. A person becomes an Associate by completing an application under the sponsorship of an existing Associate. The new Associate then becomes part of the sponsoring Associate's sales organization. New Associates sign a written contract and agree to adhere to the USANA policies and procedures. Under the policies and procedures, Associates may not, among other things: (i) use deceptive or unlawful practices to sell USANA products; (ii) make deceptive or unlawful claims or representations concerning our products or Compensation Plan; or (iii) sell competitive products to other USANA Associates or solicit USANA Associates to participate in other network marketing opportunities. New Associates are required to purchase a starter kit that includes a detailed manual describing our business and products, as well as our policies and procedures. We sell these kits at a nominal cost averaging \$30 in each of our markets. No other investment is required to become an Associate.

Once a person becomes an Associate, she or he may purchase products directly from us at wholesale prices for personal use and resale to customers. Our Associates are also entitled to build sales organizations by attracting and enrolling new Associates and establishing a network of product users. Associates are not required to recruit or sponsor new Associates and we do not compensate Associates for sponsoring or recruiting Associates. The sponsoring of new Associates results in the creation of multiple levels within our network marketing structure. Sponsored Associates are referred to as part of the sales organization of the sponsoring Associate. New Associates may also sponsor new Associates, creating additional levels in their network, but also forming a part of the same sales organization as the original sponsoring Associate. As outlined below, Associates who are interested in earning additional income must successfully sell USANA products and establish a business network in order to qualify for commissions, including bonuses. Subject to payment of a minimal annual account renewal fee, Associates may continue to distribute or consume our products as long as they adhere to our policies and procedures.

Individuals who reside in China and who are interested in being part of USANA's organization in China may do so by joining BabyCare as an Associate. The process for joining BabyCare is very similar to the process for joining USANA and requires an initial Associate application and an agreement by the Associate to adhere to the policies and procedures in China. Much like our operations in other markets, an Associate in China is provided with opportunities to build a sales organization and receive compensation for sales generated by that organization. Associates in China are compensated under a compensation plan created and implemented by BabyCare specifically for China.

*Preferred Customers.* We also sell directly to customers who purchase products only for personal use. This program is our "Preferred Customer" program. Preferred Customers may not resell or distribute our products. We believe this program gives us access to a market that would otherwise be missed, by targeting customers who enjoy USANA products, but who prefer not to maintain a distribution relationship with us. Although our policies prohibit Preferred Customers from engaging in retail sales of products, they may enroll as Associates at any time, if they desire. Preferred Customers are not eligible to earn commissions or to participate in our Compensation Plan. Our China operations also utilize a Preferred Customer program, which is based on USANA's Preferred Customer program in our other markets with modifications that we have made specifically for our China market.

*Associate Training and Motivation*

Initial training of Associates about the products, the Compensation Plan, network marketing, and USANA is provided primarily by an Associate's sponsor and others in their sales organization. We develop and sell training materials and sales tools to assist Associates in building their businesses, as well as provide reprints from other commercial publications that feature USANA and may be used as

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sales tools. We also sponsor and conduct regional, national, and international Associate events, as well as intensive leadership training seminars. Attendance at these sessions is voluntary, and we undertake no generalized effort to provide individualized training to Associates, although experience shows that the most effective and successful Associates participate in training activities. Although we provide leadership training and sales tools, we ultimately rely on our Associates to sell our products, attract new Associates and Preferred Customers to purchase our products, and to educate and train new Associates regarding our products and Compensation Plan.

*Associate Compensation*

As outlined below, our Compensation Plan provides several opportunities for Associates to earn compensation, provided they are willing to consistently work at building, training, and retaining their sales organizations to sell USANA products to consumers. The purpose behind each form of compensation under our Compensation Plan is to reward Associates for generating product sales either directly or indirectly through their sales organization and network of product consumers. We believe our Compensation Plan is distinctive for its weekly payouts to Associates.

Associates can earn compensation in four ways:

*Commissions.* The primary way an Associate is compensated is through earning commissions. Associates earn commissions through generating sales volume points, which are a measure of the product sales of their sales organization. Each of our products has an assigned sales volume point value comprised of a certain percent of the product price in U.S. dollars. To be eligible to earn commissions, an Associate must sell a certain amount of product each month ("Qualifying Sales"). Qualifying Sales may include products that the Associates either use personally or that they resell to consumers. Associates do not earn commissions on these Qualifying Sales. Associates may earn commissions on their sale of products above the Qualifying Sales as well as the sale of products by Associates in their organization and to Preferred Customers. Additionally, Associates do not earn commissions for simply recruiting and enrolling others in their organization. Commissions are paid only on the sale of products. We pay Associate commissions on a weekly basis. As noted elsewhere in this report, our China operations maintain their own compensation plan, which has been implemented by BabyCare specifically for China.

*Bonuses.* We offer Associates several bonus opportunities, including our leadership bonus, elite bonus, and lifetime matching bonus. These bonus opportunities are based on a pay-for-performance philosophy and, therefore, are paid out when the Associate achieves the required performance measures.

*Retail Mark-Ups.* As discussed previously, in markets where retail mark-ups are permitted, our Associates purchase products from us at the Preferred Price and may resell them to consumers at higher retail prices. In this case, the Associate retains the retail mark-up as another form of compensation.

*Contests and Promotions.* We periodically sponsor contests and promotions designed to incentivize Associates to generate sales, grow their sales organization, and increase the number of product users. These promotions are also based on a pay-for-performance philosophy and, therefore, are only paid upon the achievement of the promotion objectives.

We endeavor to integrate our Compensation Plan seamlessly across all markets where legally permissible, allowing Associates to receive commissions for global not merely local product sales. This seamless sales organization structure is designed to allow Associates to build a global network by establishing or expanding their sales organization in any of the markets where we operate. We believe

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our Compensation Plan significantly enhances our ability to expand internationally, and we intend to continue to integrate new markets, where permitted, into our Compensation Plan.

**Operating Strengths**

Our principal objective is to improve the overall health and nutrition of individuals and families around the world. We do this through (i) developing and manufacturing high-quality, science-based nutritional and personal care products that promote long-term health, and (ii) providing a rewarding opportunity through network marketing for our Associates who distribute our products. Our strategy is to capitalize on our operating strengths, which include: a strong research and development program; in-house manufacturing capability; science-based products; an attractive Associate Compensation Plan; a scalable business model; and an experienced management team.

*Emphasis on Research and Development.* We have a technical team of experienced scientists, including several holding Ph.D. degrees, quality engineers, and regulatory specialists who contribute to our research and development activities. In our research and development laboratories, our scientists and researchers:

Investigate activities of natural extracts and formulated products in laboratory and clinical settings;

Identify and research combinations of nutrients that may be candidates for new products;

Develop new nutritional ingredients for use in supplements;

Study the metabolic activities of existing and newly identified nutritional ingredients;

Enhance existing USANA brand products, as new discoveries in nutrition and skin care are made;

Formulate products to meet diverse regulatory requirements across all of our markets; and

Investigate processes for improving the production of our formulated products.

Our scientists and researchers also conduct double-blind, placebo-controlled, clinical studies, which are intended to further evaluate the efficacy of our products. In addition, we work with outside research organizations to further support various aspects of our research and development efforts. Our in-house research team is working closely with scientists at a number of universities and top research institutes, including those listed under the caption "Research and Development" above, to maintain our leadership in clinical research in nutrition, oxidative stress, glycemic stress, chronic inflammation and health implications of the micro-biome. We have also funded clinical research programs at Boston University, the University of Colorado, the University of Utah, the University of Sydney in Australia, TOSH, and Utah State University. Our R&D team also works closely with the Medical staff at Sanoviv Medical Institute in Rosarito, Mexico to obtain additional perspectives on the use of supplements in a clinical setting and to get feedback on formulas in development. Additionally, our Scientific Advisory Council, comprised of health care professionals and nutritional science experts worldwide, provides us with valuable insights into product applications and efficacy. It is through our internal research and development efforts, as well as our relationships with outside research organizations and health care providers, that we can provide what we believe to be some of the highest quality health products in the industry.

*In-house Manufacturing.* We manufacture products that account for approximately 76% of our product sales. We believe that our ability to manufacture our own products in-house is a significant competitive advantage for the following reasons:

We can better control the quality of raw materials and finished products;

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We can more reliably monitor the manufacturing process to better guarantee potency and bioavailability and to reduce the risk of product contamination;

We can better control production schedules to increase the likelihood of maintaining an uninterrupted supply of products for our customers;

We are able to produce most of our own prototypes in the research phase of product development; and

We are better able to manage the underlying costs associated with manufacturing our products.

*Science-based Products.* As a result of our emphasis on research and development and our in-house manufacturing capabilities, we have developed a line of high-quality health products that we believe provides health benefits to our customers. Our products have been developed based on a combination of published research, in-house laboratory and third-party clinical studies, and sponsored research.

*Attractive Associate Compensation Plan and Support.* We are committed to increasing our product sales by providing a highly competitive compensation plan to attract and retain Associates who constitute our sales force. We motivate our Associates by paying incentives on a weekly basis. Additionally, our Compensation Plan is, where permissible, a global-seamless plan, meaning that Associates can be compensated each week for their business success in any market in which they have a sales organization where we conduct business. As noted elsewhere in this report, our China operations maintain their own compensation plan, which is structured differently than USANA's plan in other markets.

To support our Associates, we sponsor meetings and events throughout the year, which offer information about our products and our network marketing system. These meetings are designed to assist Associates in business development and to provide a forum for interaction with some of our Associate leaders and with members of the USANA management team. We also provide low-cost sales tools and resources, which we believe are an integral part of building and maintaining a successful home-based business for our Associates. For example, we offer a computer-based, interactive presentation tool, called Health and Freedom Solution, which is designed to help our Associates easily explain and share the USANA opportunity, including the benefits of our products and our Compensation Plan.

In addition to company-sponsored meetings, sales tools and resources, we maintain a website exclusively for our Associates, where they can access the latest USANA news, obtain training materials, manage their personal information, enroll new customers, shop for products, and register for company-sponsored events. Additionally, through this website, Associates can access other online services to which they may subscribe. For example, we offer an online business management service, which includes a tool that helps Associates track and manage their business activity, a personal webpage to which prospects or retail customers can be directed, and e-cards for advertising.

We also believe that recognition is an important factor in supporting and retaining our Associates. We understand that being a successful USANA Associate requires hard work and dedication, and we celebrate key achievements and rank advancements of our Associates. We believe that our recognition programs greatly contribute to our ability to retain our Associates.

*Business Model.* We believe that our business model provides, among others, the following advantages:

No requirement for a company-employed sales force to sell our products, with a relatively low incremental cost to add a new Associate;

Commissions paid to our Associates are tied to sales performance;

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Accounts receivable are minimal because payment is required at the time an Associate or Preferred Customer purchases product;

A stream of recurring revenue from our monthly product subscription program known as "Auto Order," which we utilize in all of our markets (for the year ended January 2, 2016, this program represented 48% of our product sales volume); and

We can typically expand into new international markets with moderate investment because we generally maintain only warehouse facilities, customer support, and minimal administrative facilities in those international markets. Larger markets, including China however, require more significant local investment.

*Experienced Management Team.* Our management team includes individuals with expertise in various scientific and managerial disciplines, including nutrition, product research and development, international development, marketing, customer network development, information technology, manufacturing, finance, legal, regulatory, and operations. This team is responsible for supporting growth, research and development, international expansion, strengthening our financial condition, and improving our internal controls.

**Growth Strategy**

We seek to grow our business by pursuing the following strategies:

*Attract and Retain Customers.* Our customers, and Associates in particular, are central to the growth and success of our business. Accordingly, our primary growth strategy focuses on increasing our overall customer counts throughout the world. We will execute this strategy by applying both world-wide and region-specific initiatives, which include the initiatives set out below. Our management team maintains a close working relationship with our Associate leaders by interacting with them on a regular basis through in-person meetings and phone calls. Further, in addition to our Annual International Convention and our Asia Pacific Convention, we hold several regional events in key growth areas to provide support and training to Associates. We continue to invest in these events and in the marketing of our business to help Associates improve the productivity of their businesses.

*Personalization.* Our personalization initiative has been a key marketing and operating strategy for us over the last few years and will continue to be a key strategy going forward. This initiative focuses on personalizing and improving our overall business, as well as our customers' experience with USANA. We have already applied personalization to many aspects of our business and have several additional enhancements planned going forward, all of which is further discussed under "Current Focus and Recent Developments" above.

*New Product Introductions.* Our research and development team continually reviews the latest scientific findings related to nutrition, conducts or manages research and clinical trials, reviews new technologies, and attends scientific conferences. If, in the process, we see potential for a new product or ingredient that provides a measurable and important health benefit, and if we believe this benefit can be realized by a significant number of our customers, we will generally pursue development of that product. Our research and development focus has and will continue to be centered on personalization and innovation. To the extent reasonably possible, we intend to personalize our product offering and product delivery systems to our customers' individual needs. As discussed above, we have several significant new product introductions and launches planned for 2016 and 2017, which we believe will create a new foundation for USANA to build on for years to come.

*Successfully Grow each of our Regions through Market Specific Strategies and Incentives.* In light of the strength of our Asia Pacific region and our growing Associate base in Asia, we believe that Greater China continues to be the most significant and imminent growth opportunity for us. Our strategy in this

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region is focused on generating customer growth in each market, with an emphasis on China. Our wholly-owned subsidiary, BabyCare, is our operating entity in China. BabyCare has been granted licenses to engage in direct selling in the municipalities of Beijing, Jiangsu, Shaanxi and Tianjin and is working to obtain similar licenses in other provinces. We have spent the last few years registering a portfolio of USANA products for sale by BabyCare in China, educating our customers on our product offering and business model in China, and improving our information systems, technology and infrastructure in China. In 2016, we will continue to execute these strategies and finalize our new state-of-the-art manufacturing and production facility, which we anticipate will become operational during the first half of 2016.

We are also confident in our growth potential in our Southeast Asia Pacific region. While the Philippines and Australia-New Zealand have been key growth markets for us in this region, we generated local currency sales and customer growth in nearly every market in this region in 2015. We have implemented strategies for each market in this region, which are intended to continue our customer growth trend in 2016. Additionally, 2016 will be the first full operational year for Indonesia, our newest market in this region. Indonesia is USANA's 20<sup>th</sup> market and we believe it offers a promising growth opportunity for us.

Our Americas and Europe region is also very important to our business and a significant part of our growth strategy. We achieved double-digit local currency sales and Associate growth in Mexico and Canada through market-specific initiatives in 2015, and expect growth in these markets to continue in 2016. We also remain focused on customer growth in the United States. Our objective for this region in 2016 is centered on increasing the overall number of customers who consistently use USANA products. To achieve our objective, we will continue to execute our personalization and brand-awareness strategies and also utilize market-specific promotions and incentives.

*Brand Awareness:* To facilitate customer growth, we plan to continue to promote global awareness of the USANA brand through various strategies, including professional athlete sponsorships and credible associations with individuals and organizations. Examples of this include our sponsorship of the U.S. Ski Team and our partnership with the Women's Tennis Association. We continue to serve as the official health supplement supplier for these teams and organizations and are also increasing our sponsorship of individual athletes who rely on our products and brand. We seek to leverage these relationships to build brand credibility and increase product consumption and loyalty. In addition to our athlete sponsorships, we seek to advertise and collaborate with credible, nationally recognized organizations and individuals to enhance our global brand. We will also continue our relationship with Dr. Mehmet Oz as a Trusted Partner and Sponsor of *The Dr. Oz Show*, as discussed further under "Current Focus and Recent Developments" above. While branding efforts such as this have a global reach, the primary objective of this initiative is to grow sales and customers in the Americas and Europe.

*Enter New Markets.* We believe that significant growth opportunities continue to exist in markets where we currently conduct business and in new international markets. We commenced operations in Colombia in 2013, and commenced operations in Indonesia during the fourth quarter of 2015. These markets, as well as future markets, are selected following an assessment of several factors, including market size, anticipated demand for USANA products, receptiveness to network marketing, and the market entry process, which includes consideration of possible regulatory restrictions on our products or our network marketing system. We have also begun to register certain products with regulatory and government agencies in other countries in preparation for further international expansion. Wherever possible, we expect to seamlessly integrate the Compensation Plan in each market to allow Associates to receive commissions for global not merely local product sales. This seamless sales structure is designed to allow an Associate to build a global network by creating a sales organization across national borders. We believe our seamless Compensation Plan significantly enhances our ability to expand internationally, and we intend, where permitted, to integrate future markets into this

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Compensation Plan. While we deem new market expansion as a key growth strategy, given the significant opportunity that currently exists in China, we plan to focus the majority of our time and resources on growing that market.

*Pursue Strategic Acquisitions.* We believe that attractive acquisition opportunities may arise in the future. We intend to pursue strategic acquisition opportunities that would grow our customer base, expand our product lines, enhance our manufacturing and technical expertise, allow vertical integration, or otherwise complement our business or further our strategic goals.

**Competition**

We compete with manufacturers, distributors, and retailers of nutritional products for consumers, and we compete with network marketing companies for distributors. On both fronts, some of our competitors are significantly larger than we are, have a longer operating history, higher visibility and name recognition, and have greater financial resources than we do. We compete with these entities by emphasizing the underlying science, value, and superior quality of our products, the simplicity in our product offerings, and the convenience and financial benefits afforded by our network marketing system and global seamless Compensation Plan.

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

We believe that the leading network marketing company in the world, based on total sales, is Amway Corporation and its affiliates, and that Avon Products, Inc. is the leading direct seller of beauty and related products worldwide. Leading competitors in the nutritional network marketing and nutritional product industry include Herbalife Ltd., Inc.; Nu Skin Enterprises, Inc.; and NBTY, Inc. Based on information that is publicly available, 2015 net sales of the aforementioned companies ranged from \$2.3 billion to \$8.6 billion. There are other manufacturers of competing product lines that have or may launch direct selling enterprises that compete with us in certain product lines and in the recruiting of Associates. There can be no assurance that we will be able to successfully meet the challenges posed by increased competition.

**Product Returns**

Product returns have not been a material factor in our business, totaling approximately 0.9% in 2013, 0.8% in 2014, and 0.6% in 2015. Customer satisfaction has always been and will continue to be a hallmark of our business. We believe that we have always offered a generous product return policy. Historically, our standard return policy allowed Associates and Preferred Customers to return any unused product from their first purchase within the first 30 days for a 100% refund of the sales price. Thereafter, any returned product that was unused and resalable was refunded up to one year from the date of purchase at 100% of the sales price, less a 10% restocking fee. During 2015 we updated our return policy and eliminated the 10% restocking fee on product returns. Accordingly, Associates and Preferred Customers now receive a 100% refund of the sales price of unused and resalable products that are returned up to one year from the date of purchase. This standard policy differs slightly in a few of our international markets due to the regulatory environment in those markets. To avoid manipulation of our Compensation Plan, return of product where the purchase amount exceeds \$100 and was not damaged at the time of receipt by the Associate may result in cancellation of an Associate's distributorship.

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**Major Customers**

Sales are made to independent Associates and Preferred Customers. No single customer accounted for 10% or more of net sales. Notwithstanding the foregoing, the nature of our business model results in a significant amount of sales to several different Associate leaders and their sales organizations. Although no single Associate accounted for 10% or more of our net sales, the loss of a key Associate leader or that Associate's sales organization could adversely affect our net sales and our overall operating results.

**Compliance by Associates**

We continually monitor and review our Associates' compliance with our policies and procedures as well as the laws and regulations applicable to our business around the world. Part of this review entails an assessment of our Associates' sales activities to ensure that Associates are actually selling products to consumers. Our policies and procedures require Associates to present our products and the USANA opportunity ethically and honestly. Associates are not permitted to make claims about our products or Compensation Plan that are not consistent with our policies and procedures and applicable laws and regulations. The majority of our Associates must use marketing and promotional materials provided by USANA. Associates who have achieved a certain leadership level are permitted, however, to produce their own marketing and promotional materials, but only if such materials are approved by USANA prior to use.

From time to time, we have Associates who fail to adhere to our policies and procedures. We systematically review reports of alleged Associate misbehavior. Infractions of the policies and procedures are reported to our compliance group, who determine what disciplinary action is warranted in each case. More serious infractions are reported to our Compliance Committee, which includes USANA executives. If we determine that an Associate has violated any of our policies and procedures, we may take a number of disciplinary actions, such as warnings, fines or probation. We may also withdraw or deny awards, suspend privileges, withhold commissions until specific conditions are satisfied, or take other appropriate actions in our discretion, including termination of the Associate's purchase and distribution rights.

We believe that Associate compliance is critical to the integrity of our business and, therefore, we are aggressive in ensuring that our Associates comply with our policies and procedures. As explained above, when an Associate fails to comply with our policies and procedures, we may terminate their purchase and distribution rights. From time to time, we become involved in litigation with Associates whose purchase and distribution rights have been terminated. We consider such litigation to be routine and incidental to our business and will continue to be aggressive in ensuring that our Associates comply with our policies and procedures.

**Information Technology**

We believe that the ability to efficiently manage distribution, compensation, manufacturing, inventory, and communication functions through the use of secure, sophisticated, and dependable information processing systems is critical to our success. We continually evaluate changes in the information technology environment to ensure that we are capitalizing on new technologies, keeping pace with regulatory standards, and ensuring that our systems and data are secure. Over the next few years we intend to increase our investment in technology systems and infrastructure as we prepare to become a much larger company.

Our information technology resources are maintained primarily by our in-house staff to optimally support our customer base and core business processes. Our IT staff manages an array of systems and

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processes which support our global operations 24 hours a day and 365 days a year. Three of our most critical applications include:

A web-based application that provides online services to Associates, such as training sessions and presentations, online shopping, enrollment, a real-time reporting engine, Company and product information, web-hosting, email, and other tools to help Associates effectively manage their business and sales organizations.

A web-based order-entry system that handles order entry, customer information, compensation, Associate business structure, returns, invoices, and other transactional-based processes.

A fully integrated world-wide Enterprise Resource Planning ("ERP") system that handles accounting, human resources, inventory management, production processes, quality assurance, and reporting requirements in a multinational environment.

Our web applications are supported by a clustered environment providing high availability. All production systems are fully backed-up and stored off-site so that our business will not suffer significant interruption in the event of a disaster at the locations of our primary servers.

**Regulatory Matters**

*General.* In the United States and the other countries where we operate, our business is subject to extensive governmental laws and regulations. These laws and regulations exist at various levels in the United States and other countries and pertain to our products, network marketing program, and other aspects of our business as described in more detail below.

*Product Regulation.* Numerous governmental agencies in the United States and other countries regulate the manufacturing, packaging, labeling, advertising, promoting, importing, distributing, and the selling of nutrition, health, beauty, and weight-management products. In the United States, advertisement of our products is regulated by the Federal Trade Commission ("FTC") under the FTC Act and, where such advertising is considered to be product labeling by the FDA, under the Food, Drug, and Cosmetic Act ("FDCA") and the regulations thereunder. USANA products in the United States are also subject to regulation by, among others, the Consumer Product Safety Commission, the U.S. Department of Agriculture, and the Environmental Protection Agency.

Our largest selling product group includes products that are regulated as dietary supplements under the FDCA. Dietary supplements are also regulated in the United States under the Dietary Supplement Health and Education Act of 1994 ("DSHEA"), which we believe is generally favorable to the dietary supplement industry. Some of our powdered drink, food bar, and other nutrition products are regulated as foods under the Nutrition Labeling and Education Act of 1990 ("NLEA"). The NLEA establishes requirements for ingredient and nutritional labeling including product labeling claims. The manufacture of nutritional or dietary supplements and related products in the United States requires compliance with dietary supplement GMPs, which are based on the food-model GMPs and Pharmaceutical GMP's, with additional requirements that are specific to dietary supplements. We are audited annually by the US FDA, specifically for dietary supplements and have been found in full compliance with GMPs for dietary supplements. The Dietary Supplement & Nonprescription Drug Consumer Protection Act requires manufacturers of dietary supplement and over-the-counter products to notify the FDA when they receive reports of serious adverse events occurring within the United States. We have an internal adverse event reporting system that has been in place for several years, and we believe that we are in compliance with this law.

In general, our personal care products, which are regulated as cosmetic products by the FDA, are not subject to pre-market approval by that agency. Cosmetics, however, are subject to regulation by the FDA under the FDCA adulteration and misbranding provisions. Cosmetics also are subject to specific labeling regulations, including warning statements, if the safety of a cosmetic is not adequately

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substantiated or if the product may be hazardous, as well as ingredient statements and other packaging requirements under the Fair Packaging and Labeling Act. Cosmetics that meet the definition of a drug, such as sunscreens, are regulated as drugs. Over-the-counter ("OTC") drug products, including cosmetics, may be marketed if they conform to the requirements of the OTC monograph that is applicable to that drug. Drug products not conforming to monograph requirements require an approved New Drug Application ("NDA") before marketing may begin. Under these provisions, if the agency were to find that a product or ingredient of one of our OTC drug products is not generally recognized as safe and effective or is not included in a final monograph that is applicable to one of our OTC drug products, we would be required to reformulate or cease marketing that product until it is the subject of an approved NDA or until the time, if ever, that the monograph is amended to include such product.

Advertising of our products in the United States is subject to regulation by the FTC under the FTC Act. Under the FTC's Substantiation Doctrine, an advertiser is required to have a "reasonable basis" for all objective product claims before the claims are made. Failure to adequately substantiate claims may be considered either deceptive or unfair practices. Pursuant to this FTC requirement, we are required to have adequate substantiation for all material advertising claims that we make for our products in the United States. In recent years, the FTC has initiated numerous investigations of and actions against companies that sell dietary supplement, weight-management, and cosmetic products. The FTC has issued guidance to assist companies in understanding and complying with its substantiation requirement. We believe that we have adequate substantiation for all material advertising claims that we make for our products in the United States, and we believe that we have organized the documentation to support our advertising and promotional practices in compliance with these guidelines. However, no assurance can be given that the FTC would reach the same conclusion if it were to review or question our substantiation for our advertising claims in the United States.

The FTC may enforce compliance with the law in a variety of ways, both administratively and judicially, using compulsory process, cease and desist orders, and injunctions. FTC enforcement can result in orders requiring, among other things, limits on advertising, corrective advertising, consumer redress, divestiture of assets, rescission of contracts, and such other relief as the agency deems necessary to protect the public. Violation of these orders could result in substantial financial or other penalties. Although, to our knowledge, we have not been the subject of any action by the FTC, no assurance can be given that the FTC will not question our advertising or other operations in the United States in the future. Any action in the future by the FTC could materially and adversely affect our ability to successfully market our products in the United States.

The manufacturing, labeling, and advertising of our products are also regulated by various governmental agencies outside the United States in each country where they are distributed. For example, in Australia, product registration, labeling and manufacturing is regulated by the TGA and, in Japan, the Ministry of Health, Labor and Welfare. In China, the China Food and Drug Administration ("CFDA") regulates product registration, labeling and manufacturing. In markets outside the United States, prior to commencing operations or marketing products, we may be required to obtain approvals, licenses, or certifications from a country's Food Administration, Ministry of Health or comparable agency. Approvals or licensing may be conditioned on reformulation of USANA products for the market or may be unavailable with respect to certain products or product ingredients. We must also comply with local product labeling and packaging regulations that vary from country to country. For example, China extensively regulates the registration, labeling and marketing of our products. In China, our nutritional products are typically classified as "health functional foods" and our personal care products are typically classified as "non-special use cosmetics". The registration process for health functional foods is complex and generally requires extensive analysis and approval by the CFDA. As a result, it may take several years to register a product as a health functional food in China. While all products currently sold by BabyCare in China have been registered with the CFDA, we continue to

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work through the registration process for other health functional food products, which we also hope to begin selling through BabyCare in the future.

We cannot predict the nature of any future laws, regulations, interpretations, or applications, nor can we determine what effect additional governmental regulations or administrative orders, when and if promulgated, would have on our business. Future changes could include requirements for the reformulation of certain products to meet new standards, the recall or discontinuation of certain products that cannot be reformulated, additional record keeping, expanded documentation of the properties of certain products, expanded or different labeling, and additional scientific substantiation. Any or all of these requirements could have a material adverse effect on our business, financial condition, and operating results.

*Network Marketing Regulation.* Various laws and regulations in the United States and other countries regulate network marketing, or direct selling. These laws and regulations exist at many levels of government in many different forms, including statutes, rules, regulations, judicial decisions, and administrative orders. Generally, the regulations are directed at: (i) ensuring that product sales ultimately are made to consumers and that advancement within a sales organization is based on product sales rather than on investments in the organization or on other criteria that are not related to sales; and (ii) preventing the use of deceptive or fraudulent practices that have sometimes been inappropriately associated with legitimate direct selling and network marketing activities. Network marketing regulations are inherently fact-based and often do not include "bright line" rules. Additionally, we are subject to the risk that the regulations, or a regulator's interpretation and enforcement of the regulations, could change. From time to time, we have received requests to supply information regarding our network marketing plan to regulatory agencies. We have also modified our network marketing plan in the past to comply with the interpretation of the regulations by authorities. Where required by law, we obtain regulatory approval of our network marketing plan, or, where approval is not required or available, the favorable opinion of local counsel as to regulatory compliance. Nevertheless, we remain subject to the risk that, in one or more countries, our network marketing plan, or the conduct of certain of our Associates, could be found not to be in compliance with applicable laws and regulations. Additionally, we cannot predict the nature of any future law, regulation, or interpretation, nor can we predict what effect additional governmental regulations, judicial decisions, or administrative orders, when and if promulgated, would have on our business. Failure by us, or our Associates, to comply with these regulations could have a material adverse effect on our business in a particular market or in general.

Network marketing companies, and the industry in general, continue to experience significant media and public scrutiny in many countries. Several companies similar to ours have been scrutinized and penalized in several markets where we operate, including the United States, Canada, China, Japan, and South Korea. This scrutiny, along with the uncertainty of the laws and regulations pertaining to network marketing in many countries, can affect how a regulator or member of the public perceives our Company. For instance, there has been significant media and short-seller attention regarding the viability and legality of network marketing in the United States and China over the past few years. This attention has led to intense public scrutiny of the industry, as well as volatility in our stock price and the stock prices of companies similar to our company. We cannot predict the impact that this scrutiny may have on our business or the industry in general.

The Chinese government has adopted direct selling laws and regulations that are uncertain and evolving. These regulations contain a number of financial and operational restrictions for direct selling companies, most notably on pyramid selling and multi-level compensation. These regulations are also subject to discretionary interpretation and enforcement by various municipal and provincial level officials in China. Our business in China is that of BabyCare, a direct selling company that we indirectly acquired several years ago to facilitate our expansion into China. BabyCare's business model has been developed specifically for China in light of Chinese direct selling laws and regulations.

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BabyCare has been granted licenses from the Chinese government to conduct direct selling in four provinces in China and will be required to obtain licenses from municipalities and provinces in China where it does not hold a license. The process for obtaining government approval in China to conduct direct selling continues to evolve, is time-consuming, and expensive. The complexity of the approval process, as well as the government's continued cautious approach to direct selling in China, make it difficult to predict the timeline for obtaining additional approvals. If the process for obtaining approvals is delayed, changed or interpreted differently than currently understood, such events could have a negative impact on BabyCare's growth prospects in China. Ultimately, there can be no assurance that BabyCare will be successful in obtaining additional direct-selling licenses or the required approvals to expand into additional locations in China that are important to its business there.

*Transfer Pricing Regulation.* In the United States and many other countries, we are subject to transfer pricing and other tax regulations that are designed to ensure that appropriate levels of income are reported by our U.S. or international entities and are taxed accordingly. We have adopted transfer prices, which are supported by formal transfer pricing studies for the sale of products to our subsidiaries in accordance with applicable transfer pricing laws. In addition, we have entered into agreements with our subsidiaries for services and other contractual obligations, such as the payment of Associate incentives that are also supported by the same formal transfer pricing studies. If the U.S. Internal Revenue Service or the taxing authorities of any other jurisdiction were to successfully challenge these agreements or require changes in our standard transfer pricing practices for products, we could become subject to higher taxes and our earnings could be adversely affected. The tax treaties between the United States and most countries provide competent authority for relief to avoid any double taxation. We believe that we operate in compliance with all applicable transfer pricing regulations. There can be no assurance, however, that we will continue to be found to be operating in compliance with transfer pricing regulations or that those laws will not be modified, which may require that we change our operating procedures.

**Intellectual Property**

*Trademarks.* We have developed and use registered trademarks in our business, particularly relating to our corporate and product names. We own 25 trademarks that are registered with the U.S. Patent and Trademark Office. Federal registration of a trademark enables the registered owner of the mark to bar the unauthorized use of the registered mark in connection with a similar product in the same channels of trade by any third-party anywhere in the United States, regardless of whether the registered owner has ever used the trademark in the area where the unauthorized use occurs. We have filed applications and own trademark registrations, and we intend to register additional trademarks in countries outside the United States where USANA products are or may be sold in the future. Protection of registered trademarks in some jurisdictions may not be as extensive as the protection in the United States.

We also claim ownership and protection of certain product names, unregistered trademarks, and service marks under common law. Common law trademark rights do not provide the same level of protection that is afforded by the registration of a trademark. In addition, common law trademark rights are limited to the geographic area in which the trademark is actually used. We believe these trademarks, whether registered or claimed under common law, constitute valuable assets, adding to recognition of USANA and the effective marketing of USANA products. Trademark registration once obtained is essentially perpetual, subject to the payment of a renewal fee. We therefore believe that these proprietary rights have been and will continue to be important in enabling us to compete.

*Trade Secrets.* We own certain intellectual property, including trade secrets that we seek to protect, in part, through confidentiality agreements with employees and other parties. Even where these agreements exist, there can be no assurance that these agreements will not be breached, that we would have adequate remedies for any breach, or that our trade secrets will not otherwise become known to

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or independently developed by competitors. Our proprietary product formulations are generally considered trade secrets, but are not otherwise protected under intellectual property laws.

*Patents.* We have three U.S. patents. Two of our patents relate to the method of extracting an antioxidant from olives and the byproducts of olive oil production. These patents were issued in 2002 and will continue in force until December 20, 2019. Our third patent relates to a method of self-preserving our Sensé line of personal care products. This patent was issued in May 2007 and will continue in force until August 5, 2024.

We intend to protect our legal rights concerning intellectual property by all appropriate legal action. Consequently, we may become involved from time to time in litigation to determine the enforceability, scope, and validity of any of the foregoing proprietary rights. Any patent litigation could result in substantial cost and divert the efforts of management and technical personnel.

**Seasonality**

Although we are not significantly affected by seasonality, we do experience variations in the activity of our Associates in many of our markets in the first and fourth quarters around major cultural events such as Chinese New Year and Christmas.

**Backlog**

Our products are typically shipped within 72 hours after receipt of an order. As of February 26, 2016 we had no significant backlog of orders.

**Working Capital Practices**

We maintain sufficient amounts of inventory in stock in order to provide a high level of service to our Associates and Preferred Customers. Substantial inventories are required to meet the needs of our dual role as manufacturer and distributor. We also watch seasonal commodity markets and may buy ahead of normal demand to hedge against cost increases and supply risks.

**Environment**

We are not aware of any instance in which we have contravened federal, state, or local laws relating to protection of the environment or in which we otherwise may be subject to liability for environmental conditions that could materially affect operations.

**Employees**

As of February 26, 2016 we had approximately 1,664 employees worldwide, as measured by full-time equivalency. Our employees are not currently represented by a collective bargaining agreement, and we have not experienced work stoppages as a result of labor disputes. We believe that we have a good relationship with our employees.

**Additional Available Information**

We maintain executive offices and principal facilities at 3838 West Parkway Boulevard, Salt Lake City, Utah 84120. Our telephone number is (801) 954-7100. We maintain a World Wide Web site at [www.usanahealthsciences.com](http://www.usanahealthsciences.com). The information on our web site should not be considered part of this report on Form 10-K.

We make available, free of charge at our corporate web site, copies of our annual reports on United States Securities and Exchange Commission ("SEC") Form 10-K, quarterly reports on SEC Form 10-Q, current reports on SEC Form 8-K, proxy statements, and all amendments to these reports, as soon as reasonably practicable after such material is electronically filed with or furnished to the SEC pursuant to Section 13(a) or 15(d) of the Exchange Act. This information may also be obtained from the SEC's on-line database, which is located at [www.sec.gov](http://www.sec.gov).

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**Item 1A. Risk Factors**

**Forward-Looking Statements and Certain Risks**

*We encounter substantial risks in our business, any one of which may adversely affect our business, results of operations or financial condition. The fact that some of these risk factors may be the same or similar to those that we have filed with the Securities and Exchange Commission in past reports means only that the risks are present in multiple periods. We believe that many of the risks that are described here are part of doing business in the industry in which we operate and will likely be present in all periods. The fact that certain risks are endemic to the industry does not lessen their significance. These risk factors should be read together with the other items in this report, including Item 1, "Business," and Item 7, "Management's Discussion and Analysis of Financial Condition and Results of Operations." Among others, risks and uncertainties that may affect our business, financial condition, performance, development, and results of operations include the following:*

***We are a network marketing company and are dependent upon an independent sales force of "Associates" to sell our products. If we are unable to attract and retain Associates, our business may be harmed.*** We rely on non-employee, independent Associates to market and sell our products and to generate our sales. Our ability to maintain and increase sales in the future will depend in large part upon our success in increasing the number of new Associates, retaining and motivating our existing Associates, and in improving the productivity of our Associates. Associates typically market and sell our products on a part-time basis and likely will engage in other business activities, some of which may compete with us. We rely primarily upon our Associates to attract, train and motivate new Associates. Our ability to continue to attract and retain Associates can be affected by a number of factors, some of which are beyond our control, including:

General business and economic conditions;

Adverse publicity or negative misinformation about our industry, us or our products;

Negative public perceptions about network marketing programs;

High-visibility investigations or legal proceedings against network marketing companies by federal or state authorities or private citizens;

Public perceptions about the value and efficacy of nutritional or dietary supplement, products generally;

Other competing network marketing organizations entering into the marketplace that may recruit our existing Associates or reduce the potential pool of new Associates; and

Changes to the Compensation Plan required by law or implemented for business reasons that make attracting and retaining Associates more difficult.

We can provide no assurance that the number of Associates will increase or remain constant or that their productivity will increase. Our Associates may terminate their services at any time, and, like most direct selling companies, we experience a high turnover among new Associates from year to year. While our total number of active Associates has continued to increase during recent years, a few of our markets, including the United States, have experienced a decline in the number of active Associates. If our strategies and initiatives do not drive growth in our Associate numbers, particularly in the United States, China and other markets, our operating results could be harmed. We cannot accurately predict any fluctuation in the number and productivity of Associates because we primarily rely upon existing Associates to sponsor and train new Associates and to motivate new and existing Associates. Our operating results in other markets could also be adversely affected if we and our existing Associates do not generate sufficient interest in our business to successfully retain existing Associates and attract new Associates.

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***The loss of a significant USANA Associate or downline sales organization could adversely affect our business.*** We rely on the successful efforts of our Associates that become leaders within our Compensation Plan. Our Compensation Plan is designed to permit Associates to sponsor new Associates, creating multiple "business centers," or levels in the downline organization. Sponsored Associates are referred to as "downline" Associates within the sponsoring Associate's "downline network." If these downline Associates in turn sponsor new Associates, additional business centers are created, with the new downline Associates becoming part of the original sponsoring Associate's downline network. As a result of this network marketing system, Associates develop business relationships with other Associates. The loss of a key Associate or group of Associates, large turnover or decreases in the size of the key Associate force, seasonal or other decreases in purchase volume, sales volume reduction, the costs associated with training new Associates, and other related expenses may adversely affect our business, financial condition, or results of operations.

***The violation of marketing or advertising laws by Associates in connection with the sale of our products or the improper promotion of our Compensation Plan could adversely affect our business.*** All Associates sign a written contract and agree to adhere to our policies and procedures. Although these policies and procedures prohibit Associates from making false, misleading and other improper claims regarding products or income potential from the distribution of the products, Associates may, from time to time, without our knowledge and in violation of our policies, create promotional materials or otherwise provide information that does not accurately describe our marketing program. They also may make statements regarding potential earnings, product claims, or other matters in violation of our policies or applicable laws and regulations concerning these matters. These violations may result in legal action against us by regulatory agencies, state attorneys general, or private parties. Legal actions against our Associates or others who are associated with us could lead to increased regulatory scrutiny of our business, including our network marketing system. We take what we believe to be commercially reasonable steps to monitor the activities of our Associates to guard against misrepresentation and other illegal or unethical conduct by Associates and to assure that the terms of our policies and procedures and Compensation Plan are observed. There can be no assurance, however, that our efforts in this regard will be sufficient to accomplish this objective, particularly in times/regions where we may experience rapid growth. Adverse publicity resulting from such activities could also make it more difficult for us to attract and retain Associates and may have an adverse effect on our business, financial condition, and results of operations.

***We may have or could incur obligations relating to the activities of our Associates.*** Our Associates are subject to taxation, and, in some instances, legislation or governmental agencies impose an obligation on us to collect taxes, such as sales taxes or value added taxes, and to maintain appropriate records of such transactions. In addition, we are subject to the risk in some jurisdictions of being responsible for social security and similar taxes with respect to our Associates. In the event that local laws and regulations or the interpretation of local laws and regulations change to require us to treat our independent Associates as employees, or if our Associates are deemed by local regulatory authorities in one or more of the jurisdictions in which we operate to be our employees rather than independent contractors, under existing laws and interpretations, we may be held responsible for a variety of obligations that are imposed upon employers relating to their employees, including social security and related taxes in those jurisdictions, plus any related assessments and penalties, which could harm our financial condition and operating results.

***Network marketing is subject to intense government scrutiny, and regulation and changes in the law, or the interpretation and enforcement of the law, might adversely affect our business.*** Various laws and regulations in the United States and other countries regulate network marketing, or direct selling. These laws and regulations exist at many levels of government in many different forms, including statutes, rules, regulations, judicial decisions, and administrative orders. Network marketing regulations are inherently fact-based and often do not include "bright line" rules. As a result, regulators and courts

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have broad discretion in their application, interpretation and enforcement of these laws and regulations, and any of the foregoing can change. We are subject to the risk that, in one or more countries, our network marketing plan, or the conduct of certain of our Associates, could be found not to be in compliance with applicable laws and regulations. Further, we may simply be prohibited from distributing products through a network-marketing channel in some countries, or we may be forced to alter our Compensation Plan.

We are also subject to the risk that new laws or regulations might be implemented or that current laws or regulations might change, or be interpreted or enforced differently, which could require us to change or modify the way we conduct our business in certain markets. This could be particularly detrimental to us if we had to change or modify the way we conduct business in markets that represent a significant percentage of our net sales.

We are aware of regulatory challenges, investigations and litigation against other network marketing companies in the industry in the United States and other countries where we operate. Any adverse ruling in these investigations could harm our business and industry if the laws and regulations are interpreted in a manner that results in additional burdens or restrictions on network marketing companies. Additionally, we cannot assure you that we will not be subject to challenges by regulators regarding our network marketing plan.

***Our products and manufacturing activities are subject to extensive government regulation, which could limit or prevent the sale of our products in some markets.*** The manufacture, packaging, labeling, advertising, promotion, distribution, and sale of our products are subject to regulation by numerous national and local governmental agencies in the United States and other countries, including the FDA and the FTC. For example, failure to comply with FDA regulatory requirements may result in, among other things, injunctions, product withdrawals, recalls, product seizures, fines, and criminal prosecutions. Any action of this type by the FDA could materially adversely affect our ability to successfully market our products. With respect to FTC matters, if the FTC has reason to believe the law is being violated, it can initiate an enforcement action. The FTC has a variety of processes and remedies available to it for enforcement, both administratively and judicially. Any action against us by the FTC could materially and adversely affect our ability to successfully market our products.

The manufacture of nutritional or dietary supplements and related products in the United States requires compliance with dietary supplement GMPs, which are based on the food-model GMPs, with additional requirements that are specific to dietary supplements. We believe our manufacturing processes comply with these GMPs for dietary supplements. Nevertheless, any action by the FDA which determined that our processes were non-compliant with dietary supplement GMPs, could materially adversely affect our ability to manufacture and market our products. Additionally, the Dietary Supplement & Nonprescription Drug Consumer Protection Act requires manufacturers of dietary supplement and over-the-counter products to notify the FDA when they receive reports of serious adverse events occurring within the United States. Potential FDA responses to any such report could include injunctions, product withdrawals, recalls, product seizures, fines, or criminal prosecutions. We have an internal adverse event reporting system that has been in place for several years and believe that we are in compliance with this new law. Nevertheless, any action by the FDA in response to a serious adverse event report that may be filed by us could materially and adversely affect our ability to successfully market our products.

In markets outside the United States, prior to commencing operations or marketing our products, we may be required to obtain approvals, licenses, or certifications from a country's ministry of health or a comparable agency. For example, our manufacturing facility has been registered with the FDA and Health Canada and is certified by Australia's TGA. Approvals or licensing may be conditioned on reformulation of products or may be unavailable with respect to certain products or product ingredients. China also extensively regulates the registration, labeling and marketing of our products.

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Consequently, the registration process for our products in China is complex and generally requires extensive analysis and approval by the CFDA. As a result, it may take several years to register a product in China. We must also comply with product labeling and packaging regulations that vary from country to country. These activities are also subject to regulation by various agencies of the countries in which our products are sold.

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

***Our manufacturing activity is subject to certain risks.*** We manufacture approximately 76% of the products sold to our customers. As a result, we are dependent upon the uninterrupted and efficient operation of our manufacturing facilities. Those operations are subject to power failures, the breakdown, failure, or substandard performance of equipment, the improper installation or operation of equipment, natural or other disasters, and the need to comply with the requirements or directives of government agencies, including the FDA. There can be no assurance that the occurrence of these or any other operational problems at our facility would not have a material adverse effect on our business, financial condition, or results of operations. We are subject to a variety of environmental laws relating to the storage, discharge, handling, emission, generation, manufacture, use and disposal of chemicals, solid and hazardous waste, and other toxic and hazardous materials. Our manufacturing operations presently do not result in the generation of material amounts of hazardous or toxic substances. Nevertheless, complying with new or more stringent laws or regulations, or more vigorous enforcement of current or future policies of regulatory agencies, could require substantial expenditures by us that could have a material adverse effect on our business, financial condition, or results of operations. Environmental laws and regulations require us to maintain and comply with a number of permits, authorizations, and approvals and to maintain and update training programs and safety data regarding materials used in our processes. Violations of those requirements could result in financial penalties and other enforcement actions and could require us to halt one or more portions of our operations until a violation is cured. The combined costs of curing incidents of non-compliance, resolving enforcement actions that might be initiated by government authorities, or of satisfying new legal requirements could have a material adverse effect on our business, financial condition, or results of operations.

***We may incur liability with respect to our products.*** As a manufacturer and a distributor of products for human consumption and topical application, we could become exposed to product liability claims and litigation. Additionally, the manufacture and sale of these products involves the risk of injury to consumers due to tampering by unauthorized third parties or product contamination. To date, we have not been a party to any product liability litigation, although, like any dietary supplement company, we have received reports from individuals who have asserted that they suffered adverse consequences as a result of using our products. The number of reports we have received to date is nominal. These matters historically have been settled to our satisfaction and have not resulted in material payments. We are aware of no instance in which any of our products are or have been defective in any way that could give rise to material losses or expenditures related to product liability claims. Although we maintain product liability insurance, which we believe to be adequate for our needs, there can be no assurance that we will not be subject to such claims in the future or that our insurance coverage will be adequate.

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***Our Greater China region accounts for a significant part of our business and expected growth. Any decline in sales or customers in this region would harm our business, financial condition and results of operations.*** Our Greater China region consists of China, Hong Kong and Taiwan and is currently our largest and most rapidly growing region. Since our acquisition of BabyCare, Ltd. in China in 2010, our international growth strategy has been centered on growing BabyCare's business in China. As a result of this strategy, China has been our fastest growing market over the last few years and is now our largest individual market. As we have focused on China, we have also experienced a meaningful decline in sales and customers in our Hong Kong market and our results in this market may continue to decline in the future. If we are not successful in continuing to grow BabyCare's sales and customer base in China, our consolidated growth as a company will be negatively affected and our business, financial condition and results of operations may be harmed. BabyCare must comply with significant operational, financial, and other regulatory requirements to engage in direct selling in China. Although we believe that, in light of our successful Asian Associate base, we will be successful in growing BabyCare's business in China, it is difficult to assess the extent to which BabyCare's Chinese business model and Associate compensation plan will be successful in that market or deemed to be compliant with applicable laws and regulations by the Chinese government. Although we are required to conduct our operations in China through BabyCare, we believe that our long-term success in China will depend on our ability to successfully integrate, to the extent possible, our operations with BabyCare's operations. In light of the factors listed above, and the other risks to our business, there can be no assurance that we will be successful in growing sales and customers in China through BabyCare.

***Our operations in China are subject to significant government regulation and scrutiny, as well as a variety of legal, political, and economic risks. If the government modifies the direct selling regulations, or interprets and enforces the regulations in a manner that is adverse to our business in China, our consolidated business and results of operations may be materially harmed.*** Our business in China is that of BabyCare, a direct selling company that we indirectly acquired several years ago to facilitate our expansion into China. BabyCare has been granted licenses from the Chinese government to conduct direct selling operations in four provinces in China and has applied for licenses in additional municipalities and provinces. BabyCare's business model has been designed specifically for China based on a number of factors, including: (i) BabyCare's communications with the Chinese government, (ii) BabyCare's interpretation of the direct selling regulations, as well as their understanding of how the government interprets and enforces the regulations, and (iii) BabyCare's understanding of how other multinational direct selling companies operate in China. Notwithstanding the foregoing, BabyCare has not received confirmation from the Chinese government that its business model and operations in China comply with applicable laws and regulations, including those pertaining to direct selling.

The Chinese government has adopted direct selling laws and regulations that are uncertain and evolving. These regulations contain a number of financial and operational restrictions for direct selling companies, most notably on pyramid selling and multi-level compensation. These regulations are also subject to discretionary interpretation and enforcement by various municipal and provincial level officials in China. We cannot assure you that BabyCare's business model or the activities of its employees, promoters or direct sellers will be deemed by regulatory authorities to be compliant with current or future laws and regulations. In the past, the Chinese government has fined, penalized, and, in some cases, terminated direct selling licenses and shut down companies that it believed were in violation of applicable laws and regulations. As such, there can be no assurance that the Chinese government's interpretation and enforcement of applicable laws and regulations will not negatively impact BabyCare's business, result in regulatory investigations or lead to fines or penalties against BabyCare, USANA or our Associates in China.

The direct selling regulations in China prevent persons who are not Chinese nationals from engaging in direct selling in China. Although we have implemented internal policies that are designed to promote our Associates' compliance with these regulations, we cannot guarantee that any of our

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Associates living outside of China or any of BabyCare's promoters or Associates in China have not engaged or will not engage in activities that violate our policies in this market or that violate Chinese law or other applicable laws and regulations and, therefore, might result in regulatory action and adverse publicity, which would harm our business in China.

BabyCare is required to obtain various licenses and approvals from municipalities and provinces within China to operate its direct selling business model. Currently, BabyCare holds four such licenses and will be required to obtain licenses from municipalities and provinces within China where it does not hold a license. If BabyCare is unable to obtain additional direct selling licenses as quickly as we would like, it would have a negative impact on our ability to expand and grow our business. The process for obtaining the necessary government approvals to conduct direct selling continues to evolve, is time-consuming and expensive. The complexity of the approval process, as well as the government's continued cautious approach for direct selling in China, makes it difficult to predict the timeline for obtaining additional approvals. If the current processes for obtaining approvals are delayed for any reason or are changed or are interpreted differently than currently understood, these events could have a negative impact on BabyCare's growth prospects in China. Ultimately, there can be no assurance that BabyCare will be successful in obtaining additional direct-selling licenses or the required approvals to expand into additional locations in China that are important to its business.

If BabyCare's operations in China are successful, we may experience rapid growth in China, and there can be no assurances that we will be able to successfully manage rapid expansion of BabyCare's direct selling activities under license in China or the related manufacturing and retail operations required to support this expansion. If we are unable to effectively manage BabyCare's growth and expansion, including expansion of branches, warehouses, and manufacturing operations, BabyCare's government relations may be compromised and our operations in China may be harmed.

***Risks associated with operating in international markets could restrict our ability to expand globally and harm our business and prospects, and we could be adversely affected by our failure to comply with the laws applicable to our foreign activities, including the U.S. Foreign Corrupt Practices Act and other similar worldwide anti-bribery laws.*** Our international operations are presently conducted in various foreign countries, and we expect that the number of countries in which we operate could expand over the next few years. Economic conditions, including those resulting from wars, civil unrest, acts of terrorism and other conflicts or volatility in the global markets, may adversely affect our customers, their demand for our products and their ability to pay for our products. In addition, there are numerous risks inherent in conducting our business internationally, including, but not limited to, potential instability in international markets, changes in regulatory requirements applicable to international operations, currency fluctuations in foreign countries, political, economic and social conditions in foreign countries and complex U.S. and foreign laws and treaties, including tax laws, the U.S. Foreign Corrupt Practices Act (FCPA), and the Bribery Act of 2010 (U.K. Anti-Bribery Act). These risks could restrict our ability to sell products, obtain international customers, or to operate our international business profitably, which would have a negative impact on our overall business and results of operations.

The FCPA prohibits U.S.-based companies and their intermediaries from making improper payments to government officials for the purpose of obtaining or retaining business. We are also subject to the U.K. Anti-Bribery Act, which prohibits both domestic and international bribery as well as bribery across both public and private sectors. We pursue opportunities in certain parts of the world that experience government corruption and, in certain circumstances, compliance with anti-bribery laws may conflict with local customs and practices. Our policies mandate compliance with all applicable anti-bribery laws. Further, we require our partners, subcontractors, agents and others who work for us or on our behalf to comply with the FCPA and other anti-bribery laws. Although we have policies and procedures designed to ensure that we, our employees, our agents and others who work with us in foreign countries comply with the FCPA and other anti-bribery laws, there is no assurance that such policies or procedures will protect us against liability under the FCPA or other laws for actions taken

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by our agents, employees and intermediaries. If we are found to be liable for violations of these acts (either due to our own acts or our inadvertence or due to the acts or inadvertence of others), we could incur severe criminal or civil penalties or other sanctions, which could have a material adverse effect on our reputation, business, results of operations or cash flows. In addition, detecting, investigating and resolving actual or alleged violations of these acts is expensive and could consume significant time and attention of our senior management.

We believe that our ability to achieve future growth is dependent in part on our ability to continue our international expansion efforts. There can be no assurance, however, that we will be able to grow in our existing international markets, enter new international markets on a timely basis, or that new markets will be profitable. We must overcome significant regulatory and legal barriers before we can begin marketing in any international market. Also, before marketing commences in a new country or market, it is difficult to assess the extent to which our products and sales techniques will be accepted or successful in any given country. In addition to significant regulatory barriers, we may also encounter problems conducting operations in new markets with different cultures and legal systems from those encountered elsewhere. We may be required to reformulate certain of our products before commencing sales in a given country. Once we have entered a market, we must adhere to the regulatory and legal requirements of that market. No assurance can be given that we will be able to successfully reformulate our products in any of our current or potential international markets to meet local regulatory requirements or to attract local customers. Our failure to do so could have a material adverse effect on our business, financial condition, or results of operations. There can be no assurance that we will be able to obtain and retain necessary permits and approvals in new markets or that we will have sufficient capital to finance our expansion efforts in a timely manner.

In many market areas, other network marketing companies already have significant market penetration, the effect of which could be to desensitize the local Associate population to a new opportunity, such as USANA, or to make it more difficult for us to attract qualified Associates. Even if we are able to commence operations in new markets, there may not be a sufficient population of persons who are interested in our network marketing system. We believe our future success will depend in part on our ability to seamlessly integrate our Compensation Plan across all markets where legally permissible. There can be no assurance, however, that we will be able to utilize our Compensation Plan seamlessly in all existing or future markets. For example, in August 2010, we indirectly acquired BabyCare, a nutritional supplement company that is now licensed by the government of China to engage in direct selling in the Municipalities of Beijing, Jiangsu, Shaanxi, and Tianjin. In accordance with Chinese law, we utilize a compensation plan that has been designed specifically for China and implemented by BabyCare separately from our Compensation Plan in our other markets.

***Fluctuation in the value of currency exchange rates with the U.S. dollar affects our operations and our net sales and earnings.*** Over the past several years, a majority of our net sales have been generated outside the United States. Such sales for the year ended January 2, 2016 represented 84.8% of our total net sales. We will likely continue to expand our operations into new markets, exposing us to expanding risks of changes in social, political, and economic conditions, including changes in the laws and policies that govern investment or exchange in these markets. Because a significant portion of our sales are generated outside the United States, exchange rate fluctuations will have a significant effect on our sales and earnings. Further, if exchange rates fluctuate dramatically, it may become uneconomical for us to establish or to continue activities in certain countries. For instance, changes in currency exchange rates may affect the relative prices at which we and our competitors sell similar products in the same market. As our business expands outside the United States, an increasing share of our net sales and operating costs will be transacted in currencies other than the U.S. dollar. Accounting practices require that our non-U.S. financial results be converted to U.S. dollars for reporting purposes. Consequently, our reported net earnings may be significantly affected by fluctuations in currency exchange rates, with earnings generally increasing with a weaker U.S. dollar and decreasing with a

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strengthening U.S. dollar. Product purchases by our subsidiaries are transacted in U.S. dollars. As our operations expand in countries where transactions may be made in currencies other than the U.S. dollar, our operating results will be increasingly subject to the risks of exchange rate fluctuations and we may not be able to accurately estimate the impact that these changes might have on our future business, product pricing, results of operations, or financial condition. In addition, the value of the U.S. dollar in relation to other currencies may also adversely affect our sales to customers outside the United States. Currently our strategy for reducing our exposure to currency fluctuation includes the timely and efficient repatriation of earnings from international markets where such earnings are not considered to be indefinitely reinvested, and settlement of intercompany transactions. We also from time to time enter into currency exchange contracts to offset foreign currency exposure in various international markets. We do not use derivative instruments for speculative purposes. There can be no assurance that we will be successful in protecting our operating results or cash flows from potentially adverse effects of currency exchange fluctuations. Any such adverse effects could also adversely affect our business, financial condition, or results of operations.

***Difficult economic conditions may adversely affect our business.*** Over the past few years, economic conditions in many of the markets where we sell our products have resulted in challenges to our business. This is particularly true in our Americas and Europe region, where, although we have seen a recent improvement, we continue to experience difficulty generating meaningful growth. We cannot predict whether world or market-specific economies will improve or deteriorate in the future. If difficult economic conditions continue or worsen, we could experience declines in net sales, profitability and cash flow due to lower demand for our products or other factors caused by economic challenges faced by our customers, potential customers or suppliers. Additionally, these conditions may result in a material adverse effect on our liquidity and capital resources or otherwise negatively impact our operations or overall financial condition.

***Our business is subject to the effects of adverse publicity and negative public perception.*** Our ability to attract and retain Associates and to sustain and enhance sales through our Associates can be affected by adverse publicity or negative public perception regarding our industry, our competition, or our business generally. Our business prospects, financial condition and results of operations could be adversely affected if our public image or reputation were to be tarnished by negative publicity including dissemination via print, broadcast or social media, or other forms of Internet-based communications. This negative public perception may include publicity regarding the legality of network marketing, the quality or efficacy of nutritional supplement products or ingredients in general or our products or ingredients specifically, and regulatory investigations, regardless of whether those investigations involve us or our Associates or the business practices or products of our competitors or other network marketing companies.

In 2007, we were the victim of false statements made to the press and regulatory agencies, causing us to incur significant expense in defending and dispelling the allegations during 2007 and 2008. More recently, in November 2012, we were again the target of false and misleading statements concerning our business practices, particularly in China and Hong Kong. This adverse publicity also had an adverse impact on the market price of our stock and caused insecurity among our Associates.

Additionally, there has been significant media and short-seller attention regarding the viability and legality of network marketing in the United States and internationally over the past few years. This attention has led to intense public scrutiny of the industry, as well as volatility in our stock price and the stock price of companies similar to ours. There can be no assurance that we will not be subject to adverse publicity or negative public perception in the future or that such adverse publicity will not have a material adverse effect on our business, financial condition, or results of operations.

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***Our Associate Compensation Plan, or changes we make to it, may be viewed negatively by some Associates, could fail to achieve our desired objectives, and could have a negative impact on our business.*** Our line of business is highly competitive and sensitive to the introduction of new competitors, new products and/or new distributor compensation plans. Network marketing companies commonly attempt to attract new distributors by offering generous distributor compensation plans. From time to time, we modify components of our Compensation Plan in an effort to (i) keep it competitive and attractive to existing and potential Associates, (ii) cause or address a change in Associate behavior, (iii) incent Associates to grow our business, (iv) conform to legal and regulatory requirements, and (v) address other business needs. In light of the size and diversity of our Associate force and the complexity of our Compensation Plan, it is difficult to predict how any changes to the plan will be viewed by Associates and whether such changes will achieve their desired results. In 2013, we made several changes to our product pricing structure and Associate Compensation Plan to improve our business, including to increase Associate loyalty and satisfaction and to attract new Associates. There can be no assurance that the foregoing changes, or any future changes, to our Associate Compensation Plan will allow us to successfully attract new Associates or retain existing Associates, nor can we assure that any changes we make to our Compensation Plan will achieve our desired results.

Additionally, the payment of Associate incentives under our Compensation Plan is our most significant expense. These incentives include commissions, bonuses, and certain awards and prizes. Adjusting or enhancing our Compensation Plan directly affects the incentives we pay as a percentage of net sales. We may periodically adjust our Compensation Plan to prevent Associate incentives from having a significant adverse effect on our earnings. There can be no assurance that changes to the Compensation Plan or product pricing will be successful in achieving target levels of Associate incentives as a percentage of net sales. Furthermore, such changes may make it difficult to attract and retain qualified and motivated Associates or cause us to lose some of our longer-standing Associates.

***Legal action by former Associates or third parties against us could harm our business.*** We continually monitor and review our Associates' compliance with our policies and procedures as well the laws and regulations applicable to our business. From time to time, some Associates fail to adhere to our policies and procedures. If this happens, we may take disciplinary action against the particular Associate. This disciplinary action is based on the facts and circumstances of the particular case and may include anything from warnings for minor violations to termination of an Associate's purchase and distribution rights for more serious violations. From time to time, we become involved in litigation with an Associate whose purchase and distribution rights have been terminated. We consider this type of litigation to be routine and incidental to our business. While neither the existence nor the outcome of this type of litigation is typically material to our business, in the past we have been involved in litigation of this nature that resulted in a large cash award against the Company. Our competitors have also been involved in this type of litigation, and in some cases class actions, where the result has been a large cash award against the competitor or a large cash settlement by the competitor. These types of challenges, awards or settlements could provide incentives for similar actions by other former Associates against us in the future. Any such challenge involving us or others in our industry could harm our business by resulting in fines or damages against us, creating adverse publicity about us or our industry, or hurting our ability to attract and retain customers. We believe that Associate compliance is critical to the integrity of our business, and, therefore, we will continue to be aggressive in ensuring that our Associates comply with our policies and procedures. As such, there can be no assurance that this type of litigation will not occur again in the future or result in an award or settlement that has a materially adverse effect on our business.

***The inability to obtain adequate supplies of raw materials for products at favorable prices, or at all, or the inability to obtain certain products from third-party suppliers, could have a material adverse effect on our business, financial condition, or results of operations.*** We acquire all of our raw materials for the manufacture of our products from third-party suppliers. Materials used in manufacturing our products

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are purchased through purchase order, often invoking pre-negotiated annual supply agreements. We have very few long-term agreements for the supply of these materials. We also contract with third-party manufacturers and suppliers for the production of some of our products, including most of our gelatin-capsuled supplements, Probiotic, Rev3 Energy Drink, our powdered drink mixes and nutrition bars, and certain of our personal care products. These third-party suppliers and manufacturers produce and, in most cases, package these products according to formulations that have been developed by, or in conjunction with, our in-house product development team. There is a risk that any of our suppliers or manufacturers could discontinue manufacturing our products or selling their products to us. Although we believe that we could establish alternate sources for most of our products, any delay in locating and establishing relationships with other sources could result in product shortages or back orders for products, with a resulting loss of net sales. In certain situations, we may be required to alter our products or to substitute different products from another source. We have, in the past, discontinued or temporarily stopped sales of certain products that were manufactured by third parties while those products were on back order. There can be no assurance that suppliers will provide the raw materials or manufactured products that are needed by us in the quantities that we request or at the prices that we are willing to pay. Because we do not control the actual production of certain raw materials and products, we are also subject to delays caused by any interruption in the production of these materials, based on conditions not within our control, including weather, crop conditions, transportation interruptions, strikes by supplier employees, and natural disasters or other catastrophic events.

***Shortages of raw materials may temporarily adversely affect our margins or our profitability related to the sale of those products.*** In the past, we have experienced temporary shortages of the raw materials used in certain of our nutritional products. Although we had identified multiple sources to supply such raw material ingredients, quantities of the materials we purchased during these shortages were at higher prices, which had a negative impact on our gross margins for those products. While we periodically experience price increases due to unexpected raw material shortages and other unanticipated events, we have been able to manage this by increasing the price at which we sell our products, therefore, this has historically not resulted in a material effect on our overall cost of goods sold. However, there is no assurance that our raw materials will not be significantly adversely affected in the future, causing our profitability to be reduced.

***Disruptions to shipping channels that we use to distribute our products to international warehouses may adversely affect our margins and profitability in those markets.*** In the past, we have felt the impact of disruptions to the shipping channels used to distribute our products. These disruptions have included increased port congestion, a lack of capacity on the railroads, and a shortage of manpower. Most recently, we experienced the impact of the West Coast port congestion that started late in 2014 due to worker strikes. In response to this congestion, we increased lead-times for shipments to our international markets, which caused an increase in our inventory levels. We also pursued alternative routes of transportation, which increased our shipping costs. Although the west coast ports are now fully functioning, we cannot assure you that we will not experience port congestion in the future. Congestion to ports can affect previously negotiated contracts with shipping companies, resulting in unexpected increases in shipping costs and reduction in our net sales.

***Nutritional supplement products may be supported by only limited availability of conclusive clinical studies.*** Our products include nutritional supplements that are made from vitamins, minerals, herbs, and other substances for which there is a long history of human consumption. Some of our products contain innovative ingredients or combinations of ingredients. Although we believe that all of our products are safe when taken as directed, there is little long-term experience with human consumption of certain of these product ingredients or combinations of ingredients in concentrated form. We conduct research and test the formulation and production of our products, but we have performed or sponsored only limited clinical studies. Furthermore, because we are highly dependent on consumers' perception of the efficacy, safety, and quality of our products, as well as similar products distributed by

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other companies, we could be adversely affected in the event that those products prove or are asserted to be ineffective or harmful to consumers or in the event of adverse publicity associated with any illness or other adverse effects resulting from consumers' use or misuse of our products or similar products of our competitors.

***Our business is subject to the risks associated with intense competition from larger, wealthier, and more established competitors.*** We face intense competition in the business of distributing and marketing nutritional supplements, vitamins and minerals, personal care products, and other nutritional products, as described in greater detail in "Business Competition." Numerous manufacturers, distributors, and retailers compete actively for consumers and, in the case of other network marketing companies, for Associates. There can be no assurance that we will be able to compete in this intensely competitive environment. In addition, nutrition and personal care products can be purchased in a wide variety of channels of distribution, including retail stores. Our product offerings in each product category are also relatively small, compared to the wide variety of products offered by many of our competitors.

We are also subject to significant competition from other network marketing organizations for the time, attention, and commitment of new and existing Associates. Our ability to remain competitive depends, in significant part, on our success in recruiting and retaining Associates. There can be no assurance that our programs for recruiting and retaining Associates will be successful. The pool of individuals who may be interested in network marketing is limited in each market, and it is reduced to the extent other network marketing companies successfully recruit these individuals into their businesses. Although we believe we offer an attractive opportunity for Associates, there can be no assurance that other network marketing companies will not be able to recruit our existing Associates or deplete the pool of potential Associates in a given market.

***Taxation and transfer pricing considerations affect our operations.*** In many countries, including the United States, we are subject to transfer pricing and other tax regulations that are designed to ensure that appropriate levels of income are reported by our U.S. and foreign entities and are taxed appropriately. Although we believe that we are in compliance with all material regulations and restrictions in this regard, we are subject to the risk that taxing authorities could audit our transfer pricing and related practices and assert that additional taxes are owed. We are also subject to the risk that taxing authorities in any of our markets could change the laws in a manner that may increase our effective tax rate and/or duties on our products. Under tax treaties, we are eligible to receive foreign tax credits in the United States for foreign taxes paid abroad. In the event any audits or assessments are concluded adversely to us, we may or may not be able to offset the consolidated effect of foreign income tax assessments through the use of U.S. foreign tax credits. Currently, we are utilizing all foreign tax credits in the year in which they arise. Because the laws and regulations governing U.S. foreign tax credits are complex and subject to periodic legislative amendment, we cannot be sure that we would in fact be able to take advantage of any foreign tax credits in the future. As a result, adverse outcomes in these matters could have a material impact on our financial condition or operating results.

***Our business is subject to particular intellectual property risks.*** Most of our products are not protected by patents. The labeling regulations governing our nutritional supplements require that the ingredients of such products be precisely and accurately indicated on product containers. Accordingly, patent protection for nutritional supplements often is impractical given the large number of manufacturers who produce nutritional supplements having many active ingredients in common. Additionally, the nutritional supplement industry is characterized by rapid change and frequent reformulations of products, as the body of scientific research and literature refines current understanding of the application and efficacy of certain substances and the interactions among various substances. In this respect, we maintain an active research and development program that is devoted to developing better, purer, and more effective formulations of our products. We protect our investment in research, as well as the techniques we use to improve the purity and effectiveness of our products,

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by relying on trade secret laws. We have also entered into confidentiality agreements with certain of our employees involved in research and development activities. Additionally, we endeavor to seek, to the fullest extent permitted by applicable law, trademark and trade dress protection for our products, which protection has been sought in the United States, Canada, and in many of the other countries in which we are either presently operating or plan to commence operations in the future. Notwithstanding our efforts, there can be no assurance that our efforts to protect our trade secrets and trademarks will be successful. Nor can there be any assurance that third-parties will not assert claims against us for infringement of their intellectual proprietary rights. If an infringement claim is asserted, we may be required to obtain a license of such rights, pay royalties on a retrospective or prospective basis, or terminate our manufacturing and marketing of our infringing products. Litigation with respect to such matters could result in substantial costs and diversion of management and other resources and could have a material adverse effect on our business, financial condition, or operating results.

***A failure of our information technology systems would harm our business.*** The global nature of our business and our seamless global compensation plan requires the development and implementation of robust and efficiently functioning information technology systems. Such systems are vulnerable to a variety of potential risks, including damage or interruption resulting from natural disasters and telecommunication failures and human error or intentional acts of sabotage, vandalism, break-ins and similar acts. Although we have adopted and implemented a business continuity and disaster recovery plan, which includes routine back-up, off-site archiving and storage, and certain redundancies, the occurrence of any of these events could result in costly interruptions or failures adversely affecting our business and the results of our operations.

***Security breaches and other disruptions could compromise our information and expose us to liability, which would cause our business and reputation to suffer.*** In the ordinary course of our business, we collect and store sensitive data, including intellectual property, our proprietary business information and that of our customers, suppliers and business partners, and personally identifiable information of our customers and employees, in our data centers and on our networks. The secure processing, maintenance and transmission of this information is critical to our operations and business strategy. Despite our security measures, our information technology and infrastructure may be vulnerable to attacks by hackers or breached due to employee error, malfeasance or other disruptions. Any such breach could compromise our networks and the information stored there could be accessed, publicly disclosed, lost or stolen. Any such access, disclosure or other loss of information could result in legal claims or proceedings, liability under laws that protect the privacy of personal information, and regulatory penalties, disrupt our operations, and damage our reputation, which could adversely affect our business, revenues and competitive position.

***We may incur liability under our "Athlete Guarantee" program, if and to the extent participating athletes make a successful claim against USANA for testing positive for certain banned substances while taking USANA nutritional supplements.*** USANA believes that its nutritional supplement products are free from substances that have been banned by world-class training and competitive athletic programs. We retain independent testing agencies to conduct periodic checks for banned substances. We further believe that, while our products promote good health, they are not otherwise considered to be "performance enhancing" as that term has been used in defining substances that are banned from use in international competition by the World Anti-Doping Agency ("WADA"). For many years, USANA has been a sponsor of Olympic athletes and professional competitors around the world. These athletes have been tested on many occasions and have never tested positive for banned substances as a result of taking USANA nutritional products. To back up our claim that athletes who use USANA products as part of their training regimen will not be consuming banned substances, we have offered to enter into agreements with select athletes, some of whom have high-profiles and are highly compensated, which state that, during the term of the agreement, should the athlete test positive for a banned substance included in the WADA, and should such positive result be the result of taking USANA nutritional

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products, we will compensate that athlete at an amount equal to two times their current annual earnings up to \$1.0 million dollars, based on the athlete's personal level of competition, endorsement, and other income, as well as other factors. To mitigate potential exposure under these agreements, we:

Designate lots identified as dedicated to the Athlete Guarantee program and retain additional samples;

Store designated lot samples externally with a third-party; and

Establish a chain of custody that requires signatures on behalf of USANA and the third-party to transfer possession of the product lots and that restricts access by USANA employees after the transfer.

All applicants to this Athlete Guarantee program are subject to screening and acceptance by the Company in its sole discretion. Contracts are tailored to fit the athlete's individual circumstances and the amount of our exposure is limited based on the level of sponsorship of the participating athlete. Although we believe that the pool of current and potential participants in the program is small, there is no guarantee that an athlete who is accepted in the program will not successfully make a claim against us. We currently have no insurance to protect us from potential claims under this program.

***The loss of key management personnel could adversely affect our business.*** Our executive officers are primarily responsible for our day-to-day operations, and we believe our success depends in part on our ability to retain our executive officers, to compensate our executive officers at attractive levels, and to continue to attract additional qualified individuals to our management team. We cannot guarantee continued service by our key executive officers. We do not maintain key man life insurance on any of our executive officers, nor do we have an employment agreement with any of our executive officers. The loss or limitation of the services of any of our executive officers or the inability to attract additional qualified management personnel could have a material adverse effect on our business, financial condition, or results of operations.

***Failure to maintain effective internal controls in accordance with the Sarbanes-Oxley Act of 2002 could negatively impact our business.*** We are required by federal securities laws to document and test our internal control procedures in order to satisfy the requirements of the Sarbanes-Oxley Act of 2002, which requires annual management assessments of the effectiveness of internal control over financial reporting. Effective internal controls are necessary for us to provide reliable financial reports and to effectively prevent fraud. The SEC, as directed by Section 404 of the Sarbanes-Oxley Act of 2002, adopted rules requiring public companies to include a report by management on the effectiveness of our internal control over financial reporting in the companies' Annual Reports on Form 10-K. In addition, our independent registered public accounting firm must report on the effectiveness of the internal control over financial reporting. Although we review internal control over financial reporting in order to ensure compliance with the Section 404 requirements, if we fail to maintain effective internal control over financial reporting, we could be required to take costly and time-consuming corrective measures, be required to restate the affected historical financial statements, be subjected to investigations and/or sanctions by federal and state securities regulators, and be subjected to civil lawsuits by security holders. Any of the foregoing could also cause investors to lose confidence in our reported financial information and in our company and would likely result in a decline in the market price of our stock and in our ability to raise additional financing if needed in the future.

***The beneficial ownership of a significant percentage of our common stock gives our founder and parties related to or affiliated with him effective control, and limits the influence of other shareholders on important policy and management issues.*** Gull Global, Ltd., an entity that is solely owned and controlled by our founder Dr. Wentz, owned 51.4% of our outstanding common stock at January 2, 2016. By virtue of this stock ownership, Dr. Wentz is able to exert significant influence over the election of the members of our Board of Directors and our business affairs. This concentration of ownership could also have the

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effect of delaying, deterring, or preventing a change in control that might otherwise be beneficial to shareholders. In addition, Dr. Wentz currently serves as Chairman of our Board of Directors and his son, David Wentz, is our Co-Chief Executive Officer. There can be no assurance that conflicts of interest will not arise with respect to these relationships or that conflicts will be resolved in a manner favorable to other shareholders of the Company.

***Sales by our shareholders of a substantial number of shares of our common stock in the public market could adversely affect the market price of our common stock.*** A large number of outstanding shares of our common stock are held by several of our principal shareholders. If any of these principal shareholders were to decide to sell large amounts of stock over a short period of time such sales could cause the market price of our common stock to decline.

***Our stock price has been volatile and subject to various market conditions.*** There can be no assurance that an active market in our stock will be sustained. The trading price of our common stock has been subject to wide fluctuations. We have a relatively small public float compared to the number of our shares outstanding. Accordingly, we cannot predict the extent to which investors' interest in our common stock will provide an active and liquid trading market. Due to our limited public float, we are vulnerable to investors taking a "short position" in our common stock, which is likely to have a depressing effect on the price of our common stock and add increased volatility to our trading market. The price of our common stock also may fluctuate in the future in response to quarter-to-quarter variations in operating results, material announcements by us or our competitors, governmental regulatory action, conditions in the nutritional supplement industry, negative publicity, or other events or factors, many of which are beyond our control. In addition, the stock market has historically experienced significant price and volume fluctuations, which have particularly affected the market prices of many dietary and nutritional supplement companies and which have, in certain cases, not had a strong correlation to the operating performance of these companies. Our operating results in future quarters may be below the expectations of securities analysts and investors. If that were to occur, the price of our common stock would likely decline, perhaps substantially.

**Item 1B. Unresolved Staff Comments**

None.

**Item 2. Properties**

*Corporate Headquarters*

Our world-wide corporate headquarters is a 354,000 square foot company-owned facility located in Salt Lake City, Utah. This facility includes space for manufacturing and quality control, distribution, administrative functions, and research and development.

*Additional Manufacturing*

We own a 31,000 square foot manufacturing facility in Tianjin, China, which is currently used to manufacture our Sensé products that are sold in China. The majority of our other China products are manufactured at leased facilities in this market.

In 2014, we began construction of a state-of-the-art manufacturing facility in China similar in size, potential capacity, and nature to our headquarters facility located in Salt Lake City, Utah. Construction of this facility is expected to be completed in the first part of 2016. Leases on the China facilities noted above will be terminated shortly following completion of our new facility, and all manufacturing and production activities in China will be transferred to our new facility. This new facility has been designed to provide for 10 to 20 years of growth in China.

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*Other Office and Distribution Warehouse Facilities*

We own a 45,000 square foot office/warehouse building in Sydney, Australia. In each of the remainder of our markets, we lease regional offices and distribution warehouses. Additionally, we lease retail centers for our operations in China and a packaging facility in Singapore, which fulfills orders for our MyHealthPak in our Asia Pacific markets.

We believe that the facilities referenced above are in good condition and are adequately utilized. Further, we believe that our current and planned manufacturing facilities provide for the productive capacity to meet our foreseeable needs.

**Item 3. Legal Proceedings**

Rawcliffe on behalf of USANA Health Sciences, Inc. v. Certain Directors and Officers of USANA

In August 2014, a purported shareholder derivative lawsuit was filed in the Third Judicial District Court of Salt Lake County, State of Utah (James Robert Rawcliffe v. Robert Anciaux, et al.) against certain of our directors and officers. The derivative complaint, which also names USANA as a nominal defendant but is asserted on USANA's behalf, contains claims of breach of fiduciary duty, waste of corporate assets and unjust enrichment against the defendant directors and officers in connection with certain equity awards granted by the Compensation Committee of the Company's Board of Directors in February 2014. In October 2014, we filed a motion to dismiss the complaint and, in March 2015, the court granted that motion and dismissed the complaint without prejudice. On May 6, 2015, the plaintiffs filed an appeal with the Utah Supreme Court. The Supreme Court remanded our case to the Utah Court of Appeals, which recently issued a briefing schedule for the parties. We believe that the claims in the complaint are without merit and will continue to vigorously defend this suit. We continue to believe, based on information currently available, that the final outcome of this suit will not have a material adverse effect on the Company's business, results of operations or consolidated financial position.

See also our discussion under Note I to the Condensed Consolidated Financial Statements included in Item 8 of Part II of this Annual Report on Form 10-K, which is incorporated herein by reference.

From time to time we are involved in litigation arising out of our operations. We maintain liability insurance, including product liability coverage, in amounts our management believes is adequate. We are not currently engaged in any legal proceedings that we expect would materially harm our business or financial condition.

**Item 4. Mine Safety Disclosures**

None.

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Our common stock trades on the New York Stock Exchange ("NYSE") under the symbol "USNA." The following table contains the reported high and low sales prices for our common stock as reported on the NYSE for the periods indicated:

<b>2014</b>	<b>High</b>	<b>Low</b>
First Quarter	\$ 78.35	\$ 55.01
Second Quarter	\$ 80.77	\$ 66.51
Third Quarter	\$ 80.86	\$ 63.22
Fourth Quarter	\$ 118.84	\$ 71.03

<b>2015</b>	<b>High</b>	<b>Low</b>
First Quarter	\$ 114.99	\$ 96.04
Second Quarter	\$ 145.05	\$ 112.83
Third Quarter	\$ 176.88	\$ 122.54
Fourth Quarter	\$ 140.58	\$ 103.35

The market price of our common shares is subject to fluctuations in response to variations in our quarterly operating results, general trends in the market for our products and product candidates, economic and currency exchange issues in the markets where we operate, as well as other factors, many of which are not within our control. In addition, broad market fluctuations, as well as general economic, business and political conditions may adversely affect the market for our common shares, regardless of our actual or projected performance.

On February 26, 2016, the high and low sales prices of our common stock as reported by NYSE were \$117.99 and \$110.90, respectively.

**Shareholders**

As of February 26, 2016, we had approximately 294 holders of record of our common stock.

**Dividends**

We have never declared or paid cash dividends on our common stock. Future cash dividends, if any, will be determined by our Board of Directors and will be based on earnings, available capital, our financial condition, and other factors that the Board of Directors deems to be relevant.

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Purchases made under our ongoing share repurchase program during the quarter ended January 2, 2016 are summarized in the following table:

**Issuer Purchases of Equity Securities**  
(amounts in thousands, except per share data)

Period	Total Number of Shares Purchased	Average Price Paid per Share	Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs	Approximate Dollar Value of Shares that May Yet Be Purchased Under the Plans or Programs*
Fiscal October (Oct. 4, 2015 through Nov. 7, 2015)	56	\$ 129.50	56	\$ 53,981
Fiscal November (Nov. 8, 2014 through Dec. 5, 2015)	401	\$ 134.55	401	\$ 0
Fiscal December (Dec. 6, 2015 through Jan. 2, 2016)	0	\$ 0.00	0	\$ 100,000
	457		457	

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\*

The Company's share repurchase plan has been ongoing since the fourth quarter of 2000, with the Company's Board of Directors periodically approving additional dollar amounts for share repurchases under the plan. The Company began the fourth quarter of 2015 with \$61,181, remaining under the plan. As announced in a publicly issued press release on December 8, 2015, the Board of Directors authorized \$100,000 for share repurchases under the plan. Subsequent to the year ended January 2, 2016 and through February 26, 2016, the Company repurchased and retired 553 shares for a total of \$64,610 pursuant to a preset trading plan meeting the requirements of Rule 10b5-1 under the Securities Exchange Act of 1934 as amended. There is no requirement for future share repurchases, and there currently is no expiration date on the approved repurchase amount.

**Stock Performance Graph**

The following graph and table compares the performance of our common stock to the S&P 500 Index and to a market-weighted index of four companies selected in good faith from our industry (the "Peer Group") over the last five years. The data shown assumes an investment on December 31, 2010, of \$100 and reinvestment of all dividends into additional shares of the same class of equity, if applicable to the stock or index.

Each of the companies included in the Peer Group markets or manufactures products similar to USANA's products or markets its products through a similar marketing channel. The Peer Group includes the following companies: Avon Products, Inc., NuSkin Enterprises, Inc., Herbalife Ltd., and Nature's Sunshine.

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**Cumulative Shareholder Return  
Dec. 2010 - Dec. 2015**

	<b>USNA</b>	<b>S&amp;P 500</b>	<b>Peer Group</b>
<b>Dec 10</b>	\$ 136	\$ 113	\$ 126
<b>Dec 11</b>	\$ 95	\$ 113	\$ 188
<b>Dec 12</b>	\$ 103	\$ 128	\$ 189
<b>Dec 13</b>	\$ 237	\$ 166	\$ 380
<b>Dec 14</b>	\$ 322	\$ 185	\$ 387
<b>Dec 15</b>	\$ 400	\$ 183	\$ 338

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The following selected consolidated financial data should be read in conjunction with "Management's Discussion and Analysis of Financial Condition and Results of Operations" and the Consolidated Financial Statements and related notes thereto that are included in this report.

	Fiscal Year(1)				
	2011	2012	2013	2014	2015
	(in thousands, except per share data)				
<b>Consolidated Statements of Earnings Data:</b>					
Net sales	\$ 581,939	\$ 648,726	\$ 718,175	\$ 790,471	\$ 918,499
Income taxes	26,726	31,993	37,557	39,017	47,917
Net earnings	\$ 50,752	\$ 66,433	\$ 79,024	\$ 76,636	\$ 94,672
<b>Earnings per common share:</b>					
Basic	\$ 3.30	\$ 4.57	\$ 5.77	\$ 5.80	\$ 7.44
Diluted	\$ 3.26	\$ 4.45	\$ 5.56	\$ 5.60	\$ 7.18
<b>Weighted-average common shares outstanding:</b>					
Basic	15,361	14,547	13,695	13,221	12,730
Diluted	15,574	14,923	14,204	13,689	13,177
<b>Percentage of Net Sales Data:</b>					
Gross profit	82.5%	82.1%	82.3%	82.2%	82.6%
Associate incentives	45.7%	43.2%	42.9%	44.2%	44.4%
Selling, general and administrative	23.6%	23.8%	23.1%	23.3%	22.8%
Effective tax rate	34.5%	32.5%	32.2%	33.7%	33.6%
<b>Dividends per share</b>					
<b>Cash Flow Related Data:</b>					
<b>Net cash provided by (used in):</b>					
Operating activities	\$ 70,108	\$ 92,805	\$ 98,893	\$ 105,185	\$ 111,466
Investing activities	(10,609)	(8,278)	(21,589)	(16,266)	(25,124)
Financing activities	(33,372)	(64,542)	(10,165)	(113,015)	(49,157)
Purchase of property and equipment	(10,643)	(8,432)	(8,051)	(20,421)	(23,729)
Repurchase of common stock	(33,459)	(68,294)	(18,085)	(138,819)	(61,181)

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	Dec. 31, 2011	Dec. 29, 2012	As of Dec. 28, 2013	Jan. 3, 2015	Jan. 2, 2016
(in thousands, except other data)					
<b>Consolidated Balance Sheet Data:</b>					
Cash and cash equivalents	\$ 50,353	\$ 70,839	\$ 137,343	\$ 111,126	\$ 143,210
Working capital	46,363	61,701	133,174	82,222	112,852
Total assets	244,496	267,355	368,470	350,584	423,237
Other long-term liabilities	942	938	1,211	1,114	1,151
Stockholders' equity	173,910	185,572	260,522	230,164	280,852
<b>Other Data:</b>					
Active Associates	222,000	247,000	265,000	349,000	421,000
Active Preferred Customers	64,000	64,000	78,000	81,000	89,000
<b>Total Active Customers</b>	<b>286,000</b>	<b>311,000</b>	<b>343,000</b>	<b>430,000</b>	<b>510,000</b>

- (1) The Company operates on a 52-53 week year, ending on the Saturday that is closest to December 31. Fiscal years 2011 through 2013, and 2015 were 52-week years. Fiscal year 2014 was a 53-week year.

**Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations**

The following discussion and analysis of USANA's financial condition and results of operations is presented in ten sections:

Overview

Customers

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This discussion and analysis should be read in conjunction with the Consolidated Financial Statements and notes thereto appearing elsewhere in this report.

**Overview**

We develop and manufacture high-quality, science-based nutritional and personal care products that are distributed internationally through a network marketing system, which is a form of direct selling. We have chosen this distribution method as we believe it is more conducive to meeting our vision as a company, which is improving the overall health and nutrition of individuals and families around the world. Our customer base includes two types of customers: "Associates" and "Preferred Customers." Associates share in our company vision by acting as independent distributors of our products in addition to purchasing our products for their personal use. Preferred Customers purchase our products strictly for their personal use and are not permitted to resell or to distribute the products.

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As of January 2, 2016, we had approximately 421,000 active Associates and approximately 89,000 active Preferred Customers worldwide.

We have ongoing operations in the following markets, which are grouped and presented as follows:

#### Asia Pacific

Greater China Hong Kong, Taiwan, and China<sup>(1)</sup>

Southeast Asia Pacific Australia, New Zealand, Singapore, Malaysia, the Philippines, Thailand, and Indonesia<sup>(2)</sup>

North Asia Japan and South Korea

Americas and Europe United States, Canada, Mexico, Colombia<sup>(3)</sup>, the United Kingdom, the Netherlands, France, and Belgium

Asia Pacific has largely driven our growth the last several years. Our most recent market expansions in this region include our entry into Indonesia in late 2015, Thailand in 2012 and our entry into China in 2010 through our acquisition of BabyCare. Since our acquisition of BabyCare, our strategy in Asia Pacific has been centered on generating growth in China. Consequently, our growth in Asia Pacific over the last few years has been led by China, and our results in Hong Kong, which had previously been our fastest growing market, have declined. Our Hong Kong market has now reached our projected size, in terms of customers and sales, and we anticipate modest organic growth for this market going forward. We also anticipate that China will continue to drive our growth in this region going forward, but expect our business to grow in most of our other markets in this region.

Americas and Europe is our most mature region. Our most recent market expansions in this region include our entry into Colombia in 2013. Americas and Europe has grown modestly over the last several years due to sales and customer growth in Canada and Mexico. Our results in the United States and our newest markets in this region, however, have not paralleled our success in Canada and Mexico. We believe that we have the appropriate strategies in place to generate growth in the United States and our newest markets and are optimistic about these markets going forward. We also anticipate that our growth in Canada and Mexico will continue in 2016.

Because we have operations in multiple markets, with sales and expenses being generated and incurred in multiple currencies, our reported U.S. dollar sales and earnings can be significantly affected by fluctuations in currency exchange rates. In general, our operating results are affected positively by a weakening of the U.S. dollar and negatively by a strengthening of the U.S. dollar. In 2015, net sales outside of the United States represented approximately 84.8% of consolidated net sales.

### **Customers**

Because we sell our products exclusively to a customer base of independent Associates and Preferred Customers, in order to increase net sales, we must either increase the number of, or the productivity of, our Associates and Preferred Customers. Increasing the productivity of our Associates and Preferred Customers has not been our primary focus. Rather, we seek to increase the number of Associates and Preferred Customers who use our products. We believe this focus is more consistent with our vision of improving the overall health and nutrition of individuals and families around the world. Sales to Associates account for the majority of our product sales, representing 92% of product sales during 2015. The remainder of our sales comes from Preferred Customers. Increases or decreases

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(1) Our business in China is that of BabyCare, our wholly-owned subsidiary.

(2) We commenced operations in Indonesia in the fourth quarter of 2015.

(3)

We commenced operations in Colombia in the third quarter of 2013.

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in product sales are typically the result of variations in the volume of product sold relating to fluctuations in the number of active Associates and Preferred Customers purchasing our products. The number of active Associates and Preferred Customers is, therefore, used by management as a key non-financial measure.

The tables below summarize the number of active customers and year-over-year percentage growth by geographic region as of the dates indicated (quarterly). These numbers have been rounded to the nearest thousand as of the dates indicated. For purposes of this report, we only count as active customers those Associates and Preferred Customers who have purchased from us at any time during the most recent three-month period as of the date indicated.

	<b>Active Associates by Region</b>							
	<b>April 4, 2015</b>		<b>July 4, 2015</b>		<b>October 3, 2015</b>		<b>January 2, 2016</b>	
<b>Asia Pacific:</b>								
Greater China	201,000	82.7%	216,000	72.8%	218,000	69.0%	234,000	34.5%
<b>Southeast Asia</b>								
Pacific	77,000	20.3%	79,000	17.9%	85,000	21.4%	86,000	8.9%
North Asia	12,000	33.3%	13,000	44.4%	13,000	30.0%	13,000	18.2%
<b>Asia Pacific Total</b>								
	290,000	58.5%	308,000	53.2%	316,000	51.2%	333,000	26.1%
<b>Americas and</b>								
Europe	86,000	4.9%	89,000	8.5%	89,000	8.5%	88,000	3.5%
<b>Total</b>								
	376,000	41.9%	397,000	40.3%	405,000	39.2%	421,000	20.6%

	<b>Active Preferred Customers by Region</b>							
	<b>April 4, 2015</b>		<b>July 4, 2015</b>		<b>October 3, 2015</b>		<b>January 2, 2016</b>	
<b>Asia Pacific:</b>								
Greater China	4,000	33.3%	4,000	33.3%	4,000	33.3%	4,000	33.3%
<b>Southeast Asia</b>								
Pacific	12,000	20.0%	12,000	9.1%	13,000	18.2%	13,000	8.3%
North Asia	7,000	75.0%	9,000	80.0%	9,000	50.0%	9,000	50.0%
<b>Asia Pacific Total</b>								
	23,000	35.3%	25,000	31.6%	26,000	30.0%	26,000	23.8%
<b>Americas and</b>								
Europe	63,000	3.3%	66,000	10.0%	63,000	10.5%	63,000	5.0%
<b>Total</b>								
	86,000	10.3%	91,000	15.2%	89,000	15.6%	89,000	9.9%

### **Current Focus and Recent Developments**

We have implemented the following strategies and initiatives to increase the number of Associates and Preferred Customers who use our products throughout the world and, thereby, further our company vision:

*Personalization:* Over the last few years, we have focused heavily on personalizing and improving our customers' experience with USANA.

In August 2015, we introduced our new "MySmart™Foods" line of products, which continues our philosophy and strategy of personalization. MySmart™Foods are science-based, healthy nutrition shakes, bars, boosters and flavor optimizers. We

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made MySmart™Foods available to our Associates for a limited time at our 2015 International Convention only, as a pre-launch opportunity to purchase and try the products. We intend to officially launch MySmart™Foods during the first half of 2016.

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We will continue to personalize each of our product lines going forward. In this regard, we have new product and technology launches planned for 2016 and 2017, which we believe will create a new foundation of personalization for USANA to build on as we go forward.

In 2014, we launched an all-new digital marketing suite for our world-wide Associates, which is designed to personalize and simplify conducting a USANA business. This suite provides our Associates with new tools, consisting of a back office hub, personal websites, and advanced communication and marketing tools, all of which enhance our Associates' ability to personalize, manage, promote and build their business in today's demanding e-business environment.

In 2013, we implemented several strategic changes to our business (referred to throughout this report as the "2013 strategic changes"), which were all aimed at promoting customer loyalty, enjoyment and success with USANA. These changes included: (i) simplification of our pricing structure, which included an overall 10% price reduction, while maintaining a price discount on products ordered through our monthly Auto Order program (collectively "price discounts"), (ii) a new reward based on the amount of a customer's initial product order to then be credited on their subsequent two Auto Orders, and (iii) increased payout under and simplification of our Compensation Plan.

We have experienced growth in several business indicators tied to the strategic changes that we implemented in 2013 and continued promoting in 2014 and 2015. These indicators include: active customer counts; world-wide unit volume; percent of sales processed through our Auto Order program; and the number of Associates earning a commission check.

*Market-Specific Strategies:* We have implemented market-specific strategies to facilitate growth and strengthen our business around the world.

In 2015, we continued our strategy to increase our brand-recognition to make it easier for our Associates to introduce USANA to customers. In this regard, we expanded our relationship with Dr. Mehmet Oz and became a Trusted Partner and Sponsor of *The Dr. Oz Show*. Under this partnership, USANA products are regularly featured on *The Dr. Oz Show*. This partnership has helped drive growth in our North America region by (i) increasing awareness and recognition of the USANA brand, and (ii) allowing viewers of *The Dr. Oz Show* to purchase USANA products via a direct link on *The Dr. Oz Show* website. We plan on continuing this partnership in 2016.

In late 2014, after we passed the anniversary of the 2013 strategic changes, we began offering short-term incentives and promotions for our Associates around the world to generate excitement and additional customer growth. One particular incentive that we offered in late 2014 and early 2015 increased compensation to Associates for sales generated by new Associates and accelerated our sales and customer growth during the fourth quarter of 2014 and the first half of 2015. We plan to continue offering market-specific incentives and promotions going forward to generate excitement in our business.

In 2013, we implemented a price reduction in several of our mature markets to make our products and business opportunity more equitable around the world. Although these price reductions initially impacted our net sales on a year-over-year basis, they have been successful in the past helping grow our active customer counts and net sales in these markets, where growth had been declining or flat for several years. We followed up this pricing initiative with a new worldwide policy to prohibit cross-border purchasing by our customers. We believe that it is in the best interest of the Company and of our customers to have customers purchase products that are approved and offered in their home market. While this policy had a short-term negative impact on net sales in 2013, these policies have strengthened our underlying business and have improved our opportunity for growth going forward.

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*Product Innovation and Information Technology:* Although we originally planned for significant increases in our investment in product and technology innovation to further our Company vision during 2015, much of this investment was delayed as we carefully acquired the necessary human resources. In 2016, we plan to continue to pursue these investment strategies as well as additional investments in our information technology systems and infrastructure to continue to improve our customers' experience with us and to prepare to become a much larger company. These investments will be reflected as both additional SG&A expense and capital expenditures.

*International Development:* Given the significant opportunity that exists in China, we plan to continue focusing significant time and resources on growing this market. Our efforts in this regard include finalizing our new state-of-the-art manufacturing and production facility in Beijing, which we anticipate will become operational during the first half of 2016. We continue to believe that significant growth opportunities exist in new international markets. During the fourth quarter of 2015 we commenced operations in Indonesia. Indonesia is our 20th market and we believe it offers a promising growth opportunity for us.

**Presentation**

Product sales along with the shipping and handling fees billed to our customers are recorded as revenue net of applicable sales discounts when the product is delivered, title has transferred, and the risk of loss passes to the customer. Payments received for undelivered products are recorded as deferred revenue and are included in other current liabilities. Also reflected in net sales is a provision for product returns and allowances, which is estimated based on our historical experience. Additionally, the Company collects a nominal annual renewal fee from Associates that is deferred on receipt and is recognized as income on a straight-line basis over a twelve-month period.

Cost of sales primarily consists of expenses related to raw materials, labor, quality assurance, and overhead costs that are all directly associated with the production and distribution of our products and sales materials, as well as duties and taxes that are associated with the import and export of our products. As our international sales increase as a percentage of net sales, cost of sales are increasingly affected by additional duties, freight, and other factors, such as changes in currency exchange rates.

Associate incentives expense includes all forms of commissions, and other incentives paid to our Associates. Incentives paid to Associates include bonuses earned, rewards from contests and promotions, and base commissions, which makes up the majority of our Associate incentives expense. Bonuses are paid out to Associates based on certain business-related criteria, total base commission earnings, and leadership level. Contests and promotions are offered as an incentive and reward to our Associates and are typically paid out only after an Associate achieves specific criteria. Base commissions are paid out on the sale of products. Associates earn their commissions based on sales volume points that are generated in their sales organization. Sales volume points are assigned to each commissionable product and comprise a certain percent of the product price. Items such as our starter kits and sales tools have no sales volume point value, and commissions are not paid on the sale of these items. Although insignificant to our financial statements, an Associate may earn commissions on sales volume points that are generated from personal purchases that are not considered to be part of their "Qualifying Sales." To be eligible to earn commissions, an Associate must reach a certain level of Qualifying Sales each month, which may include product that they use personally or that they resell to consumers. Associates do not earn commissions on their Qualifying Sales. Commissions paid to Associates on personal purchases are considered a sales discount and are reported as a reduction to our net sales.

Selling, general and administrative expenses include wages and benefits, depreciation and amortization, rents and utilities, Associate event costs, advertising, professional fees, marketing, and research and development expenses. Wages and benefits represent the largest component of selling,

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general and administrative expenses. Significant depreciation and amortization expense is incurred as a result of investments in physical facilities, computer and telecommunications equipment, and systems to support our international operations.

Sales to customers outside the United States are transacted in the respective local currencies and are translated to U.S. dollars at weighted-average currency exchange rates for each monthly accounting period to which they relate. Most of our raw material purchases from suppliers and our product purchases from third-party manufacturers are transacted in U.S. dollars. Consequently, our net sales and earnings are affected by changes in currency exchange rates. In general, our operating results are affected positively by a weakening U.S. dollar and negatively by a strengthening U.S. dollar. In our net sales discussions that follow, we approximate the impact of currency fluctuations on net sales by translating current year net sales at the average exchange rates in effect during the comparable prior year periods.

**Results of Operations**

The following table summarizes our consolidated operating results as a percent of net sales, respectively, for the years indicated:

	2013	2014	2015
<b>Consolidated Statements of Earnings Data:</b>			
Net sales	100.0%	100.0%	100.0%
Cost of sales			