



To Our Shareholders

In fiscal 2010, we continued to make progress toward our goal of long-term profitable growth. During the year, we invested in our brands, customer relationships, facilities, and people to drive success in developing, manufacturing, and distributing superior quality nutritional supplements. We strengthened our competitive and financial position and were pleased to return value to our shareholders in the form of two special dividends, each in the amount of \$0.50 per share, paid on August 28, 2009 and April 14, 2010.

We were encouraged with our net revenue growth during fiscal 2010. We grew our branded net sales 13.1% as compared to fiscal 2009. This growth more than offset the decline in our private label business during the same period. Overall net sales increased 7.4% in fiscal 2010 as compared to fiscal 2009. We recorded a significant increase in our gross profit and operating margins which we attribute, in part, to an increase in sales, an improved branded mix, lower raw material costs, and promotional and marketing efficiencies. As a result of these and other activities, we were able to maintain a strong net cash position at fiscal year-end and retain substantial financial flexibility with our untapped \$80 million credit facility.

During fiscal 2010, we maintained a solid level of marketing support for our key branded products. We deployed several new initiatives designed to maintain and build our Move Free customer base and strengthen our position in the intensely competitive joint care category. We also increased our marketing support behind our fast-growing MegaRed Krill Oil product. We are pleased to report that our MegaRed Krill Oil product now enjoys full mass market retail distribution following resolution of the supply issues we experienced in the first half of fiscal 2010.

We devoted considerable resources to new product development during fiscal 2010 and are excited about our new product pipeline for both branded and private label products. We continue to focus on domestic and export sales opportunities with our major customers, as demonstrated by our aggressive participation in multiple private label bidding processes.

With respect to our operations, we successfully underwent an intense Food and Drug Administration (FDA) audit of our facilities and processes under the new Dietary Supplement GMP regulations in September 2009. At its conclusion, the investigator did not issue a Form FDA 483, Notice of Adverse Findings. We also installed a major new packaging line in our tablet and capsule manufacturing facility, which further enhanced our ability to deliver superior quality product and excellent customer service at an extremely competitive cost.

During fiscal 2010, we evaluated several potential acquisition targets. While we were encouraged by the quantity of the transaction opportunities we reviewed, none of the potential acquisitions met our highly disciplined criteria. We remain committed to this initiative as a complement to our organic growth activities.

Looking forward, we expect the intense competitive pressures in our industry to continue. Nevertheless, we are confident in our growth prospects and our ability to compete in the long-term based on our strong brand portfolio, operational strengths, solid customer relationships, and, most importantly, our talented associates who represent the platform for our future success.

Finally, we thank our customers, suppliers, and you, our shareholders, for your confidence and support during the past year.

Sincerely,

A handwritten signature in black ink that reads "Ryan J. Wood". The signature is written in a cursive, flowing style.

SECURITIES AND EXCHANGE COMMISSION  
WASHINGTON, D.C. 20549

FORM 10-K

ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934  
For the fiscal year ended May 31, 2010

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:

001-14608

**SCHIFF NUTRITION INTERNATIONAL, INC.**

(Exact name of Registrant as specified in its charter)

<u>Delaware</u> (State or other jurisdiction of incorporation or organization)	<u>87-0563574</u> (I.R.S. Employer Identification No.)
<u>2002 South 5070 West Salt Lake City, Utah</u> (Address of principal executive offices)	<u>84104-4726</u> (Zip Code)

Registrant's telephone number, including area code:

(801) 975-5000

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

**Class A Common Stock, par value \$0.01 per share**

(Title of Class)

**New York Stock Exchange**

(Name of Exchange)

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

**None**

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

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

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

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

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

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

Large accelerated filer

Accelerated filer

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

Smaller reporting company

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

The aggregate market value of the voting and non-voting common equity held by non-affiliates of the registrant was approximately \$66,444,268 as of November 30, 2009, the last day of the registrant's second fiscal quarter, based upon the closing price on the New York Stock Exchange of \$5.50 for shares of the registrant's Class A common stock on November 30, 2009.

As of August 13, 2010 the registrant had outstanding 12,883,559 shares of Class A common stock and 14,973,148 shares of Class B common stock.

**DOCUMENTS INCORPORATED BY REFERENCE**

Portions of the registrant's Definitive Proxy Statement for its 2010 Annual Meeting of Shareholders, to be filed with the Securities and Exchange Commission no later than 120 days after the end of the registrant's fiscal year ended May 31, 2010, are incorporated by reference into Part III hereof.

## PART I

### Note on Forward-Looking Statements

*Certain statements made in this Annual Report on Form 10-K, including statements under the captions “Business,” “Risk Factors,” “Legal Proceedings,” and “Management’s Discussion and Analysis of Financial Condition and Results of Operations,” and elsewhere herein are “forward-looking statements” within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended, that are based on management’s beliefs and assumptions, current expectations, estimates and projections. Statements that are not historical facts, including without limitation statements which are preceded by, followed by or include the words “believes,” “anticipates,” “plans,” “expects,” “estimates,” “may,” “should,” “intends,” or similar expressions, are forward-looking statements. While we believe these assumptions, expectations, estimates and projections are reasonable, such statements are subject to risks and uncertainties, certain of which are beyond our control, and therefore, actual results may differ materially. The fact that some of the risks may be the same or similar to past reports we have filed with the Securities and Exchange Commission (“SEC”) means only that the risks are present in multiple periods. We believe that many of the risks detailed here are part of doing business in the industry in which we operate and compete and will likely be present in all periods reported. The fact that certain risks are endemic to the industry does not lessen their significance. Forward-looking statements only speak as of the date hereof and we do not undertake and expressly disclaim any obligation to update or release any revisions to any forward-looking statement whether as a result of new information, future events or otherwise, except as required by law. Important factors that may cause these forward-looking statements to be false or materially different from our current expectations include, but are not limited to, the factors discussed in Items 1, 1A, 3, 7 and 7A of this Annual Report. Industry data used throughout this report was obtained from industry publications and internal company estimates. While we believe such information to be reliable, its accuracy has not been independently verified and cannot be guaranteed.*

*You should carefully consider the risks described in this Annual Report on Form 10-K, including those set forth in “Item 1A-Risk Factors” below. Any of these risks could have a material adverse effect on our results of operations and financial condition.*

### ITEM 1. BUSINESS

#### General

Schiff Nutrition International, Inc. (“we,” “us,” or “our”) develops, manufactures, markets and distributes branded and private label vitamins, nutritional supplements and nutrition bars in the United States and throughout the world. We offer a broad range of capsules, tablets and nutrition bars. Our portfolio of recognized brands, including Schiff®, Move Free®, MegaRed® and Tiger’s Milk®, is marketed primarily through the mass market (including club) and, to a lesser extent, health food store distribution channels.

Our principal executive offices are located at 2002 South 5070 West, Salt Lake City, Utah 84104 and our telephone number is (801) 975-5000. We were incorporated in Delaware in 1996. Our corporate internet web site address is [www.schiffnutrition.com](http://www.schiffnutrition.com). We have included our internet web sites here and elsewhere only as an inactive textual reference. The information contained on the internet web sites is not incorporated by reference into this Annual Report on Form 10-K. We file our proxy statements, annual reports on Form 10-K, quarterly reports on Form 10-Q and current reports on Form 8-K, and all amendments thereto with the SEC. Electronic copies of our periodic reports and current reports, and any amendments to those reports, are available free of charge by accessing our corporate internet web site at [www.schiffnutrition.com](http://www.schiffnutrition.com), which provides a link to [www.sec.gov](http://www.sec.gov), the web site maintained by the SEC. The public may read and copy any materials we file with the SEC at the SEC’s Public Reference Room at 100 F Street, NE, Washington, DC 20549. The public may obtain information on the operation of the Public Reference Room by calling the SEC at 1-800-732-0330.

#### Industry Overview

According to the “Nutrition Business Journal,” the market for vitamins, minerals and supplements in the United States was estimated to be approximately \$26.9 billion in 2009. We believe that the market has reached its present size due to a number of factors, including:

- increased awareness of the health benefits of dietary supplements, especially as reports and medical research indicating a correlation between consumption of specific nutrients and better health continue to heighten public knowledge of the benefits of dietary supplements for health;
- a growing population of older Americans, with increased levels of education and discretionary income, who are more likely to consume dietary supplements and nutritional products, with an increasing interest in more proactively managing one’s own health needs;
- successful new product introductions in part due to new scientific findings; and

- a trend towards preventative measures and healthy living due, in part, to increasing health care costs, dissatisfaction with existing health care systems, and increasing acceptance of alternative/preventative care.

In recent years, nutritional supplement companies, analysts, publications and other industry sources have referenced a slower growth rate, particularly in terms of sales dollar growth, in the nutritional supplement industry. We believe that the slower growth rate is due in part to, among other factors, increased competition, including increasing competition from pharmaceutical and food companies, increased market and pricing competition, including from private label products, the general economic slowdown in the U.S., negative publicity regarding certain nutritional supplement ingredients and companies, and the general maturing of the industry.

Although specific data from the fragmented international markets is not readily available, we believe similar demographics, events and other trends affect the nutritional supplement market internationally.

### **Brands, Products and Distribution**

We market a broad line of specialty supplements, vitamins and minerals under the Schiff brand, which has been available to consumers for over 70 years. The Schiff brand emphasizes high quality and natural ingredients, primarily consisting of tablet, capsule and softgel product forms.

Our Schiff brand specialty supplements are designed to provide consumers with targeted support for their wellness efforts. Our specialty supplements include joint care products marketed under the Schiff brand, including our Move Free and Glucosamine products. Our Move Free product is one of the leading joint care products in the mass market channel. Move Free net sales were \$71.2 million, \$71.3 million and \$82.6 million, respectively, for fiscal 2010, 2009 and 2008 and represented 35%, 37% and 47%, respectively, of total net sales for fiscal 2010, 2009 and 2008. In addition, a significant portion of our private label business is comprised of joint care products. Our concentration in the Move Free brand and the joint care category is significant. We cannot assure you that Move Free or other of our products currently experiencing strong popularity will maintain sales levels over time. A significant decrease in Move Free or joint care category sales would have a material adverse effect on our results of operations and financial condition. Other specialty supplement products include:

- omega-3 products, such as MegaRed and Fish Oil;
- specialty products for men and women, such as Prostate Health and Folic Acid; and
- other specialty products, such as Melatonin Plus, Niacin and Lutein.

Our Schiff brand vitamin products are designed to provide consumers with essential vitamins and minerals as supplements to healthy diet and exercise. Schiff brand vitamin products include:

- multivitamins, such as Single Day;
- individual vitamins, such as Vitamin B, Vitamin C and Vitamin D; and
- minerals, such as Calcium and Iron.

The Schiff brand is marketed primarily in the mass market retail channel, with additional limited distribution in health food stores. Our products are sold domestically in leading retail outlets in all 50 states. Our mass market customers include:

- warehouse clubs, such as Costco, Sam's Club and BJ's;
- mass merchandisers, such as Wal-Mart and Target;
- drug stores, such as Walgreens, CVS and Rite Aid; and
- supermarkets, such as Fred Meyer, Giant, Kroger, Publix, Safeway, Stop & Shop, H-E-B and Raley's.

We also manufacture and distribute private label products for certain retail customers where we sell our branded products. Private label products are sold to key retailers for distribution under their store brand names. Private label products include specialty supplements, vitamins and minerals, such as joint care products, Vitamin B and Calcium Citrate. Private label business is highly competitive and price-sensitive, often subject to competitive bidding processes at the retailer's discretion, which could impact, potentially significantly, our overall net sales and profit margins. We service the health food market primarily through sales to leading health food retailers and distributors.

Our largest customers are Costco and Wal-Mart and our concentration in these two customers is significant. Combined, these two customers accounted for 72%, 76% and 74%, respectively, of total net sales for fiscal 2010, 2009 and 2008. We cannot assure you that either Costco or Wal-Mart will continue to be significant customers in the future. The loss of either Costco or Wal-Mart as a customer, or a significant reduction in purchase volume by Costco or Wal-Mart, would have a material adverse effect on our results of operations and financial condition.

We also export certain Schiff products, particularly in the joint care category, to various international markets. In certain countries where we have an existing relationship with a retailer, such as Costco, we sell our products directly to the retailer. We sell to independent distributors in countries where we do not have direct relationships with retailers. See Note 1 of the Notes to Consolidated Financial Statements for domestic and international net sales amounts. See “Item 1 – Business – Government Regulation” and “Item 1A – Risk Factors” for additional information relating to our export business.

We also market two lines of nutrition bar products under the Tiger’s Milk and Fi-Bar® brands. The Tiger’s Milk product line includes several nutrition bars that supply protein, vitamins and other essential nutrients with fewer calories than a traditional candy bar. The Fi-Bar product line is comprised of snack bars that are free of hydrogenated oils and trans fat, and are made with wholesome ingredients such as grains, oats, nuts and fruit, and coated with white, semi-sweet or milk chocolate. The Tiger’s Milk and Fi-Bar brands are intended to provide consumers with a healthy alternative to traditional snack foods and candy bars and are sold primarily through warehouse clubs, mass market retailers and convenience stores, with additional limited distribution in health food stores.

We believe our business, which consists of the aggregation of the foregoing product-based operating segments, represents our only reportable segment. See Item 7, “Management’s Discussion and Analysis of Financial Condition and Results of Operation,” and the notes to our consolidated financial statements in this Annual Report, for more information concerning reportable segments and the geographic areas and channels in which we conduct our business.

## **Sales and Marketing**

Our sales force consists of dedicated sales professionals who are assigned to specific accounts, classes of trade and/or geographic territories. These sales professionals work directly with retailers and distributors to increase knowledge of our products and general nutritional supplement benefits, solicit orders for our products, maximize our shelf presence and provide related product sales assistance. We also utilize brokers to sell our products in certain accounts and classes of trade.

We market our products using a mix of trade and consumer promotions; television, internet, newspaper and print media advertising; and consumer education efforts. Our advertising and marketing expenditures, excluding sales incentives reflected as reductions in net sales or increases in cost of goods sold, were \$20.2 million, \$20.4 million and \$18.0 million, respectively, for fiscal 2010, 2009 and 2008. Classification of promotional costs as a sales reduction or increase in cost of goods sold is required when the promotion effectively represents a price reduction or free goods.

During fiscal 2010, we maintained our focus on competitively supporting our core brands, particularly relating to our Schiff Move Free brand and other joint care products. Additionally, we allocated significant trade, consumer and advertising spending to support expanded distribution of MegaRed. We continued to employ television, internet, magazine and other media in fiscal 2010, along with several targeted public relations and sampling campaigns.

Another key component of our marketing strategy is to educate consumers and key influencer groups about our innovative and beneficial nutritional supplement products. We provide educational programs at conferences and trade, consumer and healthcare professional shows. Our web sites, including [www.schiffvitamins.com](http://www.schiffvitamins.com), [www.movefreeadvanced.com](http://www.movefreeadvanced.com), [www.schiffmegared.com](http://www.schiffmegared.com) and [www.tigersmilk.com](http://www.tigersmilk.com) also provide additional educational information to consumers, customers and healthcare professionals.

## **Product Research and Development**

We are committed to research and development to create safe and efficacious new products, develop product line extensions for existing products, and develop more effective and efficient means of processing ingredients for use in products. New product development and process improvements are important to the nutritional supplement industry to create new market opportunities, meet consumer demand and strengthen relationships with customers.

We maintain an extensive research library and employ a variety of industry relationships to identify new research and development projects offering health and wellness benefits. To support our research and development efforts, we maintain a staff of scientific and technical personnel, invest in formulation, processing and packaging development, perform product quality and stability studies, invest in product efficacy and safety studies, and conduct consumer market research to sample consumer opinions on product concepts, product design, packaging, advertising and marketing campaigns. For research and development initiatives, we conduct research and development in our own facility and with third parties. Product research and development expenses were \$4.7 million, \$4.3 million and \$4.3 million, respectively, for fiscal 2010, 2009 and 2008.

## **Manufacturing and Product Quality**

We manufacture the majority of our products in a capsule and tablet manufacturing facility in Salt Lake City, Utah, which also includes our main distribution center, our primary administrative offices and our nutrition bar manufacturing operations. Our Salt Lake City capsule and tablet facility is designed and operated to meet the current Good Manufacturing Practices (“GMPs”) as promulgated by the US FDA in 21 CFR Part III. In September 2009, we underwent our first Food and Drug Administration (“FDA”) inspection under the new Dietary Supplement GMP regulations. At its conclusion, the investigator did not issue a Form FDA 483, Notice of Adverse Findings.

We participate in the United States Pharmacopeia (“USP”) Dietary Supplement Verification Program, pursuant to which our manufacturing facility has been certified as being compliant with GMPs promulgated by USP. We are also registered with NSF International (“NSF”) as being certified compliant with NSF GMPs as set forth in NSF/ANSI Standard 173-2003, Dietary Supplements, Section 8. We also underwent a GMP inspection for Complementary Medicines by the Australian Therapeutic Goods Administration (“TGA”) in connection with our introduction of Move Free into Australia. We received GMP certification from the TGA in May of 2010.

Our manufacturing process generally consists of the following operations: (i) sourcing ingredients for products, (ii) testing and warehousing raw ingredients, (iii) measuring ingredients for inclusion in such products, (iv) granulating, blending and grinding ingredients into a mixture with a homogeneous consistency, (v) encapsulating, tableting, pouring, pouching, bagging or boxing the blended mixture into the appropriate dosage form using either automatic or semiautomatic equipment, and (vi) testing finished products prior to distribution.

Our bottling and packaging, counting, check weighing and filling operations are automated to promote accuracy and compliance with weights and measures regulations. We have invested in production line flexibility to accommodate various filling sizes, weights or counts of product and final shipped unit configurations to fulfill customer and ultimate consumer needs. The distribution center features a high-rise racked warehouse and a fully automated “order-pick” system using optical readers that interpret bar coded labels on each shipping container.

We maintain and operate a Manufacturing Resource Planning (“MRP”) system that is integrated with distribution, warehousing and quality control, which provides real-time lot and quality tracking of raw materials, work in progress and finished goods. We manufactured approximately 85% of products we sold in fiscal 2010, based on net sales. By manufacturing the majority of our own products, we believe that we maintain better control over product quality and availability, while also reducing production costs. We also have a working relationship with numerous outside manufacturers, including softgel and tablet manufacturers and packagers, and utilize these outside sources from time to time. Manufacturing backlogs, to the extent they may occasionally exist, do not have a material impact on delivery time to the customer.

Our quality management systems are detailed and comprehensive, and include a supplier selection and certification process, raw material verification, analytical testing, weight deviation measurement, facility and process audits, and other procedures. The quality management systems also include a professionally equipped and staffed laboratory, enabling analysis of raw materials and finished goods for compliance to specifications. Our products are also subject to extensive shelf life stability testing through which we determine the effects of aging on our products. Outside laboratories are used routinely to evaluate our internal test laboratory performance and to supplement our internal testing procedures and capabilities.

We employ a purchasing staff that works with marketing, product development and quality control personnel to source raw materials for our products. Raw materials are sourced principally from China and the United States. We seek to mitigate the risk of a shortage of raw materials through our relationships with our principal suppliers, including identification and qualification of alternative suppliers for the same, or similar, raw materials where available.

We have long-term supply and license agreements with our third-party suppliers for a key ingredient used in our Move Free product and for the key ingredient used in our MegaRed product. While we have contracts in place providing for the continuing supply of these ingredients, we cannot assure you that the suppliers will continue to supply these ingredients in the quantities or on the terms we require, or at all. See “Item 1 – Business – Intellectual Property.” The failure of one or both of these suppliers to deliver will impact our net sales and profit margins and may damage our reputation with our customers, which could have a material adverse effect on our results of operations and financial condition. We cannot guarantee that we will be able to secure alternate suppliers to provide these ingredients on terms acceptable to us, or at all.

## **Competition**

The market for the sale of nutritional supplements is highly fragmented and competitive. We believe that competition is based principally upon price, quality and efficacy of products, customer service, brand name and marketing and trade support, and successful new product introductions.

Our competition includes numerous nutritional supplement companies that are highly fragmented in terms of geographic market coverage, distribution channels and product categories. In addition, large pharmaceutical companies and packaged food and beverage companies compete with us in the nutritional supplement market. These companies and certain nutritional supplement companies have broader product lines and/or larger sales volumes than us and have greater financial and other resources available to them and possess extensive manufacturing, distribution and marketing capabilities. Other companies are able to compete more effectively due to a greater extent of vertical integration. Private label products of our customers, which in recent years have significantly increased in certain nutrition categories (including the joint care and omega-3 categories), compete directly with our products. In several product categories, private label items are the market share leaders. Increased competition from such companies, including private label pressures, particularly relating to the joint care and omega-3 categories, could have a material adverse effect on our results of operations and financial condition.

Many companies within the industry are privately-held. Therefore, we are unable to assess the size of all of our competitors or where we rank in comparison to such privately-held competitors with respect to sales to retailers. As the nutritional supplement industry continues to evolve, we believe retailers will align themselves with suppliers who are financially stable, market a broad portfolio of products, provide exceptional quality assurance and offer superior customer service. We believe that we compete favorably with other nutritional supplement companies because of our financial stability, brand names, customer service, competitive pricing, sales and marketing support and quality of our product lines.

## **Government Regulation**

The formulation, manufacturing, packaging, labeling, advertising, distribution and sale of our products are subject to the laws and regulations of federal governmental agencies, including the Food and Drug Administration (“FDA”), the Federal Trade Commission (“FTC”), the U.S. Department of Agriculture, the U.S. Consumer Products Safety Commission, the Environmental Protection Agency and the Postal Service, and also various agencies of the states, localities and countries in which we operate and sell our products.

The FDA regulates foods and dietary supplements through the Food, Drug and Cosmetic Act (“FDCA”) and amendments thereto, including the Dietary Supplement Health and Education Act of 1994, as amended (“DSHEA”), which is intended to promote access to safe, quality dietary supplements and information about dietary supplements. DSHEA establishes a statutory class of dietary supplements, including vitamins, minerals, herbs, amino acids and other dietary substances for human use to supplement the diet, as well as concentrates, metabolites, extracts or combinations of such dietary ingredients. Generally, under DSHEA, dietary ingredients on the market before October 15, 1994 may be used without further notification to the FDA. However, dietary ingredients not marketed prior to October 15, 1994 may be “new dietary ingredients” under DSHEA and may require a submission to the FDA at least 75 days prior to marketing such ingredient evidencing a history of use or other evidence of safety to establish that the ingredient will reasonably be expected to be safe. We cannot assure you that the FDA will accept the evidence of safety for any new dietary ingredients that we may want to market, and the FDA’s refusal to accept such evidence could prevent the marketing of such dietary ingredients. In addition, increased FDA enforcement could lead the FDA to challenge dietary ingredients already on the market as “illegal” under the FDCA because of the failure to file a new dietary ingredient notification.

DSHEA permits statements of “nutritional support” for dietary supplements that may describe how particular dietary ingredients affect the structure, function or general well-being of the body or describe the mechanism of action by which dietary ingredients affect the foregoing. These statements of nutritional support, or “structure/function claims,” may not make a health claim or disease claim, meaning that a statement may not claim to diagnose, treat, prevent, cure or mitigate an illness or disease unless the claim was authorized by the FDA. A structure/function claim in advertising or on a product label must have substantiation that the claim is truthful and not misleading, and have a disclaimer that the statement has not been evaluated by the FDA and that the product is not intended to diagnose, treat, cure or prevent any disease. We cannot assure you that a regulatory agency, court or other third party will not deem one or more of our product claims or labels to be impermissible and take adverse action against us.

In addition, DSHEA provides that certain “third-party literature,” such as a reprint of a peer-reviewed scientific publication linking a particular dietary ingredient with health benefits, may be used “in connection with the sale of a dietary supplement to consumers” without the literature being subject to the same regulation as labeling. Such literature must not be false or misleading; the literature may not “promote” a particular manufacturer or brand of dietary supplement; and a balanced view of the available scientific information on the subject matter must be presented. We cannot assure you that all third-party literature that we would like to disseminate in connection with our products will satisfy each of these requirements, and failure to satisfy all requirements could prevent use of the literature or subject us to adverse actions by regulatory agencies or other third parties.

In June 2007, the FDA published final GMPs specifically for the dietary supplement industry. The effective compliance date for companies like ours with fewer than 500 employees was June 22, 2009. These GMPs are more detailed than the GMPs previously applicable to us and result in increased expenses, changes to our processes or products and/or implementation of additional recordkeeping and administrative procedures. Among other things, these GMPs: (i) require identity testing on all incoming dietary ingredients, (ii) call for a “scientifically valid system” for ensuring finished products meet all specifications, (iii) include requirements related to process controls, including statistical sampling of finished batches for testing and requirements for written

procedures, and (iv) require extensive recordkeeping. We do not currently expect the incremental cost of ongoing compliance efforts to be material.

In September of 2009 we underwent our first FDA inspection under the new Dietary Supplement GMP regulations. At conclusion, the investigator did not issue a Form FDA 483, Notice of Adverse Findings. While we believe we are currently in compliance with the GMPs, there can be no assurance that our operations or those of our suppliers will be in compliance in all respects at all times. Additionally, there is a potential risk of increased audits as the FDA and other regulators seek to ensure compliance with the GMPs.

In December 2006, Congress passed legislation requiring companies that manufacture or distribute over-the-counter (“OTC”) products or dietary supplements to report serious adverse events allegedly associated with their products to the FDA and institute recordkeeping procedures for all alleged adverse events (serious and non-serious). The legislation requires manufacturers and distributors of OTC products or dietary supplements to report to the FDA any serious adverse event reports received, even if the party making the report provides no medical or other information to the manufacturer or distributor. There is a risk that consumers, the press or government regulators could misinterpret adverse event reports as evidence of causation by the ingredient or product complained of, which could lead to consumer confusion, damage to our reputation, additional regulations, banned or recalled ingredients or products, increased insurance costs and a potential increase in product liability litigation, among other things. Any of the foregoing could have a material adverse effect on our results of operations and financial condition.

Although most of our products are classified as dietary supplements, some of our products are conventional foods, which are also subject to the Nutrition Labeling and Education Act of 1990 (“NLEA”). The NLEA also prohibits health claims being made for a food without prior FDA approval and establishes requirements for ingredient and nutrition labeling.

The FTC exercises jurisdiction over the advertising of nutritional and dietary supplements under the Federal Trade Commission Act. In November 1998, the FTC published an advertising guideline for the dietary supplement industry entitled “Dietary Supplements: An Advertising Guide for Industry.” These guidelines reiterate many of the policies regarding dietary supplements the FTC has periodically announced over the years, particularly with respect to the substantiation of claims made in advertising of dietary supplement products. In the past several years, the FTC has instituted several enforcement actions against dietary supplement companies alleging false and misleading advertising of certain products. These enforcement actions have resulted in consent decrees and/or the payment of fines by certain of the companies involved. We entered into a consent decree with the FTC effective November 2000 governing diet and weight loss claims and certain disease, safety and comparative health benefit claims.

The National Advertising Division (“NAD”) of the Council of Better Business Bureaus oversees an industry-sponsored self-regulatory system that permits competitors to resolve disputes over advertising claims. The NAD also has its own advertising monitoring program, and initiates its own challenges to advertising that it has reviewed. The NAD has no enforcement authority of its own, but may refer matters that the NAD views as violating FTC rules, regulations or guidance to the FTC for further action. In February 2009, we revised our MegaRed packaging, advertising, promotional materials and website to comply with the NAD’s recommendations arising from a competitive challenge. We cannot assure you that in the future the NAD will not deem one or more of our advertising claims to be impermissible.

Federal agencies, primarily the FDA and FTC, have a variety of procedures and enforcement remedies available to them, including initiating investigations, issuing warning letters and cease and desist orders, requiring reformulation of products, requiring corrective labeling or advertising, requiring consumer redress (for example, requiring that a company offer to repurchase products previously sold to consumers), seeking injunctive relief or product seizures, and imposing civil penalties or commencing criminal prosecution. In addition, certain state agencies have similar authority. These federal and state agencies have in the past used these remedies in regulating participants in the dietary supplement industry. In addition, the FDA has been able to generate a significant amount of media coverage when concerned about an ingredient or product. When the media covers such a story, the reputation of a company, product or ingredient may be seriously damaged, even if the information provided is incomplete or incorrect.

Our international activities are subject to regulation in each country in which we sell or distribute our products. In markets outside the United States, before commencing operations or marketing our products, we may be required to obtain approvals, licenses or certifications from a country’s ministry of health or comparable agency. Approvals or licensing may be conditioned on reformulation of products or may be unavailable with respect to certain products or product ingredients. We must also comply with product labeling and packaging regulations that vary from country to country. Furthermore, the regulations of these countries may conflict with those in the United States and with each other, sometimes causing higher costs and expenses, product reformulations, and delay. In countries in which we do not have direct relationships with retailers, independent distributors generally have responsibility for compliance with applicable foreign laws and regulations. These distributors are independent contractors over whom we have limited control.

As a result of our efforts to comply with applicable statutes and regulations, from time to time we have reformulated, eliminated or relabeled certain of our products and revised certain aspects of our sales, marketing and advertising programs. We cannot assure

you that we will not have to make such changes or revisions in the future, which could have a material adverse effect on our results of operations and financial condition.

We may be subject to additional laws or regulations by the FDA or other federal, state, county, local or foreign regulatory authorities, the repeal of laws or regulations which we consider favorable, such as DSHEA, or more stringent interpretations of current laws or regulations, from time to time in the future. There has recently been several new laws proposed at the federal level that would be unfavorable to the dietary supplement industry and our company, if enacted as proposed. We are unable to predict the nature of such future laws, regulations, interpretations or applications, nor can we predict what effect additional governmental regulations, legal proceedings or administrative orders, when and if promulgated or initiated, would have on our business in the future. Such changes could, however, require the reformulation of certain products to meet new standards, the recall or discontinuance of certain products not able to be reformulated, additional recordkeeping requirements, expanded documentation of the properties of certain products, new or different labeling, additional scientific substantiation, additional personnel, or new or additional processes, procedures or requirements. Any or all of such changes or requirements and the related costs to comply with such changes or requirements could have a material adverse affect on our results of operations and financial condition.

## **Intellectual Property**

We own, or have filed for, over 50 trademarks registered with the United States Patent and Trademark Office for our Schiff and Tiger's Milk brands and certain of our products (including Move Free and MegaRed) and slogans. We also license rights for names material to our business, including Move Free, and for the use of our brand names, including Schiff and Tiger's Milk, in certain countries outside of North America. However, the protection available in foreign jurisdictions may not be as extensive as the protection available to us in the United States.

We rely on common law trademark rights to protect our unregistered trademarks. Common law trademark rights do not provide us with the same level of protection as afforded by a United States federal registration of a trademark. In addition, common law trademark rights are limited to the geographic area in which the trademark is actually used.

Our Move Free product contains a key ingredient, the rights for which we license from a third-party supplier pursuant to a long-term supply and license agreement. The term of the agreement extends through May 29, 2014, with automatic one-year extensions unless terminated by us or by the supplier upon our breach of the agreement and failure to cure the breach within a prescribed time period. Our supplier has patents and patents pending relating to the key ingredient, and has granted us non-exclusive rights to market and sell the ingredient for joint care purposes in certain territories and classes of trade. We cannot assure you that our supplier will prevail in preventing third parties from selling the key ingredient in their competing products at a lower cost. This could have a material adverse effect on our results of operations and financial condition.

Our MegaRed product contains a key ingredient, the rights for which we license from a third-party supplier pursuant to a long-term sales agreement. The term of the agreement extends through August 31, 2012, with automatic one-year extensions unless we or the supplier gives six months notice of non-renewal. The agreement may be terminated upon a party's breach of the agreement and failure to cure the breach within a prescribed time period. Our supplier has patents and patents pending relating to the key ingredient, and has granted us non-exclusive rights to market and sell the ingredient in certain territories and classes of trade. We cannot assure you that our supplier will prevail in preventing third parties from selling the key ingredient in their competing products at a lower cost. This could have a material adverse effect on our results of operations and financial condition.

## **Employees**

At May 31, 2010, we employed 464 persons, of whom 195 were in management, sales, purchasing, logistics and administration and 269 were in manufacturing operations. In addition, we utilize temporary employees in some of our manufacturing operations. We are not party to any collective bargaining arrangements and believe that our relationship with our employees is good.

## **ITEM 1A. RISK FACTORS**

***A significant portion of our total net sales are dependent upon our Move Free product and the joint care category, and a significant decrease in sales of these products would have a material adverse effect on our results of operations and financial condition.*** Certain products and product lines (particularly in the joint care category) account for a significant amount of our total net sales. Net sales of our Schiff Move Free brand were 35%, 37% and 47%, respectively, of total net sales for fiscal 2010, 2009 and 2008. In addition, a significant portion of our private label business is comprised of joint care products. We cannot assure you that Move Free or other of our products currently experiencing strong popularity will maintain sales or margin levels over time. A significant decrease in Move Free or joint care category sales would have a material adverse effect on our results of operations and financial condition.

***Two of our customers account for a substantial portion of our net sales, and the loss of one or both of these customers would have a material adverse effect on our results of operations and financial condition.*** Our largest customers are Costco and Wal-

Mart. Combined, these two customers accounted for 72%, 76% and 74%, respectively, of total net sales for fiscal 2010, 2009 and 2008. Our concentration in these customers has generally increased in recent years. We do not have supply contracts for most of our sales to Costco and Wal-Mart and therefore cannot assure you that either Costco or Wal-Mart will continue to be significant customers in the future. The loss of either Costco or Wal-Mart as a customer, or a significant reduction in purchase volume by Costco or Wal-Mart, would have a material adverse effect on our results of operations and financial condition.

***Unfavorable publicity or consumer perception of our products and any similar products distributed by other companies could have a material adverse effect on our results of operations and financial condition.*** We believe sales of our products are highly dependent on consumer perception of the safety, quality and efficacy of our products as well as similar or other nutritional supplement products distributed and sold by other companies. Consumer perception of our products can be significantly influenced by scientific research or findings, regulatory investigations, litigation, national media attention, and other publicity regarding our products and other nutritional supplements, including publicity regarding the legality, safety or quality of particular ingredients or products or the nutritional supplement market in general. From time to time, there is unfavorable publicity, scientific research, litigation, regulatory proceedings and other media attention regarding our industry. There has recently been unfavorable publicity regarding FDA action against nutrition companies based on adverse events alleged to be caused by products sold by these companies. In recent years, there has also been unfavorable publicity regarding items imported from China, where we source a large amount of our raw materials. There can be no assurance that future publicity, scientific research or findings, litigation, regulatory proceedings, or media attention will be favorable to the nutritional supplement market or any particular product or ingredient, or consistent with earlier favorable publicity, research, findings, litigation, proceedings or media attention. Adverse publicity, media attention, research, findings, litigation, proceedings or other reports, whether or not accurate, could have a material adverse effect on our results of operations and financial condition and may lead to increased scrutiny of our operations by federal, state or other regulatory agencies, requiring further management attention and potential legal fees and other expenses. In addition, adverse publicity, reports or other media attention regarding the safety, quality, or efficacy of our products or ingredients or nutritional supplement products or ingredients in general, or associating the consumption of our products or ingredients or nutritional supplement products or ingredients in general with illness or other adverse effects, whether or not scientifically supported or accurate, could have a material adverse effect on our results of operations and financial condition.

***We operate in a highly competitive industry, in which increased competition and pricing pressures could have a material adverse effect on our results of operations and financial condition.*** The market for the sale of nutritional supplements is highly competitive. Many of our principal competitors have greater financial and other resources available to them and possess extensive manufacturing, distribution and marketing capabilities. Other competitors are vertically integrated to a greater extent. Additional national or international companies may enter or increase their presence (through acquisition or organic growth) in our industry. Private label products of our customers, the number of which in recent years has significantly increased in certain nutrition categories (including joint care), also create significant pricing pressure and competition with our products. Because nutritional supplements can be purchased in various channels of distribution, we also compete with products sold outside of the mass market retail channel, including health food stores, direct sales, direct mail and internet distribution channels. Increased competition from competitors, including expansion of private label products, or increased pricing pressure, could have a material adverse effect on our results of operations and financial condition.

Among other factors, competition among manufacturers, distributors and retailers of nutritional supplements is based upon price. Because of the high degree of price competition, we generally have not been able to pass on increases in raw material prices to our customers. If one or more of our competitors significantly reduce their prices in order to gain market share (particularly relating to the joint care and omega-3 categories), or if raw material prices increase and we are unable to pass along the increased cost to our customers (particularly relating to the joint care and omega-3 categories), our results of operations and financial condition could be materially adversely affected.

***Increased private label bidding activity could negatively impact sales and profit margins, potentially significantly.*** We manufacture and distribute private label (store brand) products for certain retail customers where we sell branded products. There has recently been a significant increase in bidding activity for the manufacture of private label dietary supplements distributed in mass market retail accounts. The increasingly competitive bidding activity began in January 2010 and is expected to continue. As a result of the bidding process, we no longer manufacture a product that represented a significant portion of our private label business. We expect to continue to participate in the bidding processes for products we believe will contribute to the success of our business. We cannot predict at this time how many new products we will win, how many existing products we will lose or the net effect on sales and profit margins. We believe that the bidding processes could negatively impact sales and profit margins, potentially significantly, though we cannot at this time quantify the magnitude of this impact.

***Increases in prices of raw materials could have a material adverse effect on our results of operations and financial condition.*** Raw materials account for a significant portion of our manufacturing costs. We have encountered material fluctuations in the pricing of key raw materials in the past, particularly relating to joint care category products. In recent years, we experienced margin volatility due to several factors, including significant raw material pricing increases in the joint care category. Beginning in late fiscal 2008 and continuing into fiscal 2009, the prices of raw materials (particularly those sourced from China, including many joint care category ingredients) increased and significantly impacted our profit margins. Historically, we generally have not been

able to pass along raw material price increases. Significant increases in raw material prices, particularly relating to the joint care and omega-3 categories, could have a material adverse effect on our results of operations and financial condition.

***We are dependent on third-party suppliers.*** We acquire all of our raw materials for the manufacture of our products from third parties. A considerable portion of our raw materials relates to our joint care category, which accounts for a significant amount of our total net sales. We cannot assure you that suppliers will provide the raw materials we need in the quantities requested, at a price we are willing to pay or that meet our quality standards and labeling requirements. This could cause product shortages and back orders, damaging our reputation and resulting in a loss of net sales and profitability.

We typically do not enter into long-term contracts with our suppliers. However, we have long-term supply and license agreements with third-party suppliers for key ingredients used in our Move Free and MegaRed products. While the contracts provide for the continuing supply of these ingredients, we cannot assure you that the suppliers will continue to supply these ingredients in the quantities or on the terms we require, or at all. See “Item 1 – Business – Intellectual Property.”

In addition, from time to time, we enter into forward purchase commitments regarding certain raw materials, primarily relating to the joint care category. We cannot assure you that the suppliers will supply the raw materials in accordance with the terms of the forward purchase commitments, or at all. For certain ingredients, we do not have alternate suppliers. Any significant failure to supply or changes in the material terms of supply by the Move Free and MegaRed key ingredient suppliers or our other raw materials suppliers, could have a material adverse effect on our results of operations and financial condition.

We are subject to potential delays in the delivery of raw materials caused by events beyond our control, including, among other factors, strikes or labor disputes, transportation interruptions, capacity issues at supplier factories, weather-related events, natural disasters or other catastrophic events, and changes in government regulations. Any significant delay in or disruption of the supply of raw materials could, among other things, substantially increase the cost of such materials, require reformulation or repackaging of products, require the qualification of new suppliers, or result in our inability to meet customer demands for certain products. The occurrence of any of the foregoing, particularly with respect to raw materials needed for our joint care products, could have a material adverse effect on our results of operations and financial condition.

***We acquire a significant amount of key ingredients for our products from foreign suppliers, and may be negatively affected by the risks associated with international trade and importation issues.*** We acquire a significant amount of key ingredients for a number of our products (particularly joint care products) from suppliers outside of the United States, particularly China. Accordingly, the acquisition of these ingredients is subject to the risks generally associated with importing raw materials, including, among other factors, delays in shipments, changes in economic and political conditions, quality assurance, nonconformity to specifications or laws and regulations, tariffs, trade disputes and foreign currency fluctuations. While we have a supplier certification program and periodically audit and inspect our suppliers’ facilities both in the United States and internationally, we cannot assure you that raw materials received from suppliers outside of the United States will conform to all specifications, laws and regulations. There has in the past been quality and safety issues with certain items imported from China, where we source a large amount of our raw materials. We may incur additional expenses and experience shipment delays due to preventative measures adopted by the Chinese and U.S. governments, our suppliers and our company.

In addition, the discovery of Bovine Spongiform Encephalopathy, commonly referred to as “mad cow disease,” in a country from which we obtain a significant amount of our raw materials (particularly related to the joint care category) derived from bovine sources could prevent us from purchasing such raw materials in the required quantities, at an acceptable price or at all. The occurrence of any of the foregoing, particularly with respect to raw materials needed for our joint care products, could have a material adverse effect on our results of operations and financial condition.

***Our inability or failure to protect our intellectual property and proprietary techniques or our infringement of others’ intellectual property could have a material adverse effect on our results of operations and financial condition.*** Although the nutritional supplement industry has historically been characterized by products with naturally occurring ingredients in capsule or tablet form, it has become more common for suppliers and competitors to apply for patents or develop proprietary technologies and processes. Although we make efforts not to infringe the intellectual property rights of others, there can be no assurance that third parties will not assert intellectual property infringement claims against us or our intellectual property licensors. Such claims of intellectual property infringement may require us to enter into costly royalty or license agreements, which we may be unable to obtain on terms acceptable to us or at all. These claims could also be costly, could cause reputational injury and could divert the attention of management and key personnel. To the extent that these developments prevent us from, or increase the cost of, offering or supplying competitive products or our licensed proprietary ingredient in the marketplace, or result in litigation or threatened litigation against us related to alleged or actual infringement of third-party rights, this could have a material adverse effect on our results of operations and financial condition.

We protect our intellectual property related to investments in research and development by relying on trade secret laws and confidentiality agreements with third parties who have access to information about our research and development activities. When we license our trademarks, proprietary ingredients or other intellectual property from a third party, we typically have contractual

rights to require the licensor to adequately protect our intellectual property interests. Nevertheless, we cannot guarantee that such measures will be sufficient to protect our interests.

Our Move Free and MegaRed products contain key ingredients, the rights for which we license from third-party suppliers pursuant to long-term supply and license agreements. Our suppliers have patents and patents pending relating to the key ingredients, and have granted us non-exclusive rights to market and sell the ingredients in certain territories and classes of trade. However, we cannot assure you that our suppliers will prevail in preventing third parties from selling the key ingredients in their competing products at lower cost. This could have a material adverse effect on our results of operations and financial condition. See “Item 1 – Business – Manufacturing and Product Quality” and “– Intellectual Property.”

In addition, we own, or have filed for, over 50 trademarks registered with the United States Patent and Trademark Office for our Schiff and Tiger’s Milk brands and certain of our products (including Move Free) and slogans, and have rights to use names material to our business in certain countries outside of North America. Our policy is to pursue registrations for certain trademarks associated with our key products (though we continue to rely on common law trademark rights to protect our unregistered marks) and to protect our trademarks against infringement. However, there can be no assurance that infringing products could not be marketed without our knowledge or consent. Further, to the extent we rely upon foreign or common law protections for our marks, we may not be provided with as extensive protection as is afforded by a United States federal registration. If we are unable to effectively protect our trademark rights, it could have a material adverse effect on our results of operations and financial condition. See “Item 1 – Business – Intellectual Property.”

***Our international sales expose us to certain risks associated with international commerce which could adversely affect our business.*** Our international sales efforts are comprised of selling products, particularly our joint care products, from the United States on an export basis to retail customers or distributors abroad. Operating in international markets exposes us to certain risks, including, among others, difficulty in understanding and complying with foreign regulations, changes in or interpretations of foreign regulations that may further limit our ability to sell certain products or ingredients in certain countries, the potential imposition of trade or foreign exchange restrictions or increased tariffs, difficulties in enforcement of contractual obligations, difficulty in collecting international accounts receivable, potentially longer payment cycles, and political instability. We are often required to reformulate our products before commencing distribution in a given country. We must comply with various and changing local labeling, customs and other regulations. Trademark rights are often difficult to obtain and enforce in countries outside the United States. There is also no assurance that we will be able to obtain and retain the necessary permits and approvals required for our international efforts. The importance of these and other risks relating to exporting goods to foreign countries increases as our export business grows and expands. We are attempting to increase our distribution of joint care and other products in international markets. Our inability to successfully launch and maintain sales (especially in the joint care and omega-3 categories) outside of the United States while maintaining the integrity of the products sold and complying with local regulations could have an adverse effect on our results of operations and financial condition.

***Our failure to appropriately respond to changing consumer preferences and demand for new products or our failure to develop and/or sustain new product launches could have a material adverse effect on our results of operations and financial condition.*** We believe our ability to grow in existing markets is partially dependent upon our ability to introduce new and innovative products and product enhancements. The development and commercialization process, particularly relating to innovative products, is both time-consuming and costly and involves a high degree of business risk. Although we seek to introduce additional products each year, the success of new products or product enhancements is subject to a number of variables, including developing products that will appeal to customers, accurately anticipate consumer needs, be successfully commercialized in a timely manner, be priced competitively, be differentiated from those of our competitors, and comply with applicable regulations. The inability to successfully implement or maintain marketing and spending programs, a consistent supply of raw material, competitive claims or strategic initiatives in support of our branded products or product enhancements could have a material adverse effect on our results of operations and financial condition. We cannot assure you that our efforts to develop and introduce new products or existing product innovations will be successful, that customers will accept new products, or, if accepted, that customers will continue to sell the new products. The failure to successfully launch, gain distribution or maintain distribution for new product offerings or product enhancements could have a material adverse effect on our results of operations and financial condition.

***If we experience material product liability claims, FDA action or other litigation, it could have a material adverse effect on our results of operations and financial condition.*** As a manufacturer and distributor of products designed to be ingested, we face an inherent risk of exposure to product liability claims, FDA action and litigation if our products are alleged to have caused significant loss or injury. In addition, the manufacture and sale of our products involve the risk of injury to consumers due to tampering by unauthorized third parties or product contamination. Our products consist of vitamins, minerals, herbs, and other ingredients that are classified as dietary supplements or foods, and generally are not subject to pre-market regulatory approval in the United States. Some of our products contain ingredients that do not have long histories of human consumption, and may not have the effects intended. Previously unknown adverse reactions resulting from human consumption of these, other of our ingredients, or combinations of ingredients could occur. We have been, and in the future may be, subject to various product liability claims, including, among others, that our products caused injury or illness, that our products include inadequate instructions for use, or that our products include inadequate warnings concerning possible side effects or interactions with other substances. Recently the FDA

has taken a more aggressive approach to enforcement. A product liability claim or FDA action against us could result in increased costs, could adversely affect our reputation with our customers and consumers, and could have a material adverse effect on our results of operations and financial condition.

We are party to various lawsuits that arise in the ordinary course of business and may become party to others. While none of the lawsuits in which we are involved as of the date of this filing are reasonably believed to be material, it is possible that future litigation could arise, or that developments could occur in existing litigation, that could have a material adverse effect on our results of operations and financial condition.

***We may be unable to obtain sufficient insurance coverage to cover losses we may incur.*** We maintain insurance relating to the operation of our business, including, among other coverages, property, general and product liability, workers' compensation, and directors' and officers' liability policies. However, our insurance coverage is subject to large individual claim deductibles for certain policies, individual claim and aggregate policy limits, exclusions, and other terms and conditions. In addition, our current product liability coverage excludes claims relating to certain categories of products and products that contain certain ingredients. Certain damages in litigation, such as punitive damages, also are generally not covered by insurance. We cannot assure you that our insurance will be sufficient to cover our losses, that future insurance coverage will not contain additional exclusions or limitations, that we will be able to continue to obtain insurance coverage, or that insurance coverage will be available at an economically reasonable cost. In the event that we do not have adequate or any insurance, product liability claims, litigation or other losses could have a material adverse effect on our results of operations and financial condition.

***Failure to comply with existing or new regulations, both in the U.S. and abroad, or an adverse action regarding product formulation, claims or advertising could have a material adverse effect on our results of operations and financial condition.*** Our business operations, including the formulation, manufacturing, packaging, labeling, advertising, distribution and sale of our products, are subject to regulation by various foreign, federal, state and local government entities and agencies, particularly the FDA and FTC in the United States. See "Item 1 - Business - Government Regulation." From time to time we may be subject to challenges to our marketing, advertising or product claims in litigation or governmental, administrative or other regulatory proceedings. Failure to comply with applicable regulations or withstand such challenges could result in changes in product labeling, packaging, or advertising, product reformulations, discontinuation of our product by retailers, loss of market acceptance of the product by consumers, additional recordkeeping requirements, injunctions, product withdrawals, recalls, product seizures, fines or criminal prosecution. Any of these actions could have a material adverse effect on our results of operations and financial condition. As a result of our efforts to comply with applicable statutes and regulations, from time to time we have reformulated, eliminated or relabeled certain of our products and revised certain aspects of our sales, marketing and advertising programs. We cannot assure you that we will not have to make such changes or revisions in the future, which could have a material adverse effect on our results of operations and financial condition.

In June 2007, the FDA published extensive GMPs for dietary supplements. See "Item 1 - Business - Government Regulation." The effective compliance date for companies like ours with fewer than 500 employees was June 22, 2009. While we do not currently expect the incremental cost of compliance efforts to be material, we cannot assure you that, in complying with the new GMPs requirements, we will not incur substantial costs that may have a material adverse effect on our results of operations and financial condition, or that our operations or those of our suppliers will be in compliance in all respects at all times. Additionally, there is a potential risk of increased audits as the FDA and other regulators seek to ensure compliance with the GMPs.

In markets outside the United States, before commencing operations or marketing our products, we may be required to obtain approvals, licenses or certifications from a country's ministry of health or comparable agency. Approvals or licensing may be conditioned on reformulation of products or may be unavailable with respect to certain products or product ingredients. We must also comply with product labeling and packaging regulations that vary from country to country. Furthermore, the regulations of these countries may conflict with those in the United States and with each other. The cost of complying with these various and potentially conflicting regulations can be substantial and could have a material adverse effect on our results of operations and financial condition.

We may also be subject to additional laws or regulations administered by federal, state or foreign regulatory authorities, the repeal or amendment of laws or regulations which we consider favorable, such as DSHEA, or more stringent interpretations of current laws or regulations. Additional or more stringent legislation and regulations regarding the nutritional supplement industry have recently been considered. We are unable to predict the nature of such future laws, regulations, interpretations or applications, nor can we predict what effect additional governmental regulations or administrative orders, when and if promulgated, would have on our business in the future. Any or all of these requirements and the related costs to comply with such requirements could have a material adverse effect on our results of operations and financial condition.

***If we experience product recalls or a significant amount of product returns, we may incur significant and unexpected costs, and our business reputation could be materially adversely affected.*** Manufacturers and distributors of products in our industry are sometimes subject to the recall or return of their products for a variety of reasons, including product defects, such as ingredient contamination, unintended harmful side effects or interactions with other ingredients, packaging safety and inadequate or inaccurate

labeling disclosure. If any of our products are recalled due to an alleged product defect or for any other reason, we could be required to incur the unexpected expense of the recall and any legal proceedings that might arise in connection with the recall. We may lose a significant amount of sales and we may not be able to replace those sales at an acceptable margin or at all. In addition, a product recall may require significant management attention. We acquire all of our raw materials for the manufacture of our products from third parties. In addition, certain products we sell are produced by third-party manufacturers. Although we have procedures in place for qualifying suppliers and contract manufactures, and for testing raw materials and finished products, we cannot assure you that any quality, potency or contamination problems will be detected in time to avoid unforeseen product recalls, FDA action or lawsuits. Additionally, if one of our significant brands were subject to recall, the image of that brand and our company could be harmed. A recall for any of the foregoing reasons could lead to decreased demand for our products and could have a material adverse effect on our results of operations and financial condition. Additionally, product recalls may lead to increased scrutiny of our operations by federal, state or other regulatory agencies, requiring further management attention and potential legal fees and other expenses.

***We are dependent on a single manufacturing facility, and any material disruptions could adversely affect our business.*** We manufacture most of the products we sell at our manufacturing facility in Salt Lake City, Utah. Accordingly, we are highly dependent on the uninterrupted and efficient operation of our manufacturing facility. Power failures, the breakdown, failure or substandard performance of equipment, the improper installation or operation of equipment, workforce disruptions, natural or other disasters, or the failure to comply with laws or regulations or the requirements or directives of government agencies, including the FDA, could disrupt our operations and have a material adverse effect on our results of operations and financial condition. While we do carry business interruption insurance, we cannot assure you that our coverage will be sufficient to cover losses from these types of business disruptions or that this insurance will continue to be available to us at an acceptable price, if at all.

***If we are unable to consummate successful strategic transactions in the future, our business could be adversely affected.*** An element of our strategy includes expanding our product offerings, gaining shelf space, enhancing business development and gaining access to new skills and other resources through strategic acquisitions, investments or other transactions when attractive opportunities arise. We cannot assure you that attractive transaction opportunities will be available to us, that we will be able to obtain financing for or otherwise consummate any transactions or that any transactions which are consummated will prove to be successful.

***If we lose key personnel or are unable to attract and fill key positions, our business could be materially adversely affected.*** Our continued success will depend largely on the efforts and abilities of our executive officers and certain other key employees. The loss or limitation of the services of any of our key management employees, or the inability to attract additional qualified personnel could have a material adverse effect on our results of operations and financial condition.

***Interruptions to our information technology systems could have a material adverse effect on our business.*** Our success is dependent on the accuracy, reliability and proper use of sophisticated and dependable information processing systems and management information technology. Our information technology systems are designed and selected in order to facilitate order entry and customer billing, maintain customer records, accurately track purchases, manage accounting, finance and manufacturing operations, generate reports, and provide customer service and technical support. Although off-site data back-up is maintained, a significant interruption in these systems could have a material adverse effect on our results of operations and financial condition.

***We are controlled by a principal stockholder.*** WHF owns all of our outstanding shares of Class B common stock, representing over 90% of the aggregate voting power of all outstanding shares of our common stock. Two of our directors also serve on the board of directors of WHF. WHF is in a position to exercise control over us and to determine the outcome of all matters required to be submitted to stockholders for approval (except as otherwise provided by law or by our amended and restated certificate of incorporation or amended and restated bylaws) and otherwise to direct and control our operations. Accordingly, we cannot engage in any strategic transactions without the approval of WHF.

**ITEM 1B. UNRESOLVED STAFF COMMENTS**

We do not have any unresolved comments from the SEC staff.

**ITEM 2. PROPERTIES**

At May 31, 2010, we leased the following facility:

<u>Location</u>	<u>Function</u>	<u>Approximate Square Feet</u>	<u>Expiration Date of Lease</u>
Salt Lake City, UT	Company Headquarters, Manufacturing & Production, Warehouse & Distribution	418,000	March 2013

We believe that this facility is adequate to meet our current needs.

**ITEM 3. LEGAL PROCEEDINGS**

From time to time, we are involved in claims, legal actions and governmental proceedings that arise from our business operations. Although ultimate liability cannot be determined at the present time, based on available information, we do not believe the resolution of these matters will have a material adverse effect on our results of operations and financial condition. However, it is possible that future litigation could arise, or that developments could occur in existing litigation, that could have a material adverse effect on our results of operations and financial condition.

**ITEM 4. [REMOVED AND RESERVED]**

## PART II

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

Our Class A common stock is traded on the New York Stock Exchange under the symbol "WNI." The high and low closing prices, unadjusted for any dividends declared, of our Class A common stock for each quarter of fiscal 2010 and 2009 are set forth below:

<b>Fiscal Year Ended May 31, 2010:</b>	<b>High</b>	<b>Low</b>
First Quarter	\$ 6.04	\$ 4.68
Second Quarter	6.45	4.92
Third Quarter	8.35	5.79
Fourth Quarter	9.62	6.95

<b>Fiscal Year Ended May 31, 2009:</b>	<b>High</b>	<b>Low</b>
First Quarter	\$ 6.82	\$ 5.31
Second Quarter	6.98	4.96
Third Quarter	6.04	3.65
Fourth Quarter	5.04	3.62

There is no active trading market for our Class B common stock, which is owned entirely by WHF.

In March 2010, our Board of Directors approved a \$0.50 per share special cash dividend, which was paid on April 14, 2010 to shareholders of record of Class A and Class B common stock at the close of business on March 31, 2010. In connection with the declaration of the special dividend, our Board of Directors approved dividend equivalent rights, allowing holders (employees and directors) of certain equity awards, including stock options and restricted stock units, to receive cash dividends on each share of common stock underlying the stock options and restricted stock units. In aggregate, at March 31, 2010, the record date, we had outstanding 29.8 million shares of common stock (including shares of common stock underlying equity awards subject to dividend equivalent rights), including 27.8 million shares of outstanding Class A and Class B common stock, 1.0 million shares of Class A common stock underlying outstanding stock options, and 1.0 million shares of Class A common stock underlying outstanding restricted stock units. The aggregate amount of the special dividend was \$14.9 million, presuming 100% vesting of shares underlying equity awards; \$7.4 million for holders of Class A common stock, including \$1.0 million for Class A common stock underlying equity awards, and \$7.5 million for the holder of Class B common stock.

In July 2009, our Board of Directors approved a \$0.50 per share special cash dividend, which was paid on August 28, 2009 to shareholders of record of Class A and Class B common stock at the close of business on August 14, 2009. In connection with the declaration of the special dividend, our Board of Directors approved dividend equivalent rights, allowing holders (employees and directors) of certain equity awards, including stock options and restricted stock units, to receive cash dividends on each share of common stock underlying the stock options and restricted stock units. In aggregate, at August 14, 2009, the record date, we had outstanding 29.9 million shares of common stock (including shares of common stock underlying equity awards subject to dividend equivalent rights), including 27.6 million shares of outstanding Class A and Class B common stock, 1.3 million shares of Class A common stock underlying outstanding stock options, and 1.0 million shares of Class A common stock underlying outstanding restricted stock units. The aggregate amount of the special dividend was \$15.0 million, presuming 100% vesting of shares underlying equity awards; \$7.5 million for holders of Class A common stock, including \$1.1 million for Class A common stock underlying equity awards, and \$7.5 million for the holder of Class B common stock.

The special dividends declared during fiscal 2010 were funded from cash and cash equivalents, including in aggregate \$28.8 million distributed as of May 31, 2010. With respect to outstanding restricted stock and restricted stock units that were unvested as of May 31, 2010, or for which the issuance of shares underlying restricted stock units has been deferred, the dividends will not be distributed until after such equity awards vest or the deferred shares are issued.

In July 2007, our Board of Directors approved a \$1.50 per share special cash dividend, which was paid on August 13, 2007 to shareholders of record of Class A and Class B common stock at the close of business on July 31, 2007. In connection with the declaration of the special dividend, our Board of Directors approved certain dividend equivalent rights, allowing holders (employees and directors) of certain equity awards, including stock options and restricted stock units, to receive cash dividends on each share of common stock underlying the stock options and restricted stock units. In aggregate, at July 31, 2007, the record date, we had outstanding 29.9 million shares of common stock (including shares of common stock underlying equity awards subject to dividend equivalent rights), including 26.6 million shares of outstanding Class A and Class B common stock, 1.8 million shares of Class A common stock underlying outstanding stock options, and 1.5 million shares of Class A common stock underlying outstanding restricted stock units. The aggregate amount of the special dividend was \$44.9 million; \$22.4 million for holders of Class A common

stock, including \$4.9 million for Class A common stock underlying certain equity awards, and \$22.5 million for the holder of Class B common stock.

This special dividend was funded from cash and cash equivalents, and liquidation of available-for-sale securities, including \$43.9 million distributed as of May 31, 2010. The remaining amount will be distributed upon issuance of the deferred shares underlying vested restricted stock units.

Our Board of Directors will determine dividend policy in the future based upon, among other factors, our results of operations, financial condition, contractual restrictions and other factors deemed relevant at the time. In addition, our credit facility contains certain customary financial covenants that may limit our ability to pay dividends on our common stock. See Note 13 of Notes to Consolidated Financial Statements. We can give no assurance that we will pay dividends in the future.

The closing price of our Class A common stock on August 13, 2010 was \$8.43. The approximate number of stockholders of record of our Class A common stock on August 13, 2010 was 267. WHF owns all of the 14,973,148 outstanding shares of our Class B common stock.

The following table presents information about our Class A common stock that may be issued upon the exercise of options, warrants and rights under existing equity compensation plans at May 31, 2010:

Plan category	Number of securities to be issued upon exercise of outstanding options, warrants and rights	Weighted-average exercise price of outstanding options, warrants and rights	Number of securities remaining available for future issuance under equity compensation plans (excluding securities reflected in column (a))
	(a)	(b)	(c)
Equity compensation plans approved by security holders	1,964,815 <sup>(1)</sup>	\$2.87 <sup>(1)</sup>	1,878,396
Equity compensation plans not approved by security holders	—	—	—
Total	1,964,815	\$2.87	1,878,396

<sup>(1)</sup> The number of securities to be issued upon exercise of outstanding options, warrants and rights includes 961,148 shares of restricted stock units, which are excluded in determining the weighted-average exercise price of outstanding options, warrants and rights.

We did not purchase any of our Class A common stock during the fiscal 2010 fourth quarter.

**ITEM 6. SELECTED CONSOLIDATED FINANCIAL AND OPERATING DATA**

	<b>Fiscal Year Ended May 31,</b>				
	<b>2010</b>	<b>2009</b>	<b>2008</b>	<b>2007</b>	<b>2006</b>
<b>Operating Statement Data:</b>	<i>(in thousands, except per share data)</i>				
Net sales	\$ 204,887	\$ 190,691	\$ 176,914	\$ 172,656	\$ 178,372
Cost of goods sold	119,837	123,861	102,491	103,959	119,303
Gross profit	85,050	66,830	74,423	68,697	59,069
Operating expenses	56,240	51,644	58,090	51,415	46,693
Reimbursement of import costs	—	—	(31)	(394)	(2,665)
Total operating expenses	56,240	51,644	58,059	51,021	44,028
Income from operations	28,810	15,186	16,364	17,676	15,041
Other income (expense):					
Interest, net	(176)	765	1,917	2,943	1,840
Foreign currency translation gain	—	—	—	—	1,613
Other, net	8	(4)	13	(8)	(135)
Total other income (expense), net	(168)	761	1,930	2,935	3,318
Income from continuing operations before income taxes	28,642	15,947	18,294	20,611	18,359
Income tax expense	10,196	5,617	6,992	8,175	2,393
Income from continuing operations	18,446	10,330	11,302	12,436	15,966
Loss from discontinued operations, net of income taxes	—	—	—	—	(127)
Net income	<u>\$ 18,446</u>	<u>\$ 10,330</u>	<u>\$ 11,302</u>	<u>\$ 12,436</u>	<u>\$ 15,839</u>
Weighted average shares outstanding:					
Basic	<u>28,360</u>	<u>27,333</u>	<u>26,636</u>	<u>26,532</u>	<u>26,274</u>
Diluted	<u>28,928</u>	<u>28,638</u>	<u>28,000</u>	<u>27,343</u>	<u>26,999</u>
Net income per share:					
Basic	<u>\$ 0.65</u>	<u>\$ 0.38</u>	<u>\$ 0.42</u>	<u>\$ 0.47</u>	<u>\$ 0.60</u>
Diluted	<u>\$ 0.64</u>	<u>\$ 0.36</u>	<u>\$ 0.40</u>	<u>\$ 0.45</u>	<u>\$ 0.59</u>
Cash dividends declared per common share	<u>\$ 1.00</u>	<u>\$ —</u>	<u>\$ 1.50</u>	<u>\$ —</u>	<u>\$ —</u>

	<b>At May 31,</b>				
	<b>2010</b>	<b>2009</b>	<b>2008</b>	<b>2007</b>	<b>2006</b>
<b>Balance Sheet Data:</b>	<i>(in thousands)</i>				
Cash and cash equivalents	\$ 31,768	\$ 52,648	\$ 45,979	\$ 34,463	\$ 24,899
Working capital	79,417	92,215	81,481	104,869	90,516
Total assets	129,980	130,197	124,486	145,079	131,615
Total debt	—	—	—	—	—
Total stockholders' equity	100,448	109,693	99,487	124,095	107,507

**ITEM 7. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS**

The following discussion and analysis should be read in conjunction with the consolidated financial statements, including the notes thereto, appearing elsewhere in this Annual Report on Form 10-K.

**Overview**

Schiff Nutrition International, Inc. develops, manufactures, markets and distributes branded and private label vitamins, nutritional supplements and nutrition bars in the United States and throughout the world. We offer a broad range of capsules, tablets and nutrition bars. Our portfolio of recognized brands, including Schiff, Move Free, MegaRed and Tiger's Milk, is marketed primarily through the mass market (including club) and, to a lesser extent, health food store distribution channels.

According to the “Nutrition Business Journal,” the market for vitamins, minerals and supplements in the United States was estimated to be approximately \$26.9 billion in 2009. We believe that the market has reached its present size due to a number of factors, including increased awareness of the health benefits of dietary supplements, a growing population of older Americans, successful new product introductions, and a trend towards preventative measures and healthy living.

In recent years, nutritional supplement companies, analysts, publications and other industry sources have referenced a slower growth rate, particularly in terms of sales dollar growth, in the nutritional supplement industry. We believe that the slower growth rate is due in part to, among other factors, increased competition, including increasing competition from pharmaceutical and food companies, increased market and pricing competition, including from private label products, the general economic slowdown in the United States, negative publicity regarding certain nutritional supplement ingredients and companies, and the general maturing of the industry.

Our Schiff brand, which consists primarily of our joint care products, including Move Free, as well as other specialty vitamins, minerals and supplements, including MegaRed, has historically accounted for approximately 65% to 75% of total net sales. Our concentration in the Move Free brand and the joint care category is significant with our Move Free product historically constituting approximately 35% to 50% of total net sales. We provide significant selling and marketing support intended both to defend our Schiff business against competition, including private label, and ultimately to increase our market share. These selling and marketing activities can significantly impact our profitability.

Private label products, which we produce for certain retail customers where we sell our branded products, have historically accounted for approximately 20% to 30% of total net sales. Private label business is highly competitive and price-sensitive, often subject to competitive bidding processes at the retailer’s discretion, which could impact, potentially significantly, our overall net sales and profit margins. In addition, changes in our branded/private label sales mix can significantly impact our profitability because the gross profit percentage associated with private label sales is generally significantly lower than that for branded sales.

The vast majority of our branded and private label products are marketed and distributed, both domestically and internationally, in the mass market retail channel. Our products are sold throughout the United States in the stores of leading retailers, including warehouse clubs, mass merchandisers, drug stores and supermarkets. Our sales concentration in two customers is significant. Combined, these customers have historically accounted for approximately 70% to 80% of total net sales.

We also export certain Schiff products, primarily in the joint care category, to various international markets, including primarily the Pacific Rim (Asia), Mexico and the United Kingdom. Export net sales, which have historically accounted for less than 5% of total net sales, have been increasing at a higher rate than our domestic sales in recent years.

Raw materials, particularly certain raw materials contained in our joint care and omega-3 category products, account for a significant portion of our total cost of goods sold. Fluctuations in the cost of these key raw materials can significantly impact our profitability. We attempt to maintain an adequate supply of these key raw materials at prices that enhance our profitability by developing and maintaining relationships with our principal suppliers, including identifying and qualifying alternative suppliers for the same key materials, if possible; entering into long-term supply and license agreements and/or forward purchase commitments, where appropriate; and maintaining adequate safety stocks of inventory as deemed necessary.

We manufacture the majority of our products in a capsule and tablet manufacturing facility in Salt Lake City, Utah, which also includes our main distribution center, our primary administrative offices and our nutrition bar manufacturing operations. Our Salt Lake City capsule and tablet facility is designed and operated to meet the current Good Manufacturing Practices as promulgated by the US FDA in 21 CFR Part III.

Our competition includes numerous nutritional supplement companies that are highly fragmented in terms of geographical market coverage, distribution channels and product categories. In addition, large pharmaceutical companies and packaged food and beverage companies compete with us in the nutritional supplement market. These companies and certain nutrition supplement companies have broader product lines and/or larger sales volumes than us and have greater financial and other resources available to them and possess extensive manufacturing, distribution and marketing capabilities. In addition, private label products of our customers compete directly with our products.

To maintain our competitive market share, we attempt to differentiate our products through continuous product innovations; including the introduction of a new Advanced formula for our Move Free product in fiscal 2006 and the introduction of a smaller tablet for our joint care category products in fiscal 2008. We also attempt to grow and/or maintain our market share through the introduction of new products, such as MegaRed, an omega-3 krill oil product, successfully launched in fiscal 2008, as well as growing our export business. In addition, we actively pursue opportunities to maintain and grow our private label business since, in several product categories, private label items are the market share leaders. The acquisition of private label business also enhances our already strong customer relationships and helps drive purchasing and manufacturing cost efficiencies. We believe our comprehensive quality control standards and superior customer service also enhance our customer relationships and assist in differentiating our products.

During fiscal 2010, 2009 and 2008, we provided selling and marketing support intended both to defend our overall Move Free business against competition, including private label, and ultimately to increase our market share in the joint care product category. During fiscal 2010, 2009 and 2008, we also increased the distribution of our joint care products in international markets.

During fiscal 2008, we introduced smaller tablets for our existing Move Free items and announced the launch of a Move Free line extension. Also during fiscal 2008, we introduced MegaRed, an omega-3 krill oil product, into Costco. During fiscal 2009, and continuing in fiscal 2010, we introduced MegaRed into additional retail accounts. During the second half of fiscal 2009, we launched a national marketing campaign to support MegaRed growth.

In regards to our private label business, during the second half of fiscal 2010, a very active and price competitive bidding process for the manufacture of private label dietary supplements distributed in mass market retail accounts commenced and is expected to continue. Although fiscal 2010 private label sales and margins were not significantly impacted by the bidding process, fiscal 2011 private label sales and margins will be negatively impacted, potentially significantly.

Subject to the ongoing impact of competitive pricing pressures, including from both branded and private label products, the success of new product sales, including MegaRed, incremental private label bidding activity, the effectiveness of our branded marketing initiatives and the ability to increase our distribution in international markets, among other factors, we believe fiscal 2011 net sales, as compared to fiscal 2010 net sales, will reflect a low single-digit percentage increase, primarily due to overall branded growth. Subject to the ongoing private label bidding process, we believe fiscal 2011 private label sales, as compared to fiscal 2010, will be relatively constant.

Our gross profit and operating margins for fiscal 2010, as compared to fiscal 2009, were positively impacted by a higher mix of branded sales, lower raw material costs, price increases implemented in the fourth quarter of fiscal 2009 for certain branded and private label products and promotional cost efficiencies. During the second half of fiscal 2009, we discontinued certain private label products resulting in a decrease in private label sales for fiscal 2010, as compared to fiscal 2009. The decrease in lower-margin private label sales, branded sales volume growth, certain price increases and lower raw material costs resulted in an overall higher gross profit percentage for fiscal 2010, as compared to fiscal 2009. Based on current assumptions, we believe fiscal 2011 gross profit percentage will approximate 36.0% to 38.0%, compared to 41.5% for fiscal 2010. The decrease reflects significant erosion in private label margins due to the competitive bidding process, an expected increase in promotional activity and modest overall raw material pricing pressures; partially offset by the expected increase in branded sales.

Our gross profit and operating margins for fiscal 2009 were negatively impacted by incremental private label business awarded in the latter part of fiscal 2008. The incremental business coupled with increased volume from existing private label business resulted in a significant change in sales mix for fiscal 2009, compared to fiscal 2008. The significant increase in lower-margin private label sales coupled with higher raw material costs resulted in both lower gross profit and operating margins for fiscal 2009, as compared to fiscal 2008.

Our operating results for fiscal 2010 were also impacted by the adoption of a long-term management incentive plan on December 12, 2008. See Note 12 of Notes to Consolidated Financial Statements for further description of the long-term management incentive plan and its impact on operating results for fiscal 2010. Subject to the periodic assessment of the probability of achieving pre-established financial performance targets, fiscal 2011 operating results may continue to be impacted from recognition of compensation expense related to the management incentive plan.

Our financial results for fiscal 2008 were impacted by the declaration of a \$1.50 per share special cash dividend in July 2007. In connection with the declaration of the special dividend, our Board of Directors approved certain dividend equivalent rights allowing holders (employees and directors) of certain equity awards, including stock options and restricted stock units, to receive cash dividends on each share of common stock underlying the stock options and restricted stock units. As a result, we recognized \$4.9 million in non-cash compensation expense during fiscal 2008, together with a corresponding increase in additional paid-in-capital. Fiscal 2008 operating results were also unfavorably impacted by \$1.4 million in merger and acquisition related costs.

Factors affecting our historical results, including the previous implementation of strategic initiatives as well as continuing refinement of our growth and business strategies, are ongoing considerations and processes. While the focus of these considerations is to improve future profitability, we cannot assure you that our decisions relating to these initiatives will not adversely affect our results of operations and financial condition.

## Results of Operations

### Fiscal 2010 Compared to Fiscal 2009

The following tables show comparative results for selected items as reported and as a percentage of net sales for fiscal 2010 and 2009, (dollars in thousands):

	2010		2009	
Net sales	\$ 204,887	100.0%	\$ 190,691	100.0%
Cost of goods sold	119,837	58.5	123,861	65.0
Gross profit	85,050	41.5	66,830	35.0
Operating expenses:				
Selling and marketing	33,611	16.4	33,702	17.6
General and administrative	17,883	8.7	13,669	7.2
Research and development	4,746	2.3	4,273	2.2
Total operating expenses	56,240	27.4	51,644	27.0
Income from operations	28,810	14.1	15,186	8.0
Other income (expense), net	(168)	(0.1)	761	0.4
Income tax expense	(10,196)	(5.0)	(5,617)	(3.0)
Net income	<u>\$ 18,446</u>	<u>9.0%</u>	<u>\$ 10,330</u>	<u>5.4%</u>

**Net Sales.** Net sales increased 7.4% to \$204.9 million for fiscal 2010, from \$190.7 million for fiscal 2009, primarily due to an increase in branded net sales, partially offset by a decrease in private label net sales.

Aggregate branded net sales increased 13.1% to \$149.0 million for fiscal 2010, from \$131.8 million for fiscal 2009, primarily due to an increase in sales volume of \$16.4 million, or 8.8%, together with \$2.5 million in aggregate sales price increases and a \$0.4 million decrease in sales return allowances, partially offset by a \$2.1 million increase in sales promotional incentives classified as sales price reductions. Classification of certain promotional costs as a reduction from gross sales is required when the promotion effectively represents a sales price decrease. The increase in branded sales volume was primarily attributable to an increase in MegaRed sales. The increase in MegaRed sales was primarily due to incremental sales resulting from new distribution into various accounts in the latter part of fiscal 2009 and during fiscal 2010, as well as continued sales growth in existing accounts supported by increases in advertising and other promotional incentives. Move Free net sales were \$71.2 million and \$71.3 million, respectively, for fiscal 2010 and 2009.

Private label net sales decreased 5.2% to \$55.9 million for fiscal 2010, from \$58.9 million for fiscal 2009, primarily due to a \$9.5 million decrease in sales volume resulting from the discontinuation of certain unprofitable private label business in the second half of fiscal 2009, partially offset by a \$4.6 million sales volume increase and a \$1.7 million price increase for ongoing private label business. In regards to our private label business, during the second half of fiscal 2010, a very active and price competitive bidding process for the manufacture of private label dietary supplements distributed in mass market retail accounts was initiated by key retail customers. Although fiscal 2010 financial results were not significantly impacted by the bidding process, fiscal 2011 financial results will be negatively impacted, potentially significantly.

**Gross Profit.** Gross profit increased 27.3% to \$85.0 million for fiscal 2010, from \$66.8 million for fiscal 2009. Gross profit, as a percentage of net sales, increased to 41.5% for the fiscal 2010, from 35.0% for fiscal 2009, primarily resulting from the higher mix of branded sales, lower raw material costs, price increases implemented in the fourth quarter of fiscal 2009 for certain branded and private label products and promotional cost efficiencies. Subject to raw material pricing stability, competitive pressures and the overall branded to private label sales mix, among other factors, we expect fiscal 2011 gross profit percentage to approximate 36.0% to 38.0%, compared to 41.5% for fiscal 2010. The decrease reflects significant erosion in private label margins due to the competitive bidding processes, an expected increase in promotional activity and modest overall raw material pricing pressures; partially offset by an expected increase in branded sales. Since certain of our warehousing and distribution costs are included in general and administrative expenses, our gross profit may not be comparable to other entities who may include these expenses as a component of cost of goods sold.

**Operating Expenses.** Operating expenses increased 8.9% to \$56.2 million for fiscal 2010, from \$51.6 million for fiscal 2009, primarily resulting from a significant increase in general and administrative expenses. In spite of the overall increase, operating expenses, as a percentage of net sales, remained relatively constant at 27.4% and 27.0%, respectively, for fiscal 2010 and 2009, primarily due to the increase in net sales.

Selling and marketing expenses, including sales, marketing, advertising, freight and other costs, remained relatively constant at \$33.6 and \$33.7 million, respectively, for fiscal 2010 and 2009. Increases in recognized long-term and annual management incentive plan costs totaling \$1.5 million, were more than offset by a \$1.0 million decrease in other personnel related costs, including severance, and a \$0.7 million decrease in freight costs.

General and administrative expenses increased to \$17.9 million for fiscal 2010, from \$13.7 million for fiscal 2009, primarily resulting from increases in recognized long-term and annual management incentive plan costs totaling \$4.6 million, partially offset by a decrease in consulting fees.

Research and development costs increased to \$4.7 million for fiscal 2010, from \$4.3 million for fiscal 2009, primarily resulting from an increase in product clinical research costs.

**Other Income (Expense), Net.** Other income (expense), net, was \$0.2 million expense for fiscal 2010, compared to \$0.8 million income for fiscal 2009. The decrease was primarily due to an overall lower yield on investments, together with an increase in credit facility related commitment fees and amortized financing fees.

**Income Tax Expense.** Income tax expense was \$10.2 million for fiscal 2010, compared to \$5.6 million for fiscal 2009. The increase primarily resulted from an increase in pre-tax income. The tax rate remained relatively constant at 35.6% and 35.2%, respectively, for fiscal 2010 and 2009.

## Results of Operations

### *Fiscal 2009 Compared to Fiscal 2008*

The following tables show comparative results for selected items as reported and as a percentage of net sales for fiscal 2009 and 2008, (*dollars in thousands*):

	2009		2008	
Net sales	\$ 190,691	100.0%	\$ 176,914	100.0%
Cost of goods sold	123,861	65.0	102,491	57.9
Gross profit	66,830	35.0	74,423	42.1
Operating expenses:				
Selling and marketing	33,702	17.6	31,366	17.7
General and administrative	13,669	7.2	22,475	12.7
Research and development	4,273	2.2	4,249	2.4
Reimbursement of import costs	—	—	(31)	—
Total operating expenses	51,644	27.0	58,059	32.8
Income from operations	15,186	8.0	16,364	9.3
Other income, net	761	0.4	1,930	1.1
Income tax expense	(5,617)	(3.0)	(6,992)	(4.0)
Net income	<u>\$ 10,330</u>	<u>5.4%</u>	<u>\$ 11,302</u>	<u>6.4%</u>

**Net Sales.** Net sales increased approximately 7.8% to \$190.7 million for fiscal 2009, from \$176.9 million for fiscal 2008, primarily due to a significant increase in private label net sales, partially offset by a decrease in branded net sales.

Aggregate branded net sales decreased 5.3% to \$131.8 million for fiscal 2009, from \$139.2 million for fiscal 2008, primarily due to a \$3.3 million decrease in sales volume, a \$1.4 million increase in sales returns and a \$2.7 million increase in promotional incentives classified as sales price reductions. Classification of certain promotional costs as a reduction from gross sales is required when the promotion effectively represents a sales price decrease. We are utilizing more price-discount like promotions in the joint care category to defend our market share against both branded and private label competition. The decrease in sales volume resulted from a reduction in our joint care category volume, significantly offset by incremental MegaRed new product sales. Move Free net sales were \$71.3 million and \$82.6 million, respectively, for fiscal 2009 and 2008. The decrease in Move Free net sales, as well as decreases in other joint care category sales, primarily resulted from decreases in sales volume due to adjustments to customer inventory levels, private label volume growth due to significant price discounting, and the impact of uncertain economic conditions.

Private label net sales increased 56.2% to \$58.9 million for fiscal 2009, from \$37.7 million for the fiscal 2008, primarily due to incremental business awarded in the latter part of fiscal 2008 together with an increase in customer promotional activity on existing business.

**Gross Profit.** Gross profit decreased 10.2% to \$66.8 million for fiscal 2009, from \$74.4 million for fiscal 2008. Gross profit, as a percentage of net sales, decreased to 35.0% for fiscal 2009, from 42.1% for fiscal 2008, primarily due to the reduction in branded joint care category sales, the significant increase in lower margin private label sales, higher raw material costs and incremental promotional incentives. Since certain of our warehousing and distribution costs are included in general and administrative expenses, our gross profit may not be comparable to other entities who may include these expenses as a component of costs of goods sold.

**Operating Expenses.** Operating expenses decreased 11.1% to \$51.6 million for fiscal 2009, from \$58.1 million for fiscal 2008. Operating expenses, as a percentage of net sales, were 27.0% and 32.8%, respectively, for fiscal 2009 and 2008. The decrease in operating expenses resulted primarily from a substantial decrease in general and administrative expenses, partially offset by a modest increase in selling and marketing expenses.

Selling and marketing expenses, including sales, marketing, advertising, freight and other costs, increased to \$33.7 million for fiscal 2009, from \$31.4 million for fiscal 2008. An increase in promotional and freight costs was partially offset by a \$1.0 million reduction in management incentive program costs and the fiscal 2008 recognition of \$0.5 million in incremental compensation expenses associated with distribution of a special dividend. The special dividend compensation expense represents a non-cash charge for dividend equivalent rights received by holders of certain equity awards, including stock options and restricted stock units. The increase in promotional costs resulted from additional price discounting in joint care category products due to competitive pressures, including private label, and incremental advertising in support of MegaRed. Freight costs increased due to higher sales volumes and increases in fuel costs.

General and administrative expenses decreased to \$13.7 million for fiscal 2009, from \$22.5 million for fiscal 2008, primarily due to the fiscal 2008 recognition of \$4.4 million in incremental compensation expense for a special dividend and \$1.4 million in merger and acquisition related costs, together with a \$4.5 million year over year reduction in management incentive program costs.

Research and development costs remained relatively constant at \$4.3 million for fiscal 2009 and 2008.

**Other Income, Net.** Other income, net, was \$0.8 million for fiscal 2009, compared to \$1.9 million for fiscal 2008. The decrease was primarily due to a reduction in interest income resulting from an overall lower yield on investments.

**Income Tax Expense.** Income tax expense was \$5.6 million for fiscal 2009, compared to \$7.0 million for fiscal 2008. The effective tax rate was 35.2% and 38.2%, respectively, for fiscal 2009 and 2008. The decrease in the effective tax rate primarily resulted from an increase in utilized tax credits.

## Liquidity and Capital Resources

Working capital decreased \$12.8 million to \$79.4 million at May 31, 2010, from \$92.2 million at May 31, 2009, reflecting a \$11.5 million decrease in cash and cash equivalents and available-for-sale securities, a \$1.0 million decrease in net receivables, a \$5.1 million increase in inventories and a \$5.6 million increase in current liabilities. The decrease in cash and cash equivalents and available-for-sale securities reflects \$26.1 million in cash flows provided by operating activities, more than offset by special dividend payments of \$28.8 million, capital expenditures of \$2.9 million and an increase in long-term available-for-sales securities of \$6.1 million. The decrease in net receivables is primarily due to a reduction in refundable income taxes. The increase in inventories, as well as the corresponding increase in accounts payable, primarily reflects promotional timing considerations, new products and raw material buy forward strategies. The \$3.2 million increase in accrued expenses is primarily due to an increase in recognized annual management incentive plan costs.

At May 31, 2010, we held \$20.4 million in available-for-sale securities, consisting of \$5.8 million in certificates of deposit and commercial paper and \$14.6 million in debt securities; including \$0.4 million in illiquid ARS which are fully insured state agency issued securities. Although we have experienced failed auctions with these ARS, and will therefore not be able to access our funds invested in these ARS until future auctions of these investments are successful, or the securities are called by the issuer, we believe we will be able to successfully liquidate these investments. However, we believe the unsuccessful liquidation of some, or all, of these securities over the next twelve months will not significantly impact our liquidity needs.

On August 18, 2009, we entered into, through our wholly-owned direct operating subsidiary Schiff Nutrition Group, Inc. ("SNG"), a new \$80.0 million revolving credit facility (the "Credit Facility") with U.S. Bank National Association, as Agent. The Credit Facility replaced our previous \$25.0 million credit facility which expired on June 30, 2009, and contains customary terms and conditions, including, among others, financial covenants that may limit our ability to pay dividends on our common stock and certain other restrictions. SNG's obligations under the Credit Facility are guaranteed by us and SNG's domestic subsidiaries and secured by a first priority security interest in all of the capital stock of SNG and its current and future subsidiaries, as well as a first priority security interest in substantially all of our domestic assets. Borrowings under the Credit Facility bear interest at floating rates based on U.S. Bank's prime rate, the Federal Funds rate, or the LIBOR rate. The Credit Facility, which matures on August 18, 2012, can be used to fund our normal working capital and capital expenditure requirements, with availability to fund certain permitted strategic transactions. We incurred \$0.5 million in financing fees related to the Credit Facility, which are being amortized over its three-year

term. In addition, we are obligated to pay certain commitment fees on any unused amounts based on rates ranging from 0.25% to 0.50%. At May 31, 2010, there were no amounts outstanding and, subject to limitations based on certain financial covenant requirements, \$80.0 million was available for borrowing under the Credit Facility.

We believe that our cash and cash equivalents, cash flows from operations and the financing sources discussed above will be sufficient to meet our normal cash operating requirements during the next twelve months. However, we continue to review opportunities to acquire or invest in companies, product rights and other investments that are compatible with or complimentary to our existing business. We could use cash and financing sources discussed herein, or financing sources that subsequently become available, to fund acquisitions or investments. In addition, we may consider issuing additional debt or equity securities in the future to fund potential acquisitions or growth, or to refinance existing debt. If a material acquisition, divestiture or investment is completed, our operating results and financial condition could change materially in future periods. However, no assurance can be given that additional funds will be available on satisfactory terms, or at all, to fund such activities.

Our Board of Directors will determine dividend policy in the future based upon, among other factors, results of operations, financial condition, contractual restrictions and other factors deemed relevant at the time. In addition, our Credit Facility contains certain customary financial covenants that may limit our ability to pay dividends on our common stock. We can give no assurance that we will pay dividends in the future.

### Off-Balance Sheet Arrangements

We have no off-balance sheet arrangements. For information relating to certain contractual cash obligations see below.

### Contractual Obligations

A summary of our outstanding contractual obligations at May 31, 2010 is as follows (in thousands):

Contractual Cash Obligations <sup>(1)</sup>	Total Amounts Committed	Less than 1 Year	1-3 Years	3-5 Years	More than 5 Years
Operating leases	\$ 6,612	\$ 2,352	\$ 4,251	\$ 9	\$ —
Purchase obligations <sup>(2)</sup>	27,994	27,994	—	—	—
Total obligations	\$ 34,606	\$ 30,346	\$ 4,251	\$ 9	\$ —

<sup>(1)</sup> Unrecognized income tax benefits totaling \$340 are excluded since we are unable to estimate the period of settlement, if any.

<sup>(2)</sup> Purchase obligations consist primarily of open purchase orders for goods and services, including primarily raw materials, packaging and outsourced contract manufacturing commitments.

### Critical Accounting Policies and Estimates

In preparing our consolidated financial statements, we make assumptions, estimates and judgments that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the dates of the consolidated financial statements and the reported amounts of net sales, cost of goods sold and operating expenses during the reported periods. We periodically evaluate our estimates and judgments related to the valuation of available-for-sale securities, inventories and intangible assets, allowances for doubtful accounts, sales returns and discounts, uncertainties related to certain tax benefits, valuation of deferred tax assets, valuation of share-based payments or cash awards and recoverability of long-lived assets. Note 1 of Notes to the Consolidated Financial Statements describes the accounting policies governing each of these matters. Our estimates are based on historical experience and on our future expectations that are believed to be reasonable. The combination of these factors forms the basis for making judgments about the carrying values of assets and liabilities that are not readily apparent from other sources. Actual results may differ from our current estimates and those differences may be material.

We believe the following accounting policies affect some of our more significant estimates and judgments used in preparation of our consolidated financial statements:

- We provide for valuation adjustments for changes in the fair values of our available-for-sale securities. Fair values are based upon quoted market prices and/or other considerations, including fair values determined by financial institutions, current credit rating of the debt securities, insurance provisions and discounted cash flow analysis as deemed appropriate. Changes in valuation adjustments for declines in the fair values of our available-for-sales securities did not impact net income for

fiscal 2010, 2009 or 2008. At May 31, 2010 and 2009, respectively, unrealized losses resulting from fair market adjustments to our available-for-sale securities totaled \$0.1 million and \$0.2 million.

- We provide for inventory valuation adjustments for estimated obsolescence or unmarketable inventory equal to the difference between the cost of inventory and the estimated market value based upon assumptions about future demand, market conditions and/or liquidation value. For fiscal 2010, 2009 and 2008, respectively, inventory valuation adjustments resulted in a decrease in our gross profit and operating income of \$0.7 million, \$0.2 million and \$0.9 million. If actual demand and/or market conditions are less favorable than those projected by management, additional inventory write-downs would be required.
- We maintain allowances for doubtful accounts, sales returns and discounts for estimated losses resulting from customer exposures, including among others, product returns, inability to make payments and expected utilization of offered discounts. Changes in our allowances for doubtful accounts, sales returns and discounts resulted in an increase in our gross profit and operating income of \$0.1 million for fiscal 2010. Changes in these allowances resulted in a decrease in our gross profit and operating income of \$0.8 million for fiscal 2009. Changes in these allowances did not significantly impact our gross profit and operating income for fiscal 2008. At May 31, 2010 and 2009, respectively, our allowances for doubtful accounts, sales returns and discounts in aggregate amounted to \$2.0 million and \$2.3 million. Actual results may differ from our current estimates, resulting in adjustment of the respective allowance(s).
- We currently have deferred tax assets resulting from temporary differences between financial and income tax reporting. These deferred tax assets are subject to periodic recoverability assessments. The realization of these deferred tax assets is primarily dependent on future operating results. Changes in valuation allowances relating to deferred tax assets did not significantly impact net income for fiscal 2010, 2009 and 2008. At May 31, 2010 and 2009, deferred tax asset valuation allowances were zero.
- We recognize tax benefits relative to certain tax positions in which we may be uncertain as to whether that tax position will ultimately be sustained as filed in our tax return. The recognition or derecognition of these tax benefits is subject to periodic evaluation of the sustainability of the tax position based upon changes in facts, circumstances or available information. Changes in the recognition of these tax benefits did not significantly impact net income for fiscal 2010, 2009 and 2008.
- We recognize compensation expense for certain performance based equity instrument (share-based payments) or cash awards over the performance period based on a periodic assessment of the probability that the performance criteria will be achieved. Our periodic assessment of the probability that the performance criteria will be achieved considers such factors as historical financial results and future financial expectations, including an analysis of sales trends and operating margins; as well as changes in the nutritional supplements industry and competitive environment. For fiscal 2010, 2009 and 2008, respectively, we recognized compensation expense related to these awards of \$2.5 million, zero and \$3.4 million. At May 31, 2010, total unrecognized compensation expense, based on the estimated fair value as determined by our assessment of the probability that the performance criteria will be achieved, was \$1.8 million. This amount, which is subject to change based on the estimated fair value determined at each future reporting period, is expected to be recognized over the remaining service period.
- We have certain intangible assets, primarily consisting of goodwill, which are tested for impairment at least annually. We did not recognize any intangible asset impairment losses for fiscal 2010, 2009 or 2008. The determination of whether or not goodwill is impaired involves significant judgment. Changes in strategy or market conditions could significantly impact our judgment and require adjustment to the recorded goodwill balance.

### **Impact of Inflation**

Inflation affects the cost of raw materials, goods and services we use. In recent years, inflation has been modest. We seek to mitigate the adverse effects of inflation primarily through improved productivity, strategic buying initiatives, and cost containment programs. However, the nutritional supplement industry competitive environment limits our ability to raise prices in order to recover higher costs resulting from inflation. See further discussion of raw material pricing matters in the “General” and “Results of Operations” sections above.

### **Seasonality**

Our business is not inherently seasonal; however, we experience fluctuations in sales resulting from timing of marketing and promotional activities, customer buying patterns and consumer spending patterns. In addition, as a result of changes in product sales mix, competitive conditions, raw material pricing pressures and other factors, as discussed above, we experience fluctuations in gross profit and operating margins on a quarter-to-quarter basis.

## **Recently Issued Accounting Standards**

See Note 1 of Notes to the Consolidated Financial Statements in this Annual Report on Form 10-K.

### **ITEM 7A. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK**

The following discussion involves forward-looking statements of market risk which assume that certain adverse market conditions may occur. Actual future market conditions may differ materially from such assumptions. Accordingly, the forward-looking statements should not be considered our projections of future events or losses.

Our cash flows and net earnings may be subject to fluctuations resulting from changes in interest rates. Our current policy does not allow speculation in derivative instruments for profit or execution of derivative instrument contracts for which there is no underlying exposure. We do not use financial instruments for trading purposes. We measure market risk, related to our holdings of financial instruments, based on changes in interest rates utilizing a sensitivity analysis. Our Credit Facility, under which borrowings bear interest at floating rates, had no amounts outstanding at May 31, 2010. Interest income earned on our short-term investments is impacted by changes in interest rate. We do not believe that a hypothetical 10% change in interest rates would have a material effect on our pretax earnings or cash flows.

### **ITEM 8. FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA**

The consolidated financial statements and supplementary data and the report of Deloitte & Touche LLP, our independent registered public accountants, are on the following pages F-1 through F-19 and are incorporated herein by reference.

### **ITEM 9. CHANGES IN AND DISAGREEMENTS WITH ACCOUNTANTS ON ACCOUNTING AND FINANCIAL DISCLOSURE**

None.

### **ITEM 9A. CONTROLS AND PROCEDURES**

We maintain disclosure controls and procedures that are designed to ensure that information required to be disclosed in our Exchange Act reports is recorded, processed, summarized and reported within the time periods specified in the SEC's rules and forms and that such information is accumulated and communicated to our management, including our Chief Executive Officer and Chief Financial Officer, as appropriate, to allow for timely decisions regarding required disclosure. In designing and evaluating the disclosure controls and procedures, we recognize that any controls and procedures, no matter how well designed and operated, can provide only reasonable assurance of achieving the desired control objectives, and we are required to apply our judgment in evaluating the cost-benefit relationship of possible controls and procedures.

Our disclosure controls and procedures are designed to provide reasonable assurance of achieving their objectives. As required by Exchange Act Rule 13a-15(b), we carried out an evaluation, under the supervision and with the participation of our management, including our Chief Executive Officer and Chief Financial Officer, of the effectiveness of the design and operation of our disclosure controls and procedures as of the end of the fiscal quarter covered by this report. Based on the foregoing, our Chief Executive Officer and Chief Financial Officer have concluded that our disclosure controls and procedures were effective at the reasonable assurance level.

There has been no change in our internal controls over financial reporting during our most recent fiscal quarter that has materially affected, or is reasonably likely to materially affect, our internal controls over financial reporting.

#### **Management's Report on Internal Control over Financial Reporting**

Internal control over financial reporting refers to the process designed by, or under the supervision of, our Chief Executive Officer and Chief Financial Officer, and affected by our Board of Directors, management and other personnel, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles, and includes those policies and procedures that:

- Pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of our assets;
- Provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that our receipts and expenditures are being made only in accordance with authorizations of our management and directors; and

- Provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use or disposition of our assets that could have a material effect on the financial statements.

Internal control over financial reporting cannot provide absolute assurance of achieving financial reporting objectives because of its inherent limitations. Internal control over financial reporting is a process that involves human diligence and compliance and is subject to lapses in judgment and breakdowns resulting from human failures. Internal control over financial reporting also can be circumvented by collusion or improper management override. Because of such limitations, there is a risk that material misstatements may not be prevented or detected on a timely basis by internal control over financial reporting. However, these inherent limitations are known features of the financial reporting process. Therefore, it is possible to design into the process safeguards to reduce, though not eliminate, the risk. Management is responsible for establishing and maintaining adequate internal control over our financial reporting.

Management has used the framework set forth in the report entitled “Internal Control-Integrated Framework” published by the Committee of Sponsoring Organizations (“COSO”) of the Treadway Commission to evaluate the effectiveness of its internal control over financial reporting. Management has concluded that its internal control over financial reporting was effective as of the end of the most recent fiscal year.

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

The foregoing has been approved by our management, including our Chief Executive Officer and Chief Financial Officer, who have been involved with the assessment and analysis of our internal controls over financial reporting.

## PART III

### **ITEM 9B. OTHER INFORMATION**

None.

### **ITEM 10. DIRECTORS, EXECUTIVE OFFICERS AND CORPORATE GOVERNANCE**

See our 2010 Definitive Proxy Statement, incorporated by reference in Part III of this Annual Report on Form 10-K, under the headings “Board of Directors and Corporate Governance Information,” “Nominees for Election to our Board of Directors,” “Executive Officers” and “Section 16(a) Beneficial Ownership Reporting Compliance.” Information regarding our Code of Business Conduct and Ethics is also incorporated by reference to our 2010 Definitive Proxy Statement under the heading “Board of Directors and Corporate Governance Information.”

### **ITEM 11. EXECUTIVE COMPENSATION**

See our 2010 Definitive Proxy Statement, incorporated by reference in Part III of this Annual Report on Form 10-K, under the headings “Board of Directors and Corporate Governance Information,” “Executive Compensation” and “Certain Relationships and Related Transactions.”

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

See the information set forth under Item 5 herein and in our 2010 Definitive Proxy Statement, incorporated by reference in Part III of this Annual Report on Form 10-K, under the heading “Stock Ownership of Beneficial Owners, Directors and Management.”

### **ITEM 13. CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS, AND DIRECTOR INDEPENDENCE**

See our 2010 Definitive Proxy Statement, incorporated by reference in Part III of this Annual Report on Form 10-K, under the heading “Certain Relationships and Related Transactions.”

### **ITEM 14. PRINCIPAL ACCOUNTING FEES AND SERVICES**

See our 2010 Definitive Proxy Statement, incorporated by reference in Part III of this Annual Report on Form 10-K, under the heading “Fees Paid to Independent Public Accountants.”

## PART IV

### ITEM 15. EXHIBITS, FINANCIAL STATEMENT SCHEDULES

(a) Documents filed as part of this report

1) Financial Statements

See “Item 8. Financial Statements and Supplementary Data” for Financial Statements included with this Annual Report on Form 10-K.

2) Financial Statement Schedules

Schedule II - Valuation and Qualifying Accounts. All other schedules have been omitted because they are not required, not applicable, or the information is otherwise set forth in the financial statements or notes thereto.

3) Exhibits

- 3.1. Amended and Restated Certificate of Incorporation of Schiff Nutrition International, Inc. (1)
- 3.2. Amended and Restated Bylaws of Weider Nutrition International, Inc. (2)
- 4.1. Form of specimen Class A common stock certificate. (3)
- 4.2. Loan Agreement dated as of August 18, 2009 between Schiff Nutrition Group, Inc. and U.S. Bank National Association. (20)
- 10.1. Build-To-Suit Lease Agreement dated March 20, 1996, between SCI Development Services Incorporated and Weider Nutrition Group, Inc. (2)
- 10.2. 1997 Equity Participation Plan of Weider Nutrition International, Inc. (4)\*
- 10.3. Form of Tax Sharing Agreement by and among Weider Nutrition International, Inc. and its subsidiaries and Weider Health and Fitness and its subsidiaries. (4)
- 10.4. License Agreement dated as of December 1, 1996 between Mariz Gestao E Investimentos Limitada and Weider Nutrition Group, Inc. (4)
- 10.5. Amendments No. 1, 2 and 3 to 1997 Equity Participation Plan of Weider Nutrition International, Inc. (5)\*
- 10.6. Consulting Agreement dated as of February 1, 2004 between Weider Nutrition Group, Inc. and Gustin Foods, LLC. (6)
- 10.7. Schiff Nutrition International, Inc. 2004 Incentive Award Plan. (7)\*
- 10.8. Amendment effective as of March 1, 2005 to License Agreement between Mariz Gestao E Investimentos Limitada and Weider Nutrition Group, Inc. (8)
- 10.9. Stock and Asset Purchase Agreement effective as of March 1, 2005 among Weider Nutrition International, Inc., Weider Nutrition Group, Inc. and Weider Global Nutrition, LLC. (8)
- 10.10. Promissory Note of Weider Global Nutrition, LLC payable to Weider Nutrition Group, Inc. (8)
- 10.11. Guarantee by Weider Health and Fitness in favor of Weider Nutrition International, Inc. and Weider Nutrition Group, Inc. (8)
- 10.12. Form of Indemnification Agreement between Schiff Nutrition Group, Inc. and certain of its executives and directors. (9)\*
- 10.13. Form of Restricted Stock Unit Award Grant Notice, Restricted Stock Unit Award Agreement and Deferral Election between Schiff Nutrition International, Inc. and certain of its executives. (10)\*
- 10.14. Amendment No. 1 to the Schiff Nutrition International, Inc. 2004 Incentive Award Plan. (11)\*
- 10.15. Form of Director Restricted Stock Unit Agreement and Deferral Election. (12)\*
- 10.16. Form of Director Restricted Stock Agreement. (12)\*
- 10.17. Employment and Change in Control Agreement dated as of June 1, 2007 between Schiff Nutrition Group, Inc. and Bruce J. Wood (13)\*
- 10.18. Form of Amended and Restated Agreement between Schiff Nutrition Group, Inc. and certain of its executives. (13)\*
- 10.19. License Agreement dated as of September 19, 2007 between Mariz Gestao E Investimentos Limitada and Schiff Nutrition Group, Inc. (14)
- 10.20. Amendment No. 2 to the Schiff Nutrition International, Inc. 2004 Incentive Award Plan. (15)\*
- 10.21. Form of Performance Award Grant Notice, Performance Award Agreement and Deferral Election. (16)\*
- 10.22. Amendment No. 3 to the Schiff Nutrition International, Inc. 2004 Incentive Award Plan. (13)\*
- 10.23. Amendment No. 4 to the 1997 Equity Participation Plan of Weider Nutrition International Inc. (13)\*
- 10.24. Consulting Agreement dated as of November 3, 2008 between Schiff Nutrition Group, Inc. and Daniel A. Thomson. (13)\*
- 10.25. Second Amended and Restated License and Product Supply Agreement dated as of May 29, 2009 between Unigen Pharmaceuticals, Inc. and Schiff Nutrition Group, Inc. (17)
- 10.26. Security Agreement dated as of August 18, 2009 among Schiff Nutrition Group, Inc., Schiff Nutrition International, Inc., WNG Holdings (International) Ltd., Coppal Research, Inc. and U.S. Bank National Association. (18)
- 10.27. Continuing and Unconditional Guaranty dated as of August 18, 2009 by Schiff Nutrition International, Inc. in favor of U.S. Bank National Association. (18)
- 10.28. Continuing and Unconditional Guaranty dated as of August 18, 2009 by WNG Holdings (International) Ltd. in favor of U.S. Bank National Association. (18)
- 10.29. Continuing and Unconditional Guaranty dated as of August 18, 2009 by Coppal Research, Inc. in favor of U.S. Bank National Association. (18)
- 10.30. Sales Agreement dated as of August 31, 2009 between Aker BioMarine Antarctic AS and Schiff Nutrition Group, Inc. (19)

- 21.1. Subsidiaries of Schiff Nutrition International, Inc. (20)
- 23.1. Consent of Independent Registered Public Accounting Firm. (20)
- 31.1. Certification of Chief Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act. (20)
- 31.2. Certification of Chief Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act. (20)
- 32.1. Certification of Chief Executive Officer and Chief Financial Officer pursuant to Section 906 of the Sarbanes-Oxley Act. (21)

- 
- (1) Previously filed in the Company's Quarterly Report on Form 10-Q filed on January 17, 2006 and incorporated herein by reference.
  - (2) Previously filed in the Company's Registration Statement on Form S-1/A (File No. 333-12929) filed on October 16, 1996 and incorporated herein by reference.
  - (3) Previously filed in the Company's Annual Report on Form 10-K filed on August 29, 2006 and incorporated herein by reference.
  - (4) Previously filed in the Company's Registration Statement on Form S-1/A (File No. 333-12929) filed on March 20, 1997 and incorporated herein by reference.
  - (5) Previously filed in the Company's Quarterly Report on Form 10-Q filed on January 14, 2002 and incorporated herein by reference.
  - (6) Previously filed in the Company's Quarterly Report on Form 10-Q filed on April 14, 2004 and incorporated herein by reference.
  - (7) Previously filed in the Company's Definitive Proxy Statement on Form 14A filed on September 28, 2004 and incorporated herein by reference.
  - (8) Previously filed in the Company's Current Report on Form 8-K filed on April 4, 2005 and incorporated herein by reference.
  - (9) Previously filed in the Company's Current Report on Form 8-K filed on August 10, 2005 and incorporated herein by reference.
  - (10) Previously filed in the Company's Current Report on Form 8-K filed on March 23, 2006 and incorporated herein by reference.
  - (11) Previously filed in the Company's Definitive Proxy Statement on Form 14A filed on September 27, 2006 and incorporated herein by reference.
  - (12) Previously filed in the Company's Current Report on Form 8-K filed on October 30, 2006 and incorporated herein by reference.
  - (13) Previously filed in the Company's Quarterly Report on Form 10-Q filed on January 9, 2009 and incorporated herein by reference.
  - (14) Previously filed in the Company's Current Report on Form 8-K filed on September 25, 2007 and incorporated herein by reference.
  - (15) Previously filed in the Company's Definitive Proxy Statement on Form 14A filed on September 27, 2007 and incorporated herein by reference.
  - (16) Previously filed in the Company's Current Report on Form 8-K filed on December 18, 2008 and incorporated herein by reference.
  - (17) Previously filed in the Company's Current Report on Form 8-K filed on June 4, 2009 and incorporated herein by reference.
  - (18) Previously filed in the Company's Annual Report on Form 10-K filed on August 20, 2009 and incorporated herein by reference.
  - (19) Previously filed in the Company's Current Report on Form 8-K filed on September 4, 2009 and incorporated herein by reference.
  - (20) Filed herewith.
  - (21) Furnished herewith.

\* Management contract.

## SIGNATURES

Pursuant to the requirements of section 13 or 15(d) of the Securities Exchange Act of 1934, the Registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

### Schiff Nutrition International, Inc.

By: /s/ Bruce J. Wood

**Bruce J. Wood**  
**Chief Executive Officer and President**

Dated: August 17, 2010

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

<u>Name</u>	<u>Title</u>	<u>Date</u>
<u>/s/ Eric Weider</u> <b>Eric Weider</b>	Chairman of the Board and Director	<u>August 17, 2010</u>
<u>/s/ Bruce J. Wood</u> <b>Bruce J. Wood</b>	Chief Executive Officer, President and Director (Principal Executive Officer)	<u>August 17, 2010</u>
<u>/s/ Joseph W. Baty</u> <b>Joseph W. Baty</b>	Executive Vice President and Chief Financial Officer (Principal Financial Officer and Principal Accounting Officer)	<u>August 17, 2010</u>
<u>/s/ Ronald L. Corey</u> <b>Ronald L. Corey</b>	Director	<u>August 17, 2010</u>
<u>/s/ Michael Hyatt</u> <b>Michael Hyatt</b>	Director	<u>August 17, 2010</u>
<u>/s/ Eugene B. Jones</u> <b>Eugene B. Jones</b>	Director	<u>August 17, 2010</u>
<u>/s/ Roger H. Kimmel</u> <b>Roger H. Kimmel</b>	Director	<u>August 17, 2010</u>
<u>/s/ George F. Lengvari</u> <b>George F. Lengvari</b>	Vice Chairman of the Board and Director	<u>August 17, 2010</u>
<u>/s/ Brian P. McDermott</u> <b>Brian P. McDermott</b>	Director	<u>August 17, 2010</u>

**SCHIFF NUTRITION INTERNATIONAL, INC.**  
**INDEX TO CONSOLIDATED FINANCIAL STATEMENTS**

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# REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

The Board of Directors

Schiff Nutrition International, Inc. and Subsidiaries:

We have audited the accompanying consolidated balance sheets of Schiff Nutrition International, Inc. and subsidiaries (collectively, the "Company") as of May 31, 2010 and 2009, and the related consolidated statements of income, stockholders' equity and cash flows for each of the three years in the period ended May 31, 2010. Our audits also included the financial statement schedule listed in the Index at Item 15. These financial statements and financial statement schedule are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements and financial statement schedule based on our audits.

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

In our opinion, such consolidated financial statements present fairly, in all material respects, the financial position of Schiff Nutrition International, Inc. and subsidiaries at May 31, 2010 and 2009, and the results of their operations and their cash flows for each of the three years in the period ended May 31, 2010 in conformity with accounting principles generally accepted in the United States of America. Also, in our opinion, such financial statement schedule, when considered in relation to the basic consolidated financial statements taken as a whole, presents fairly in all material respects the information set forth therein.

DELOITTE & TOUCHE LLP

Salt Lake City, Utah  
August 17, 2010

**SCHIFF NUTRITION INTERNATIONAL, INC. AND SUBSIDIARIES**  
**CONSOLIDATED BALANCE SHEETS**  
**MAY 31, 2010 AND 2009**  
*(dollars in thousands, except share data)*

**ASSETS**

	<b>2010</b>	<b>2009</b>
Current assets:		
Cash and cash equivalents	\$ 31,768	\$ 52,648
Available-for-sale securities	13,641	4,241
Receivables, net	19,732	20,716
Inventories	35,081	30,024
Prepaid expenses and other	1,284	1,434
Deferred taxes, net	2,578	2,186
Total current assets	104,084	111,249
Property and equipment, net	13,882	13,920
Other assets:		
Goodwill	4,346	4,346
Available-for-sale securities	6,763	621
Deposits and other assets	435	61
Deferred taxes, net	470	—
Total other assets	12,014	5,028
Total assets	\$ 129,980	\$ 130,197

**LIABILITIES AND STOCKHOLDERS' EQUITY**

Current liabilities:		
Accounts payable	\$ 11,945	\$ 9,553
Accrued expenses	12,637	9,481
Dividends payable	85	—
Total current liabilities	24,667	19,034
Long-term liabilities:		
Dividends payable	1,985	1,022
Deferred taxes, net	—	245
Other	2,880	203
Total long-term liabilities	4,865	1,470
Commitments and contingencies		
Stockholders' equity:		
Preferred stock, par value \$.01 per share; shares authorized-10,000,000; no shares issued and outstanding	—	—
Class A common stock, par value \$.01 per share; shares authorized - 50,000,000; shares issued and outstanding -12,880,038 (2010) and 12,660,932 (2009)	129	126
Class B common stock, par value \$.01 per share; shares authorized - 25,000,000; shares issued and outstanding -14,973,148	150	150
Additional paid-in capital	91,481	89,367
Accumulated other comprehensive loss	(78)	(106)
Retained earnings	8,766	20,156
Total stockholders' equity	100,448	109,693
Total liabilities and stockholders' equity	\$ 129,980	\$ 130,197

See notes to consolidated financial statements.

**SCHIFF NUTRITION INTERNATIONAL, INC. AND SUBSIDIARIES**  
**CONSOLIDATED STATEMENTS OF INCOME**  
**YEARS ENDED MAY 31, 2010, 2009 AND 2008**  
*(dollars in thousands, except share data)*

	<u>2010</u>	<u>2009</u>	<u>2008</u>
Net sales	\$ 204,887	\$ 190,691	\$ 176,914
Cost of goods sold	<u>119,837</u>	<u>123,861</u>	<u>102,491</u>
Gross profit	<u>85,050</u>	<u>66,830</u>	<u>74,423</u>
Operating expenses:			
Selling and marketing	33,611	33,702	31,366
General and administrative	17,883	13,669	22,475
Research and development	4,746	4,273	4,249
Reimbursement of import costs	<u>—</u>	<u>—</u>	<u>(31)</u>
Total operating expenses	<u>56,240</u>	<u>51,644</u>	<u>58,059</u>
Income from operations	<u>28,810</u>	<u>15,186</u>	<u>16,364</u>
Other income (expense):			
Interest income	174	888	2,045
Interest expense	(350)	(123)	(128)
Other, net	<u>8</u>	<u>(4)</u>	<u>13</u>
Total other income (expense), net	<u>(168)</u>	<u>761</u>	<u>1,930</u>
Income before income taxes	28,642	15,947	18,294
Income tax expense	<u>10,196</u>	<u>5,617</u>	<u>6,992</u>
Net income	<u>\$ 18,446</u>	<u>\$ 10,330</u>	<u>\$ 11,302</u>
Weighted average shares outstanding:			
Basic	<u>28,360,184</u>	<u>27,332,659</u>	<u>26,636,315</u>
Diluted	<u>28,928,162</u>	<u>28,637,848</u>	<u>27,999,755</u>
Net income per share:			
Basic	<u>\$ 0.65</u>	<u>\$ 0.38</u>	<u>\$ 0.42</u>
Diluted	<u>\$ 0.64</u>	<u>\$ 0.36</u>	<u>\$ 0.40</u>

See notes to consolidated financial statements.

**SCHIFF NUTRITION INTERNATIONAL, INC. AND SUBSIDIARIES**  
**CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY**  
**YEARS ENDED MAY 31, 2010, 2009 AND 2008**  
*(in thousands)*

	Common Stock		Class B Amount	Add'l Paid-In Capital	Accum. Other Comp. Loss	Retained Earnings	Total
	Class A						
	Shares	Amount					
<b>Balance at June 1, 2007</b>	11,664	\$ 116	\$ 150	\$ 92,640	\$ —	\$ 31,189	\$ 124,095
Comprehensive income:							
Net income	—	—	—	—	—	11,302	11,302
Other comprehensive income	—	—	—	—	—	—	—
Total comprehensive income							11,302
Stock options exercised	77	1	—	259	—	—	260
Excess tax benefit from equity instruments	—	—	—	407	—	—	407
Stock received for payment of income taxes on stock-based compensation	(23)	—	—	(120)	—	—	(120)
Special cash dividend	—	—	—	(12,340)	—	(32,577)	(44,917)
Restricted shares issued	64	1	—	(1)	—	—	—
Stock-based compensation	—	—	—	3,691	—	—	3,691
Special dividend stock-based compensation expense	—	—	—	4,857	—	—	4,857
Adoption of ASC 740-10	—	—	—	—	—	(88)	(88)
<b>Balance at May 31, 2008</b>	11,782	118	150	89,393	—	9,826	99,487
Comprehensive income:							
Net income	—	—	—	—	—	10,330	10,330
Available-for-sale debt securities valuation adjustment, net of income taxes	—	—	—	—	(106)	—	(106)
Total comprehensive income							10,224
Stock options exercised	533	5	—	1,567	—	—	1,572
Common stock surrendered for cashless options exercised	(188)	(2)	—	(1,187)	—	—	(1,189)
Excess tax benefit from equity instruments	—	—	—	654	—	—	654
Stock received for payment of income taxes on stock-based compensation	(304)	(3)	—	(1,687)	—	—	(1,690)
Restricted shares issued	862	8	—	(8)	—	—	—
Cancellation of restricted stock	(24)	—	—	—	—	—	—
Stock-based compensation	—	—	—	613	—	—	613
Special dividend stock-based compensation expense	—	—	—	22	—	—	22
<b>Balance at May 31, 2009</b>	12,661	126	150	89,367	(106)	20,156	109,693
Comprehensive income:							
Net income	—	—	—	—	—	18,446	18,446
Available-for-sale debt securities valuation adjustment, net of income taxes	—	—	—	—	28	—	28
Total comprehensive income							18,474
Stock options exercised	268	3	—	693	—	—	696
Common stock surrendered for cashless options exercised	(86)	(1)	—	(533)	—	—	(534)
Excess tax benefit from equity instruments	—	—	—	596	—	—	596
Stock received for payment of income taxes on stock-based compensation	(2)	—	—	(10)	—	—	(10)
Special cash dividends	—	—	—	—	—	(29,836)	(29,836)
Restricted shares issued	52	1	—	(1)	—	—	—
Cancellation of restricted stock	(13)	—	—	—	—	—	—
Stock-based compensation	—	—	—	863	—	—	863
Special dividend stock-based compensation expense	—	—	—	506	—	—	506
<b>Balance at May 31, 2010</b>	12,880	\$ 129	\$ 150	\$ 91,481	\$ (78)	\$ 8,766	\$ 100,448

See notes to consolidated financial statements.

**SCHIFF NUTRITION INTERNATIONAL, INC. AND SUBSIDIARIES**  
**CONSOLIDATED STATEMENTS OF CASH FLOWS**  
**YEARS ENDED MAY 31, 2010, 2009 AND 2008**  
*(dollars in thousands)*

	<u>2010</u>	<u>2009</u>	<u>2008</u>
Cash flows from operating activities:			
Net income	\$ 18,446	\$ 10,330	\$ 11,302
Adjustments to reconcile net income to net cash provided by operating activities:			
Deferred taxes	(1,084)	50	65
Depreciation and amortization	3,105	3,083	3,475
Amortization of debt issue costs	156	12	15
Loss (gain) on disposition of property and equipment	(4)	2	—
Stock-based compensation	2,217	635	8,548
Excess tax benefit from equity instruments	(596)	(654)	(407)
Other	16	5	(3)
Changes in operating assets and liabilities:			
Receivables	47	1,495	(2,835)
Inventories	(5,057)	(791)	(5,535)
Prepaid expenses and other	150	514	203
Deposits and other assets	—	(61)	78
Accounts payable	2,237	(1,529)	3,672
Accrued expenses	3,156	(1,672)	611
Income taxes receivable/payable	1,488	979	(3,691)
Other long-term liabilities	1,830	63	47
	<u>26,107</u>	<u>12,461</u>	<u>15,545</u>
Net cash provided by operating activities			
Cash flows from investing activities:			
Purchase of property and equipment	(2,942)	(3,434)	(3,200)
Proceeds from disposition of property and equipment	17	1	35
Purchase of available-for-sale securities	(25,761)	(5,995)	(33,590)
Proceeds from sale of available-for-sale securities	10,269	5,517	74,844
	<u>(18,417)</u>	<u>(3,911)</u>	<u>38,089</u>
Net cash provided by (used in) investing activities			
Cash flows from financing activities:			
Proceeds from debt	—	1,338	1,350
Payments on debt	—	(1,338)	(1,350)
Dividends paid	(28,788)	(1,225)	(42,670)
Proceeds from stock options exercised	162	383	260
Purchase and retirement of common stock	(10)	(1,690)	(120)
Excess tax benefit from equity instruments	596	654	407
Payments for debt issue costs	(530)	—	—
	<u>(28,570)</u>	<u>(1,878)</u>	<u>(42,123)</u>
Net cash used in financing activities			
Effect of exchange rate changes on cash	—	(3)	5
Increase (decrease) in cash and cash equivalents	(20,880)	6,669	11,516
Cash and cash equivalents, beginning of year	<u>52,648</u>	<u>45,979</u>	<u>34,463</u>
Cash and cash equivalents, end of year	<u>\$ 31,768</u>	<u>\$ 52,648</u>	<u>\$ 45,979</u>

See notes to consolidated financial statements.

**SCHIFF NUTRITION INTERNATIONAL, INC. AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

*(dollars in thousands, except share data)*

**1. SIGNIFICANT ACCOUNTING POLICIES**

**Description of Business** – We develop, manufacture, market and distribute branded and private label vitamins, nutritional supplements and nutrition bars in the United States and throughout the world. We offer a broad range of capsules, tablets and nutrition bars. Our portfolio of recognized brands, including Schiff, Move Free, MegaRed and Tiger’s Milk, is marketed primarily through the mass market (including club) and, to a lesser extent, health food store distribution channels.

**Principles of Consolidation** – Our consolidated financial statements include the accounts of Schiff Nutrition International, Inc. and its wholly-owned subsidiaries. All significant inter-company accounts and transactions have been eliminated. We are a majority-owned subsidiary of Weider Health and Fitness (“WHF”).

**Use of Estimates and Assumptions in Preparing Financial Statements** – In preparing our consolidated financial statements, we make assumptions, estimates and judgments that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the dates of the consolidated financial statements and the reported amounts of net sales and expenses during the reported periods. We periodically evaluate our estimates and judgments related to the valuation of available-for-sale securities, inventories and intangible assets, allowances for doubtful accounts, sales returns and discounts, uncertainties related to certain tax benefits, valuation of deferred tax assets, valuation of share-based payments and recoverability of long-lived assets. Our estimates are based on historical experience and on our future expectations that are believed to be reasonable. The combination of these factors forms the basis for making judgments about the carrying values of assets and liabilities that are not readily apparent from other sources. Actual results may differ from our current estimates and those differences may be material.

**Cash Equivalents** – Cash equivalents include highly liquid investments with a remaining maturity at date of acquisition of three months or less.

**Available-for-Sale Securities** – Available-for-sale securities, consisting of certificates of deposit, commercial paper and debt securities, are carried at their fair value based upon the quoted market prices or other valuation methods at period end. Accordingly, unrealized gains and losses, net of income taxes, are computed on the basis of specific identification and included in accumulated other comprehensive income or loss in stockholders’ equity until realized. We periodically evaluate whether any declines in the fair values of our available-for-sale securities are other-than temporary. This evaluation consists of a review of qualitative and quantitative factors, including available quoted market prices; recent financial results and operating trends of the company that issued the securities; other publicly available information; implied values from any recent financing by the company that issued the security; or other conditions that indicate the value of our investments.

**Receivables** – Receivables are reported at estimated net realizable values. Accordingly, we estimate allowances for doubtful accounts, sales returns and discounts. The allowance for doubtful accounts is estimated by reviewing delinquency status, determined by classifying, or aging, individual invoices in terms of the length of the period past due, and analyzing historical account write-off rates relative to receivable balances. Receivables are written off when determined to be uncollectible. The allowance for sales returns is estimated by reviewing open sales return authorizations granted to customers and analyzing historical return rates relative to sales. Allowances for cash discounts are estimated by reviewing customer payment terms and historical remittances. Accounts with credit balances are reported as current liabilities in the balance sheet.

**Inventories** – Inventories, primarily consisting of direct materials, direct labor and manufacturing overhead, are stated at the lower of cost (on a first-in, first-out basis) or market value.

**Property and Equipment** – Property and equipment are stated at cost less accumulated depreciation. Depreciation and amortization expense was \$3,105 (2010), \$3,083 (2009) and \$3,475 (2008), computed using the straight-line method over the estimated useful lives of 2 to 10 years for furniture and equipment and 3 to 16 years for leasehold improvements. Leasehold improvements are depreciated over the shorter of their useful life or of the lease term.

**Intangible Assets** – Goodwill and other intangible assets with indefinite lives are tested for impairment, at least annually during the fourth quarter of each fiscal year, rather than amortized. Other intangibles with definite lives are amortized using the straight-line method over estimated useful lives of 2 to 5 years.

**Long-Lived Assets** – We evaluate the carrying value of long-lived assets based upon current and anticipated undiscounted cash flows, and recognize an impairment when such estimated cash flows will be less than the carrying value of the asset. This evaluation is performed whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. Measurement of the amount of impairment, if any, is based upon the difference between carrying value and fair value.

**SCHIFF NUTRITION INTERNATIONAL, INC. AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - (continued)**

*(dollars in thousands, except share data)*

**Income Taxes** – We record deferred income tax assets and liabilities for temporary differences in the basis of assets and liabilities as reported for financial statement purposes and income tax purposes. Deferred tax assets are reduced by a valuation allowance when, in our opinion, it is more likely than not that some portion or all of the deferred tax assets will not be realized.

**Capital Structure** – We have two classes of common stock outstanding. Both classes of common stock generally have identical rights and privileges, with the exception of voting and conversion, or transfer rights. Each holder of Class A or Class B common stock is entitled to share ratably in any dividends, liquidating distributions or consideration resulting from certain business combinations. However, each holder of Class A common stock is entitled to one vote for each share held while each holder of Class B common stock is entitled to ten votes for each share held. The holders of the Class A common stock and Class B common stock vote together as a single class. Class A common stock cannot be converted into any other securities of the Company, while Class B common stock holders have the right to convert their shares into Class A common stock on a one-to-one basis. In addition, generally, any shares of Class B common stock that are transferred will automatically convert into shares of Class A common stock on a one-to-one basis.

**Operating Segments** – We believe our business, which consists of the aggregation of several product based operating segments, represents our only reportable segment.

**Revenue Recognition** – Sales are recognized when all of the following criteria are met: (1) persuasive evidence of an arrangement exists; (2) delivery has occurred or services have been rendered; (3) the seller's price to the buyer is fixed or determinable; and, (4) collectibility is reasonably assured. Although we utilize a variety of shipping terms, our primary shipping terms are "FOB Destination."

Net sales represent products at gross sales price, less estimated returns and allowances for which provisions are made at the time of sale and less certain other discounts, allowances and sales incentives. We utilize various types of sales incentives and promotions in marketing our products; including, price reductions, coupons, rebate offers, slotting fees and free product. Generally, the cost of these sales incentives and promotions, with the exception of free product, are accounted for as a direct reduction of sales. The cost of free product is classified as cost of goods sold.

**Sales by Geographic Area** – Total domestic and international, primarily Asia and Mexico, net sales amounted to \$192,922 and \$11,965, respectively, for fiscal 2010; \$181,966 and \$8,725, respectively, for fiscal 2009; and \$168,979 and \$7,935, respectively, for fiscal 2008. Net sales are attributed to the country in which our customer is located.

**Advertising Costs** – Advertising costs, including cooperative advertising payments to retailers, are charged to expense in the period that the advertising first takes place. Cooperative advertising payments to retailers are generally accounted for as an operating expense; however, the portion of the cost in excess of the estimated fair value of the benefit received is classified as a direct reduction of sales. Total advertising costs, included in selling and marketing expenses, were \$15,105, \$14,514 and \$12,669, respectively, for fiscal 2010, 2009 and 2008.

**Costs of Goods Sold and Shipping and Handling Costs** – Costs of goods sold include expenses incurred to acquire and produce inventory for sales, including product costs, purchasing costs, freight-in, import costs, internal transfer costs, quality assurance costs and certain warehousing, or handling, costs associated with the receiving or manufacturing of goods for sale.

Shipping and certain warehousing, or handling, costs which are not associated with the receiving or manufacturing of goods for sale are excluded from costs of goods sold. Shipping costs, included in selling and marketing expenses, were \$5,063, \$5,774 and \$4,833, respectively, for fiscal 2010, 2009 and 2008. Handling costs, included in general and administrative expenses, were \$2,796, \$3,130 and \$2,716, respectively, for fiscal 2010, 2009 and 2008.

**Concentration of Credit Risk and Significant Customers and Products** – Financial instruments that potentially subject us to significant concentrations of credit risk consist primarily of cash and cash equivalents, available-for-sale securities and accounts receivable.

Generally, our cash and cash equivalents, which may include money market accounts, certificates of deposit, United States Treasury Bills with maturities of three months or less, and high-quality commercial paper exceed Federal Deposit Insurance Corporation limits on insurable amounts; thus exposing us to certain credit risk. We minimize our risk by investing in or through major financial institutions. We have not experienced any realized losses on our cash equivalents and available-for-sale securities.

At May 31, 2010, we held \$20,404 in available-for-sale securities; consisting of \$5,813 in certificates of deposit and commercial paper and \$14,591 in debt securities, including \$455 in illiquid auction rate securities ("ARS") which are fully insured state agency issued securities. In determining the fair value of our available-for-sale securities at May 31, 2010, we have taken into consideration

**SCHIFF NUTRITION INTERNATIONAL, INC. AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - (continued)**

*(dollars in thousands, except share data)*

quoted market prices and/or other considerations, including fair values determined by the financial institutions, current credit rating of the debt securities, insurance provisions, discounted cash flow analysis, as deemed appropriate, and our current liquidity position. Although we believe the debt securities will ultimately be liquidated at or near our cost basis, any impairment in the value of these securities could adversely impact our results of operations and financial condition.

With respect to accounts receivable, we perform ongoing credit evaluations of our customers and monitor collections from customers continuously. We maintain an allowance for doubtful accounts which is based upon historical experience as well as specific customer collection issues. Historically, bad debt expense has not been significant and has been within expectations and allowances established. However, we cannot guarantee that we will continue to experience the same credit loss rates that we have in the past. If the financial condition of one or more of our customers were to deteriorate, additional allowances may be required.

The combined net sales to our two largest customers are significant. At May 31, 2010 and May 31, 2009, respectively, amounts due from Customer A represented approximately 45% and 46%, and amounts due from Customer B represented approximately 26% and 24%, of total trade accounts receivable. For fiscal 2010, 2009 and 2008, respectively, Customer A accounted for approximately 40%, 44% and 39% and Customer B accounted for approximately 32%, 32% and 35% of total net sales. Of total net sales, our Schiff® Move Free® brand accounted for approximately 35%, 37% and 47%, respectively, for fiscal 2010, 2009 and 2008.

**Stock-Based Compensation** – For equity-classified awards, compensation expense is recognized over the requisite service period based on the computed fair value on the grant date of the award. For liability-classified awards, fluctuations in the fair value of the liability, which is remeasured at each reporting period until the award is settled, are recorded as increases or decreases in compensation expense either immediately or over the remaining service period depending on the vested status of the award.

**Net Income Per Share** – Basic net income per share is computed using the weighted average number of common shares outstanding during the period. Diluted net income per share is computed using the weighted average number of common shares and potentially diluted common shares outstanding during the period. Potentially dilutive common shares consist of common stock options, restricted stock and restricted stock units (“Common Stock Equivalents”).

**Fair Value Measurements** – We measure the fair value of a financial instrument as the amount that could be received upon the sale of an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. Financial assets are marked to bid prices and financial liabilities are marked to offer prices. Fair value measurements do not include transaction costs. A fair value hierarchy is used to prioritize the quality and reliability of the information used to determine fair values. Categorization within the fair value hierarchy is based on the lowest level of input that is significant to the fair value measurement. The fair value hierarchy is defined into the following three categories:

Level 1: Quoted market prices in active markets for identical assets or liabilities.

Level 2: Observable market based inputs or unobservable inputs that are corroborated by market data.

Level 3: Unobservable inputs that are not corroborated by market data.

In determining the fair value of a financial asset in an inactive or dislocated market, we utilize facts and circumstances that may require significant management judgment; including, using inputs based on management estimates or assumptions, or making adjustments to observable inputs to determine fair value when markets are not active and relevant observable inputs are not available.

**Financial Instruments** – Our financial instruments, including primarily cash and cash equivalents, accounts receivable and accounts payable, when valued using market interest rates, would not be materially different from the amounts presented in the consolidated financial statements.

**Foreign Currency Translation** – We consider the local currency as the functional currency for our foreign operations. Assets and liabilities are translated at period-end exchange rates and all amounts included in the statements of income and cash flows are translated using average monthly rates.

**Reimbursement of Import Costs** – Our operating results for fiscal 2008 were favorably impacted by \$31 in reimbursement of import costs from certain suppliers. These reimbursements, resulting primarily from the favorable outcome of litigation between one of our suppliers and the U.S. Government, represent refunds of previously paid tariffs on imported raw materials.

**Recently Issued Accounting Standards** – In July 2006, the Financial Accounting Standards Board (“FASB”) issued guidance now codified as Accounting Standards Codification (“ASC”) 740-10, “Income Taxes”, which establishes guidelines for recognizing, measuring and disclosing uncertainties relating to tax benefits reflected in an enterprise’s financial statements. ASC 740-10 establishes a “more-likely-than-not” recognition threshold that must be met before a tax benefit, relative to a tax position in which the enterprise may be uncertain as to whether it will ultimately be sustained as filed in its tax return, can be recognized in the financial

**SCHIFF NUTRITION INTERNATIONAL, INC. AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - (continued)**

*(dollars in thousands, except share data)*

statements. We were required to apply the provisions of ASC 740-10 on June 1, 2007. The cumulative effect of adopting ASC 740-10 resulted in a decrease in retained earnings of approximately \$88. The total amount of unrecognized tax benefits at June 1, 2007 was \$473, which includes unrecognized tax benefits of \$88.

In December 2007, the FASB issued guidance now codified as ASC 805-10, "Business Combinations" that requires all business combinations completed after the effective date to be accounted for by applying the acquisition method (previously referred to as the purchase method). ASC 805-10 requires that the acquirer be identified and that the acquirer recognize the fair values of the identifiable assets acquired, liabilities assumed, and any noncontrolling interests in the acquiree at the acquisition date. In the case of a bargain purchase, the acquirer is required to reevaluate the measurements of the recognized assets and liabilities at the acquisition date and recognize a gain on that date if an excess remains. ASC 805-10 became effective for fiscal periods beginning after December 15, 2008. This accounting standard will be applied to acquisitions occurring after May 31, 2009, and will also require us to expense any costs related to such acquisitions.

In June 2009, the FASB issued ASC 105-10, "Generally Accepted Accounting Principles-Overall," which superseded all existing accounting standard documents and became the single source of authoritative non-governmental generally accepted accounting principles accepted in the United States ("GAAP"). ASC 105-10 was implemented on July 1, 2009 and is effective for interim and annual periods ending after September 15, 2009. We adopted ASC 105-10 in our fiscal 2010 second quarter. The adoption did not have an impact on our results of operations or financial condition. However, because ASC 105-10 completely replaces existing standards, it affects the way GAAP is referenced within the financial statements.

**2. AVAILABLE-FOR-SALE SECURITIES**

Available-for-sale securities at fair value consist of the following at May 31:

	<u>2010</u>	<u>2009</u>
Certificates of deposit and commercial paper	\$ 5,813	\$ 4,241
Federal, state and municipal debt securities	5,497	483
Corporate debt securities	<u>9,094</u>	<u>138</u>
<b>Total</b>	<b>20,404</b>	<b>4,862</b>
Less long-term portion	<u>6,763</u>	<u>621</u>
Short-term portion	<u>\$ 13,641</u>	<u>\$ 4,241</u>

Available-for-sale securities include ARS, long-term variable rate bonds tied to short-term interest rates that are reset through a "dutch auction" process which occurs every 7 to 35 days, and other variable rate debt securities. Despite the underlying long-term contractual maturity of ARS, there generally was a ready liquid market for these securities based on the interest reset mechanism. However, as a result of negative liquidity and uncertainty in financial credit markets, we experienced "failed" auctions associated with our ARS. In the case of a failed auction, the ARS become illiquid long-term bonds (until a future auction is successful, the security is called prior to the contractual maturity date by the issuer, or the securities mature) and the rates are reset in accordance with terms in the prospectus/offering circular. At May 31, 2010, total available-for-sale securities included \$671 in debt securities, including \$455 in illiquid ARS, valued below cost which are included in long-term assets. The ARS consist of fully insured, state agency issued securities.

Available-for-sale securities were measured at fair value using the following inputs at May 31:

	<u>2010</u>	<u>2009</u>
Quoted prices in active markets for identical assets (Level 1)	\$ 19,949	\$ 4,379
Significant other observable inputs (Level 2)	—	—
Significant unobservable inputs (Level 3)	<u>455</u>	<u>483</u>
<b>Total</b>	<u>\$ 20,404</u>	<u>\$ 4,862</u>

**SCHIFF NUTRITION INTERNATIONAL, INC. AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - (continued)**

*(dollars in thousands, except share data)*

The following is a reconciliation of the beginning and ending balances of available-for-sale securities measured at fair value using significant unobservable inputs (Level 3) for the year ended May 31:

	<u>2010</u>	<u>2009</u>
Beginning balance	\$ 483	\$ 1,265
Total losses (all unrealized and included in accumulated other comprehensive loss)	(28)	(17)
Sales	—	(465)
Transfers out	—	(300)
Ending balance	<u>\$ 455</u>	<u>\$ 483</u>

Contractual maturities of debt securities are as follows at May 31, 2010:

Less than one year	\$ 7,828
One to five years	6,092
Over five years	671
Total	<u>\$ 14,591</u>

### 3. RECEIVABLES, NET

Receivables, net, consist of the following at May 31:

	<u>2010</u>	<u>2009</u>
Trade accounts	\$ 20,878	\$ 21,341
Refundable income taxes	707	1,644
Other	116	66
	21,701	23,051
Less allowances for doubtful accounts, sales returns and discounts	(1,969)	(2,335)
Total	<u>\$ 19,732</u>	<u>\$ 20,716</u>

### 4. INVENTORIES

Inventories consist of the following at May 31:

	<u>2010</u>	<u>2009</u>
Raw materials	\$ 15,299	\$ 12,021
Work in process	1,910	1,270
Finished goods	17,872	16,733
Total	<u>\$ 35,081</u>	<u>\$ 30,024</u>

### 5. PROPERTY AND EQUIPMENT, NET

Property and equipment, net, consists of the following at May 31:

	<u>2010</u>	<u>2009</u>
Furniture and equipment	\$ 38,480	\$ 35,647
Leasehold improvements	12,252	11,890
Construction in progress	1,156	1,962
Total cost	51,888	49,499
Less accumulated depreciation and amortization	(38,006)	(35,579)
Total, net	<u>\$ 13,882</u>	<u>\$ 13,920</u>

**SCHIFF NUTRITION INTERNATIONAL, INC. AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - (continued)**  
*(dollars in thousands, except share data)*

Purchase of property and equipment included in accounts payable amounted to \$206, \$68 and \$63, respectively, at May 31, 2010, 2009 and 2008.

**6. GOODWILL AND INTANGIBLE ASSETS, NET**

Goodwill and intangible assets, net, consist of the following at May 31:

	<u>2010</u>			<u>2009</u>		
	<u>Gross Carrying Amount</u>	<u>Accumul. Amortiz.</u>	<u>Net Book Value</u>	<u>Gross Carrying Amount</u>	<u>Accumul. Amortiz.</u>	<u>Net Book Value</u>
Goodwill	\$ 4,346	\$ —	\$ 4,346	\$ 4,346	\$ —	\$ 4,346
Intangible assets - patents and trademarks	\$ 700	\$ (700)	\$ —	\$ 700	\$ (700)	\$ —

Estimated amortization expense, assuming no changes in our intangible assets, is zero for all future fiscal years.

**7. ACCRUED EXPENSES**

Accrued expenses consist of the following at May 31:

	<u>2010</u>	<u>2009</u>
Accrued personnel related costs	\$ 5,323	\$ 1,652
Accrued promotional costs	6,076	6,225
Other	1,238	1,604
Total	<u>\$ 12,637</u>	<u>\$ 9,481</u>

**8. INCOME TAXES**

The components of income tax expense for fiscal 2010, 2009 and 2008, are as follows:

	<u>2010</u>	<u>2009</u>	<u>2008</u>
Federal:			
Current	\$ 10,365	\$ 4,936	\$ 6,246
Deferred	(976)	48	58
State and local:			
Current	915	631	681
Deferred	(108)	2	7
Total	<u>\$ 10,196</u>	<u>\$ 5,617</u>	<u>\$ 6,992</u>

Income tax expense differs from a calculated income tax at the Federal statutory rate as follows:

	<u>2010</u>	<u>2009</u>	<u>2008</u>
Computed Federal income tax expense at the statutory rate of 35%	\$ 10,025	\$ 5,581	\$ 6,403
State income tax expense	793	632	688
Tax exempt interest	(4)	(28)	(292)
Other	(618)	(568)	193
Total	<u>\$ 10,196</u>	<u>\$ 5,617</u>	<u>\$ 6,992</u>

Net cash income tax payments amounted to \$9,655, \$4,524 and \$10,574, respectively, for fiscal 2010, 2009 and 2008.

**SCHIFF NUTRITION INTERNATIONAL, INC. AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - (continued)**

*(dollars in thousands, except share data)*

Deferred income taxes, net, consist of the following at May 31:

	<u>2010</u>		<u>2009</u>	
	<u>Current</u>	<u>Long-Term</u>	<u>Current</u>	<u>Long-Term</u>
<b>Assets:</b>				
Accounts receivable allowances	\$ 596	\$ —	\$ 666	\$ —
Inventories adjustment	1,069	—	903	—
Long-term incentive awards	—	2,655	—	1,430
Accrued vacation, bonuses, dividends and other	1,354	439	1,115	563
<b>Total</b>	<b>3,019</b>	<b>3,094</b>	<b>2,684</b>	<b>1,993</b>
<b>Liabilities:</b>				
Basis differences in fixed and intangible assets	—	(2,624)	—	(2,186)
Prepaid insurance	(162)	—	(298)	—
Other	(279)	—	(200)	(52)
<b>Total</b>	<b>(441)</b>	<b>(2,624)</b>	<b>(498)</b>	<b>(2,238)</b>
<b>Deferred income taxes, net</b>	<b>\$ 2,578</b>	<b>\$ 470</b>	<b>\$ 2,186</b>	<b>\$ (245)</b>

At May 31, 2010, we have no net operating loss, capital loss or tax credit carryforwards. The amount of the deferred tax assets considered realizable, could be reduced or increased in the near-term if facts, including the amount of taxable income, differs from our estimates.

A reconciliation of the beginning and ending amount of unrecognized tax benefits (excluding interest and penalties) is as follows:

Balance at June 1, 2007	\$ 444
Additions based on tax positions related to the current year	37
Balance at May 31, 2008	481
Additions based on tax positions related to the current year	54
Additions based on tax positions related to prior years	45
Reductions for tax positions of prior years	(384)
Balance at May 31, 2009	196
Additions based on tax positions related to the current year	121
Additions based on tax positions related to prior years	38
Reductions for tax positions of prior years	(26)
Balance at May 31, 2010	\$ 329

Of the total unrecognized tax benefits of \$329 at May 31, 2010, \$304 would affect the effective income tax rate, if recognized. During fiscal 2010, unrecognized tax benefits for certain timing differences related to the amortization of certain intangible assets decreased by \$26 due to the lapse of applicable statute of limitations. We recognize interest and penalties accrued related to unrecognized tax benefits in income tax expense. During fiscal 2010, we recognized an increase of \$4 in interest and penalties. During fiscal 2009, we recognized a decrease of \$36 in interest and penalties. At May 31, 2010 and 2009, respectively, we had \$11 and \$7 in accrued interest and penalties. The total unrecognized tax benefit accrued (including interest and penalties) was \$340 and \$203, respectively, at May 31, 2010 and 2009. We do not anticipate that unrecognized tax benefits will significantly increase or decrease within 12 months of the reporting date. We file income tax returns in the U.S. federal jurisdiction, and in various state and local jurisdictions. We are no longer subject to U.S. federal income tax examinations for years prior to fiscal 2007, and we are no longer subject to state and local income tax examinations for years prior to fiscal 2006.

## 9. CASH DIVIDENDS

In July 2007, our Board of Directors approved a \$1.50 per share special cash dividend, which was paid on August 13, 2007 to shareholders of record of Class A and Class B common stock at the close of business on July 31, 2007. In connection with the declaration of the special dividend, our Board of Directors approved certain dividend equivalent rights, allowing holders of certain

**SCHIFF NUTRITION INTERNATIONAL, INC. AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - (continued)**

*(dollars in thousands, except share data)*

equity awards, including stock options and restricted stock units, to receive cash dividends on each share of common stock underlying the stock options and restricted stock units. In aggregate, at July 31, 2007, the record date, the Company had outstanding approximately 29.9 million shares of common stock (including shares of common stock underlying equity awards subject to dividend equivalent rights), including approximately 26.6 million shares of outstanding Class A and Class B common stock, approximately 1.8 million shares of Class A common stock underlying outstanding stock options, and approximately 1.5 million shares of Class A common stock underlying outstanding restricted stock units. The aggregate amount of the special dividend was approximately \$44,917; \$22,457 for holders of Class A common stock, including \$4,883 for Class A common stock underlying certain equity awards, and \$22,460 for the holder of Class B common stock. At May 31, 2008, we had unpaid dividends of \$2,247, of which \$1,016 remains unpaid at May 31, 2010.

In July 2009, our Board of Directors approved a \$0.50 per share special cash dividend, payable on August 28, 2009 to shareholders of record of Class A and Class B common stock at the close of business on August 14, 2009. In connection with the declaration of the special dividend, our Board of Directors approved dividend equivalent rights, allowing holders (employees and directors) of certain equity awards, including stock options and restricted stock units, to receive cash dividends on each share of common stock underlying the stock options and restricted stock units. In aggregate, at August 14, 2009, the record date, we had outstanding approximately 29.9 million shares of common stock (including shares of common stock underlying equity awards subject to dividend equivalent rights), including approximately 27.6 million shares of outstanding Class A and Class B common stock, approximately 1.3 million shares of Class A common stock underlying outstanding stock options, and approximately 1.0 million shares of Class A common stock underlying outstanding restricted stock units. The aggregate amount of the special dividend was approximately \$14,927, presuming 100% vesting of shares underlying equity awards; \$7,440 for holders of Class A common stock, including \$1,105 for Class A common stock underlying equity awards, and \$7,487 for the holder of Class B common stock.

In March 2010, our Board of Directors approved a \$0.50 per share special cash dividend, which was paid on April 14, 2010 to shareholders of record of Class A and Class B common stock at the close of business on March 31, 2010. In connection with the declaration of the special dividend, our Board of Directors approved dividend equivalent rights, allowing holders (employees and directors) of certain equity awards, including stock options and restricted stock units, to receive cash dividends on each share of common stock underlying the stock options and restricted stock units. In aggregate, at March 31, 2010, the record date, we had outstanding 29.8 million shares of common stock (including shares of common stock underlying equity awards subject to dividend equivalent rights), including 27.8 million shares of outstanding Class A and Class B common stock, 1.0 million shares of Class A common stock underlying outstanding stock options, and 1.0 million shares of Class A common stock underlying outstanding restricted stock units. The aggregate amount of the special dividend was approximately \$14,909, presuming 100% vesting of shares underlying equity awards; \$7,422 for holders of Class A common stock, including \$991 for Class A common stock underlying equity awards, and \$7,487 for the holder of Class B common stock.

In connection with the dividends paid or payable on the dividend equivalent rights received by holders (employees and directors) of stock options and certain restricted stock units, we recognized non-cash compensation expense and corresponding increase in additional paid-in capital of \$506, \$22 and \$4,857, respectively, during fiscal 2010, 2009 and 2008; and cash compensation expense of \$63 during fiscal 2008.

With respect to outstanding restricted stock and restricted stock units that were unvested at May 31, 2010, or for which the issuance of shares underlying restricted stock units has been deferred, the dividends will not be distributed until after such equity awards vest or the deferred shares are issued. At May 31, 2010, we had unpaid dividends of \$1,054 relating to dividends declared during fiscal 2010.

**10. ACCUMULATED OTHER COMPREHENSIVE LOSS**

The components of accumulated other comprehensive loss for fiscal 2010 and 2009, are as follows:

<b>2010:</b>	<u>Pre-tax Loss</u>	<u>Tax Expense</u>	<u>Net Loss</u>
Available-for-sale debt securities valuation adjustment:			
Unrealized gains	\$ 129	\$ 51	\$ 78
Reclassification adjustment for realized loss (gain)	—	—	—
Net unrealized loss	<u>\$ 129</u>	<u>\$ 51</u>	<u>\$ 78</u>

**SCHIFF NUTRITION INTERNATIONAL, INC. AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - (continued)**

*(dollars in thousands, except share data)*

<b>2009:</b>	<u>Pre-tax Loss</u>	<u>Tax Expense</u>	<u>Net Loss</u>
Available-for-sale debt securities valuation adjustment:			
Unrealized gains	\$ 179	\$ 73	\$ 106
Reclassification adjustment for realized loss (gain)	—	—	—
Net unrealized loss	<u>\$ 179</u>	<u>\$ 73</u>	<u>\$ 106</u>

We had no accumulated other comprehensive income or loss for fiscal 2008.

## 11. EARNINGS PER SHARE

The reconciliation of numerators and denominators basic and diluted earnings per share computations for fiscal 2010, 2009 and 2008, are as follows:

	<u>2010</u>	<u>2009</u>	<u>2008</u>
Income available to common shareholders (numerator):			
Net income	\$ 18,446	\$ 10,330	\$ 11,302
Adjustments	—	—	—
Income on which basic and diluted earnings per share are calculated	<u>\$ 18,446</u>	<u>\$ 10,330</u>	<u>\$ 11,302</u>
Weighted-average number of common shares outstanding (denominator):			
Basic	28,360,184	27,332,659	26,636,315
Add-incremental shares from restricted stock	32,838	17,904	5,024
Add-incremental shares from restricted stock units	107,749	759,207	676,461
Add-incremental shares from stock options	427,391	528,078	681,955
Diluted	<u>28,928,162</u>	<u>28,637,848</u>	<u>27,999,755</u>

Options to purchase 254,000 shares of Class A common stock at prices ranges from \$4.61 to \$7.05 per share were outstanding during fiscal 2009 but were not included in the computation of diluted earnings per share because the options' exercise prices were greater than the average market price of the common shares.

## 12. STOCK-BASED COMPENSATION PLANS

Our 1997 Equity Participation Plan, as amended (the "1997 Plan"), provided for the granting of stock options, stock appreciation rights, restricted or deferred stock and other awards ("Awards") to officers, directors and key employees responsible for the direction and management of our company and to non-employee consultants. Such Awards were granted at fair value as of the date of grant. Under the 1997 Plan, a total of 3,500,000 shares of Class A common stock (or the equivalent in other equity securities) were reserved for issuance.

On October 26, 2004, our stockholders adopted the Schiff Nutrition International, Inc. 2004 Incentive Award Plan, as amended, (the "2004 Plan"). Our 2004 Plan provides for the grant of incentive stock options, nonqualified stock options, restricted stock, stock appreciation rights, performance shares, performance stock units, dividend equivalents, stock payments, deferred stock, restricted stock units, other stock-based awards, and performance-based awards to officers, directors, employees and consultants of our company and its subsidiaries.

Shares available for grant include 3,200,000 shares of Class A common stock reserved for issuance under the 2004 Plan, plus the number of shares of Class A common stock that as of the date of adoption of the 2004 Plan were, or thereafter would otherwise become, available for issuance under the 1997 Plan.

Stock options granted under the 1997 Plan and 2004 Plan primarily become exercisable after one to five years from the date of grant in equal, ratable amounts on each successive anniversary date. Stock options expire no later than eight years after the date of grant under the 1997 Plan and no later than ten years after the date of grant under the 2004 Plan.

The fair value of options granted was estimated at the date of grant using a Binomial Option pricing model with the following weighted average assumptions for fiscal 2009 and 2008, respectively. There were no options granted during fiscal 2010.

**SCHIFF NUTRITION INTERNATIONAL, INC. AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - (continued)**

*(dollars in thousands, except share data)*

	<b>2009</b>	<b>2008</b>
Expected volatility	32.80 %	48.92 %
Expected term	2.00 years	3.67 years
Risk-free interest rate	0.90 %	4.46 %
Dividend yield	0.00 %	0.00 %

Expected volatility is based on historical volatility of our stock. The expected term, which represents the period of time that options granted are expected to be outstanding, is based on historical data and other factors; including, exercise behavior patterns of differing groups of employees. The risk-free interest rate is based on the U.S. treasury yield curve in effect at the time of the grant.

Information relating to stock options issued under the 1997 Plan and 2004 Plan is as follows:

	<b>Number of Shares</b>	<b>Weighted Average Exercise Price</b>	<b>Weighted Average Remaining Contractual Term (in years)</b>	<b>Aggregate Intrinsic Value</b>
Options outstanding, June 1, 2007	1,826,651	\$ 2.77		
Granted	45,000	5.97		
Exercised	(77,167)	3.38		
Canceled, forfeited and/or expired	(5,000)	3.00		
Options outstanding, May 31, 2008	1,789,484	2.84		
Granted	15,000	4.68		
Exercised	(533,217)	2.95		
Canceled, forfeited and/or expired	—	—		
Options outstanding, May 31, 2009	1,271,267	2.82		
Granted	—	—		
Exercised	(267,600)	2.60		
Canceled, forfeited and/or expired	—	—		
Options outstanding, May 31, 2010	1,003,667	\$ 2.87	1.82	\$ 4,242
Exercisable options, May 31, 2010	1,003,667	\$ 2.87	1.82	\$ 4,242

The weighted average grant-date fair value of options granted was \$0.91 and \$2.90, respectively, for fiscal 2009 and 2008. The total intrinsic value of options exercised was \$927, \$1,772 and \$183, respectively, for fiscal 2010, 2009 and 2008. We received \$162, \$383 and \$260, respectively, for stock options exercised during fiscal 2010, 2009 and 2008. In addition, during fiscal 2010 and 2009, respectively, 86,064 and 188,024 shares of common stock valued at \$534 and \$1,189 (the aggregate exercise price) were surrendered as a result of 205,000 and 403,350 stock options exercised in cashless transactions.

Effective August 16, 2002, we issued 640,000 restricted shares of Class A common stock to certain officers and employees. The aggregate value of the restricted shares at issuance was \$1,038, which we expensed on a straight-line basis over the accompanying five-year vesting period. During fiscal 2008, 83,800 restricted shares vested. Concurrent with fiscal 2008 vesting, we reacquired (and ultimately retired) 22,676 shares from certain employees in connection with the payment of individual income taxes. As of May 31, 2009, of the 640,000 restricted shares originally issued, 528,800 shares vested, of which 103,338 shares were reacquired (and retired), and 111,200 shares were cancelled.

During fiscal 2010, 2009 and 2008, respectively, we granted 58,518, 113,146 and 114,157 restricted shares and restricted stock units to employee or non-employee directors at an average grant date fair value of \$5.74, \$5.11 and \$5.74 per share. The shares generally vest over three years. Unvested restricted shares and restricted stock units totaled 165,249, 182,146 and 133,144, respectively, at May 31, 2010, 2009 and 2008.

Stock-based compensation expense for stock options, restricted stock units and restricted shares amounted to \$406, \$365 and \$327, respectively, and the related tax benefit was approximately \$161, \$145 and \$125, respectively, for fiscal 2010, 2009 and

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**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - (continued)**

*(dollars in thousands, except share data)*

2008. At May 31, 2010, total unrecognized compensation cost related to these non-vested share-based compensation awards was approximately \$518, which is expected to be recognized over a weighted average period of 1.9 years.

On March 17, 2006, the Compensation Committee of our Board of Directors, pursuant to our 2004 Plan, approved the adoption of a long term incentive plan involving the grant of performance based restricted stock units (the "Units"). On March 20, 2006, a total of 1,437,200 Units were issued to certain officers and employees. Each Unit represents the right to receive one share of the Company's Class A common stock, subject to certain performance based vesting requirements. The Units vest based on the Company's performance in relation to certain specified pre-established performance criteria targets over a performance period beginning on January 1, 2006 and expiring on May 31, 2008. The performance criteria upon which the Units vest is based upon a "Business Value Created" formula, which is comprised of two performance criteria components: operating earnings and return on net capital. Based upon the amount of Business Value Credited in accordance with the formula, the Units were vested in full at May 31, 2008. The grant date fair value of each Unit was \$5.11. We recognized compensation expense over the performance period based on a periodic assessment of the probability that the performance criteria would be achieved. For fiscal 2008, we recognized compensation expense of \$3,364, and the related tax benefit was approximately \$1,286.

On December 12, 2008, the Compensation Committee of our Board of Directors, pursuant to our 2004 Incentive Award Plan, approved the grant of long term incentive performance awards ("Performance Awards") to certain officers and employees. The Performance Awards were granted based on a target award value of \$5,525, but will be earned based on the Company's cumulative performance against three pre-established financial performance targets over a performance period commencing October 1, 2008 and ending on May 31, 2011, as follows: (i) 50% of the award opportunity will be based on cumulative net sales for the performance period; (ii) 35% of the award opportunity will be based on cumulative operating income for the performance period; and (iii) 15% of the award opportunity will be based on cumulative net cash flow for the performance period; provided, however, that no amount will be earned or payable if cumulative operating income for the performance period does not meet or exceed a pre-established threshold amount. In the event that the cumulative operating income threshold is met, participants can earn from 17.5% of the target award value for the Company's threshold performance against the cumulative operating income goal (and failure to meet the thresholds for the other two financial goals) and up to 150% of the target award value for maximum Company performance against all three financial goals.

The earned value of the Performance Awards will vest on May 31, 2011 subject to continued service by the participant(s) through that date. The vested portion of the earned value of the Performance Awards will be paid in a combination of cash and shares of the Company's Class A common stock. Two-thirds of the earned value will be delivered to participants in cash (subject to any applicable plan limitations, less applicable taxes), and the remaining balance will be paid in shares, based on the closing price of the Company's common stock on the day preceding the date of the Committee's certification of the Company's performance. No dividends will be paid or accrued with respect to shares granted in payment of the Performance Awards until such shares are issued.

Recognition of compensation expense and accrual of the corresponding liability related to the Performance Awards is based on the periodic assessment of the probability that the performance criteria will be achieved. At May 31, 2010 and 2009, respectively, based on our probability assessments we determined that the fair value of the Performance Awards was \$4,282 and zero. Thus, for the years ended May 31, 2010 and 2009, respectively, we recognized compensation expense of \$2,540 and zero. At May 31, 2010 and 2009, respectively, accrued compensation expense included in other long-term liabilities totaled \$2,540 and zero.

Also, on December 12, 2008, the Compensation Committee of our Board of Directors granted 240,500 restricted stock units (the "New Units") to certain employees not participating in the Performance Awards program. Each New Unit represents the right to receive one share of the Company's Class A common stock upon vesting. The aggregate value of the New Units at the grant date was \$1,332, which is being expensed over the vesting (service) period. The New Units cliff vest on May 31, 2011, assuming the holder is still employed. Any dividends paid between the grant date and vesting will be payable to the holder upon vesting of the New Units. For the years ended May 31, 2010 and 2009, respectively, we recognized \$448 and \$248 in compensation expense.

### **13. COMMITMENTS AND CONTINGENCIES**

**Leases** – We lease warehouse and office facilities, manufacturing and production facilities, transportation equipment and other equipment under operating lease agreements expiring through 2013. At May 31, 2010, future minimum payments of \$6,612 under these non-cancelable operating leases are due as follows: \$2,352 (2011), \$2,318 (2012), \$1,933 (2013), \$7 (2014), and \$2 (2015). Rental expense was \$2,416, \$2,500 and \$2,584, respectively, for fiscal 2010, 2009 and 2008.

**Purchase Commitments** – At May 31, 2010, we are committed to future purchases primarily for inventory related items, including raw materials, packaging and outsourced contract manufacturing, under open purchase orders for specified quantities with fixed price provisions aggregating \$27,994.

**SCHIFF NUTRITION INTERNATIONAL, INC. AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - (continued)**

*(dollars in thousands, except share data)*

**Credit Facility** – On August 18, 2009, we entered into, through our wholly-owned direct operating subsidiary Schiff Nutrition Group, Inc. (“SNG”), a new \$80,000 revolving credit facility (the “Credit Facility”) with U.S. Bank National Association, as Agent. The Credit Facility replaced our previous \$25.0 million credit facility which expired on June 30, 2009, and contains customary terms and conditions, including, among others, financial covenants that may limit our ability to pay dividends on our common stock and certain other restrictions. SNG’s obligations under the Credit Facility are guaranteed by us and SNG’s domestic subsidiaries and secured by a first priority security interest in all of the capital stock of SNG and its current and future subsidiaries, as well as a first priority security interest in substantially all of our domestic assets. Borrowings under the Credit Facility bear interest at floating rates based on U.S. Bank’s prime rate, the Federal Funds rate, or the LIBOR rate. The Credit Facility, which matures on August 18, 2012, can be used to fund our normal working capital and capital expenditure requirements, with availability to fund certain permitted strategic transactions. At May 31, 2010, there were no amounts outstanding and, subject to limitations based on certain financial covenant requirements, \$80,000 was available for borrowing under the Credit Facility.

Cash interest payments amounted to \$194, \$111 and \$113, respectively, for fiscal 2010, 2009 and 2008.

**Litigation** – From time to time, we are involved in claims, legal actions and governmental proceedings that arise from our business operations. Although ultimate liability cannot be determined at the present time, based on available information, we do not believe the resolution of these matters will have a material adverse effect on our results of operations and financial condition. However, it is possible that future litigation could arise, or that developments could occur in existing litigation, that could have a material adverse effect on our results of operations and financial condition.

**Royalties** – Pursuant to an agreement with WHF and certain other parties, Mariz Gestao E Investimentos Limitada (“Mariz”) obtained the exclusive international rights to use the trademarks and brand names used by WHF and its affiliates on or prior to December 1996. Mariz is a company incorporated under the laws of Portugal and owned by a trust of which the family members of a director are included among the beneficiaries. Pursuant to a sublicense agreement with Mariz dated as of December 1, 1996, we obtained the exclusive international worldwide rights to use these trademarks and brand names outside the United States, Canada, Mexico, Spain and Portugal (for which countries we have the rights outside of the Mariz sublicense), except in Japan. (see discussion below) Certain terms of the sublicense were amended and the rights under the sublicense to the Weider name and certain related trademarks were transferred as of March 1, 2005 in connection with the sale of our Weider branded business to Weider Global Nutrition, LLC (“WGN”), a wholly owned subsidiary of WHF.

Under the terms of the amended sublicense agreement, we are required to make annual royalty payments to Mariz on sales of products covered by the agreement in countries other than those listed above. The royalty payments, as amended, are equal to (i) 4% of sales up to \$7,000 (ii) 3.5% of sales greater than \$7,000 and less than \$14,000; (iii) 3.0% of sales greater than \$14,000 and less than \$21,000; and (iv) 2.5% of sales over \$21,000. The sublicense agreement includes an irrevocable buy-out option, exercisable by us after February 28, 2009, for a purchase price equal to the greater of \$2,000 or 6.5 times the aggregate royalties paid by us in the royalty year immediately preceding the date of the exercise of the option.

On September 19, 2007, we entered into a license agreement with Mariz providing for non-exclusive rights to use the Schiff and Move Free trademarks in connection with the sale of joint care products to Costco Wholesale Corporation (“Costco”) in Japan. The initial term of the license agreement is for three years following the launch of our product into Japan. We may renew the license agreement for two successive three-year terms if certain minimum sales levels are achieved during the third and sixth years following the product launch. The license agreement provides that we pay royalties equal to 5% of joint care product sales to Costco in Japan with guaranteed minimum annual royalties ranging from \$100 to \$225 for each year the agreement is in effect. Each party has certain termination rights, and depending on which party terminates and the reason for the termination, we may continue to owe the guaranteed minimum royalties for a period following termination of the license agreement.

Royalty expense, related to the Mariz licensing agreements, amounted to \$512, \$423 and \$286, respectively, for fiscal 2010, 2009 and 2008.

**Retirement Plan** – We sponsor a contributory 401(k) savings plan covering all employees who have met minimum age and service requirements. We make discretionary contributions of 50% of the employee’s contributions up to the first seven percent (six percent prior to January 1, 2008) of the employee’s compensation. Contribution expense amounted to \$482, \$536 and \$457, respectively, for fiscal 2010, 2009 and 2008.

**Other Taxes** – At May 31, 2010 and 2009, we have recorded liabilities for certain non-income tax uncertainties of \$129.

**SCHIFF NUTRITION INTERNATIONAL, INC. AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - (continued)**  
*(dollars in thousands, except share data)*

**14. RELATED PARTY TRANSACTIONS**

Significant related party transactions, not otherwise disclosed, are summarized below.

We provide contract manufacturing services to WGN. For fiscal 2010, 2009 and 2008, respectively, net sales to WGN were \$1,037, \$1,280 and \$1,308, with a gross profit of \$99, \$116 and \$120. In addition, we received \$249, \$418 and \$465 (reflected as a reduction in operating expenses), respectively, for certain general and administrative, research and development, and logistics services provided to WGN during fiscal 2010, 2009 and 2008. At May 31, 2010 and 2009, respectively, net receivables due from WGN totaled \$18 and \$104.

**15. QUARTERLY RESULTS (UNAUDITED)**

Quarterly results (unaudited) for fiscal 2010 and 2009 are as follows:

	<b>Quarter Ended</b>			
	<b>Aug. 31</b>	<b>Nov. 30</b>	<b>Feb. 28</b>	<b>May 31</b>
<b>2010:</b>				
Net sales	\$ 48,565	\$ 53,754	\$ 53,318	\$ 49,250
Gross profit	19,162	24,235	22,181	19,472
Income from operations	7,026	9,470	8,484	3,830
Income tax expense	2,671	3,506	2,679	1,340
Net income	4,391	5,883	5,733	2,439
Basic net income per share	0.16	0.21	0.20	0.08
Diluted net income per share	0.15	0.20	0.20	0.08

	<b>Quarter Ended</b>			
	<b>Aug. 31</b>	<b>Nov. 30</b>	<b>Feb. 28</b>	<b>May 31</b>
<b>2009:</b>				
Net sales	\$ 47,790	\$ 47,293	\$ 49,872	\$ 45,736
Gross profit	17,878	17,603	17,309	14,040
Income from operations	5,020	4,462	5,211	493
Income tax expense	2,050	1,810	1,712	45
Net income	3,249	2,912	3,616	553
Basic net income per share	0.12	0.11	0.13	0.02
Diluted net income per share	0.11	0.10	0.13	0.02

**SCHIFF NUTRITION INTERNATIONAL, INC. AND SUBSIDIARIES**  
**VALUATION OF QUALIFYING ACCOUNTS**  
**YEARS ENDED MAY 31, 2010, 2009 AND 2008**  
*(in thousands)*

<u>Description</u>	<u>Balance at Beginning of Year</u>	<u>Reductions Charged to Costs / Expenses</u>	<u>Additions Charged to Net Sales</u>	<u>Reductions due to Divestiture</u>	<u>Deductions / Write-offs</u>	<u>Balance at End of Year</u>
<b>ALLOWANCE FOR DOUBTFUL ACCOUNTS:</b>						
2008	\$ 380	\$ —	\$ —	\$ —	\$ (59)	\$ 321
2009	\$ 321	\$ —	\$ 132	\$ —	\$ (3)	\$ 450
2010	\$ 450	\$ —	\$ —	\$ —	\$ (274)	\$ 176
<b>ALLOWANCE FOR SALES RETURNS AND DISCOUNTS:</b>						
2008	\$ 1,781	\$ —	\$ 7,069	\$ —	\$ (7,638)	\$ 1,212
2009	\$ 1,212	\$ —	\$ 9,353	\$ —	\$ (8,680)	\$ 1,885
2010	\$ 1,885	\$ —	\$ 8,811	\$ —	\$ (8,903)	\$ 1,793