NATURAL ALTERNATIVES INTERNATIONAL INC Form 10-Q February 16, 2010 Table of Contents

UNITED STATES SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

QUARTERLY REPORT

pursuant to Section 13 or 15(d)

of the Securities Exchange Act of 1934

FOR THE QUARTERLY PERIOD ENDED DECEMBER 31, 2009

000-15701

(Commission file number)

NATURAL ALTERNATIVES INTERNATIONAL, INC.

(Exact name of registrant as specified in its charter)

Delaware (State of incorporation)

84-1007839 (IRS Employer Identification No.)

1185 Linda Vista Drive San Marcos, California 92078 (Address of principal executive offices)

(760) 744-7340 (Registrant s telephone number)

Indicate by check mark whether Natural Alternatives International, Inc. (NAI) (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 NAI was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

x Yes "No

Indicate by check mark whether NAI 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 during the preceding 12 months (or for such shorter period that NAI was required to submit and post such files).

" Yes " No

Indicate by check mark whether NAI is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company.

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

Indicate by check mark whether NAI is a shell company (as defined in Rule 12b-2 of the Exchange Act).

" Yes x No

As of February 16, 2010, 7,078,793 shares of NAI s common stock were outstanding, net of 180,941 treasury shares.

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SPECIAL NOTE ABOUT FORWARD-LOOKING STATEMENTS

Certain statements in this report, including information incorporated by reference, are forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, Section 21E of the Securities Exchange Act of 1934, and the Private Securities Litigation Reform Act of 1995. Forward-looking statements reflect current views about future events and financial performance based on certain assumptions. They include opinions, forecasts, intentions, plans, goals, projections, guidance, expectations, beliefs or other statements that are not statements of historical fact. Words such as may, will, should, could, would, expects, plans, believes, anticipates, intends, estimates, projects, or the negative or other variation of such words, and similar expressions may identify a statement as a forward-looking statement. Any statements that refer to projections of our future financial performance, our anticipated growth and trends in our business, our goals, strategies, focus and plans, and other characterizations of future events or circumstances, including statements expressing general optimism about future operating results, are forward-looking statements. Forward-looking statements in this report may include statements about:

gı	results, are forward-looking statements. Forward-looking statements in this report may include statements about:
	future financial and operating results, including projections of net sales, revenue, income or loss, net income or loss per share, profit margins, expenditures, liquidity, goodwill valuation and other financial items;
	our ability to develop relationships with new customers and maintain or improve existing customer relationships;
	future levels of our revenue concentration risk;
	development of new products, brands and marketing strategies;
	the effect of the discontinuance of Dr. Cherry s television program and our ability to develop a new marketing plan for, and to sustain, our Pathway to Healing® product line;
	distribution channels, product sales and performance, and timing of product shipments;
	inventories and the adequacy and intended use of our facilities;
	current or future customer orders;
	the impact on our business and results of operations and variations in quarterly net sales from cost reduction programs, seasonal and other factors;
	management s goals and plans for future operations;
	our ability to improve operational efficiencies, manage costs and business risks and improve or maintain profitability;
	growth, expansion, diversification, acquisition, divestment and consolidation strategies, the success of such strategies, and the

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benefits we believe can be derived from such strategies;

personnel;
the outcome of regulatory, tax and litigation matters;
our ability to operate within the standards set by the Food and Drug Administration s Good Manufacturing Practices;
sources and availability of raw materials;
operations outside the United States (U.S.);
the adequacy of reserves and allowances;
overall industry and market performance;
competition and competitive advantages resulting from our quality commitment;
current and future economic and political conditions;
the impact of accounting pronouncements; and

other assumptions described in this report underlying or relating to any forward-looking statements.

The forward-looking statements in this report speak only as of the date of this report and caution should be taken not to place undue reliance on any such forward-looking statements. Forward-looking statements are subject to certain events, risks, and uncertainties that may be outside of our control. When considering forward-looking statements, you should carefully review the risks, uncertainties and other cautionary statements in this report as they identify certain important factors that could cause actual results to differ materially from those expressed in or implied by the forward-looking statements. These factors include, among others, the risks described under Item 1A of Part II and elsewhere in this report, as well as in other reports and documents we file with the United States Securities and Exchange Commission (SEC).

Unless the context requires otherwise, all references in this report to the Company, NAI, we, our, and us refer to Natural Alternatives International, Inc. and, as applicable, Natural Alternatives International Europe S.A. (NAIE), and our other wholly owned subsidiaries.

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PART I FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

NATURAL ALTERNATIVES INTERNATIONAL, INC.

Condensed Consolidated Balance Sheets

(In thousands, except share and per share data)

	eember 31, 2009 naudited)	June 30, 2009
Assets		
Current assets:		
Cash and cash equivalents	\$ 4,553	\$ 3,995
Certificate of deposit	699	699
Accounts receivable - less allowance for doubtful accounts of \$8 at December 31, 2009 and \$27 at June 30, 2009	5,614	5,685
Inventories, net	8,599	9,320
Deferred income taxes	368	
Prepaids and other current assets	1,398	1,261
Assets of discontinued operations	171	1,187
•		ĺ
Total current assets	21,402	22,147
Property and equipment, net	14,113	14,133
Other noncurrent assets, net	159	159
outer noneutral assets, not	10)	10)
Total assets	\$ 35,674	\$ 36,439
Liabilities and Stockholders Equity		
Current liabilities:		
Accounts payable	\$ 2,915	\$ 4,327
Accrued liabilities	934	1,001
Accrued compensation and employee benefits	570	1,164
Income taxes payable	836	490
Current portion of long-term debt	155	669
Liabilities of discontinued operations	100	599
Total current liabilities	5,510	8,250
Long-term debt, less current portion	520	598
Deferred rent	985	1,054
Long-term pension liability	480	505
Zong term pension maximy	100	303
Total liabilities	7,495	10,407
	ŕ	ŕ
Commitments and contingencies		
Stockholders equity:		
Preferred stock; \$.01 par value; 500,000 shares authorized; none issued or outstanding		
Common stock; \$.01 par value; 20,000,000 shares authorized; issued and outstanding 7,259,734 at		
December 31, 2009 and 7,249,734 June 30, 2009	71	71
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Additional paid-in capital	19,031	18,899
Accumulated other comprehensive loss	(565)	(565)
Retained earnings	10,741	8,726
Treasury stock, at cost, 180,941 shares at December 31, 2009 and June 30, 2009	(1,099)	(1,099)
Total stockholders equity	28,179	26,032
Total liabilities and stockholders equity	\$ 35,674	\$ 36,439

See accompanying notes to condensed consolidated financial statements.

NATURAL ALTERNATIVES INTERNATIONAL, INC.

Condensed Consolidated Statements of Operations and Comprehensive Income (Loss)

(In thousands, except share and per share data)

(Unaudited)

			nths Ended aber 31,				onths Ended ember 31,	
		2009		2008		2009		2008
Net sales	\$	17,249	\$	17,616	\$	34,210	\$	37,142
Cost of goods sold		14,779		16,844		28,585		33,970
Gross profit		2,470		772		5,625		3,172
Selling, general & administrative expenses		1,734		2,838		3,482		5,456
Operating income (loss) from continuing operations		736		(2,066)		2,143		(2,284)
Other (expense) income:								
Interest income		2				7		5
Interest expense		(24)		(79)		(66)		(122)
Foreign exchange loss		(25)		(45)		(2)		(344)
Other, net		19		4		44		28
		(28)		(120)		(17)		(433)
				(2.400)				.a
Income (loss) from continuing operations before income taxes		708		(2,186)		2,126		(2,717)
Provision for income taxes		94		362		266		180
Income (loss) from continuing operations		614		(2,548)		1,860		(2,897)
Income (loss) from discontinued operations, net of tax		60		(756)		155		(1,804)
meone (1088) from discontinued operations, net of tax		00		(730)		133		(1,004)
Net income (loss) and comprehensive income (loss)	\$	674	\$	(3,304)	\$	2,015	\$	(4,701)
Net income (loss) per common share:								
Basic:								
Continuing operations	\$	0.09	\$	(0.36)	\$	0.26	\$	(0.41)
Discontinued operations		0.01		(0.11)		0.02		(0.26)
Net income (loss)	\$	0.10	\$	(0.47)	\$	0.28	\$	(0.67)
Diluted:								
Continuing operations	\$	0.09	\$	(0.36)	\$	0.26	\$	(0.41)
Discontinued operations		0.01		(0.11)		0.02		(0.26)
Net income (loss)	\$	0.10	\$	(0.47)	\$	0.28	\$	(0.67)
Weighted average common shares outstanding:								
Basic	7	,071,076	7	,057,614	7	,069,934	7	,045,413
Diluted		.096.823		,057,614		,103,816		,045,413
See accompanying notes to condensed		, ,		, ,	•	, 2-,	•	,,

${\bf NATURAL\ ALTERNATIVES\ INTERNATIONAL,\ INC.}$

Condensed Consolidated Statements of Cash Flows

(In thousands)

(Unaudited)

	Six Montl Decemb 2009	
Cash flows from operating activities		
Income (loss) before discontinued operations	\$ 1,860	\$ (2,897)
Adjustments to reconcile net income (loss) to net cash provided by (used in) operating activities:		
Reduction of uncollectible accounts receivable	(19)	(9)
Depreciation and amortization	1,605	1,547
Non-cash compensation	112	181
Tax benefit from exercise of stock options		(88)
Deferred income taxes	(368)	(61)
Pension expense, net of contributions	(25)	25
Loss on disposal of assets	16	8
Changes in operating assets and liabilities:		
Accounts receivable	90	1,772
Inventories, net	721	522
Other assets	(137)	250
Accounts payable and accrued liabilities	(1,548)	(1,237)
Income taxes payable	346	168
Accrued compensation and employee benefits	(594)	(58)
Net cash provided by operating activities from continuing operations	2,059	123
Net cash provided by (used in) operating activities from discontinued operations	172	(1,866)
Net cash provided by (used in) operating activities	2,231	(1,743)
Cash flows from investing activities		
Capital expenditures	(1,601)	(2,771)
Purchase of certificate of deposit		(699)
•		Ì
Net cash used by investing activities from continuing operations	(1,601)	(3,470)
Net cash provided by investing activities from discontinued operations, including proceeds from the sale of the	(1,001)	(2,170)
legacy RHL business assets and As We Change®	500	2,155
		_,
Net cash used by investing activities	(1,101)	(1,315)
Cash flows from financing activities		
Net borrowings on line of credit		3,538
Payments on long-term debt	(592)	(736)
Tax benefit from exercise of stock options		88
Net activity from issuance of common stock	20	(13)
Net cash (used in) provided by financing activities	(572)	2,877
Net increase (decrease) in cash and cash equivalents	558	(181)

Cash and cash equivalents at beginning of period	:	3,995		3,518
Cash and cash equivalents at end of period	\$.	4,553	\$ 3	3,337
Supplemental disclosures of cash flow information Cash paid during the period for: Interest	\$	56	\$	140
Taxes	\$	320	\$	60

See accompanying notes to condensed consolidated financial statements.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(UNAUDITED)

A. Basis of Presentation and Summary of Significant Accounting Policies

Basis of Presentation

The accompanying interim unaudited condensed consolidated financial statements have been prepared in accordance with the instructions to Form 10-Q and applicable rules and regulations. Certain information and footnote disclosures normally included in financial statements prepared in accordance with U.S. generally accepted accounting principles have been condensed or omitted pursuant to such rules and regulations. In management s opinion, all adjustments necessary for a fair presentation of the financial position, results of operations and cash flows have been included and are of a normal, recurring nature. The results of operations for the three and six months ended December 31, 2009 are not necessarily indicative of the operating results for the full fiscal year or any future periods.

You should read the financial statements and these notes, which are an integral part of the financial statements, together with our audited financial statements included in our Annual Report on Form 10-K for the fiscal year ended June 30, 2009 (2009 Annual Report). The accounting policies used to prepare the financial statements included in this report are the same as those described in the notes to the consolidated financial statements in our 2009 Annual Report unless otherwise noted below.

Subsequent Events Evaluation

The Company evaluated all events or transactions that occurred after December 31, 2009 and through February 16, 2010, the date these financial statements were filed with the SEC as part of this report.

Net Income (Loss) per Common Share

We compute net income per common share using the weighted average number of common shares outstanding during the period, and diluted net income per common share using the additional dilutive effect of all dilutive securities. The dilutive impact of stock options account for the additional weighted average shares of common stock outstanding for our diluted net income per common share computation. We calculated basic and diluted net income per common share as follows (in thousands, except per share data):

		nths Ended iber 31,		ths Ended iber 31,
	2009	2008	2009	2008
Numerator				
Net income (loss)	\$ 674	\$ (3,304)	\$ 2,015	\$ (4,701)
Denominator				
Basic weighted average common shares outstanding	7,071	7,058	7,070	7,045
Dilutive effect of stock options	26		34	
Diluted weighted average common shares outstanding	7,097	7,058	7,104	7,045
Basic net income (loss) per common share	\$ 0.10	\$ (0.47)	\$ 0.28	\$ (0.67)
Diluted net income (loss) per common share	\$ 0.10	\$ (0.47)	\$ 0.28	\$ (0.67)

Shares related to stock options representing the right to acquire 415,354 shares of common stock for the three months ended December 31, 2009, and 487,815 shares for the six months ended December 31, 2009, were excluded from the calculation of diluted net income (loss) per common share, as the effect of their inclusion would have been anti-dilutive.

Shares related to stock options representing the right to acquire 879,492 shares of common stock for the three months ended December 31, 2008, and 973,096 shares for the six months ended December 31, 2008, were excluded from the calculation of diluted net (loss) income per common

share, as the effect of their inclusion would have been anti-dilutive.

Stock-Based Compensation

We have a new omnibus incentive plan that was approved by our Board of Directors effective as of October 15, 2009 and approved by our stockholders at the Annual Meeting of Stockholders held on November 30, 2009. Under the plan, we may grant nonqualified and incentive stock options and other stock-based awards to employees, non-employee directors and consultants. As of December 31, 2009, no awards had been granted under the plan. Our prior equity incentive plan was terminated effective as of November 30, 2009. We also had an employee stock purchase plan that was terminated effective as of June 30, 2009.

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We estimate the fair value of stock option awards at the date of grant and estimated employee stock purchase plan shares at the beginning of the offering period using the Black-Scholes option valuation model. The Black-Scholes option valuation model was developed for use in estimating the fair value of traded options that have no vesting restrictions and are fully transferable. Option valuation models require the input of highly subjective assumptions. Black-Scholes uses assumptions related to volatility, the risk-free interest rate, the dividend yield (which we assume to be zero, as we have not paid any cash dividends) and employee exercise behavior. Expected volatilities used in the model are based mainly on the historical volatility of our stock price. The risk-free interest rate is derived from the U.S. Treasury yield curve in effect in the period of grant. The expected life of stock option grants is derived from historical experience.

Our net income included stock based compensation expense of approximately \$69,000 for the three months ended December 31, 2009 and approximately \$112,000 for the six months ended December 31, 2009. Our net loss included stock based compensation expense of approximately \$112,000 for the three months ended December 31, 2008 and approximately \$181,000 for the six months ended December 31, 2008.

Fair Value of Financial Instruments

Our financial statements include the following financial instruments: cash and cash equivalents, short-term investments, accounts payable, and accrued expenses. We believe the carrying amounts of these assets and liabilities in the financial statements approximate the fair values of these financial instruments at December 31, 2009 and June 30, 2009. Fair value is defined as the exchange price that would be received to sell an asset or paid to transfer a liability (i.e., the exit price) in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants at the measurement date.

We use a three-level hierarchy for inputs used in measuring fair value that maximizes the use of observable inputs and minimizes the use of unobservable inputs by requiring that observable inputs be used when available. Observable inputs are inputs that market participants would use in pricing the asset or liability based on market data obtained from independent sources. Unobservable inputs are inputs that reflect our assumptions about the inputs that market participants would use in pricing the asset or liability and are developed based on the best information available under the circumstances.

The fair value hierarchy is broken down into three levels based on the source of inputs. In general, fair values determined by Level 1 inputs use quoted prices (unadjusted) in active markets for identical assets or liabilities that the Company has the ability to access. We classify cash, cash equivalents, and marketable securities balances as Level 1 assets. Fair values determined by Level 2 inputs are based on quoted prices for similar assets or liabilities in active markets, quoted prices for identical or similar assets or liabilities in markets that are not active and models for which all significant inputs are observable or can be corroborated, either directly or indirectly by observable market data. Level 3 inputs are unobservable inputs for the asset or liability, and include situations where there is little, if any, market activity for the asset or liability. These include certain pricing models, discounted cash flow methodologies and similar techniques that use significant unobservable inputs. As of December 31, 2009 and June 30, 2009, we did not have any financial assets or liabilities classified as Level 2 or 3.

Adoption of New Accounting Standards

During the first quarter of 2010, we adopted the new Accounting Standards Codification (ASC) as issued by the Financial Accounting Standards Board (FASB). The ASC has become the source of authoritative United States generally accepted accounting principles (GAAP) recognized by the FASB to be applied by nongovernmental entities. The ASC is not intended to change or alter existing GAAP. The adoption of the ASC did not have a material impact on our consolidated financial statements.

B. Discontinued Operations

In an effort to enhance stockholder value, improve working capital and enable us to focus on our core contract manufacturing business, during the fourth quarter of fiscal 2008 we undertook a careful review of our branded products portfolio and operations. As a result, we decided to narrow our branded products focus and portfolio and developed a plan to do so, which included a decision to sell the legacy business of Real Health Laboratories (RHL). On August 4, 2008, RHL sold certain assets related to its catalog and internet business conducted under the name As We Change[®] to Miles Kimball Company for a cash purchase price of \$2.3 million. We recorded a loss of \$226,000 as a result of this sale and recognized \$221,000 in severance and related payroll costs during fiscal 2009.

On July 29, 2009, we entered into an Asset Purchase Agreement with PharmaCare US Inc. and PharmaCare Laboratories Pty Ltd. for the sale of substantially all of the remaining assets of RHL related to its wholesale and direct-to-consumer business. The sale closed on July 31, 2009 for a cash purchase price of \$500,000. NAI provided a guarantee of RHL s indemnity obligations under the Asset Purchase Agreement, which potential liability is capped at the amount of the purchase price paid by the buyers to RHL. We recorded a loss of \$6,000 as a result of this sale

during the first quarter of fiscal 2010. RHL has agreed to provide certain transition services and support to the buyers for a period of up to six months and will receive an amount equal to \$9,000 per month for such services. Following the sale of substantially all of the assets of RHL, we changed the name of RHL to Disposition Company, Inc.

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As part of the original Asset Purchase Agreement, we had the potential to receive up to an additional \$500,000 from the buyers as a conditional earn-out if the RHL business acquired by the buyers met or exceeded certain budgeted profitability criteria during the period August 1, 2009 through July 31, 2010. Effective as of February 12, 2010, based on the loss of one or more customers, the results of operation of the RHL business since the closing date of the sale, the anticipated results of operation of the RHL business through July 31, 2010, and the corresponding anticipated reduction and or elimination in the conditional earn-out amount, and in an effort to avoid the time and expense associated with the procedures required in connection with the earn-out, including, without limitation, the time and expense associated with the preparation of the required reports and a review of the books and records of PharmaCare US and PharmaCare Australia, we amended the Asset Purchase Agreement to eliminate the potential earn-out compensation.

As a result of our decision to sell the legacy RHL business, we initiated an operational consolidation program during the first quarter of fiscal 2009 that transitioned the remaining branded products business operations to our corporate offices. We substantially completed this operational consolidation program as of September 30, 2008. The program resulted in a charge to discontinued operations of \$820,000 in severance and other business related exit costs during the six months ended December 31, 2008.

As the plan to dispose of the legacy RHL business met the criteria of accounting for the impairment or disposal of long-lived assets, the current and prior periods presented in this report have been reclassified to reflect the legacy RHL business as discontinued operations.

During the third quarter of fiscal 2009, RHL s wholesale operation experienced a decline in sales activity from one of its largest customers as a result of the discontinuance of certain RHL product lines. Historically these product sales represented a significant portion of RHL s overall annual sales to this customer. Additionally, during this same period we received feedback from multiple parties related to their preliminary interest in acquiring the then remaining RHL operations. Due in part to the expected decline in future RHL sales as noted above and the current depressed worldwide economic conditions, the preliminary purchase price valuations provided by these third parties provided us with an indication that an impairment of the RHL net asset carrying values may exist.

We performed an analysis that compared the fair value of RHL s net assets as indicated by the third party purchase price valuations noted above to the current carrying amounts to determine if an impairment of value was evident. As a result of this analysis, we determined that as of the related measurement date the book value of RHL s net assets exceeded the fair value by approximately \$1.8 million and recorded an impairment charge for this amount to discontinued operations during the third quarter of fiscal 2009.

The following table presents the activity and the reserve balances related to these restructuring programs for the six months ended December 31, 2009 (in thousands):

	 nce at 0, 2009	Charg Expe	,	Cash ments	 nce at r 31, 2009
Employee termination costs	\$ 19	\$	1	\$ (17)	\$ 3
Lease liabilities and related facility closure costs	15		1	(16)	
Total	\$ 34	\$	2	\$ (33)	\$ 3
Accrued restructuring charges:					
Current portion continuing operations					\$ 3
Discontinued operations					
Total					\$ 3

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The following table summarizes the results of the legacy RHL business, classified as discontinued operations, for the periods ended December 31 (in thousands):

		nths Ended aber 31,	Six Months Ended December 31,		
	2009	2008	2009	2008	
Net sales	\$	\$ 800	\$ 323	\$ 2,174	
Cost of goods sold and operating expense	(63)	724	125	2,691	
Restructuring expenses	(3)	199	(2)	1,050	
Loss on the sale of As We Change®				226	
Loss on the sale of remaining legacy RHL assets			6		
Other expense		12	7	11	
Income (loss) before income taxes	66	(135)	187	(1,804)	
Income tax provision	6	621	32		
Income (loss) from discontinued operations	\$ 60	\$ (756)	\$ 155	\$ (1,804)	

Assets and liabilities of the legacy RHL business included in the Condensed Consolidated Balance Sheets are summarized as follows (in thousands):

	December 31, 2009	June 30, 2009
Assets		
Cash	\$ 165	\$ 144
Accounts receivable, net		510
Inventory, net		286
Other current assets	6	39
Goodwill and intangible assets		208
Total assets	\$ 171	\$ 1,187
Liabilities		
Accrued liabilities	100	599
Total liabilities	100	599
Net assets of discontinued operations	\$ 71	\$ 588

C. Inventories

Inventories, net consisted of the following (in thousands):

	Dec	cember 31, 2009	June 30, 2009
Raw materials	\$	6,296	\$ 6,368
Work in progress		1,618	1,445
Finished goods		1,657	2,287
Reserves		(972)	(780)

\$ 8,599 \$ 9,320

D. Property and Equipment

Property and equipment consisted of the following (dollars in thousands):

	Depreciable Life In Years	December 31, 2009	June 30, 2009
Land	N/A	\$ 393	\$ 393
Building and building improvements	7 39	2,752	2,679
Machinery and equipment	3 12	25,067	23,681
Office equipment and furniture	3 5	3,396	3,419
Vehicles	3	204	204
Leasehold improvements	1 15	10,112	10,067
Total property and equipment		41,924	40,443
Less: accumulated depreciation and amortization		(27,811)	(26,310)
-			
Property and equipment, net		\$ 14,113	\$ 14,133

E. Debt

We have a bank credit facility of \$8.2 million as of December 31, 2009, comprised of a \$7.5 million working capital line of credit and \$675,000 in outstanding term loans. The working capital line of credit has a maturity date of November 1, 2010 and is secured by our accounts receivable and other rights to payment, general intangibles, inventory and equipment, has a fluctuating or fixed interest rate as elected by NAI from time to time and borrowings are subject to eligibility requirements for current accounts receivable and inventory balances. As of December 31, 2009, the outstanding balances on the term loans consisted of a \$170,000, 15 year term loan due June 2011, secured by our San Marcos building, at an interest rate of 8.25%; and a \$505,000, 10 year term loan due May 2014 with a twenty year amortization, secur