

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

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**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, 2005

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.  Yes  No

Indicate by check mark whether NAI is a large accelerated filer, an accelerated filer, or a non-accelerated filer (as defined in Rule 12b-2 of the Exchange Act).

Large accelerated filer  Accelerated filer  Non-accelerated filer

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

As of February 14, 2006, 6,573,099 shares of NAI's common stock were outstanding, net of 61,000 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,” “approximates,” “predicts,” or “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:

- future financial and operating results, including projections of net sales, revenue, income, net income per share, profit margins, expenditures, liquidity and other financial items;
- inventories and the adequacy and intended use of our facilities;
- the adequacy of reserves and allowances;
- sources and availability of raw materials;
- personnel;
- operations outside the United States;
- overall industry and market performance;
- competition;
- current and future economic and political conditions;
- development of new products, brands and marketing strategies;
- distribution channels and product sales and performance;
- growth, expansion, diversification and acquisition strategies, the success of such strategies, and the benefits we believe can be derived from such strategies;
- the outcome of regulatory, tax and litigation matters;
- our ability to develop relationships with new customers and maintain or improve existing customer relationships;
- our ability to reduce costs and maintain profitability;
- the impact of accounting pronouncements;
- management’s goals and plans for future operations; 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 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), Real Health Laboratories, Inc. (RHL) and our other wholly owned subsidiaries.

## PART I – FINANCIAL INFORMATION

## ITEM 1. FINANCIAL STATEMENTS

NATURAL ALTERNATIVES INTERNATIONAL, INC.  
Condensed Consolidated Balance Sheets  
(in thousands, except share and per share data)

	December 31, 2005	June 30, 2005
	(Unaudited)	
<b>Assets</b>		
Current assets:		
Cash and cash equivalents	\$ 2,235	\$ 1,916
Accounts receivable - less allowance for doubtful accounts of \$304 at December 31, 2005 and \$221 at June 30, 2005	6,486	10,834
Inventories, net	14,883	12,987
Deferred income taxes	559	421
Other current assets	1,589	1,012
	<u>25,752</u>	<u>27,170</u>
Property and equipment, net	15,885	16,507
Goodwill and purchased intangibles, net	10,976	—
Deferred income taxes	276	276
Other noncurrent assets, net	197	185
	<u>\$ 53,086</u>	<u>\$44,138</u>
<b>Liabilities and Stockholders' Equity</b>		
Current liabilities:		
Accounts payable	\$ 7,441	\$ 7,973
Accrued liabilities	2,461	1,923
Accrued compensation and employee benefits	1,145	1,351
Income taxes payable	684	664
Current portion of long-term debt	1,720	861
	<u>13,451</u>	<u>12,772</u>
Deferred tax liability	1,737	—
Long-term debt, less current portion	5,523	2,979
Deferred rent	1,267	1,264
Long-term pension liability	253	206
	<u>22,231</u>	<u>17,221</u>
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; issue and outstanding 6,629,199 at December 31, 2005 and 6,064,467 at June 30, 2005	66	61
Additional paid-in capital	14,600	11,494
Accumulated other comprehensive loss	(183)	(137)
Retained earnings	16,665	15,792
Treasury stock, at cost, 61,000 shares at December 31, 2005 and June 30, 2005	(293)	(293)
	<u>30,855</u>	<u>26,917</u>
	<u>\$ 53,086</u>	<u>\$44,138</u>

See accompanying notes to condensed consolidated financial statements.

**NATURAL ALTERNATIVES INTERNATIONAL, INC.**  
**Condensed Consolidated Statements of Income And Comprehensive Income**  
(in thousands, except share and per share data)  
(Unaudited)

	Three Months Ended December 31,		Six Months Ended December 31,	
	2005	2004	2005	2004
Net sales	\$ 19,868	\$ 21,545	\$ 41,601	\$ 44,272
Cost of goods sold	15,678	16,953	33,355	34,362
Gross profit	4,190	4,592	8,246	9,910
Selling, general & administrative expenses	3,347	3,710	6,725	7,634
Income from operations	843	882	1,521	2,276
Other income (expense):				
Interest income	16	6	26	10
Interest expense	(83)	(54)	(141)	(105)
Foreign exchange (loss) gain	(23)	168	(2)	166
Other, net	(3)	25	(3)	24
	(93)	145	(120)	95
Income before income taxes	750	1,027	1,401	2,371
Provision for income taxes	289	242	528	734
Net income	\$ 461	\$ 785	\$ 873	\$ 1,637
Unrealized loss resulting from change in fair value of derivative instruments, net of tax	1	75	46	125
Comprehensive income	\$ 460	\$ 710	\$ 827	\$ 1,512
Net income per common share:				
Basic	\$ 0.07	\$ 0.13	\$ 0.14	\$ 0.28
Diluted	\$ 0.07	\$ 0.12	\$ 0.13	\$ 0.25
Weighted average common shares outstanding:				
Basic	6,185,816	5,928,766	6,099,603	5,928,521
Diluted	6,485,091	6,571,995	6,477,097	6,512,099

*See accompanying notes to condensed consolidated financial statements.*

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**NATURAL ALTERNATIVES INTERNATIONAL, INC.**  
**Condensed Consolidated Statements of Cash Flows**  
**(in thousands)**  
**(Unaudited)**

	Six Months Ended December 31,	
	2005	2004
<b>Cash flows from operating activities</b>		
Net income	\$ 873	\$ 1,637
Adjustments to reconcile net income to net cash provided by operating activities:		
Provision (reduction) for uncollectible accounts receivable	(43)	55
Depreciation and amortization	1,469	1,178
Amortization of purchased intangibles	21	—
Deferred income taxes	—	59
Non-cash compensation	26	40
Pension expense, net of contributions	50	21
Loss on disposal of asset	—	17
Changes in operating assets and liabilities (net of effects of business acquisition):		
Accounts receivable	4,235	1,272
Inventories, net	(1,108)	(322)
Other assets	(184)	(597)
Accounts payable and accrued liabilities	(1,434)	718
Accrued compensation and employee benefits	(292)	(1,532)
Net cash provided by operating activities	<u>3,613</u>	<u>2,546</u>
<b>Cash flows from investing activities</b>		
Capital expenditures	(716)	(5,238)
Repayment of notes receivable	—	13
Net cash paid for business acquisition	<u>(5,617)</u>	<u>—</u>
Net cash used in investing activities	<u>(6,333)</u>	<u>(5,225)</u>
<b>Cash flows from financing activities</b>		
Proceeds from long-term debt	3,800	—
Payments on long-term debt	(987)	(402)
Proceeds from issuance of common stock	226	224
Net cash provided by (used in) financing activities	<u>3,039</u>	<u>(178)</u>
Net increase (decrease) in cash and cash equivalents	319	(2,857)
Cash and cash equivalents at beginning of period	1,916	7,495
Cash and cash equivalents at end of period	<u>\$ 2,235</u>	<u>\$ 4,638</u>
<b>Supplemental disclosures of cash flow information</b>		
Cash paid during the period for:		
Interest	\$ 123	\$ 105
Taxes	\$ 495	\$ 814

*See accompanying notes to condensed consolidated financial statements.*

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

**A. Basis of Presentation and 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, 2005 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, 2005 ("2005 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 2005 Annual Report unless otherwise noted below.

**Stock-Based Compensation**

We have an equity incentive plan under which we have granted nonqualified and incentive stock options to employees, non-employee directors and consultants. We also have an employee stock purchase plan. Before July 1, 2005, we accounted for stock-based awards to employees, including shares issued pursuant to the employee stock purchase plan, under the recognition and measurement provisions of Accounting Principles Board Opinion No. 25, "Accounting for Stock Issued to Employees" (APB 25), and related interpretations, as permitted by Statement of Financial Accounting Standard No. 123, "Accounting for Stock-Based Compensation" (SFAS 123).

Effective July 1, 2005, we adopted the fair value recognition provisions of Statement of Financial Accounting Standards No. 123R, "Share Based Payment" (SFAS 123R), using the modified-prospective-transition method. Under that transition method, compensation cost is recognized (a) for all stock-based awards granted before, but not yet vested as of, July 1, 2005, based on the grant date fair value estimated in accordance with the original provisions of SFAS 123, and (b) for all stock-based awards granted after July 1, 2005, based on the grant-date fair value estimated in accordance with the provisions of SFAS 123R. Results for prior periods have not been restated.

We estimated the fair value of the stock option awards at the date of grant and 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, including expected life and stock price volatility.

Effective April 27, 2005, our Board of Directors approved the acceleration of the vesting of all outstanding and unvested options held by directors, officers and other employees under our 1999 Omnibus Equity Incentive Plan. As a result of the acceleration, options to acquire 827,932 shares of our common stock, which otherwise would have vested over the next 36 months, became immediately exercisable. This action was taken to eliminate, to the extent permitted, the transition expense that we otherwise would have incurred in connection with the adoption of SFAS 123R.

On December 2, 2005, pursuant to our 1999 Omnibus Equity Incentive Plan, our Board of Directors granted options to buy 100,000 shares, in the aggregate, of NAI's common stock to John Dullea, the President of RHL, at an exercise price of \$6.655 per share and with a term of five years. The options vest 34% on December 2, 2006 and an additional 33% on each of December 2, 2007 and December 2, 2008.

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The following table illustrates the effect on net income and net income per common share as if the fair value method had been applied to all outstanding and unvested awards in each period (in thousands, except per share data):

	Three Months Ended December 31,		Six Months Ended December 31,	
	2005	2004	2005	2004
Net income - as reported	\$ 461	\$ 785	\$ 873	\$ 1,637
Plus: Reported stock-based compensation	15	20	26	40
Less: Fair value stock-based compensation	(15)	(309)	(26)	(615)
Net income - pro forma	\$ 461	\$ 496	\$ 873	\$ 1,062
Reported basic net income per common share	\$ 0.07	\$ 0.13	\$ 0.14	\$ 0.28
Pro forma basic net income per common share	\$ 0.07	\$ 0.08	\$ 0.14	\$ 0.18
Reported diluted net income per common share	\$ 0.07	\$ 0.12	\$ 0.13	\$ 0.25
Pro forma diluted net income per common share	\$ 0.07	\$ 0.08	\$ 0.13	\$ 0.16

### Net Income per Common Share

We compute net income per common share in accordance with SFAS 128, "Earnings Per Share." This statement requires the presentation of basic 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):

	Three Months Ended December 31,		Six Months Ended December 31,	
	2005	2004	2005	2004
<b>Numerator</b>				
Net income	\$ 461	\$ 785	\$ 873	\$ 1,637
<b>Denominator</b>				
Basic weighted average common shares outstanding	6,186	5,929	6,100	5,929
Dilutive effect of stock options	299	643	377	583
Diluted weighted average common shares outstanding	6,485	6,572	6,477	6,512
Basic net income per common share	\$ 0.07	\$ 0.13	\$ 0.14	\$ 0.28
Diluted net income per common share	\$ 0.07	\$ 0.12	\$ 0.13	\$ 0.25

Shares related to stock options of 697,000 for the three months ended December 31, 2005, and 446,000 for the six months ended December 31, 2005, were excluded from the calculation of diluted net income per common share, as the effect of their inclusion would have been anti-dilutive.

Shares related to stock options of 15,000 for the three months ended December 31, 2004, and 99,000 for the six months ended December 31, 2004, were excluded from the calculation of diluted net income per common share, as the effect of their inclusion would have been anti-dilutive.



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**B. Acquisition**

On December 5, 2005, we acquired Real Health Laboratories, Inc. (RHL), an integrated direct marketer of branded nutritional supplements and other lifestyle products. RHL, with net sales of \$10.0 million for its fiscal year ended October 31, 2005, markets and distributes its own branded nutraceutical products and third party branded nutraceutical products that address major health related matters including general wellness, arthritis support, prostate support and sexual function enhancement for both men and women. RHL's operations include in-house creative, catalog design, supply chain management and call center and fulfillment activities. We believe the acquisition of RHL marks a significant advance in our strategy to market our own branded products and expand our distribution channels and could provide the following benefits:

- Additional expertise in direct marketing and retail channels;
- Existing leading branded products in the Food, Drug and Mass Market (FDM) retail channel;
- Access to additional direct marketing and mass-market channels for NAI's existing products and concepts; and
- Cost savings from integrating certain NAI outsourced activities with RHL's existing operations and eliminating certain duplicative costs.

The aggregate consideration given to the selling stockholders of RHL by NAI in connection with the acquisition was approximately \$8.7 million, consisting of cash in the amount of \$5.8 million and the issuance of 510,000 shares of NAI's authorized but unissued shares of common stock, \$0.01 par value per share. Additionally, NAI assumed \$590,000 of RHL's debt, which was repaid at the close of the acquisition, and agreed to pay \$35,000 of the legal fees and expenses incurred by RHL and the selling stockholders in connection with the acquisition. At the close of the acquisition, RHL became a wholly owned subsidiary of NAI.

The RHL acquisition was accounted for as a purchase business combination in accordance with Statement of Financial Accounting Standards No. 141 "Business Combinations." Assets acquired and liabilities assumed were recorded in the accompanying condensed consolidated balance sheet at their fair values as of December 5, 2005. The allocation is based on a preliminary valuation using management's estimates and assumptions and is subject to adjustment as we have not yet finalized our evaluation. The preliminary allocation of the purchase price, including the consideration given to RHL's selling stockholders and associated transaction costs, was allocated to the assets acquired and liabilities assumed at December 5, 2005, as follows (in thousands):

Current assets	\$ 1,448
Property and equipment	132
Other assets	120
Goodwill	6,787
Intangibles:	
Distributor relationships	500
Direct consumer relationships	400
Tradenames	3,300
Non-compete agreements	10
<b>Total assets acquired</b>	<b>12,697</b>
Current liabilities	2,034
Deferred tax liability	1,737
<b>Total liabilities assumed</b>	<b>3,771</b>
<b>Net assets acquired</b>	<b>8,926</b>
Cash acquired	(191)
Debt assumed	590
<b>Purchase price and debt assumed, net of cash acquired</b>	<b>\$ 9,325</b>

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Unaudited pro forma consolidated financial information is presented below as if the acquisition of RHL had occurred at the beginning of the periods shown. The pro forma information presented below does not purport to present what actual results would have been had the acquisition in fact occurred at the beginning of such period, nor does the information project results for any future period. The unaudited pro forma consolidated financial information should be read in conjunction with the historical financial information of NAI included in this report, as well as the historical financial information of NAI and RHL included in other reports and documents we file with the SEC. The unaudited pro forma consolidated financial information for the three and six month periods ended December 31, 2005 and 2004 is as follows (in thousands):

	Three Months Ended December 31,		Six Months Ended December 31,	
	2005	2004	2005	2004
Net sales	\$19,895	\$23,823	\$44,364	\$49,620
Net income (loss)	\$ (434)	\$ 789	\$ (101)	\$ 1,561
Basic/diluted net income (loss) per common share	\$ (0.07)	\$ 0.11	\$ (0.02)	\$ 0.22

The unaudited pro forma consolidated financial information presented above includes the following adjustments to the combined results for NAI and RHL for the three and six months ended December 31, 2005 and 2004:

- A decrease in net income in the amount of \$63,000 pre-tax or \$40,000 after-tax for the three months ended December 31, 2005 and 2004, and \$126,000 pre-tax or \$80,000 after-tax for the six months ended December 31, 2005 and 2004, to reflect the interest expense relating to the additional \$3.8 million term loan acquired to partially fund the cash purchase price of the RHL acquisition;
- A decrease in net income in the amount of \$63,000 pre-tax or \$40,000 after-tax for the three months ended December 31, 2005 and 2004, and \$126,000 pre-tax or \$80,000 after-tax for the six months ended December 31, 2005 and 2004, to reflect the amortization of purchased intangible assets; and
- Basic/diluted net income (loss) per common share includes the impact of the 510,000 shares of NAI's common stock issued as part of the consideration for the RHL acquisition.

The unaudited pro forma consolidated financial information presented above does not take into account any benefit that may result from the acquisition of RHL due to synergies that may be derived from the elimination of any duplicative costs, nor has it been adjusted to remove the effect of a one-time reduction of net sales related to a rebate program offered by RHL to introduce a new product and develop the RHL brand. Under the terms of the rebate program, the customers of a major Food, Drug and Mass Market (FDM) retailer were offered a one-time rebate on a certain RHL product purchased during the period September 25, 2005 through October 25, 2005 (Rebate Period), provided the customer submitted a completed rebate form to the FDM retailer postmarked no later than November 5, 2005. In accordance with the SEC Emerging Issues Task Force Abstract (EITF) No. 01-09, "Accounting for Consideration Given by a Vendor to a Customer (Including a Reseller of the Vendor's Products)", the results of the rebate program were included as a reduction to revenue during the Rebate Period, which resulted in a decrease to net income in the amount of \$833,000 pre-tax or \$525,000 after tax for the three months ended December 31, 2005, and \$1 million pre-tax or \$630,000 after tax for the six months ended December 31, 2005.

### C. Goodwill and purchased intangibles

Goodwill and other acquisition-related intangibles as of December 31, 2005 were as follows (in thousands):

	Amortization Life in Years	Gross Amount	Accumulated Amortization	Net Amount
Goodwill	N/A	\$ 6,787	\$ —	\$ 6,787
Distributor relationships	13	500	(3)	497
Direct consumer relationships	9	400	(4)	396
Tradenames	20	3,300	(14)	3,286
Non-compete agreements	2	10	—	10
		\$10,997	\$ (21)	\$ 10,976

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The estimated future amortization expense of purchased intangible assets as of December 31, 2005 was as follows (in thousands):

Six months ending June 30, 2006	\$ 126
Fiscal year 2007	252
Fiscal year 2008	249
Fiscal year 2009	247
Fiscal year 2010	247
Thereafter	3,068
	<u>\$4,189</u>

## D. Inventories

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

	December 31, 2005	June 30, 2005
Raw materials	\$ 9,558	\$ 8,068
Work in progress	2,887	3,230
Finished goods	2,438	1,689
	<u>\$ 14,883</u>	<u>\$12,987</u>

## E. Property and Equipment

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

	Depreciable Life In Years	December 31, 2005	June 30, 2005
Land	N/A	\$ 393	\$ 393
Building and building improvements	7 – 39	2,721	2,713
Machinery and equipment	3 – 12	18,872	18,470
Office equipment and furniture	3 – 5	3,609	3,280
Vehicles	3	204	204
Leasehold improvements	1 – 15	9,424	9,244
Total property and equipment		<u>35,223</u>	<u>34,304</u>
Less: accumulated depreciation and amortization		<u>(19,338)</u>	<u>(17,797)</u>
Property and equipment, net		<u>\$ 15,885</u>	<u>\$ 16,507</u>

## F. Debt

As of December 1, 2005, we amended our credit facility to extend the maturity date of our working capital line of credit and modify certain financial covenants. The amendments included (i) an increase in our ratio of total liabilities/tangible net worth covenant from 1.0/1.0 to 1.25/1.0 through June 2007 (the ratio returns to 1.0/1.0, thereafter); (ii) a limit on capital expenditures of \$5,500,000 for fiscal years 2006 and 2007; (iii) an extension of the maturity date for the working capital line of credit from November 2006 to November 2007; (iv) an increase in our ability to incur additional aggregate annual operating lease expenses from \$100,000 to \$500,000 without prior approval from the lender; (v) an increase in our ability to create specific indebtedness other than with our current lender from \$0 to \$1,000,000; and (vi) replacement of the EBITDA coverage ratio with a fixed charge coverage ratio (aggregate of net profit after taxes, depreciation and amortization expenses and net contributions/aggregate current maturity of long-term debt and capitalized lease payments) not less than 1.25/1.0 as of each fiscal quarter end.

On December 5, 2005, to fund, in part, the cash purchase price of the RHL acquisition, we obtained an additional \$3.8 million term loan, which increased our bank credit facility to a total of \$15.8 million, comprised of an \$8.0 million working capital line of credit and \$7.8 million in term loans. The working capital line of credit is secured by our accounts receivable and other rights to payment, general intangibles, inventory and equipment, has an interest rate of

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Prime Rate or LIBOR plus 1.75%, as elected by NAI from time to time, and borrowings are subject to eligibility requirements for current accounts receivable and inventory balances. The term loans consist of a \$700,000 ten year term loan with a twenty year amortization, secured by our San Marcos building, at an interest rate of LIBOR plus 2.25%; a \$1.8 million four year term loan, secured by our accounts receivable and other rights to payment, general intangibles, inventory and equipment, at an interest rate of LIBOR plus 2.10%; a \$1.5 million five year term loan, secured by equipment, at an interest rate of LIBOR plus 2.10%; and the \$3.8 million four year term loan, secured by equipment, at an interest rate of LIBOR plus 2.10%. Monthly payments on the term loans are approximately \$131,000 plus interest. As of December 31, 2005, the amount outstanding on the term loans was \$6.7 million and we did not have an outstanding balance on the working capital line of credit. As of December 31, 2005, we had \$7.7 million available under the line of credit, net of a \$270,000 outstanding letter of credit issued to our landlord.

As of December 31, 2005 we were not in compliance with our tangible net worth financial covenant under our credit facility, which our lender has agreed to waive at December 31, 2005. Tangible net worth is defined in our credit facility as the aggregate of total stockholders' equity plus subordinated debt less any intangible assets and must be greater than \$20 million. As of December 31, 2005 our tangible net worth as defined in the credit facility was \$19.9 million.

Additionally, we have a term loan agreement for \$1.1 million, secured by our San Marcos building, at an annual interest rate of 8.25%. The loan is due in June 2011 and provides for principal and interest payable in monthly installments of \$10,800. As of December 31, 2005, the amount outstanding on the term loan was \$561,000.

The composite interest rate on all of our outstanding debt was 6.36% at December 31, 2005, and 4.58% at December 31, 2004.

### G. Defined Benefit Pension Plan

We sponsor a defined benefit pension plan that provides retirement benefits to employees based generally on years of service and compensation during the last five years before retirement. Effective June 20, 1999, our Board of Directors amended the plan to freeze the accrued benefit of each plan member at its then current amount and to no longer allow inactive plan members or other employees to become active members of the plan. We contribute an amount not less than the minimum funding requirements of the Employee Retirement Income Security Act of 1974 nor more than the maximum tax-deductible amount.

The components included in the net periodic benefit for the periods ended December 31 were as follows (in thousands):

	Three Months Ended December 31,		Six Months Ended December 31,	
	2005	2004	2005	2004
Interest cost	\$ 20	\$ 17	\$ 40	\$ 34
Expected return on plan assets	(23)	(18)	(46)	(36)
Net periodic benefit	\$ (3)	\$ (1)	\$ (6)	\$ (2)

### H. Economic Dependency

We had substantial net sales to certain customers during the periods shown in the following table. The loss of any of these customers, or a significant decline in net sales or the growth rate of net sales to these customers could have a material adverse impact on our net sales and net income. Net sales to any one customer representing 10% or more of the respective period's total net sales were as follows (dollars in thousands):

	Three Months Ended December 31,				Six Months Ended December 31,			
	2005		2004		2005		2004	
	Net Sales by Customer	% of Total Net Sales	Net Sales by Customer	% of Total Net Sales	Net Sales by Customer	% of Total Net Sales	Net Sales by Customer	% of Total Net Sales
Customer 1	\$ 8,826	44%	\$ 9,681	45%	\$ 19,158	46%	\$ 17,954	41%
Customer 2	6,323	32	6,746	31	13,918	34	15,834	36
	\$ 15,149	76%	\$ 16,427	76%	\$ 33,076	80%	\$ 33,788	77%

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We buy certain products from a limited number of raw material suppliers. The loss of any of these suppliers could have a material adverse impact on our net sales and net income. Raw material purchases from any one supplier representing 10% or more of the respective period's total raw material purchases were as follows (dollars in thousands):

	Three Months Ended December 31,				Six Months Ended December 31,			
	2005		2004		2005		2004	
	Raw Material Purchases by Supplier	% of Total Raw Material Purchases	Raw Material Purchases by Supplier	% of Total Raw Material Purchases	Raw Material Purchases by Supplier	% of Total Raw Material Purchases	Raw Material Purchases by Supplier	% of Total Raw Material Purchases
Supplier 1	\$ 1,291	18%	\$ (a)	(a)	\$ 3,510	23%	\$ (a)	(a)
Supplier 2	1,582	22	874	11%	2,613	17	2,041	10%
Supplier 3	(a)	(a)	1,968	24	(a)	(a)	6,156	30
	<u>\$ 2,873</u>	<u>40%</u>	<u>\$ 2,842</u>	<u>35%</u>	<u>\$ 6,123</u>	<u>40%</u>	<u>\$ 8,197</u>	<u>40%</u>

(a) Purchases were less than 10% of the respective period's total raw material purchases.

## I. Segment Information

Following the acquisition of RHL on December 5, 2005, our business consists of two segments: NAI, which primarily provides private label contract manufacturing services to companies that market and distribute nutritional supplements and other health care products; and RHL, which markets and distributes branded nutritional supplements and other lifestyle products. Our operating results by business segment were as follows (in thousands):

	Three Months Ended December 31,		Six Months Ended December 31,	
	2005	2004	2005	2004
	NAI	\$19,369	\$21,545	\$41,102
RHL	499	—	499	—
<b>Total Net Sales</b>	<u>\$19,868</u>	<u>\$21,545</u>	<u>\$41,601</u>	<u>\$44,272</u>

  

	Three Months Ended December 31,		Six Months Ended December 31,	
	2005	2004	2005	2004
	NAI	\$ 768	\$ 882	\$ 1,446
RHL	75	—	75	—
<b>Total Income from Operations</b>	<u>\$ 843</u>	<u>\$ 882</u>	<u>\$ 1,521</u>	<u>\$ 2,276</u>

NAI's products are sold both in the United States and in markets outside the United States, including Europe, Australia and Japan. NAI's primary market outside the United States is Europe. RHL's products are only sold in the United States.

Net sales by geographic region, based upon the customers' location, were as follows (in thousands):

	Three Months Ended December 31,		Six Months Ended December 31,	
	2005	2004	2005	2004
	United States	\$14,747	\$16,779	\$31,746
Markets Outside the United States	5,121	4,766	9,855	11,442
<b>Total Net Sales</b>	<u>\$19,868</u>	<u>\$21,545</u>	<u>\$41,601</u>	<u>\$44,272</u>

Products manufactured by NAIE accounted for 47% of net sales in markets outside the United States for the three months ended December 31, 2005 and 55% for the three months ended December 31, 2004. NAIE accounted for 48% of net sales in markets outside the United States for the six months ended December 31, 2005 and 48% for the six months ended December 31, 2004.

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No products manufactured by NAIE were sold in the United States during the six months ended December 31, 2005 and 2004.

Assets and capital expenditures by geographic region, based on the location of the company or subsidiary at which they were located or made, were as follow (in thousands):

	Long-Lived Assets		Total Assets		Capital Expenditures	
	Six Months Ended					
	December 31, 2005	June 30, 2005	December 31, 2005	June 30, 2005	December 31, 2005	December 31, 2004
United States	\$ 27,510	\$17,144	\$ 48,999	\$40,470	\$ 581	\$ 5,191
Europe	1,042	1,053	4,087	3,668	135	47
	<u>\$ 28,552</u>	<u>\$18,197</u>	<u>\$ 53,086</u>	<u>\$44,138</u>	<u>\$ 716</u>	<u>\$ 5,238</u>

**J. Contingencies**

From time to time, we become involved in various investigations, claims and legal proceedings that arise in the ordinary course of our business. These matters may relate to product liability, employment, intellectual property, tax, regulation, contract or other matters. The resolution of these matters as they arise will be subject to various uncertainties and, even if such claims are without merit, could result in the expenditure of significant financial and managerial resources. While unfavorable outcomes are possible, based on available information, we generally do not believe the resolution of these matters, including that discussed below, will result in a material adverse effect on our business, consolidated financial condition, or results of operation. However, a settlement payment or unfavorable outcome could adversely impact our results of operation. Our evaluation of the likely impact of these actions, including that discussed below, could change in the future and we could have unfavorable outcomes that we do not expect.

On February 10, 2005, a complaint was filed against NAI on behalf of Novogen Research Pty. Ltd. in the United States District Court, Southern District of New York alleging a cause of action for patent infringement of a Novogen patent by products manufactured by NAI. Novogen had agreed to settle the matter for a one-time payment by NAI of \$75,000 but certain terms of the settlement continue to be negotiated and there can be no assurance that this matter will be resolved in an out-of-court settlement.

As of February 14, 2006, other than as set forth above, neither NAI nor its subsidiaries were a party to any material pending legal proceeding nor was any of their property the subject of any material pending legal proceeding.

## ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

The following discussion and analysis is intended to help you understand our financial condition and results of operations for the three and six months ended December 31, 2005. You should read the following discussion and analysis together with our unaudited condensed consolidated financial statements and the notes to the condensed consolidated financial statements included under Item 1 in this report, as well as the information included in our 2005 Annual Report and other reports and documents we file with the SEC. Our future financial condition and results of operations will vary from our historical financial condition and results of operations described below.

### Executive Overview

*The following overview does not address all of the matters covered in the other sections of this Item 2 or other items in this report or contain all of the information that may be important to our stockholders or the investing public. This overview should be read in conjunction with the other sections of this Item 2 and this report.*

Our primary business activity is to provide private label contract manufacturing services to companies that market nutritional supplements. Our revenue is dependent, to a large degree, on two customers who market nutritional supplements through the direct sales marketing channel. The timing of our customers' orders is impacted by their marketing programs, supply chain management, entry into new markets and new product introductions. All of these attributes have had and will have a significant impact on our business.

Private label contract manufacturing net sales decreased 8% from the comparable year to date period last year. An increase in net sales from our largest customer was offset by a reduction in net sales from our second largest customer. Net sales to our two largest customers as a percentage of total net sales increased to 80% from 77% in the comparable year to date period last year.

A cornerstone of our strategy is to generate long-term growth and diversification of our net sales. During fiscal 2006 we have focused and expect to continue to focus on the following initiatives:

- Leveraging our new facility and TGA recertification to:
  - Increase the value of the goods and services we provide to our highly valued customers; and
  - Assist us in developing relationships with additional quality oriented customers;
- Implementing focused initiatives to market our own branded products through new distribution channels;
- Identifying and evaluating acquisition opportunities that could increase product lines and expand distribution channels.

We believe our efforts to generate long-term growth and diversification of our net sales are beginning to be rewarded based on the following accomplishments:

- Obtained two new contract manufacturing customers; and
- Acquisition of Real Health Laboratories, Inc. (RHL), an integrated direct marketer of branded nutritional supplements and other lifestyle products.

We have established relationships with two new customers who are leaders in the direct sales marketing channel. We have received purchase orders from these new customers, totaling \$11.1 million, which we expect to fill during the last six months of our fiscal year ending June 30, 2006. We remain optimistic our relationships with these new customers will continue though there can be no assurance of future sales.

On December 5, 2005, we completed the acquisition of RHL, which primarily markets branded nutritional supplements and other lifestyle products through the following channels:

- Wholesale distribution of RHL branded products to Food, Drug and Mass Market (FDM) retailers; and
- As We Change ("AWC"), a lifestyle catalog geared towards women between the ages of 45 and 65.

RHL's operations include in-house creative, catalog design, supply chain management and call center and fulfillment activities. RHL's branded nutritional supplements address major health related matters including general wellness, arthritis support, prostate support and sexual function enhancement for both men and women.

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We believe the acquisition of RHL marks a significant advance in our strategy to market our own branded products and expand our distribution channels and could provide the following benefits:

- Additional expertise in direct marketing and retail channels;
- Existing leading branded products in the FDM retail channel;
- Access to additional direct marketing and mass-market channels for NAI's existing products and concepts; and
- Cost savings from integrating certain NAI outsourced activities with RHL's existing operations and eliminating certain duplicative costs.

### **Critical Accounting Policies and Estimates**

The preparation of our financial statements requires that we make estimates and assumptions that affect the amounts reported in our financial statements and their accompanying notes. We have identified certain policies that we believe are important to the portrayal of our financial condition and results of operations. These policies require the application of significant judgment by our management. We base our estimates on our historical experience, industry standards, and various other assumptions that we believe are reasonable under the circumstances. Actual results could differ from these estimates under different assumptions or conditions. An adverse effect on our financial condition, changes in financial condition, and results of operations could occur if circumstances change that alter the various assumptions or conditions used in such estimates or assumptions.

Our critical accounting policies are discussed under Item 7 of our 2005 Annual Report. There have been no significant changes to these policies during the six months ended December 31, 2005, except for our policies described below as a result of the acquisition of RHL on December 5, 2005.

#### *Goodwill and Intangible Asset Valuation*

The purchase method of accounting for acquisitions requires extensive use of accounting estimates and judgments to allocate the purchase price to the fair value of the net tangible and intangible assets acquired. Goodwill and intangible assets deemed to have indefinite lives are not amortized, but are subject to annual impairment tests. The amounts and useful lives assigned to other intangible assets impact future amortization. Determining the fair values and useful lives of intangible assets requires the use of estimates and the exercise of judgment. While there are a number of different generally accepted valuation methods to estimate the value of intangible assets acquired, we primarily use the discounted cash flow method and relief-from-royalty method. These methods require significant management judgment to forecast the future operating results used in the analysis. In addition, other significant estimates are required such as residual growth rates and discount factors. The estimates we use to value and amortize intangible assets are consistent with the plans and estimates that we use to manage our business and are based on available historical information and industry estimates and averages. These judgments can significantly affect our net operating results.

We are required to assess goodwill impairment annually using the methodology prescribed by Statement of Financial Accounting Standards No. 142, "Goodwill and Other Intangible Assets" (SFAS 142). SFAS 142 requires that goodwill be tested for impairment at the reporting unit level on an annual basis or more frequently if we believe indicators of impairment exist. Application of the goodwill impairment test requires judgment, including the identification of reporting units, assigning assets and liabilities to reporting units, assigning goodwill to reporting units and determining the fair value of each reporting unit. The goodwill impairment test compares the implied fair value of the reporting unit with the carrying value of the reporting unit. The implied fair value of goodwill is determined in the same manner as in a business combination. Determining the fair value of the implied goodwill is judgmental in nature and often involves the use of significant estimates and assumptions. These estimates and assumptions could have a significant impact on whether or not an impairment charge is recognized and also the magnitude of any such charge. Estimates of fair value are primarily determined using discounted cash flows and market comparisons. These approaches use significant estimates and assumptions, including projection and timing of future cash flows, discount rates reflecting the risk inherent in future cash flows, perpetual growth rates, determination of appropriate market comparables, and determination of whether a premium or discount should be applied to comparables. It is reasonably possible that the plans and estimates used to value these assets may be incorrect. If our actual results, or the plans and estimates used in future impairment analyses, are lower than the original estimates used to assess the recoverability of these assets, we could incur additional impairment charges.



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### Revenue Recognition

We have expanded our revenue recognition accounting policies to account for payments made to RHL's customers in accordance with EITF No. 01-09 and sales transactions where the buyer has the right to return the product in accordance with Statement of Financial Accounting Standards No. 48, "Revenue Recognition When Right of Return Exists" (SFAS 48).

EITF No. 01-09 states that cash consideration (including a sales incentive) given by a vendor to a customer is presumed to be a reduction of the selling prices of the vendor's products or services and, therefore, should be characterized as a reduction of revenue when recognized in the vendor's income statement, rather than a sales and marketing expense. RHL has various agreements with customers that provide for discounts and rebates. These agreements are classified as a reduction of revenue. Certain other costs associated with customers that meet the requirements of EITF No. 01-09 are recorded as sales and marketing expense.

SFAS 48 states that revenue from sales transactions where the buyer has the right to return the product shall be recognized at the time of sale only if (1) the seller's price to the buyer is substantially fixed or determinable at the date of sale, (2) the buyer has paid the seller, or the buyer is obligated to pay the seller and the obligation is not contingent on resale of the product, (3) the buyer's obligation to the seller would not be changed in the event of theft or physical destruction or damage of the product, (4) the buyer acquiring the product for resale has economic substance apart from that provided by the seller, (5) the seller does not have significant obligations for future performance to directly bring about resale of the product by the buyer, and (6) the amount of future returns can be reasonably estimated. Revenue is recognized upon determination that all criteria for revenue recognition have been met. The criteria are usually met at the time title passes to the customer, which usually occurs upon delivery and an allowance is recorded for the estimated future returns.

### Results of Operations

The results of our operations for the periods ended December 31 were as follows (in thousands, except per share amounts):

	Three Months Ended December 31,			Six Months Ended December 31,		
	2005	2004	% Change	2005	2004	% Change
Private label contract manufacturing	\$17,363	\$19,580	(11)%	\$37,070	\$40,176	(8)%
Direct-to-consumer marketing program	2,006	1,965	2	4,032	4,096	(2)
RHL	499	—	n/a	499	—	n/a
<b>Total net sales</b>	<b>19,868</b>	<b>21,545</b>	<b>(8)</b>	<b>41,601</b>	<b>44,272</b>	<b>(6)</b>
Cost of goods sold	15,678	16,953	(8)	33,355	34,362	(3)
<b>Gross profit</b>	<b>4,190</b>	<b>4,592</b>	<b>(9)</b>	<b>8,246</b>	<b>9,910</b>	<b>(17)</b>
Gross profit %	21.1%	21.3%		19.8%	22.4%	
Selling, general & administrative expenses	3,347	3,710	(10)	6,725	7,634	(12)
% of net sales	16.8%	17.2%		16.2%	17.2%	
Other income (expense), net	(93)	145	(164)	(120)	95	(226)
<b>Income before taxes</b>	<b>750</b>	<b>1,027</b>	<b>(27)</b>	<b>1,401</b>	<b>2,371</b>	<b>(41)</b>
% of net sales	3.8%	4.8%		3.4%	5.4%	
<b>Net income</b>	<b>\$ 461</b>	<b>\$ 785</b>	<b>(41)</b>	<b>\$ 873</b>	<b>\$ 1,637</b>	<b>(47)</b>
% of net sales	2.3%	3.6%		2.1%	3.7%	
Diluted net income per common share	\$ 0.07	\$ 0.12	(42)%	\$ 0.13	\$ 0.25	(48)%

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The percentage decrease in private label contract manufacturing net sales over the comparable periods last year was attributed to the following:

	Three Months Ended	Six Months Ended
NSA International, Inc. net sales growth (reduction)	(3)% <sup>(1)</sup>	3% <sup>(2)</sup>
Mannatech, Incorporated net sales reduction	(2) <sup>(3)</sup>	(5) <sup>(3)</sup>
Discontinuation of two customer relationships	(4) <sup>(4)</sup>	(4) <sup>(4)</sup>
Impact of foreign exchange rates	(1)	—
Other customers net sales reduction	(1)	(2)
<b>Total</b>	<b>(11)%</b>	<b>(8)%</b>

- (1) Resulted primarily from lower average prices per unit, which reduced our net sales growth by five percentage points, partially offset by higher volumes of established products in existing markets, which contributed two percentage points of the net sales growth.
- (2) Resulted primarily from higher volumes of established products in existing markets, which contributed six percentage points of the net sales growth, partially offset by lower average prices per unit, which reduced our net sales growth by three percentage points.
- (3) Resulted primarily from changes in volumes of established products in existing markets, which contributed two percentage points of our net sales growth over the comparable quarter and attributed one percentage point of our net sales reduction from the comparable year to date period last year, and a shift in sales mix to lower priced products, which resulted in five percentage points of the decrease over the comparable quarter and comparable year to date period last year, partially offset by the introduction of existing products into new markets, which contributed one percentage point over the comparable quarter and comparable year to date period last year.
- (4) We discontinued relationships with two of our customers in March 2005 due to the disproportionate risks related to inventory levels and accounts receivable required to continue serving these customers.

Gross profit margin remained consistent with the comparable quarter and decreased 2.6 percentage points from the comparable year to date period last year. The change in gross profit margin was primarily due to the following:

	Three Months Ended	Six Month Ended
Shift in sales mix <sup>(1)</sup>	2.2%	1.1%
Incremental overhead expenses <sup>(2)</sup>	(4.0)	(2.9)
Change in inventory reserves	0.9	(0.4)
Incremental direct and indirect labor <sup>(3)</sup>	(0.4)	(0.9)
RHL operations	1.1	0.5
<b>Total</b>	<b>(0.2)%</b>	<b>(2.6)%</b>

- (1) The shift in sales mix resulted from selling lower volumes of established powder products to one of our largest customers. Powder products typically include higher material cost as a percentage of selling price compared to capsule or tablet products, resulting in lower gross profit margins.
- (2) Overhead expenses as a percentage of net sales increased four percentage points, or \$506,000, from the comparable quarter and 2.9 percentage points, or \$778,000, from the comparable year to date period last year primarily due to:
- Incremental outsourced lab testing of \$54,000 over the comparable quarter and \$126,000 over the comparable year to date period last year as a result of increased testing for compliance with certain countries' regulatory requirements;
  - Incremental expenses related to our facility expansion in Vista, California as follows:
    - Rent and facility related expenses of \$36,000 over the comparable quarter and \$116,000 over the comparable year to date period last year; and

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- Depreciation and amortization of \$243,000 over the comparable quarter and \$368,000 over the comparable year to date period last year;
  - Incremental rent expense of \$72,000 over the comparable quarter and year to date periods last year related to our facility expansion in Lugano, Switzerland; and
  - Incremental freight and shipping costs of \$80,000 over the comparable quarter and \$139,000 over the comparable year to date period last year.
- (3) Direct and indirect labor increased as a percentage of net sales primarily due to producing higher volumes of products with a lower average price per unit. This was partially offset by the termination of our second shift operation in late October 2005, net of employee separation costs.

Selling, general and administrative expenses decreased \$363,000, or 10%, from the comparable quarter and \$909,000, or 12% from the comparable year to date period last year primarily due to the following:

- Reduced personnel costs of \$117,000 from the comparable quarter and \$323,000 from the comparable year to date period last year primarily due to the termination of regulatory compliance and product formulation personnel in June 2005, including our former Vice President of Science & Technology;
- Reduced clinical study costs of \$180,000 from the comparable quarter and \$336,000 from the comparable year to date period last year due to lowering our level of participation in clinical studies;
- Reduced Sarbanes-Oxley compliance costs of \$95,000 from the comparable quarter and \$210,000 from the comparable year to date period last year;
- Reduced regulatory costs of \$392,000 associated with certification requirements to improve service to our customers selling products in international markets from the comparable quarter and year to date periods last year;
- Incremental litigation expense of \$84,000 over the comparable year to date period last year for legal fees and settlement costs associated with the Novogen claim;
- Reduction of \$201,000 in incentive compensation in the second quarter of fiscal 2005;
- Incremental direct-to-consumer marketing brand development spending of \$101,000 over the comparable quarter and \$152,000 over the comparable year to date period last year primarily for the launch on a test basis of a new direct mail campaign featuring Dr. Richard Linchitz, a nationally recognized physician, and Theraflex™, one of our proprietary formulas. We plan to continue testing this direct mail campaign in the third quarter; and
- Additional expenses for RHL's selling, general and administrative expenses of \$249,000 for the three and six months ended December 31, 2005.

Other income (expense), net decreased \$238,000 from the comparable quarter and \$215,000 from the comparable year to date period last year primarily due to the following:

- A decrease in foreign exchange gain (loss) of \$191,000 from the comparable quarter and \$168,000 from the comparable year to date period last year due to the weakening of the Euro and the related impact on the translation of Euro denominated cash and receivables; and
- An increase in interest expense of \$29,000 over the comparable quarter and \$36,000 over the comparable year to date period last year primarily due to the additional \$3.8 million term loan obtained in December 2005 to partially fund the RHL acquisition and an increase in our weighted average interest rate on our variable rate debt.

Our effective tax rate for the six months ended December 31, 2005 increased to 37.7% from 31.0% in the comparable year to date period last year primarily due to the expiration of NAIE's Swiss federal and cantonal income tax holiday that ended on June 30, 2005. Under the tax holiday, NAIE's effective tax rate for Swiss federal, cantonal and communal taxes was approximately 5% compared to our current effective rate of approximately 23%.

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**Liquidity and Capital Resources**

Our primary sources of liquidity and capital resources are cash flows provided by operating activities and the availability of borrowings under our credit facility. Net cash provided by operating activities was \$3.6 million in the six months ended December 31, 2005, compared to \$2.5 million in the comparable year to date period last year. Our operating cash flow during the six months ended December 31, 2005 was impacted by the following:

- Net income of \$873,000;
- Reduction of accounts receivable of \$4.2 million; and
- Incremental inventory of \$1.1 million.

Cash provided by operating activities for the six months ended December 31, 2004 included payments of \$1.6 million under the NAI Management Incentive Plan.

Cash used in investing activities in the six months ended December 31, 2005 included \$5.6 million of net cash used in the acquisition of RHL. The reconciliation of RHL net assets acquired to net cash used in the acquisition at December 5, 2005, is as follows (in thousands):

RHL net assets acquired	\$ 8,926
NAI stock consideration	(2,859)
Transaction costs	(259)
RHL cash acquired	(191)
	<hr/>
Total	\$ 5,617

Approximately \$555,000 of our operating cash flow was generated by NAIE during the six months ended December 31, 2005. As of December 31, 2005, NAIE's undistributed retained earnings are considered indefinitely reinvested.

Our consolidated debt increased to \$7.2 million at December 31, 2005 from \$3.8 million at June 30, 2005 primarily due to the additional \$3.8 million term loan obtained from our credit facility to fund, in part, the cash purchase price of the RHL acquisition, partially offset by monthly payments on our long term debt.

As of December 1, 2005, we amended our credit facility to extend the maturity date of our working capital line of credit and modify certain financial covenants. The amendments included (i) an increase in our ratio of total liabilities/tangible net worth covenant from 1.0/1.0 to 1.25/1.0 through June 2007 (the ratio returns to 1.0/1.0 thereafter); (ii) a limit on capital expenditures of \$5,500,000 for fiscal years 2006 and 2007; (iii) an extension of the maturity date for the working capital line of credit from November 2006 to November 2007; (iv) an increase in our ability to incur additional aggregate annual operating lease expenses from \$100,000 to \$500,000 without prior approval from the lender; (v) an increase in our ability to create specific indebtedness other than with our current lender from \$0 to \$1,000,000; and (vi) replacement of the EBITDA coverage ratio with a fixed charge coverage ratio (aggregate of net profit after taxes, depreciation and amortization expenses and net contributions/aggregate current maturity of long-term debt and capitalized lease payments) not less than 1.25/1.0 as of each fiscal quarter end.

On December 5, 2005, to fund, in part the cash purchase price of the RHL acquisition, we obtained the additional \$3.8 million term loan, which increased our bank credit facility to a total of \$15.8 million, comprised of an \$8.0 million working capital line of credit and \$7.8 million in term loans. The working capital line of credit, is secured by our accounts receivable and other rights to payment, general intangibles, inventory and equipment, has an interest rate of Prime Rate or LIBOR plus 1.75%, as elected by NAI from time to time, and borrowings are subject to eligibility requirements for current accounts receivable and inventory balances. The term loans consist of a \$700,000 ten year term loan with a twenty year amortization, secured by our San Marcos building, at an interest rate of LIBOR plus 2.25%; a \$1.8 million four year term loan, secured by our accounts receivable and other rights to payment, general intangibles, inventory and equipment, at an interest rate of LIBOR plus 2.10%; a \$1.5 million five year term loan, secured by equipment, at an interest rate of LIBOR plus 2.10%; and the \$3.8 million four year term loan, secured by equipment, at an interest rate of LIBOR plus 2.10%. Monthly payments on the term loans are approximately \$131,000 plus interest. As of December 31, 2005, the amount outstanding on the term loans was \$6.7 million and we did not have an outstanding balance on the working capital line of credit. As of December 31, 2005, we had \$7.7 million available under the line of credit, net of a \$270,000 outstanding letter of credit issued to our landlord.

As of December 31, 2005 we were not in compliance with our tangible net worth financial covenant under our credit facility, which our lender has agreed to waive at December 31, 2005. Tangible net worth is defined in our credit facility as the aggregate of total stockholders' equity plus subordinated debt less any intangible assets and must be greater than \$20 million. As of December 31, 2005 our tangible net worth as defined in the credit facility was \$19.9 million.

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Additionally, we have a term loan agreement for \$1.1 million, secured by our San Marcos building, at an annual interest rate of 8.25%. The loan is due in June 2011 and provides for principal and interest payable in monthly installments of \$10,800. As of December 31, 2005, the amount outstanding on the term loan was \$561,000.

On May 13, 2005, we purchased seven option contracts designated and effective as cash flow hedges to protect against the foreign currency exchange risk inherent in a portion of our forecasted transactions denominated in Euros. The seven options expired monthly beginning June 2005 and ending December 2005. The option contracts had a notional amount of \$4.2 million, a weighted average strike price of \$1.19, and a purchase price of \$21,000. The risk of loss associated with the options was limited to the purchase price paid for the option contracts. As of December 31, 2005, we had exercised one of the options and six of the options had expired.

On July 7, 2005, we purchased 12 option contracts designated and effective as cash flow hedges to protect against the foreign currency exchange risk inherent in a portion of our forecasted transactions denominated in Euros. The 12 options expire monthly beginning January 2006 and ending December 2006. The option contracts had a notional amount of \$7.0 million, a weighted average strike price of \$1.16, and a purchase price of \$152,000. The risk of loss associated with the options is limited to the purchase price paid for the option contracts.

On October 5, 2005, we purchased an option contract to protect against the foreign currency translation risk inherent in our Euro denominated working capital components. The option contract, which expires on June 30, 2006, had a notional amount of \$1.2 million, a strike price of \$1.19, and a purchase price of \$29,000. The risk of loss associated with the option is limited to the purchase price paid for the option contract.

There are no other derivative financial instruments at December 31, 2005.

As of December 31, 2005, we had \$2.2 million in cash and cash equivalents. We plan on funding our current working capital needs, capital expenditures and debt payments using available cash, cash flow from operations and our credit facility.

### **Off-Balance Sheet Arrangements**

We do not have any off-balance sheet debt nor do we have any transactions, arrangements, obligations (including contingent obligations) or other relationships with any unconsolidated entities or other persons that may have a material current or future effect on our financial condition, changes in financial condition, results of operations, liquidity, capital expenditures, capital resources, or significant components of revenue or expenses.

### **Recent Accounting Pronouncements**

Recent accounting pronouncements are discussed under Item 7 of our 2005 Annual Report. As of December 31, 2005, other than the pronouncements discussed in our 2005 Annual Report, we are not aware of any other pronouncements that materially affect our financial position or results of operations.

### **ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK**

We are exposed to market risk, which is the potential loss arising from adverse changes in market rates and prices, such as foreign currency exchange and interest rates. We generally do not enter into derivatives or other financial instruments for trading or speculative purposes. We may, however, enter into financial instruments to try to manage and reduce the impact of changes in foreign currency exchange rates. We cannot predict with any certainty our future exposure to fluctuations in foreign currency exchange and interest rates or other market risks or the impact, if any, such fluctuations may have on our future business, product pricing, consolidated financial condition, results of operations or cash flows. The actual impact of any fluctuations in foreign currency exchange or interest rates may differ significantly from those discussed below.

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### **Interest Rates**

At December 31, 2005, we had fixed rate debt of \$561,000 and variable rate debt of approximately \$6.7 million. The interest rates on our variable rate debt range from LIBOR plus 1.75% to LIBOR plus 2.25%. As of December 31, 2005, the weighted average effective interest rate on our variable rate debt was 6.12%. An immediate one hundred basis point (1.0%) increase in the interest rate on our variable rate debt, holding other variables constant, would have increased our interest expense by \$19,000 for the six months ended December 31, 2005. Interest rates have been at or near historic lows in recent years. There can be no guarantee that interest rates will not rise. Any increase in interest rates may adversely affect our results of operations and financial condition.

### **Foreign Currencies**

To the extent our business continues to expand outside the United States, an increasing share of our net sales and cost of sales may be transacted in currencies other than the United States dollar. Accounting practices require that our non-United States dollar-denominated transactions be converted to United States dollars for reporting purposes. Consequently, our reported net earnings may be significantly affected by fluctuations in currency exchange rates. When the United States dollar strengthens against currencies in which products are sold or weakens against currencies in which we incur costs, net sales and costs could be adversely affected.

Our main exchange rate exposures are with the Swiss Franc and the Euro against the United States dollar. This is due to NAIE's operations in Switzerland and the payment in Euros by our largest customer for finished goods. Additionally, we pay our NAIE employees and other expenses in Swiss Francs. We may enter into forward exchange contracts, foreign currency borrowings and option contracts to hedge our foreign currency risk. Our goal in seeking to manage foreign currency risk is to provide reasonable certainty to the functional currency value of foreign currency cash flows and to help stabilize the value of non-United States dollar-denominated earnings.

On May 13, 2005, we purchased seven option contracts designated and effective as cash flow hedges to protect against the foreign currency exchange risk inherent in a portion of our forecasted transactions denominated in Euros. The seven options expired monthly beginning June 2005 and ending December 2005. The option contracts had a notional amount of \$4.2 million, a weighted average strike price of \$1.19, and a purchase price of \$21,000. The risk of loss associated with the options was limited to the purchase price paid for the option contracts. As of December 31, 2005, we had exercised one of the options and six of the options had expired.

On July 7, 2005, we purchased 12 option contracts designated and effective as cash flow hedges to protect against the foreign currency exchange risk inherent in a portion of our forecasted transactions denominated in Euros. The 12 options expire monthly beginning January 2006 and ending December 2006. The option contracts had a notional amount of \$7.0 million, a weighted average strike price of \$1.16, and a purchase price of \$152,000. The risk of loss associated with the options is limited to the purchase price paid for the option contracts.

On October 5, 2005, we purchased an option contract to protect against the foreign currency translation risk inherent in our Euro denominated working capital components. The option contract, which expires on June 30, 2006, had a notional amount of \$1.2 million, a strike price of \$1.19, and a purchase price of \$29,000. The risk of loss associated with the option is limited to the purchase price paid for the option contract.

On December 31, 2005, the Swiss Franc closed at 1.32 to 1.00 United States dollar and the Euro closed at 0.84 to 1.00 United States dollar. A 10% adverse change to the exchange rates between the Swiss Franc and the Euro against the United States dollar, holding other variables constant, would have decreased our net income for the six months ended December 31, 2005 by \$122,000.

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**ITEM 4. CONTROLS AND PROCEDURES**

We maintain certain disclosure controls and procedures. They are designed to help ensure that material information is: (1) gathered and communicated to our management, including our principal executive and financial officers, on a timely basis; and (2) recorded, processed, summarized, reported and filed with the SEC as required under the Securities Exchange Act of 1934.

Our management, with the participation of our Chief Executive Officer and Chief Financial Officer, evaluated the effectiveness of our disclosure controls and procedures as of December 31, 2005. Based on such evaluation, our Chief Executive Officer and Chief Financial Officer concluded that our disclosure controls and procedures were effective for their intended purpose described above. There were no changes to our internal controls during the quarterly period ended December 31, 2005 that have materially affected, or that are reasonably likely to materially affect, our internal controls.

**PART II - OTHER INFORMATION**

**ITEM 1. LEGAL PROCEEDINGS**

From time to time, we become involved in various investigations, claims and legal proceedings that arise in the ordinary course of our business. These matters may relate to product liability, employment, intellectual property, tax, regulation, contract or other matters. The resolution of these matters as they arise will be subject to various uncertainties and, even if such claims are without merit, could result in the expenditure of significant financial and managerial resources. While unfavorable outcomes are possible, based on available information, we generally do not believe the resolution of these matters, including that discussed below, will result in a material adverse effect on our business, consolidated financial condition, or results of operation. However, a settlement payment or unfavorable outcome could adversely impact our results of operation. Our evaluation of the likely impact of these actions, including that discussed below, could change in the future and we could have unfavorable outcomes that we do not expect.

On February 10, 2005, a complaint was filed against NAI on behalf of Novogen Research Pty. Ltd. in the United States District Court, Southern District of New York alleging a cause of action for patent infringement of a Novogen patent by products manufactured by NAI. Novogen had agreed to settle the matter for a one-time payment by NAI of \$75,000 but certain terms of the settlement continue to be negotiated and there can be no assurance that this matter will be resolved in an out-of-court settlement.

As of February 14, 2006, other than as set forth above, neither NAI nor its subsidiaries were a party to any material pending legal proceeding nor was any of their property the subject of any material pending legal proceeding.

**ITEM 1A. RISK FACTORS**

*On December 5, 2005, we acquired RHL and may, in the future, pursue acquisitions of other companies that, if not successful, could adversely affect our business, financial condition and results of operations.*

On December 5, 2005, we completed our acquisition of RHL, an integrated direct marketer of nutritional supplements and other lifestyle products. RHL's business is subject to all of the operational risks that normally arise for a direct marketing company, including those related to competition, profitability, economic conditions, suppliers, customers, adverse publicity, product liability claims and other litigation, regulation, personnel, and intellectual property rights.

In the future, we may pursue additional acquisitions of other companies as part of our strategy focused on long-term growth and diversification of net sales and our customer base. Acquisitions, including the RHL acquisition, involve numerous risks, including:

- potential difficulties related to integrating the products, personnel and operations of the acquired company;
- failure to operate as a combined organization utilizing common information and communication systems, operating procedures, financial controls and human resources practices;
- diverting management's attention from the normal daily operations of the business;
- entering markets in which we have no or limited prior direct experience and where competitors in such markets have stronger market positions;
- potential loss of key employees of the acquired company;

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- potential inability to achieve cost savings and other potential benefits expected from the acquisition; and
- an uncertain sales and earnings stream from the acquired company.

There can be no assurance that our acquisition of RHL or other acquisitions that we may pursue will be successful. If we pursue an acquisition but are not successful in completing it, or if we complete an acquisition but are not successful in integrating the acquired company's employees, products or operations successfully, our business, financial position or results of operations could be adversely affected.

In addition to the risk factor above, you should carefully consider the other risks described under Item 7 of our 2005 Annual Report, as well as the other information in our 2005 Annual Report, this report and other reports and documents we file with the SEC, when evaluating our business and future prospects. If any of the identified risks actually occur, our business, financial condition and results of operations could be seriously harmed. In that event, the market price of our common stock could decline and you could lose all or a portion of the value of your investment in our common stock.

**ITEM 2. UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS**

On December 5, 2005, as part of the consideration payable to the selling stockholders of RHL in connection with the acquisition by NAI of all of the issued and outstanding shares of common stock, no par value, of RHL, NAI issued to the selling stockholders 510,000 shares, in the aggregate, of NAI's authorized but unissued shares of common stock, \$0.01 par value per share, under Rule 506 of Regulation D promulgated under the Securities Act of 1933, as amended. Each selling stockholder represented to NAI that he or it was an "accredited investor" as such term is defined under such Regulation D.

**ITEM 3. DEFAULTS UPON SENIOR SECURITIES**

None.



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**ITEM 4. SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS**

Our annual meeting of stockholders was held on December 2, 2005. The following table sets forth the matters voted upon at the meeting and the results of the voting on each matter voted upon:

<u>Matter Voted Upon</u>	<u>Votes For</u>	<u>Withheld</u>	<u>Votes Against</u>	<u>Abstentions</u>	<u>Broker Non-Votes</u>
Election of one Class III director to serve until the next annual meeting of stockholders held to elect Class III directors and until his successor is elected and qualified: Alan J. Lane	5,485,089	70,777	—	—	—
Ratification of the selection of Ernst & Young LLP as our independent registered public accounting firm for the fiscal year ending June 30, 2006	5,546,158	—	6,708	3,000	—

In accordance with the terms set forth in the proxy statement related to the solicitation of proxies for use at the annual meeting, an abstention from voting was used for the purpose of establishing a quorum, and was considered a vote “against” a proposal. A broker non-vote was also used for the purpose of establishing a quorum, but was not otherwise counted in the voting process. The named director and the above matter were each approved by the stockholders at the annual meeting.

**ITEM 5. OTHER INFORMATION**

None.

**ITEM 6. EXHIBITS**

The following exhibit index shows those exhibits filed with this report and those incorporated by reference:

**EXHIBIT INDEX**

<u>Exhibit Number</u>	<u>Description</u>	<u>Incorporated By Reference To</u>
3(i)	Amended and Restated Certificate of Incorporation of Natural Alternatives International, Inc. filed with the Delaware Secretary of State on January 14, 2005	Exhibit 3(i) of NAI’s Quarterly Report on Form 10-Q for the quarterly period ended December 31, 2004, filed with the commission on February 14, 2005
3(ii)	By-laws of Natural Alternatives International, Inc. dated as of December 21, 1990	NAI’s Registration Statement on Form S-1 (File No. 33-44292) filed with the commission on December 21, 1992
4(i)	Form of NAI’s Common Stock Certificate	Exhibit 4(i) of NAI’s Annual Report on Form 10-K for the fiscal year ended June 30, 2005, filed with the commission on September 8, 2005
10.1	1999 Omnibus Equity Incentive Plan as adopted effective May 10, 1999, amended effective January 30, 2004, and further amended effective December 3, 2004	Exhibit 10.1 of NAI’s Quarterly Report on Form 10-Q for the quarterly period ended December 31, 2004, filed with the commission on February 14, 2005

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10.2	1999 Employee Stock Purchase Plan as adopted effective October 18, 1999	Exhibit B of NAI's definitive Proxy Statement filed with the commission on October 21, 1999
10.3	Management Incentive Plan	Exhibit 10.3 of NAI's Quarterly Report on Form 10-Q for the quarterly period ended September 30, 2003, filed with the commission on November 5, 2003
10.4	Amended and Restated Employment Agreement dated as of January 30, 2004, by and between NAI and Mark Zimmerman	Exhibit 10.4 of NAI's Annual Report on Form 10-K for the fiscal year ended June 30, 2004, filed with the commission on September 14, 2004
10.5	Amended and Restated Employment Agreement dated as of January 30, 2004, by and between NAI and Randell Weaver	Exhibit 10.5 of NAI's Annual Report on Form 10-K for the fiscal year ended June 30, 2004, filed with the commission on September 14, 2004
10.6	Amended and Restated Employment Agreement dated as of January 30, 2004, by and between NAI and Mark A. LeDoux	Exhibit 10.6 of NAI's Annual Report on Form 10-K for the fiscal year ended June 30, 2004, filed with the commission on September 14, 2004
10.7	Amended and Restated Employment Agreement dated as of January 30, 2004, by and between NAI and John Wise	Exhibit 10.7 of NAI's Annual Report on Form 10-K for the fiscal year ended June 30, 2004, filed with the commission on September 14, 2004
10.8	Amended and Restated Employment Agreement dated as of January 30, 2004, by and between NAI and John Reaves	Exhibit 10.8 of NAI's Annual Report on Form 10-K for the fiscal year ended June 30, 2004, filed with the commission on September 14, 2004
10.9	Amended and Restated Employment Agreement dated as of January 30, 2004, by and between NAI and Timothy E. Belanger	Exhibit 10.9 of NAI's Annual Report on Form 10-K for the fiscal year ended June 30, 2004, filed with the commission on September 14, 2004
10.10	Amended and Restated Exclusive License Agreement effective as of September 1, 2004 by and among NAI and Dr. Reginald B. Cherry	Exhibit 10.11 of NAI's Annual Report on Form 10-K for the fiscal year ended June 30, 2004, filed with the commission on September 14, 2004
10.11	Exclusive License Agreement effective as of September 1, 2004 by and among NAI and Reginald B. Cherry Ministries, Inc.	Exhibit 10.12 of NAI's Annual Report on Form 10-K for the fiscal year ended June 30, 2004, filed with the commission on September 14, 2004
10.12	First Amendment to Exclusive License Agreement effective as of December 10, 2004 by and among NAI and Reginald B. Cherry Ministries, Inc.	Exhibit 10.3 of NAI's Quarterly Report on Form 10-Q for the quarterly period ended December 31, 2004, filed with the commission on February 14, 2005
10.13	Lease of Facilities in Vista, California between NAI and Calwest Industrial Properties, LLC, a California limited liability company (lease reference date June 12, 2003)	Exhibit 10.10 of NAI's Quarterly Report on Form 10-Q for the quarterly period ended September 30, 2003, filed with the commission on November 5, 2003

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10.14	Credit Agreement dated as of May 1, 2004 by and between NAI and Wells Fargo Bank, National Association	Exhibit 10.11 of NAI's Quarterly Report on Form 10-Q for the quarterly period ended March 31, 2004, filed with the commission on May 17, 2004
10.15	First Amendment to Credit Agreement dated as of February 1, 2005 by and between NAI and Wells Fargo Bank, National Association	Exhibit 10.1 of NAI's Current Report on Form 8-K dated February 1, 2005, filed with the commission on February 7, 2005
10.16	Form of Indemnification Agreement entered into between NAI and each of its directors	Exhibit 10.15 of NAI's Annual Report on Form 10-K for the fiscal year ended June 30, 2004, filed with the commission on September 14, 2004
10.17	Lease of Facilities in Manno, Switzerland between NAIE and Mr. Silvio Tarchini dated May 9, 2005 (English translation)	Exhibit 10.19 of NAI's Quarterly Report on Form 10-Q for the quarterly period ended March 31, 2005, filed with the commission on May 13, 2005
10.18	Lease of Facilities in Manno, Switzerland between NAIE and Mr. Silvio Tarchini dated July 25, 2003 (English translation)	Exhibit 10.19 of NAI's Annual Report on Form 10-K for the fiscal year ended June 30, 2005, filed with the commission on September 8, 2005
10.19	Lease of Facilities in Manno, Switzerland between NAIE and Mr. Silvio Tarchini dated June 8, 2004 (English translation)	Exhibit 10.20 of NAI's Annual Report on Form 10-K for the fiscal year ended June 30, 2005, filed with the commission on September 8, 2005
10.20	Lease of Facilities in Manno, Switzerland between NAIE and Mr. Silvio Tarchini dated February 7, 2005 (English translation)	Exhibit 10.21 of NAI's Annual Report on Form 10-K for the fiscal year ended June 30, 2005, filed with the commission on September 8, 2005
10.21	License Agreement effective as of April 28, 1997 by and among Roger Harris, Mark Dunnnett and NAI	Exhibit 10.22 of NAI's Annual Report on Form 10-K for the fiscal year ended June 30, 2005, filed with the commission on September 8, 2005
10.22	Amendment to License Agreement effective as of March 17, 2001 by and among Roger Harris, Mark Dunnnett and NAI	Exhibit 10.23 of NAI's Annual Report on Form 10-K for the fiscal year ended June 30, 2005, filed with the commission on September 8, 2005
10.23	Amendment effective as of September 15, 2005 to Lease of Facilities in Manno, Switzerland between NAIE and Mr. Silvio Tarchini dated May 9, 2005 (English translation)	Exhibit 10.24 of NAI's Quarterly Report on Form 10-Q for the quarterly period ended September 30, 2005, filed with the commission on November 4, 2005
10.24	Stock Purchase Agreement effective as of December 5, 2005, by and among NAI and William H. Bunten II and/or Elizabeth W. Bunten, as the trustees of The Bunten Family Trust dated April 14, 2001, John F. Dullea and Carolyn A. Dullea, as the trustees of The John F. and Carolyn A. Dullea Trust dated June 20, 2001, Lincoln Fish, and Michael L. Irwin, as trustee of The Michael L. Irwin Trust u/t/a June 25, 1991	Exhibit 10.1 of NAI's Current Report on Form 8-K dated December 5, 2005, filed with the commission on December 9, 2005

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10.25	Form of Lock-Up Agreement effective as of December 5, 2005 entered into between NAI and each Selling Stockholder	Exhibit 10.2 of NAI's Current Report on Form 8-K dated December 5, 2005, filed with the commission on December 9, 2005
10.26	Employment Agreement effective as of December 5, 2005, by and between RHL and John F. Dullea	Exhibit 10.3 of NAI's Current Report on Form 8-K dated December 5, 2005, filed with the commission on December 9, 2005
10.27	Lease of RHL Facilities in San Diego, California between RHL and Lessor dated February 5, 2003	Exhibit 10.4 of NAI's Current Report on Form 8-K dated December 5, 2005, filed with the commission on December 9, 2005
10.28	Promissory Note made by NAI for the benefit of Wells Fargo Equipment Finance, Inc. in the amount of \$3,800,000	Exhibit 10.5 of NAI's Current Report on Form 8-K dated December 5, 2005, filed with the commission on December 9, 2005
10.29	Patent License Agreement by and between Unither Pharma, Inc. and RHL dated May 1, 2002	Exhibit 10.6 of NAI's Current Report on Form 8-K dated December 5, 2005, filed with the commission on December 9, 2005
10.30	Second Amendment to Credit Agreement dated as of December 1, 2005 by and between NAI and Wells Fargo Bank, National Association	Filed herewith
10.31	Revolving Line of Credit Note (as revised) made by NAI for the benefit of Wells Fargo Bank, National Association in the amount of \$8,000,000	Filed herewith
10.32	Exclusive License Agreement by and between NAI and Richard Linchitz, M.D. effective as of August 23, 2005	Filed herewith
10.33	Letter amendment to Lease of RHL Facilities in San Diego, California between RHL and Lessor dated January 10, 2006	Filed herewith
10.34	First Amendment to Lease of Facilities in Vista, California between NAI and Calwest Industrial Properties, LLC, a California limited liability company, effective December 21, 2004	Filed herewith
10.35	Second Amendment to Lease of Facilities in Vista, California between NAI and Calwest Industrial Properties, LLC, a California limited liability company, effective January 13, 2006	Filed herewith
31.1	Rule 13a-14(a)/15d-14(a) Certification of Chief Executive Officer	Filed herewith
31.2	Rule 13a-14(a)/15d-14(a) Certification of Chief Financial Officer	Filed herewith
32	Section 1350 Certification	Filed herewith

**SIGNATURES**

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

Date: February 14, 2006

NATURAL ALTERNATIVES INTERNATIONAL, INC.

By: /s/ John R. Reaves  
John R. Reaves, Chief Financial Officer

Mr. Reaves is the principal financial officer of Natural Alternatives International, Inc. and has been duly authorized to sign on its behalf.

## SECOND AMENDMENT TO CREDIT AGREEMENT

THIS AMENDMENT TO CREDIT AGREEMENT (this "Amendment") is entered into as of December 1, 2005, by and between NATURAL ALTERNATIVES INTERNATIONAL, INC., a Delaware corporation ("Borrower"), and WELLS FARGO BANK, NATIONAL ASSOCIATION ("Bank").

RECITALS

WHEREAS, Borrower is currently indebted to Bank pursuant to the terms and conditions of that certain Credit Agreement between Borrower and Bank dated as of May 1, 2004, as amended from time to time ("Credit Agreement").

WHEREAS, Bank and Borrower have agreed to certain changes in the terms and conditions set forth in the Credit Agreement and have agreed to amend the Credit Agreement to reflect said changes.

NOW, THEREFORE, for valuable consideration, the receipt and sufficiency of which are hereby acknowledged, the parties hereto agree that the Credit Agreement shall be amended as follows:

1. Section 1.1.(a) is hereby amended by deleting "November 1, 2006" as the last day on which Bank will make advances under the Line of Credit, and by substituting for said date "November 1, 2007," with such change to be effective upon the execution and delivery to Bank of a promissory note dated as of December 1, 2005 (which promissory note shall replace and be deemed the Line of Credit Note defined in and made pursuant to the Credit Agreement) and all other contracts, instruments and documents required by Bank to evidence such change.

2. Section 1.4.(a) is hereby deleted in its entirety, and the following substituted therefor:

"(a) Foreign Exchange Facility. Subject to the terms and conditions of this Agreement, Bank hereby agrees to make available to Borrower a facility (the "Foreign Exchange Facility") under which Bank, from time to time up to and including November 1, 2007, will enter into foreign exchange contracts for the account of Borrower for the purchase and/or sale by Borrower in United States dollars of foreign currencies designated by Borrower; provided however, that the contact limit shall not at any time exceed an aggregate of One Million Eight Hundred Thousand United States Dollars (US\$1,800,000.00). No foreign exchange contract shall be executed for a term which extends beyond November 1, 2008. Borrower shall have a "Delivery Limit" under the Foreign Exchange Facility not to exceed at any time the aggregate principal amount of Zero United States Dollars (US\$0.00) with PVD ("Payment versus Delivery") which will require Borrower to provide funds before the currency is delivered

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and this will eliminate the 1 or 2 business day settlement period and mitigate settlement risk. All foreign exchange transactions shall be subject to the additional terms of a Foreign Exchange Agreement dated as of May 1, 2004 ("Foreign Exchange Agreement"), all terms of which are incorporated herein by this reference."

3. Section 4.3.(d) is hereby deleted in its entirety, and the following substituted therefor:

"(d) not later than 15 days after and as of the end of each month, an inventory collateral report, an aged listing of accounts receivable and accounts payable, and a reconciliation of accounts; semi-monthly collateral report if Borrower elects to use 35% concentration allowance for Obesity Research, Fiber Thin and Mannatech, Inc., and not later than 30 days after and as of the end of each May and November, a list of the names, addresses and contact phone numbers of all Borrower's account debtors;"

4. Sections 4.9.(b) and (d) are hereby deleted in their entirety, and the following substituted therefor:

"(b) Total Liabilities divided by Tangible Net Worth not greater than 1.25 to 1.0 until fiscal year end June 30, 2007 and not greater than 1.0 to 1.0, thereafter, with "Total Liabilities" defined as the aggregate of current liabilities and non-current liabilities less subordinated debt, and with "Tangible Net Worth" as defined above.

(d) Fixed Charge Coverage Ratio not less than 1.25 to 1.0 as of each fiscal quarter end, with "Fixed Charge Coverage Ratio" defined as the aggregate of net profit after taxes plus depreciation expense, amortization expense and net contributions, divided by the aggregate of the current maturity of long-term debt and capitalized lease payments."

5. Sections 5.2., 5.3., 5.4., 5.5. and 5.9. are hereby deleted in their entirety, and the following substituted therefor:

"SECTION 5.2. CAPITAL EXPENDITURES. Make any additional investment in fixed assets in any fiscal year in excess of an aggregate of \$5,500,000.00.

SECTION 5.3. LEASE EXPENDITURES. Incur operating lease expense in any fiscal year in excess of an aggregate of \$500,000.00.

SECTION 5.4. OTHER INDEBTEDNESS. Create, incur, assume or permit to exist any indebtedness or liabilities resulting from borrowings, loans or advances, whether secured or

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unsecured, matured or unmatured, liquidated or unliquidated, joint or several, except (a) the liabilities of Borrower to Bank, (b) any other liabilities of Borrower existing as of, and disclosed to Bank prior to, the date hereof, and (c) liabilities which may be obtained for NAI Europe not to exceed an aggregate of \$1,000,000.00.

SECTION 5.5. MERGER, CONSOLIDATION, TRANSFER OF ASSETS. Merge into or consolidate with any other entity; make any substantial change in the nature of Borrower's business as conducted as of the date hereof; acquire all or substantially all of the assets of any other entity; nor sell, lease, transfer or otherwise dispose of all or a substantial or material portion of Borrower's assets except (a) in the ordinary course of its business, and (b) the acquisition of Real Health Laboratories, Inc. to be completed during fiscal year end of 2006.

SECTION 5.9. PLEDGE OF ASSETS. Mortgage, pledge, grant or permit to exist a security interest in, or lien upon, all or any portion of Borrower's assets now owned or hereafter acquired, except any of the foregoing in favor of Bank or which is existing as of, and disclosed to Bank in writing prior to, the date hereof, and liens to the extent permitted under Section 5.4. hereunder."

6. Section 7.2. is hereby amended by deleting the reference to "Carlsbad LPO, 5857 Owens Avenue, Suite 106, Carlsbad, CA 92008" as the Bank's address, and by substituting therefor: "San Diego Regional Commercial Banking Office, 401 B Street, Suite 2201, San Diego, CA 92101"

7. In consideration of the set forth herein and as a condition to the effectiveness hereof, Borrower shall pay to Bank a non-refundable commitment fee equal to \$10,000.00, which fee shall be due and payable in full on November 1, 2006.

8. Except as specifically provided herein, all terms and conditions of the Credit Agreement remain in full force and effect, without waiver or modification. All terms defined in the Credit Agreement shall have the same meaning when used in this Amendment. This Amendment and the Credit Agreement shall be read together, as one document.

9. Borrower hereby remakes all representations and warranties contained in the Credit Agreement and reaffirms all covenants set forth therein. Borrower further certifies that as of the date of this Amendment there exists no Event of Default as defined in the Credit Agreement, nor any condition, act or event which with the giving of notice or the passage of time or both would constitute any such Event of Default.



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IN WITNESS WHEREOF, the parties hereto have caused this Amendment to be executed as of the day and year first written above.

NATURAL ALTERNATIVES  
INTERNATIONAL, INC.

WELLS FARGO BANK,  
NATIONAL ASSOCIATION

By: /s/ Randell Weaver  
Randell Weaver  
President

By: /s/ Bernie Palmer  
Bernie Palmer  
Vice President

By: /s/ John Reaves  
John Reaves  
Chief Financial Officer

WELLS FARGO

**\$8,000,000.00****REVOLVING LINE OF CREDIT NOTE****San Diego, California  
December 1, 2005**

FOR VALUE RECEIVED, the undersigned **Natural Alternatives International, Inc.** ("Borrower") promises to pay to the order of WELLS FARGO BANK, NATIONAL ASSOCIATION ("Bank") at its office at **San Diego RCBO, 401 B Street, Suite #2201, San Diego, CA 92101**, or at such other place as the holder hereof may designate, in lawful money of the United States of America and in immediately available funds, the principal sum of **\$8,000,000.00**, or so much thereof as may be advanced and be outstanding, with interest thereon, to be computed on each advance from the date of its disbursement as set forth herein.

**1. DEFINITIONS:**

As used herein, the following terms shall have the meanings set forth after each, and any other term defined in this Note shall have the meaning set forth at the place defined:

1.1 "Business Day" means any day except a Saturday, Sunday or any other day on which commercial banks in California are authorized or required by law to close.

1.2 "Fixed Rate Term" means a period commencing on a Business Day and continuing for **1, 2, 3, 6 or 12 months**, as designated by Borrower, during which all or a portion of the outstanding principal balance of this Note bears interest determined in relation to LIBOR; provided however, that no Fixed Rate Term may be selected for a principal amount less than **\$100,000.00**; and provided further, that no Fixed Rate Term shall extend beyond the scheduled maturity date hereof. If any Fixed Rate Term would end on a day which is not a Business Day, then such Fixed Rate Term shall be extended to the next succeeding Business Day.

1.3 "LIBOR" means the rate per annum (rounded upward, if necessary, to the nearest whole 1/8 of 1%) determined by dividing Base LIBOR by a percentage equal to 100% less any LIBOR Reserve Percentage.

(a) "Base LIBOR" means the rate per annum for United States dollar deposits quoted by Bank as the Inter-Bank Market Offered Rate, with the understanding that such rate is quoted by Bank for the purpose of calculating effective rates of interest for loans making reference thereto, on the first day of a Fixed Rate Term for delivery of funds on said date for a period of time approximately equal to the number of days in such Fixed Rate Term and in an amount approximately equal to the principal amount to which such Fixed Rate Term applies. Borrower understands and agrees that Bank may base its quotation of the Inter-Bank Market Offered Rate upon such offers or other market indicators of the Inter-Bank Market as Bank in its discretion deems appropriate including, but not limited to, the rate offered for U.S. dollar deposits on the London Inter-Bank Market.

(b) "LIBOR Reserve Percentage" means the reserve percentage prescribed by the Board of Governors of the Federal Reserve System (or any successor) for "Eurocurrency Liabilities" (as defined in Regulation D of the Federal Reserve Board, as amended), adjusted by Bank for expected changes in such reserve percentage during the applicable Fixed Rate Term.

1.4 "Prime Rate" means at any time the rate of interest most recently announced within Bank at its principal office as its Prime Rate, with the understanding that the Prime Rate is one of Bank's base rates and serves as the basis upon which effective rates of interest are calculated for those loans making reference thereto, and is evidenced by the recording thereof after its announcement in such internal publication or publications as Bank may designate.

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## 2. INTEREST:

2.1 Interest. The outstanding principal balance of this Note shall bear interest (computed on the basis of a **360**-day year, actual days elapsed) either (a) at a fluctuating rate per annum **equal to** the Prime Rate in effect from time to time, or (b) at a fixed rate per annum determined by Bank to be **1.75000%** above LIBOR in effect on the first day of the applicable Fixed Rate Term. When interest is determined in relation to the Prime Rate, each change in the rate of interest hereunder shall become effective on the date each Prime Rate change is announced within Bank. With respect to each LIBOR selection option selected hereunder, Bank is hereby authorized to note the date, principal amount, interest rate and Fixed Rate Term applicable thereto and any payments made thereon on Bank's books and records (either manually or by electronic entry) and/or on any schedule attached to this Note, which notations shall be prima facie evidence of the accuracy of the information noted.

2.2 Selection of Interest Rate Options. At any time any portion of this Note bears interest determined in relation to LIBOR, it may be continued by Borrower at the end of the Fixed Rate Term applicable thereto so that all or a portion thereof bears interest determined in relation to the Prime Rate or to LIBOR for a new Fixed Rate Term designated by Borrower. At any time any portion of this Note bears interest determined in relation to the Prime Rate, Borrower may convert all or a portion thereof so that it bears interest determined in relation to LIBOR for a Fixed Rate Term designated by Borrower. At such time as Borrower requests an advance hereunder or wishes to select a LIBOR option for all or a portion of the outstanding principal balance hereof, and at the end of each Fixed Rate Term, Borrower shall give Bank notice specifying: (a) the interest rate option selected by Borrower; (b) the principal amount subject thereto; and (c) for each LIBOR selection, the length of the applicable Fixed Rate Term. Any such notice may be given by telephone (or such other electronic method as Bank may permit) so long as, with respect to each LIBOR selection, (i) if requested by Bank, Borrower provides to Bank written confirmation thereof not later than 3 Business Days after such notice is given, and (ii) such notice is given to Bank prior to 10:00 a.m. on the first day of the Fixed Rate Term, or at a later time during any Business Day if Bank, at its sole option but without obligation to do so, accepts Borrower's notice and quotes a fixed rate to Borrower. If Borrower does not immediately accept a fixed rate when quoted by Bank, the quoted rate shall expire and any subsequent LIBOR request from Borrower shall be subject to a redetermination by Bank of the applicable fixed rate. If no specific designation of interest is made at the time any advance is requested hereunder or at the end of any Fixed Rate Term, Borrower shall be deemed to have made a Prime Rate interest selection for such advance or the principal amount to which such Fixed Rate Term applied.

2.3 Taxes and Regulatory Costs. Borrower shall pay to Bank immediately upon demand, in addition to any other amounts due or to become due hereunder, any and all (a) withholdings, interest equalization taxes, stamp taxes or other taxes (except income and franchise taxes) imposed by any domestic or foreign governmental authority and related in any manner to LIBOR, and (b) future, supplemental, emergency or other changes in the LIBOR Reserve Percentage, assessment rates imposed by the Federal Deposit Insurance Corporation, or similar requirements or costs imposed by any domestic or foreign governmental authority or resulting from compliance by Bank with any request or directive (whether or not having the force of law) from any central bank or other governmental authority and related in any manner to LIBOR to the extent they are not included in the calculation of LIBOR. In determining which of the foregoing are attributable to any LIBOR option available to Borrower hereunder, any reasonable allocation made by Bank among its operations shall be conclusive and binding upon Borrower.

2.4 Payment of Interest. Interest accrued on this Note shall be payable on the **1st** day of each **month**, commencing **January 1, 2006**.

2.5 Default Interest. From and after the maturity date of this Note, or such earlier date as all principal owing hereunder becomes due and payable by acceleration or otherwise, the outstanding principal balance of this Note shall bear interest until paid in full at an increased rate per annum (computed on the basis of a **360**-day year, actual days elapsed) equal to **4%** above the rate of interest from time to time applicable to this Note.

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### 3. BORROWING AND REPAYMENT:

3.1 Borrowing and Repayment. Borrower may from time to time during the term of this Note borrow, partially or wholly repay its outstanding borrowings, and reborrow, subject to all of the limitations, terms and conditions of this Note and of the Credit Agreement between Borrower and Bank defined below; provided however, that the total outstanding borrowings under this Note shall not at any time exceed the principal amount stated above. The unpaid principal balance of this obligation at any time shall be the total amounts advanced hereunder by the holder hereof less the amount of principal payments made hereon by or for any Borrower, which balance may be endorsed hereon from time to time by the holder. The outstanding principal balance of this Note shall be due and payable in full on **November 1, 2007**.

3.2 Advances. Advances hereunder, to the total amount of the principal sum available hereunder, may be made by the holder at the oral or written request of (a) **Randell Weaver, John Reaves**, any one acting alone, who are authorized to request advances and direct the disposition of any advances until written notice of the revocation of such authority is received by the holder at the office designated above, or (b) any person, with respect to advances deposited to the credit of any deposit account of any Borrower, which advances, when so deposited, shall be conclusively presumed to have been made to or for the benefit of each Borrower regardless of the fact that persons other than those authorized to request advances may have authority to draw against such account. The holder shall have no obligation to determine whether any person requesting an advance is or has been authorized by any Borrower.

3.3 Application of Payments. Each payment made on this Note shall be credited first, to any interest then due and second, to the outstanding principal balance hereof. All payments credited to principal shall be applied first, to the outstanding principal balance of this Note which bears interest determined in relation to the Prime Rate, if any, and second, to the outstanding principal balance of this Note which bears interest determined in relation to LIBOR, with such payments applied to the oldest Fixed Rate Term first.

### 4. PREPAYMENT:

4.1 Prime Rate. Borrower may prepay principal on any portion of this Note which bears interest determined in relation to the Prime Rate at any time, in any amount and without penalty.

4.2 LIBOR. Borrower may prepay principal on any portion of this Note which bears interest determined in relation to LIBOR at any time and in the minimum amount of **\$100,000.00**; provided however, that if the outstanding principal balance of such portion of this Note is less than said amount, the minimum prepayment amount shall be the entire outstanding principal balance thereof. In consideration of Bank providing this prepayment option to Borrower, or if any such portion of this Note shall become due and payable at any time prior to the last day of the Fixed Rate Term applicable thereto by acceleration or otherwise, Borrower shall pay to Bank immediately upon demand a fee which is the sum of the discounted monthly differences for each month from the month of prepayment through the month in which such Fixed Rate Term matures, calculated as follows for each such month:

(a) Determine the amount of interest which would have accrued each month on the amount prepaid at the interest rate applicable to such amount had it remained outstanding until the last day of the Fixed Rate Term applicable thereto.

(b) Subtract from the amount determined in (a) above the amount of interest which would have accrued for the same month on the amount prepaid for the remaining term of such Fixed Rate Term at LIBOR in effect on the date of prepayment for new loans made for such term and in a principal amount equal to the amount prepaid.

(c) If the result obtained in (b) for any month is greater than zero, discount that difference by LIBOR used in (b) above.

Each Borrower acknowledges that prepayment of such amount may result in Bank incurring additional costs, expenses and/or liabilities, and that it is difficult to ascertain the full extent of such costs, expenses and/or liabilities. Each Borrower, therefore, agrees to pay the above-described prepayment fee and agrees that said amount represents a reasonable estimate of the prepayment costs, expenses and/or liabilities of Bank. If Borrower fails to pay any prepayment fee when due, the amount of such prepayment fee shall thereafter bear interest until paid at a rate per annum **2.000%** above the Prime Rate in effect from time to time (computed on the basis of a **360**-day year, actual days elapsed). Each change in the rate of interest on any such past due prepayment fee shall become effective on the date each Prime Rate change is announced within Bank.

**5. EVENTS OF DEFAULT:**

This Note is made pursuant to and is subject to the terms and conditions of that certain Credit Agreement between Borrower and Bank dated as of **May 1, 2004**, as amended from time to time (the "Credit Agreement"). Any default in the payment or performance of any obligation under this Note, or any defined event of default under the Credit Agreement, shall constitute an "Event of Default" under this Note.

**6. MISCELLANEOUS:**

6.1 Remedies. Upon the occurrence of any Event of Default, the holder of this Note, at the holder's option, may declare all sums of principal and interest outstanding hereunder to be immediately due and payable without presentment, demand, notice of nonperformance, notice of protest, protest or notice of dishonor, all of which are expressly waived by each Borrower, and the obligation, if any, of the holder to extend any further credit hereunder shall immediately cease and terminate. Each Borrower shall pay to the holder immediately upon demand the full amount of all payments, advances, charges, costs and expenses, including reasonable attorneys' fees (to include outside counsel fees and all allocated costs of the holder's in-house counsel), expended or incurred by the holder in connection with the enforcement of the holder's rights and/or the collection of any amounts which become due to the holder under this Note, and the prosecution or defense of any action in any way related to this Note, including without limitation, any action for declaratory relief, whether incurred at the trial or appellate level, in an arbitration proceeding or otherwise, and including any of the foregoing incurred in connection with any bankruptcy proceeding (including without limitation, any adversary proceeding, contested matter or motion brought by Bank or any other person) relating to any Borrower or any other person or entity.

6.2 Obligations Joint and Several. Should more than one person or entity sign this Note as a Borrower, the obligations of each such Borrower shall be joint and several.

6.3 Governing Law. This Note shall be governed by and construed in accordance with the laws of the State of California.

IN WITNESS WHEREOF, the undersigned has executed this Note as of the date first written above.

Natural Alternatives International, Inc.

By: /s/ Randell Weaver  
Randell Weaver, President

By: /s/ John Reaves  
John Reaves, Chief Financial Officer

**EXCLUSIVE LICENSE AGREEMENT**

This EXCLUSIVE LICENSING AGREEMENT ("Agreement") is entered into effective as of August 23, 2005, between Natural Alternatives International, Inc., a Delaware corporation ("NAI"), with its principal offices at 1185 Linda Vista Drive, San Marcos, California 92078, and Richard Linchitz, M.D. ("Linchitz") an individual with a principal business address at 66 Highland Road, Glen Cove, New York 11542. The parties to this Agreement are sometimes referred to as "Party" or "Parties."

**RECITALS**

A. NAI desires to research, formulate, manufacture, package and market nutritional supplements and related goods using the name, image, signature, voice, likeness, style and persona of Linchitz ("Linchitz Name") in all channels of distribution worldwide.

B. Linchitz desires that NAI have an exclusive license to use the Linchitz Name to market nutritional supplements, dietary supplements and related materials, products and goods of any description in all channels of distribution worldwide and that NAI have the right to file applications for registrations and obtain registrations for, without limitation, patents, trademarks, logos, domain names and copyrights ("NAI Registrations" and as further defined in Section 2.2 below) in connection with NAI's use of the Linchitz Name.

C. The success of NAI's investment in the Linchitz Name, Linchitz Registrations and the NAI Registrations relies heavily on the enthusiasm of Linchitz in promoting the products as spokesperson in a variety of media, including NAI developed communications, and through active article and book writing and speaking engagements.

**AGREEMENT**

Incorporating the above recitals and in consideration of the covenants and obligations contained herein and other good and valuable consideration, the receipt and sufficiency of which is hereby acknowledged, the Parties agree as follows:

**1. DEFINITIONS**

1.1 "Channels of Distribution" shall mean all channels of distribution including without limitation retail, Direct Response TV, Series TV, Direct Mail, Direct Response Radio, Direct Response Print and the Internet or World Wide Web. For purposes of this Agreement, "Internet" or "World Wide Web" or "Web" shall mean a system for accessing and viewing text, graphics, sound and other media via the collection of computer networks known as the Internet.

1.2 "Direct Competitor" shall refer to any person or business entity that develops items and/or sells products or provides services relating to the research, formulation, manufacture, packaging and marketing of nutritional products or other Products or services contemplated by this Agreement, excluding medical services and management provided by Linchitz (collectively, starting with the phrase "or services", "Services").

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1.3 "Net Sales" shall mean the gross invoice amount billed by NAI to purchasers of the Products, less customer shipping and handling charges, credit card charge fees and returns actually credited.

1.4 "Product" or "Products" means all nutritional foods, nutritional and dietary supplements and related materials or products of any description, including without limitation capsules, tablets, powders, liquids, bars, creams, lotions, gels and other forms, using the Linchitz Name, Linchitz Registrations and NAI Registrations, packaged in any manner and promoted in any manner, both in accordance with the terms of this Agreement, including without limitation in newsletters, on the Internet, in workshops and at seminars, and all other attributes of such products whether currently existing or to be developed during the term as part of the Linchitz Name, Linchitz Registrations and NAI Registrations. The definition of Product includes any modification, derivative, alteration, improvement, enhancement or successor thereof (collectively "Enhanced Product(s)") developed or contemplated by the Parties during the term of this Agreement; provided that, NAI demonstrates a bona fide good faith intent to market and sell any such contemplated Enhanced Product(s) within a commercially reasonable time of such contemplation. NAI shall have the right to have the labeling and all promotional materials for all Products include a representation that the Product has been manufactured by NAI.

1.5 "Territory" shall mean worldwide.

## **2. GRANT OF LICENSE**

2.1 Subject to the terms and conditions of this Agreement, Linchitz grants to NAI an exclusive, worldwide license to use the Linchitz Name and Linchitz Registrations on or in connection with the development, marketing and sale of any Products or services of NAI in all Channels of Distribution in the Territory during the term of this Agreement.

2.2 Linchitz grants to NAI the worldwide right to develop, use and register derivatives of the Linchitz Name for new NAI Registrations. NAI may combine any designation with the Linchitz Name so as to form without limitation a new trademark, service mark, trade name, patent, logo, domain name or copyright. Such NAI Registrations shall include any names or marks used by NAI prior to the Effective Date of this Agreement. Subject to the terms of this Agreement, NAI shall be the owner of the NAI Registrations (but not of the Linchitz Name incorporated therein or any registrations, applications, names or marks related thereto, collectively starting with "the Linchitz Name . . .", the "Linchitz Registrations"). After Linchitz's death or disability, NAI may use the Linchitz Name and NAI Registrations for any additional use contemplated by this Agreement provided that any such use is substantially consistent with the image, look and goodwill of the Linchitz Name. Notwithstanding the foregoing, Linchitz shall not have the right to use any mark or name which is identical to or likely to be confused with any mark or name owned by NAI.

2.3 NAI acknowledges that it is not and will not become by virtue of this Agreement the owner of any right, title or interest in and to the Linchitz Name or Linchitz Registrations in any form or embodiment. NAI shall promptly take all necessary actions to protect the Linchitz Name, Linchitz Registrations and the goodwill related thereto consistent with the provisions of

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this Section. All goodwill generated under this Agreement in the Linchitz Name and Linchitz Registrations shall inure to the benefit of Linchitz.

**3. DUTIES, WARRANTS AND REPRESENTATIONS OF LINCCHITZ**

3.1 **Duties of Linchitz.** In connection with this License Agreement and the rights granted hereunder, Linchitz warrants and represents to:

3.1.1 Use commercially reasonable best efforts to promote and develop the Linchitz Name and Linchitz Registrations and educate the general public about the benefits of using the Products through active writing of books, through active writing of articles in magazines, journals and other publications, through speaking engagements designed to teach about the benefits of the Products and through a variety of media including without limitation personal appearances on selected national and/or local network televisions and/or radio shows such as the Oprah Winfrey Show, Dateline, Larry King Live and Regis. In connection with such educational and promotional efforts, Linchitz shall maintain his medical license in all currently active jurisdictions and use commercially reasonable best efforts to maintain or expand the scope of distribution and public awareness of the existing programs, workshops, seminars, Web site, books and articles featuring the Linchitz Name and Linchitz Registrations (hereafter, all of the above, collectively, the "Linchitz Educational and Promotional Efforts").

3.1.2 Devote such time, effort, attention and energies as commercially reasonably required to create print, videotape and audiotape materials connected to the development of custom produced Direct Response TV, Series TV, Direct Mail, Direct Response Radio and Direct Response Print programs and the Internet or World Wide Web and be responsible for participating in ongoing advertising and marketing efforts relating to the Products (hereafter, all of the above, collectively, the "Linchitz's Direct Marketing Efforts").

3.1.2.1. Linchitz acknowledges the success of the Products and investment being made in the Linchitz Name and Linchitz Registrations by NAI depends heavily on Linchitz's personality, persona, image and leadership and, that as the spokesperson for the brand, Linchitz's dedicated good faith pronouncements are crucial to the successful marketing of all Products. Linchitz acknowledges and accepts that NAI will develop and that Linchitz will promote Linchitz approved communications that are highly personal, passionate and persuasive and that such communications must be delivered by Linchitz's good faith credible voice.

3.1.2.2. Linchitz acknowledges familiarity with the types of acquisition marketing to be utilized by NAI under this Agreement and understands that successful acquisition marketing of those types is educational, aggressive, promises to solve a health problem, is outspoken and opinionated and showcases the passion and personality of the spokesperson doctor, provided that, any such marketing does not constitute a violation of any applicable law, rule or regulation of any government or regulatory body.

3.1.3 Remain knowledgeable and up to date with new research regarding nutrition and health and develop opinions based on new research and findings in the nutritional



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supplements industry. Remain knowledgeable and up to date regarding new ingredients, raw materials, studies and discoveries.

3.1.4 Regularly meet, confer and cooperate with NAI in connection with the development of Products and marketing plans, the prioritizing of Product development and marketing, the review of business ideas and issues facing Products and other action items related to the marketing of Products.

3.1.5 Make available to NAI a monthly business schedule and public and media appearance schedule and vacation schedule for use in scheduling meetings and conferences with NAI and for coordinating review of NAI's promotional copy materials.

3.1.6 Subject to any known conflict with Linchitz's vacation schedule, review, edit and approve within six (6) business days of receipt all new promotional copy with a focus on the technical accuracy of the information. Any failure to approve or disapprove of such materials in writing within the time period provided shall constitute approval. It is understood only new promotional copy will be reviewed by Linchitz and that minor modifications of current packages already tested do not require the further approval of Linchitz. For purposes of this subsection only and without amending or modifying any other section of this Agreement, the Parties agree notice or consent may be given via facsimile or email. All notices under this subsection delivered either by facsimile or email will be deemed to have been duly given one day after confirmation of receipt provided that in either case a confirmation copy of the facsimile notice or email notice shall also be subsequently delivered within one day either (i) by hand (prepaid, with written confirmation of receipt by such receiving Party) or (ii) via overnight delivery by a nationally recognized overnight delivery service (prepaid, receipt requested along with such receiving Party's manual signature).

3.1.7 Cooperate to be available to NAI for up to ten (10) full business days each calendar year for exclusive business meetings or product development meetings with NAI. Linchitz shall be entitled to a per diem expense budget of One Hundred Fifty Dollars (\$150) per day, adjusted from time to time through the term, plus reimbursement for reasonable travel related expenses and other approved costs incurred exclusively on behalf of NAI. Travel related expenses eligible for reimbursement include without limitation first class airfare, car and driver and hotel and meals accommodations. NAI shall approve and promptly reimburse Linchitz for travel related expenses incurred in connection with promotion of Products on a non-exclusive basis in amounts mutually agreed upon by the Parties.

3.1.8 Not knowingly permit, do or commit any act or thing that would degrade, tamish, deprecate or disparage Linchitz, the Products or NAI or the public image of NAI in society or standing in the community and that Linchitz will terminate such activities promptly upon notice.

### **3.2 Additional Representations of Linchitz.**

3.2.1 Linchitz represents he is the exclusive owner of all right, title and interest in and to (i) his image, signature, voice and likeness and goodwill appurtenant thereto, (ii) all

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rights of publicity in and to his name, image, likeness, voice, signature and other elements of his persona and identity, (iii) all rights in and to his name, (iv) all common law and statutory rights in the foregoing and has complete authority to grant this license to use the Linchitz Name in the manner and form provided in this Agreement.

3.2.2 Linchitz further represents (i) he has not received notice of any claim with respect to the Linchitz Name inconsistent with his exclusive ownership of the Linchitz Name and has not received notice at any time of any unauthorized use thereof; (ii) to the best of Linchitz's knowledge and belief, the Linchitz Name does not infringe upon or violate any rights of any third party, and (iii) neither the execution and delivery of this Agreement nor the consummation of the transactions contemplated hereunder will violate or constitute a default under any agreement or instrument to which Linchitz is a party or by which he is bound.

3.2.3 Linchitz grants permission to NAI to conduct any reasonable physical examination, background test or drug test during the term of this Agreement. NAI shall bear all costs of such testing.

**3.3 Competitive Protection.** Effective as of the date of this Agreement and continuing throughout the term, Linchitz agrees:

3.3.1 to not render services in the form of advertising, publicizing, promoting, sponsoring or endorsing any items, products or services that compete in the marketplace with any Products or Services contemplated by this Agreement;

3.3.2 to neither permit nor authorize the use of the Linchitz Name or Linchitz Registrations, including without limitation the name and/or likeness (photograph and/or drawing), voice, signature and/or endorsement of Linchitz, by any Direct Competitor or by any third party whose items, products or services compete in the marketplace with any Products or services contemplated by this Agreement or that are manufactured by NAI;

3.3.3 to not allow Bio Quest medical centers (to the extent Linchitz has such restricted authority), an entity in which Linchitz has no formal relationship but one with which Linchitz is in negotiations to potentially do business with as an operator and manager of medical practices, or Metropolitan Medical Health Care and Wellness, a New York based medical facility owned by Linchitz, to use the Linchitz Name and Linchitz Registrations to promote items, products or services of any Direct Competitor or any third party whose items, products or services compete in the marketplace with any Products or services contemplated by this Agreement.

3.3.4 notwithstanding the foregoing, Linchitz is entitled to (i) use the Linchitz Name and Linchitz Registrations solely in connection with marketing, selling and distribution of Products in the Medical Health Care and Wellness channel of distribution or any other channel of distribution mutually agreed to by the Parties in writing, and (ii) operate, service and manage the Medical Health Care and Wellness medical practice in his sole discretion, provided all such activities under (i) and (ii) are not related in any way to the promotion of items, products or services of any Direct Competitor or any third party whose items, products or services directly

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compete in the marketplace with any NAI Products or Services contemplated by this Agreement; provided further that any such promotions, Products or Services or any restrictions placed upon Linchitz related thereto shall not conflict with Linchitz abiding by his sworn medical oath or professional ethical standards.

#### **4. DUTIES, WARRANTS AND REPRESENTATIONS OF NAI**

**4.1 Exclusive Duties of NAI.** In connection with this License Agreement and the rights granted hereunder, NAI shall:

4.1.1 Have all responsibility for the funding and management of Product development, Product research, Product formulations and specifications, brand strategy, marketing, securing and maintaining registration of the Linchitz Name and Linchitz Registrations in the Territory and all related business operations including profit and loss management.

4.1.2 Have all responsibility for the funding and management of Linchitz Educational and Promotional Efforts and Linchitz's Direct Marketing Efforts when such efforts are at the request of and managed by, through or on behalf of NAI. When such efforts are at the request of Linchitz, Linchitz shall present to NAI a budget and schedule for Linchitz Educational and Promotional Efforts and Linchitz Direct Marketing Efforts and obtain NAI's written approval in advance, which approval shall be at NAI's discretion, and NAI will then have all responsibility for the funding and management of such agreed to efforts.

4.1.3 Develop, fund, produce, distribute and/or maintain all marketing materials including all communications, Web site design and content, collateral, special reports, e-letters, public relations support and Product marketing.

4.1.4 Manage and fund cross functional teams consisting of without limitation research and development, packaging, legal, call center and fulfillment.

4.1.5 Take such actions as are commercially reasonable in an effort to successfully develop, promote, advertise and market the Products.

#### **4.2 Additional Duties of NAI.**

4.2.1 Take such actions, in accordance with the terms of this Agreement, as are commercially reasonable in an effort to design, develop, manufacture, promote, advertise, market and sell the maximum number of Products while maintaining quality and service to all customers.

4.2.2 Maintain a mutually agreed upon regular schedule of contact with Linchitz to discuss ideas, priorities, action steps and issues.

4.2.3 Review and/or provide material, in accordance with the terms of this Agreement, for inclusion in or use in connection with programs, workshops, seminars, Web site, books, CDs and audiotapes featuring the Linchitz Name and Linchitz Registrations.

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4.2.4 Use reasonable best efforts to commence production, promotion, marketing and distribution of Products as soon as reasonably practical following the date of this Agreement.

4.2.5 Not knowingly permit, do or commit any act or thing that would degrade, tamish or deprecate or disparage itself, the Products or Linchitz or the public image of Linchitz in society or standing in the community and that it will terminate such activities promptly upon notice.

#### 4.3 Additional Representations of NAI.

4.3.1 NAI represents, warrants and covenants that: (i) it has the authority to enter into this Agreement; (ii) neither the execution and delivery of this Agreement nor the consummation of the transactions contemplated hereunder will violate or constitute a default under any agreement, order, judgment, decree or instrument to which NAI is a party or by which it is bound nor require NAI to obtain any-permit, consent or approval of any government or regulatory body, person, firm, corporation or other entity; (iii) it is the owner or valid licensee of all Product formulations, specifications and technical information about the Products, all packaging, designs and other intellectual property associated with the Products, and any element or component proprietary to NAI included in the Products or any part thereof, (iv) such Product formulations, specifications and technical information about the Products, all packaging, designs, materials and other intellectual property associated with the NAI Registrations, Products and any element or component proprietary to NAI included in the Products or any part thereof do not (a) infringe upon or violate any rights of any third party, or (b) constitute a violation of any applicable law, rule or regulation of any government or regulatory body, and (v) none of the actions contemplated by this Agreement will violate or constitute a default under any agreement, order, judgment, decree or instrument to which NAI is a party or by which it is bound and (vi) agrees to obtain and maintain and keep in full force and effect, at NAI's expense, Commercial General Liability insurance on an occurrence basis as mutually agreed between the Parties.

4.3.2 NAI acknowledges that (i) Linchitz exclusively owns all right, title and interest in and to the Linchitz Name, which Linchitz Name has intrinsic value, and (ii) Linchitz otherwise reserves all rights and licenses to the Linchitz Name except those specifically granted to NAI herein.

## 5. ROYALTIES

5.1 **Royalties.** NAI shall pay Linchitz a royalty on annual Net Sales revenue from Products.

5.1.1 **Annual Net Sale Royalty.** During the term of this Agreement and any renewals, the royalty due on annual Net Sales shall be:

5% of annual Net Sales not exceeding \$5,000,000;

6% of annual Net Sales in excess of \$5,000,000 but not exceeding \$10,000,000;

7% of annual Net Sales in excess of \$10,000,000 but not exceeding \$25,000,000;

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8% of annual Net Sales in excess of \$25,000,000 but not exceeding \$45,000,000;

9% of annual Net Sales in excess of \$45,000,000 but not exceeding \$75,000,000;

10% of annual Net Sales in excess of \$75,000,000.

**5.1.2 Royalty Payments.** Royalty payments shall be made monthly, on or before the 30th day of the month succeeding the close of each calendar month. Each royalty payment shall be supplemented by a report setting forth the information described in Section 5.2. All payments shall be made in United States currency and be drawn on a United States bank. NAI is not required to pay a royalty for any Product purchased by or fulfilled for Linchitz pursuant to this Agreement. There shall be applied to any amounts not subject to good faith dispute not paid when due a delinquency charge, computed at the lesser of 1.5% per month or the maximum rate permitted by law, with interest accrued from the date the payment was originally due.

**5.2 Reports and Inspection.** NAI shall deliver a report to Linchitz within thirty (30) days after the end of each calendar month, which shall consist of an accurate statement of Net Sales of Products for such calendar month, along with any royalty payments due. Such reports shall be provided regardless of whether any Products were sold during the period covered by the report. The acceptance by Linchitz of any of the statements furnished or royalties paid shall not preclude Linchitz's questioning the correctness at any time of any payments or statements. In connection therewith, Linchitz shall be entitled to examine or audit at his own expense the documents underlying the royalty statements described in this Section not more often than annually. The audit shall be conducted by an independent certified public accounting firm of Linchitz's choosing and reasonably acceptable to NAI. The independent certified public accounting firm must enter into a confidentiality agreement reasonably acceptable to NAI and may not disclose any information learned in the course of such audit other than the existence and amount of underpayment, if any. Such audit must be conducted during NAI's normal business hours in a manner that does not unduly interfere with NAI's normal business activities. If any audit discloses underpayment of royalties, NAI shall promptly pay Linchitz the royalties, which in no event shall exceed thirty days from notification of any such underpayment. Linchitz is responsible for all expenses it incurs in connection with any audit unless the audit discloses an underpayment of royalties in excess of ten percent (10%), in which case, NAI shall promptly reimburse Linchitz for the reasonable and necessary cost of the audit. Any such underpayment shall be immediately due and payable, with interest accrued from the date the payment was originally due at the lesser of 1.5% per month or the maximum rate permitted by law.

## **6. TERM OF AGREEMENT**

**6.1 Effective Date.** The term "Effective Date" shall mean, and this Agreement is effective as, of the date first written above.

### **6.2 Term and Termination.**

**6.2.1 Initial Term.** This Agreement shall remain in effect for a period of ten (10) years from the date hereof unless earlier terminated in accordance herewith. Upon expiration of the initial term, the term of this Agreement shall be automatically extended for

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successive one (1) year periods unless terminated by either Party by written notice delivered at least 90 days prior to expiration of any such period.

6.2.2 **Right to Terminate by NAI.** NAI may terminate this Agreement at any time for any reason upon giving Linchitz ninety (90) days notice.

6.3 **Right to Terminate by Linchitz.** Linchitz shall have the right to terminate this Agreement if:

6.3.1 After notice from Linchitz, NAI materially fails to comply with any covenant in this Agreement and such failure continues for more than thirty (30) days following receipt of written notice unless such failure cannot reasonably be cured within 30 days then only if NAI fails to commence such cure within thirty (30) days and diligently thereafter prosecutes such cure to completion within 90 days or other commercially reasonable time period;

6.3.2 Except as provided in Section 10.13, NAI assigns its rights to a party without first receiving the prior written consent of Linchitz;

6.3.3 NAI fails to make the royalty payments as required by Section 5 or any other payment within thirty (30) days following receipt of written notice from Linchitz of the late payment;

6.3.4 Commencing on January 1, 2009, if annual Net Sales have not reached \$5,000,000 for the immediately preceding calendar year, NAI shall have the option to retain all rights and an exclusive license under this Agreement by paying to Linchitz the difference between the royalties actually paid to Linchitz pursuant to Section 5.1.1 and the royalties that would have been due if annual Net Sales reached \$5,000,000 in the immediately preceding year. If annual Net Sales have not reached \$5,000,000 for the immediately preceding calendar year and NAI does not pay to Linchitz such difference, the Parties shall decide, within sixty (60) days of such calendar year, (i.e., on or before March 1st of such calendar year), through good faith negotiations, whether or not to continue their relationship, amend the terms of this Agreement or terminate this Agreement.

6.4 **Termination on Specific Events.** Either Party may terminate this Agreement immediately only if:

6.4.1 The other Party suspends or discontinues its business operations, makes any assignment for the benefit of its creditors, commences voluntary proceedings for liquidation in bankruptcy, admits in writing its inability to pay its debts generally as they become due or consents to the appointment of a receiver, trustee or liquidator of the other Party or of all or any material part of its property, or if there is an execution of a material portion of its assets.

6.4.2 The other Party shall commence any case, proceeding or other action under any existing or future law of any jurisdiction, domestic or foreign, relating to bankruptcy, insolvency, reorganization or relief of debtors seeking to have an order for relief entered with respect to it, or seeking to adjudicate it a bankrupt or insolvent, or seeking reorganization,

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arrangement, adjustment, winding-up, liquidation, dissolution, composition or other relief with respect to it or its debts.

6.4.3 (A) There shall be commenced against the other Party any case, proceeding or other action of a nature referred to in Section 6.4.2 above which results in the entry of an order for relief or any such adjudication or appointment or remains undismissed, undischarged, unstayed or unbonded for period of ninety (90) days; or (B) there shall be commenced against the other Party any case, proceeding or other action seeking issuance of a warrant of attachment, execution, distraint or similar process against all or any substantial part of its assets, which results in the entry of an order for any such relief which shall not have been vacated, discharged or stayed or bonded pending appeal within ninety (90) days from the entry thereof; or (C) the other Party shall take any action in furtherance of, or indicating its consent to, approval of, or acquiescence in, any of the acts set forth in clause (A) or (B) above.

6.4.4 A Party acts in a manner deemed by the other Party to be in breach of either Section 3.1.8 or Section 4.2.5 of this Agreement whereupon the other Party shall have the right to give written notice of termination of this Agreement, providing complete information regarding the claimed breach and providing a period of ten (10) calendar days in which to either completely correct the conduct deemed in violation of either Section 3.1.8 or Section 4.2.5 to the reasonable satisfaction of the Party giving notice, or prove to the reasonable satisfaction of the Party giving notice that no violation occurred.

**6.5 Duties on Termination.** Upon termination of this Agreement, copies of all records related to Linchitz shall be kept by NAI for a minimum of three (3) years. The Parties shall cooperate and utilize their good faith reasonable best efforts to prepare such final reconciliations of accounts and amounts to be provided as between them in connection with such termination. Notwithstanding any of the foregoing, the termination or expiration of this Agreement shall not release any Party of any obligation to pay any monies that became due or owing or arose out of any transaction prior to the date of termination or expiration, and all fees, charges and any balances owed to Linchitz shall become due and payable in accordance with the terms of this Agreement.

## **7. INTELLECTUAL PROPERTY; QUALITY CONTROL**

**7.1 Protection of Proprietary Components.** NAI may seek in its own name and at its own expense, and if obtained, shall maintain appropriate patent, trademark, copyright or registration protection and ownership for any element or component proprietary to NAI that is included in the Products or any part thereof.

**7.2 Ownership of Formulas, Specifications and Technical Information.** All non-public formulas, specifications and technical information related to the Products, all NAI Confidential Information and all Products (collectively, "NAI Intellectual Property") shall remain the exclusive property of NAI during and following the term of this Agreement and Linchitz disclaims all interest in such NAI Intellectual Property including without limitation any modifications or improvements made by Linchitz to NAI's Intellectual Property during the term of this Agreement. During the term of this Agreement and at anytime thereafter, Linchitz shall

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not directly or indirectly develop, manufacture or market an “equivalent product” for any form of distribution using NAI’s Intellectual Property. For the purpose of this Agreement, “equivalent product” means any product formulated by Linchitz that substantially replicates the Products as to the combination of specific ingredients, nutrients, and functional features with Linchitz’s own ingredients and/or formulations.

**7.3 Assignment Upon Termination.** Upon termination or expiration of this Agreement and expiration of the Product Sell Off Period (if any), NAI shall (i) cease and desist from all use of the Linchitz Name and any Linchitz Registrations, and (ii) certify it has destroyed any remaining Products. For purposes of this Agreement, “Product Sell Off Period” means that one hundred eighty (180) day period following termination of the Agreement or expiration of the term or any extensions of this Agreement granted by Linchitz in this subsection to NAI to sell off finished Products on a non exclusive basis through all Channels of Distribution in the Territory.

**7.4 Quality Control, Inspection Rights, Samples.** Linchitz is familiar with and will rely upon NAI’s quality control measures for the production of Products. NAI’s manufacturing facilities shall meet all requirements established by state, local or federal regulations including without limitation Good Manufacturing Practices. Linchitz and his agents shall have access to inspect NAI’s facilities at all reasonable times while Products are in process for the purpose of conducting and performing quality control audits and shall have access to the results of any such test performed by NAI or at NAI’s direction. NAI shall be notified in advance of the names of all visiting personnel or agents and their intended dates of arrival. All such inspections must be conducted during NAI’s normal business hours in a manner that does not unduly interfere with NAI’s normal business activities. NAI grants Linchitz the right to request samples of finished product in reasonable quantities from time to time. NAI is not required to pay a royalty for any Product fulfilled to Linchitz in this manner. Breach of this section shall settle in accordance with Section 6.3.1 above.

**7.5 Enforcement of Intellectual Property Rights.**

7.5.1 In the event any Party becomes aware of any claim or unauthorized use, or infringement on the Linchitz Name, Linchitz Registrations or Products during the term of this Agreement, that Party shall immediately notify the other Party of such violation and shall consult with and cooperate in any way reasonably requested by the other Party with respect to the enforcement of all intellectual property rights.

7.5.2 NAI shall, at its own cost and expense, take all action necessary to enforce its rights and license and cause any violation with respect to the Linchitz Name and Linchitz Registrations to cease and be remedied. In the event NAI fails to take all action necessary to remedy any such violation, Linchitz shall have the right to promptly take such action at his own expense. In connection with such action, the Parties shall execute all papers reasonably necessary or appropriate in the discretion of the Party taking such action in response to a violation or infringement of the Linchitz Name and Linchitz Registrations, and shall testify in any legal action whenever reasonably requested to do so by the prosecuting Party.



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7.5.3 In addition to their respective undertakings set forth in the preceding Sections, the Parties agree to render to each other all assistance reasonably requested of them in connection with the protection of the Linchitz Name and Linchitz Registrations and to make promptly available to one another information they possess or to which they have access that may be of use to the other in such protection.

7.5.4 Linchitz undertakes and agrees to maintain his existing image and public persona and will use commercially reasonable best efforts to further develop, improve and otherwise enhance his image and public persona. In no event will Linchitz knowingly take any action inconsistent with his public image or denigrate any of the Products or the Linchitz Name and Linchitz Registrations or in any way reflect negatively on the Products or the Linchitz Name and Linchitz Registrations.

## **8. CONFIDENTIALITY**

**8.1 Duty to Protect Confidential Information.** “Confidential Information” includes, but shall not be limited to, the Products, trade secrets, policies, procedures, techniques, designs, drawings, know-how, technical information, specifications, computer software, intellectual property, information and data relating to the development, research, testing, manufacturing, costs, marketing and uses of the Products and Services developed, manufactured or sold by NAI, its budgets and strategic plans, the identity and special needs of the disclosing Party’s customers for the Products and the disclosing Party’s databases and data, and all technology relating to disclosing Party’s business, systems, methods of operation, customer lists, customer information, business and financial information, solicitation leads, marketing and advertising materials, methods and manuals and forms, all of which that are non-public and pertain to the activities or operations of the disclosing Party. Confidential Information may only be used if necessary in the fulfillment of obligations of the recipient Party under this Agreement. Confidential Information shall not be used in any way which is directly or indirectly detrimental to the disclosing Party or its business.

8.1.1 Confidential Information shall be kept confidential by the receiving Party except that such Party may disclose the Confidential Information or portions thereof to those of his attorneys and agents (collectively, “Representatives”) who (i) absolutely need to know such Confidential Information and (ii) have previously agreed in writing to be bound by the terms and conditions as protective of the Confidential Information as those in this Agreement. The receiving Party agrees to be responsible for any breach of this Agreement by its Representatives.

8.1.2 All Confidential Information shall be treated by the receiving Party as secret and confidential and shall be held in trust for the disclosing Party. The receiving Party shall treat such information and take such steps to assure its continued confidentiality in like manner as it would use to protect its own trade secrets or confidential information and will not, except as required by law, disclose any such confidential information received from the disclosing Party to any third party who is not bound under a confidentiality and non-disclosure agreement.

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**8.2 Means of Protecting Confidential Information.** NAI and Linchitz agree to take reasonable steps to ensure the proprietary and confidential nature of the other's confidential information and the Linchitz Name, NAI Registrations, Linchitz Registrations and Products in which confidential information is embodied or included and to protect the same from loss or theft and agree to clearly mark such confidential information and properly indicate its proprietary nature.

**8.3 Terms of Agreement.** Except as otherwise required by law including, but not limited to, NAI's disclosure obligations in connection with the U.S. Securities Act of 1934, the Parties agree that the terms of this Agreement are proprietary and confidential, as is the existence of this Agreement. Each Party agrees to maintain the existence of this Agreement and the terms and information contained herein strictly confidential and will not disclose any such information to any person who is not a Party hereto without the prior written consent of all Parties, which consent may be granted or withheld in the absolute discretion of each Party.

**8.4 Provisions Divisible.** It is agreed by all Parties that the foregoing covenants are appropriate and reasonable in light of the nature and extent of the business conducted by the Parties and their respective relationships. It is further agreed that the covenants set forth herein are divisible in the event they are held to be invalid, unreasonable, arbitrary or against public policy. Further, it is agreed by the Parties that if any court of competent jurisdiction or authorized arbitrator makes such a determination, they may determine what time period and geographical area are reasonably necessary to protect the Parties' legitimate business interests and which are enforceable.

**8.5 Irreparable Injury.** Each Party acknowledges that damages at law will be an insufficient remedy for violation of the terms of this Section and that the other Party would suffer irreparable injury as a result of such violation. Accordingly, it is agreed upon application to a court of competent jurisdiction, the Parties may obtain injunctive relief to enforce the provisions of this Section of this Agreement, which injunctive relief shall be in addition to any other rights or remedies available to it or them.

**8.6 Extended Term of Confidentiality.** It is recognized by all Parties that due to their respective positions of confidence giving rise to access to confidential, proprietary information during the term of this Agreement, that the provisions of this Section 8 apply during the term of this Agreement and for a period of three (3) years thereafter.

## **9. CLAIMS AND INDEMNIFICATION**

**9.1 Indemnification by NAI Against Third-Party Claims.** NAI shall indemnify, defend, and hold harmless Linchitz from and against any damage, loss, expense (including reasonable attorneys' fees and costs), award, settlement, or other obligation or liability arising out of any claims, demands, actions, suits, investigations or prosecutions that may be made or instituted against Linchitz, (i) arising from any alleged or actual breach of NAI's representations and warranties contained herein, and (ii) any claims arising out of NAI's, its subsidiaries, affiliated and/or controlled companies and all sublicensees, manufacturing, development, advertising, marketing, distribution, promotion, sale or use of Products.

**9.2 Indemnification by Linchitz Against Third-Party Claims.** Linchitz shall indemnify, defend and hold harmless NAI, its subsidiaries, affiliated and/or controlled companies as well as their respective officers, directors, agents, and employees, from and against all damage, loss, expense (including reasonable attorneys' fees and costs), award, settlement, other obligation or liability, demands, actions, suits, investigations or prosecutions that may be made or instituted against them or any of them, arising out of (i) any alleged or actual breach of Linchitz's representations and warranties contained in Section 3.2 above.

**9.3 No Consequential Damages.** In no event shall either Party or any person or entity that has been involved in the creation or production of the Products be liable to the other Party for any indirect, incidental, special or consequential damages, including without limitation loss of profits, loss of data or loss of goodwill, regardless of the form of action, arising out of or in connection with this Agreement, the furnishing of, performance or use of any Products, or any portion of the Products, and any other material and/or services provided for, or performed in connection with, this Agreement or either Party's failure to perform their respective obligations to third parties, even if such party has been advised of the possibility of such damages.

**9.4** Notwithstanding anything set forth in this Agreement, no limitation of liability or exculpation or hold harmless provision apply to any liability arising out of or in connection with acts or omissions that constitute bad faith, willful misconduct, gross negligence, or intentional breach of this Agreement.

**9.5 Insurance.** NAI shall carry products liability insurance with a combined single limit of at least Ten Million Dollars (\$10,000,000). All insurance coverage required herein will provide primary coverage for all losses and damages caused by the perils or causes of loss covered thereby and any valid and collectible insurance available to Linchitz will be excess and non-contributory. NAI shall submit policies and/or certificates of insurance evidencing the above coverage upon Linchitz's written request. NAI shall name Linchitz as an additional insured under such policies. In case of NAI's failure to carry said coverage and/or furnish certificates of insurance or upon cancellation of any required insurance, Linchitz may, at his option, terminate this Agreement on 10 days notice unless NAI has obtained substitute insurance coverage before such insurance becomes canceled and provides Linchitz with satisfactory evidence thereof.

#### **MISCELLANEOUS PROVISIONS**

**10.1 Sublicense.** NAI may sublicense the rights and licenses granted pursuant to this Agreement and in any such sublicense agreement a provision shall be made so that Linchitz receives such revenue or royalty payment as provided for herein. Any sublicense granted in violation of this provision shall be void. Any sublicense granted hereunder will not release or discharge NAI from any liability or obligation hereunder and NAI is fully liable for any and all sublicensees.

**10.2 Entire Agreement; Amendment.** This Agreement contains the entire understanding between the Parties with respect to the subject matter hereof and supersedes all prior or contemporaneous written or oral negotiations and agreements between them regarding the subject matter hereof. Only a writing manually signed by all Parties or by duly authorized

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corporate officers of a Party and clearly designated as an amendment to this Agreement by an appropriate heading may amend this Agreement.

**10.3 Severability.** If any provision or portion thereof of this Agreement is determined to be invalid or unenforceable, the provision or portion shall be deemed to be severable from the remainder of this Agreement and shall not cause the invalidity or unenforceability of the remainder of this Agreement.

**10.4 No Implied Waivers.** The failure of either Party at any time to require performance by the other Party of any provision hereof shall not affect in any way the right to require such performance at any later time, nor shall the waiver by either Party of a breach of any provision hereof be taken or held to be a waiver of such provision.

**10.5 Arbitration.** Any dispute, controversy or claim arising from, out of or in connection with, or relating to, this Agreement or any breach or alleged breach of this Agreement, except allegations of violations of Federal or State securities laws, or where a party may suffer irreparable harm, will upon the request of any Party involved be submitted to any private arbitration service utilizing former judges as mediators and approved by the Parties. The dispute once submitted shall be settled by binding arbitration conducted in San Diego, California (or at any other place or under any other form of arbitration mutually acceptable to Parties involved). The single arbitrator shall follow and apply the federal rules of evidence and the applicable local federal rules of governing discovery in the arbitration. Any award rendered shall be final, binding and conclusive upon the Parties and shall be non-appealable, and a judgment thereon may be entered in the highest State or Federal court of the forum, having jurisdiction. The expenses of the arbitration shall be borne equally by the Parties to the arbitration, provided that each Party shall pay for and bear the cost of its own experts, evidence and attorneys' fees, except that in the discretion of the arbitrator, any award may include the costs, fees and expenses of a Party's attorneys.

**10.6 Governing Law.** This Agreement shall be construed and interpreted under the laws of the State of California. All disputes or controversies or questions arising under or relating to this Agreement between the Parties hereto in relation to this Agreement shall be construed and resolved under the laws of the State of California. Each Party acknowledges and waives any objection to venue for such disputes in state or federal courts sitting in San Diego, California. Any judgments upon the award entered by the arbitrator may be entered in the State or Federal Courts situated in the State of California.

**10.7 Counterparts.** This Agreement may be executed in one or more counterparts, each of which shall be deemed an original, but all of which together shall constitute one and the same instrument.

**10.8 Captions.** The captions of the sections and subsections of this Agreement are included for reference purposes only and are not intended to be a part of the Agreement or in any way to define, limited or describe the scope or intent of the particular provision to which they refer.

**10.9 Relationship of the Parties.** The terms and provisions of this agreement are intended to be a license agreement and it shall not in any respect be construed to constitute NAI or Linchitz as the agent, employee, partner or joint venturer of the other. All persons employed by any Party in connection with the manufacture, distribution, marketing, promotion and sale of the Products shall be the employees or agents of that Party and under no circumstances shall a Party's employees or agents be deemed to be employees or agents of any other Party.

**10.10 Notices.** All notices, consents, waivers and other communications under this Agreement must be in writing and will be deemed to have been duly given upon (i) delivery by hand (prepaid, with written confirmation of receipt), (ii) one day after deposit with a nationally recognized overnight delivery service (prepaid, receipt requested), or (iii) five days after deposit in the United States mail by certified delivery, postage prepaid, return receipt requested. Notices shall be sent in each case to the appropriate addresses indicated for each Party below, or to such other addresses as a Party may designate in writing by notice to the other Party:

If to NAI:

Natural Alternatives International, Inc.  
1185 Linda Vista Drive  
San Marcos, California 92078  
Attn: President

with a copy to:

Fisher Thurber LLP  
4225 Executive Square, Suite 1600  
La Jolla, California 92037  
Attention: David A. Fisher

If to Linchitz:

Richard Linchitz, M.D.  
66 Highland Road  
Glen Cove, New York 11542

with a copy to:

Collen IP  
80 South Highland Avenue  
Ossining, New York 10562  
Attn: Douglas Pulitzer

**10.10.1 Designated Contact.** If a specific contact person is designated in a provision, notice concerning the subject matter of such provision shall be directed to such person. The address, facsimile number or the name of any Party or contact person or other number may be changed by sending notice in the manner set forth above.

**10.11 Key Man Insurance.** NAI shall have the right but no obligation to apply for and purchase policies of life, health and accident insurance or disability insurance upon Linchitz in such amounts as NAI deems appropriate which life insurance as key man insurance shall designate NAI as the exclusive beneficiary. Linchitz agrees to aid NAI in procuring such insurance, including submitting to a physical examination, background test and drug test, and completing all forms required for application for any insurance policy and any other reasonable action requested by NAI in order to facilitate the issuance of such policies. NAI shall bear all costs of premiums associated with such policies.

**10.12 Incapacity or Death of Richard Linchitz.** Unless otherwise provided herein, the rights granted to NAI in this Agreement are intended to survive the incapacity or death of

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Richard Linchitz. Upon the occurrence of any such event, all actions with respect to Richard Linchitz hereunder shall be exercisable on behalf of Richard Linchitz by another person (the "Linchitz Representative") who, at the execution date of this agreement, is hereby designated by Richard Linchitz to be his wife Rita A. Linchitz.

10.12.1 If prior to the death of Linchitz, he is pronounced to be incapacitated (*i.e.*, as being incapable of managing or conducting his own business affairs due to physical or mental infirmity) by the Linchitz Representative, then the Linchitz Representative shall thereafter and for so long as Richard Linchitz is incapacitated have full right to take all acts on behalf of Richard Linchitz under this Agreement. Any Linchitz Representative appointed in accordance with this Section shall have full right to take all acts on behalf of Richard Linchitz under this Agreement and NAI may rely on such acts as the lawful and duly authorized acts of Richard Linchitz.

10.13 **Successors, Assignment.** This Agreement shall inure to the benefit of and be binding upon the successors and permitted assigns of the Parties. NAI may only assign its rights and obligations under this Agreement to its Affiliate or in connection with a merger, reorganization or sale of all or substantially all of its assets. Any assignment in violation of this clause is void ab initio. Any such assignment will not release or discharge NAI from any liability or obligation hereunder. The rights and obligations of Linchitz are personal and may not be assigned. As used herein, Affiliate shall refer to any person or entity that is under direct or indirect control of NAI. The term "control" includes without limitation, ownership of interest representing a majority of the total voting power in an entity or the ability to manage or direct such entity.

10.14 **Further Assurances.** The Parties agree (i) to furnish upon request to each other such further information, (ii) to execute and deliver to each other such other documents, and (iii) to do such other acts and things, all as the other Party may reasonably request for the purpose of carrying out the intent of this Agreement and the documents referred to in this Agreement.

10.15 **Relief.** Each Party acknowledges that damages at law will be an insufficient remedy for violation of certain terms of this Agreement and that the other Party would suffer irreparable injury as a result of such violation. Accordingly, it is agreed the Parties may obtain injunctive relief to enforce the provisions of this Agreement when a party may suffer irreparable harm, which injunctive relief shall be in addition to any other rights or remedies available to it or them.

10.16 **Remedies.** All remedies set forth in this Agreement are cumulative and in addition to and not in lieu of any other remedy of the Parties at law or in equity

*[signature page follows]*

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The Parties have executed this Exclusive License Agreement as of the Effective Date.

NATURAL ALTERNATIVES INTERNATIONAL, INC.  
a Delaware corporation

By: /s/ Randell Weaver  
Randell Weaver, President

RICHARD LINCHITZ, M.D.

By: /s/ Richard Linchitz, M.D.  
Richard Linchitz, M.D.



January 10, 2006

Real Health Laboratories, Inc.  
Jay Beltz  
1424 30<sup>th</sup> Street, #B1  
San Diego, CA 92154

Re: Option  
1424 30<sup>th</sup> St., San Diego, CA

Dear Jay:

This letter is to confirm receipt of your letter dated January 9, 2006 exercising your three (3) year option commencing May 13, 2006 and ending May 12, 2009 for the above referenced address.

Effective May 13, 2006 per the Option To Extend section of your Lease your new monthly rental amount shall be \$9,106.00.

If you have any questions, please feel free to contact me at (619) 442-9200.

Sincerely,

ECP COMMERCIAL

/s/ Michelle Anderson

Michelle Anderson  
Asst. Property Manager

8530 La Mesa Boulevard, Suite 300 • La Mesa, California 91941  
619.442.9200 • Fax.442.6157 • E-mail: [ecpcommercial@ecpcommercial.com](mailto:ecpcommercial@ecpcommercial.com)  
[www.ecpcommercial.com](http://www.ecpcommercial.com)



**FIRST AMENDMENT TO LEASE**

THIS FIRST AMENDMENT TO LEASE is made effective this 21<sup>st</sup> day of December, 2004, between Calwest Industrial Properties, LLC, ("Landlord") and Natural Alternatives International, Inc., ("Tenant").

**WITNESSETH:**

**WHEREAS**, Landlord and Tenant entered into that certain Lease dated June 12, 2003, (hereinafter collectively referred to as the "Lease");

**WHEREAS**, the premises under the Lease are located in the City of Vista, County of San Diego, State of California, commonly known as 121 1-B&C and 1215 Park Center Drive (the "Premises"); and

**WHEREAS**, Landlord and Tenant desire to amend the Lease as more fully set forth below.

**NOW, THEREFORE**, in consideration of the mutual covenants and conditions contained herein and other good and valuable consideration, the receipt and sufficiency of which is hereby acknowledged, the parties agree as follows:

1. Definitions. Unless otherwise specifically set forth herein, all capitalized terms herein shall have the same meaning as set forth in the Lease.
2. Addendum to Lease: Tenant Improvement Allowance. The completion date for Tenant's Work within the Expansion Space at 1211-B Park Center Drive as set forth in Section 12.d of Addendum to Lease shall be extended to December 31, 2005. The two (2) references to "Exhibit B" in Section 12.d of Addendum to Lease shall be changed to read "Section 12.d of Addendum to Lease."
3. Exhibit B to Lease: Tenant Improvement Allowance. The completion date for Tenant's Work within the Premises at 1215 Park Center Drive as set forth in Section 5 of Exhibit B to the Lease shall be extended to January 31, 2005.
4. Incorporation. Except as modified herein, all other terms and conditions of the Lease between the parties above described, as attached hereto, shall continue in full force and effect.
5. Limitation of Landlord's Liability. Redress for any claims against Landlord under this Amendment or under the Lease shall only be made against Landlord to the extent of Landlord's interest in the property to which the Premises are a part. The obligations of Landlord under this Amendment and the Lease shall not be personally binding on, nor shall any resort be had to the private properties of, any of its trustees or board of directors and officers, as the case may be, the general

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partners thereof or any beneficiaries, stockholders, employees or agents of Landlord, or its investment manager.

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IN WITNESS WHEREOF, Landlord and Tenant have executed this FIRST AMENDMENT TO LEASE as of the day and year first written above.

**LANDLORD:**

CALWEST INDUSTRIAL PROPERTIES, LLC,  
a California limited liability company

By: RREEF MANAGEMENT COMPANY,  
a Delaware corporation, Its Property Manager

By: /s/ Jill E. Shanahan  
Name: Jill E. Shanahan  
Title: Vice President  
Dated: 1/21/05

**TENANT:**

NATURAL ALTERNATIVES INTERNATIONAL, INC.,  
a California corporation

By: /s/ Mark A. LeDoux  
Name: Mark A. LeDoux  
Title: Chairman and Chief Executive Officer  
Dated: 12-21-04

By: /s/ Randell Weaver  
Name: Randell Weaver  
Title: President  
Dated: 12-21-04

SECOND AMENDMENT TO LEASE

THIS AMENDMENT, dated this 13<sup>th</sup> day of January, 2006, Calwest Industrial Properties, LLC, ("Landlord") and Natural Alternatives International, Inc., ("Tenant"), for the premises located in the City of Vista, County of San Diego, State of California, commonly known as 1211-B&C and 1215 Park Center Drive (the "Premises").

WITNESSETH:

WHEREAS, Landlord and Tenant entered into that certain Lease dated June 12, 2003, as amended by First Amendment to Lease dated December 21, 2004, (hereinafter collectively referred to as the "Lease"); and

WHEREAS, Landlord and Tenant desire to amend the Lease as more fully set forth below.

NOW, THEREFORE, in consideration of the mutual covenants and conditions contained herein and other good and valuable consideration, the receipt and sufficiency of which is hereby acknowledged, the parties agree as follows:

1. Definitions. Unless otherwise specifically set forth herein, all capitalized terms herein shall have the same meaning as set forth in the Lease.
2. Tenant Improvement Allowance. The completion date of the Tenant's Work for 1211-B Park Center Drive as stated in Section 12.d of Addendum to Lease shall be extended to December 31, 2006.
3. Incorporation. Except as modified herein, all other terms and conditions of the Lease between the parties above described, as attached hereto, shall continue in full force and effect.
4. Limitation of Landlord's Liability. Redress for any claims against Landlord under this Amendment or under the Lease shall only be made against Landlord to the extent of Landlord's interest in the property to which the Premises are a part. The obligations of Landlord under this Amendment and the Lease shall not be personally binding on, nor shall any resort be had to the private properties of, any of its trustees or board of directors and officers, as the case may be, the general partners thereof or any beneficiaries, stockholders, employees or agents of Landlord, or its investment manager.

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IN WITNESS WHEREOF, Landlord and Tenant have executed the Amendment as of the day and year first written above.

**LANDLORD:**

CALWEST INDUSTRIAL PROPERTIES, LLC, a California limited liability company

By: RREEF MANAGEMENT COMPANY,  
a Delaware corporation, Its Property Manager

By: /s/ Jill Shanahan  
Name: Jill E. Shanahan  
Title: Vice President  
Dated: 1/31/06

**TENANT:**

NATURAL ALTERNATIVES INTERNATONAL, INC., a California corporation

By: /s/ Randell Weaver  
Name: Randell Weaver  
Title: President  
Dated: 1/26/06

**Certification of Chief Executive Officer  
Pursuant to  
Rule 13a-14(a)/15d-14(a)**

I, Mark A. LeDoux, Chief Executive Officer of Natural Alternatives International, Inc., certify that:

1. I have reviewed this Quarterly Report on Form 10-Q of Natural Alternatives International, Inc.;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer(s) and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) for the registrant and have:
  - a) designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
  - b) evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
  - c) disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting;
5. The registrant's other certifying officer(s) and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
  - a) all significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
  - b) any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: February 14, 2006

/s/ Mark A. LeDoux  
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Mark A. LeDoux, Chief Executive Officer

**Certification of Chief Financial Officer  
Pursuant to  
Rule 13a-14(a)/15d-14(a)**

I, John R. Reaves, Chief Financial Officer of Natural Alternatives International, Inc., certify that:

1. I have reviewed this Quarterly Report on Form 10-Q of Natural Alternatives International, Inc.;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer(s) and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) for the registrant and have:
  - a) designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
  - b) evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
  - c) disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting;
5. The registrant's other certifying officer(s) and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
  - a) all significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
  - b) any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: February 14, 2006

/s/ John R. Reaves

John R. Reaves, Chief Financial Officer

**Certification**  
**Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002**  
**(Subsections (a) and (b) of Section 1350, Chapter 63 of Title 18, United States Code)**

Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 (Subsections (a) and (b) of Section 1350, Chapter 63 of Title 18, United States Code), each of the undersigned officers of Natural Alternatives International, Inc., a Delaware corporation, does hereby certify, to such officer's knowledge, that the Quarterly Report on Form 10-Q for the quarterly period ended December 31, 2005 of Natural Alternatives International, Inc. fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934 (15 U.S.C. 78m or 78o(d)) and that information contained in such report fairly presents, in all material respects, the financial condition and results of operations of Natural Alternatives International, Inc.

Date: February 14, 2006

/s/ Mark A. LeDoux  
Mark A. LeDoux, Chief Executive Officer

Date: February 14, 2006

/s/ John R. Reaves  
John R. Reaves, Chief Financial Officer

The foregoing certification is furnished solely pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 (Subsections (a) and (b) of Section 1350, Chapter 63 of Title 18, United States Code) and is not being filed as part of the Form 10-Q or as a separate disclosure document.