NATURAL HEALTH TRENDS CORP
Form 10-Q
August 14, 2009

UNITED STATES SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549
FORM 10-Q

(Mark One)

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

For the quarterly period ended June 30, 2009

OR

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

For the transition period from __________ to __________

Commission File Number: 0-26272

NATURAL HEALTH TRENDS CORP.

(Exact name of registrant as specified in its charter)

Delaware (State or other jurisdiction of incorporation or organization)	59-2705336 (I.R.S. Employer Identification No.)
2050 Diplomat Drive Dallas, Texas (Address of principal executive offices)	75234 (Zip Code)

Registrant s telephone number, including area code: (972) 241-4080

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

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

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

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

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

At August 3, 2009, the number of shares outstanding of the registrant s common stock was 10,783,709 shares.

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FORWARD-LOOKING STATEMENTS

Certain statements contained in this report constitute forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended. All statements included in this report, other than statements of historical facts, regarding our strategy, future operations, financial position, estimated revenues, projected costs, prospects, plans and objectives are forward-looking statements. When used in this report, the words believe, anticipate, intend, estimate, expect, project, could, would, predict, pursue, continue, feel and similar expressions are intended to identify forward-looking statements, although not all forward-looking statements contain these identifying words.

We cannot guarantee future results, levels of activity, performance or achievements, and you should not place reliance on our forward-looking statements. Our forward-looking statements do not reflect the potential impact of any future acquisitions, mergers, dispositions, joint ventures or strategic investments. In addition, any forward-looking statements represent our expectation only as of the date of this report and should not be relied on as representing our expectations as of any subsequent date. While we may elect to update forward-looking statements at some point in the future, we specifically disclaim any obligation to do so, even if our expectations change.

Although we believe that the expectations reflected in any of our forward-looking statements are reasonable, actual results could differ materially from those projected or assumed in any of our forward-looking statements. Our future financial condition and results of operations, as well as any forward-looking statements, are subject to change and to inherent risks and uncertainties, such as those disclosed in this report. Important factors that could cause our actual results, performance and achievements, or industry results to differ materially from forward-looking statements include the risks described under the caption Risk Factors in our most recent Annual Report on Form 10-K and in this report, which include the following:

- we may continue to experience substantial negative cash flows;
- we may need to seek additional debt or equity financing on unfavorable terms, if available at all;
- our dependence on the Hong Kong and China markets and our vulnerability to sometimes unpredictable changes in those markets;
- our ability to attract and retain distributors;
- our ability to recruit and retain key management, directors and consultants;
- our inability to directly control the marketing of our products;
- our inability to control our distributors to the same extent as if they were our own employees;
- our ability to protect or use our intellectual property rights;
- adverse publicity associated with our products, ingredients or network marketing programs, or those of similar companies;
- our ability to maintain or expand the number of our distributors or their productivity levels;
- changes to our distributor compensation plan may not be accepted;
- our failure to properly pay business taxes or customs duties, including those of China;
- risks associated with operating internationally;
- risks associated with the amount of compensation paid to distributors, which can affect our profitability;
- we face risks related to litigation;
- we rely on our suppliers product liability insurance and product liability claims could hurt our business;
- our internal controls and accounting methods may require further modification;
- we could be adversely affected if we fail to maintain an effective system of internal controls;
- risks associated with our reliance on information technology systems;
- risks associated with the extensive regulation of our business and the implications of changes in such regulations;

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- currency exchange rate fluctuations could lower our revenue and net income;
- failure of new products to gain distributor or market acceptance;
- failure of our information technology system could harm our business;
- we have a limited product line;
- our reliance on outside manufacturers;
- the intensely competitive nature of our business;
- terrorist attacks, cyber attacks, acts of war or other disasters, particularly given the scope of our international operations;
- disappointing quarterly revenue or operating results, which could adversely affect our stock price;
- our common stock is particularly subject to volatility because of the industry in which we operate;
- consequences arising if an active public trading market for our common stock does not continue;
- consequences if we fail to regain compliance with applicable Nasdaq requirements;
- failure to maintain the registration statements covering the resale of shares of common stock for certain investors will result in liquidated damages;
- the implications of the actual or anticipated conversion or exercise of our convertible securities; and
- future sales by us or our stockholders of shares of common stock could depress the market price of our common stock.

Additional factors that could cause actual results to differ materially from our forward-looking statements are set forth in this report, including under the heading Management s Discussion and Analysis of Financial Condition and Results of Operations and in our financial statements and the related notes.

Forward-looking statements in this report speak only as of the date hereof, and forward looking statements in documents incorporated by reference speak only as of the date of those documents. The Company does not undertake any obligation to update or release any revisions to any forward-looking statement or to report any events or circumstances after the date hereof or to reflect the occurrence of unanticipated events, except as required by law.

Unless otherwise noted, the terms we, our, us, Company, refer to Natural Health Trends Corp. and its subsidiaries.

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PART I FINANCIAL INFORMATION

Item 1. FINANCIAL STATEMENTS

NATURAL HEALTH TRENDS CORP.
CONSOLIDATED BALANCE SHEETS
(In Thousands, Except Share Data)

	December 31, 2008	June 30, 2009 (Unaudited)
ASSETS		
Current assets:		
Cash and cash equivalents	$ 3,491	$ 5,031
Restricted cash	340	377
Accounts receivable	71	99
Inventories, net	2,141	1,607
Other current assets	735	578
Total current assets	6,778	7,692
Property and equipment, net	1,173	1,006
Goodwill	1,764	1,764
Intangible assets, net	1,800	1,400
Restricted cash	3,646	369
Other assets	1,464	1,082
Total assets	$ 16,625	$ 13,313
LIABILITIES AND STOCKHOLDERS EQUITY		
Current liabilities:		
Accounts payable	$ 1,746	$ 2,585
Income taxes payable	187	211
Accrued distributor commissions	554	1,030
Other accrued expenses	2,456	3,007
Deferred revenue	2,841	1,065
Current portion of convertible debentures, net of discount of $2,320 and $970 at December 31, 2008 and June 30, 2009, respectively	1,534	1,863
Deferred tax liability	351	351
Other current liabilities	1,170	1,188
Total liabilities	10,839	11,300
Commitments and contingencies		
Stockholders equity:		
Natural Health Trends stockholders equity:		
Preferred stock, $0.001 par value; 5,000,000 shares authorized; 1,761,900 shares designated Series A convertible preferred stock, 138,400 shares issued and outstanding at December 31, 2008 and June 30, 2009, aggregate liquidation value of $271	124	124
	11	11

Common stock, $0.001 par value; 50,000,000 shares authorized; 10,691,582 and 10,788,714 shares issued and outstanding at December 31, 2008 and June 30, 2009, respectively				
Additional paid-in capital		79,711		80,077
Accumulated deficit		(74,853)		(78,946)
Accumulated other comprehensive income:				
Foreign currency translation adjustments		759		734
Total Natural Health Trends stockholders equity		5,752		2,000
Noncontrolling interest		34		13
Total stockholders equity		5,786		2,013
Total liabilities and stockholders equity	$	16,625	$	13,313

See accompanying notes to consolidated financial statements.

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NATURAL HEALTH TRENDS CORP.
CONSOLIDATED STATEMENTS OF OPERATIONS (UNAUDITED)
(In Thousands, Except Per Share Data)

	Three Months Ended June 30, 2008	Three Months Ended June 30, 2009	Six Months Ended June 30, 2008	Six Months Ended June 30, 2009
Net sales	$ 12,323	$ 8,472	$ 23,718	$ 18,341
Cost of sales	3,445	2,505	6,535	5,302
Gross profit	8,878	5,967	17,183	13,039
Operating expenses:				
Distributor commissions	4,600	3,322	8,597	7,101
Selling, general and administrative expenses (including stock-based compensation expense of $129 and $255 during the three months ended June 30, 2008 and 2009, respectively, and $293 and $366 during the six months ended June 30, 2008 and 2009, respectively)	4,272	3,718	8,868	7,489
Depreciation and amortization	366	338	752	668
Impairment of long-lived assets	4		28	
Total operating expenses	9,242	7,378	18,245	15,258
Loss from operations	(364)	(1,411)	(1,062)	(2,219)
Other income (expense), net:				
Gain (loss) on foreign exchange	(118)	(41)	253	(43)
Interest income	33	10	68	24
Interest expense (including amortization of debt issuance costs and accretion of debt discount of $449 and $853 during the three months ended June 30, 2008 and 2009, respectively, and $811 and $1,628 during the six months ended June 30, 2008 and 2009, respectively)	(556)	(989)	(943)	(1,855)
Other	(22)	3	(14)	14
Total other income (expense), net	(663)	(1,017)	(636)	(1,860)
Loss before income taxes	(1,027)	(2,428)	(1,698)	(4,079)
Income tax provision	(42)	79	(79)	(35)
Net loss	(1,069)	(2,349)	(1,777)	(4,114)
Plus: Net loss attributable to the noncontrolling interest				21
Net loss attributable to Natural Health Trends	(1,069)	(2,349)	(1,777)	(4,093)
Preferred stock dividends	(4)	(4)	(8)	(8)

Net loss attributable to common stockholders of Natural Health Trends	$	(1,073)	$	(2,353)	$	(1,785)	$	(4,101)
Loss per share of Natural Health Trends basic and diluted	$	(0.11)	$	(0.23)	$	(0.19)	$	(0.41)
Weighted-average number of shares outstanding		9,619		10,068		9,610		9,986

See accompanying notes to consolidated financial statements.

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NATURAL HEALTH TRENDS CORP.
CONSOLIDATED STATEMENTS OF CASH FLOWS (UNAUDITED)
(In Thousands)

	Six Months Ended June 30, 2008	Six Months Ended June 30, 2009
CASH FLOWS FROM OPERATING ACTIVITIES:		
Net loss	$ (1,777)	$ (4,114)
Adjustments to reconcile net loss to net cash used in operating activities:		
Depreciation and amortization of property and equipment	352	268
Amortization of intangibles	400	400
Amortization of debt issuance costs	138	278
Accretion of debt discount	673	1,350
Stock-based compensation	293	366
Impairment of long-lived assets	28	
Changes in assets and liabilities:		
Accounts receivable	86	(28)
Inventories, net	712	513
Other current assets	239	155
Other assets	142	87
Accounts payable	(703)	841
Income taxes payable	2	31
Accrued distributor commissions	(495)	476
Other accrued expenses	(683)	554
Deferred revenue	(892)	(1,775)
Other current liabilities	(43)	20
Net cash used in operating activities	(1,528)	(578)
CASH FLOWS FROM INVESTING ACTIVITIES:		
Purchases of property and equipment	(146)	(99)
Decrease in restricted cash	707	3,220
Net cash provided by investing activities	561	3,121
CASH FLOWS FROM FINANCING ACTIVITIES		
Proceeds from debt	145	
Payments on debt		(1,021)
Net cash provided by (used in) financing activities	145	(1,021)
Effect of exchange rates on cash and cash equivalents	(251)	18
Net increase (decrease) in cash and cash equivalents	(1,073)	1,540
CASH AND CASH EQUIVALENTS, beginning of period	6,282	3,491

CASH AND CASH EQUIVALENTS, end of period	$ 5,209	$ 5,031

See accompanying notes to consolidated financial statements.

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NATURAL HEALTH TRENDS CORP.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

1. NATURE OF OPERATIONS AND BASIS OF PRESENTATION

Nature of Operations

Natural Health Trends Corp. (the Company), a Delaware corporation, is an international direct-selling and e-commerce company headquartered in Dallas, Texas. Subsidiaries controlled by the Company sell personal care, wellness, and quality of life products under the NHT Global brand to an independent distributor network that either uses the products themselves or resells them to consumers.

Our majority-owned subsidiaries have an active physical presence in the following markets: North America; Greater China, which consists of Hong Kong, Taiwan and China; South Korea; Japan; and Europe, which consists of Italy and Slovenia. In July 2009, the Company activated an engagement with a service provider in Russia to provide storage, distribution and order processing services.

Basis of Presentation

The unaudited interim consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America for interim financial information and with the instructions to Form 10-Q and Rule 10-01 of Regulation S-X. As a result, certain information and footnote disclosures normally included in financial statements prepared in accordance with accounting principles generally accepted in the United States of America have been condensed or omitted. In the opinion of management, the accompanying unaudited interim consolidated financial statements contain all adjustments, consisting of normal recurring adjustments, considered necessary for a fair statement of the Company s financial information for the interim periods presented. The results of operations of any interim period are not necessarily indicative of the results of operations to be expected for the fiscal year. These consolidated financial statements should be read in conjunction with the consolidated financial statements and related notes included in our 2008 Annual Report on Form 10-K filed with the United States Securities and Exchange Commission (SEC) on March 23, 2009.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Principles of Consolidation

The consolidated financial statements include the accounts of the Company and all of its majority-owned subsidiaries. All significant inter-company balances and transactions have been eliminated in consolidation.

Use of Estimates

The preparation of financial statements in accordance with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and the disclosure of contingent assets and liabilities at the date of the consolidated financial statements and the reported amounts of revenues and expenses during the reported period.

The most significant accounting estimates inherent in the preparation of the Company s financial statements include estimates associated with obsolete inventory and the fair value of acquired intangible assets, including goodwill, and other long-lived assets, as well as those used in the determination of liabilities related to sales returns, distributor commissions, and income taxes. Various assumptions and other factors prompt the determination of these significant estimates. The process of determining significant estimates is fact specific and takes into account historical experience and current and expected economic conditions. The actual results may differ materially and adversely from the Company s estimates. To the extent that there are material differences between the estimates and actual results, future results of operations will be affected.

Reclassification

Certain balances have been reclassified in the prior year consolidated financial statements to conform to current year presentation.

Cash and Cash Equivalents

In April 2009, the Company reclassified non-current restricted cash in the amount of $2.9 million to cash and cash equivalents as the restrictions on the cash have been removed and the cash is made available for operations in China. The amount was previously held as part of a statutory requirement when a direct selling license application was pending. The Company has since tentatively withdrawn its last application, which has turned stale over the past year, with the intention to re-submit an updated application in the future.

Income Taxes

The Company recognizes income taxes under the liability method of accounting for income taxes. Deferred income taxes are recognized for differences between the financial reporting and tax bases of assets and liabilities at enacted statutory tax rates in effect for the years in which the differences are expected to reverse. Valuation allowances are established when necessary to reduce deferred tax assets to the amounts expected to be ultimately realized.

The Company and its subsidiaries file income tax returns in the United States, various states, and foreign jurisdictions. The Company is no longer subject to U.S. federal income tax examinations for years prior to 2005, and is no longer subject to state income tax examinations for years prior to 2004. No jurisdictions are currently examining any income tax returns of the Company or its subsidiaries.

Fair Value of Financial Instruments

The carrying amounts of the Company s cash and cash equivalents approximate fair value because of their short maturities. The carrying amount of the noncurrent restricted cash approximates fair value since, absent the restrictions, the underlying assets would be included in cash and cash equivalents.

The fair value of the Company s convertible debentures is approximately $2.8 million, which is equal to its carrying amount plus the debt discount. The convertible debentures mature on October 19, 2009, but were redeemed by the Company on August 10, 2009 (see Note 7).

Revenue Recognition

Product sales are recorded when the products are shipped and title passes to independent distributors. Product sales to distributors are made pursuant to a distributor agreement that provides for transfer of both title and risk of loss upon our delivery to the carrier that completes delivery to the distributors, which is commonly referred to as F.O.B. Shipping Point. The Company primarily receives payment by credit card at the time distributors place orders. Amounts received for unshipped product are recorded as deferred revenue. The Company s sales arrangements do not contain right of inspection or customer acceptance provisions other than general rights of return.

Actual product returns are recorded as a reduction to net sales. The Company estimates and accrues a reserve for product returns based on its return policies and historical experience.

Enrollment package revenue, including any nonrefundable set-up fees, is deferred and recognized over the term of the arrangement, generally twelve months. Enrollment packages provide distributors access to both a personalized marketing website and a business management system. No upfront costs are deferred as the amount is nominal.

Shipping charges billed to distributors are included in net sales. Costs associated with shipments are included in cost of sales.

Various taxes on the sale of products and enrollment packages to distributors are collected by the Company as an agent and remitted to the respective taxing authority. These taxes are presented on a net basis and recorded as a liability until remitted to the respective taxing authority.

Income Per Share

Basic income per share is computed by dividing net income applicable to common stockholders by the weighted-average number of common shares outstanding during the period. Diluted income per share is determined using the weighted-average number of common shares outstanding during the period, adjusted for the dilutive effect of common stock equivalents, consisting of non-vested restricted stock and shares that might be issued upon the exercise of outstanding stock options and warrants and the conversion of preferred stock and debentures.

The dilutive effect of non-vested restricted stock, stock options and warrants is reflected by application of the treasury stock method. Under the treasury stock method, the amount the employee must pay for exercising stock options, the amount of compensation cost for future service that the Company has not yet recognized, and the amount of tax benefit that would be recorded in additional paid-in capital when the award becomes deductible are assumed to be used to repurchase shares. The potential tax benefit derived from exercise of non-qualified stock options has been excluded from the treasury stock calculation as the Company is uncertain that the benefit will be realized.

In periods where losses are reported, the weighted-average number of common shares outstanding excludes common stock equivalents because their inclusion would be anti-dilutive. The following securities were not included for the time periods indicated as their effect would have been anti-dilutive:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2008	2009	2008	2009
Options to purchase common stock	55,167	37,500	70,500	42,500
Warrants to purchase common stock	6,281,310	6,281,310	6,281,310	6,281,310
Non-vested restricted stock	761,350	906,921	907,478	906,921
Convertible preferred stock	138,400	138,400	138,400	138,400
Convertible debentures	1,700,000	1,700,000	1,700,000	1,700,000

Options and warrants to purchase 27,500 and 4,785,358 shares of common stock, respectively, were outstanding at June 30, 2009. Such options expire on November 17, 2011. The warrants have expirations through April 21, 2015. The convertible debentures mature on October 19, 2009, but were redeemed by the Company on August 10, 2009 (see Note 7).

Recently Issued and Adopted Accounting Pronouncements

In September 2006, the Financial Accounting Standards Board (FASB) issued SFAS No. 157, Fair Value Measurements, which defines fair value, establishes a framework for measuring fair value in generally accepted accounting principles (GAAP), and expands disclosures about fair value measurements. SFAS No. 157 is effective for fiscal years beginning after November 15, 2007 for financial assets and liabilities, as well as for any other assets and liabilities that are carried at fair value on a recurring basis in financial statements. In February 2008, the FASB issued FASB Staff Position (FSP) No. 157-2, Effective Date of FASB Statement No. 157, which provided a one year deferral for the implementation of SFAS No. 157 for other non-financial assets and liabilities. The Company adopted SFAS No. 157 as of January 1, 2008, except as it applies to those non-financial assets and liabilities affected by the one year deferral. The partial adoption of SFAS No. 157 did not have a material impact on the Company s financial position or results of operations. In October 2008, the FASB issued FSP No. 157-3, Determining the Fair Value of a Financial Asset When the Market for That Asset Is Not Active, which clarifies the application of SFAS No. 157 as it relates to the valuation of financial assets in a market that is not active for those financial assets. FSP No. 157-3 became effective for the Company upon issuance, and had no material impact on the Company s financial position or results of operations. The application of SFAS No. 157 to the Company s non-financial assets and liabilities did not have a material impact on its financial position or results of operations.

In December 2007, the FASB issued SFAS No. 160, Noncontrolling Interests in Consolidated Financial Statements An Amendment of ARB No. 51, which establishes accounting and reporting standards for the noncontrolling interest in a subsidiary and for the deconsolidation of a subsidiary. SFAS No. 160 is effective on or after the beginning of the first annual reporting period beginning on or after December 15, 2008. On January 1, 2009, the Company adopted the provisions of SFAS No. 160 and reclassified the noncontrolling interest (formerly minority interest) from mezzanine presentation to stockholders equity on a retrospective basis. The Company also presented the noncontrolling interest in its statement of operations as net loss attributable to noncontrolling interest.

In April 2008, the FASB issued FSP No. 142-3, Determination of the Useful Life of Intangible Assets, which amends the factors that should be considered in developing renewal or extension assumptions used to determine the useful life of a recognized intangible asset under SFAS No. 142. This pronouncement requires enhanced disclosures concerning a company s treatment of costs incurred to renew or extend the term of a recognized intangible asset. FSP No. 142-3 is effective for financial statements issued for fiscal years beginning after December 15, 2008. FSP No. 142-3 was adopted on January 1, 2009 on a prospective basis and did not have a material impact on the Company s consolidated financial statements.

In May 2008, the FASB issued SFAS No. 162, The Hierarchy of Generally Accepted Accounting Principles. SFAS No. 162 identifies the sources of accounting principles and the framework for selecting the principles to be used in the preparation of financial statements of nongovernmental entities that are presented in conformity with generally accepted accounting principles in the United States. The adoption of SFAS No. 162 will have no material impact on the Company s consolidated financial position or results of operations.

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In June 2008, the FASB issued FASB Staff Position (FSP) No. EITF 03-6-1, Determining Whether Instruments Granted in Share-Based Payment Transactions Are Participating Securities. The FSP addresses whether instruments granted in share-based payment transactions are participating securities prior to vesting and, therefore, need to be included in the earnings allocation in computing earnings per share under the two-class method. This FSP is effective for financial statements issued for fiscal years beginning after December 15, 2008. The Company s adoption of this FSP did not have a material impact on earnings per share as its outstanding non-vested restricted stock awards currently do not contain nonforfeitable rights to dividends.

In June 2008, the FASB ratified the consensus on Emerging Issues Task Force (EITF) Issue 07-5, Determining whether an Instrument (or Embedded Feature) is indexed to an Entity s Own Stock. This issue addresses whether an instrument (or an embedded feature) is indexed to an entity s own stock, which is the first part of the scope exception in paragraph 11(a) of SFAS No. 133, for purposes of determining whether the instrument should be classified as an equity instrument or accounted for as a derivative instrument. The provisions of EITF Issue No. 07-5 are effective for financial statements issued for fiscal years beginning after December 15, 2008. The adoption of EITF Issue No. 07-5 did not have an impact on the Company s financial condition or results of operations.

In April 2009, the FASB issued FSP No. SFAS 107-1 and APB No. 28-1, Interim Disclosures about Fair Value of Financial Instruments. This staff position amends SFAS No. 107, Disclosures about Fair Value of Financial Instruments, to require disclosures about fair value of financial instruments for interim reporting periods as well as in annual financial statements and also amends APB Opinion No. 28, Interim Financial Reporting, to require those disclosures in summarized financial information at interim reporting periods. The Company adopted this staff position in the second quarter of 2009. The adoption did not have an impact on the Company s financial condition or results of operations.

In May 2009, the FASB issued SFAS, Subsequent Events, which provides authoritative accounting literature for a topic that was previously addressed only in the auditing literature. The guidance in SFAS No. 165 largely is similar to the current guidance in the auditing literature with some exceptions that are not intended to result in significant changes in practice. The Company adopted SFAS No. 165 in the second quarter of 2009. The Company has evaluated subsequent events through August 14, 2009, the date this quarterly report was filed.

3. SHARE-BASED COMPENSATION

Share-based compensation expense totaled approximately $129,000 and $255,000 for the three months ended June 30, 2008 and 2009, respectively, and approximately $293,000 and $366,000 for the six months ended June 30, 2008 and 2009, respectively. No tax benefits were attributed to the share-based compensation because a valuation allowance was maintained for substantially all net deferred tax assets.

The following table summarizes the Company s stock option activity:

	Shares	Wtd. Avg. Exercise Price	Wtd. Avg. Remaining Contractual Life	Aggregate Intrinsic Value[1]
Outstanding at December 31, 2008	42,500	$ 1.80		
Cancelled, forfeited or expired	(15,000)	1.80		
Outstanding at June 30, 2009	27,500	1.80	2.4	$