

 **Medifast.**  
**2014** ANNUAL  
REPORT



**BOTTOM LINE:**  
**Medifast works**



# Medifast. 2014

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## 2014: An Eventful Year

Medifast's greatest value is that its products and programs *work*. It's backed by science; developed and recommended by doctors, dietitians, and nutritionists; and supported by Health Coaches and counselors.

We have the success stories to prove it. People come to us with health concerns, with dreams of feeling and looking better, being able to fit into a special dress or a bathing suit, and we deliver.

In order to reach new people, stay competitive, and make an even bigger difference in the lives of our customers, we continue to add new products and programs to help ensure customer success. People like variety, so we added new flavors. Once they lose weight, they need to keep it off, so we added a Healthy Living Program. They want to monitor their health no matter where they may be, so we developed dashboards and trackers and forged a partnership with Fitbit®.

Losing weight and adopting a healthy lifestyle are hard work. Food and nutritional science can take you only so far. We ask our clients to push themselves, and we never stop pushing ourselves. Add everything up, and the bottom line is: Medifast works.

## LETTER TO SHAREHOLDERS



Michael C. MacDonald, *Medifast Chairman and Chief Executive Officer*

**“In 2014, we took decisive action and set future strategic direction to better position our business for long-term profitability and growth. We are confident that the strategic actions we’ve undertaken will help to drive future growth in revenue and continue to deliver increased operational efficiencies as we enhance long-term shareholder value.”**

Our goal at Medifast is to develop innovative weight management and lifestyle products, programs, and support. We work with Clients to create lasting health through our clinically proven approach, our multiple distribution channels, and tools to help people wherever they are in the journey to a healthy lifestyle.

With our focus on driving long-term profitability and delivering shareholder value, 2014 was a year of continued evolution for Medifast.

We anticipated a revenue decline in 2014 related to our Weight Control Centers’ transition to the franchise model. Additionally, Take Shape For Life revenues decreased 10% to \$206.7 million, and Medifast Direct revenues decreased 24% to \$57.2 million. However, despite a challenging market environment, we were pleased with our continued profit delivery.

Our teams worked hard all year to identify opportunities to improve the trends and then put in motion specific strategies to reinvigorate growth in these important channels. We were able to make timely adjustments to our expense base to ensure we continued to generate healthy profitability and cash flow. By year’s end, our employee base was under 600 people — down from 808 in 2013. Our manufacturing and business operations were made more sophisticated and efficient.

We introduced 43 new products and several new incremental product categories. These new categories and channel-specific products provide a more diverse offering for our customer base. We also introduced important technology, tools, and apps to help drive customer lifetime value

and to better position us for future growth in an evolving consumer marketplace.

Additionally, we introduced new BeSlim Club and Medifast Advantage programs to provide a new value-focused introductory offer along with ongoing retention benefits to members who receive automatic monthly shipment of product. We know the customers who join those programs tend to be more committed to health and weight loss and have a higher lifetime value, so we will continue to provide incentives and motivate our Health Coaches and customers to take advantage of them.

Moving to our Weight Control Centers, at the end of 2014, we completed our two-year effort to transition from corporate-owned Weight Control Centers to the more effective franchise model. With 73 franchise centers in Arizona, California, Louisiana, Maryland, Minnesota, Pennsylvania, Texas, Virginia, and Wisconsin, customers are able to receive counseling and support to effectively lose weight and gain the knowledge to help change their lifestyle.

### 2014 FINANCIAL SUMMARY

- Income from continuing operations for the fiscal year was \$21 million or \$1.65 per diluted share based on approximately 12.8 million shares outstanding, compared to \$27.1 million or \$1.96 per diluted share for the comparable period last year, based on approximately 13.8 million shares outstanding. Adjusted income from continuing operations for the fiscal year was \$24.1 million or \$1.89 per diluted share, compared to the same \$27.1 million or \$1.96 per diluted share in 2013.

- Our effective tax rate for 2014 was 33.6%, compared to 30.5% in 2013. The increase in effective tax rate for 2014 is primarily due to the tax benefits realized in 2013 related to prior years.
- Net revenue decreased 12% to \$285.3 million for the fiscal year, as compared to \$324.1 million in 2013. Take Shape For Life revenue was \$206.7 million, Medifast Direct revenue was \$57.2 million, Franchise (Medifast Weight Control Centers) revenue was \$15.4 million, and Medifast wholesale revenue was \$6 million.
- Our cash, cash equivalents, and investment securities for the fourth quarter of 2014 decreased to \$52.6 million compared to \$67.8 million on December 31, 2013. The decrease reflects the full year impact of repurchasing 1.1 million shares of stock during 2014 for approximately \$34 million. Including the recent addition to our stock buyback authorization, we have 1.2 million shares authorized for repurchase as of December 31, 2014.
- The Company's balance sheet remains strong, with stockholders' equity at \$80.5 million and working capital of \$55 million as of December 31, 2014.

## STRATEGIES THAT WORK

For 2015, we're poised to embrace the key differences and competitive advantages of direct selling and direct response, while continuing to leverage operational and cost synergies where possible. Our strategies can be summarized in three key focus areas: grow and simplify Take Shape For Life, optimize Medifast Direct response, and innovate with our products and programs.

We will focus this year on improving the Health Coach journey — from the sign-up process to just-in-time training — through leadership development. We'll be sure to provide our Coaches with the right

messaging, process, and tools to efficiently grow their businesses and attract others to replicate their experience. In close partnership with field leaders, we'll craft an easy-to-replicate approach to the business, with Health Coach sponsoring a critical measure of success. Leadership development will be imperative, and we will deliver enhanced training in 2015.

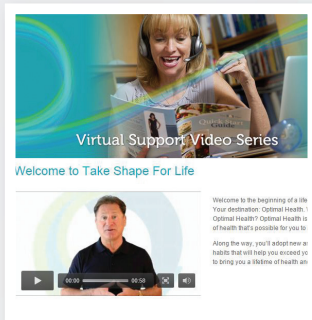
Improving conversion in Medifast Direct is our second area of focus in 2015. We will work to improve the overall customer experience, including site navigation, offer presentation, clear attribution of spending, and effective use of mobile technologies. We are actively building interest and brand awareness with our new 2015 campaign, Your Whole World Gets Better, which focuses on three inspirational Medifast successes whose worlds did, indeed, get better. The creative assets touch all mediums.

Product and program innovation is our third area of focus. After a full year of product launches, we are working on the innovation pipeline for 2016 to 2018 across the ingredients, technology, and weight wellness categories. We will capitalize on the feedback gained from consumer research and trend analysis, both of which are integral to product development and overall success. While we continue to strive for leadership in weight-loss products, the healthy living approach is equally important, and we see great opportunity for market share in this area. Our programs, too, will address weight management and healthy living, and clinical research continues to differentiate us in the marketplace.

We will execute these strategies with financial discipline and will execute our growth initiatives without significant capital investment.

We are confident that Medifast will move to even greater growth and returns in the years ahead.

## TAKE SHAPE FOR LIFE



Take Shape For Life is the direct selling division of Medifast. Our Health Coaches work closely with their Clients to guide and mentor them throughout their Optimal Health journey, including the processes of weight loss, weight management, and the establishment of lasting, healthy habits for life. Take Shape For Life continues to evolve with innovative ways to help people transform their lives. In 2014, we produced successful recognition events, a Go Global event in Austin, TX with over 900 attendees, and a National Convention in Anaheim, CA with over 3,000 Health Coaches and Clients in attendance. We created the Stop. Challenge. Choose. 12-Week Health Transformation with over 20,000 participants and celebrated our second annual Discover Your Optimal Health Day. With the goal to continue providing Health Coaches with tools to improve their businesses, we also launched a new virtual support video series and a revamped BeSlim Club rewards program.

### BOTTOM LINE:

## Take Shape For Life works



Kimberly Yost, *Certified Health Coach, Take Shape For Life*

“It’s not an overstatement to say Take Shape For Life changed the way I view health. Now I’m helping others do the same through my work as a Certified Health Coach.”

## MEDIFAST DIRECT

In Medifast Direct, customers order Medifast products directly through the Company's website, medifastnow.com, or through our in-house Client Solutions Center. A popular choice for those who prefer an independent means of achieving their weight-loss goals, Medifast Direct also offers support through an online customer community and access to discussion boards, one-on-one phone conversations with a nutrition support team member, and our vast social media properties. In 2014, we made continued improvements to our website with new, compelling content and easier navigation and introduced updates to the Medifast Advantage program, with benefits for customers who opt to receive their product order automatically each month. We continued to build our mobile capabilities for customers with the introduction of new trackers and apps.



BOTTOM LINE:

**Medifast Direct  
works**



Ruth Ann Somervell, *Happy After Winner and Medifast Direct Customer*

"I chose Medifast because it showed the fastest results and was designed by doctors, so I knew it would be a healthy way to lose weight. I decided that the best way to motivate me to stay on the program was a jump start — like the weight I lost in the first month. That was incentive enough to stick with it!"



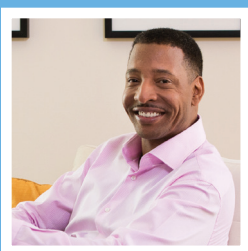
## MEDIFAST WEIGHT CONTROL CENTERS FRANCHISES

Our Medifast Weight Control Centers offer structured programs to help customers achieve weight-loss and weight-management success. Counselors work with each member to provide nutritional and behavioral support based on the member's personal needs. In 2014, we focused on the implementation of our long-term strategy and transitioned the Centers exclusively to a franchise model. In the second quarter, Medifast sold and transferred 24 corporate centers in the San Antonio, Austin, Miami, and D.C. markets to franchise owners. In December, we sold 17 more corporate centers in the Baltimore, Houston, and Dallas markets to two existing franchise owners. Finally, at the end of December 2014, Medifast closed the remaining 34 corporate centers, which left us with 73 franchise locations and eight franchise owners in nine states. We look forward to working with our franchise partners to evolve this business model for long-term success.



BOTTOM LINE:

## Medifast Weight Control Centers work



Terry Morse, *Happy After Winner and MWCC Client*

"After the first month, I was getting lots of folks stopping me in the halls asking, 'OK, what the heck are you doing to lose all the weight, and you look vibrant!' ... I always ended the conversation with: if you are serious about losing the weight, then Medifast, in my opinion, is the way to go!"



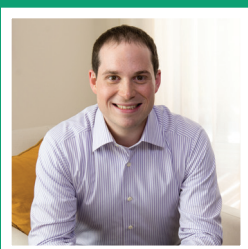
## MEDICAL PROVIDERS

Our Medical Providers are licensed healthcare providers who recommend the Medifast program through their practice and offer support to patients who use it. When we arm our Medical Providers with the very best tools and support, we put them in the position to change more lives. This year's goal was to better enable Medifast Providers to affect successful, sustainable weight loss for their patients, while diversifying and increasing the growth opportunity for their practices. In 2014, we delivered a robust content marketing program for increased practice and patient engagement, launched an on-boarding implementation program for new accounts, and developed unique and differentiated online resources for all Medical Providers.



BOTTOM LINE:

## Medifast Medical Providers work



Adam Clutter, *Customer*

“After Medifast was recommended by my doctor, I started the program, and after the first week I lost weight! That’s when I knew that I could do this, and this was going to work.”

# THE WORKS

## PRODUCT DEVELOPMENT

One of the key reasons Medifast products and programs work is that we continually add new products and programs to ensure our customers' success. To help them make smart, easy choices outside of their five meal replacements each day, we focused on expanding our product lines to include lean & green-style meals, tasty snack options, and new maintenance lines — Thrive by Medifast™ and Optimal Health by Take Shape For Life™ — to help with long-term success. The products allow Medifast to cement a reputation as a healthy living company, with products that take consumers from weight loss through the rest of their lives. To that end, Medifast launched the most new products in our company's history. Here's the complete rundown:

### MEDIFAST MEALS

- Garlic Mashed Potatoes (March)
- Sour Cream & Chive Mashed Potatoes (March)
- Gingerbread Soft Bake (October)

### FLAVORS OF HOME

- Turkey Meatball Marinara (March)
- Chicken Cacciatore (March)
- Chicken with Rice & Vegetables (March)
- Beef Stew (July)

### SLEEP (Take Shape For Life only)

- Melatonin (July)
- Chilltime Stress Relief Gum (July)
- Restfulmind™ Herbal Sleep Tea (July)
- Sleep Mask & Ear Plugs (July)
- Far-Infrared Blanket (July)
  - Sleep Kit with Blanket (July)
  - Sleep Kit without Blanket (July)

### SNACKS (July)

- Sea Salt & Olive Oil Veggie Chips
- Spicy Black Bean Veggie Chips
- Sea Salt Popcorn
- Cheddar & Sour Cream Popcorn

### THRIVE BY MEDIFAST™ AND OPTIMAL HEALTH BY TAKE SHAPE FOR LIFE™ (November)

- Salted Caramel Nut Bar
- Dark Chocolate Dream Bar
- Strawberry Yogurt Bar
- Cookies & Cream Shake
- Strawberry Banana Smoothie
- Chocolate Peanut Butter Shake
- Piña Colada Smoothie



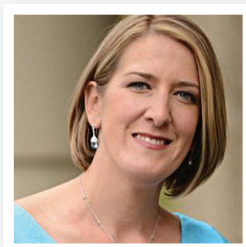
### ENERGY DROPS & INFUSERS (December)

- Lemon Energy Infuser
- Mandarin Orange Energy Infuser
- Lemonade Energy Drops
- Wild Strawberry Energy Drops
- Pineapple Mango Energy Drops

Our partnership with Fitbit® allowed us to sell trackers and scales that integrate seamlessly with our digital dashboards to help customers stay on track through heightened awareness and accountability.

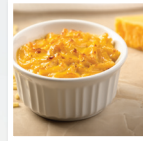
### BOTTOM LINE:

## Medifast products work



**Meg Sheetz**, *President and Chief Operating Officer, Medifast, Chief Executive Officer of Take Shape for Life*

**“Medifast has always been a healthy choice for clients who want to lose weight. Now, we can offer even more products and programs to a broader audience to help with long-term wellness. Our exclusive Optimal Health by Take Shape For Life™ products bring unique solutions to our current and future clients.”**



## NUTRITION AND WELLNESS

At the core of everything we do is our Nutrition and Wellness team. It's just one more reason we know beyond a shadow of a doubt that Medifast products and programs flat-out work. Consisting of Registered Dietitian Nutritionists, a Licensed Clinical Professional Counselor, and Registered Nurses, our Nutrition and Wellness team develops evidence-based meal plans and programs for all divisions of Medifast.



Every lean & green meal includes 5 to 7 oz of lean protein, plus three servings of vegetables and up to two servings of healthy fats, depending on your lean protein choices.

**BOTTOM LINE:**  
**Medifast**  
**nutrition works**



Jennifer Christman, RDN, LDN, *Medifast Dietitian*

“As a healthcare professional, I truly want to help educate people on proper nutrition. The key really is to meet people where they are in their personal journey. It's imperative to keep an open mind, encourage, listen, guide, and hold people accountable.”

## THE WORKS *(continued)*



### SCIENTIFIC AND CLINICAL AFFAIRS

The Scientific and Clinical Affairs Department conducts clinical research to provide scientific evidence of the efficacy of Medifast's weight-management programs and products. The department oversees the Company's Scientific Advisory Board and together with this board continually evaluates the safety and efficacy of current products and reviews the medical literature to identify new trends and the latest scientific evidence in the fields of nutrition and weight-management.

In July of 2014, Medifast announced the addition of three new members to its Scientific Advisory Board: Simon Barquera, MD, PhD, President of the Nutrition Board of Professors at the Mexican School of Public Health and Director of Research on Nutrition Policies and Programs, National Institute of Public Health; Susan Barr, PhD, RD, Professor, Food Nutrition and Health, University of British Columbia; and Steven Heymsfield, MD, Professor and Chair, Pennington Biomedical Research Center, Louisiana State University.



**Linda Arterburn PhD**, *Vice President of Scientific and Clinical Affairs of Medifast*

**"As Medifast expands its products and programs globally, it is important to elevate our international presence in the clinical and scientific community. We are honored to now have representation from Mexico and Canada on our prestigious Scientific Advisory Board."**

## OUR SCIENTIFIC ADVISORY BOARD: BUILDING ON OUR SCIENTIFIC HERITAGE

Medifast's Scientific Advisory Board is now comprised of nine medical and scientific experts in the food science, nutrition, and weight-management arena.

"The addition of these esteemed health professionals reinforces our commitment and demonstrates our dedication to evolving with medical advancements," said Michael MacDonald, Medifast Chairman and Chief Executive Officer.

The new board members join Scientific Advisory Board Chairman Lawrence Cheskin, MD, Associate Professor of Health, Behavior and Society, Johns Hopkins Bloomberg School of Public Health, and Director, Johns Hopkins Weight Management Center; and board members George Bray, MD, Boyd Professor Emeritus and Professor of Medicine Emeritus at the Pennington Biomedical Research Center, Baton Rouge, LA, John Foreyt, PhD, Professor, Department of Psychiatry and



Behavioral Sciences Department of Medicine, Baylor College of Medicine; John E. Hayes, PhD, Assistant Professor of Food Science and Director, Sensory Evaluation Center, The Pennsylvania State University; Mark Messina, PhD, President) of Nutrition Matters and Adjunct Associate Professor, Department of Nutrition, School of Public Health, Loma Linda University; and Sylvia B. Rowe, President of SR Strategy and

Adjunct Professor at Tufts Friedman School of Nutrition Science and Policy and University of Massachusetts, Amherst.

In 2014, we completed several studies and presented the results at several conferences throughout the year. Medifast also provided funding to The V Foundation for Cancer Research for a grant awarded to Dr. Parveen Bhatti, PhD, at the Fred Hutchinson Cancer Research Center in Seattle.

**BOTTOM LINE:**

**Medifast  
science works**

BOTTOM LINE:  
**Medifast works**

For the convenience of the reader, this annual report includes our annual report on Form 10-K for the year ended December 31, 2014 filed with the Securities and Exchange Commission (the “SEC”) on March 16, 2015 (the “Original Filing”) and Amendment No. 1 on Form 10-K/A to amend the Original Filing filed with the SEC on April 30, 2015 (the “Amendment”). This annual report continues to describe conditions as of the date of the Original Filing and the Amendment, respectively, and the disclosures contained herein have not been updated to reflect events, results or developments that occurred after their respective filing dates, or to modify or update those disclosures affected by subsequent events. Among other things, forward-looking statements made in those filings have not been revised to reflect events, results or developments that occurred or facts that became known to us after the date of those reports, and such forward-looking statements should be read in conjunction with our filings with the SEC after the filing of the Original Filing and the Amendment.

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

**FORM 10-K  
Amendment No. 1**

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

For the fiscal year ended December 31, 2014

or

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

For the transition period from \_\_\_\_\_ to \_\_\_\_\_.

Commission file number 001-31573

**Medifast, Inc.**

(Exact name of registrant as specified in its charter)

**Delaware**  
(State or other jurisdiction of incorporation or organization)

**13-3714405**  
(I.R.S. Employer Identification No.)

**3600 Crondall Lane, Owings Mills, Maryland 21117**  
(Address of principal executive offices) (Zip code)

**Registrant's telephone number, including area code:**  
**(410) 581-8042**

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

<u>Title of each class</u>	<u>Name of each exchange on which registered</u>
Common Stock, par value \$.001	New York Stock Exchange
Preferred Stock Purchase Rights	New York Stock Exchange

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

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act.

Yes  No

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act.

Yes  No

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

Yes  No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files).

Yes  No

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

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

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

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

Yes  No

As of June 30, 2014, the last business day of the Registrant's most recently completed second fiscal quarter, the aggregate market value of the Registrant's common stock (based on the closing sale price of \$30.41, as reported by the New York Stock Exchange on such date) held by non-affiliates was approximately \$368 million based on the closing price as reported on the New York Stock Exchange.

The number of shares of common stock outstanding as of April 28, 2015 was 12,140,069.



## CAUTIONARY STATEMENT REGARDING FORWARD-LOOKING STATEMENTS

This 2014 Annual Report on Form 10-K (“Report”) contains “forward-looking statements” within the provisions of the Private Securities Litigation Reform Act of 1995 and Section 21E of the Securities Exchange Act of 1934, as amended (the “Exchange Act”). Forward-looking statements often include words such as “may,” “will,” “should,” “anticipate,” “estimate,” “expect,” “project,” “intend,” “plan,” “believe,” “seek,” “would,” “could,” and similar words or are made in connection with discussions of future operating or financial performance.

Forward-looking statements reflect management’s expectations, beliefs, plans, objectives, goals strategies as of the date of this Report. Although we believe that these forward-looking statements and the underlying assumptions are reasonable, we cannot assure you that they will be correct. By their nature, forward-looking statements are subject to risks and uncertainties. Our actual results and financial condition may differ materially from what is anticipated in the forward-looking statements. Some of those factors (in addition to others described elsewhere in this report and in subsequent securities filings) include:

- health related claims by our customers;
- the effectiveness of our marketing and advertising programs;
- adverse publicity associated with our products or sales channels;
- the departure of one or more key personnel;
- our ability to continue to develop innovative new services and products;
- the failure of our services or products to continue to appeal to the market;
- our ability to protect our brand and other intellectual property rights;
- product liability claims;
- disruptions in our supply chain, the impact of existing and future laws and regulations, risks associated with unauthorized penetration of our information security;
- our ability to successfully make acquisitions or enter into joint ventures, including our ability to successfully integrate, operate or realize the projected benefits of such businesses; and
- overall economic and market conditions and the resultant impact on consumer spending patterns. These factors in addition to others described elsewhere in this Report, including those described under Item 1A-Risk Factors, and in subsequent filings with the Securities and Exchange Commission (the “SEC”), including those set forth in Item 1A of this Report.

Readers are cautioned not to place undue reliance on forward-looking statements, which speak only as of the date they are made, are not guarantees of future performance or results, and are subject to risks, uncertainties and assumptions that are difficult to predict or quantify. We undertake no obligation to update any information contained in this Report or to publicly release the results of any revisions to forward-looking statements to reflect events or circumstances of which we may become aware of after the date of this Report. Undue reliance should not be placed on forward-looking statements.

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## PART I

### ITEM 1. BUSINESS

#### SUMMARY

Medifast, Inc. (the “Company” or “Medifast”) is a Delaware corporation, incorporated in 1989. The Company’s fiscal year ends December 31 and all references to this year refer to the fiscal year ended December 31, 2014. The Company is engaged in the production, distribution, and sale of weight loss and weight management products and other consumable health and diet products. The Company’s operations are primarily conducted through its wholly owned subsidiaries, Jason Pharmaceuticals, Inc., Take Shape For Life, Inc., Jason Enterprises, Inc., Medifast Franchise Systems (“MFSI”), Inc., Jason Properties, LLC, Medifast Nutrition, Inc. and Seven Crondall, LLC. Medifast product lines include weight loss and management, meal replacement, and vitamins. The Company has one modern, Food and Drug Administration (“FDA”)-approved manufacturing facility located in Owings Mills, Maryland.

#### MARKETS

Over the past 30 years, obesity in the United States has risen dramatically. In 2013, the American Medical Association officially declared obesity a disease and The American Heart Association, the American College of Cardiology, and The Obesity Society recommended that obesity be managed as a chronic disease. Throughout the world, the World Health Organization estimates that approximately 1.9 billion people are overweight. In the United States, over two-thirds of the adult population fall within the overweight or obese categories. According to the Centers for Disease Control and Prevention (“CDC”), over 78 million U.S. adults are obese.

Obesity is defined as a Body Mass Index (“BMI”) of 30 kg/m<sup>2</sup> or greater, whereas overweight is defined as a BMI ranging between 25 and 29.9 kg/m<sup>2</sup>. According to the CDC in 2012, all states in the U.S. had a prevalence of obesity of at least 20%. Furthermore, the CDC reported that forty-one states had adult obesity rates of 25% or higher, and thirteen of these states had obesity rates that exceeded 30%.

According to the CDC, health conditions related to obesity include heart disease, stroke, Type 2 diabetes, and certain types of cancers. Obesity is not an age-specific condition; the CDC showed children and adolescents are also affected. According to the CDC, the prevalence of obesity in children age 6-11 years has doubled and obesity rates have quadrupled in adolescents age 12-19 years in the past 30 years. Approximately 18% of children and 21% of adolescents are obese and are at an increased risk of developing health problems such as high blood pressure, high cholesterol and prediabetes.

According to the study, “Projection of the year 2050 burden of diabetes in the US adult population: dynamic modeling of incidence, mortality, and prediabetes prevalence” published in 2010 in *Popular Health*, Type 2 diabetes is expected to increase from 1 in 10 adults to between 1 in 3 and 1 in 5 adults between 2010 and 2050.

The primary factors contributing to obesity are well-known: unhealthy food choices and lack of physical activity. Studies completed by the CDC reported Americans incurred \$147 billion in costs associated with obesity in 2008 and that average annual medical costs for those who are obese are over \$1,400 higher than those of people in normal weight ranges. The U.S. weight loss market itself is estimated to be a \$65 billion per year industry, including consumer spending on diet foods, drinks and low-calorie sweeteners; health clubs and workout videos; medically supervised and commercial weight loss programs; children’s weight loss camps; diet books; appetite suppressants and more. According to the Trust for America’s Health and The Robert Wood Johnson Foundation, assuming the current trajectory of trends, approximately half of U.S. adults would be categorized as obese by 2030. The study also estimates that there could be 7.9 million new cases of diabetes each year compared with 1.9 million new cases per year in recent years. The study also notes that there could be 6.8 million new cases of chronic heart disease and stroke per year as compared with 1.3 million new cases per year now. Also according to this study, health conditions related to obesity will result in an additional \$66 billion in obesity related medical costs as compared to recent spending estimates of \$147 billion per year.

#### DISTRIBUTION CHANNELS

**Medifast Direct** – In the direct-to-consumer channel (“Medifast Direct”), customers order Medifast product directly through the Company’s website, [www.medifastnow.com](http://www.medifastnow.com) or our in-house call center. This business is driven by a multi-media customer acquisition and retention strategy that includes both national and regional television, print, radio, digital advertising, direct mail, and email as well as public relations, word of mouth referrals, and social media initiatives. The Medifast Direct division focuses on targeted marketing initiatives to acquire and retain customers and provides support through its on-line community, MyMedifast, and its in-house call center and nutrition support team of registered dietitians to better serve its customers.

**Take Shape For Life™** – Take Shape For Life is the personal coaching division of Medifast. This physician led coaching network consists of independent contractor health coaches (“Health Coaches”), who are trained to provide coaching and support to clients on Medifast weight-loss products and programs. The role of the Health Coach is to give clients the encouragement and mentoring to assist them to successfully reach a healthy weight and adopt a healthy lifestyle. The Take Shape For Life program provides a road map to empower the individual to take control of their health through adopting better long-term habits. Take Shape For Life moves beyond the scope of weight loss to teach clients how to achieve optimal health through the balance of body, mind, and finances. Health Coaches and their clients follow the principles of the *Discover Your Optimal Health* book, *Habits of Health* book, and *Habits of Health* companion workbook written by the NY Times Best-Selling author and Take Shape For Life co-founder and medical director to create a lifelong health optimization program. In addition to the encouragement and support of a Health Coach, clients of Take Shape For Life are offered a bio-network of support including product and program information on our website, weekly medical and general support calls, and access to our registered dietitians.

Program entrants are encouraged to consult with their primary care physician and a Health Coach to determine the Medifast program that is right for them. Health Coaches are required to become qualified based upon testing of their knowledge of Medifast products and programs. Our Health Coaches provide coaching and support to their clients throughout the weight-loss and weight-maintenance process. Health Coaches are qualified based upon testing of their knowledge of Medifast products and programs. Most new Health Coaches are introduced to the opportunity by an existing Health Coach. The vast majority

of new Health Coaches started as weight-loss clients of a Health Coach, had success on the Medifast program, and became a Health Coach to help others through the weight-loss process.

Health Coaches are compensated on product sales referred to the Company. Health Coaches can earn compensation under the Integrated Compensation Plan in two ways:

- **Commissions:** The primary way a Health Coach is compensated is through earning commissions on product sold. Health Coaches earn commissions by referring product sales through their own replicated website or through the Company's in-house call center. The clients of Health Coaches are responsible for ordering and paying for products, and their order is shipped directly from the Company to the client's home or designated address. Our Health Coaches do not handle payments and are not required to purchase or store products in order to receive a commission. In addition, Health Coaches do not receive a commission on their own personal product orders. Health Coaches pay the same price for products as their clients. The Company pays retail commissions to qualified Health Coaches on a weekly basis.
- **Bonuses:** Health Coaches are offered several bonus opportunities, including client support bonuses, certification bonuses, team growth bonuses, generation bonuses, elite leadership bonuses, consistency bonuses, client acquisition bonuses, and assist bonuses. The purposes of these bonuses are to reward Health Coaches for successfully referring product sales to the Take Shape For Life network, and to incentivize Health Coaches to further support and develop other Health Coaches within their network. Health Coaches are encouraged to reach full integration at their appropriate business level (Health Coach, Business Coach, Business Leader). An Integrated Health Coach is rewarded for their higher level of performance by receiving higher earning potential for the bonuses outlined below. The Company pays bonuses on a monthly basis to qualified Health Coaches.
  - Client Support bonuses are paid to Health Coaches who have at least \$1,200 in frontline product sales to either clients or personally sponsored Health Coaches. These are incremental bonuses based on each Health Coach's frontline product sales performance.
  - Certification bonus are paid to Health Coaches who have purchased the Center for Obesity Prevention and Education (COPE) online certification course, completed the course work and passed a final examination. This bonus is earned on all frontline product sales starting in the month certification status is obtained.
  - Team growth bonuses are paid to Health Coaches who have at least five ordering clients per month and who have generated over \$1,200 in group product sales per month. Monthly growth bonuses are incremental bonuses that enable Health Coaches to earn income on product orders placed by clients and/or Health Coach teams within their network.
  - Generation bonuses are paid to Health Coaches who qualify as an "Executive Director" and have one or more Health Coaches in their business who have achieved the rank of Executive Director. An "Executive Director" is a Health Coach who has obtained five Qualifying Points. "Qualifying Points" are points earned for every \$1,200 in frontline product sales generated or every qualified Senior Coach team. A "Senior Coach" is a Health Coach who generates at least \$1,200 a month in group product sales from a combination of at least five personally enrolled, ordering clients, and/or Health Coaches, Health Coach teams, or a combination of both.
  - Elite leadership bonuses are paid to Health Coaches who qualify as an Executive Director and have three or more Health Coaches in their business who have achieved the rank of Executive Director.
  - Consistency bonuses are paid to Health Coaches who are certified and maintain frontline product sales and/or qualified Senior Coach team performance with order consistency month after month. Health Coaches who generate at least \$2,000 or more in frontline product sales for three consecutive months are paid a Health Coach consistency bonus. Certified Health Coaches who maintain at least \$6,000 in frontline product sales, at least \$15,000 in group product sales, and qualify five Senior Coach teams for three consecutive months are paid a Fully Integrated Business Coach Consistency Bonus.
  - The client acquisition bonuses are paid to new Health Coaches who develop five frontline clients and generate \$1,000 in frontline product sales within their first 30 calendar days in Take Shape For Life program.
  - The assist bonuses are paid to Health Coaches who assist a newly sponsored Health Coach attain the Client acquisition bonus.

Health Coaches do not earn a commission or bonus when they recruit a new Health Coach into the Take Shape For Life network. Fees paid by new Health Coaches for start-up materials are at the Company's approximate cost.

Take Shape For Life is a member of the Direct Selling Association (the "DSA"), a national trade association representing over 200 direct selling companies doing business in the United States. To become a member of the DSA, Take Shape For Life, like other active DSA member companies, underwent a comprehensive and rigorous one-year company review by DSA legal staff that included a detailed analysis of its company business-plan materials. This review is designed to ensure that a company's business practices do not contravene DSA's Code of Ethics. Compliance with the requirements of the Code of Ethics is paramount to becoming and remaining a member in good standing of DSA. Accordingly, we believe membership in DSA by Take Shape For Life demonstrates its commitment to the highest standards of ethics and a pledge not to engage in any deceptive, unlawful, or unethical business practices. Among those Code of Ethics proscriptions are pyramid schemes or endless chain schemes as defined by federal, state, or local laws. Moreover, Take Shape For Life, like other DSA member companies in good standing, has pledged to provide consumers with accurate and truthful information regarding the price, grade, quality, and performance of the products Take Shape For Life markets.

**Franchise Medifast Weight Control Centers** – Franchise Medifast Weight Control Centers is the brick and mortar clinic channel of Medifast. In 2014, the Company sold 41 corporate centers to existing franchise partners and closed the remaining 34 corporate centers.

In 2008, MFSI, a subsidiary of Medifast, began offering the Center model as a franchise opportunity. MFSI currently has franchised centers located in Arizona, California, Louisiana, Minnesota, Maryland, Pennsylvania, Texas, Virginia and Wisconsin. As of December 31, 2014, 73 franchise locations were in operation.

MFSI currently offers the Medifast Weight Control Center franchise opportunity in all states under a registered (where required) franchise disclosure document ("FDD"). The MFSI Franchise Agreement requires franchisees to develop a minimum of three Medifast Weight Control Centers within a defined geographic area in the time frame set forth in the Development Agreement between MFSI and the franchisee.

MFSI's franchise strategy depends on our franchisees' active involvement in, and management of, Medifast Weight Control Center operations. Candidates are reviewed for appropriate operational experience and financial stability, including specific net worth and liquidity requirements. Upon execution of the Franchise and Development Agreements, franchisees are required to promptly select sites for the Centers, each of which are subject to MFSI's approval.

A franchisee's initial fee includes the franchise fee for the first Center to be developed and a non-refundable deposit for the second and third Centers to be developed, and covers the cost of MFSI resources provided for, among other things, the training of franchisees and their staff, and approval of the proposed territory for development. If a franchisee desires to open more than three centers in the designated territory, there is an additional fee charged for each additional Center to be developed.

Prior to the opening of each Medifast Weight Control Center franchise established under the Franchise and Development Agreements, MFSI will do the following:

- i. designate the Center's protected territory.
- ii. review for approval the sites selected by the franchisee for the Center.
- iii. review for approval the lease governing the location where the Center is to be located.
- iv. provide the franchisee with standard plans and specifications for the build-out of the Center along with a list of equipment and improvements which the franchisee is required to purchase and install.
- v. provide an initial training program.
- vi. provide the franchisee on-site assistance and guidance for approximately three to five days on or about the opening of the Center.
- vii. provide the franchisee with online access to a password-protected, electronic version of the Medifast Weight Control Centers® Franchise Operations Manuals.

MFSI may, in certain limited circumstances, cause its affiliate to provide products at a discounted price. Medifast may, in certain circumstances guarantee a franchisee's notes, leases or other obligations. MFSI does not offer direct or indirect financing.

While MFSI does not currently have a purchase option included in its Franchise Agreement, it does have the right of first refusal to acquire a Center if the franchisee wishes to sell a Center.

**Medifast Wholesale** – Since 1980, over 20,000 doctors have recommended Medifast products and programs to their patients as a medically-proven solution to control their weight and improve their health. Medifast medical provider practices carry an inventory of wholesale products and resell them to patients while providing appropriate medical monitoring, testing, and support to ensure healthy weight loss.

The Company offers extensive resources to assist the providers, their staff and their patients in achieving success with their program. Medifast medical providers have access to marketing assets and training modules to help the practice grow their program and enable patients to achieve their weight loss and associated health goals. Medifast's nutrition support team includes registered dietitians and a behavioral specialist who provide program support and advice via phone and email.

In 2014, the Company began piloting an online offering that features a resource center that gives Medifast medical providers access to the most current product and program material to support their patients and their business. In addition to opening up the opportunity for our current Medifast medical providers to incorporate an e-commerce solution into their Medifast offering, they now have access to online training, news and tips from Medifast, and customizable marketing material to help them reach more patients via our wholesale healthcare channel.

In 2012, the Company entered into a 3-year strategic partnership with Medix, a leader in pharmaceutical obesity products in Mexico. The agreement granted Medix an exclusive license for the distribution of Medifast products and programs through physicians and weight control centers in Mexico under the Medifast brand. Inventory is shipped to Medix within the United States and the resulting revenues are classified as domestic sales for the Company.

In January 2013, the Company and Medix, amended their agreement to provide an exclusive 5-year licensing agreement to increase distribution of Medifast meal replacement products and programs beyond Mexico and into Argentina, Bolivia, Chile, Colombia, Costa Rica, Dominican Republic, Ecuador, El Salvador, Guatemala, Honduras, Nicaragua, Panama, Paraguay, Peru, Venezuela, and Uruguay. In September 2013, Medix held the grand opening of the first international Medifast Weight Control Center in Mexico City. Medix now has four weight control centers open in Mexico with plans to expand. In December 2013, Medix opened the first Medifast Weight Control Center in Bogota, Colombia. In March 2014, Medix acquired 13 Slim Center locations across Mexico City and Guadalajara. This acquisition gives them 12 locations in Mexico City, creating a strong geographic footprint and allows them to integrate complementary weight management brands including Medifast, Slim Center and Medix nutraceuticals. The Slim Center locations are currently selling Medifast products with plans to deploy the Medifast weight loss and maintenance programs in 2015. Including the 4 Medifast Weight Control Centers and the 13 Slim Centers, Medix now has 17 locations in operation in Mexico that offer Medifast products. The Company expects this relationship to continue to grow throughout 2015 with the focus on expanding into additional countries and further penetrating the market in established regions.

The Company also expanded its international presence into Canada in March 2014, opening new channels of distribution. Our current sales are through the Medifast Direct and Medifast medical provider channels, with the long-term goal of expanding other Medifast channels into Canada.

## SEASONALITY

The Company's weight management products and programs have historically been subject to seasonality. Traditionally the holiday season impacts the fourth quarter with fewer sales of diet control products and services. January and February generally show increases in sales, as these months are considered the commencement of the "diet season."

## THE MEDIFAST® BRAND

Medifast enriches lives by providing clinically proven weight loss, weight management, and health living products and programs. Medifast offers clinically proven products and programs for weight management, weight maintenance, healthy living and long-term health through multiple channels of distribution. Medifast products are high-quality, portion-controlled meal-replacement foods.

The Medifast Program is suitable for individuals with Type 2 diabetes and offers products with a nutritionally balanced formulation. Portion-controlled, meal-replacement weight-management programs are continuing to gain popularity, as consumers search for a safe and effective solution that provides balanced nutrition, effective weight loss, and valuable behavior-modification education.

## SCIENTIFIC ADVISORY BOARD

Medifast has a Scientific Advisory Board that consists of a multi-disciplinary, international panel that serves as the foundation for scientifically-valid, consumer-centric, high quality innovations for lasting health. Its mission is to help guide Medifast in making informed decisions regarding medical, nutritional, and scientific matters by providing expertise and information on research and emerging trends.

The work of this cross-disciplinary group builds on Medifast's heritage of medically sound approaches to weight loss, and the incorporation of leading-edge clinical research into the Company's products and programs. The Scientific Advisory Board is chaired by Lawrence Cheskin, M.D., F.A.C.P., associate professor of Health, Behavior, and Society at Johns Hopkins Bloomberg School of Public Health and director at Johns Hopkins Weight Management Center.

## COMPETITION

There are various weight loss products and programs within the highly competitive weight-loss industry. These include a wide variety of commercial weight-loss programs, pharmaceutical products, books, self-help diets, dietary supplements, appetite suppressants, and meal replacements. Medifast's identified peers and competitors in the general health and wellness diet industry include NutriSystem Inc., Herbalife Ltd., USANA Health Sciences, and Weight Watchers International, Inc. The Company believes that it competes effectively in the weight-loss industry and differentiates itself from the competition.

The Company believes its scientific and clinical heritage and ongoing commitment to evaluating its products and programs through clinical research are primary differentiators that allow it to compete in this market. Another primary differentiator is the Company's unique multi-channel distribution strategy, which provides varying support modalities, and broadens the availability of the Medifast brand by targeting a customer's individual needs. Originally developed by a physician, Medifast has been on the cutting edge in the development of nutritional and weight-management products since the Company was founded. Medifast meals are individually portioned, calorie- and carbohydrate-controlled meal replacements that share a similar nutritional "footprint" and provide a balance of protein and good carbohydrates, including fiber.

Another primary differentiator is the Company's unique multi-channel distribution strategy, which provides varying support modalities, and broadens the availability of the Medifast brand by targeting a customer's individual needs. Medifast medical providers offer Medifast products and programs to patients in their practice and utilize wholesale sales. Medifast Direct serves customers through the Medifast website and call center with a free online community, various online support tools, along with free access to registered dietitians and certified personal trainers. The Take Shape For Life division offers the personal support of a Health Coach that is often a person who has achieved success with Take Shape For Life and has turned their success into a business opportunity. Medifast Weight Control Centers offer a supervised and structured model for customers who prefer more accountability and personalized counseling including body analysis and metabolic rate reviews as part of the ongoing program. Medifast programs utilize meal replacements as part of a structured meal plan that clinical research has shown to be an effective way to lose and maintain weight loss over time.

## PRODUCTS

Originally developed by a physician, Medifast has been on the cutting edge in the development of nutritional and weight-management products since the Company was founded. The Company offers a variety of weight loss, weight management products, and healthy living products under the Medifast®, Thrive by Medifast, Optimal Health by Take Shape For Life, and Essential 1® brands and for select private label customers. The Medifast meal replacement line includes more than 70 options, including, but not limited to bars, bites, pretzels, puffs, cereal crunch, drinks, eggs, hearty choices, oatmeal, pancakes, pudding, soft serve, shakes, smoothies, soft bakes, and soups. The Thrive by Medifast and Optimal Health by Take Shape For Life lines include a variety of specially formulated bars, shakes, and smoothies for those who are maintaining their weight for long-term healthy living.

Medifast nutritional products are formulated with high-quality, low-calorie, and low-fat ingredients. Medifast meals are individually portioned, calorie- and carbohydrate-controlled meal replacements that share a similar nutritional "footprint" and provide a balance of protein and good carbohydrates, including fiber. Medifast meal replacements are also fortified to contain 24 vitamins and minerals, as well as other nutrients essential for good health.

Medifast brand awareness continues to expand through the Company's marketing campaigns, improved product quality, and an emphasis on quality customer service, technical support, and publications developed by the Company's marketing staff. Medifast products have been proven to be effective for weight loss and weight management in clinical studies conducted by researchers from leading universities. The Company has continued to develop its sales and marketing operations with qualified management and innovative programs. The Company's facility in Owings Mills, Maryland manufactures all powder based products and the Company subcontracts the production of all other products.

## **NEW PRODUCTS**

Medifast expanded its product line in 2014 by introducing the most new products in the Company's history. New introductions include meal replacements, Flavors of Home Meals, Thrive by Medifast & Optimal Healthy by Take Shape For, Flavor Infusers, Energy Drops, Snacks, Sleep & Stress, and Fitness & Tracking. Medifast identifies opportunities to expand its product line by regularly surveying its customer base and studying industry and consumer trends. This allows Medifast to introduce new, high quality products that meet consumer demand.

## **MARKETING**

In 2014, Medifast continued to build and leverage its core Medifast brand through multiple marketing strategies for each of our distinct distribution channels: Medifast Direct, Medical Wholesale, Medifast Weight Control Centers, and Take Shape For Life to their target audiences. Customer acquisition and retention strategies include national and regional advertising across television, online properties, print publications, direct mailings, email campaigns, radio, and sponsorships. In addition, the Company executed strategic public relations efforts to secure local and national editorial placements to raise brand awareness. Medifast and Take Shape For Life have also developed a comprehensive social media strategy utilizing Facebook, Twitter, YouTube, blogger endorsements, and more. These mediums were used to target new customers by stressing Medifast's simple, safe, and effective approach to weight loss and management and long term optimal health. Many of these programs were also utilized to reactivate, encourage and support existing customers and Coaches. Medifast continued to enhance all company websites and launched an entirely overhauled digital dashboard and mobile application.

## **MANUFACTURING**

Jason Pharmaceuticals, Inc., the Company's wholly owned subsidiary, manufactures and produces approximately 43% of Medifast products in their manufacturing facility in Owings Mills, Maryland. The Company purchased the plant in July 2002 and increased production capacity with additional investments in blending and packaging equipment in the past two years. The new equipment has significantly improved the Company's production capability, while also improving overall efficiencies. The raw materials utilized in the manufacturing of the Company's products are sourced from multiple suppliers within the United States. The remaining 57% of Medifast products are manufactured by third party vendors in accordance with Medifast proprietary formulas and manufacturing standards. The Owings Mills manufacturing facility is regulated and inspected by the FDA, the USDA and the Maryland State Department of Health and Mental Hygiene. It is certified as a Safe Quality Food Program (SQF) Level 2 facility compliant with the Global Food Safety Initiative.

## **GOVERNMENTAL REGULATION HISTORY**

The formulation, processing, packaging, labeling, marketing, advertising and selling of the Company's products are subject to regulation by federal, state and local agencies. Products must comply with the Federal Food Drug and Cosmetic Act, the Food Safety Modernization Act, the Federal Trade Commission Act, State Consumer Protection laws and several other federal, state and local statutes and regulations applicable in localities in which the company products are made or are sold.

The FDA and USDA and State and local Health departments are the major agencies whose regulatory mission is to assure that products are made using approved: ingredients, manufacturing procedures and testing to ensure that Safe Quality products are delivered to consumers. The Federal Trade Commission ("FTC") has principal regulatory control over the Company's advertising and trade practices, its enforcement powers are aimed at protecting the consumer from being deceived by unfair marketing and trading practices.

The Federal Trade Commission ("FTC") has principal regulatory control over the Company's advertising. To the extent that sales of foods and nutritional supplements may constitute improper trade practices or endanger the safety of consumers, the operations of the Company are subject to the regulations and enforcement powers of the FTC, and the Consumer Product Safety Commission. In 2012, a subsidiary of the Company entered into a consent decree with the FTC regarding certain statements in the Company's advertising for its weight-loss programs. See Note 8, "Contingencies".

## **PRODUCT LIABILITY AND INSURANCE**

The Company, like other producers and distributors of ingested products, faces an inherent risk of exposure to product liability claims in the event that, among other things, the use of its products results in injury. The Company maintains insurance against product liability claims with respect to the products it manufactures. With respect to the retail and direct marketing distribution of products produced by others, the Company's principal form of insurance consists of arrangements with each of its suppliers of those products to name the Company as beneficiary on each of such vendor's product liability insurance policies. The Company does not buy products from suppliers who do not maintain such coverage.

## **EMPLOYEES**

As of December 31, 2014, the Company's subsidiaries employed 579 full-time employees, of whom 213 were engaged in manufacturing, logistics, and supply chain support, and 366 in marketing, administrative, Medifast Weight Control Centers, call center and corporate support functions. None of the employees are subject to a collective bargaining agreement with the Company. All employees are employed by either Jason Pharmaceuticals, Inc. or Jason Properties, LLC.

## **INFORMATION SYSTEMS INFRASTRUCTURE**

Our websites are based on commercially developed software and are hosted at a co-location data center located in Baltimore, Maryland. This data center is SSAE16 and PCI-DSS compliant. This facility provides redundant network connections, uninterruptible power supplies, robust physical security, fire prevention controls, and diesel generated power back up for the equipment on which our websites rely. Our servers and our network are monitored 24 hours a day, seven days a week.

We use a variety of security techniques to protect our confidential customer data, including regularly scheduled penetration security tests on our websites. We also use an industry leading network monitoring service for our Intrusion Detection Services solution along with Intrusion Prevention System devices on our network's perimeter. When our customers place an order or access their account information, we use secure channels to encrypt and transmit information. Our security certificates encrypt all information entered before it is sent to our servers. We have a secondary firewall layer of security between our customer facing websites and the databases which house their information and we have deployed mitigation devices to protect against Distributed Denial of Service attacks. Customer data is protected against unauthorized access. We have a redundant network across our organization which provides for inter-connectivity and redundancy for our corporate locations.

As our operations grow in both size and scope, we will continuously improve and upgrade our information systems and infrastructure while maintaining their reliability and integrity.

## **INTELLECTUAL PROPERTY**

Products manufactured by and programs marketed by the Company are sold primarily under its own trademarks and trade names.

Our policy is to protect our products and programs through trademark registrations both in the U.S. and in significant international markets. The Company carefully monitors trademark use and promotes enforcement of its trademarks in a manner that is designed to balance the cost of such protection against obtaining the greatest value for the Company.

## **AVAILABLE INFORMATION**

Our principal office is located at 3600 Crondall Lane, Owings Mills, Maryland 21117. Our telephone number at this office is (410) 581-8042. Our corporate website is located at <http://www.medifastnow.com>. Our Annual Report on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K and amendments to reports filed or furnished pursuant to Section 13(a) and 15(d) of The Exchange Act are also available free of charge on our website, as soon as reasonably practicable after such material is filed with, or furnished to, the SEC. The information contained on our corporate website is not a part of and is not incorporated by reference in this Report.

## **CERTIFICATIONS**

The Company's Chief Executive Officer and Chief Financial Officer have filed their certifications as required by the SEC regarding the quality of the Company's public disclosure for each of the periods ended during the Company's fiscal year ended December 31, 2014 and the effectiveness of internal control over financial reporting as of December 31, 2014. Further, the Company's Chief Executive Officer has certified to the New York Stock Exchange ("NYSE") that he is not aware of any violation by the Company of the NYSE corporate governance listing standards, as required by Section 303A.12(a) of the NYSE listing standards.



**QUARTERLY RESULTS (Unaudited)**

	<u>First Quarter</u>	<u>Second Quarter</u>	<u>Third Quarter</u>	<u>Fourth Quarter</u>
<b>2014</b>				
Revenue	\$ 79,233,000	\$ 74,732,000	\$ 69,017,000	\$ 62,303,000
Gross Profit	57,924,000	55,574,000	50,734,000	44,975,000
Income from continuing operations before income taxes	9,930,000	10,094,000	7,508,000	4,161,000
Income from continuing operations	6,545,000	6,619,000	5,281,000	2,584,000
Net Income	5,967,000	5,720,000	4,855,000	(3,361,000)
Earnings per share from continuing operations- diluted	0.49	0.50	0.42	0.21
Earnings (loss) per common share- diluted	0.45	0.44	0.39	(0.28)
<b>2013</b>				
Revenue	\$ 87,007,000	\$ 88,297,000	\$ 78,477,000	\$ 70,273,000
Gross Profit	64,856,000	65,568,000	58,217,000	51,925,000
Income from continuing operations before income taxes	9,170,000	11,334,000	8,772,000	9,767,000
Income from continuing operations	6,246,000	7,381,000	6,311,000	7,197,000
Net Income	5,933,000	7,073,000	5,673,000	5,290,000
Earnings per share from continuing operations	0.45	0.53	0.45	0.53
Earnings per common share- diluted	0.43	0.51	0.41	0.39

Earnings per common share (sometimes referred to as “EPS”) is computed independently for each of the quarters presented; accordingly, the sum of the quarterly earnings per common share may not equal the total computed for the year.

**ITEM 1A. RISK FACTORS**

*In evaluating the Company, the following risk factors in addition to all other information in this Report should be considered carefully when reading this Report. If any of the events described below occurs, the Company’s business financial condition and operating results could be materially and adversely affected. Additional risks and uncertainties also may adversely affect our business and operations including those discussed in Item 7. – Management’s Discussion and Analysis of Financial Condition and Results of Operations in this Form 10-K. If any of the following events actually occur, our business and financial results could be materially adversely affected.*

**We may be subject to health related claims from our customers.**

A customer that suffers health problems may allege that the Medifast program contributed to the ailment. The Company is not currently the subject of any such claims; however, we would defend ourselves vigorously against such claims. Regardless of the ultimate outcome, such claims could reduce our brand image and customer loyalty and defending against such claims would be costly and could adversely affect our results of operations and financial condition.

**Much of our growth and future profitability depends on the effectiveness of our advertising spent in the Direct Response marketing channel.**

Our business success depends on our ability to attract and retain customers which significantly depends on our marketing practices. Our marketing expenditures may not result in increased revenue or generate sufficient awareness of the program or the brand to the consumer. We may not be able to manage our advertising expenditures in a cost effective manner which may increase the cost to acquire a new customer to an elevated level that will decrease profits.

**Adverse publicity associated with our products, ingredients, or sales channels, or those of similar companies, could harm our financial condition, operating results, and stock price.**

Adverse publicity, whether or not accurate, relating to the Company, our products or our operations, our sales channels and independent Health Coaches and franchisees could adversely impact the Company’s financial condition, operating results, and stock price. If the press were to come out with negative media about low-calorie diets, meal replacements, or soy protein this could harm our business. Even if not directed at Medifast, this perception could be instilled in our target market and cause harm to our operating results. In addition, it could lead to lawsuits or other legal challenges and could negatively impact our reputation, the market demand for our products, or our general business.

**Our lack of control over individual Health Coaches could result in claims against us.**

Our Health Coaches are independent contractors and, accordingly, we are not in a position to directly provide the same oversight as we would if Health Coaches were our own employees. As a result, there can be no assurance that our Health Coaches will participate in our marketing strategies or plans, accept our introduction of new products, or comply with our health coach policies and procedures despite our internal compliance efforts.

We can provide no assurances that the number of independent Health Coaches will increase or remain constant or that their productivity will increase. The number of active independent Health Coaches may not increase and could decline in the future. Independent Health Coaches may terminate their services at any time, and, like most direct selling companies, we experience turnover among new independent Health Coaches from year to year. We cannot accurately predict any fluctuation in the number and productivity of independent Health Coaches because we primarily rely upon existing independent Health Coaches to sponsor and train new independent Health Coaches and to motivate new and existing independent Health Coaches. Our operating results could be adversely affected if we and our existing independent Health Coaches do not generate sufficient interest in our business to successfully retain existing independent Health Coaches and attract new independent Health Coaches.

Extensive federal, state and local laws regulate our business, products and direct selling program. While we have implemented health coach policies and procedures designed to govern their conduct and to protect the trademarks and brand of the Company, it can be difficult to enforce these policies and procedures because of the large number of Health Coaches and their statuses as independent contractors. Violations by our independent Health Coaches of applicable law or of our policies and procedures in dealing with customers could reflect negatively on our products and operations and harm our business reputation. In addition, it is possible that a court could hold us civilly or criminally accountable based on vicarious liability because of the actions of our Health Coaches.

**The loss of key personnel could adversely affect our ability to operate and result in a negative financial condition.**

Certain key personnel oversee integral components of our Company. Although we do not anticipate the departure of any key employees including but not limited to the executive management team, we cannot guarantee their tenure indefinitely. Our future success depends to a significant degree on the skills, experience and efforts of our key executive officers. The loss of the services of any of these individuals could harm our business. If any of our key executive officers left the business could be harmed.

**If we do not continue to develop innovative new services and products or if our services and products do not continue to appeal to the market, our business may suffer.**

The weight management industry is subject to changing customer demands based, in large part, on the efficacy and popular appeal of weight management programs. Our future success depends on our ability to continue to develop and market new services and products and to enhance our existing services and products, each on a timely basis to respond to new and evolving customer demands, achieve market acceptance and keep pace with new nutritional and weight management developments. We may not be successful in developing, introducing on a timely basis or marketing any new or enhanced services and products, and we cannot assure you that any new or enhanced services or products will appeal to the market. Our failure to develop new services and products and to enhance our existing services and products or the failure of our services and products to continue to appeal to the market could have an adverse impact on our ability to attract and retain members and subscribers and thus adversely affect our business.

**Third parties may infringe on our brand and other intellectual property rights, which may have an adverse impact on our business**

We currently rely on a combination of trademark, copyright, trade secret, patent and other intellectual property laws and confidentiality procedures to establish and protect our proprietary rights, including our brand. If we fail to successfully enforce our intellectual property rights, the value of our brand, services and products could be diminished and our business may suffer. Our precautions may not prevent misappropriation of our intellectual property, particularly in foreign countries where laws or law enforcement practices may not protect our proprietary rights as fully as in the United States. Any legal action that we may bring to protect our brand and other intellectual property could be unsuccessful and expensive and could divert management's attention from other business concerns. In addition, legal standards relating to the validity, enforceability and scope of protection of intellectual property, especially in internet-related businesses, are uncertain and evolving. We cannot assure you that these evolving legal standards will sufficiently protect our intellectual property rights in the future.

**Our ability to compete could be negatively affected in the event we fail to protect our brand names, trademarks or other intellectual property.**

Because our business relies heavily on direct to consumer models, brand awareness is an important factor in our sales strategy. Failure to protect our brand or maintain an image of good standing with the public could result in a negative effect on our operations. Additionally, failure to protect our intellectual property could result in the arrival of a similar competitor which could reduce our competitive edge or decrease our market share.

**As a manufacturer, we may be subject to product liability claims.**

As a manufacturer and a distributor of products for human consumption and topical application, we could become exposed to product liability claims and litigation. Additionally, the manufacture and sale of these products involves the risk of injury to consumers due to tampering by unauthorized third parties or product contamination. To date, we have not been a party to any product liability litigation. We are aware of no instance in which any of our products are or have been defective in any way that could give rise to material losses or expenditures related to product liability claims. Although we maintain product liability insurance, which we believe to be adequate for our needs, there can be no assurance that we will not be subject to such claims in the future or that our insurance coverage will be adequate.

**The sale of ingested products involves product liability and other risks.**

Like other distributors of products that are ingested, we face an inherent risk of exposure to product liability claims if the use of our products results in illness or injury. The foods that we sell in the United States are subject to laws and regulations, including those administered by the FDA that establish manufacturing practices and quality standards for food products. Product liability claims could have a material adverse effect on our business as existing insurance coverage may not be adequate. The successful assertion or settlement of an uninsured claim, a significant number of insured claims or a claim exceeding the limits of our insurance coverage would harm us by adding costs to the business and by diverting the attention of senior management from the operation of the business. We may also be subject to claims that our products contain contaminants, are improperly labeled, include inadequate instructions as to use or inadequate warnings covering interactions with other substances. Product liability litigation, even if not meritorious, is very expensive and could also create adverse publicity and reduce our revenue. In addition, the products we distribute, or certain components of those products, may be subject to product recalls or other deficiencies. Any negative publicity associated with these actions would adversely affect our brand and may result in decreased product sales and, as a result, lower revenues and profits.

**A disruption in the supply of raw materials or the inability of third party manufacturing for certain products could affect operating results.**

We rely heavily on our vendors to provide quality raw materials for us to utilize in our on-site manufacturing processes. Any disruption in the availability of these materials could potentially interrupt our ability to provide certain products to customers in a timely manner. Also certain products are currently manufactured through a third party. The availability of these products is prone to fluctuations dependent on the manufacturer's ability to secure and produce a quality product that meets our standards. Our inability to secure products in a timely manner could cause loss of revenue, loss of customers, and damage to our brand.

**Disruption to the Company's supply chain could adversely affect its business.**

Damage or disruption to the Company's suppliers or to the Company's manufacturing or distribution capabilities due to weather, natural disaster, fire, terrorism, pandemic, strikes, or other reasons could impair the Company's ability to manufacture and/or sell its products. Failure to take adequate steps to mitigate the likelihood or potential impact of such events, or to effectively manage such events if they occur, particularly when a product is sourced from a single location, could adversely affect the Company's business or financial results.

**Our manufacturing activity is subject to certain risks.**

We manufacture approximately 43% of the products sold to our customers. As a result, we are dependent upon the uninterrupted and efficient operation of our manufacturing facility in Owings Mills, Maryland. Those operations are subject to power failures, the breakdown, failure, or substandard performance of equipment, the improper installation or operation of equipment, natural or other disasters, and the need to comply with the requirements or directives of government agencies, including the FDA. There can be no assurance that the occurrence of these or any other operational problems at our facility would not have a material adverse effect on our business, financial condition, or results of operations. We are subject to a variety of environmental laws relating to the storage, discharge, handling, emission, generation, manufacture, use and disposal of chemicals, solid and hazardous waste, and other toxic and hazardous materials. Our manufacturing operations presently do not result in the generation of material amounts of hazardous or toxic substances. Nevertheless, complying with new or more stringent laws or regulations, or more vigorous enforcement of current or future policies of regulatory agencies, could require substantial expenditures by us that could have a material adverse effect on our business, financial condition, or results of operations. Environmental laws and regulations require us to maintain and comply with a number of permits, authorizations, and approvals and to maintain and update training programs and safety data regarding materials used in our processes. Violations of those requirements could result in financial penalties and other enforcement actions and could require us to halt one or more portions of our operations until a violation is cured. The combined costs of curing incidents of non-compliance, resolving enforcement actions that might be initiated by government authorities, or of satisfying new legal requirements could have a material adverse effect on our business, financial condition, or results of operations.

**Our business is subject to regulatory and legislative restrictions.**

A number of laws and regulations govern our production, operation, and advertising. The FTC and certain states regulate advertising, disclosures to consumers, privacy, consumer pricing or billing arrangements, and other consumer matters. Our direct selling distribution channel is subject to risk of interpretation of certain laws pertaining to the prevention of "pyramid" or "chain sale" schemes. Although we believe we are in full compliance, should the governing body alter or enforce the law in an unanticipated way, there may be a negative result on the Company's operations. Future laws and regulations could potentially have a material negative impact on the Company. Failure to comply with any regulations of current or future authoritative entities could have a detrimental effect on the Company's financial standing or operating results.

**New or more stringent governmental regulations could adversely affect our business.**

Food production and the marketing of food products are highly regulated by a variety of federal, state, local and foreign agencies. Changes in laws or regulations, or interpretations of those laws, could result in additional regulatory requirements on us, such as the recently proposed food safety legislation that would require registration fees and mandatory product testing. These could increase our costs or restrict our marketing efforts, causing our results of operations to be adversely affected. Increased governmental interest in advertising practices may result in regulations that could require us to change or restrict our advertising practices.

Increased government regulations to limit carbon dioxide and other greenhouse gas emissions as a result of concern over climate change may result in increased compliance costs, capital expenditures and other financial obligations for us. We use natural gas, diesel fuel, and electricity in the manufacturing and distribution of our products. Legislation or regulation affecting these inputs could materially affect our profitability. In addition, climate change could affect our ability to procure commodities at reasonable costs and in quantities required. This may also necessitate unplanned capital expenditures.

Additionally, our selling practices are regulated by competition authorities in the United States and abroad. A finding that we are in violation of, or no longer in compliance with, applicable laws or regulations could subject us to civil remedies, including fines, damages, injunctions or product recalls, or criminal sanctions, any of which could adversely affect our business.

**The business may grow too quickly for the current infrastructure to handle.**

If our advertising is extremely successful and our Take Shape For Life division sees a large uptick in recruitment, we may be unable to handle the growth from an operational perspective. Increasing demands on our infrastructure could cause long hold times in the call center as well as delays on our website. In addition, there could be delays in order processing, packaging and shipping. We could run out of a majority of our inventory if growth exceeded our production capacity. If these difficulties are encountered in a period of hyper-growth then our operating results could suffer.

**We are subject to risks associated with our reliance upon information technology systems.**

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

**Any deficiencies or shortcomings in our information technology could prevent an efficient execution of routine business procedures.**

We rely heavily on our IT infrastructure to support major business components. Any disruption to the integrity of this support structure including but not limited to; software, telecommunications, Electronic Resource Platform, or the information technology architecture as a whole could severely limit our ability to provide customers and vendors with adequate service and operating responses. In addition, our financial reporting is directly correlated with our Company-wide software Microsoft Navision 4.0. Any compromise in the veracity of this system could severely alter the accuracy of our tracking, volumes, and general reporting including financial statements.

**Our business is subject to online security risks, including security breaches and identity theft.**

To succeed, online commerce and communications must provide a secure transmission of confidential information over public networks. Currently, a significant number of our customers authorize us to bill their credit cards directly for all fees charged by us. We rely on third party software products to secure our credit card transactions. Although we have developed systems and processes that are designed to protect consumer information and prevent fraudulent payment transactions and other security breaches, failure to prevent or mitigate such fraud or breaches may adversely affect our operating results.

**Our stock price may experience volatility due to fluctuations in our operating results.**

Our stock price is subject to fluctuations sometimes in response to our operating results, a competitor's operating results, other factors beyond the Company's control, or our ability to meet stock analysts forecasts and our yearly revenue and EPS guidance. In addition, general trends in the weight-loss industry as a whole can have an effect on our stock price. These factors may have an adverse affect on the market price of our stock and cause it to fluctuate significantly.

**Taxation risks could subject us to liability for past sales, increase our costs and could impact our profitability.**

The issuance by the Internal Revenue Service and/or state tax authorities of new tax regulations or changes to existing standards and actions by federal, state, or local tax agencies and judicial authorities with respect to applying applicable tax laws and regulations and the resolution of disputes with any taxing jurisdictions could subject us to liability for past sales, increase our costs and could impact our profitability.

**We may not successfully make acquisitions or enter into joint ventures and we may not successfully integrate, operate or realize the anticipated benefits of such businesses.**

As part of our growth strategy, we may pursue selected acquisitions or joint ventures. We cannot assure you that we will be able to effect these transactions on commercially reasonable terms or at all. Any future acquisitions or joint ventures may require access to additional capital, and we cannot assure you that we will have access to such capital on commercially reasonable terms or at all. Even if we enter into these transactions, we may not realize the benefits we anticipate or we may experience difficulties in integrating any acquired companies and products into our existing business, attrition of key personnel from acquired businesses, significant charges or expenses, higher costs of integration than we anticipated, or unforeseen operating difficulties that require significant financial and managerial resources that would otherwise be available for the ongoing development or expansion of our existing operations.

Our ability to influence the control of our joint ventures may be limited by contract or otherwise. In addition, we may not be able to influence the occurrence or timing of distributions from our joint ventures. If any of the other investors in a joint venture fails to observe its commitments, the joint venture may not be able to operate according to its business plan or we may be required to increase our level of commitment. The interests of our joint venture partners may differ from ours, and they may cause such entities to take actions which are not in our best interest. If we are unable to maintain our relationships with our joint venture partners, we could lose our ability to operate in the geographies and/or markets in which they operate, which could have a material adverse effect on our business, financial condition or results of operations.

Consummating these transactions could also result in the incurrence of additional debt and related interest expense, as well as unforeseen contingent liabilities, all of which could have a material adverse effect on our business, financial condition or results of operations. We may also issue additional equity in connection with these transactions, which would dilute our existing stockholders.

**The sale of our products in markets outside of the United States may subject us to risks.**

We have entered into certain arrangements for the sale of our products in international markets and we plan to expand our international sales, marketing and distribution activities on our own and through arrangements with partners located in other countries. The sale, marketing and distribution of our products and programs in such locations is subject to a number of uncertainties, including, but not limited to, the following:

- economic and political instability;
- import or export licensing requirements;
- trade restrictions;
- product registration requirements;

- longer payment cycles;
- changes in regulatory requirements and tariffs;
- fluctuations in currency exchange rates;
- potentially adverse tax consequences; and
- potentially weak protection of intellectual rights.

**New diets or pharmaceutical solutions could put us at a competitive disadvantage.**

The weight loss industry is highly subjective and influenced by many factors. For example, a low carbohydrate diet trend hit the United States several years ago and had an adverse impact on many weight loss companies, including ours. Another new diet could sweep the nation or consumer preferences could change, which is common in our industry. Our failure to adapt or respond quickly enough to these changes could have an adverse affect on our results of operations. In addition, pharmaceutical companies are constantly trying to develop safe, effective drugs that promote weight loss. If successful, many dieters could perceive this to be easier than the Medifast program, which would put us at a competitive disadvantage.

**Our results of operations may decline as a result of a downturn in general economic conditions or consumer confidence.**

Our results of operations are highly dependent on product sales and program fees. A downturn in general economic conditions or consumer confidence and spending in any of our major markets could result in people curtailing their discretionary spending, which, in turn, could lead to a decrease in product sales in our Medifast Direct and Take Shape For Life divisions and a decrease in product and program fees at our Medifast Weight Control Centers. Any such reduction would adversely affect our results of operations.

**A competitor or new entrant into the market may develop a product and program similar to or more effective or more favorably perceived than ours.**

The weight loss industry is highly competitive. We compete with a wide variety of commercial weight loss programs, pharmaceutical products, weight loss books, self-help diets, supplements and meal replacements. Many of our competitors are significantly larger than us and have more financial resources to develop new products and programs. Our business could be affected if one of our competitors or a new entrant to the market develops similar products and programs through similar marketing channels or more effective or more favorably perceived products. This could result in lower sales as well as pricing competition which could adversely affect the Company's results from operations.

**ITEM 1B. UNRESOLVED STAFF COMMENTS**

None

**ITEM 2. DESCRIPTION OF PROPERTY**

In Owings Mills, Maryland, the Company owns a 49,000 square-foot manufacturing facility and leases two buildings which serve as corporate headquarters which are set to expire on August 31, 2016 and October 31, 2017. The Company owns a 119,000 square-foot distribution facility in Ridgley, Maryland and leases a second distribution center in Dallas, Texas which includes a call center, and is set to expire on March 31, 2018. Both distribution facilities give the Company adequate product distribution capacity for the foreseeable future. The Company owns a 3,000 square-foot conference and training facility in Ocean City, Maryland. The Company leases a raw materials warehouse in Arbutus, Maryland that expires in May 2018. The Company also has 77 leases for what were its corporate owned Medifast Weight Control Centers throughout eight states; Texas, Florida, Maryland, Pennsylvania, Delaware, New Jersey, North Carolina and Virginia. The 77 leases include 3 agreements for centers that were closed in December 2013 and 34 agreements for centers that were closed in December 2014 that the Company is in the process of negotiating lease terminations or sublease arrangements, if possible. The remaining 40 agreements are for centers that were sold to franchise partners during 2014 and the Company entered into sublease agreements with the franchisees. All corporate leases range in terms from one to ten years.

**ITEM 3. LEGAL PROCEEDINGS**

The Company filed a civil complaint on February 17, 2010 in the U.S. District Court (SD, Cal) against Barry Minkow and the Fraud Discovery Institute, Inc. (collectively, "Minkow"), iBusiness Reporting, and its editor William Lobdell, Tracy Coenen and Sequence, Inc. (collectively, "Coenen"), "Zee Yourself", and Robert L. Fitzpatrick ("FitzPatrick") for defamation, market manipulation and unfair business practices, alleging a scheme of market manipulation of Medifast stock for Defendants' for monetary gain, and damaging the business reputation of Medifast and its Take Shape For Life division. Bradley T. MacDonald, former Executive Chairman of Medifast and a stockholder, joined the lawsuit individually. The lawsuit seeks \$270 million in compensatory damages, punitive damages, and ancillary relief. In March 2011, the District Court granted in part and denied in part certain Anti-SLAPP Motions to Strike (i.e. motions to dismiss) previously filed by all Defendants. The Company appealed that portion of the District Court's ruling which dismissed its defamation claims against Minkow and Coenen in the 9th Circuit Court of Appeals. Defendant FitzPatrick's motion was denied as to the Company's defamation claim, and FitzPatrick appealed that portion of the Court's ruling. On June 4, 2014, the Panel of the 9th Circuit Court of Appeals issued a decision, denying FitzPatrick's appeal and remanding to the District Court for further consideration; reversing the District Court's decision as to Minkow and remanding for further consideration; denying MacDonald's appeal in its entirety; and denying Medifast's appeal as to Coenen. On September 26, 2014, the District Court obtained jurisdiction of the case once again and the parties set a briefing schedule on the outstanding issues remanded by the Ninth Circuit. Coenen filed a motion for attorneys' fees, which Medifast has opposed. That motion is now fully-briefed and currently remains sub judice. Medifast has been engaged in settlement discussions with Minkow and FitzPatrick. There is a status conference with the District Court scheduled for March 20, 2015.

Medifast entered into a number of Franchise Agreements with Team Wellness, Inc. and Team Wellness Louisiana, LLC for the operation of Medifast centers in the States of Alabama, Tennessee, and Louisiana. The primary owner and representative of the Team Wellness companies personally guaranteed the companies' obligations.

Team Wellness, Inc. failed to make payments required under the terms of a Loan Agreement that Team Wellness, Inc. had entered into with Bank of America and for which Medifast provided a limited guarantee. As a result, Medifast served Team Wellness, Inc. with a Notice of Default and Opportunity to Cure. After Team Wellness, Inc. failed to cure and pay the outstanding amounts, Medifast served Team Wellness, Inc. with a Notice of Termination.

When the companies and the guarantor failed to pay the monies owed or comply with their post-termination obligations, Medifast filed a lawsuit against the guarantor and the companies in the United States Federal Court for the District of Maryland. The complaint seeks damages, enforcement of the termination of the Franchise Agreements, and an injunction ordering the defendants to comply with their post-termination obligations under the Franchise Agreements. The matter is in its initial stages.

In addition to the above matter, the Company is, from time to time, subject to a variety of litigation and similar proceedings incidental to its business. Based upon the Company's experience, current information and applicable law, it does not believe that these proceedings and claims will have a material adverse effect on its results of operations, financial position or liquidity.

**ITEM 4. MINE SAFETY DISCLOSURES**

Not applicable

## PART II

### ITEM 5. MARKET FOR COMMON EQUITY AND RELATED STOCKHOLDER MATTERS.

The Company's common stock is quoted under the symbol MED. The common stock is traded on the New York Stock Exchange. The following is a list of the low and high closing prices by fiscal quarters for 2014 and 2013:

	2014	
	Low	High
Quarter Ended March 31, 2014	24.23	29.57
Quarter Ended June 30, 2014	28.88	34.08
Quarter Ended September 30, 2014	26.15	34.98
Quarter Ended December 31, 2014	29.39	33.79

	2013	
	Low	High
Quarter Ended March 31, 2013	22.26	28.10
Quarter Ended June 30, 2013	22.23	29.32
Quarter Ended September 30, 2013	24.85	28.88
Quarter Ended December 31, 2013	23.31	27.49

#### Holders

There were approximately 125 record holders of the common stock as of March 9, 2015. This number does not include beneficial owners of our securities held in the name of nominees.

#### Dividends

No dividends on common stock were declared by the Company during 2014 or 2013. The Company has not and does not plan to declare dividends in the foreseeable future.

The Bank of America revolving unsecured line of credit contains customary covenants including covenants that, in certain circumstances, restrict the Company's ability to incur additional indebtedness, pay dividends on and redeem capital stock, make other payments, including investments, sell its assets and enter into consolidations, mergers and transfers of all or substantially all of its assets.

#### Stock Repurchase Program

At the outset of the quarter ended December 31, 2014, there were 1,211,908 shares of the Company's common stock eligible for repurchase under the repurchase authorization dated September 16, 2014.

No repurchases were made during the fourth quarter of 2014.

#### Stockholders' Rights Plan

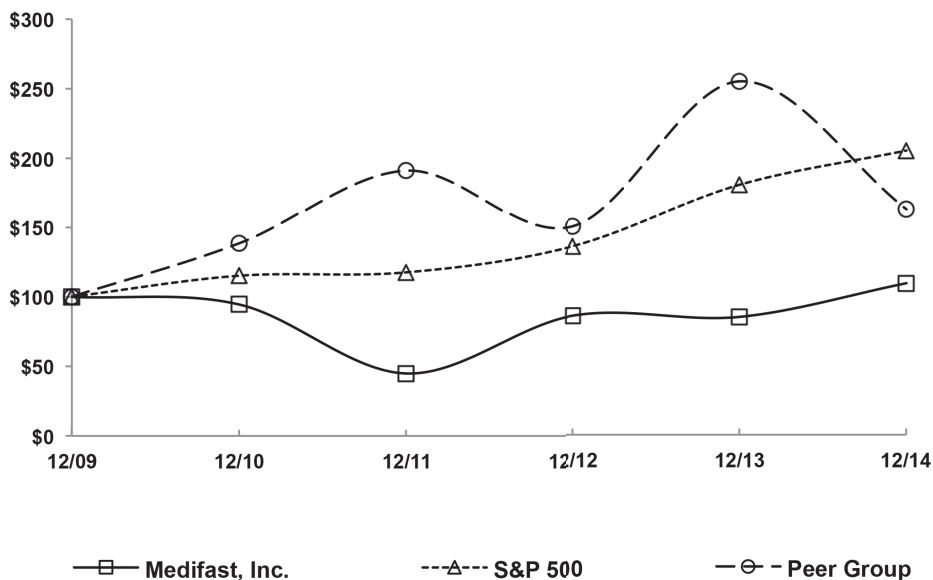
On August 28, 2014, the Company adopted a stockholders' rights plan whereby the Board of Directors authorized and declared a dividend distribution of one right for each outstanding share of common stock of the Company to the stockholders of record at the close of business on September 9, 2014. The rights are not presently exercisable and remain attached to the shares of common stock until the occurrence of certain triggering events. The rights will expire on August 28, 2015, unless exercised, redeemed, or exchanged prior to that time. The Board of Directors may terminate the rights plan before the expiration date.

**Performance Graph**

The following graph compares the Company’s cumulative total stockholder return (Common Stock price appreciation plus dividends, on a reinvested basis) over the last five fiscal years with the Standard & Poor’s S&P 500 Index and the Company’s selected peer group, including NutriSystem Inc., Herbalife Ltd., USANA Health Sciences, and Weight Watchers International, Inc.

**COMPARISON OF 5 YEAR CUMULATIVE TOTAL RETURN\***

Among Medifast, Inc., the S&P 500 Index, and a Peer Group



\*\$100 invested on 12/31/09 in stock or index, including reinvestment of dividends. Fiscal year ending December 31.

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	<u>12/09</u>	<u>12/10</u>	<u>12/11</u>	<u>12/12</u>	<u>12/13</u>	<u>12/14</u>
<b>Medifast, Inc.</b>	<b>100.00</b>	<b>94.44</b>	<b>44.87</b>	<b>86.30</b>	<b>85.45</b>	<b>109.71</b>
<b>S&amp;P 500</b>	<b>100.00</b>	<b>115.06</b>	<b>117.49</b>	<b>136.30</b>	<b>180.44</b>	<b>205.14</b>
<b>Peer Group</b>	<b>100.00</b>	<b>138.33</b>	<b>191.27</b>	<b>150.62</b>	<b>254.91</b>	<b>162.84</b>



## ITEM 6. SELECTED FINANCIAL DATA

The selected condensed consolidated financial data set forth below should be read in conjunction with “Management’s Discussion and Analysis of Financial Condition and Results of Operations” included in Part II, Item 7 of this Report, and the consolidated financial statements and notes thereto of the Company included in Part II, Item 8 of this Report. The historical results provided below are not necessarily indicative of future results.

	<u>2014</u>	<u>2013</u>	<u>2012</u>	<u>2011</u>	<u>2010</u>
(In thousands, except per share data)					
Revenue	\$ 285,285	\$ 324,054	\$ 318,571	\$ 272,467	\$ 239,440
Income from Operations	30,246	38,410	27,140	33,768	28,881
Income from Continuing Operations before Income Taxes	31,693	39,043	28,356	34,067	28,933
Basic EPS from continuing operations	\$ 1.66	\$ 1.97	\$ 1.34	\$ 1.63	\$ 1.28
Basic EPS	1.04	1.74	1.16	1.33	1.39
Diluted EPS from continuing operations	1.65	1.96	1.34	1.60	1.23
Diluted EPS	1.03	1.73	1.16	1.31	1.35
Total Assets	\$ 115,910	\$ 132,650	\$ 130,251	\$ 105,665	\$ 94,059
Current Portion of long-term debt and capital lease facilities	232	222	528	1,426	944
Total long-term debt and capital leases	242	474	3,809	4,251	4,855
Weighted average shares outstanding					
Basic	12,670	13,774	13,722	13,965	14,082
Diluted	12,778	13,818	13,740	14,198	14,573

## ITEM 7. MANAGEMENT’S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS.

### CRITICAL ACCOUNTING POLICIES AND ESTIMATES

Our consolidated financial statements are prepared in accordance with U.S. generally accepted accounting principles (“GAAP”). Our significant accounting policies are described in Note 2 to the consolidated financial statements.

The preparation of these financial statements requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities at the date of the financial statements, and the reported amounts of revenue and expenses during the reporting period. Management develops, and changes periodically, these estimates and assumptions based on historical experience and on various other factors that are believed to be reasonable under the circumstances. Actual results may differ from these estimates under different assumptions or conditions. Management considers the following accounting policies to be the most critical in preparing our consolidated financial statements. These critical accounting policies have been discussed with our Audit Committee, as appropriate.

**Revenue Recognition:** Revenue is recognized net of discounts, rebates, promotional adjustments, price adjustments, and estimated returns and upon transfer of title and risk to the customer which occurs at shipping (F.O.B. terms). Upon shipment, the Company has no further performance obligations and collection is reasonably assured as the majority of sales are paid for prior to shipping. Medifast Weight Control Centers’ program fees are recognized over the estimated service period.

**Impairment of Fixed Assets and Intangible Assets:** We continually assess the impairment of long-lived assets whenever events or changes in circumstances indicate that the carrying value of the assets may not be recoverable. Judgments regarding the existence of impairment indicators are based on legal factors, market conditions and our operating performance. Future events could cause us to conclude that impairment indicators exist and the carrying values of fixed and intangible assets may be impaired. Any resulting impairment loss would be limited to the value of net fixed and intangible assets.

**Income Taxes:** The benefit of a tax position is recognized in the financial statements in the period during which, based on all available evidence, management believes it is more-likely-than-not that the position will be sustained upon examination, including the resolution of appeals or litigation processes, if any. Tax positions taken are not offset or aggregated with other positions. Tax positions that meet the more-likely-than-not recognition threshold are measured as the largest amount of tax benefit that is more than 50 percent likely of being realized upon settlement with the applicable taxing authority. The portion of the benefits associated with tax positions taken that exceeds the amount measured as described above is reflected as a liability for unrecognized tax benefits in the accompanying balance sheet along with any associated interest and penalties that would be payable to the taxing authorities upon examination.

We evaluated our tax positions and determined that we did not have any material uncertain tax positions requiring recognition of a liability. Our policy is to recognize interest and penalties accrued on uncertain tax positions as part of income tax expense. For the twelve months ended December 31, 2014 and 2013, no material estimated interest or penalties were recognized for the uncertainty of certain tax positions. We file income tax returns in the United States and various states jurisdictions. With few exceptions, we are no longer subject to U.S. federal, state and local income tax examinations by tax authorities for the years before 2010.

**Reserves for Returns:** We review the reserves for customer returns at each reporting period and adjust them to reflect data available at that time. To estimate reserves for returns, we consider actual return rates in preceding periods. To the extent the estimate of returns changes, we will adjust the reserve, which will impact the amount of product sales revenue recognized in the period of the adjustment. Our estimates for returns have not differed materially from our actual returns. The provision for estimated returns as of December 31, 2014 and 2013 were \$290,000 and \$525,000, respectively.

Operating leases: Medifast leases retail stores, distribution facilities, and office space under operating leases. Many lease agreements contain tenant improvement allowances, rent holidays, rent escalation clauses and contingent rent provisions. The Company recognizes incentives and minimum rental expenses on a straight-line basis over the terms of the leases. We commence recording rent expense on the date of initial possession, which is generally when we enter the space and begin to make improvements to properties for our intended use. For tenant improvement allowances and rent holidays, we record a deferred rent liability on the consolidated balance sheets and amortize the deferred rent over the terms of the leases as reductions to rent expense on the consolidated statements of income.

For scheduled rent escalation clauses during the lease terms or for rental payments commencing at a date other than the date of initial occupancy, we record minimum rental expenses on a straight-line basis over the terms of the leases on the consolidated statements of income. Several leases provide for contingent rents, which are determined as a percentage of gross sales in excess of specified levels. We record a contingent rent liability on the consolidated balance sheets and the corresponding rent expense when we determine achieving specified levels is probable.

**BACKGROUND:**

The Company is engaged in the production, distribution, and sale of weight loss and weight management products and other consumable health and diet products. The Company's product lines include weight loss and weight management, meal replacements, and vitamins. Our product sales accounted for 98% of our revenues in 2014 and 2013. Shipping revenue and other accounted for 2% of revenue in 2014 and 2013.

We review and analyze a number of key operating and financial metrics to manage our business, including revenue to advertising spend and the number of active Health Coaches and average monthly revenue generated per health coach in the Take Shape For Life channel.

In 2014, the Company exited the MWCC corporate center model by selling 41 centers to existing franchise partners (24 centers were sold in June 2014 and the remaining 17 centers were sold in December 2014) and closing the remaining 34 corporate centers. The assets, liabilities, operating results, and cash flows of the MWCC corporate center channel have been presented separately as discontinued operations in the Consolidated Financial Statements for all periods presented.

**CONSOLIDATED RESULTS OF OPERATIONS**  
**2014 COMPARISON WITH 2013**

**Overview of the Twelve Months Ended December 31, 2014 Compared to Twelve Months Ended December 31, 2013**

	<b>Twelve Months Ended December 31,</b>			
	<b>2014</b>	<b>2013</b>	<b>\$ Change</b>	<b>% Change</b>
Revenue	\$ 285,285,000	\$ 324,054,000	\$ (38,769,000)	-12%
Cost of sales	76,078,000	83,488,000	(7,410,000)	-9%
<b>Gross Profit</b>	<b>209,207,000</b>	<b>240,566,000</b>	<b>(31,359,000)</b>	<b>-13%</b>
Selling, general, and administrative costs	178,961,000	202,156,000	(23,195,000)	-11%
<b>Income from operations</b>	<b>30,246,000</b>	<b>38,410,000</b>	<b>(8,164,000)</b>	<b>-21%</b>
Other income				
Interest income, net	716,000	509,000	207,000	41%
Other income	731,000	124,000	607,000	490%
	1,447,000	633,000	814,000	129%
<b>Income from continuing operations before income taxes</b>	<b>31,693,000</b>	<b>39,043,000</b>	<b>(7,350,000)</b>	<b>-19%</b>
Provision for income tax expense	10,664,000	11,908,000	(1,244,000)	-10%
Income from continuing operations	21,029,000	27,135,000	(6,106,000)	-23%
Loss from discontinued operations, net of tax	(7,848,000)	(3,166,000)	(4,682,000)	148%
<b>Net income</b>	<b>\$ 13,181,000</b>	<b>\$ 23,969,000</b>	<b>\$ (10,788,000)</b>	<b>-45%</b>
<b>% of revenue</b>				
Gross Profit	73.3%	74.2%		
Selling, general, and administrative costs	62.7%	62.4%		
Income from Operations	10.6%	11.9%		

Revenue: Revenue decreased to \$285.3 million in 2014 compared to \$324.1 million in 2013, a decrease of \$38.8 million. The Take Shape For Life sales channel accounted for 72.5%, the Medifast Direct channel accounted for 20.0%, the Franchise Medifast Weight Control Centers channel accounted for 5.4%, and the Medifast Wholesale channel accounted for 2.1% of total revenue. The year to date revenue to spend ratio for continuing operations for 2014 was 16.8-to-1 compared to 14.7-to-1 for 2013. Total advertising spend, inclusive of broker fees, for continuing operations was \$17.0 million in 2014 compared to \$22.1 million in 2013.

Take Shape For Life revenue decreased 10% to \$206.7 million in 2014 compared with \$228.7 million in 2013. The decline in revenue for Take Shape For Life was driven by a decrease in the number of active Health Coaches and revenue per Health Coach along with the accrued impact from the creation of the new BeSlim Club loyalty program. The number of active Health Coaches at the end of 2014 decreased to 9,300 compared with 10,500 during the period a year ago, a decrease of 11%. The average revenue per Health Coach per month decreased to \$1,524 in 2014 from \$1,605 in 2013. Approximately half of the decrease of the Health Coach count is due to having less pay periods used in the calculation versus the number of pay periods used in the prior year.

Medifast Direct Sales revenue decreased 24% to \$57.2 million as compared with \$75.5 million in 2013, a decrease of \$18.3 million. Revenues in this channel are primarily driven by targeted customer advertising on-line, across local radio, via email and direct mail campaigns, and by highlighting customer successes in large national publications and on television. The Company experienced lower marketing efficiencies and new customer acquisition during the year; and therefore, reduced marketing spending to optimize profitability. The Company's decision to reduce spending impacted the year-over-year revenue for the channel. As compared to 2013, the Company increased fourth quarter spending in an effort to drive 2015 sales.

Franchise Medifast Weight Control Centers channel revenue increased 1% year-over-year, with revenue of \$15.4 million in 2014 compared to \$15.3 million in 2013. 73 franchise centers were in operation as of December 31, 2014, including 19 corporate centers that were transitioned in June 2014 and 17 corporate centers that were transitioned in December 2014. 17 Franchise centers were closed during 2014, including 5 centers transitioned to the franchise model in June 2014 and 7 centers opened during 2014. There were 41 franchise centers in operation as of December 31, 2013. The increase in revenue was driven by the conversion of corporate centers over to Franchise Centers offset by franchise center closures as well as a decrease in sales of franchise centers open greater than one year.

Medifast Wholesale revenue increased 30%, or \$1.4 million, to \$6.0 for the year ended December 31, 2014 compared to \$4.6 million for the year ended December 31, 2013. The increase was driven by a reallocation of internal sales resources to improve revenue in the channel for both domestic and international customers.

Costs of Sales: Cost of sales decreased \$7.4 million in 2014 to \$76.1 million as compared to \$83.5 million in 2013. As a percentage of sales, gross margin decreased from 74.2% in 2013 to 73.3% in 2014, which was the result of increased year-over-year product costs primarily driven by a reduction in manufacturing volumes.

Selling, General and Administrative Costs: Selling, general and administrative expenses decreased by \$23.2 million compared to 2013. As a percentage of sales, selling, general and administrative expenses increased to 62.7% versus 62.4% in 2013. Included in selling general and administrative costs for 2014 are \$2.6 million in extraordinary legal expenses resulting from recent 13D filings and a \$2.0 million accrual for a franchise loan default guaranteed by Medifast. Excluding these items, selling, general, and administrative expense as a percentage of sales would have been 61.1%, a decrease of 130 basis points compared to 2013.

Take Shape For Life commission expense, which is variable based upon product sales, decreased by approximately \$15.6 million, or 15.4% as a result of a new compensation plan introduced in late 2013 and a 10% decrease in sales for the channel.

Salaries and benefits decreased by approximately \$3.5 million in 2014 as compared to 2013. The year-over-year decrease was driven by reductions in bonuses, salaries, and medical expenses resulting from the Company's continued focus on headcount. These improvements were partially offset by an increase in stock compensation expense.

Sales and marketing expense decreased by \$5.1 million in 2014 as compared to the prior year as a result of lower advertising expenses. The Company continues to focus on efficiency improvements and balancing sales and marketing expense in an effort to drive profitability. The Company increased year-over-year fourth quarter revenue spending in an effort to drive 2015 sales.

General expenses increased \$3.0 million in 2014 as compared to 2013. The year-over-year change was driven by a \$2.0 million accrual relating to a default on a franchise loan guaranteed by Medifast and an increase in legal expenses, inclusive of \$2.6 million in extraordinary expenses resulting from recent 13D filings. These were partially offset by a decrease in information technology consulting fees.

Other expenses consisting primarily of depreciation and credit card processing fees, decreased by \$1.7 million. The decrease in expenses for the period was the result of a reduction in credit card fees due to reduced revenues and the final settlement of Voluntary Disclosure Agreement's (VDA) accrued in 2012 and issued in 2013.

Income taxes: In 2014, the Company recorded \$10.7 million in income tax expense, an effective rate of 33.6%. In 2013, the Company recorded \$11.9 million in income tax expense, an effective rate of 30.5%. The increase in the effective tax rate in 2014 over 2013 was a result of benefits realized in 2013 from research and development credits of \$0.5 million that were retroactive to 2012, as well as realizing benefits of \$0.8 million from extensive state income tax restructuring (to take advantage of apportionment methodology) which also related to prior years. As a manufacturing entity based in Maryland, in 2013 the Company adopted the single sales factor apportionment method in addition to claiming new state jobs credits and research and development credits. The Company anticipates a tax rate of approximately 33 – 34% in 2015.

Income from continuing operations: Income from continuing operations was \$21.0 million in 2014 as compared to \$27.1 million in 2013, a decrease of \$6.1 million. Income from operations decreased by \$8.2 million, or 21%, versus 2013 with the percent of sales decreasing to 10.6% in 2014 as compared to 11.9% in 2013. The year-over-year decrease in profitability was primarily driven by the 11.9% reduction in sales coupled with an increase in product costs, a \$1.8 million after tax extraordinary legal and advisory expenses incurred in relation to the recent 13D filings and a \$1.3 million after tax accrual relating to a default on a franchise loan guaranteed by Medifast. These negative impacts to profits were partially offset by the Company's continued efforts to closely monitor spending as demonstrated in the decrease in selling, general, and administrative expenses outlined above.

Loss from discontinued operations: In 2014, the Company exited the MWCC corporate center model by selling 41 centers to existing franchise partners (24 centers were sold in June 2014 and the remaining 17 centers were sold in December 2014) and closing the remaining 34 corporate centers. Loss from discontinued operations was \$7.8 million in 2014 as compared to \$3.1 million in 2013, a decrease of \$4.7 million. The year-over-year decrease includes the \$8.6 million pre-tax, \$5.2 million after-tax, charge for the closure of 34 centers in December 2014. This charge includes \$0.6 million for one-time termination benefits, \$4.4 million for closed clinic lease obligations, \$3.3 million for impaired assets, and \$0.5 million in other facility related closure costs. These exit activity costs were partially offset by a gain of \$0.2 million on the sale of centers.

Net income: Net income was \$13.2 million in 2014 compared to \$24.0 million in 2013. The year-over-year change was driven by the factors described above in the explanations for income from continuing operations and loss from discontinued operations.

## Non-GAAP Financial Measures

In addition to providing results that are determined in accordance with GAAP, the Company provides certain non-GAAP financial measures. The Company's 2014 non-GAAP financial measures of adjusted net income and adjusted diluted earnings per share exclude the charges the Company incurred in relation to the franchise loan default guaranteed by Medifast, the extraordinary legal expenses in connection with the 13D filings. The 2012 non-GAAP financial measures exclude the non-tax deductible FTC settlement as well as the charge taken to accrue for sales tax exposures. Because all of these charges are unique events, not directly related to the Company's normal operations, the Company believes these non-GAAP financial measures may help investors better understand and compare our operating results and trends by eliminating this component.

The reconciliations of these non-GAAP financial measures are as follows:

	Years Ended December 31,		
	2014	2013	2012
Income from operations	\$ 30,246,000	\$ 38,410,000	\$ 27,140,000
Adjustments			
Franchise loan guarantee accrual	1,980,000	-	-
Legal expenses- 13D	2,597,000	-	-
Sales Tax Expense Accrual	-	-	3,256,000
FTC Settlement Expense	-	-	3,700,000
Adjusted Income from operations	<u>\$ 34,823,000</u>	<u>\$ 38,410,000</u>	<u>\$ 34,096,000</u>

	Years Ended December 31,		
	2014	2013	2012
Income from continuing operations	\$ 21,029,000	\$ 27,135,000	\$ 18,442,000
Adjustments			
Franchise loan guarantee accrual	1,342,000	-	-
Legal expenses- 13D	1,761,000	-	-
Sales Tax Expense Accrual	-	-	2,026,000
FTC Settlement Expense	-	-	3,700,000
Adjusted income from continuing operations	<u>\$ 24,132,000</u>	<u>\$ 27,135,000</u>	<u>\$ 24,168,000</u>
Loss on discontinued operations, net of tax	<u>(7,848,000)</u>	<u>(3,166,000)</u>	<u>(2,566,000)</u>
Adjusted Net Income	<u>\$ 16,284,000</u>	<u>\$ 23,969,000</u>	<u>\$ 21,602,000</u>
Diluted earnings per share from continuing operations	\$ 1.65	\$ 1.96	\$ 1.34
Impact for adjustments	0.24	-	0.41
Adjusted diluted earnings per share continuing operations	<u>\$ 1.89</u>	<u>\$ 1.96</u>	<u>\$ 1.75</u>
Diluted Loss per share from discontinued operations	<u>\$ (0.62)</u>	<u>\$ (0.23)</u>	<u>\$ (0.18)</u>
Adjusted diluted earnings per share	<u>\$ 1.27</u>	<u>\$ 1.73</u>	<u>\$ 1.57</u>

Excluding the impact of the \$2.0 million franchise loan guarantee and the \$2.6 extraordinary legal expenses in connection with the 13D filings, income from operations for the year ended December 31, 2014, decreased \$3.6 million to \$34.8 million from \$38.4 million for the year ended December 31, 2013. Adjusted income from continuing operations for the year ended December 31, 2014 decreased to \$24.1 million from income from continuing obligations of \$27.1 million for the year ended December 31, 2013. Adjusted net income for the year ended December 31, 2014 decreased to \$16.3 million from net income of \$24.0 million for the year ended December 31, 2013. Adjusted diluted earnings per share from continuing operations for the year ended December 31, 2014 decreased to \$1.89 as compared to diluted earnings per of \$1.96 for the same period in 2013. Adjusted diluted earnings per share for the year ended December 31, 2014 decreased to \$1.27 as compared to adjusted diluted earnings per share of \$1.73 for the same period in 2013.

## Contractual Obligations and Commercial Commitments

The Company has the following contractual obligations as of December 31, 2014:

	<u>2015</u>	<u>2016</u>	<u>2017</u>	<u>2018</u>	<u>2019</u>	<u>Total</u>
Operating Leases <sup>(a)</sup>	\$ 1,352,000	\$ 1,128,000	\$ 676,000	\$ 84,000	\$ -	\$ 3,240,000
Operating Leases for Closed MWCC Centers <sup>(b)</sup>	1,490,000	1,288,000	574,000	178,000	35,000	3,565,000
Operating Leases for Sold MWCC Centers <sup>(c)</sup>	1,629,000	1,217,000	717,000	226,000	36,000	3,825,000
Capital Leases <sup>(d)</sup>	248,000	248,000	-	-	-	496,000
Total contractual obligations	<u>\$ 4,719,000</u>	<u>\$ 3,881,000</u>	<u>\$ 1,967,000</u>	<u>\$ 488,000</u>	<u>\$ 71,000</u>	<u>\$ 11,126,000</u>

(a) The Company has operating leases in place for leased corporate offices, our Texas Distribution center, our raw materials warehouse, and the Company's printers.

(b) The Company has 24 operating leases in place that extend beyond December 31, 2015 for closed Medifast Corporate Weight Control Centers. The Company is actively seeking to reach lease termination agreements on these obligations.

(c) The Company has 32 operating leases in place that extend beyond December 31, 2015 for previously Medifast Corporate Weight Control Centers sold to franchise partners. The Company remains named on the leases, however the obligations have been subleased to the franchisees.

(d) We lease large commercial printers for our printing operations that are accounted for as capital leases, these obligations are detailed in Note 7 of the financial statements.

## LIQUIDITY AND CAPITAL RESOURCES

The Company had stockholders' equity of \$80.5 million and working capital of \$55.0 million on December 31, 2014 compared with \$98.4 million and \$64.9 million at December 31, 2013, respectively. The \$17.9 million net decrease in stockholder's equity reflects \$13.2 million in 2014 profits significantly offset by the \$33.9 million used to purchase shares of the Company's common stock as well as other equity transactions as outlined in the "Consolidated Statement of Changes in Stockholders' Equity". The Company's cash and cash equivalents position decreased from \$36.4 million at December 31, 2013 to \$24.5 million at December 31, 2014.

In the year ended December 31, 2014 the Company generated cash flow of \$27.3 million from continuing operations, partially attributable to \$21.0 million in income from continuing operations. Cash provided by operating activities of \$14.1 million include depreciation and amortization of \$8.1 million, share-based compensation of \$3.9 million, a decrease in inventory of \$1.8 million, and deferred income taxes of \$0.3 million. This was offset by cash used by operating activities of \$7.7 million which includes a \$5.2 million increase in prepaid income taxes, a net realized gain on investment securities of \$0.8 million, an increase in accounts receivable of \$0.7 million, an increase in prepaid expenses and other current assets of \$0.3 million, a decrease in accounts payable and accrued expenses of \$0.4 million and an increase in other long-term assets of \$0.3 million.

Net cash used in operating activities from discontinued operations was \$1.8 million including loss from discontinued operations of \$7.8 million. Cash provided by operating activities from discontinued operations totaled \$9.1 million and include depreciation and amortization of \$1.6 million, \$3.3 million for the impairment of fixed assets, an increase in accounts payable and accrued expenses of \$3.1 million, a decrease in inventory of \$0.4 million, a decrease in prepaid expenses and other current assets of \$0.4 million, a decrease in accounts receivable of \$0.2 million, and a decrease of \$0.1 million in other long-term assets. Non-cash benefits include \$3.1 million of deferred income benefit.

In the year ended December 31, 2014, net cash used in investing activities from continuing operations was \$3.5 million, which was due to \$26.1 million for the purchase of investment securities offset by \$29.6 million of cash generated by the sale of investment securities and \$7.0 million for the purchase of property and equipment. Net cash provided by investing activities from discontinued operations was \$1.0 million, which was the cash generated by the sale of property and equipment.

In the year ended December 31, 2014, financing activities from continuing operations used \$34.9 million in cash. Cash was used to purchase \$33.9 million of treasury stock in the open market, to repurchase shares to cover employee taxes of \$1.2 million, and to repay \$0.2 million in capital leases. The Company realized a cash benefit for excess tax benefits from share-based compensation in the amount of \$0.3 million. As of December 31, 2014, there are 1,211,908 shares of the Company's common stock eligible for repurchase under the repurchase authorization dated September 16, 2014.

In pursuing its business strategy, the Company may require additional cash for operating and investing activities. The Company expects future cash requirements, if any, to be funded from operating cash flow and financing activities.

The Company has an undrawn, unsecured, revolving \$5 million line of credit with Bank of America. The line of credit will expire on August 1, 2015, at which point the Company expects to extend the term or pursue other financing opportunities.

The Company evaluates acquisitions from time to time as presented.

## OFF BALANCE SHEET ARRANGEMENTS

The Company has entered into guarantee agreements with two key franchisee partners in order to support them obtaining additional funding to expand their business into new markets.

The first guarantee provides financial coverage for a \$1.0 million loan and a \$1.0 million line of credit. The variable rate term loan has a 2 year term expiring in September 2015; payment calculations assume a 7 year amortization with a balloon payment due at the end of the term. The line of credit has a two year term expiring in September 2015. The franchisee associated with these loans has failed to pay the monthly obligations and the Company expects to be required to perform under this guarantee and has accrued a charge of \$2.0 million as of December 31, 2014. The Company is a secondary guarantor on the loan and line of credit and has pursued personal recourse against the franchise owner.

The second guarantee provides financial coverage for a \$1.4 million loan. The variable rate term loan has a 2 year term expiring in October 2015; payment calculations assume a 7 year amortization with a balloon payment due at the end of the term. The Company is the third guarantor on these loans and has recourse against another entity owned by the franchisee and the franchisee owner(s) themselves should it be deemed necessary. As of March 10, 2015, the franchisee has an outstanding balance of \$0.1 million on the loan.

## CONSOLIDATED RESULTS OF OPERATIONS 2013 COMPARISON WITH 2012

### Overview of the Twelve Months Ended December 31, 2013 Compared to Twelve Months Ended December 31, 2012

	Twelve Months Ended December 31,			
	2013	2012	\$ Change	% Change
Revenue	\$ 324,054,000	\$ 318,571,000	\$ 5,483,000	2%
Cost of sales	83,488,000	82,662,000	826,000	1%
<b>Gross Profit</b>	<b>240,566,000</b>	<b>235,909,000</b>	<b>4,657,000</b>	<b>2%</b>
Selling, general, and administrative costs	202,156,000	208,769,000	(6,613,000)	-3%
<b>Income from operations</b>	<b>38,410,000</b>	<b>27,140,000</b>	<b>11,270,000</b>	<b>42%</b>
Other income				
Interest income, net	509,000	304,000	205,000	67%
Other income	124,000	912,000	(788,000)	-86%
	633,000	1,216,000	(583,000)	-48%
<b>Income from continuing operations before income taxes</b>	<b>39,043,000</b>	<b>28,356,000</b>	<b>10,687,000</b>	<b>38%</b>
Provision for income tax expense	11,908,000	9,914,000	1,994,000	20%
Income from continuing operations	27,135,000	18,442,000	8,693,000	47%
Loss from discontinued operations, net of tax	(3,166,000)	(2,566,000)	(600,000)	23%
<b>Net income</b>	<b>\$ 23,969,000</b>	<b>\$ 15,876,000</b>	<b>\$ 8,093,000</b>	<b>51%</b>
<b>% of revenue</b>				
Gross Profit	74.2%	74.1%		
Selling, general, and administrative costs	62.4%	65.5%		
Income from Operations	11.9%	8.5%		

Revenue: Revenue increased to \$324.1 million in 2013 compared to \$318.6 million in 2012, an increase of \$5.5 million. The Take Shape For Life sales channel accounted for 70.6%, the Medifast Direct channel accounted for 23.3%, the Franchise Medifast Weight Control Centers channel accounted for 4.7% and the Medifast Wholesale channel accounted for 1.4% of total revenue. The year to date revenue to spend ratio for 2013 for continuing operations was 14.7-to-1 compared to 11.7-to-1 for 2012. Total advertising spend, inclusive of broker fees, was \$22.1 million in 2013 compared to \$27.2 million in 2012.

Take Shape For Life revenue increased 6% to \$228.7 million in 2013 compared with \$216.1 million in 2012. Growth in revenues for the channel was driven by pricing resulting from our revised discount structure. The number of active Health Coaches at the end of 2013 increased to 10,500 compared with 10,200 during the period a year ago, an increase of 3%. "Active Health Coaches" are defined as Health Coaches receiving income from a product sale in the last month of the quarter. The average revenue per Health Coach per month decreased to \$1,605 in 2013 from \$1,635 in 2012.

Medifast Direct Sales revenue decreased 11% to \$75.5 million as compared with \$84.4 million in 2012, a decrease of \$8.9 million. Revenues in this channel are primarily driven by targeted customer advertising on-line, across local radio, via email and direct mail campaigns, and by highlighting customer successes in large national publications and on television. The decrease in revenue was primarily caused by a more challenging consumer discretionary spending environment and reduction in advertising spending.

Franchise Medifast Weight Control Centers revenue increased 7% to \$15.3 million in 2013 compared to \$14.3 million in 2012. Six franchise centers were opened in 2013, for a total of forty-one centers as of December 31, 2013 driving the year-over-year increase in revenue.

Medifast Wholesale revenue increased 21% to \$4.6 million in 2013 compared with \$3.8 million in 2012; which resulted from improved customer relationships and education of the Medifast products and programs, driving an increase in volumes.

Costs of Sales: Cost of sales increased \$0.8 million in 2013 to \$83.5 million as compared to \$82.7 million in 2012 which is primarily the result of higher shipping expenses. As a percentage of sales, gross margin increased from 74.1% in 2012 to 74.2%.

Selling, General and Administrative Costs: Selling, general and administrative expenses decreased by \$6.6 million compared to 2012. As a percentage of sales, selling, general and administrative expenses were reduced to 62.4% versus 65.5% in 2012.

Two non-recurring items recorded in 2012 contributed to \$7.0 million of the improvement in expenses. The FTC settlement recorded in the second quarter of \$3.7 million as well as the recording of a sales tax accrual of \$3.3 million recorded in the fourth quarter. The focus of sales tax on internet based remote sellers has gained momentum in many states. Because of this, combined with the desire of the Company to create symmetry among all sales channels, we have re-aligned our position to be more consistent with other major internet sellers and will now be collecting and remitting sales tax in all states that impose sales or use taxes. In order to mitigate the financial impact on any prior year activity, the Company is taking advantage of voluntary disclosure agreements with various states.

Take Shape For Life commission expense, which is variable based upon product sales, increased by approximately \$4.5 million as Take Shape For Life sales grew 6% compared to 2012. Take Shape For Life Health Coaches are independent contractors who are paid commissions on product sales referred to the Company. Health Coaches earn commissions by referring product sales through a personalized Company-owned replicated website or through the Company's in-house call center. The clients of Health Coaches are responsible for order and payment of product and their order is shipped directly to their home or designated address. Health Coaches are not required to purchase product in order to receive a commission. In addition, Health Coaches do not receive a commission on their personal product orders.

Salaries and benefits decreased by approximately \$0.5 million in 2013 as compared to 2012. The decrease was driven by a reduction in bonuses and medical expenses year-over-year. The cost savings were partially offset by the hiring of and increased salaries for key technical and executive positions.

Sales and marketing expense decreased by \$5.8 million in 2013 as compared to the prior year as a result of lower advertising expenses and a reduction in conference and tradeshow expenses for the Take Shape For Life channel. The Company continues to balance marketing expenses to deliver a strong bottom line.

Exclusive of the effect of the non-recurring FTC settlement in 2012, general expenses decreased \$0.2 million in 2013 as compared to 2012. The savings were driven by a decrease in information technology consulting fees.

Other expenses consisting primarily of depreciation and credit card processing fees, decreased by \$0.4 million. The decrease was driven by the \$3.2 million sales tax accrual in 2012 compared to \$0.9 million in 2013, partially offset by a \$1.7 million increase in licenses and fees.

Income taxes: In 2013, the Company recorded \$11.9 million in income tax expense, an effective rate of 30.5%. In 2012, the Company recorded \$9.9 million in income tax expense, an effective rate of 35.0%. Excluding the \$3.7 million FTC settlement, the effective tax rate for 2012 would have been 30.9%. The decrease in the effective tax rate was a result of research and development credits effective January 1, 2013, applicable retroactively to 2012 activity. In both years, the Company benefited from extensive state income tax restructuring to take advantage of apportionment methodology. As a manufacturing entity based in Maryland, the Company adopted the single sales factor apportionment method in addition to claiming new state jobs credits and research & development credits.

Income from continuing operations: Income from continuing operations was approximately \$39.0 million in 2013 as compared to approximately \$28.4 million in 2012, an increase of \$10.6 million. Income from operations as a percent of sales increased to 11.9% in 2013 as compared to 8.5% in 2012. The increase in profitability in 2013 was primarily a result of the 2012 settlement charge of \$3.7 million with the FTC, the 2012 \$3.3 million charge to accrue for sales tax exposure, the 2012 \$0.4 million accelerated compensation for the Executive Chairman of the Board, and the Company's overall focus to reduce expenses during 2013 in order to improve profitability. These items were offset by the 2012 key man insurance proceeds. Excluding the impact of the 2012 FTC settlement and sales tax accrual, income from operations for 2012 would have been \$34.1 million, or 10.7% of sales.

Loss from discontinued operations: Loss from discontinued operations was \$3.2 million in 2013 versus \$2.6 million in 2012, a decrease of \$0.6 million. The decrease in profit was driven by a 14% year-over-year decrease in sales partially offset by reduced advertising spend as a percentage of sales for each corporate center and savings from the staffing re-alignment completed in the first quarter of 2012.

Net income: Net income was \$24.0 million in 2013 compared to \$15.9 million in 2012. The year-over-year increase was driven by the factors described above in the explanations for income from continuing operations and loss from discontinued operations.

## **INFLATION**

To date, inflation has not had a material effect on the Company's business.

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

Market risk is the potential loss arising from adverse changes in market rates and prices, such as interest rates and a decline in the stock market. The Company does not enter into derivatives, foreign exchange transactions or other financial instruments for trading or speculative purposes. The Company paid off its outstanding debt during the first quarter of 2013, eliminating our current exposure to interest rate risk. However, we have an undrawn and unsecured revolving line of credit for \$5,000,000, should we choose to draw on this line of credit in the future we would be subject to market risk due to changing interest rates.



We are exposed to market risk related to changes in interest rates and market pricing impacting our investment portfolio. Our current investment policy is to maintain an investment portfolio consisting mainly of U.S. money market and high-grade corporate securities, directly or through managed funds. Our cash is deposited in and invested through highly rated financial institutions in North America. Our marketable securities are subject to interest rate risk and market pricing risk and will fall in value if market interest rates increase or if market pricing decreases. If market interest rates were to increase and market pricing were to decrease immediately and uniformly by 10% from levels at December 31, 2014, we estimate that the fair value of our investment portfolio would decline by an immaterial amount and therefore we would not expect our operating results or cash flows to be affected to any significant degree by the effect of a change in market conditions on our investments.

## **ITEM 8. FINANCIAL STATEMENTS**

The information required by this item is set forth on pages 59 to 75 hereto and incorporated by reference herein.

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

There were no disagreements with the Company's independent auditors, regarding accounting and financial disclosures for the fiscal year ending December 31, 2014.

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

### **Disclosure Controls and Procedures**

In accordance with Exchange Act Rule 13a-15(e), we carried out an evaluation, under the supervision and with the participation of management, including our Chief Executive Officer and Chief Financial Officer, of the effectiveness of our disclosure controls and procedures as required by Exchange Act Rule 13a-15(b) as of the end of the period covered by this report. Based upon that evaluation, our management has concluded that our disclosure controls and procedures are effective as of December 31, 2014.

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

Our management is responsible for establishing and maintaining adequate internal control over financial reporting for the Company. Internal control over financial reporting is a process to provide reasonable assurance regarding the reliability of our financial reporting for external purposes in accordance with accounting principles generally accepted in the United States of America. Internal control over financial reporting includes maintaining records that in reasonable detail accurately and fairly reflect our transactions, providing reasonable assurance that transactions are recorded as necessary for preparation of our financial statements, providing reasonable assurance that receipts and expenditures of Company assets are made in accordance with management authorization, and providing reasonable assurance that unauthorized acquisition, use or disposition of Company assets that could have a material effect on our financial statements would be prevented or detected on a timely basis. Because of its inherent limitations, internal control over financial reporting is not intended to provide absolute assurance that a misstatement of our financial statements would be prevented or detected.

Management conducted an evaluation of the effectiveness of our internal control over financial reporting based on the framework in Internal Control – Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission in 2013. Based on this evaluation, our management concluded that the Company's internal control over financial reporting was effective as of December 31, 2014.

The effectiveness of the Company's internal control over financial reporting as of December 31, 2014, was audited by McGladrey LLP, our independent registered public accounting firm, as stated in their report appearing below.

### **Changes in our Internal Control**

No change in our internal control over financial reporting (as defined in Rules 13a-15(f) and 15d-15(f) under the Exchange Act) occurred during the fourth quarter ended December 31, 2014 that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

### **Limitations on the Effectiveness of Controls**

Our management, including our Chief Executive Officer and Chief Financial Officer, does not expect that our disclosure controls or our internal controls will prevent or detect all errors and all fraud. A control system, no matter how well designed and operated, can provide only reasonable, not absolute, assurance that the control system's objectives will be met. Further, the design of a control system must reflect the fact that there are resource constraints, and the benefits of controls must be considered relative to their costs. Because of the inherent limitations in all control systems, no evaluation of controls can provide absolute assurance that all control issues and instances of fraud, if any, within the Company have been detected. These inherent limitations include the realities that judgments in decision-making can be faulty, and that breakdowns can occur because of simple error or mistake. Controls can also be circumvented by the individual acts of some persons, by collusion of two or more people, or by management override of the controls. The design of any system of controls is based in part upon certain assumptions about the likelihood of future events, and there can be no assurance that any design will succeed in achieving its stated goals under all potential future conditions. Over time, controls may become inadequate because of changes in conditions or deterioration in the degree of compliance with associated policies or procedures. Because of the inherent limitations in a cost-effective control system, misstatements due to error or fraud may occur and not be detected.

## Report of Independent Registered Public Accounting Firm

To the Board of Directors and Stockholders of  
Medifast, Inc.

We have audited Medifast, Inc. and subsidiaries' (the "Company") internal control over financial reporting as of December 31, 2014, based on criteria established in *Internal Control—Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission in 2013. The Company's management is responsible for maintaining effective internal control over financial reporting and for its assessment of the effectiveness of internal control over financial reporting included in the accompanying "*Management's Report on Internal Control Over Financial Reporting*". Our responsibility is to express an opinion on the Company's internal control over financial reporting based on our audit.

We conducted our audit in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether effective internal control over financial reporting was maintained in all material respects. Our audit included obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, and testing and evaluating the design and operating effectiveness of internal control based on the assessed risk. Our audit also included performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion.

A company's internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company's internal control over financial reporting includes those policies and procedures that (a) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (b) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (c) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company's assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

In our opinion, the Company maintained, in all material respects, effective internal control over financial reporting as of December 31, 2014, based on criteria established in *Internal Control — Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission in 2013.

We have also audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the consolidated balance sheets as of December 31, 2014 and 2013, and the related consolidated statements of income, comprehensive income, stockholders' equity, and cash flows for each of the three years in the period ended December 31, 2014 of the Company and our report dated March 16, 2015 expressed an unqualified opinion.

/s/ McGladrey LLP

Baltimore, Maryland  
March 16, 2015

**ITEM 9B. OTHER INFORMATION**

Not applicable

## PART III

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

#### BOARD OF DIRECTORS

The Board is currently composed of twelve directors and divided into three classes, Class I, Class II or Class III. Pursuant to the terms of the Cooperation Agreement the size of the Board will be reduced to 7 and all directors will stand for election annually commencing at the 2015 annual meeting. In connection with the Cooperation Agreement, Jason L. Groves, John P. McDaniel, Donald F. Reilly, OSA, Margaret Sheetz, Barry B. Bondroff and Catherine T. Maguire have agreed not to stand for reelection to the Board. Additionally, Harvey C. Barnum, Jr. and Jerry D. Reece, who are also current members of the Board, will not stand for reelection at the 2015 annual meeting because they have reached, or will reach, the Company's mandatory retirement age for non-management directors by December 31, 2015. Additionally, the amendment to the Bylaws discussed above provides that commencing with the 2015 annual meeting the Board will be declassified and all directors will be elected annually for one year terms that will expire at the next year's annual meeting.

#### Current Class I Directors

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**Charles P. Connolly**, age 66, has been a director of the Company since 2006. Mr. Connolly is the Chairman of the Audit Committee and also serves as a member of the Special Mergers & Acquisitions Committee. Mr. Connolly spent 29 years at First Union Corp., which merged with Wachovia Bank in 2001. He retired in 2001 as the President and Chief Executive Officer of First Union Corp. of Pennsylvania and Delaware. Mr. Connolly serves on the board of numerous profit and non-profit organizations. He holds an MBA from the University of Chicago and AB from Villanova University.

*Qualifications:* Mr. Connolly brings to the Board extensive executive experience and financial acumen derived from a lengthy executive career in the banking industry. He possesses a unique financial and risk assessment perspective into the operations and financial management of the Company and spends significant time with our executive team providing guidance and consultation on key metrics and performance objectives that have served Medifast well in the past few years.

**Jason L. Groves, Esq.**, age 44, has been a director of the Company since 2009. Mr. Groves serves as a member of the Executive Committee. Mr. Groves has served as the Company's Executive Vice President and General Counsel since November 2011. Prior to joining Medifast in November 2011, Mr. Groves served as Assistant Vice President of Government Affairs for Verizon Maryland, since 2003. Mr. Groves is also an Army veteran. He was a direct commissioned Judge Advocate in the United States Army Judge Advocate General's Corp ("JAG"). As a JAG Officer, he practiced law and had the distinction of prosecuting criminal cases in the District Court of Maryland as a Special Assistant United States Attorney. Over the course of three years, he received two Army Achievement Medals, and one Army Commendation Medal. Mr. Groves also sits on several non-profit boards including Anne Arundel Medical Center and the Maryland Hospital Association. Mr. Groves received his Bachelor of Science degree, cum laude, in Business with a concentration in Hospitality Management, from Bethune-Cookman University. He also obtained his juris doctorate from North Carolina Central University School of Law and is a member of the New Jersey and District of Columbia bars as well as several bar associations.

*Qualifications:* Mr. Groves was first selected as a director in 2009 based on his military, business and legal background. In addition he has extensive experience with government relations and knowledge of the healthcare and communications technology fields. His background as a federal prosecutor gives him insight into the regulatory and legal issues the Company faces in today's business climate.

**John P. McDaniel**, age 72, has been a director of the Company since 2009. Mr. McDaniel serves as a member of the Audit Committee and the Special Mergers & Acquisitions Committee. He is a seasoned healthcare executive with more than 36 years of experience as a chief executive officer, most recently at MedStar Health Systems in Columbia, Maryland, one of the largest and most comprehensive healthcare delivery systems in the mid-Atlantic region. He is presently Chair and Partner in The Hickory Ridge Group, an advisory, development and investment company that focuses on emerging healthcare and technology related entities. He is also a member of the Executive Committee and on the board of the Greater Washington Board of Trade, on the board of Wittenberg University, and is the Chair and member of the board of the Washington Real Estate Trust, a New York Stock Exchange ("NYSE") listed company. Mr. McDaniel has a degree in Business Administration from Wittenberg University, an MHA in Health Management and Policy from the University of Michigan, and an Honorary Doctorate of Humane Letters from Wittenberg University.

*Qualifications:* Mr. McDaniel brings extensive healthcare executive and entrepreneurial experience to the Board. His extensive management and board knowledge concerning the health care industry and health care policy provides seasoned oversight.

**Donald F. Reilly, OSA**, age 67, has been a director of the Company since 1998. Fr. Reilly serves as Chairman of the Nomination Committee. He holds a Doctorate in Ministry (Counseling) from New York Theological and an M.A. from Washington Theological Union as well as a B.A. from Villanova University. Fr. Reilly was ordained a priest in 1974. He is currently on the board of Villanova University. He also serves on the board of trustees of Merrimack College, MA, St. Augustine Prep, NJ, and Malvern Prep, PA. Fr. Reilly was Prior Provincial of the Augustinian Order at Villanova, PA from 2002 to 2010. He oversaw more than 220 Augustinian Friars and their service to the Church, teaching at universities and high schools, ministering to parishes, serving as chaplain in the Armed Forces and hospitals, ministering to AIDS victims, and serving missions in Japan, Peru, and South Africa. Fr. Reilly is currently the President of St. Augustine Preparatory School in Richland, New Jersey.

*Qualifications:* Father Reilly brings to the Board a strong background in personnel and executive management. Father Reilly was present during the restructuring of the Company in 1999 and has an extensive knowledge of the history of the Company. He was also instrumental in developing the current business model in consultation with the Business School at Villanova University. A nationally known academic holding a Ph.D., Father Reilly has been an invaluable asset providing guidance to the company and creating stockholder value. He has also been instrumental in assisting the Nomination Committee

in identifying and evaluating potential director candidates for the characteristics we consider necessary to perform high performance, risk assessment and be transparent which are desirable characteristics for all potential directors.

**Carl E. Sassano**, age 65, has been a director of the Company since 2013. Mr. Sassano serves as a member of the Compensation Committee and the Special Mergers & Acquisitions Committee. He is a member of the board of Transcat, Inc. and the Lead Director. Mr. Sassano was Chairman of the Board of Transcat from October 2003 until July, 2013. From April 2007 to May 2008, he also served as executive chairman of the board. Mr. Sassano became President and Chief Executive Officer of Transcat in March 2002 and was named Chairman of the board in October 2003. In May 2006, he ceased serving as president when Charles P. Hadeed assumed that position. He ceased serving as CEO in April, 2007. Mr. Sassano was president and chief operating officer of Bausch & Lomb Incorporated in 1999 and 2000. He also held positions in Bausch & Lomb as president-global vision care (1996-1999), president-contact lens division (1994-1996), group president (1993-1994) and president-Polymer Technology (1983-1992), a subsidiary of Bausch & Lomb. Mr. Sassano is a partner in CSW Equity Partners, a small private equity investment company. He also serves as Chairman of the board of Voiceport, one of the companies in the CSW portfolio. He has a BA from Rochester Institute of Technology and an MBA from the University of Rochester.

*Qualifications:* Mr. Sassano's brings to the Board leadership skills and significant public corporate experience from both small companies (Transcat) and large corporations (Bausch & Lomb). He also brings a strong understanding of the issues organizations face in executing a growth strategy.

## **Current Class II Directors**

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**Michael C. MacDonald**, age 61, has been a director of the Company since 1998. Mr. MacDonald serves as a member of the Executive Committee. Mr. MacDonald has served as Executive Chairman of the Board since November 2011, and was promoted to Chairman and Chief Executive Officer in February 2012. Prior to this role, Mr. MacDonald was Executive Vice President of OfficeMax, overseeing the Contract Division, a \$3.6 billion division of the OfficeMax Company. Mr. MacDonald has spent an additional 33 years in sales, marketing, and general management at Xerox Corporation. Among his most significant roles was leading the turnaround in North America from the years 2000-2004 as President of the North American Solutions Group, a \$6.5 billion division of Xerox. In addition, Mr. MacDonald was President of Global Accounts and Marketing from 2004-2007, where he led the re-branding of the Xerox Corporation. Mr. MacDonald also has international experience in marketing, sales, and operations with both Xerox and OfficeMax. In addition to serving as Chairman and Chief Executive Officer of the Company, Mr. MacDonald also serves on the Jimmy V Foundation and the Archdiocese of Baltimore Catholic Community Foundation.

Mr. MacDonald received his Bachelor of Arts, Political Science at Rutgers University, earned 44 MBA Credits at Iona College, and attended premier executive education courses in leadership and management at Harvard and Columbia Universities. Mr. MacDonald is the uncle of Margaret Sheetz.

*Qualifications:* Mr. MacDonald brings to the Board leadership skills and significant experience from large corporations. His significant leadership and management experience helps drive innovation and results.

**Margaret E. Sheetz**, age 38, has been a director of the Company since 2008. Ms. Sheetz serves as a member of the Executive Committee. Ms. Sheetz has served as the President and Chief Operating Officer of Medifast since 2008. In March 2011, Ms. Sheetz also became the Chief Executive Officer of Take Shape for Life. Prior to joining the Company in 2000, she worked with the firm of Carrington, Coleman, Sloman and Blumenthal in Dallas, Texas. Ms. Sheetz supports the efforts of the American Diabetes Association, the American Heart Association, and Toys for Tots Foundation. She sits on the board for Stevenson University, the Greater Baltimore Committee, Siloam, and is also a member of the Villanova President's Leadership Circle. In addition, she is the managing trustee of the MacDonald Family Foundation and the Take Shape for Life Foundation which focuses on grants to support educational programs for disadvantaged students. She holds a Bachelor of Arts degree from Villanova University and received an Executive MBA from Loyola University. Ms. Sheetz is the niece of Michael C. MacDonald.

*Qualifications:* As Medifast continues to see strong year-over-year growth, Ms. Sheetz has provided the operational and technical leadership that has resulted in Medifast providing the proper infrastructure to support the growth of the Company. Her accomplishments include making dramatic productivity improvement in the Company's operational capabilities, as well as building a strong infrastructure of distribution, manufacturing, information systems and human resource operations necessary to support rapid business growth. Her leadership and oversight skills are greatly admired, and she is recognized in the Company as a detail-oriented executive who builds high-performance teams. The Board considers her the source person to get information pertinent to the oversight of Medifast's operations.

**Harvey C. Barnum, Jr.**, age 74, has been a director of the Company since 2009. Mr. Barnum was the Deputy Assistant Secretary of the Navy for Reserve Affairs from July 2001 to January 2009. In this capacity he was responsible for all matters regarding the Navy and Marine Corps Reserve including manpower, equipment, policy and budgeting. In January 2009, Mr. Barnum was designated Acting Assistant Secretary of the Navy (Manpower and Reserve Affairs), a position he held until May 2009. In 1962 MR. Barnum was commissioned as a Second Lieutenant and he retired from the Marine Corps as a Colonel in August 1989 after more than 27 years of service. Upon retirement in 1989, Mr. Barnum served as the principal director, Drug Enforcement Policy, Office of the Secretary of Defense. Mr. Barnum's personal medals and decorations include: the Medal of Honor; Defense Superior Service Medal; Legion of Merit; the Bronze Star Medal with Combat "V" and gold star in lieu of a second award; Purple Heart; Meritorious Service Medal; Navy Commendation Medal; Navy Achievement Medal with Combat "V"; Combat Action Ribbon; Presidential Unit Citation; Army Presidential Unit Citation; Joint Meritorious Unit Award; Navy Unit Citation; two awards of the Meritorious Unit Citation; the Vietnamese Cross of Gallantry (silver) and the Department of the Navy Distinguished Public Service Award. Mr. Barnum is the past president of the Congressional Medal of Honor Society, Connecticut Man of the Year '67, presented Honorary Legum Doctorem St. Anselm College; Rotary Paul Harris Fellow; Abe Pollin Leadership Award '03, Marine Corps League "Iron Mike" Award, Order of the Carabao Distinguished Service Award, and Ted Williams Leadership Award. Mr. Barnum Holds a B.S. in Economics from St. Anselm College.

*Qualifications:* Mr. Barnum was first selected to be a director in 2009 because of his extensive distinguished government service at the Department of the Navy Executive level and his distinguished military career. Mr. Barnum brings expertise to the Board in the area of public policy initiatives as it relates to his knowledge of the Executive and Legislative Branch of the U.S. Government and his oversight of our governmental relations and policy initiatives on obesity related to the Company's products, protocols and clinical studies. Mr. Barnum serves on the Company's Compensation and the Nomination committees.

**Kevin G. Byrnes**, age 67, has been a director of the Company since 2013. Mr. Byrnes serves as Chairman for the Special Mergers & Acquisitions Committee and as a member of the Audit Committee. Mr. Byrnes has more than 40 years of financial experience working in the retail and commercial banking industries. He is currently Chairman of the Board of Bay Bank, with assets of approximately \$500 million and 12 branches located in the Baltimore metropolitan area. Mr. Byrnes served as President/COO and Director of Provident Bank from 2002 to 2009. Provident, acquired by M&T Bank in May 2009, was the largest independent financial institution in the Maryland and Northern Virginia marketplaces at that time, with \$6.5 billion in assets, 150 branches and 1,600 employees. Prior to Provident Bank, Mr. Byrnes spent 25 years with the Chase Manhattan Bank in various executive management positions. Mr. Byrnes began his career at Bankers Trust Co. in New York. He holds a BBA from Pace University.

*Qualifications:* Mr. Byrnes was selected based on his extensive financial experience given his long career in the banking industry. Because of his public-company experience and significant prior board experience, Mr. Byrnes is serving on the Company's Audit Committee and Chairs the Special Mergers & Acquisitions Committee.

**Jerry D. Reece**, age 75, has been a director of the Company since 2009. Mr. Reece is Chairman Emeritus of Reece & Nichols, a Berkshire Hathaway Affiliate, and from January 2002 until July 2013 he served as their Chief Executive Officer. Reece and Nichols is involved in residential and commercial real estate brokerage, mortgage origination, title insurance and insurance. Mr. Reece joined the United States Marine Corps and served in Hawaii and Vietnam as a first lieutenant. Following completion of active duty service, he continued his service in the Marine Corps Reserve until he retired with the rank of Colonel. His personal decorations include the Legion of Merit, the Navy Commendation Medal with Combat "V" and the Combat Action Ribbon. Mr. Reece was a past member of the board of the Marine Toys for Tots Foundation and was an Advisory Board Member of Commerce Bank, K.C., from 2003 to 2011. Mr. Reece holds a B.S. in Finance from the University of Oregon.

*Qualifications:* Mr. Reece first selected to be a director in 2009 because of his distinguished military service and his executive experience. Mr. Reece brings his leadership experience to the Board having previously served as chief executive officer of a corporation. Mr. Reece is a member of the Compensation Committee.

### **Current Class III Directors**

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**Barry B. Bondroff, CPA**, age 66, has been a director of the Company since 2008. Mr. Bondroff serves as a member of the Audit Committee, the Executive Committee and the Special Mergers & Acquisitions Committee. On July 22, 2013, the Board appointed Mr. Bondroff as Lead Director. Mr. Bondroff is an officer and director with Gorfine, Schiller & Gardyn, PA, a full-service certified public accounting firm offering a wide range of accounting and consulting services. Previously, he was a Senior Managing Director with SMART, a diverse team of business advisory professionals. Mr. Bondroff brings over 42 years of experience providing companies of all sizes and industries with practical and cost-effective accounting, assurance, tax, business, technology and financial advisory services. Prior to managing SMART, Mr. Bondroff was the Managing Director for Grabush, Newman & Co., P.A., which combined with SMART in May 2003. Mr. Bondroff began his career with Grabush Newman in 1970, and in 1976 became Officer and was promoted to Managing Director in 1982. He earned his Bachelor of Science degree in Accounting from the University of Baltimore. Additionally, Mr. Bondroff serves on the board for First Mariner Bank of Maryland, a NASDAQ listed company. He is active with First Mariner serving on the executive committee, loan committee, audit committee and as chairman of the compensation committee. In addition to his professional affiliations, Mr. Bondroff served on the Executive Committee for Israel Bonds and was a Director of Cycle Across Maryland. He has served on the National Jewish Medical and Research Center, the Jewish Center for Business Development and has assisted the Baltimore Symphony Orchestra in its fundraising efforts. In addition, Mr. Bondroff was a past President and Treasurer of the Edward A. Meyerberg Northwest Senior Center, and also served as a member of the Board for the Levindale Hebrew Geriatric Center and Hospital. Mr. Bondroff is currently a member of the audit committee of the Associated. He was Treasurer for Special Olympics of Maryland, his term ending in 2012 and was a Trustee for Stevenson University in Maryland. In May 2014 Mr. Bondroff was nominated as an Outstanding Director by the Baltimore Business Journal.

*Qualifications:* Mr. Bondroff was first selected as a director in 2008 because of his more than 36 years of experience as a CPA, and with corporate governance including serving on the board of another public company. He utilizes that experience as a financial expert and his elected position of Vice Chairman of the Board. His service on the Audit Committee and his availability as a local director in Baltimore provide for local oversight and practical consulting in the area of financial management, risk assessment and Sarbanes-Oxley regulations. Mr. Bondroff also serves on the Special Mergers & Acquisitions Committee and provides an extensive rolodex that assists Medifast's management team to find the best talent in the market to assist in our growth and development.

**Catherine T. Maguire**, age 64, a Sister of Mercy, has been a director of the Company since 2009. Sr. Macquire serves as a member of the Compensation Committee and Nomination Committee. Sr. Maguire has served as Executive Director at SILOAM, a Body, Mind, Spirit wellness center for the HIV/AIDS community, from 2011 to present. Prior to this, Sr. Maguire worked in AIDS Ministry within the prison system in Washington, DC. and served as a vocation director for her religious community for 8 years. She received a BS degree in Education/English in 1972, a MS degree in Library Science in 1974 both from Villanova University, and a MA degree in Theology with an emphasis in Pastoral Ministry & Spirituality in 1995 from St. Michael's College in Vermont. She served on the board of the National Religious Vocation Conference from 1990 to 1992.

*Qualifications:* Ms. Maguire was first selected as a director in 2009 for her extensive executive experience with not for profit human services organizations and her strong background in organizational ethics and human resources and personnel management. She has multiple advanced degrees and assists in developing the women executives of Medifast. As a result of her extensive management and human resources background she was elected to the Nomination Committee where she assists in screening and evaluating potential director candidates and insures the corporate values related to diversity are implemented in the Company and on the Board.

## INFORMATION CONCERNING OUR BOARD OF DIRECTORS

### Director Independence

We are required to have a majority of independent directors serving on our Board and may only have independent directors serving on each of our Audit, Compensation and Nomination, Committees pursuant to the listing rules of the New York Stock Exchange (the “NYSE”) and, with respect to our Audit Committee, the rules and regulations existing under the Securities Exchange Act of 1934, as amended (the “Exchange Act”).

Our Board undertook an annual review of our directors. The purpose of this review was to determine whether any relationships or transactions involving our directors (including their family members and affiliates) were inconsistent with a determination that such director is independent under the independence standards prescribed by the NYSE’s listing rules and our Corporate Governance Guidelines. Our Board also considered whether our Audit Committee members continue to satisfy the independence standards prescribed for audit committee members by the rules and regulations of the Exchange Act.

In making its determination, the Board considered not only the criteria for independence set forth in the listing rules of the NYSE but also any other relevant facts and circumstances that may have come to the Board’s attention, after inquiry, relating to transactions, relationships or arrangements between a director (or any member of their immediate family or any entity of which such director or one of their immediate family members is an executive officer, general partner or significant equity holder) on the one hand, and Medifast or any of its subsidiaries or affiliates, on the other hand, that might signal potential conflicts of interest, or that might bear on the materiality of a director’s relationship to Medifast or any of its subsidiaries. The Board considered the independence issue not merely from the standpoint of the director, but also from that of the persons or organizations with which the director is affiliated.

Based on its review, our Board determined that each of the non-employee directors qualifies as independent under the independence standards prescribed by the listing rules of the NYSE. Our Board also determined that Messrs. Bondroff, Byrnes Connolly, and McDaniel qualify as “independent” under the independence standards for audit committee members adopted by the SEC.

### Director Attendance

In 2014, our Board convened eight times, including three telephonic meetings, and our Board Committees held the following number of meetings: (i) Audit Committee — five meetings; (ii) Compensation Committee — five meetings; (iii) Nomination Committee — four meetings; and (iv) Special Mergers & Acquisitions Committee — three meetings.

Under our Corporate Governance Guidelines, directors are expected to regularly attend Board meetings and meetings of the Board committees on which they serve in person or by conference telephone, and all directors are expected to attend the Company’s annual meeting of stockholders. All of our current directors attended the 2014 Annual Meeting of Stockholders on June 17, 2014 and at least 90% of the aggregate of all meetings of the Board and the Committees on which they served in 2014.

### Board Leadership Structure

The Board is committed to strong corporate governance and board independence. The Board recognizes that having the same person serve in the Chief Executive Officer and Chairman positions can present an issue for some companies and some boards. However, the 2004 Blue Ribbon Commission of the National Association of Corporate Directors found that separation of the roles of chairman and chief executive officer was not necessary for effective board leadership. The Nomination Committee and the Board continue to consider the issue of board leadership and do not believe there is any material corporate governance benefit to separating these positions at this time. Our Chairman of the Board does not have any enhanced rights as a director, but has the same voting authority as any other director and the role of Chairman is one which is principally that of presiding at meetings of the Board and taking the initiative on establishing the proposed agenda for meetings of the Board, which is a role our senior management would play a significant part in regardless of which director serves as Chairman. Our Board continues to believe that the current structure is in our best interests and our stockholders’ best interests and allows Michael C. MacDonald, who serves as our Chairman and Chief Executive Officer, to focus on our strategy, business and operations.

The Board believes that there is no one best leadership structure model that is most effective in all circumstances. The Board retains the authority to separate the positions of Chairman and Chief Executive Officer in the future if such change is determined to be in our best interests and those of our stockholders. Thus, the Board remains flexible and committed to a strong corporate governance structure and board independence. The Board is committed to adopting corporate management and governance policies and strategies that promote our effective and ethical management. In this regard, the Board strongly believes that it should have maximum flexibility in deciding whether the offices of Chairman and Chief Executive Officer are combined or separate and, if separate, whether the Chairman should be an independent director or an employee.

### Lead Director

As noted above, the Board appointed Barry B. Bondroff, CPA, as Lead Independent Director effective July 22, 2013. The Lead Independent Director is responsible for facilitating and coordinating the activities of the independent directors. For the purpose of balancing the interests of the stockholders and management when the CEO also serves as the Chairman of the Board, the Lead Independent Director serves as Chairman for meetings of the independent directors separate from management. The Lead Independent Director also represents the best practices regarding corporate governance, provides independent leadership to the Board, and performs such other duties and responsibilities as the Board may determine.

The principal responsibilities of the Lead Independent Director are as follows:

- Act as the principal liaison between the independent directors of the Board and the CEO and Chairman of the Board;
- Develop the agenda for and preside at executive sessions of the Board's independent directors;
- Communicate to the Chairman any and all feedback from the executive sessions;
- Prepare minutes of the meeting of independent directors, share minutes with the full Board when appropriate, and deliver the minutes to the Company for filing with the minutes of the Company;
- Review and approve the agenda for the Board;
- Participate in the compensation committee's evaluation of the CEO's performance;
- Supervise the evaluations (self and otherwise) of the directors;
- Initiate a review of the independent Board members' performances, discuss the results with the Chairman and make recommendations for improvement, if required;
- Handle difficult and underperforming directors to improve the functionality of the Board;
- Assist in Board succession plans;
- Preside at all meetings at which the Chairman is not present;
- Retain the authority to call meetings of the independent directors;
- Subject to the authority of any committee of the Board, recommend to the Board the retention of advisors and consultants who report directly to the Board;
- As the Board determines, serve as a liaison and be available for consultation and direct communication with major stockholders;
- Make recommendations to the Board on behalf of the independent directors; and
- Undertake further such responsibilities that the independent directors may designate to the Lead Independent Director from time to time.

## **THE COMMITTEES OF THE BOARD**

The Board has four standing committees: the Audit Committee, the Compensation Committee, the Nomination Committee and the Special Mergers & Acquisitions Committee. The Board has determined that each of the members of the Audit Committee, Compensation Committee and Nomination Committee meets the standards of "independence" established by the NYSE as currently in effect. A description of each Board committee is set forth below.

### **Audit Committee**

The present members of the Audit Committee are Charles P. Connolly (Chairman), Barry B. Bondroff, Kevin G. Byrnes, and John P. McDaniel, all of whom have been determined by the Board to be independent within the meaning of SEC rules and the applicable NYSE listing rules. The Board has also determined that each member of the Audit Committee is "financially literate" as required by the NYSE rules and an Audit Committee Financial Expert within the meaning of the SEC rules based on, among other things, the experience of such member, as described under "Board of Directors".

The Audit Committee is responsible for, among other things, the review and oversight of the Company's performance with respect to its financial responsibilities and the integrity of the Company's accounting and reporting practices. The Audit Committee, on behalf of the Board, also appoints the Company's independent auditors, subject to stockholder ratification, at the annual meeting of stockholders.

The Audit Committee operates under the Audit Committee Charter adopted and approved by the Board. A copy of the charter can be obtained from the Company's website (<http://ir.medifastnow.com/>) or by sending a request to the Office of the General Counsel, Medifast, Inc., 3600 Crondall Lane, Suite 100, Owings Mills, Maryland 21117.

### **Compensation Committee**

The present members of the Compensation Committee are Carl E. Sassano (Chairman), Jerry D. Reece, Harvey C. Barnum, Jr., and Catherine T. Maguire, all of whom have been determined by the Board to be independent within the meaning of the applicable NYSE listing rules.

The Compensation Committee is responsible for, among other things, reviewing and approving annually the corporate goals and objectives applicable to the compensation of our chief executive officer and determining the compensation of our chief executive officer based on the achievement of these goals, approving the compensation of our other executive officers, overseeing our incentive compensation plans and equity-based plans, and reviewing and recommending changes to the Board with respect to director compensation. For information regarding our Compensation Committee, including its processes and procedures for determining executive compensation, see "How Compensation Decisions are Made – Role of Compensation Committee."

The Compensation Committee has the authority to delegate any of its responsibilities under its charter, along with the authority to take action in relation to such responsibilities, to one or more subcommittees as the Committee may deem appropriate in its sole discretion.

The Compensation Committee operates under the Compensation Committee Charter adopted and approved by the Board. A copy of the charter can be obtained from the Company's website (<http://ir.medifastnow.com/>) or by sending a request to the Office of the General Counsel, Medifast, Inc., 3600 Crondall Lane, Suite 100, Owings Mills, Maryland 21117.



## **Nomination Committee**

The present members of the Nomination Committee are Rev. Donald Francis Reilly, OSA (Chairman), Harvey C. Barnum, Jr., and Catherine T. Maguire, all of whom have been determined by the Board to be independent within the meaning of the applicable NYSE listing rules.

The Nomination Committee is responsible for, among other things, recommending to the Board potential director nominees for election to the Board, recommending to the Board directors to serve on the various Board committees, advising the Board with respect to Board composition, procedures and committees, developing and recommending to the Board corporate governance principles applicable to the Company, and evaluating and making recommendations to the Board regarding the compensation of directors.

The Nomination Committee operates under the Nomination Committee Charter adopted and approved by the Board. A copy of the Charter can be obtained from the Company's website (<http://ir.medifastnow.com/>) or by sending a request to the Office of the General Counsel, Medifast, Inc., 3600 Condall Lane, Suite 100, Owings Mills, Maryland 21117.

*Director Qualifications.* Director nominees are selected on the basis of, among other things, experience, knowledge, skills, expertise, integrity, ability to make independent analytical inquiries, understanding the Company's global business environment and willingness to devote adequate time and effort to Board responsibilities so as to enhance the Board's ability to oversee and direct the affairs and business of the Company.

*Diversity.* The Company does not maintain a separate policy regarding the diversity of the Board. However, the charter of the Nomination Committee requires that the Committee review the composition of the Board to ensure it has the "appropriate balance" of experience, skills, expertise and diversity for the Board as a whole. Consistent with these guidelines, both the Nomination Committee and the full Board seek director nominees with distinct professional backgrounds, experience and perspectives so that the Board as a whole has the range of skills and viewpoints necessary to fulfill its responsibilities. As part of our annual Board self-evaluation process, the Board evaluates whether or not the Board as a whole has the skills and backgrounds for the current issues facing the Company. The Board also evaluates its effectiveness with regard to specific areas of expertise.

*Director Nomination Process.* Pursuant to our Corporate Governance Guidelines, our Nomination Committee reviews the qualifications of proposed director nominees to serve on our Board and recommends director nominees to our Board for election at the Company's annual meeting of stockholders. The Board proposes a slate of director nominees to the stockholders for election to the Board, using information provided by the Nomination Committee.

In certain instances, a third party may assist the Nomination Committee or the Board in identifying potential director nominees. The Nomination Committee also considers potential nominations for director provided by the Company's stockholders and submits any such suggested nominations, when appropriate, to the Board for approval. Stockholder nominees for director are evaluated using the same criteria described above. Stockholders wishing to recommend persons for consideration by the Nomination Committee as nominees for election to the Board can do so by writing to the Office of the Corporate Secretary, Medifast, Inc., 3600 Crondall Lane, Suite 100, Owings Mills, Maryland 21117 and providing the information and following the additional procedures set forth in the Bylaws.

## **Special Mergers & Acquisitions Committee**

The present members of the Special Mergers & Acquisitions Committee are Kevin G. Byrnes (Chairman), Barry B. Bondroff, Charles P. Connolly and John P. McDaniel.

The Special Mergers & Acquisitions Committee is responsible for reviewing and overseeing all mergers, acquisitions, investment transactions and similar transactions being considered by the Company and making recommendations to the Board.

The Special Mergers & Acquisitions Committee operates under the Special Mergers & Acquisitions Committee Charter adopted and approved by the Board. A copy of the charter can be obtained from the Company's website (<http://ir.medifastnow.com/>) or by sending a request to the Office of the General Counsel, Medifast, Inc., 3600 Crondall Lane, Suite 100, Owings Mills, Maryland 21117.

## **COOPERATION AGREEMENT WITH STOCKHOLDER**

As previously disclosed, the Company entered into a Cooperation Agreement, dated April 3, 2015 (the "Cooperation Agreement"), with Engaged Capital, LLC, Engaged Capital Master Feeder I, L.P., Engaged Capital Master Feeder II, L.P., Engaged Capital I, L.P., Engaged Capital I Offshore, LTD, Engaged Capital II, L.P., Engaged Capital II Offshore LTD., Engaged Capital Holdings, LLC and Glenn W. Welling (collectively, the "Engaged Group"). Pursuant to the terms of the Cooperation Agreement, the Company agreed to (i) amend the Amended and Restated Bylaws (the "Bylaws") to, commencing with the 2015 annual meeting of stockholders, eliminate the classification of the board and provide for the annual election of all directors to the company's board of directors (the "Board") and (ii) adopt a resolution, effective as of the 2015 annual meeting of stockholders, to decrease the size of the Board from twelve directors to seven directors (subject to increase to nine directors when the additional independent directors have been elected or appointed).

The foregoing is not a complete description of the Cooperation Agreement. For a further description of the Cooperation Agreement and a copy of the Cooperation Agreement, please see our Current Report on Form 8-K filed with the SEC on April 6, 2015.

## **EXECUTIVE OFFICERS**

Except for Michael C. MacDonald, Jason Groves and Margaret Sheetz who are presently also directors of the Company, the biographical information of the Company's current executive officers is below.

**Timothy G. Robinson, CPA**, age 52, has served as the Company's Chief Financial Officer since February 2013. Prior to joining the Company, Mr. Robinson was Vice President, Business Operations for Canon Business Solutions, Inc., from 2008 to 2013, where he served as a key member of the executive team for this national office products subsidiary of Canon U.S.A. From 1995 to 2008, Mr. Robinson was Vice President, Finance & Administration for Canon Business Solutions-East, Inc. Mr. Robinson was Controller of Dupli-Fax, Inc. from 1989 to 1995 and was a Senior Emerging Business Consultant for Deloitte & Touche from 1985 to 1989. Mr. Robinson received his Bachelor of Science degree in accounting from Villanova University.

**Mehrnaz Mona Ameli**, age 44, is the President of Take Shape For Life and is responsible for providing day-to-day leadership and direction to Take Shape for Life in order to optimize performance and profitability. Ms. Ameli's focus is on helping to develop and implement effective and creative plans for the long-term growth of the business and providing leadership, direction, and coaching to Field Marketing, Field Operations, and Field Business development. She is also responsible for driving TSFL's strategic initiatives while insuring their alignment with Medifast's overall strategic goals.

Ms. Ameli brings over 20 years of progressive and successful executive leadership, management, and cross functional international expertise in the direct selling industry covering all major regions of the world: North America, Western and Eastern Europe, Middle East, Asia Pacific and Latin America. Before joining Medifast, Ms. Ameli held the role of General Manager, United States Division of Belcorp, the ninth largest direct selling company in the world with \$2B in sales across 15 markets. Prior to joining Belcorp, Ms. Ameli was the Vice President of Marketing & Business Development at CGT in California where she managed the development and execution of their business strategy, market segmentation, branding, and budget and product portfolio. In addition, Ms. Ameli has had leadership positions at Shaklee Corporation, Natural Alternatives International, and Herbalife.

Ms. Ameli has a proven track record of results-driven leadership in opening new markets as well as growing and enhancing sales and profitability for both established companies as well as start-ups. Her expertise in building multi-national consumer packaged goods brands, developing new products, and expanding new business units internationally with a special focus in the direct-to-consumer and direct selling industries makes her a valuable addition to the Medifast Team.

Ms. Ameli serves on the Direct Selling Association Diversity Council and was honored in 2012 as one of the most influential women in the direct selling industry by Direct Selling News. She earned her Diploma of Economics and Master of Business Management from the University of Paris - Dauphine.

**Donald Gould**, age 56, has served as the Company's Executive Vice President for Information Technology since January 2011. Prior to joining the Company, Mr. Gould worked in information technology at Godiva Chocolatier, Inc. and Campbell Soup Company. Mr. Gould has 30 years of information technology experience with the majority being in the consumer products industry. Mr. Gould has managed a variety of projects both in the United States and internationally, mostly focusing on supply chain and retail operations. Mr. Gould holds a Bachelor of Science degree from Slippery Rock University and a Master of Business Administration degree from Saint Joseph's University.

**Brian Kagen**, age 42, has served as the Company's Executive Vice President & Chief Marketing Officer since August 2012. Prior to this he served as the Company's Executive Vice President, Marketing, Sales & Business Development since June 2011. In his current role, Brian oversees all marketing across the organization, driving day-to-day execution and initiating long-term plans to build awareness, drive revenue and profit growth all while working to expand the Medifast brand. Brian's responsibilities include brand strategy, product marketing, channel management, creative services, pricing and promotion, consumer insights, public relations, social media, and marketing communications. Brian came to Medifast in June 2011 after a 14-year career with Fortune 500 Company, Stanley Black & Decker, where he held the position of Global Vice President of Marketing. In this position, Brian was charged with leadership for the company's largest consumer products business segment. Brian earned his Bachelor of Arts degree from the University of Pennsylvania and his Masters of Business Administration degree from the Sellinger School of Business at Loyola University of Maryland where he serves as a guest lecturer. Brian is a graduate of Leadership Baltimore County and is active in the community as a youth football and basketball coach.

**Joseph Kelleman**, age 60, is the Vice President of Finance, Corporate Controller. Mr. Kelleman joined Medifast as Director of Finance – Supply Chain in February 2012 with over 30 years of experience in finance at Stanley Black & Decker, Inc. Prior to joining Medifast, Mr. Kelleman was the Global Operations Controller – CDIY Business at Stanley Black & Decker, Inc. from 2010 to 2012. From 2009 through 2010, Mr. Kelleman held the position of Director of Finance – Asian Operations having financial oversight for all Power Tool manufacturing in Asia and the global sourcing operations for the Company. From 2001 to 2009, Mr. Kelleman held the position of Director of Finance for the North American Power Tool Commercial Operations of Black & Decker and prior to that role held numerous positions of increasing responsibility over his career within the company. Mr. Kelleman received his Bachelor of Science Degree in Accounting from Mount St. Mary's University.

## **CODE OF CONDUCT AND BUSINESS ETHICS AND CORPORATE GOVERNANCE GUIDELINES**

Our Board has adopted a corporate Code of Conduct and Business Ethics applicable to our directors, officers, including our principal executive officer, principal financial officer and principal accounting officer, and employees, as well as Corporate Governance Guidelines, in accordance with applicable rules and regulations of the SEC and the NYSE. Each of our Code of Conduct and Business Ethics and Corporate Governance Guidelines are available on our website at <http://ir.medifastdiet.com/> by following the links through "Investor Relations" to "Corporate Governance."

Any amendment to, or waiver from, a provision of the Company's Code of Conduct and Business Ethics with respect to the Company's principal executive officer, principal financial officer, principal accounting officer or controller will be posted on the Company's website, <http://ir.medifastdiet.com/>.

## SECTION 16(A) BENEFICIAL OWNERSHIP REPORTING COMPLIANCE

Section 16(a) of the Exchange Act requires the Company's directors and executive officers and persons who beneficially own more than ten percent of a registered class of the Company's equity securities to file with the SEC initial reports of ownership and reports of changes in ownership of equity securities of the Company. Directors, officers and greater-than-ten-percent beneficial owners are required by SEC regulations to furnish the Company with copies of all Section 16(a) forms filed by them. We have reviewed copies of reports provided to us, as well as other records and information. Based on that review, we concluded that all reports were timely filed in 2014, except as follows: (i) Mr. Barnum had 2 late Form 4 reports, which resulted in 2 stock grants by the Company (for an aggregate of 1,101 shares) being untimely reported; (ii) Mr. Bondroff had 2 late Form 4 reports, which resulted in 2 stock grants by the Company (for an aggregate of 1,201 shares) being untimely reported; (iii) Mr. Byrnes had 1 late Form 4 report, which resulted in 1 stock grant by the Company for 750 shares being untimely reported; (iv) Mr. Connolly had 2 late Form 4 reports, which resulted in 2 stock grants by the Company (for an aggregate of 1,224 shares) being untimely reported; (v) Mr. Gould had 2 late Form 4 reports, which resulted in 1 stock grant by the Company for 1,875 shares and 1 forfeiture of shares for tax withholdings of 657 shares being untimely reported; (vi) Mr. Kagen had 2 late Form 4 reports, which resulted in 1 stock grant by the Company for 1,875 shares and 1 forfeiture of shares for tax withholdings of 657 shares being untimely reported; (vii) Mr. MacDonald had 2 late Form 4 reports, which resulted in 1 stock grant by the Company for 30,000 shares and 1 forfeiture of shares for tax withholdings of 2,334 shares being untimely reported; (viii) Ms. Maguire had 2 late Form 4 reports, which resulted in 2 stock grants by the Company (for an aggregate of 915 shares) being untimely reported; (ix) Mr. McDaniel had 2 late Form 4 reports, which resulted in 2 stock grants by the Company (for an aggregate of 1,101 shares) being untimely reported; (x) Ms. Mills had 3 late Form 4 reports, which resulted in 1 stock grant by the Company for 1,094 shares and 2 forfeiture of shares for tax withholdings (for an aggregate of 1,083 shares) being untimely reported; (xi) Mr. Reece had 2 late Form 4 reports, which resulted in 2 stock grants by the Company (for an aggregate of 1,142 shares) being untimely reported; (xii) Mr. Reilly had 1 late Form 4 report, which resulted in 1 stock grant by the Company for 750 shares being untimely reported; (xiii) Mr. Robinson had 2 late Form 4 reports, which resulted in 1 stock grant by the Company for 3,750 shares and 1 forfeiture of shares for tax withholdings of 467 shares being untimely reported; (xiv) Mr. Sassano had 2 late Form 4 reports, which resulted in 2 stock grants by the Company (for an aggregate of 915 shares) being untimely reported; and (xv) Ms. Sheetz had 7 late Form 4 reports, which resulted in 1 stock grant by the Company for 15,000 shares, 1 forfeiture of shares for tax withholdings of 1,167 shares, 1 initial reporting of indirect ownership of 95 shares, 2 indirect ownership stock grants by the Company (for an aggregate of 5,875 shares) and 2 indirect ownership forfeiture of shares for tax withholdings (for an aggregate of 2,071 shares) being untimely reported.

## ITEM 11. EXECUTIVE COMPENSATION

### EXECUTIVE COMPENSATION

#### Compensation Discussion and Analysis ("CD&A")

##### Introduction

This Compensation Discussion and Analysis discusses our 2014 compensation program as it relates to our "named executive officers." For 2014, our named executive officers are:

- ▶ Michael MacDonald – our Chief Executive Officer and Chairman of the Board
- ▶ Timothy Robinson – our Chief Financial Officer
- ▶ Margaret Sheetz – our President and Chief Operating Officer
- ▶ Brian Kagen- our Executive Vice President, Chief Marketing Officer
- ▶ Don Gould- our Executive Vice President of Technology
- ▶ Jeannette Mills – our former Executive Vice President, Take Shape for Life

##### Executive Summary

2014 was a year of transition for our company. We took actions during 2014 that we believe will position us for long-term profitability and growth. During 2014, we transitioned company-owned centers to a franchise model and expanded our product line. However, due in part to these actions, our revenue and net income decreased over 2013 levels, and certain other financial results did not reach our budgeted levels for 2014. Specifically, our financial results for 2014 included one-time charges related to our exit from the MWCC corporate center model and the sale of 41 centers to existing franchise partners, as well as the write-off of a franchise loan and certain legal expenses. Despite these results, we have delivered strong returns for our shareholders, as our one and three-year total stockholder return are approximately 28% and 144%, respectively.

We believe that it is important, during this time of transition, to retain the talented executives who can lead us to become a stronger company and to deliver value to our shareholders, but also to ensure that our executives are rewarded in line with the results that they deliver. In light of these challenges and of the negative results of the "say on pay" advisory vote held at our annual meeting of stockholders in 2014, we have focused in 2014 on assessing and improving our executive compensation policies and programs to effectively achieve our compensation goals: to attract, retain and motivate these highly qualified executives, and to align their interests with the interests of our stockholders. This assessment has resulted in the implementation of several new policies that help to align executive interests with the interests of our stockholders, which will ensure that our executives continue to be focused on long-term results. Our assessment of our compensation programs has continued into 2015, and we expect that we will continue to make changes to our programs to further achieve our compensation goals.

We spent a majority of the 2014 year following the “say on pay” advisory vote analyzing our compensation programs, and based on our analysis and the feedback we received, we made changes that we believe were necessary to strengthen the overall executive compensation program and address the concerns of our stockholders. The following is a summary of compensation actions taken during 2014.

2014 Actions	
✓	Amended our 2012 Share Incentive Plan (the “2012 Plan”) to provide for a double-trigger in the event of a Change in Control on future grants of equity and equity-related awards.
✓	Amended our 2012 Plan to provide that dividends paid on performance-based restricted shares will only be paid at the time and to the extent the underlying restrictions lapse.
✓	Corrected actions taken in 2013 and 2014 in which equity and equity-based awards were granted in excess of the limits in the 2012 Plan, and improved our internal controls with respect to equity grant practices.
✓	No new grants of restricted shares to any of our named executive officers.

In addition to the above actions, we have continued our policies which are what we consider to be our ongoing “best practices” with respect to compensation.

Compensation Best Practices	
✓	We do not provide excessive perquisites to our executives.
✓	Our executives will not be entitled to tax gross-ups under section 4999 of the Internal Revenue Code of 1986, as amended, if there is a change in ownership or control of Medifast.
✓	We do not provide supplemental retirement benefits to our executives.
✓	We do not have employment agreements with our executives.
✓	We provide only limited severance benefits to our CEO, President, and CFO.
✓	Approximately 81% of the target compensation for our CEO in 2014 was based on company performance or the performance of our stock.
✓	The 2012 Plan prohibits repricing of underwater stock options without stockholder approval.

#### 2014 Say on Pay Advisory Vote Results and 2014 Compensation Actions

As required by the Dodd-Frank Wall Street Reform and Consumer Protection Act (“Dodd-Frank”), we held a “say on pay” advisory vote on executive compensation at our annual meeting of stockholders in 2014. At that meeting, only 28% of our stockholders voted in favor of our executive compensation proposal. Since that time, we have conducted an in-depth review of our compensation policies and programs, and have adopted several new policies to promote good governance and an alignment of the interests of our executives with our stockholders. We have also engaged in discussions with several of our stockholders, in order to better understand their concerns with our executive compensation policies and programs. These discussions were informative, and assisted us in understanding how our compensation programs can be better structured and how we can improve the understanding of our compensation programs by our stockholders. The chart below summarizes the main concerns raised by our stockholders and how we have responded to such concerns.

Stockholder Feedback	Medifast Response
▶ Annual cash bonus awards assumed to be discretionary.	▶ Our annual cash bonus awards are made pursuant to a plan with pre-established performance goals based on our financial performance. We have clarified our disclosure regarding the annual cash bonus awards.
▶ Restricted share awards to our CEO in 2013 were thought to be excessive.	▶ The restricted share awards granted to our CEO in 2013 were one-time grants – one as a reward for performance during 2012 and in consideration of his taking on the role of CEO, and the second as a retention award with a 7-year vesting schedule – and we have not historically granted restricted share awards on an annual basis.
▶ Perceived disconnect between CEO pay and Company performance.	▶ We have enhanced our disclosure of how we link CEO pay to performance, and we did not grant new restricted share awards to our CEO during 2014.
▶ Lack of stock ownership guidelines.	▶ We are currently considering stock ownership guidelines.
▶ Lack of a clawback policy.	▶ We are currently considering a clawback policy.
▶ Lack of anti-pledging policy.	▶ We are currently considering an anti-pledging policy.

The discussions we have engaged in with our stockholders have helped us understand the concerns with our compensation programs, and we hope to keep this dialogue open during our ongoing assessment of our compensation programs. Our “say-on-pay” advisory vote on executive compensation is required to be held no later than at our annual meeting of stockholders in 2017.

### Compensation Philosophy

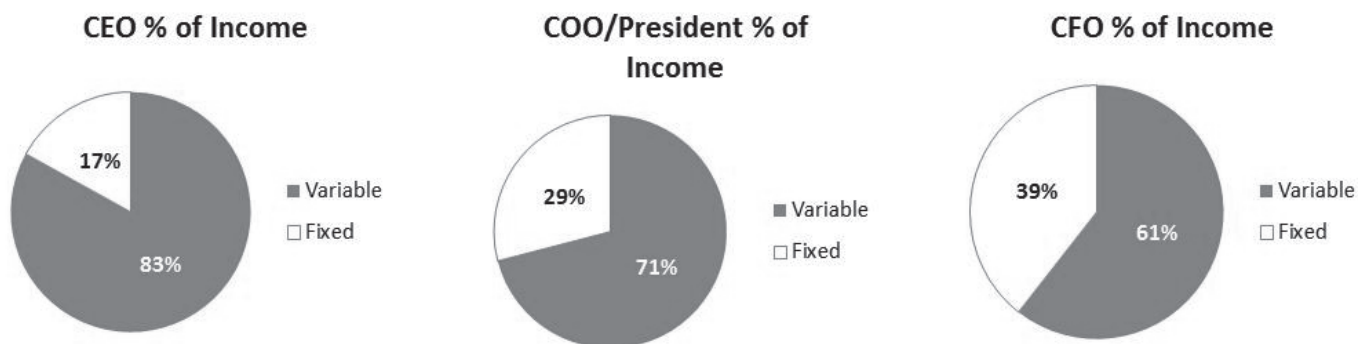
In today’s rapidly changing marketplace, it is important to locate and secure the talented individuals who will be able to steer our company to long-term success and to provide positive returns for our stockholders. Our executive compensation program is designed to attract, retain and motivate these highly qualified executives, and to align their interests with the interests of our stockholders.

- ▶ *Attract:* We compete with other companies in our industry for talent, and many of these companies are much larger and have higher revenues. We offer our executives competitive compensation packages, including sign-on awards, so that we can attract the talent needed to deliver quality results and position our company to succeed now and into the future.
- ▶ *Retain:* A stable management team benefits our strategic long-term goals, and ensures that we are managed by executives who have a deep knowledge and understanding of our company and the ability to make well informed decisions. We retain our executives by providing them competitive on-going pay packages, and tying a portion of their compensation to their long-term service with the company.
- ▶ *Motivate:* We believe in pay for performance. A large percentage of our executives’ compensation is based on our performance. The only fixed element of compensation for our executives is base salary, with the remainder of compensation based on our financial performance (our executive cash bonus plan and performance-based deferred shares) and the value of our stock (the retention awards granted to our senior executives periodically, stock options granted to our Executive Vice Presidents annually, and performance-based deferred shares). Placing the value of a portion of our executives’ pay at risk ensures that our executives will work to achieve our stated business objectives and create stockholder value.
- ▶ *Align Interests with Stockholder Interests:* It is vital for our executives to make decisions that will create positive results for our stockholders. We believe that the best way to ensure our executives understand the pressing concerns of stockholders is for our executives to be stockholders themselves, and to have a meaningful proportion of their compensation paid in shares. Since the value of the executive’s compensation is dependent on our share price, the executive is motivated to increase long-term company value.

### Pay for Performance

Executive compensation at Medifast is focused on executive performance keyed to results. We provide fair and equitable compensation to our executives by combining conservative base pay, annual incentive awards paid based on our performance (consisting of both cash and performance-based deferred shares), and stock-based long-term incentives. The Compensation Committee has designed our executive compensation program so that performance-based and other variable pay elements (annual incentive awards and equity-based awards) constitute a significant portion of the targeted annual compensation that each executive is eligible to earn during the year. The total amount of compensation each executive could receive with respect to a fiscal year is variable based on our performance, which motivates our executives to focus on creating value for our stockholders.

The following charts demonstrate that these performance-based and variable pay elements comprised at least 80% of the targeted annual compensation for the Chief Executive Officer, 70% of the targeted annual compensation for the Chief Operating Officer/President, and 60% of the targeted annual compensation for the Chief Financial Officer.



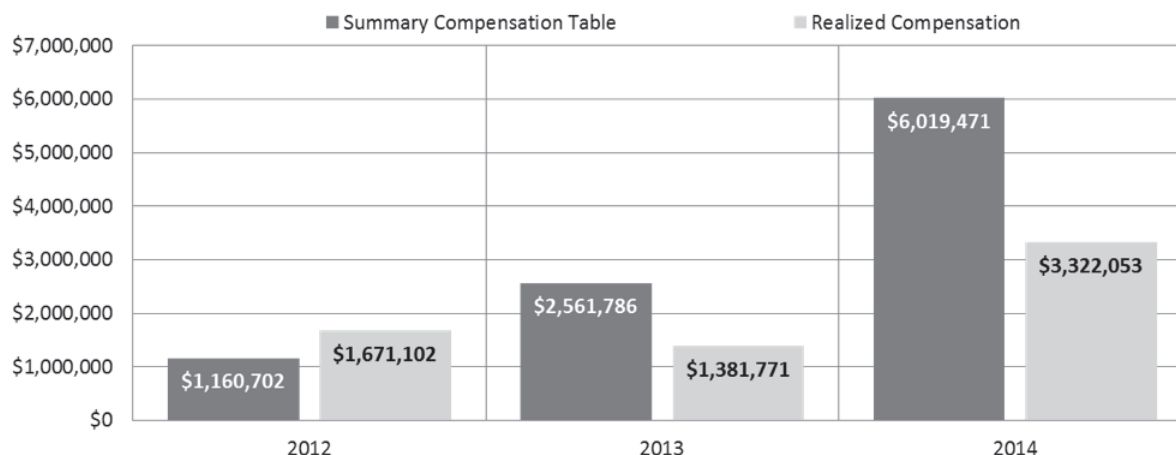
For purposes of these charts, “fixed” compensation is the executive’s base salary, and “variable” is a combination of the target cash bonus, the grant date fair value of the deferred shares granted in connection with 2014 performance (assuming performance at the target level), and the grant date fair value of the portion of the restricted share awards that our CEO, President and CFO each received in 2013 that were scheduled to vest during 2014. We have included the grant date fair value of the restricted share awards granted in 2013 that vested during the 2014 because this is the amount the Compensation Committee took into consideration for compensation planning purposes when it granted the restricted share awards.

### Realized Compensation

The amounts included in the Summary Compensation Table are calculated based on SEC regulations and do not reflect the actual amounts that our named executive officers will receive during the year – the totals in the Summary Compensation Table are much higher than the amounts each named executive officer will actually receive in the applicable year. The amounts included in the Summary Compensation Table are particularly misleading with respect to restricted share awards granted to our named executive officers, since the full grant date fair value of the awards are reported in the year of grant, and we have not historically granted restricted share awards to our named executive officers on an annual basis. Instead, we have historically made one-time grants of restricted share awards that vest over a long vesting period. As a result, our Summary Compensation Table is required to show a larger “total compensation”

in the year in which a restricted share award is granted, and lower “total compensation” in the years in which no such awards are made. To illustrate the disconnect between the amounts reported in the 2014 Summary Compensation Table and the actual amounts realized by our CEO, the table below shows the amounts realized by our CEO, Michael MacDonald, in the applicable year, and the amount reported in the 2014 Summary Compensation Table.

**Realized Compensation**

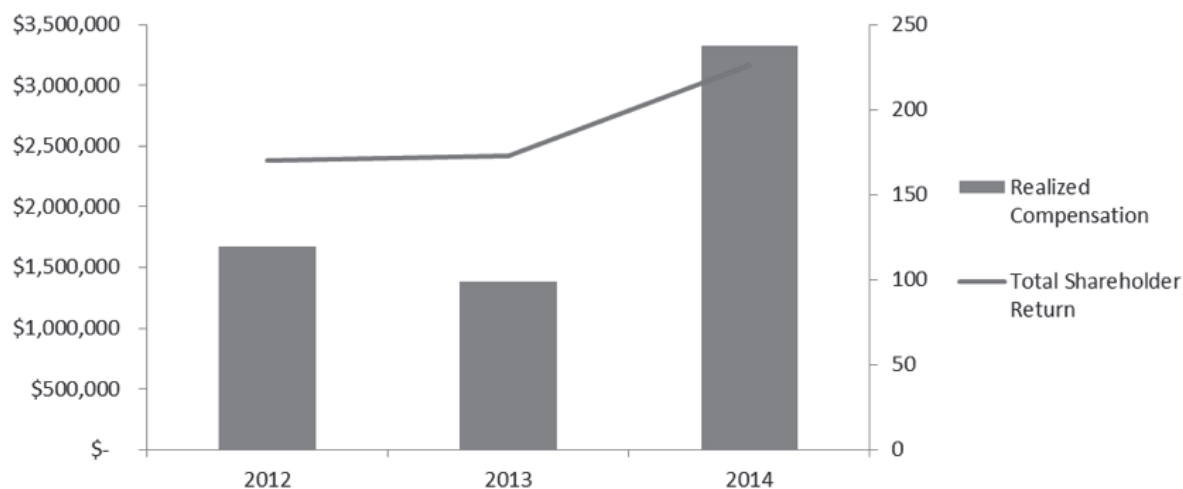


The amounts in the “Summary Compensation Table” columns are as reported in the Total column of the 2014 Summary Compensation Table. The amounts in the “Realized Compensation” column include (a) base salary, (b) actual cash bonus earned for the applicable year, (c) the value on vesting of deferred shares that vest and are paid during the applicable year (which relate to performance in the prior year), (d) the value on vesting of restricted shares that vest during the year, (e) the value realized from the exercise of stock options during the year, and (f) all other compensation paid (or earned) during the applicable year (which is included in the “All Other Compensation” column of the Summary Compensation Table for the applicable year). The Summary Compensation Table amounts for 2013 and 2014 reflect the re-grant of certain restricted share and deferred share awards in 2014, discussed below under “Long-Term Compensation Correction During 2014.”

*CEO Compensation and Company Results*

Our focus on pay for performance can best be demonstrated through a comparison of our total stockholder return and our CEO’s realized pay over the same period. Since our CEO took the position in February 2012, we have delivered excellent returns for our stockholders. Our one and three-year total stockholder return are approximately 28% and 144%, respectively. The realizable pay for our CEO is directly linked to the value of our stock and to the positive returns for our stockholders. Due to the increase in the value of our stock, our CEO’s realized compensation for this period has increased as well.

To demonstrate the linkage between CEO pay and Company performance, the chart below compares our CEO’s realized pay (as disclosed above) for the last three fiscal years to our total stockholder return for that period. The total stockholder return is based on the amount that a stockholder would have at the end of each fiscal year, assuming \$100 was invested in the beginning of 2012.



## How Compensation Decisions are Made

### *Role of Compensation Committee*

The Compensation Committee is responsible for developing and approving the executive compensation program for all executive officers, including the named executive officers, and for reviewing, approving and, where appropriate, recommending to the full Board for approval, our incentive compensation and equity-based plans. The Compensation Committee is also responsible for the creation and periodic review of the overall executive compensation philosophy, the analysis and assessment of any material risk to the Company related to our compensation programs, and the determination of the components and levels of executive compensation.

### *Role of Management*

The Compensation Committee works closely with members of our management team in designing our executive compensation programs, including Mr. MacDonald, our CEO, and Mr. Robinson, our CFO and Jeanne Uphouse, Executive Vice President, Human Resources. Our management team evaluates the performance of our executives (other than our CEO), and makes recommendations as to the compensation levels of our executives and the goals for our short-term incentives. The advice of our management is important in order for the Compensation Committee to design compensation programs that align to corporate goals and our strategic direction. All compensation decisions are made by the Compensation Committee in its sole discretion.

### *Use of Peer Group*

The Compensation Committee measures the total direct compensation (which includes base pay, annual cash and stock-based incentives and stock-based long-term incentives) of each executive against other organizations in the general weight-loss industry. There is a wide variety of diet products and programs which comprise the weight loss industry, which include a wide variety of commercial weight loss programs, pharmaceutical products, weight loss books, self-help diets, dietary supplements, appetite suppressants and meal replacement shakes and bars. Some of our competitors are substantially larger than we are, and have considerably greater financial resources than we have. Our ability to remain competitive depends, in significant part, on our success in recruiting and retaining executive leadership with an attractive compensation package. The Company targets total direct compensation for each executive near median for organizations in the general weight-loss industry, with the mix of pay (base pay, annual cash incentives and long-term incentives) designed to reflect a strong bias towards pay for performance by placing a majority of target compensation at risk.

Each year, the Compensation Committee compares the total direct compensation for our executives to compensation paid by an industry peer group approved by the Compensation Committee. The criteria used to identify the peer group were: (1) industry — Medifast competes for talent with other healthy living and wellness companies and general weight-loss industry companies of similar and larger size; and (2) financial scope — our management talent should be compensated similar to that of companies of a similar and larger size in terms of revenues.

For 2014, the peer group was comprised of the following five corporations. The peer group revenue range is from \$214 million to \$4.9 billion.

- NutriSystem Inc.,
- Nutraceutical, Inc.,
- Herbalife Ltd.,
- USANA Health Sciences, and
- Weight Watchers International Inc.

### *Role of Compensation Consultants and Survey Data*

During Fiscal 2013, the Compensation Committee engaged an independent executive compensation consultant firm, Keating Advisors, LLC. (“Keating”), to advise and make recommendations regarding Medifast’s executive compensation program. Keating provided advice with respect to compensation through June 2014. The Compensation Committee has evaluated the independence of Keating and concluded that no conflict of interest exists that would prevent Keating from independently advising the Compensation Committee.

In addition to advice provided by Keating the Compensation Committee utilized the following materials, along with other resources and tools, to render compensation decisions for 2014: (i) surveys and reports of executive compensation paid by other public companies with characteristics similar to ours and (ii) professionally published surveys from Towers Watson, WTPF Compensation Survey, Direct Selling Association Management Compensation & Benefits Survey, Economic Research Institute Salary Assessor, and HRA-NCA. These materials and other resources help to provide us with solid benchmarks for each component of our executive compensation package as well as a general understanding of best practices of companies in our industry who are competing for with us for top talent.

## Elements of Executive Compensation

Our executive compensation program has three main elements: base salary, annual incentive bonus (cash and equity), and long-term equity awards.

### *Base Salary*

Base salary is the only element of fixed compensation that we provide to our executives. Our base salary determinations principally reflect the skills and performance levels of our individual executives, the needs of the Company, and pay practices of comparable public companies within the general health and wellness diet industry.

It is not our policy to pay our executive officers at the highest base salary level. Instead, we establish executive base salaries below the midpoint level relative to our peers. The Compensation Committee evaluates our executives' base salaries on an annual basis and asks for input and recommendations from the CEO and CFO and then considers (i) the particular executive's role and responsibilities; (ii) his or her level of performance, achievements, and contributions to the Company; (iii) current market data and salary levels for such executive's particular position; and (iv) the total compensation paid to such executive. We believe this policy sets a prudent and fiscally responsible tone for the Company's overall base salary compensation program.

In 2014, the salary increases were based on Keating engaged in a general market study of base salaries in our industry, and base salaries were adjusted to be in line with the median salary level as determined in the study. Base salary for 2014 for each named executive officer is illustrated below:

Name	2014 Base Salary
Mr. MacDonald	\$635,400
Mr. Robinson	\$317,700
Ms. Sheetz	\$423,600
Mr. Kagen	\$266,400
Mr. Gould	\$220,000
Ms. Mills	\$242,050

### *Annual Incentive Bonus*

Our annual incentive bonus awards are paid to participants in a combination of cash and performance-based deferred shares. These bonus awards principally reflect the Company's financial performance and achievement of corporate objectives approved by our Board. The executive cash bonus plan and the performance-based deferred share awards are designed to reward our executives for the achievement of shorter-term financial goals, predominantly revenue growth, profitability, and cash flow. In consultation with the Chairman and CEO, the Compensation Committee evaluates, adjusts and approves the target cash bonus and the amount of deferred shares to be granted to each executive officer. In determining the target amounts for each executive, the Compensation Committee and the Chairman and CEO consider each executive's contribution to current and long-term corporate goals, and value in the labor market.

The financial targets for the annual cash and equity incentives are set based on the annual budget approved by the Board during the first quarter of 2014, and are intended to reward executives if the financial performance projections are met.

For 2014, the financial targets were based on corporate revenue, income before tax, and cash flow. The performance targets were the same for both the cash and the deferred share components of the annual incentive bonus. However, as discussed below, the deferred shares have an additional service requirement, and only vest if the executive remains employed for an additional year after the end of the performance period.

The Compensation Committee set the target for pre-tax profit at \$40.7 million, the target for corporate revenue at \$388.2 million, and net increase in cash and cash equivalents at \$26.2 million (excluding adjustments from / to investment accounts, treasury stock repurchases and change in year over year deferred income tax and Income tax payable balances versus last year). The target performance level is set to promote solid performance in line with our budget for the year. The executive is eligible to receive an amount greater than the target if performance is greater than the target level. The components of the incentive plan outlined below are in place to focus the organization towards achieving growth/improved market share, shareholder value, and the effective use of cash.

The financial targets for annual cash and equity incentives are divided into three components as follows:

- *Corporate Revenue:* 25% of the total target payout is based on the achievement of our corporate revenue target. For 2014, the corporate revenue target was \$388.2 million in net revenue, an increase of 8.8% over 2013 net revenue of \$356.9 million.
- *Income Before Tax ("IBT"):* 50% of the total target payout is based on a pre-tax profit target of \$40.7 million, an increase of 19.0% over 2013 IBT of \$34.2 million.
- *Cash Flow:* 25% of the total target payout is based on an increase in cash and cash equivalents of \$26.2 million. Cash flow is defined as total cash generated adjusted for treasury stock repurchases and the change in year over year deferred income tax and income tax payable year end balances versus last year or adjustments from/to investment accounts.



Each performance goal was assigned a target, as described above, along with a threshold level and a maximum level, which increase or decrease the payout for executives. The financial targets, along with the threshold and maximum level for each of these goals and the actual performance are set forth below.

Goal	Percentage of Total Bonus Payout	Threshold	Target	Maximum for EVPS	Maximum for CEO, President and CFO
Net Revenue	25%	\$340 million	\$388.2 million	\$402.8 million	\$410.8 million
Income Before Tax <sup>(1)</sup>	50%	\$34 million	\$40.7 million	\$48 million	\$52.0 million
Net Increase in Cash and Cash Equivalents <sup>(2)</sup>	25%	\$21.5 million	\$26.2 million	\$30.2 million	\$34.2 million

(1) Income Before Tax, for purposes of determining payouts under the executive cash bonus plan, may be adjusted for certain non-recurring items as approved by the Compensation Committee.

(2) Defined as total cash generated adjusted for treasury stock purchases and the change in year over year deferred income tax and income tax payable year end balances versus 2013 or adjustments from/to investment accounts.

To the extent that the actual performance with respect to a performance goal is above or below the target, the portion of the bonus attributable to that performance goal is increased or decreased accordingly. After the end of the fiscal year, our Compensation Committee reviews our financial results, and determines the final achievement of each of the performance goals and the actual bonus amount that was earned and is payable to each of our executives. The Compensation Committee has the discretion to increase or decrease the award payable to any executive in its sole discretion, based on the Compensation Committee's assessment of that executive's individual performance during the year.

Our financial results for 2014 included certain one-time charges which were outside of the control of our executive team related to our exit from the MWCC corporate center model and the sale of 41 centers to existing franchise partners, as well as the write-off of a franchise loan and certain expenses related to 13D filers. In December 2014, our Compensation Committee examined our financial results to date, both including and excluding the assets, liabilities, operating results and cash flows relating to these one-time expenses, which were expected to be included in the Company's financial statements in December 2014. The Compensation Committee determined that these expenses could not have been anticipated at the beginning of the performance period, and should not be included in the determination of the actual performance for purposes of the annual incentive bonus. The Compensation Committee also determined that the executive team had performed admirably during the 2014 fiscal year. The Compensation Committee amended the 2014 annual incentive cash and equity incentives such that the threshold payout would be the minimum payment that the executives would receive with respect to 2014.

The actual results with respect to 2014 performance (including discontinued operations as well as non-GAAP adjustments) are set forth in the table below:

Goal	Actual Performance (In Millions)
Net Revenue	\$307.8
Income Before Tax <sup>(1)</sup>	\$32.7
Net Increase in Cash and Cash Equivalents <sup>(2)</sup>	\$25.0

(1) Income before tax was adjusted to exclude certain one-time expenses recorded in 2014, including the Company's gain/loss on the sale of corporate centers, the write-off of a franchise loan, and certain legal expenses.

(2) Cash flow was adjusted to exclude certain one-time impacts on cash recorded in 2014 to include the cash impact the Company realized regarding the gain/loss on the sale of corporate centers, the write-off of a franchise loan, and certain legal expenses.

#### *Cash Component*

The target incentive cash bonus amount for each of our named executive officers for 2014 is set forth below, along with the minimum amount they were entitled to, the maximum amount that each executive would have been entitled to for above-target performance, and the actual bonus amount for 2014.

Name	Minimum Payout	Target Payout	Maximum Payout	Actual Payout
<b>Mr. MacDonald</b>	\$317,700	\$635,400	\$1,906,200	\$317,700
<b>Mr. Robinson</b>	\$95,310	\$190,620	\$571,860	\$95,310
<b>Ms. Sheetz</b>	\$211,800	\$423,600	\$1,270,800	\$211,800
<b>Mr. Kagen</b>	\$53,280	\$106,560	\$213,120	\$53,280
<b>Mr. Gould</b>	\$46,596	\$93,192	\$186,384	\$46,596
<b>Ms. Mills</b>	\$48,410	\$96,800	\$193,640	\$0 <sup>(1)</sup>

(1) Ms. Mills did not earn an annual incentive cash bonus due to her termination of employment on September 12, 2014.

#### *Performance-Based Deferred Share Component*

The equity portion of our annual incentive bonus is composed of performance-based deferred shares. The performance goals and targets are the same as the goals and targets for the cash portion of the annual incentive bonus. At the end of the year, the Compensation Committee reviews our results and determines the number of performance-based deferred shares that will be deemed “earned.” The earned deferred shares are paid to the executives as restricted shares with a one year vesting period. The target number of performance-based deferred shares for each of our named executive officers for 2014 is set forth below, along with the minimum number of shares they are entitled to, the maximum number that each executive would have earned for above-target performance, and the actual amount earned with respect to 2014 performance, which will vest in full December 31, 2015.

Name	Minimum Number of Deferred Shares	Target Number of Deferred Shares	Maximum Number of Deferred Shares	Actual Number of Deferred Shares
<b>Mr. MacDonald</b>	20,000	40,000	80,000	20,000
<b>Mr. Robinson</b>	5,000	10,000	20,000	5,000
<b>Ms. Sheetz</b>	10,000	20,000	40,000	10,000
<b>Mr. Kagen</b>	1,250	2,500	5,000	1,250
<b>Mr. Gould</b>	1,250	2,500	5,000	1,250
<b>Ms. Mills</b>	1,250	2,500	5,000	0 <sup>(1)</sup>

(1) The Deferred Shares held by Ms. Mills were forfeited upon her termination of employment on September 12, 2014.

#### *Long-Term Compensation*

Our Compensation Committee provides long-term compensation to our executives in the form of equity or equity-based awards, in order to incentivize them to create stockholder value, and to align their interests with the interests of our stockholders. We generally grant these awards in the form of restricted shares or stock options, as described below. Other than with respect to the corrective action discussed below under the heading “Long-Term Compensation Correction During 2014”, we granted only performance-based deferred shares (described above under “Annual Incentive Bonus”) and stock options to our named executive officers during 2014, and we did not grant any restricted shares to our named executive officers. The description of restricted share awards and retention awards below relates to awards granted in 2013.

#### *Restricted Share Awards*

We have not historically made grants of restricted shares on an annual basis to our named executive officers. Instead, our Compensation Committee has generally made one-time grants of restricted shares that vest over long periods. We grant restricted shares as sign-on awards, long-term retention awards, or, in some cases, rewards for exceptional performance. We believe that these larger one-time restricted share awards with long vesting schedules assist us in retaining our executives and encourage our executives to create long-term stockholder value.

With the exception of the restricted shares granted to our CEO as a result of the corrective actions described below in the section titled “Long-Term Compensation Correction During 2014”, we did not grant any restricted shares to any of our named executive officers in 2014. However, each of our CEO, President and CFO received a grant of retention shares in 2013, as described below.

#### *Retention Shares*

During 2013, our Compensation Committee made grants of restricted shares to Mr. MacDonald (100,000), Ms. Sheetz (50,000), and Mr. Robinson (12,000) that are referred to herein as Retention Shares. These grants have a particularly long vesting schedule. The Retention Shares are meant to retain the services of these executives over the seven year vesting schedule (five years for Mr. Robinson), and to reward them for their performance over that period. Retention Shares are not granted on an annual basis to our executives. The vesting schedule of the Retention Shares is nested in such a way as to be the equivalent of making a smaller grant each year for five years (three years for Mr. Robinson) that vests over three years. The Compensation Committee determined that, rather than making an award each year, the award should be granted at one time. This would give the executives some certainty as to their compensation and incentivize them to create long-term stockholder value to increase the value of their awards. Taking this unique vesting schedule into account, the value of the Retention Shares in each tranche was comparable to similar annual grants made to CEOs of our peer companies.

The Retention Shares granted to Mr. MacDonald and Ms. Sheetz vest in five equal tranches, with each tranche vesting over a three year period, as illustrated below:

	Total Shares In Tranche	Year of Vesting						
		2014	2015	2016	2017	2018	2019	2020
<b>Mr. MacDonald</b>	20,000	6,666	6,667	6,667				
	20,000		6,666	6,667	6,667			
	20,000			6,666	6,667	6,667		
	20,000				6,666	6,667	6,667	
	20,000					6,666	6,667	6,667
<b>Ms. Sheetz</b>	10,000	3,333	3,333	3,334				
	10,000		3,333	3,333	3,334			
	10,000			3,333	3,333	3,334		
	10,000				3,333	3,333	3,334	
	10,000					3,333	3,333	3,334

The Retention Shares granted to Mr. Robinson vest in three equal tranches, with each tranche vesting over a three year period, as illustrated below:

	Total Shares In Tranche	Year of Vesting				
		2014	2015	2016	2017	2018
<b>Mr. Robinson</b>	4,000	1,333	1,333	1,333		
	4,000		1,333	1,333	1,334	
	4,000			1,333	1,333	1,334

#### *Other Restricted Share Grants*

Our Compensation Committee also made certain restricted share grants in 2013 to executives in addition to the grants set forth above.

- Mr. MacDonald received a restricted share grant of 100,000 shares in January 2013, in recognition of his performance during 2012 and in consideration of his stepping into the CEO role during 2012. These restricted shares were meant to serve as a sign-on grant for Mr. MacDonald even though they were not granted until 2013, and the number of restricted shares was determined to be reasonable based on our competition for talent in the market and Mr. MacDonald's experience. These restricted shares vest in equal annual installments over a five year period.
- Ms. Mills received a restricted share grant of 10,000 shares in June 2013, in connection with her stepping into the role of Executive Vice President, Take Shape for Life. These shares vest in equal annual installments over a five year period. In connection with her termination on September 12, 2014, we accelerated a pro-rata portion of the restricted shares that would have vested had she remained employed through the next vesting date, and the remaining restricted shares were forfeited.

#### *Stock Options*

Our Compensation Committee granted stock options to our Executive Vice Presidents in both 2013 and 2014, but stock options have not been granted to our CEO, President, or CFO. The Compensation Committee determined that our CEO, President and CFO hold adequate equity awards, as described above, to align their interests with stockholders, to retain their services, and to reward them for positive results that they have created. Stock options help us maintain a competitive level of total compensation for our Executive Vice Presidents, and are an important part of our effort to attract, retain, and motivate high-quality talent in key positions.

We grant stock options to our Executive Vice Presidents rather than restricted shares in order to incentivize them to create stockholder value and to retain their services. Stock options are granted with an exercise price equal to the fair market value of our shares on the date of grant, and have value only if the stock price increases from that date. We generally intend for our stock options to qualify as "incentive" stock options, which provide certain tax benefits for the grantee. Stock options vest 33% each year on the anniversary of the date of grant and have a term of 10 years from the date of grant. The number of stock options granted to each Executive Vice President is determined on a discretionary basis, rather than by a formula. We do not time the grant of our options to coincide with the announcement of any financial results.

#### **Long-Term Compensation Correction During 2014**

Following a review in 2014 of our compensation awards and procedures, our Compensation Committee determined that it had inadvertently exceeded the limit on grants of awards of restricted shares and deferred shares to an individual during a 12-month period under the 2012 Plan with respect to grants made to Mr. MacDonald during 2013 and 2014 and to Ms. Sheetz during 2014.

We promptly took corrective action. Mr. MacDonald and Ms. Sheetz agreed that the portion of the award of 100,00 restricted shares granted to Mr. MacDonald on January 2, 2013, the award of 100,000 restricted shares granted to Mr. MacDonald on February 19, 2013, the award of 80,000 performance-based deferred shares granted to Mr. MacDonald on February 19, 2013, the award of 80,000 performance-based deferred shares granted to Mr. MacDonald on February 5, 2014, and the award of 40,000 performance-based deferred shares granted to Ms. Sheetz on February 5, 2014 exceeded the limit on grants of awards under the 2012 Plan, and would be cancelled and forfeited. The amount of the remaining awards did not exceed the limits on grants to an individual during a 12-month period.

The Board amended the 2012 Plan to provide that no participant may be granted more than 150,000 restricted shares or deferred shares during a calendar year, as disclosed on the Form 8-k filed on June 17, 2014.

The Compensation Committee determined that, while the awards were mistakenly made in excess of the limits in the 2012 Plan, the awards themselves were reasonable and in line with the compensation philosophy described above. The Compensation Committee thereafter granted new awards of restricted shares and deferred shares to Mr. MacDonald and Ms. Sheetz, subject to the same vesting schedules and performance criteria as the cancelled awards. These awards were granted in compliance with the limits on grants of restricted shares or deferred shares to an individual during a calendar year under the amended 2012 Plan. The Compensation Committee has taken actions since the date of the corrective action to strengthen its internal controls and procedures, to ensure that no similar mistakes occur in the future.

As a result of the cancellation and re-grant of these awards during 2014, the Summary Compensation Table disclosure with respect to 2014 shows a level of compensation for Mr. MacDonald that is much larger than the amount the Compensation Committee intended to award him in 2014. SEC rules require that we include the value of the replacement grants in the 2014 compensation of Mr. MacDonald, even though the Compensation Committee did not intend to grant these awards in 2014. Conversely, we have adjusted the 2013 compensation in the Summary Compensation Table so that the value of the portion of the grants made in 2013 that were cancelled and forfeited as a result of corrective action taken by our Compensation Committee are not included in Mr. MacDonald's 2013 compensation amounts, since the portions of the grants that are in excess of the limits in the plan are deemed ineffective under the terms of the 2012 Plan. We have included an additional column in for Mr. MacDonald in the Summary Compensation Table, as well as an illustrative table in the "Narrative to Summary Compensation Table and Grants of Plan-Based Awards Table" below, which displays what Mr. MacDonald's 2013 and 2014 Summary Compensation Table disclosure would have been had there been no need for the corrective action with respect to his equity and equity-based awards.

#### **Retirement Benefits**

Executives may participate in the Company 401(k) retirement plans on the same terms and conditions, including Company matching provisions, as other employees.

#### **Perquisites**

It is our general practice not to provide significant perquisites or personal benefits to our executives. The Compensation Committee considers and awards reasonable perquisites or personal benefits to executives as necessary to accomplish the objectives under our compensation philosophy. In 2014, the Compensation Committee decided to provide perquisite allowances in an amount equal \$10,000 net of all tax obligations. The amount of the perquisite allowance for each of our executives is set forth below. This perquisite allowance is intended to cover the basic perquisites that a typical executive would expect to receive.

	<b>2014 Perquisite Allowance</b>
<b>Mr. MacDonald</b>	\$14,185
<b>Mr. Robinson</b>	\$17,141
<b>Ms. Sheetz</b>	\$15,656
<b>Mr. Kagen</b>	\$18,211
<b>Mr. Gould</b>	\$17,928
<b>Ms. Mills</b>	\$18,293

#### **Severance Benefits**

We have entered into severance agreements generally only with our senior executives, including our CEO, President and CFO. The severance agreements contain provisions regarding severance benefits upon certain terminations of employment, including a termination by the Company without "cause" or by the executive for "good reason". The severance benefits provided to our CEO, President and CFO under these agreements consist of one year of continued payment of base salary, the annual bonus (cash and stock) that he or she would have been entitled to receive for the year of termination if the performance goals are reached (paid at the target level at the time such bonuses are paid to other employees), and continued participation in our health and welfare plans for one year. Severance benefits provide some security for our executives during times of uncertainty, and allow them to focus their attention on leading the Company. Severance benefits are typical for executives in these senior positions in our industry, and it is necessary for us to offer such benefits in order to attract the talent needed for our success. We believe that these severance benefits are an important factor in the retention of our executives, while still remaining modest in the overall marketplace.

We provided severance payments and benefits to Ms. Mills upon her termination of employment on September 12, 2014, which are set forth in greater detail under the heading “Potential Payments Upon Termination” below.

Our other named executive officers do not have severance agreements, and would be entitled to severance benefits only under any general severance policy that we may put in place from time to time or as are determined at the time of their termination.

#### **Other Compensation**

We do not currently provide pension arrangements, post-retirement health coverage, or similar benefits for our executives or employees. In 2014, we paid health, life, and disability insurance premiums on behalf of our executives, all on the same terms as those that we provided to all of the Company’s employees.

#### **Anti-Hedging Policy**

Our insider trading policy contains a strict anti-hedging policy. Our executives and directors are prohibited from engaging in hedging, monetization transactions or similar arrangements involving our stock, including short sales, margin transactions, and buying put or call options.

#### **Compensation Committee Interlocks and Insider Participation**

No member of our Compensation Committee was an officer or employee while serving on the Compensation Committee during Fiscal 2014, or has ever been an officer of Medifast or its subsidiaries. No executive officer of Medifast has served as a director or a member of the Compensation Committee of another entity that has one or more executive officers who are also members of our Board or Compensation Committee.

#### **Compensation Committee Report**

We have reviewed and discussed with management certain Compensation Discussion and Analysis provisions to be included in the Company’s Annual Report on Form 10-K. Based on the review and discussions referred to above, we recommend to the Board that the Compensation Discussion and Analysis referred to above be included in the Company’s Annual Report on Form 10-K for the year-ended December 31, 2014.

#### **COMPENSATION COMMITTEE OF THE BOARD**

Carl E. Sassano, Chairman  
Jerry D. Reece  
Harvey C. “Barney” Barnum  
Catherine T. Maguire

#### **ANALYSIS OF RISK INHERENT IN OUR COMPENSATION POLICIES AND PRACTICES**

The Compensation Committee has conducted a risk assessment of all of our compensation policies and practices to ensure that they do not foster risk taking above the level of risk associated with our business model. Based upon that review and a review by management of the Company’s internal controls, the Compensation Committee has concluded that the Company’s compensation programs do not encourage executives or other employees to take inappropriate risks that are reasonably likely to have a material adverse effect on the Company.

The Compensation Committee based its conclusion on a variety of factors, including the following specific aspects of the Company’s compensation practices:

- Our annual incentive compensation program is based on balanced performance metrics that promote disciplined progress towards longer-term Company goals;
- We do not offer significant short-term incentives that might drive high-risk investments at the expense of long-term Company and shareowner value;
- At the senior management and executive levels, our compensation programs are weighted towards offering incentives that reward sustainable performance by requiring continued service to receive payment; and
- All of our compensation awards are capped at reasonable and sustainable levels, as determined by a review of our economic position and prospects, as well as the compensation offered within our peer group and by comparable companies.

## 2014 Summary Compensation Table

The following table sets forth the annual and long-term compensation for the last three fiscal years of the Company's Chairman of the Board and Chief Executive Officer, the Chief Financial Officer, the Chief Operating Officer and President, the Executive Vice President and Chief Marketing Officer, the Executive Vice President of Technology and the former Executive Vice President of Take Shape For Life. These individuals are our "Named Executive Officers" for fiscal year 2014.

Name and Principal Position	Year	Salary (\$)	Bonus (\$)	Stock Awards \$(1)	Option Awards \$(2)	Non-Equity Incentive Plan Compensation (\$)	All Other Compensation \$(3)	Total (\$)
<b>Michael C. MacDonald</b>	2014	635,400	-	5,039,300 <sup>(4)</sup>	-	317,700	27,071	6,019,471
Chairman of the Board	2013	600,000	-	1,273,900 <sup>(4)</sup>	-	675,000 <sup>(8)</sup>	12,886	2,561,786
Chief Executive Officer	2012	344,231	-	-	-	815,150 <sup>(8)</sup>	1,321	1,160,702
<b>Timothy G. Robinson</b>	2014	317,700	-	132,600	-	95,310	26,138	571,748
Chief Financial Officer	2013	285,000	-	382,095	-	202,500 <sup>(8)</sup>	70,275	939,870
<b>Margaret Sheetz</b>	2014	423,600	-	265,200 <sup>(5)</sup>	-	211,800	24,595	925,195
Chief Operating Officer	2013	400,000	-	1,576,900	-	450,000 <sup>(8)</sup>	8,939	2,435,839
President	2012	247,115	-	-	-	582,500 <sup>(8)</sup>	6,083	835,698
<b>Brian Kagen</b>	2014	266,400	-	33,150	30,740	53,280	28,171	411,741
Executive Vice President Chief Marketing Officer								
<b>Don Gould</b>	2014	232,980	-	33,150	30,740	46,596	26,233	369,699
Executive Vice President	2013	220,000	-	45,488	28,659	55,000	8,135	357,282
Technology	2012	220,000	-	-	-	174,900 <sup>(8)</sup>	4,114	399,014
<b>Jeannette Mills (6)</b>	2014	383,091	-	55,141	30,740	-	281,221	750,193
Executive Vice President, Take Shape For Life	2013	132,000	-	343,987	19,629 <sup>(7)</sup>	34,271 <sup>(8)</sup>	5,297	535,184

(1) Amounts shown represent the aggregate grant date fair value of the stock awards in the year indicated, computed in accordance with FASB ASC Topic 718. For a discussion of the assumptions made in the valuation reflected in these columns, see Note 2 of the Notes to Consolidated Financial Statements included in the Company's Annual Report. The values do not correspond to the actual value that will be recognized by the named executives at the time such awards vest. With respect to the award of performance-based deferred shares to each of our named executive officers during 2014, the amount included in the grant date fair value of the number of deferred shares that were earned based on our performance for 2014 (or, for Ms. Mills, the number of deferred shares that would have been earned had she remained employed for the full year). The maximum value of such deferred shares were: \$2.1 million, \$0.5 million, \$1.1 million, \$0.1 million, \$0.1 million and \$0.1 million for Mr. MacDonald, Mr. Robinson, Ms. Sheetz, Mr. Kagen, Mr. Gould, and Ms. Mills, respectively. Ms. Mills forfeited the deferred shares upon her termination on September 12, 2014. For information with respect to the individual performance-based awards made in fiscal year 2014, please see the 2014 Grants of Plan-Based Awards Table.

(2) Amounts shown represent the aggregate grant date fair value of the option awards in the year indicated, computed in accordance with FASB ASC Topic 718. The values do not correspond to the actual value that will be recognized by the named executives at the time such awards are exercised. For information with respect to the stock option awards made in fiscal year 2014, please see the 2014 Grants of Plan-Based Awards Table.

(3) The amounts reported in this column represent the perquisite allowances, Company's matching contributions under the 401(K) plan and contributions to group term life insurance and health savings accounts. Mr. MacDonald's all other compensation total includes group term life insurance contributions, \$11,500 in matched 401(K) plan contributions made by the Company and a \$14,200 perquisite allowance. Mr. Robinson's all other compensation total includes group term life insurance contributions, health savings account contributions, matched 401(K) plan contributions and a \$17,141 perquisite allowance. Ms. Sheetz's all other compensation total includes group term life insurance contributions, matched 401(K) plan contributions, and a \$15,656 perquisite allowance. Mr. Kagen's all other compensation total includes group term life insurance contributions, health savings account contributions, matched 401(K) plan contributions, and a \$18,211 perquisite allowance. Mr. Gould's all other compensation total includes group term life insurance contributions, health savings account contributions, matched 401(K) plan contributions, and a \$17,928 perquisite allowance. Ms. Mills' all other compensation total includes group term life insurance contributions, matched 401(K) plan contributions, a \$18,293 perquisite allowance, and \$256,015 in severance benefits.

(4) The amount in Mr. MacDonald's Stock Awards column for 2013 does not include the value of certain restricted share and deferred share awards granted to him during 2013 that were determined to be in excess of the limits on individual grants under the 2012 Plan and are not considered to be effective. The amount in Mr. MacDonald's Stock Awards column for 2014 does not include the grant of performance-based deferred shares that was determined to be in excess of the limits on individual grants under the 2012 Plan and was not considered to be effective. These awards were re-granted in 2014, and the

value of the re-grants are included in the Stock Awards column for 2014. For more information on these awards, please see the section titled “Long-Term Compensation Correction During 2014” above.

(5) The amount in Ms. Sheetz’s Stock Awards column for 2014 does not include the grant of performance-based deferred shares that was determined to be in excess of the limits on individual grants under the 2012 Plan and was not considered to be effective. This award was re-granted in 2014, and the value of the re-grant is included in the Stock Awards column for 2014. For more information on this award, please see the section titled “Long-Term Compensation Correction During 2014” above.

(6) Ms. Mills resigned from the Company effective September 12, 2014 and the unvested portion of her awards were forfeited.

(7) The stock options awarded to Ms. Mills on May 31, 2013 were inadvertently not included in the 2013 Summary Compensation Table. This was due to an accounting issue regarding the date of grant. The 2013 amount has been updated.

(8) These amounts reflect cash bonus payments in accordance with the compensation plan. The balances were improperly reflected in the “Bonus” column on the prior years’ Summary Compensation Table and have been corrected in this filing.

## 2014 Grants of Plan-Based Awards Table

The following table outlines all stock awards granted to named executive officers during fiscal 2014. All awards were granted under the 2012 Share Incentive Plan, which was approved by stockholders.

Name	Grant Date	Estimated Future Payouts Under Non-Equity Incentive Plan			Estimated Future Payouts Under Equity Incentive Plan Awards			All Other Stock Awards: Number of Shares or Units (#)	All Other Option Awards: Number of Securities Underlying Options (#)	Exercise or Base Price of Option Awards (\$/Sh)	Grant Date Fair Value of Stock and Option Awards
		Threshold (\$)	Target (\$)	Maximum (\$)	Threshold (\$)	Target (\$)	Maximum (\$)				
<b>Michael C. MacDonald</b>	2/5/2014	317,700	635,400	1,906,200							
Chairman of the Board	2/5/2014				20,000	40,000	80,000				530,400 <sup>(1)</sup>
Chief Executive Officer	6/17/2014				20,000	40,000	80,000				530,400 <sup>(2)</sup>
	6/17/2014							30,000 <sup>(3)</sup>			727,800 <sup>(5)</sup>
	6/17/2014							150,000 <sup>(4)</sup>			3,781,100 <sup>(6)</sup>
<b>Timothy G. Robinson</b>	2/5/2014	95,310	190,620	571,860							
Chief Financial Officer	2/5/2014				5,000	10,000	20,000				132,600 <sup>(9)</sup>
<b>Margaret Sheetz</b>	2/5/2014	211,800	423,600	1,270,800							
Chief Operating Officer,	2/5/2014				10,000	20,000	40,000				265,200 <sup>(7)</sup>
President	6/17/2014				10,000	20,000	40,000				265,200 <sup>(8)</sup>
<b>Brian Kagen</b>	2/5/2014	53,280	106,560	213,120							
Executive Vice President	2/5/2014				1,250	2,500	5,000				33,150 <sup>(9)</sup>
Chief Marketing Officer	2/5/2014								2,000	26.52	30,740 <sup>(10)</sup>
<b>Don Gould</b>	2/5/2014	46,596	93,192	186,384							
Executive Vice President	2/5/2014				1,250	2,500	5,000				33,150 <sup>(9)</sup>
of Technology	2/5/2014								2,000	26.52	30,740 <sup>(10)</sup>
<b>Jeannette Mills</b>	2/5/2014	48,410	96,820	193,640 <sup>(13)</sup>							
Executive Vice President,	2/5/2014				1,250	2,500	5,000				33,150 <sup>(11)</sup>
Take Shape For Life	2/5/2014								2,000	26.52	30,740 <sup>(12)</sup>

(1) The reflected grant is for deferred shares for 2014 performance that was erroneously granted in excess of the allowed limits in the 2012 Share Plan Agreement. These shares were cancelled and re-granted on June 17, 2014, see note (2) below.

(2) The reflected grant is a regrant of the deferred shares granted for 2014 performance that were made in excess of the allowed limits in the 2012 Share Plan Agreement. The requirements for receiving these shares are outlined in the “Target Bonus” section outlined above. This award will vest in entirety on December 31, 2015. Upon regrant, the terms of the grant did not materially change; and therefore, the grant date fair value is based on the stock price as of the original grant date, February 5, 2014.

- (3) On February 19, 2013, a deferred shares performance grant was issued and on February 5, 2014 it was approved that the payout under the plan would be 30,000 shares. The grant was made in excess of the 2012 Share Plan Agreement allowances and was therefore cancelled and reissued as deferred shares on June 17, 2014. These shares vested in full on December 31, 2014.
- (4) On January 2, 2013, a grant for 100,000 shares was made for 2012 performance and on February 19, 2013 a grant of 100,000 retention shares was made vesting in tranches over a 7 year period. Both of these grants were erroneously made in excess of the 2012 Share Plan Agreement allowances and therefore were cancelled and re-granted as restricted stock on June 17, 2014. The regrant includes 70,000 shares related to the January 2, 2013 2012 performance grant and 80,000 shares related to the February 19, 2013 retention grant. The 70,000 shares will vest as follows: 10,000 shares on January 2, 2015, 20,000 shares on January 2, 2016, 20,000 shares on January 2, 2017, and 20,000 shares on January 2, 2018. The 80,000 shares will vest in accordance with the following schedule: 6,667 shares on February 19, 2015, 13,333 shares on February 19, 2016, 20,000 shares on February 19, 2017, 20,000 shares on February 19, 2018, 13,333 shares on February 19, 2019, and 6,667 shares on February 19, 2020. The terms of these grants did not materially change.
- (5) As the terms of the grant did not materially change, the grant date fair value is based on the original grant date, February 19, 2013, stock price of \$24.26.
- (6) As the terms of the grant did not materially change, the grant date fair value is based on the stock price as of the original grant dates, January 2, 2013 (\$26.29) and February 19, 2013 (\$24.26).
- (7) The reflected grant is for deferred shares for 2014 performance that was erroneously granted in excess of the allowed limits in the 2012 Share Plan Agreement. These shares were cancelled and re-granted on June 17, 2014, see note (8) below.
- (8) The reflected grant is a regrant of the deferred shares granted for 2014 performance that were made in excess of the allowed limits in the 2012 Share Plan Agreement. The requirements for receiving these shares are outlined in the “Target Bonus” section outlined above. This award will vest in entirety on December 31, 2015. Upon regrant, the terms of the grant did not materially change; and therefore, the grant date fair value is based on the stock price as of the original grant date, February 5, 2014.
- (9) These awards are deferred shares granted for 2014 performance and will vest in full on December 31, 2015. The requirements for receiving the awards are outlined in the “Target Bonus” section outlined above.
- (10) These options vest over a 3 year period beginning on the anniversary of the grant date and have a 10 year term.
- (11) The award is deferred shares granted for 2014 performance that were forfeited by Ms. Mills on September 12, 2014 when she resigned from the Company. The requirements for receiving the award are outlined in the “Target Bonus” section outlined above.
- (12) These options vest over a 3 year period beginning on the anniversary of the grant date and have a 10 year term. Ms. Mills forfeited all 2,000 options on September 12, 2014 when she resigned from the Company.

#### **Narrative to Summary Compensation Table and Grants of Plan-Based Awards Table**

##### *Employment Agreements*

We do not have employment agreements with any of our named executive officers. We have entered into severance agreements with Mr. MacDonald, Ms. Sheetz, and Mr. Robinson, which provide for severance payments and benefits upon certain terminations of employment, which are described in further detail below under the heading “Potential Payments Upon Termination or Change in Control.”

##### *Annual Incentive Bonus*

Our annual incentive bonus has a cash component and a performance-based deferred share component, with the earned shares vesting one year after the end of the performance period. For 2014, our named executive officers received 50% of their target cash bonus amounts based on our performance in 2014, which is set forth in the “Non-Equity Incentive Plan Compensation” column of the Summary Compensation Table. The performance-based deferred shares were deemed to be earned at the minimum level based on our performance, and the value of such deferred shares are included in the “Stock Awards” column of the Summary Compensation Table. These deferred shares will not be fully vested until December 31, 2015, provided the executive remains employed through that date. Ms. Mills did not receive an annual cash bonus and all performance-based deferred shares were forfeited upon her termination of employment. A more detailed discussion of our annual incentive bonus is included above under the heading “Annual Incentive Bonus”.

##### *Corrective Action With Respect to Certain Long-Term Compensation*

As discussed above under the heading “Long-Term Compensation Correction During 2014”, we took actions during 2014 to correct certain grants of restricted shares and performance-based deferred shares made to Mr. MacDonald during 2013 and 2014 and Ms. Sheetz during 2014 that were in excess of the limit on grants to an individual during a 12-month period under our 2012 Plan. The Summary Compensation Table reflects the value of these corrected grants in the 2014 column entitled “Stock Awards.” For Mr. MacDonald, the values in the “Stock Awards” column for 2013 have been adjusted to remove the value of the grants that were deemed to be ineffective due to this correction.



As a result of the corrective action, the amounts in the “Total Compensation” column of the Summary Compensation Table for 2013 and 2014 do not reflect the intentions of the Compensation Committee with respect to Mr. MacDonald’s compensation, as the amounts included in 2014 compensation include amounts intended to be granted in 2013. The table below more accurately reflects the intention of the Compensation Committee with respect to Mr. MacDonald’s compensation.

Name and Principal Position	Year	Salary (\$)	Stock Awards (\$)	Non-Equity Incentive Plan Compensation (\$)	All Other Compensation (\$)	Total (\$)
<b>Michael C. MacDonald</b>	2014	635,400	530,400	317,700	27,071	1,510,571
Chairman of the Board	2013	600,000	5,782,800	675,000	12,886	7,070,686
Chief Executive Officer						

As noted above, however, the “Total Compensation” for 2014 for Mr. MacDonald does not reflect the value actually received by Mr. MacDonald during 2014, and “Total Compensation” for 2013 includes the value of awards granted in 2013 that have a vesting period of up to seven years. For a more accurate display of the value of compensation received by Mr. MacDonald with respect to 2014, see “Realized Compensation” above.

#### Outstanding Equity Awards at 2014 Fiscal Year-End Table

Name	Number of Securities Underlying Unexercised Options (#) Exercisable	Number of Securities Underlying Unexercised Options (#) Unexercisable	Option Exercise Price (\$)	Option Expiration Date	Number of Shares or Units of Stock That Have Not Vested (#)	Market Value of Shares or Units of Stock that have not Vested (\$)(1)
<b>Michael C. MacDonald</b>					150,000 <sup>(6)</sup>	5,032,500
Chairman of the Board					10,000 <sup>(7)</sup>	335,500
Chief Executive Officer					13,334 <sup>(8)</sup>	447,356
					20,000 <sup>(2)</sup>	671,000
<b>Timothy G. Robinson</b>					3,750 <sup>(3)</sup>	125,813
Chief Financial Officers					10,667 <sup>(4)</sup>	357,878
					5,000 <sup>(2)</sup>	167,750
<b>Margaret Sheetz</b>					15,000 <sup>(3)</sup>	503,250
Chief Operating Officer, President					46,667 <sup>(5)</sup>	1,565,678
					10,000 <sup>(2)</sup>	335,500
<b>Brian Kagen</b>	666	1,334	24.26	2/19/2023		
Executive Vice President	-	2,000	26.52	2/5/2024		
Chief Marketing Officer					1,250 <sup>(2)</sup>	41,938
<b>Don Gould</b>	666	1,334	24.26	2/19/2023		
Executive Vice President of Technology	-	2,000	26.52	2/5/2024		
					1,250 <sup>(2)</sup>	41,938

(1) The market value of shares of stock that have not vested is based on the closing price of our common stock on December 31, 2014, or \$33.55 per share.

(2) The deferred shares will vest in full on December 31, 2015.

(3) The deferred shares will vest in full on January 1, 2015.

(4) The restricted stock will vest according to the following schedule: 2,666 shares on February 19, 2015; 4,000 shares on February 19, 2016; 2,667 shares on February 19, 2017, and 1,334 shares on February 19, 2018.

(5) The restricted stock will vest according to the following schedule: 6,666 shares on February 19, 2015; 10,000 shares on February 19, 2016; 10,000 shares on February 19, 2017, 10,000 shares on February 19, 2018, 6,667 shares on February 19, 2019, and 3,334 shares on February 19, 2020.

(6) The restricted stock is a regrant of two awards granted in 2013 which contained different vesting schedules. The vesting schedules of the original awards were kept intact resulting in the following vesting schedule: 10,000 shares on January 2, 2015; 6,666 shares on February 19, 2015; 20,000 shares on January 2, 2016; 13,333 shares on February 19, 2016; 20,000 shares on January 2, 2017; 20,000 shares on February 19, 2017; 20,000 shares on January 2, 2018; 20,000 shares on February 19, 2018; 13,334 shares on February 19, 2019; and 6,667 shares on February 19, 2020.

(7) The restricted stock will vest on January 2, 2015.

(8) The restricted stock will vest 6,667 shares on February 19, 2015 and 6,667 shares on February 19, 2016.

## 2014 Option Exercises and Stock Vested Table

The following table sets forth information regarding stock vesting for the Named Executive Officers during 2014 and the resulting value realized.

Name	Stock Awards	
	Number of Shares Acquired on Vesting (#)	Value Realized on Vesting (\$)(1)
<b>Michael C. MacDonald</b>	20,000	634,800
Chairman of the Board	20,000	521,600
Chief Executive Officer	30,000	1,006,500
	6,666	178,982
<b>Timothy G. Robinson</b>	1,333	35,791
Chief Financial Officer		
<b>Margaret Sheetz</b>	20,000	583,000
Chief Operating Officer	3,333	89,491
President		
<b>Brian Kagen</b>	1,875	49,725
Executive Vice President		
Chief Marketing Officer		
<b>Don Gould</b>	1,875	49,725
Executive Vice President of Technology		
<b>Jeannette Mills</b>	2,000	62,860
Executive Vice President, Take Shape For Life	667	21,991

(1) Represents the number of shares vested multiplied by the fair market value of the common stock on the vesting date.

### Potential Payments upon Termination or Change in Control

*Mr. MacDonald, Mr. Robinson and Ms. Sheetz*

On June 19, 2013, the Company executed certain severance agreements with each of the Company's Chairman and CEO; CFO; and President and COO.

Under the terms of these agreements, in the event of a termination of employment by the Company without "Cause" or by any of these executives with "Good Reason," the officer would be eligible to receive the following as severance (in addition to receiving all accrued but unpaid salary and accrued vacation as of the termination date):

- i. the executive's then-current annual salary, which will be paid in accordance with the Company's regular payroll practices, for a period of one (1) year following the date of termination;
- ii. the annual bonus, including any cash or stock that the executive would have been entitled to had he or she been employed for the entire calendar year (provided that the related performance metrics are satisfied), at the target level, which will be paid when such consideration is normally paid to executives in accordance with the Company's regular practices; and
- iii. continued coverage under the Company's health, disability and other insurance benefits for a period of one (1) year following the termination date.

In addition, under the terms of these agreements, and notwithstanding anything to the contrary in the Company's 2012 Plan or in any other agreement between the executive and the Company, upon the occurrence of a "Change of Control" as defined in the 2012 Plan, any and all awards previously granted under the plan, will become immediately and fully vested and, to the extent applicable, exercisable as of the date immediately prior to such Change of Control.

For purposes of these agreements, the Company will have "Cause" to terminate the executive's employment in the event that the executive violates any material provision of the Company's Code of Conduct and Business Ethics.

For purposes of these agreements, these executives will be deemed to have “Good Reason” to terminate his or her employment if any of the following occur: (i) a material diminution in title, status, authority, duties or responsibilities, including the imposition of any requirement that the executive report to a person other than the CEO; (ii) any material reduction in compensation from the executive’s current total compensation, including current base salary and bonuses; (iii) the Company’s breach of any of its obligations under the agreement, provided, however, if cure is possible, the failure by the Company to cure the circumstance or breach within 30 days after receiving notice from the executive; (iv) the relocation of the executive’s work location by more than 50 miles from the current location in Baltimore, Maryland; and (v) the failure by any successor of the Company to assume in writing the Company’s obligations under this agreement.

The payments and benefits to be provided under these agreements are subject to certain confidentiality, non-solicitation and non-disparagement provisions.

*Mr. Kagen and Mr. Gould*

We do not have employment agreements or severance arrangements with Mr. Kagen or Mr. Gould. Upon a termination of employment, they would not be entitled to any cash severance from the Company or the acceleration of any equity awards.

*Ms. Mills*

Ms. Mills left the Company on September 12, 2014 to pursue other opportunities. We did not have any severance obligations to Ms. Mills under any employment agreement or other severance policy. However we agreed to continue to pay Ms. Mills’ base salary for a period of 55 weeks following her termination of employment and to continue her participation in our medical, dental and/or vision plans during that period. We also agreed to accelerate and vest on a pro-rata basis, the portion of the 10,000 restricted shares granted to her in connection with her hiring that would have vested on the next vesting date following her termination. No adjustments were made to the restricted shares granted to her in 2013 in connection with her service to the Board of Directors that will vest on January 1, 2015. All other unvested equity awards held by Ms. Mills were forfeited in their entirety. Ms. Mills executed a general release of claims in favor of the Company and is bound by a covenant not to compete for six months following her termination.

## Potential Payments Upon Termination or Change in Control Table

The table below details the payments and benefits that would be provided to each of our named executive officers if he or she was terminated by the Company without Cause or terminated employment for Good Reason, or if a Change in Control occurred, in each case on December 31, 2014. For Ms. Mills, the table details the payments and benefits actually received by her in connection with her termination of employment on September 12, 2014.

Name	Severance	Annual Cash Bonus (1)	Health, Disability and Insurance Benefits	Restricted Shares (2) (unvested)	Performance-Based Shares (2) (unvested)	Stock Options (2) (unvested)
<b>Michael C. MacDonald</b>						
<i>Termination Without Cause or for Good Reason</i>	635,400	635,400	18,474	5,815,356	1,262,000	-
<i>Change in Control</i>	-	-	-	5,815,356	1,262,000	-
<b>Timothy G. Robinson</b>						
<i>Termination Without Cause or for Good Reason</i>	317,700	190,620	15,818	483,691	315,500	-
<i>Change in Control</i>	-	-	-	483,691	315,500	-
<b>Margaret Sheetz</b>						
<i>Termination Without Cause or for Good Reason</i>	423,600	423,600	29,501	2,068,928	631,000	-
<i>Change in Control</i>	-	-	-	2,068,928	631,000	-
<b>Brian Kagen</b>						
<i>Termination Without Cause or for Good Reason</i>	-	-	-	-	-	-
<i>Change in Control</i>	-	-	-	-	-	-
<b>Don Gould</b>						
<i>Termination Without Cause or for Good Reason</i>	-	-	-	-	-	-
<i>Change in Control</i>	-	-	-	-	-	-
<b>Jeannette Mills</b>						
<i>Termination on September 12, 2014</i>	256,015	-	11,360	21,991	-	-

(1) The annual cash bonus reflects the target cash bonus that the executive would have been entitled to receive under our 2014 Annual Incentive Bonus program, without pro-ration since the assumed date of termination is also the last day of the fiscal year.

(2) The value of the restricted shares, performance-based shares, and stock options that would be accelerated upon a termination of employment is based on the value of our common stock on December 31, 2014, which was \$33.55. The restricted shares column represents the grants outlined in the Outstanding Equity Awards table on page 51 except the unvested performance-based deferred shares that were granted in 2014 and earned based on 2014 performance that are reflected in the Performance-Based Shares column.

## Compensation of Directors

The non-employee directors of Medifast receive an annual stock grant for their service on the Board. In Fiscal 2014, each non-employee director received 750 shares of restricted stock and 5,000 stock options. The Lead Director received 850 shares of restricted stock. The number of shares and options received was prorated for directors who joined the Board mid-year in 2013. Stock options are granted at the February meeting of the Board and vest over a three year term, and restricted shares vest on January 1, 2016. In Fiscal 2014, directors also received a meeting fee of \$7,500 for attending a quarterly Board meeting and between \$500 and \$4,000 for attending a quarterly committee meeting (depending on the committee and the position held). The committee fees and Board meeting fees may, at each director's election, be received in cash or common shares (equivalent in value to 120% of the cash value of the compensation based on the stock price on the last day of the quarter). All common shares granted in lieu of compensation vest on the respective quarter-end date. For additional committee meetings or board service, directors receive \$1,500 per day or a pro rata portion thereof. Employee directors do not receive any additional compensation for their services as director.

The following table contains information concerning the compensation of our non-employee Directors during 2014.

Name	Fees Earned or			Total (\$)
	Paid in Cash (\$)	Stock Awards (\$ (1))	Option Awards (\$ (2))	
Harvey C. Barnum	844	60,761	76,851	138,456
Barry B. Bondroff	3,719	72,430	76,851	153,000
Kevin G. Byrnes	35,219	19,890	44,835	99,944
Charles P. Connolly	2,156	75,129	76,851	154,136
Catherine T. Maguire	18,625	39,749	76,851	135,225
John P. McDaniel	1,313	60,761	76,851	138,925
Jerry D. Reece	938	65,529	76,851	143,317
Rev. Donald F. Reilly, O.S.A.	34,563	19,890	76,851	131,304
Carl E. Sassano	18,521	39,152	22,410	80,093

(1) Amounts are calculated based on the aggregate grant date fair value of these awards computed in accordance with FASB ASC Topic 718, "Stock Compensation," excluding the effect of estimated forfeitures. The assumptions and methodologies used to calculate these amounts are discussed in Note 2 to our Consolidated Financial Statements included in the Company's Annual Report. Under generally accepted accounting principles, compensation expense with respect to stock awards granted to our employees is recognized over the vesting periods of the applicable rewards.

(2) Amounts are based on the aggregate grant date fair value of the option awards, computed in accordance with FASB ASC Topic 718.

Our non-employee directors held the following outstanding awards as of December 31, 2014:

Name	Outstanding Restricted Stock Awards (#)	Outstanding Stock Option Awards (#)
Harvey C. Barnum	1,500	5,000
Barry B. Bondroff	1,600	5,000
Kevin G. Byrnes	1,188	2,917
Charles P. Connolly	1,500	5,000
Catherine T. Maguire	1,500	5,000
John P. McDaniel	1,500	5,000
Jerry D. Reece	1,500	5,000
Rev. Donald F. Reilly, O.S.A.	1,500	5,000
Carl E. Sassano	969	1,458

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

### SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS, DIRECTORS, AND EXECUTIVE OFFICERS

The following table sets forth, as of April 28, 2015, information with respect to the beneficial ownership of our common stock by:

- each person known to us to be the beneficial owner of more than 5% of our common stock;
- each of our directors;
- each of the NEOs set forth in the Summary Compensation Table; and
- all of our current directors and executive officers as a group.

The number of shares beneficially owned by each person, director, or NEO is determined under Rule 13d-3 of the Exchange Act; this information is not necessarily indicative of beneficial ownership for any other purpose. Under these rules, beneficial ownership includes any shares for which the individual has sole or shared voting power or investment power and also any shares with respect to which the person has the right to acquire sole or shared voting or investment power on or before June 27, 2015 (60 days after April 28, 2015) through the exercise of any stock option, warrant or other right. Unless we indicate otherwise, each person has sole investment and/or voting power with respect to the shares set forth in the following tables.

Except as otherwise indicated, the address for each person below is c/o Medifast, Inc., 3600 Crondall Lane, Suite 100, Owings Mills, Maryland 21117.

Name of Beneficial Owner	Title	Shares Beneficially Owned (1)	Percent of Outstanding Common Stock (%)
Visium Asset Management, L.P. (2) c/o Visium Asset Management, L.P. 888 7th Avenue New York, NY 10019		1,325,458	10.93%
ModusLink Global Solutions, Inc. (3) 1601 Trapelo Road Waltham, MA 02154		1,260,925	10.40%
BlackRock, Inc. (4) 40 East 52nd Street New York, NY 10022		1,098,074	9.06%
Engaged Capital, LLC (5) 610 Newport Center Drive, Suite 250 Newport Beach, CA 92660		718,670	5.93%
Michael C. MacDonald (6)	Director, Chairman of the Board & Chief Executive Officer	340,988	2.81%
Margaret Sheetz (7)	Director, President & Chief Operating Officer	416,912	3.44%
Donald F. Reilly (8)	Director	29,650	*
Charles P. Connolly	Director	46,030	*
Barry B. Bondroff, CPA (8)	Director	25,246	*
John P. McDaniel	Director	21,289	*
Catherine T. Maguire (8)	Director	15,074	*
Harvey C. Barnum (8)	Director	8,742	*
Jerry D. Reece (8)	Director	8,792	*
Jason L. Groves	Director, Executive Vice President & General Counsel	21,697	*
Kevin G. Byrnes	Director	2,952	*
Carl E. Sassano	Director	4,196	*
Timothy G. Robinson	Chief Financial Officer	17,716	*
Jeannette M. Mills	Former Executive Vice President, Take Shape for Life	12,549	*
Brian Kagen	Executive Vice President, Chief Marketing Officer	5,054	*
Don Gould	Executive Vice President of Technology	8,054	*
All current directors and executive officers as a group (17 persons):		979,392	8.08%

\* Shares held represent less than 1% of the total number of outstanding shares of common stock of the Company.

(1) Based on 12,124,699 shares outstanding at April 28, 2015. In calculating the percentage of ownership, all shares of common stock of which the identified person or group has the right to acquire beneficial ownership on or before June 27, 2015, are deemed to be outstanding for the purpose of computing the percentage of the shares of common stock owned by that person or group. These shares are not, however, deemed to be outstanding for the purpose of computing the percentage of the shares of common stock owned by any other person or group.

(2) Based solely on information reported on Schedule 13G, as amended, filed by Visium Asset Management, LP on April 8, 2014. As reported in such filing, Visium Asset Management, LP has shared voting power with respect to 1,274,351 shares and share dispositive power with respect to 1,325,458 shares and an aggregate beneficial ownership of 1,325,458 shares of the Company's common stock.

(3) Based solely on information reported on Schedule 13D filed by ModusLink Global Solutions, Inc. on August 14, 2014. As reported in such filing, ModusLink Global Solutions, Inc. has shared dispositive power with respect to 1,260,925 shares and an aggregate beneficial ownership of 1,260,925 shares of the Company's common stock.

(4) Based solely on information included in a Schedule 13G/A filed with the SEC by BlackRock, Inc. ("BlackRock") on January 15, 2015. In such filing BlackRock indicates that it has sole voting power with respect to 1,067,062 shares of our common stock and sole dispositive power with respect to 1,098,074 shares of our common stock.

(5) Based solely on information included in a Schedule 13 D/A filed with the SEC by Glenn W. Welling and Engaged Capital, LLC ("Engaged") on April 7, 2015. In such filing Engaged indicates that it has sole voting and dispositive power with respect to 718,670 shares of our common stock.

(6) Includes 92,656 shares that are pledged as collateral for loans.

(7) Includes 5,149 indirect shares owned by Ms. Sheetz' spouse.

(8) The following shares are held in joint accounts: Mr. Reilly holds 289,1650 shares in joint accounts with The Brothers of the Order of Hermits of St Augustine and has no pecuniary interest in the shares, Mr. Bondroff holds 23,046 shares in a joint account with his spouse, Ms. Maguire holds 15,074 shares in joint accounts with the Sisters of Mercy, Mr. Barnum holds 1,869 shares in a living trust, and Mr. Reece holds 7,727 shares in a trust account.

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

The Board has established a policy and certain procedures that must be followed prior to any transaction, arrangement or relationship or series of similar transactions, arrangements or relationships, including any indebtedness or guarantee of indebtedness, with a "related person" (as defined by the SEC's rules and regulations). Under this policy, the Nomination Committee monitors and reviews issues involving potential conflicts of interest involving officers and directors of the Company, including reviewing all related party transactions (generally, transactions involving amounts exceeding \$120,000 in which a related person has a direct or indirect material interest).

Please see "Item 10. Information Concerning Our Board of Directors – Director Independence" for information concerning director independence.

### ITEM 14. PRINCIPAL ACCOUNTANT FEES AND SERVICES

The following table outlines the aggregate fees billed to the Company for the fiscal years ended December 31, 2014 and 2013 by the Company's principal accounting firm, McGladrey.

	<u>2014</u>	<u>2013</u>
Audit Fees	\$ 350,000	\$ 249,000
Audit-Related Fees	-	-
Tax Fees	99,000	148,000
All Other Fees	<u>5,000</u>	<u>4,000</u>
Total	<u>\$ 454,000</u>	<u>\$ 401,000</u>

**Audit Fees:** The amounts noted above for Audit Fees include the aggregate fees billed for each of the last two fiscal years for professional services rendered by the principal accountant for the audits of the Company's consolidated annual financial statements and local subsidiaries' annual financial statements, reviews of the Company's quarterly financial statements, attestation of internal control over financial reporting, as required by the Sarbanes-Oxley Act, Section 404 and comfort letters, consents and other services related to SEC matters.

**Tax Fees:** The amounts noted above for Tax Fees include tax compliance and advisory services.

**All Other Fees:** The amounts noted above for All Other Fees include fees incurred for the review of the Company's annual Franchise Disclosure Document and other services not reported above.

#### **Audit Committee Pre-Approval of Audit and Permissible Non-Audit Services of the Independent Registered Public Accountant**

The Audit Committee pre-approves all audit and permissible non-audit services provided by the independent registered public accountant. These services may include audit services, audit-related services, tax services and other services. The Audit Committee has adopted a policy for the pre-approval of services provided by the independent registered public accountant.

Under the policy, pre-approval is generally provided for work associated with the following:

- registration statements under the Securities Act of 1933 (for example, comfort letters or consents);
- due diligence work for potential acquisitions or dispositions;
- attest services not required by statute or regulation;
- adoption of new accounting pronouncements or auditing and disclosure requirements and accounting or regulatory consultations;
- internal control reviews and assistance with internal control reporting requirements;
- review of information systems security and controls;
- tax compliance, tax planning and related tax services, excluding any tax service prohibited by regulatory or other oversight authorities; expatriate and other individual tax services; and
- assistance and consultation on questions raised by regulatory agencies.

For each proposed service, the independent registered public accountant is required to provide detailed back-up documentation at the time of approval to permit the Audit Committee to make a determination whether the provision of such services would impair the independent registered public accountant's independence.

The Audit Committee has approved in advance certain permitted services whose scope is routine across business units, including statutory or other financial audit work for non-U.S. subsidiaries that is not required for Exchange Act audits.

The Audit Committee pre-approved all audit, audit-related, tax and other services provided by McGladrey LLP, Inc. during fiscal year 2014 in accordance with this policy.

**PART IV**

**ITEM 15. EXHIBITS AND FINANCIAL STATEMENT SCHEDULES**

The following documents are filed as part of this Report

(a) 1. Financial Statements

See Index to the Consolidated Financial Statements on page 59 of this Report

2. Financial Statement Schedules

None, as all information required in these schedules is included in the Notes to the Consolidated Financial Statements.

3. Exhibits

Reference is made to the Exhibit Index on page 76 of this Report for a list of exhibits required by Item 601 of Registration S-K to be filed as part of this Report.



MEDIFAST, INC. AND SUBSIDIARIES  
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**REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM**

To the Board of Directors and Stockholders of  
Medifast, Inc.

We have audited the consolidated balance sheets of Medifast, Inc. and subsidiaries (the “Company”) as of December 31, 2014 and 2013, and the related consolidated statements of income, comprehensive income, stockholders’ equity, and cash flows for each of the three years in the period ended December 31, 2014. These financial statements are the responsibility of the Company’s management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Medifast, Inc. and subsidiaries as of December 31, 2014 and 2013, and the results of their operations and their cash flows for each of the three years in the period ended December 31, 2014, in conformity with U.S. generally accepted accounting principles.

We have also audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the Company’s internal control over financial reporting as of December 31, 2014, based on criteria established in *Internal Control—Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission in 2013, and our report dated March 16, 2015 expressed an unqualified opinion on the effectiveness of the Company’s internal control over financial reporting.

/s/ McGladrey LLP

Baltimore, Maryland  
March 16, 2015

**MEDIFAST, INC. AND SUBSIDIARIES**  
**CONSOLIDATED BALANCE SHEETS**  
As of December 31, 2014 and 2013

	<u>2014</u>	<u>2013</u>
<b>ASSETS</b>		
<b>Current assets:</b>		
Cash and cash equivalents	\$ 24,459,000	\$ 36,382,000
Accounts receivable-net of allowance for sales returns and doubtful accounts of \$354,000 and \$564,000	1,650,000	942,000
Inventory	15,735,000	17,537,000
Investment securities	28,185,000	31,420,000
Income taxes, prepaid	5,099,000	-
Prepaid expenses and other current assets	2,875,000	2,526,000
Deferred tax assets	3,727,000	1,957,000
Current assets of discontinued operations	184,000	1,190,000
<b>Total current assets</b>	<b><u>81,914,000</u></b>	<b><u>91,954,000</u></b>
Property, plant and equipment - net	33,477,000	34,476,000
Other assets	497,000	231,000
Long-term assets of discontinued operations	22,000	5,989,000
<b>TOTAL ASSETS</b>	<b><u>\$ 115,910,000</u></b>	<b><u>\$ 132,650,000</u></b>
<b>LIABILITIES AND STOCKHOLDERS' EQUITY</b>		
<b>Current liabilities:</b>		
Accounts payable and accrued expenses	\$ 21,854,000	\$ 22,230,000
Income taxes payable	-	99,000
Current maturities of capital leases	232,000	222,000
Current liabilities of discontinued operations	4,858,000	4,550,000
<b>Total current liabilities</b>	<b><u>26,944,000</u></b>	<b><u>27,101,000</u></b>
<b>Other liabilities:</b>		
Capital leases, net of current portion	242,000	474,000
Deferred tax liabilities	5,492,000	6,659,000
Long-term liabilities of discontinued operations	2,756,000	-
<b>Total liabilities</b>	<b><u>35,434,000</u></b>	<b><u>34,234,000</u></b>
<b>Stockholders' Equity:</b>		
Preferred stock, \$.001 par value (1,500,000 authorized, no shares issued and outstanding)	-	-
Common stock; par value \$.001 per share; 20,000,000 shares authorized; 12,365,690 and 13,143,309 issued 12,075,764 and 13,115,642 issued and outstanding	12,000	13,000
Additional paid-in capital	1,132,000	-
Accumulated other comprehensive income	435,000	703,000
Retained earnings	78,897,000	97,700,000
<b>Total stockholders' equity</b>	<b><u>80,476,000</u></b>	<b><u>98,416,000</u></b>
<b>TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY</b>	<b><u>\$ 115,910,000</u></b>	<b><u>\$ 132,650,000</u></b>

The accompanying notes are an integral part of these consolidated financial statements.

**MEDIFAST, INC. AND SUBSIDIARIES**  
**CONSOLIDATED STATEMENTS OF INCOME**  
**Years Ended December 31, 2014, 2013, and 2012**

	<u>2014</u>	<u>2013</u>	<u>2012</u>
Revenue	\$ 285,285,000	\$ 324,054,000	\$ 318,571,000
Cost of sales	76,078,000	83,488,000	82,662,000
<b>Gross Profit</b>	<b>209,207,000</b>	<b>240,566,000</b>	<b>235,909,000</b>
Selling, general, and administrative	178,961,000	202,156,000	208,769,000
<b>Income from operations</b>	<b>30,246,000</b>	<b>38,410,000</b>	<b>27,140,000</b>
Other income			
Interest and dividend income, net	716,000	509,000	304,000
Other income	731,000	124,000	912,000
	<u>1,447,000</u>	<u>633,000</u>	<u>1,216,000</u>
<b>Income from continuing operations before income taxes</b>	<b>31,693,000</b>	<b>39,043,000</b>	<b>28,356,000</b>
Provision for income taxes	10,664,000	11,908,000	9,914,000
Income from continuing operations	21,029,000	27,135,000	18,442,000
Loss from discontinued operations, net of tax	(7,848,000)	(3,166,000)	(2,566,000)
<b>Net income</b>	<b>\$ 13,181,000</b>	<b>\$ 23,969,000</b>	<b>\$ 15,876,000</b>
Basic earnings per share			
Earnings per share from continuing operations	<u>\$ 1.66</u>	<u>\$ 1.97</u>	<u>\$ 1.34</u>
Loss per share from discontinued operations	<u>\$ (0.62)</u>	<u>\$ (0.23)</u>	<u>\$ (0.18)</u>
Earnings per share	<u>\$ 1.04</u>	<u>\$ 1.74</u>	<u>\$ 1.16</u>
Diluted earnings per share			
Earnings per share from continuing operations	<u>\$ 1.65</u>	<u>\$ 1.96</u>	<u>\$ 1.34</u>
Loss per share from discontinued operations	<u>\$ (0.62)</u>	<u>\$ (0.23)</u>	<u>\$ (0.18)</u>
Earnings per share	<u>\$ 1.03</u>	<u>\$ 1.73</u>	<u>\$ 1.16</u>
Weighted average shares outstanding -			
Basic	<u>12,670,387</u>	<u>13,774,083</u>	<u>13,721,997</u>
Diluted	<u>12,778,277</u>	<u>13,817,693</u>	<u>13,739,824</u>

The accompanying notes are an integral part of these consolidated financial statements.

**MEDIFAST, INC. AND SUBSIDIARIES**  
**CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME**  
**Years Ended December 31, 2014, 2013, and 2012**

	<u>2014</u>	<u>2013</u>	<u>2012</u>
Net income	\$ 13,181,000	\$ 23,969,000	\$ 15,876,000
Other comprehensive income, net of tax			
Change in unrealized gains/losses on marketable securities:			
Change in fair value of marketable securities, net of tax	207,000	257,000	269,000
Adjustment for net (gains)/losses realized and included in net income, net of tax	<u>(475,000)</u>	<u>(107,000)</u>	<u>(112,000)</u>
Total change in unrealized (gains)/losses on marketable securities, net of tax	<u>(268,000)</u>	<u>150,000</u>	<u>157,000</u>
Other comprehensive income (loss)	<u>(268,000)</u>	<u>150,000</u>	<u>157,000</u>
Comprehensive income	<u>\$ 12,913,000</u>	<u>\$ 24,119,000</u>	<u>\$ 16,033,000</u>

The accompanying notes are an integral part of these consolidated financial statements.

**MEDIFAST, INC. AND SUBSIDIARIES**  
**CONSOLIDATED STATEMENTS OF CHANGES IN STOCKHOLDERS' EQUITY**  
**Years Ended December 31, 2014, 2013, and 2012**

	Number of Shares Issued	Par Value \$0.001 Amount	Additional Paid-In Capital	Retained Earnings	Accumulated other comprehensive income	Treasury Stock	Total
Balance, December 31, 2011	15,510,185	\$ 16,000	\$36,076,000	\$60,658,000	\$ 396,000	\$(23,744,000)	\$73,402,000
Share-based compensation, net of shares repurchased for employee taxes			2,850,000				2,850,000
Share-based compensation tax benefit			1,265,000				1,265,000
Restricted shares issued to executives and directors	15,770						-
Treasury stock purchases						(2,764,000)	(2,764,000)
Net income				15,876,000			15,876,000
Net change in unrealized gain on investments					157,000		157,000
Balance, December 31, 2012	15,525,955	\$ 16,000	\$ 40,191,000	\$ 76,534,000	\$ 553,000	\$(26,508,000)	\$ 90,786,000
Shares issued to executives	16,163						
Share-based compensation, net of shares repurchased for employee taxes			3,209,000				3,209,000
Share-based compensation tax benefit			383,000				383,000
Treasury stock purchases						(20,081,000)	(20,081,000)
Treasury stock retirement	(2,398,809)	(3,000)	(43,783,000)	(2,803,000)		46,589,000	-
Net income				23,969,000		23,969,000	
Net change in unrealized gain on investments					150,000		150,000
Balance, December 31, 2013	13,143,309	\$ 13,000	\$ -	\$ 97,700,000	\$ 703,000	\$ -	\$ 98,416,000
Shares issued to executives and directors	349,473						
Share-based compensation, net of shares repurchased for employee taxes			2,766,000				2,766,000
Share-based compensation tax benefit			275,000				275,000
Treasury stock purchases						(33,894,000)	(33,894,000)
Treasury stock retirement	(1,127,092)	(1,000)	(1,909,000)	(31,984,000)		33,894,000	-
Net income				13,181,000			13,181,000
Net change in unrealized gain on investments					(268,000)		(268,000)
Balance, December 31, 2014	12,365,690	\$ 12,000	\$ 1,132,000	\$ 78,897,000	\$ 435,000	\$ -	\$ 80,476,000

The accompanying notes are an integral part of these consolidated financial statements.

**MEDIFAST, INC. AND SUBSIDIARIES**  
**CONSOLIDATED STATEMENTS OF CASH FLOWS**  
**Years Ended December 31, 2014, 2013 & 2012**

	<u>2014</u>	<u>2013</u>	<u>2012</u>
Cash flows from operating activities: Net income	\$ 13,181,000	\$ 23,969,000	\$ 15,876,000
Loss from discontinued operations, net of tax	(7,848,000)	(3,166,000)	(2,566,000)
Income from continuing operations	21,029,000	27,135,000	18,442,000
Adjustments to reconcile net income to net cash provided by operating activities from continuing operations:			
Depreciation and amortization	8,052,000	7,901,000	8,385,000
Realized gain (loss) on investment securities, net	(771,000)	(74,000)	2,000
Share-based compensation	3,918,000	3,209,000	2,850,000
Deferred income taxes	286,000	428,000	(598,000)
(Gain)/loss on disposal of fixed assets	(29,000)	392,000	100,000
Changes in assets and liabilities which provided (used) cash:			
Accounts receivable	(708,000)	87,000	(389,000)
Inventory	1,802,000	2,615,000	(734,000)
Prepaid expenses and other current assets	(349,000)	204,000	(810,000)
Other assets	(318,000)	746,000	155,000
Accounts payable and accrued expenses	(376,000)	(1,427,000)	8,974,000
Income taxes	(5,198,000)	972,000	4,561,000
<b>Net cash provided by operating activities- continuing operations</b>	<b>27,338,000</b>	<b>42,188,000</b>	<b>40,938,000</b>
<b>Net cash provided by (used in) operating activities- discontinued operations</b>	<b>(1,802,000)</b>	<b>172,000</b>	<b>(674,000)</b>
<b>Net cash provided by operating activities</b>	<b>25,536,000</b>	<b>42,360,000</b>	<b>40,264,000</b>
Cash Flow from Investing Activities:			
Sale of investment securities	29,636,000	14,359,000	8,109,000
Purchase of investment securities	(26,080,000)	(25,355,000)	(8,390,000)
Purchase of property and equipment	(7,024,000)	(11,386,000)	(8,127,000)
<b>Net cash used in investing activities- continuing operations</b>	<b>(3,468,000)</b>	<b>(22,382,000)</b>	<b>(8,408,000)</b>
<b>Net cash provided by (used in) investing activities- discontinued operations</b>	<b>950,000</b>	<b>(220,000)</b>	<b>(3,256,000)</b>
<b>Net cash used in investing activities</b>	<b>(2,518,000)</b>	<b>(22,602,000)</b>	<b>(11,664,000)</b>
Cash Flow from Financing Activities:			
Repayment of long-term debt and capital leases	(222,000)	(3,641,000)	(1,444,000)
Decrease in note receivable	52,000	26,000	18,000
Net shares repurchased for employees taxes	(1,152,000)	-	-
Excess tax benefits from share-based compensation	275,000	383,000	1,265,000
Purchase of treasury stock	(33,894,000)	(20,081,000)	(2,764,000)
<b>Net cash used in financing activities- continuing operations</b>	<b>(34,941,000)</b>	<b>(23,313,000)</b>	<b>(2,925,000)</b>
<b>Net cash used in financing activities- discontinued operations</b>	<b>-</b>	<b>-</b>	<b>-</b>
<b>Net cash used in financing activities</b>	<b>(34,941,000)</b>	<b>(23,313,000)</b>	<b>(2,925,000)</b>
<b>NET CHANGE IN CASH AND CASH EQUIVALENTS</b>	<b>(11,923,000)</b>	<b>(3,555,000)</b>	<b>25,675,000</b>
Cash and cash equivalents - beginning of the period	36,382,000	39,937,000	14,262,000
Cash and cash equivalents - end of period	<u>\$ 24,459,000</u>	<u>\$ 36,382,000</u>	<u>\$ 39,937,000</u>
Supplemental disclosure of cash flow information:			
Interest paid	\$ 131,000	\$ 57,000	\$ 123,000
Income taxes paid	\$ 12,721,000	\$ 9,983,000	\$ 4,093,000
Supplemental disclosure of non cash activity:			
Capitalized lease additions	\$ -	\$ -	\$ 104,000

The accompanying notes are an integral part of these consolidated financial statements.

**Medifast, Inc. and Subsidiaries**  
**Notes to Consolidated Financial Statements**  
**For the Years Ended December 31, 2014, 2013 and 2012**

**1. Nature of the Business**

Medifast, Inc. (the “Company” or “Medifast”) is a Delaware corporation, incorporated in 1989. The Company’s operations are primarily conducted through seven of its wholly owned subsidiaries, Jason Pharmaceuticals, Inc., Take Shape For Life, Inc., Jason Enterprises, Inc., Jason Properties, LLC, Medifast Franchise Systems, Medifast Nutrition, Inc. and Seven Crondall, LLC. The Company is engaged in the production, distribution, and sale of weight loss and weight management products and other consumable health and diet products. Medifast, Inc.’s product lines include weight loss and management, meal replacement, and vitamins. The Company has one modern, Food and Drug Administration (“FDA”) approved facility in Owings Mills, Maryland.

The Company is engaged in the manufacturing and distribution of Medifast branded and private-label weight loss and weight management products and other consumable health and diet products. These products are sold through various channels of distribution, including the internet, call center, independent health advisors, medical professionals, franchise weight loss clinics, and direct consumer marketing supported via the phone and internet. The processing, formulation, packaging, labeling and advertising of the Company’s products are subject to regulation by one or more federal agencies, including the FDA, the Federal Trade Commission (“FTC”), the Consumer Product Safety Commission, the United States Department of Agriculture, and the United States Environmental Protection Agency.

**2. Summary of Significant Accounting Policies**

Significant accounting policies followed in the preparation of the consolidated financial statements are as follows:

**Principles of Consolidation** - The consolidated financial statements include the accounts of the Company and its wholly owned subsidiaries, Jason Pharmaceuticals, Inc., Take Shape For Life, Inc., Seven Crondall Associates, LLC, Jason Properties, LLC, Medifast Franchise Systems, Inc., Medifast Nutrition, Inc. and Jason Enterprises, Inc. All inter-Company transactions and balances have been eliminated in consolidation.

**Reclassification** – Certain amounts reported for prior periods have been reclassified to be consistent with the current period presentation. No reclassification in the consolidated financial statements had a material impact on the presentation except for the reclassifications of discontinued operations as a result of the sale and closure of the Medifast Corporate Weight Control Centers.

**Use of Estimates** – The preparation of financial statements in conformity with generally accepted accounting principles in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and reported amounts of revenue and expenses during the reporting period. Actual results could differ materially from those estimates.

**Cash and Cash Equivalents** - Cash and cash equivalents consist of cash on deposit in financial institutions, institutional money funds and other short-term investments with a maturity of 90 days or less at the time of purchase.

**Concentration of Credit Risk** – Our cash and cash equivalents and available-for-sale securities are maintained at several financial institutions, and the balances with these financial institutions often exceed the amount of insurance provided on such accounts by the Federal Deposit Insurance Corporation. The cash and cash equivalents generally are maintained with financial institutions with reputable credit, and therefore bear minimal credit risk. Historically, we have not experienced any losses due to such concentration of credit risk.

**Fair Value of Financial Instruments** - Our financial instruments include cash and cash equivalents, investment in available-for-sale securities, trade receivables and debt. The carrying amounts of cash and cash equivalents, and trade receivables approximate fair value due to their short maturities. The fair values of investment in available-for-sale securities are based on dealer quotes. The Company believes that its indebtedness approximates fair value based on current yields for debt instruments with similar terms.

**Accounts Receivable and Allowance for Sales Returns and Doubtful Accounts** - Accounts receivable are recorded net of reserves for sales returns and allowances, and net of provisions for doubtful accounts.

We review the reserves for customer returns at each reporting period and adjust them to reflect data available at that time. To estimate reserves for returns, we consider actual return rates in preceding periods. To the extent the estimate of returns changes, we will adjust the reserve, which will impact the amount of product sales revenue recognized in the period of the adjustment. Our estimates for returns have not differed materially from our actual returns. The provision for estimated returns as of December 31, 2014 and 2013 was \$290,000 and \$525,000, respectively.

Allowances for doubtful accounts are based primarily on an analysis of aged accounts receivable balances and the credit worthiness of our customers as determined by credit checks and analysis, as well as customer payment history. The allowance for doubtful accounts as of December 31, 2014 and 2013 was \$64,000 and \$122,000, respectively.

**Inventory** - Inventories consist principally of packaged meal replacements held in the Company’s warehouses. Inventory is stated at the lower of cost or market, utilizing the first-in, first-out method. The cost of finished goods includes the cost of raw materials, packaging supplies, direct and indirect labor and other indirect manufacturing costs. On a quarterly basis, management reviews inventory for unsalable or obsolete inventory.

**Investment Securities** – The Company’s investments consist of debt and equity securities classified as available-for-sale securities. Available-for-sale securities are stated at fair value, and unrealized holding gains and losses, net of the related deferred tax effect, are reported as a separate component of



accumulated other comprehensive income in stockholders' equity. Interest and dividends on marketable debt and equity securities are recognized in income when declared. Realized gains and losses, including losses from declines in value of specific securities determined by management to be other-than-temporary, if any, are included in income.

**Income Taxes** – The benefit of a tax position is recognized in the financial statements in the period during which, based on all available evidence, management believes it is more-likely-than-not that the position will be sustained upon examination, including the resolution of appeals or litigation processes, if any. Tax positions taken are not offset or aggregated with other positions. Tax positions that meet the more-likely-than-not recognition threshold are measured as the largest amount of tax benefit that is more than 50 percent likely of being realized upon settlement with the applicable taxing authority. The portion of the benefits associated with tax positions taken that exceeds the amount measured as described above is reflected as a liability for unrecognized tax benefits in the accompanying balance sheet along with any associated interest and penalties that would be payable to the taxing authorities upon examination.

We evaluated our tax positions and determined that we did not have any material uncertain tax positions requiring recognition of a liability. Our policy is to recognize interest and penalties accrued on uncertain tax positions as part of income tax expense. For the years ending December 31, 2014 and 2013, no material estimated interest or penalties were recognized for the uncertainty of certain tax positions. We file income tax returns in the United States and various states jurisdictions. With few exceptions, we are no longer subject to U.S. federal, state and local income tax examinations by tax authorities for the years before 2010.

Deferred tax assets are recognized for deductible temporary differences and deferred tax liabilities are recognized for taxable temporary differences. Temporary differences are the differences between the reported amounts of assets and liabilities and their tax bases. Deferred tax assets are reduced by a valuation allowance when, in the opinion of management, it is more likely than not that some portion or all of the deferred tax assets will not be realized. Deferred tax assets and liabilities are adjusted for the effects of changes in tax laws and rates on the date of enactment.

**Advertising Costs** - Advertising costs are expensed as incurred, except for the preparation, layout, design and production of advertising costs which are expensed when the advertisement is first used. Advertising expense for continuing operations, excluding broker fees, for the years ended December 31, 2014, 2013, and 2012, amounted to \$17 million, \$21 million, and \$26 million, respectively.

**Operating Leases** - Medifast leases retail stores, distribution facilities, and office space under operating leases. Many of our lease agreements contain tenant improvement allowances, rent holidays, rent escalation clauses, and contingent rent provisions. The Company recognizes incentives and minimum rental expenses on a straight-line basis over the terms of the leases. We commence recording rent expense on the date of initial possession, which is generally when we enter the space and begin to make improvements to properties for our intended use. For tenant improvement allowances and rent holidays, we record a deferred rent liability on the consolidated balance sheets and amortize the deferred rent over the terms of the leases as reductions to rent expense on the consolidated statements of income.

For scheduled rent escalation clauses during the lease terms or for rental payments commencing at a date other than the date of initial occupancy, we record minimum rental expenses on a straight-line basis over the terms of the leases on the consolidated statements of income. Several leases provide for contingent rents, which are determined as a percentage of gross sales in excess of specified levels. We record a contingent rent liability on the consolidated balance sheets and the corresponding rent expense when we determine achieving the specified levels is probable.

**Clinic Opening Costs** - Clinic opening costs are expensed as incurred.

**Clinic Closure Costs** - Clinic closure costs are expensed and recognized as a liability at their fair value when incurred. One-time employee severance costs are expensed and recognized as a liability when the plan is finalized by management, approved and committed to by management, and communicated to the employee. Contractual costs that will continue to be incurred (operating leases) are recognized at the cease use date. The fair value of operating lease contracts is determined based on the present value of the remaining lease payments. Other costs associated with closing the clinic or relocating employees are expensed as incurred.

**Property, Plant, and Equipment** - Property, plant and equipment are stated at cost less accumulated depreciation and amortization. The Company computes depreciation and amortization using the straight-line method over the estimated useful lives of the assets acquired as follows:

Building and building improvements	10 - 35 years
Equipment and fixtures	3 - 15 years
Leasehold Improvements	Lease term
Vehicles	5 years

The depreciation life for leasehold improvements is the lesser of the estimated useful life of the addition or the term of the related lease.

Long-lived assets are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. Recoverability of assets to be held and used is measured by a comparison of the carrying amount of an asset to estimated undiscounted future cash flows expected to be generated by the asset. If the carrying amount of an asset exceeds its estimated future cash flows, an impairment charge is recognized by the amount by which the carrying amount of the asset exceeds the fair value of the asset.

**Revenue Recognition** - Revenue is recognized net of discounts, rebates, promotional adjustments, price adjustments, and estimated returns and upon transfer of title and risk to the customer which occurs at shipping (F.O.B. terms). Upon shipment, the Company has no further performance obligations and collection is reasonably assured as the majority of sales are paid prior to shipping. Medifast Weight Control Centers program fees were recognized over the estimated service period.

**Shipping and Handling Costs** - Our shipping and handling costs for shipments of our product to our customers are included in cost of sales. All shipping and handling charges that are billed to customers are included in net revenue. All other shipping and handling costs are included in selling, general and administration expenses.

**Earnings per Share** - Basic earnings per share (“EPS”) computations are calculated utilizing the weighted average number of common shares outstanding during the periods presented. Diluted EPS is calculated utilizing the weighted average number of common shares outstanding adjusted for the effect of dilutive common stock equivalents.

The following table sets forth the computation of basic and diluted EPS for the fiscal years ended December 31:

	<u>2014</u>	<u>2013</u>	<u>2012</u>
<b>Numerator:</b>			
Income from continuing operations	\$ 21,029,000	\$ 27,135,000	\$ 18,442,000
Loss from discontinued operations	(7,848,000)	(3,166,000)	(2,566,000)
Net income	<u>\$ 13,181,000</u>	<u>\$ 23,969,000</u>	<u>\$ 15,876,000</u>
<b>Denominator:</b>			
Weighted average shares of common stock outstanding	12,670,387	13,774,083	13,721,997
Effect of dilutive common stock equivalents	<u>107,890</u>	<u>43,610</u>	<u>17,827</u>
Weighted average shares of common stock outstanding	<u>12,778,277</u>	<u>13,817,693</u>	<u>13,739,824</u>
<b>EPS:</b>			
<b>Basic earnings per share</b>			
Earnings per share from continuing operations	<u>\$ 1.66</u>	<u>\$ 1.97</u>	<u>\$ 1.34</u>
Loss per share from discontinued operations	<u>\$ (0.62)</u>	<u>\$ (0.23)</u>	<u>\$ (0.18)</u>
Earnings per share	<u>\$ 1.04</u>	<u>\$ 1.74</u>	<u>\$ 1.16</u>
<b>Diluted earnings per share</b>			
Earnings per share from continuing operations	<u>\$ 1.65</u>	<u>\$ 1.96</u>	<u>\$ 1.34</u>
Loss per share from discontinued operations	<u>\$ (0.62)</u>	<u>\$ (0.23)</u>	<u>\$ (0.18)</u>
Earnings per share	<u>\$ 1.03</u>	<u>\$ 1.73</u>	<u>\$ 1.16</u>

The calculation of diluted earnings per share excluded 62,713 options outstanding for the year ended December 31, 2014 that could potentially dilute base earnings per share in the future. No options were excluded from the calculation for years ended December 31, 2013 and 2012.

**Share-Based Compensation** - Share-based compensation, primarily restricted stock awards to employees and directors, is measured at the grant date, based on the calculated fair value of the award, and is recognized as an expense over the requisite service period.

**Comprehensive Income (Loss)** - Other comprehensive income (loss) refers to revenues, expenses, gains and losses that are not included in net income but rather are recorded directly in stockholders’ equity. Comprehensive income (loss) consists of net income and unrealized gains and losses on available-for-sale securities.

### Recent Accounting Pronouncements

We have considered all new accounting pronouncements and have concluded that there are no new pronouncements that may have a material impact on our results of operations, financial condition, or cash flows, based on current information, except for Accounting Standards Update (“ASU”) 2014-09, *Revenue from Contracts with Customers (Topic 606)* and ASU 2014-08, *Presentation of Financial Statements (Topic 205) and Property Plant, and Equipment (Topic 360): Reporting Discontinued Operations and Disclosures of Disposals of Components of an Entity*.

ASU 2014-09, *Revenue from Contracts with Customers (Topic 606)*, requires the Company to recognize revenue for the transfer of goods or services to customers for the amount the Company expects to be entitled in exchange for those goods or services. The Company will be required to identify the contract, identify the relevant performance obligations, determine the transaction price, allocate the transaction price to the performance obligations in the contract, and recognize the revenue when the entity satisfies a performance obligation. The provisions of this ASU are effective for interim and annual periods beginning after December 15, 2016. Management is currently evaluating the effect that the provisions of ASU 2014-12 will have on the Company’s financial statements.

ASU 2014-08, *Presentation of Financial Statements (Topic 205) and Property Plant, and Equipment (Topic 360): Reporting Discontinued Operations and Disclosures of Disposals of Components of an Entity*, raises the threshold for a disposal to qualify as a discontinued operation and requires new disclosures of both discontinued operations and certain other disposals that do not meet the definition of a discontinued operation. It is effective for annual periods beginning on or after December 15, 2014. The Company elected early option of the pronouncement and accounted for the discontinued operations of the Medifast Corporate Weight Control Center channel in accordance with these guidelines.

### 3. Financial Instruments

Certain financial assets and liabilities are accounted for at fair value, which is defined as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. The following fair value hierarchy prioritizes the inputs used to measure fair value:

Level 1 – Quoted prices are available in active markets for identical assets or liabilities as of the reporting date. Active markets are those in which transactions for the asset or liability occur in sufficient frequency and volume to provide pricing information on an ongoing basis.

Level 2 – Pricing inputs are other than quoted prices in active markets included in Level 1, which are either directly or indirectly observable as of the reporting date. Level 2 includes those financial instruments that are valued using models or other valuation methodologies.

Level 3 – Pricing inputs include significant inputs that are generally less observable from objective sources. These inputs may be used with internally developed methodologies that result in management’s best estimate of fair value from the perspective of a market participant.

The following table represents cash and the available-for-sale securities adjusted cost, gross unrealized gains, gross unrealized losses and fair value by significant investment category recorded as cash and cash equivalents or investment securities as of December 31, 2014 and 2013:

<b>December 31, 2014</b>							
	<u>Cost</u>	<u>Unrealized Gains</u>	<u>Unrealized Losses</u>	<u>Accrued Interest</u>	<u>Estimated Fair Value</u>	<u>Cash &amp; Cash Equivalents</u>	<u>Investment Securities</u>
Cash	\$23,894,000	\$ -	\$ -	\$ -	\$23,894,000	\$23,894,000	\$ -
Level 1:							
Money Market Accounts	565,000	-	-	-	565,000	565,000	-
Mutual Funds	10,733,000	63,000	(129,000)	-	10,667,000	-	10,667,000
Corporate Equity Securities	3,408,000	695,000	(31,000)	-	4,072,000	-	4,072,000
Government & Agency Securities	4,559,000	49,000	(5,000)	15,000	4,618,000	-	4,618,000
	<u>19,265,000</u>	<u>807,000</u>	<u>(165,000)</u>	<u>15,000</u>	<u>19,922,000</u>	<u>565,000</u>	<u>19,357,000</u>
Level 2:							
Municipal Bonds	3,652,000	78,000	(7,000)	28,000	3,751,000	-	3,751,000
Corporate Bonds	5,022,000	29,000	(12,000)	38,000	5,077,000	-	5,077,000
	<u>8,674,000</u>	<u>107,000</u>	<u>(19,000)</u>	<u>66,000</u>	<u>8,828,000</u>	<u>-</u>	<u>8,828,000</u>
<b>Total</b>	<u>\$51,833,000</u>	<u>\$ 914,000</u>	<u>\$ (184,000)</u>	<u>\$ 81,000</u>	<u>\$52,644,000</u>	<u>\$24,459,000</u>	<u>\$28,185,000</u>

<b>December 31, 2013</b>							
	<u>Cost</u>	<u>Unrealized Gains</u>	<u>Unrealized Losses</u>	<u>Accrued Interest</u>	<u>Estimated Fair Value</u>	<u>Cash &amp; Cash Equivalents</u>	<u>Investment Securities</u>
Cash	\$30,958,000	\$ -	\$ -	\$ -	\$30,958,000	\$30,958,000	\$ -
Level 1:							
Money Market Accounts	5,424,000	-	-	-	5,424,000	5,424,000	-
Mutual Funds	7,887,000	127,000	(164,000)	-	7,850,000	-	7,850,000
Corporate Equity Securities	4,614,000	1,076,000	(9,000)	-	5,681,000	-	5,681,000
Government & Agency Securities	6,112,000	62,000	(43,000)	26,000	6,157,000	-	6,157,000
	<u>24,037,000</u>	<u>1,265,000</u>	<u>(216,000)</u>	<u>26,000</u>	<u>25,112,000</u>	<u>5,424,000</u>	<u>19,688,000</u>
Level 2:							
Municipal Bonds	3,524,000	103,000	-	25,000	3,652,000	-	3,652,000
Corporate Bonds	7,995,000	74,000	(47,000)	58,000	8,080,000	-	8,080,000
	<u>11,519,000</u>	<u>177,000</u>	<u>(47,000)</u>	<u>83,000</u>	<u>11,732,000</u>	<u>-</u>	<u>11,732,000</u>
<b>Total</b>	<u>\$66,514,000</u>	<u>\$ 1,442,000</u>	<u>\$ (263,000)</u>	<u>\$ 109,000</u>	<u>\$67,802,000</u>	<u>\$36,382,000</u>	<u>\$31,420,000</u>

The Company had realized gains of \$771,000 and \$74,000 for the years ended December 31, 2014 and 2013, respectively, and a realized loss of \$2,000 for the year ended December 31, 2012.

#### 4. INVENTORY

Inventories consisted of the following at December 31, 2014 and 2013:

	<u>2014</u>	<u>2013</u>
Raw Materials	\$ 4,410,000	\$ 5,381,000
Packaging	920,000	757,000
Non-food Finished Goods	1,108,000	855,000
Finished Goods	9,689,000	10,809,000
Reserve for Obsolete Inventory	<u>(392,000)</u>	<u>(265,000)</u>
	<u>\$ 15,735,000</u>	<u>\$ 17,537,000</u>

#### 5. PROPERTY, PLANT AND EQUIPMENT

Property, plant, and equipment consisted of the following at December 31, 2014 and 2013:

	<u>2014</u>	<u>2013</u>
Land	\$ 650,000	\$ 650,000
Building and leasehold improvements	13,346,000	12,391,000
Equipment and fixtures	59,501,000	53,347,000
Vehicle	<u>149,000</u>	<u>155,000</u>
	<u>\$ 73,646,000</u>	<u>\$ 66,543,000</u>
Less accumulated depreciation and amortization	<u>40,169,000</u>	<u>32,067,000</u>
Property, plant and equipment- net	<u>\$ 33,477,000</u>	<u>\$ 34,476,000</u>

Depreciation and amortization expense for continuing operations for the years ended December 31, 2014, 2013 and 2012 was \$8,052,000, \$7,810,000, and \$7,683,000, respectively. Depreciation and amortization expense for discontinued operations related to the Medifast Corporate Weight Control Centers for the years ended December 31, 2014, 2013 and 2012 was \$1,699,000, \$3,144,000, and \$2,433,000, respectively. As a result of the sale and closure of the Medifast Weight Control Centers, the Company incurred an asset impairment loss of \$3.3 million in 2014 that is included in discontinued operations.

#### 6. ACCOUNTS PAYABLE AND ACCRUED EXPENSES

Accounts payable and accrued expenses consisted of the following at December 31, 2014 and 2013:

	<u>2014</u>	<u>2013</u>
Trade payables	\$ 12,178,000	\$ 12,031,000
Sales commissions payable	3,890,000	5,403,000
Sales tax payable	806,000	1,335,000
Accrued loan guarantee	1,980,000	-
Accrued payroll and related taxes	<u>3,000,000</u>	<u>3,461,000</u>
	<u>\$ 21,854,000</u>	<u>\$ 22,230,000</u>

#### 7. LEASES

##### Operating and Capital Leases:

As of December 31, 2014, the Company leases office space for corporate offices, a distribution facility in Texas, a raw materials warehouse in Maryland, as well as 77 leases for previously corporate-operated Medifast Weight Control Centers under lease terms ranging from five to ten years. The 77 leases include 3 Centers closed in December 2013, 34 Centers that were closed in December 2014, and 40 leases for Centers that were sold to franchise partners during 2014 and entered into sublease agreements with the franchisees. The Company accrued for the remaining lease obligations net of any sublease income, see Note 13 for exit activity and clinic obligations. Monthly payments under the Medifast Weight Control Centers leases range in price from \$1,500 to \$5,000. The Company is additionally required to pay property taxes, utilities, insurance and other costs relating to the leased facilities.

The Company leases large commercial printers for our printing operation that supports our sales channels and network equipment for information technology that are accounted for as capital leases. The leases extend through December 2016.

The following table summarizes our future minimum rental and lease payments required under non-cancelable lease terms in excess of one year as of December 31, 2014:

	<u>Operating Leases</u>	<u>Capital Leases</u>
2015	\$ 4,471,000	\$ 248,000
2016	3,633,000	248,000
2017	1,967,000	-
2018	488,000	-
2019	71,000	-
Total minimum lease payments	<u>\$ 10,630,000</u>	<u>\$ 496,000</u>
Less amount representing interest		<u>22,000</u>
Present value of minimum lease payments		\$ 474,000
Current portion		<u>232,000</u>
Long-term portion		<u>\$ 242,000</u>

Total minimum lease payments have not been reduced by minimum sublease rent income of approximately \$3.8 million due under future non-cancelable subleases.

The following is a summary of the Company's rent expense for the years ended December 31, 2014, 2013 and 2012:

	<u>2014</u>	<u>2013</u>	<u>2012</u>
Continuing Operations	\$ 1,460,000	\$ 1,400,000	\$ 1,415,000
Discontinued Operations	<u>7,189,000</u>	<u>5,233,000</u>	<u>3,956,000</u>
	<u>\$ 8,649,000</u>	<u>\$ 6,633,000</u>	<u>\$ 5,371,000</u>

Included in the discontinued operations rent expense is an accrual of \$4.4 million and \$1.1 million for the periods ended December 31, 2014 and 2013, respectively for continuing obligations for operating leases related to centers closed during the periods.

Equipment lease expense for continuing operations the years ended December 31, 2014, 2013, and 2012 was \$1.2 million, \$1.4 million, and \$1.8 million, respectively.

## 8. CONTINGENCIES

The Company filed a civil complaint on February 17, 2010 in the U.S. District Court (SD, Cal) against Barry Minkow and the Fraud Discovery Institute, Inc. (collectively, "Minkow"), iBusiness Reporting, and its editor William Lobdell, Tracy Coenen and Sequence, Inc. (collectively, "Coenen"), "Zee Yourself", and Robert L. Fitzpatrick ("FitzPatrick") for defamation, market manipulation and unfair business practices, alleging a scheme of market manipulation of Medifast stock for Defendants' for monetary gain, and damaging the business reputation of Medifast and its Take Shape For Life division. Bradley T. MacDonald, former Executive Chairman of Medifast and a stockholder, joined the lawsuit individually. The lawsuit seeks \$270 million in compensatory damages, punitive damages, and ancillary relief. In March 2011, the District Court granted in part and denied in part certain Anti-SLAPP Motions to Strike (i.e. motions to dismiss) previously filed by all Defendants. The Company appealed that portion of the District Court's ruling which dismissed its defamation claims against Minkow and Coenen in the 9th Circuit Court of Appeals. Defendant FitzPatrick's motion was denied as to the Company's defamation claim, and FitzPatrick appealed that portion of the Court's ruling. On June 4, 2014, the Panel of the 9th Circuit Court of Appeals issued a decision, denying FitzPatrick's appeal and remanding to the District Court for further consideration; reversing the District Court's decision as to Minkow and remanding for further consideration; denying MacDonald's appeal in its entirety; and denying Medifast's appeal as to Coenen. On September 26, 2014, the District Court obtained jurisdiction of the case once again and the parties set a briefing schedule on the outstanding issues remanded by the Ninth Circuit. Coenen filed a motion for attorneys' fees, which Medifast has opposed. That motion is now fully-briefed and currently remains sub judice. Medifast has been engaged in settlement discussions with Minkow and FitzPatrick. There is a status conference with the District Court scheduled for March 20, 2015.

The Company has entered into guarantee agreements with two key franchisee partners in order to support them obtaining additional funding to expand their business into new markets. This is in line with the Company's long-term strategy of expanding the franchise business utilizing knowledgeable franchise partners. The first guarantee provides financial coverage for a \$1.0 million loan and a \$1.0 million line of credit. The variable rate term loan has a 2 year term expiring in September 2015; payment calculations assume a 7 year amortization with a balloon payment due at the end of the term. The line of credit has a two year term expiring in September 2015. The franchisee associated with these loans has failed to pay the monthly obligations and the Company expects to be required to perform under this guarantee and has accrued a charge of \$2.0 million as of December 31, 2014. The Company is a secondary guarantor on the loan and line of credit and has pursued personal recourse against the franchise owner. The second guarantee provides financial coverage for a \$1.4 million loan. The variable rate term loan has a 2 year term expiring in October 2015; payment calculations assume a 7 year amortization with a balloon payment due at the end of the term. The Company is the third guarantor on these loans and has recourse against another entity owned by the franchisee and the franchisee owner(s) themselves should it be deemed necessary. As of March 10, 2015, the franchisee has an outstanding balance of \$0.1 million on the loan.

On July 20, 2012, Jason Pharmaceuticals, Inc., a wholly-owned subsidiary of the Company, signed a proposed consent decree with the Federal Trade Commission ("FTC"), in response to the FTC's investigation of certain statements in the Company's advertising for its weight-loss programs. On September 17, 2012 the consent decree was entered and approved by the United States District Court for the District of Columbia. The consent decree replaces a previous consent order entered into by Jason Pharmaceuticals, Inc. and the FTC in 1992. The FTC expressed concern that some of the Company's advertising

contained claims which were not compatible with current standards for substantiation. Pursuant to the consent decree, the Company agreed to modify certain advertising claims in this regard and agreed to ensure that its clinical studies meet the protocol contained in the consent agreement. The Company paid a civil penalty of \$3.7 million to resolve the FTC's concerns and avoid protracted legal proceedings. The Company recorded the penalty in the second quarter of 2012 as part of selling, general & administration expenses.

## 9. INCOME TAXES

The components of the income tax expense from continuing operations are as follows:

	<u>2014</u>	<u>2013</u>	<u>2012</u>
Current			
Federal	\$ 10,282,000	\$ 11,682,000	\$ 10,380,000
State	96,000	(202,000)	132,000
Total Current	<u>10,378,000</u>	<u>11,480,000</u>	<u>10,512,000</u>
Deferred			
Federal	176,000	365,000	(528,000)
State	206,000	63,000	(70,000)
Foreign	(96,000)	-	-
Total Deferred	<u>286,000</u>	<u>428,000</u>	<u>(598,000)</u>
Total Income Tax Expense from Continuing Operations	<u>\$ 10,664,000</u>	<u>\$ 11,908,000</u>	<u>\$ 9,914,000</u>

The total tax provision for the years ended December 31, 2014, 2013, and 2012 was \$4.9 million, \$10.0 million, \$7.4 million, respectively. Those amounts have been allocated to the following financial statement items:

	<u>2014</u>	<u>2013</u>	<u>2012</u>
Income from continuing operations	\$ 10,664,000	\$ 11,908,000	\$ 9,914,000
Loss from discontinued operations	(5,302,000)	(1,690,000)	(1,332,000)
Stockholders' equity, unrealized gain (loss) on investment securities	(182,000)	143,000	83,000
Additional paid in capital, share-based compensation tax benefit	(275,000)	(383,000)	(1,265,000)
Total Income Tax Expense	<u>\$ 4,905,000</u>	<u>\$ 9,978,000</u>	<u>\$ 7,400,000</u>

Deferred tax assets (liabilities) consisted of the following at December 31,

	<u>2014</u>	<u>2013</u>	<u>2012</u>
Reserves on inventory and sales	\$ 291,000	\$ 332,000	\$ 336,000
Credit and loss carryforwards	699,000	413,000	692,000
Stock compensation	1,283,000	896,000	-
Accrued expenses and deferred costs	3,170,000	1,260,000	690,000
Inventory capitalization	142,000	337,000	526,000
Sales tax accrual	8,000	337,000	1,228,000
Total deferred tax assets	<u>5,593,000</u>	<u>3,575,000</u>	<u>3,472,000</u>
Unrealized gain/loss on investments	(294,000)	(476,000)	(333,000)
Prepaid expenses	(779,000)	(710,000)	(752,000)
Depreciation	(6,285,000)	(7,091,000)	(7,729,000)
Stock compensation	-	-	(105,000)
Total deferred tax liabilities	<u>(7,358,000)</u>	<u>(8,277,000)</u>	<u>(8,919,000)</u>
Net deferred tax liabilities	<u>\$ (1,765,000)</u>	<u>\$ (4,702,000)</u>	<u>\$ (5,447,000)</u>

The differences between the United States federal statutory tax rate and the Company's effective tax rate are as follows:

	<u>2014</u>		<u>2013</u>		<u>2012</u>	
Statutory federal tax	\$ 11,093,000	35.0%	\$ 13,665,000	35.0%	\$ 9,925,000	35.0%
State income taxes, net of federal benefit	314,000	1.0%	393,000	1.0%	736,000	2.6%
Foreign Taxes	73,000	0.2%	-	0.0%	-	0.0%
Domestic manufacturer deduction	(811,000)	-2.6%	(979,000)	-2.5%	(902,000)	-3.2%
FTC settlement	-	0.0%	-	0.0%	1,389,000	4.9%
Other permanent differences	200,000	0.6%	173,000	0.4%	(190,000)	-0.7%
Research and development and jobs credits	(203,000)	-0.6%	(459,000)	-1.2%	(267,000)	-0.9%
Other state income tax benefits	(113,000)	-0.4%	(707,000)	-1.8%	(686,000)	-2.4%
Other	111,000	0.4%	(178,000)	-0.4%	(91,000)	-0.3%
	<u>\$ 10,664,000</u>	<u>33.6%</u>	<u>\$ 11,908,000</u>	<u>30.5%</u>	<u>\$ 9,914,000</u>	<u>35.0%</u>

The 2014, 2013 and 2012 effective tax rates were impacted by the Company's extensive state income tax planning. This planning includes taking advantage of Maryland's apportionment methodology. As a manufacturing entity based in Maryland, the Company utilizes the single sales factor apportionment method

in addition to claiming new state jobs credits and research & development credits. These benefits were offset in 2012 by a \$3.7 million FTC nondeductible settlement. In 2013 the Company benefited from research and development credits effective January 1, 2013, applicable retroactively to 2012 activity. In 2014 the Company benefited from research and development credits effective January 1, 2014 in addition to filing an amended federal return to claim 2010 research and development credits due to changes in Federal regulations.

The Company has separate company state net operating loss carry forwards totaling \$10.6 million start expiring in 2031. Maryland state credits carry forwards totaling \$197,000 will begin to expire in 2018.

## 10. SHARE-BASED COMPENSATION

### Stock Options:

The Company has issued non-qualified and incentive stock options to employees and nonemployee directors. The fair value of these options are estimated on the date of grant using the Black-Scholes option pricing model, which requires estimates of the expected term of the option, the expected volatility of the price of the Company's common stock, dividend yield and the risk-free interest rate. Options outstanding as of December 31, 2014 vest over a period of three years with an expiration term of ten years. The exercise price of these options ranges from \$24.26 to \$28.81. The expected volatility is based on the historical volatility of the Company's common stock over the period of time equivalent to the expected term for each award. Due to the Company's lack of option exercise history, the expected term is calculated using the simplified method defined as the midpoint between the vesting period and the contractual term of each award. The risk free interest rate is based on the U.S. Treasury yield curve in effect on the date of grant which most closely corresponds to the expected term of the option. The Company historically has not issued dividends and therefore does not utilize a dividend yield in the calculation. The weighted average input assumptions used and resulting fair values were as follows:

	2014	2013
Expected life (in years)	6	-
Risk-free interest rate	1.61%	-
Expected volatility	63.15%	-
Dividend yield	-	-

The following table summarizes the stock option activity:

	Shares	Weighted-Average Exercise Price	Weighted-Average Remaining Contractual Life (Yrs)	Aggregate Intrinsic Value
Outstanding at December 31, 2013	-	\$ -	-	-
Granted	70,542	26.11	-	-
Exercised	-	-	-	-
Forfeited	(2,778)	27.16	-	-
Expired	(389)	28.81	-	-
Outstanding at December 31, 2014	67,375	\$ 26.05	8.90	505,286
Exercisable at December 31, 2014	4,662	\$ 24.26	8.14	43,310

The weighted-average grant date fair value of options granted was \$15.19. The unrecognized compensation expense calculated under the fair value method for shares expected to vest as of December 31, 2014 was approximately \$0.6 million and is expected to be recognized over a weighted average period of 1.9 years.

### Restricted Stock:

The Company has issued restricted stock to employees and nonemployee directors generally with terms ranging up to seven years. The fair value is equal to the market price of the Company's common stock on the date of grant. Expense for restricted stock is amortized ratably over the vesting period. The following table summarizes the restricted stock activity:

	Shares	Weighted-Average Grant Date Fair Value
Unvested at December 31, 2013	393,532	\$ 24.23
Granted	23,115	28.43
Vested	(119,388)	23.68
Forfeited	(7,333)	28.81
Unvested at December 31, 2014	289,926	\$ 25.13

The total share-based compensation expense charged against income during the years ended December 31, 2014, 2013, and 2012 were \$3,918,000, \$3,209,000, and \$2,850,000, respectively. In addition to the unvested shares listed above, the Company recognized \$734,000 in share-based compensation in 2014 for 43,750 shares of performance awards to be issued to certain key employees based on achieving 2014 financial plan that will vest on December 31, 2015. The Company intends to issue additional performance awards in 2015 to certain key employees if certain 2015 financial plans are met. During 2014, the Company issued 7,000 restricted stock awards to certain key employees vesting over 3 - 4 years. The Company issued additional awards to members of the Board of Directors including: 6,850 shares to vest over a one year period and 9,265 granted in lieu of meeting fees that vested immediately. The total income tax benefit recognized in the consolidated statement of income for these restricted stock awards was approximately \$1,398,000, \$1,123,000 and \$969,000 for the years ending December 31, 2014, 2013, and 2012, respectively. The tax benefit recognized in additional paid-in capital upon vesting of restricted stock

awards was approximately \$275,000, \$383,000 and \$1,265,000 for the years ending December 31, 2014, 2013, 2012, respectively. There was approximately \$5.8 million of total unrecognized compensation cost related to restricted stock awards as of December 31, 2014. The cost is expected to be recognized over a weighted-average period of approximately 3.1 years.

## 11. LONG-TERM DEBT AND LINE OF CREDIT

The Company has an unused unsecured \$5,000,000 revolving line of credit with Bank of America at the LIBOR rate plus 1.75%, which was 1.92% at December 31, 2014. The agreement expires on August 1, 2015.

The Bank of America line of credit contains customary covenants including covenants that, in certain circumstances, restrict the Company's ability to incur additional indebtedness, pay dividends and redeem capital stock, make other payments, including investments, sell its assets and enter into consolidations, mergers and transfers of all or substantially all of its assets. The line of credit agreement also requires the Company to maintain specified financial ratios and satisfy certain financial condition tests. At December 31, 2014, the Company was in compliance with all of the required financial ratios and also met all of the financial condition tests. Upon the occurrence of an event of default under the line of credit, the lenders may cease making loans and declare amounts outstanding to be immediately due and payable.

## 12. BUSINESS SEGMENTS

As a result of the closure and sale of the Medifast Corporate Weight Control Centers, the Company re-evaluated the segment results being reported. The consolidated operating profit of the Company is reviewed by the chief operating decision maker as a single segment and sales are reviewed at the channel level.

The following table represents sales by channel for the years ended December 31, 2014, 2013 and 2012:

	<u>2014</u>	<u>2013</u>	<u>2012</u>
Medifast Direct	\$ 57,159,000	\$ 75,521,000	\$ 84,417,000
Take Shape For Life	206,657,000	228,729,000	216,094,000
Medifast Weight Control Centers - Franchise	15,424,000	15,336,000	14,309,000
Medifast Wholesale	6,045,000	4,468,000	3,751,000
Net Revenue	<u>\$ 285,285,000</u>	<u>\$ 324,054,000</u>	<u>\$ 318,571,000</u>

## 13. DISCONTINUED OPERATIONS, EXIT ACTIVITIES, AND CLINIC OBLIGATIONS

In 2014, the Company exited the MWCC corporate center model by selling 41 centers to existing franchise partners (24 centers were sold in June 2014 and the remaining 17 centers were sold in December 2014) and closing the remaining 34 corporate centers. In accordance with ASU 2014-08, *Presentation of Financial Statements (Topic 205) and Property Plant, and Equipment (Topic 360): Reporting Discontinued Operations and Disclosures of Disposals of Components of an Entity* the assets, liabilities, operating results, and cash flows of the MWCC corporate center channel have been presented separately as discontinued operations in the Consolidated Financial Statements for all periods presented.

During 2014, the Company incurred a pre-tax charge of \$8.6 million associated with the discontinued operations. This charge includes \$0.6 million for one-time termination benefits, \$4.4 million for closed clinic lease obligations, \$3.3 million for impaired assets, and \$0.5 million in other facility related closure costs. These exit activity costs were partially offset by a gain of \$0.2 million on the sale of centers.

Included in the results of discontinued operations, is \$2.1 million of clinic closure costs recorded for the closure of 8 corporate centers in December 2013 and \$7.4 million of clinic closure costs for the closure of 34 corporate centers in December 2014. As of December 31, 2014, \$6.5 million of clinic closure costs are included in accrued expenses. The accrual is comprised of \$4.6 million for closed clinic lease obligations, \$0.9 million for customer refunds, \$0.6 million for accrued severance charges, and \$0.4 million for other closure costs.

The following is a summary of the Company's operating results for discontinued operations for the years ended December 31, 2014, 2013 and 2012:

	<u>2014</u>	<u>2013</u>	<u>2012</u>
Revenue	\$ 22,509,000	\$ 32,832,000	\$ 38,135,000
Loss before income taxes from discontinued operations	(13,150,000)	(4,856,000)	(3,898,000)
Income benefit provision	(5,302,000)	(1,690,000)	(1,332,000)
Loss from discontinued operations, net of tax	<u>\$ (7,848,000)</u>	<u>\$ (3,166,000)</u>	<u>\$ (2,566,000)</u>



The following table presents the aggregate carrying amounts of the major classes of assets and liabilities divested as of December 31, 2014 included in discontinued operations:

	<u>2014</u>
<b>ASSETS</b>	
<b>Current assets:</b>	
Receivables, net	\$ 57,000
Inventory	123,000
Prepaid expenses and other current assets	4,000
<b>Total current assets</b>	<b><u>184,000</u></b>
Other assets	22,000
<b>Total assets</b>	<b><u>\$ 206,000</u></b>
<b>LIABILITIES</b>	
<b>Current liabilities:</b>	
Accounts payable and accrued expenses	\$ 4,858,000
<b>Total current liabilities</b>	<b><u>4,858,000</u></b>
Long-term lease obligations	2,756,000
<b>Total liabilities</b>	<b><u>\$ 7,614,000</u></b>

The following table summarizes the exit obligations primarily closed clinic lease obligations, severance accruals, and customer refunds incurred as of December 31, 2014:

Ending accrued balance as of December 31, 2012	\$ -
Charges incurred during the period	1,361,000
Payments during the period	-
Ending accrued balance as of December 31, 2013	\$ 1,361,000
Charges incurred during the period	6,006,000
Payments during the period	(833,000)
Ending accrued balance as of December 31, 2014	\$ 6,534,000

These charges were recorded in the balance sheet as of December 31, 2014 as follows:

Total current liabilities of discontinued operations	\$ 3,778,000
Total long-term liabilities of discontinued operations	2,756,000
Ending accrued balance as of December 31, 2014	\$ 6,534,000

#### 14. STOCKHOLDERS' RIGHTS PLAN

On August 28, 2014, the Company adopted a stockholders' rights plan whereby the Board of Directors authorized and declared a dividend distribution of one right for each outstanding share of common stock of the Company to the stockholders of record at the close of business on September 9, 2014. The rights are not presently exercisable and remain attached to the shares of common stock until the occurrence of certain triggering events. The rights will expire on August 28, 2015, unless exercised, redeemed, or exchanged prior to that time. The Board of Directors may terminate the rights plan before the expiration date. In connection with the 13D filings, the Company incurred \$2.6 million in legal expenses in 2014.

## INDEX TO EXHIBITS

### No.

- 3.1 Restated and Amended Certificate of Incorporation of the Company incorporated by reference to Exhibit 3.1 of the Company's current report on Form 8-K filed February 27, 2015.
- 3.2 Amended and Restated By Laws incorporated by reference to Exhibit 3.1 to the Company's current report on Form 10-K filed March 31, 2010.
- 3.3 Amendment to the Amended and Restated By Laws incorporated by reference to Exhibit 3.1 to the Company's current report on Form 8-K filed on February 11, 2014.
- 10.1 2012 Share Incentive Plan incorporated by reference to the Definitive Proxy Statement on Form DEFA filed July 30, 2012.\*
- 10.2 Form of Incentive Stock Option Agreement incorporated by reference to Exhibit 99.1 of the Company's current report on Form 8-K filed February 4, 2014.\*
- 10.3 Lease relating to the Company's Owings Mills, Maryland facility incorporated by reference to the Registration Statement on Form S-4 of the Company (File No. 33-81524).
- 21.1 Subsidiaries of Medifast, Inc. (filed herewith).
- 23.1 Consent of McGladrey LLP (filed herewith).
- 31.1 Certification of Chief Executive Officer pursuant to Item 601(b)(31) of Regulation S-K, as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 (filed herewith).
- 31.2 Certification of Chief Financial Officer pursuant to Item 601(b)(31) of Regulation S-K, as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 (filed herewith).
- 32 Certification of Chief Executive Officer and Chief Financial Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 (furnished herewith).
- 101 The following financial statements from Medifast, Inc.'s Annual Report on Form 10-K for the year ended December 31, 2014, filed March 16, 2015, formatted in XBRL (eXtensible Business Reporting Language): (i) Consolidated Balance Sheets, (ii) Consolidated Statements of Income, (iii) Consolidated Statements of Comprehensive Income, (iv) Consolidated Statements of Changes in Stockholders' Equity (v) Consolidated Statements of Cash Flows, and (vi) Notes to the Consolidated Financial Statements (filed herewith).

\* Indicates a management contract or compensatory plan.



**2014** ANNUAL  
REPORT

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