LANDSTAR SYSTEM INC
Form 10-Q
October 30, 2009

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

(Mark One)

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

For the quarterly period ended September 26, 2009

OR

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

For the transition period from __________ to __________

Commission File Number: 0-21238

LANDSTAR SYSTEM, INC.

(Exact name of registrant as specified in its charter)

Delaware	**06-1313069**
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

13410 Sutton Park Drive South, Jacksonville, Florida

(Address of principal executive offices)

32224

(Zip Code)

(904) 398-9400

(Registrant s telephone number, including area code)

N/A

(Former name, former address and former fiscal year, if changed since last report)

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

Yes þ No o

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

Yes o No o

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

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

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

Yes o No þ

The number of shares of the registrant s common stock, par value $0.01 per share, outstanding as of the close of business on October 16, 2009 was 50,835,499.

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PART I FINANCIAL INFORMATION

Item 1. Financial Statements

The interim consolidated financial statements contained herein reflect all adjustments (all of a normal, recurring nature) which, in the opinion of management, are necessary for a fair statement of the financial condition, results of operations, cash flows and changes in equity for the periods presented. They have been prepared in accordance with Rule 10-01 of Regulation S-X and do not include all the information and footnotes required by generally accepted accounting principles for complete financial statements. Operating results for the thirty nine weeks ended

September 26, 2009 are not necessarily indicative of the results that may be expected for the entire fiscal year ending December 26, 2009.

These interim financial statements should be read in conjunction with the audited financial statements and notes thereto included in the Company s 2008 Annual Report on Form 10-K.

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LANDSTAR SYSTEM, INC. AND SUBSIDIARY
CONSOLIDATED BALANCE SHEETS
(Dollars in thousands, except per share amounts)
(Unaudited)

	Sept. 26, 2009	Dec. 27, 2008
ASSETS		
Current Assets		
Cash and cash equivalents	$ 68,990	$ 98,904
Short-term investments	23,706	23,479
Trade accounts receivable, less allowance of $7,190 and $6,230	258,565	315,065
Other receivables, including advances to independent contractors, less allowance of $4,808 and $4,298	9,978	10,083
Deferred income taxes and other current assets	26,627	27,871
Total current assets	387,866	475,402
Operating property, less accumulated depreciation and amortization of $119,890 and $106,635	122,297	124,178
Goodwill	57,297	31,134
Other assets	50,284	32,816
Total assets	$ 617,744	$ 663,530
LIABILITIES AND EQUITY		
Current Liabilities		
Cash overdraft	$ 21,219	$ 32,065
Accounts payable	110,029	105,882
Current maturities of long-term debt	25,988	24,693
Insurance claims	26,039	23,545
Accrued income taxes	12,456	12,239
Other current liabilities	33,941	38,161
Total current liabilities	229,672	236,585
Long-term debt, excluding current maturities	49,053	111,752
Insurance claims	35,667	38,278
Deferred income taxes	28,307	23,779
Equity		
Landstar System, Inc. and subsidiary shareholders equity		
Common stock, $0.01 par value, authorized 160,000,000 shares, issued 66,192,767 and 66,109,547 shares	662	661
Additional paid-in capital	159,581	154,533
Retained earnings	749,739	704,331

Cost of 15,357,268 and 14,424,887 shares of common stock in treasury	(636,349)	(605,828)
Accumulated other comprehensive income (loss)	251	(561)
Total Landstar System, Inc. and subsidiary shareholders equity	273,884	253,136
Noncontrolling interest	1,161	
Total equity	275,045	253,136
Total liabilities and equity	$ 617,744	$ 663,530

See accompanying notes to consolidated financial statements.

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LANDSTAR SYSTEM, INC. AND SUBSIDIARY
CONSOLIDATED STATEMENTS OF INCOME
(Dollars in thousands, except per share amounts)
(Unaudited)

	Thirty Nine Weeks Ended		Thirteen Weeks Ended	
	Sept. 26, 2009	**Sept. 27, 2008**	**Sept. 26, 2009**	**Sept. 27, 2008**
Revenue	$ 1,461,081	$ 2,039,232	$ 500,670	$ 732,753
Investment income	954	2,686	279	817
Costs and expenses:				
Purchased transportation	1,090,219	1,573,209	372,328	569,864
Commissions to agents	117,735	153,857	39,484	54,267
Other operating costs	21,749	20,814	6,911	6,874
Insurance and claims	29,056	27,159	10,257	8,125
Selling, general and administrative	99,690	105,457	33,078	34,499
Depreciation and amortization	17,414	15,558	6,213	5,251
Total costs and expenses	1,375,863	1,896,054	468,271	678,880
Operating income	86,172	145,864	32,678	54,690
Interest and debt expense	3,093	5,635	957	1,757
Income before income taxes and noncontrolling interest	83,079	140,229	31,721	52,933
Income taxes	31,466	53,904	11,859	20,116
Net income	51,613	86,325	19,862	32,817
Less: Net loss attributable to noncontrolling interest	(214)		(214)	
Net income attributable to Landstar System, Inc. and subsidiary	$ 51,827	$ 86,325	$ 20,076	$ 32,817
Earnings per common share attributable to Landstar System, Inc. and subsidiary	$ 1.01	$ 1.64	$ 0.39	$ 0.62
Diluted earnings per share attributable to Landstar System, Inc. and subsidiary	$ 1.01	$ 1.62	$ 0.39	$ 0.62
Average number of shares outstanding:				
Earnings per common share	51,325,000	52,680,000	51,069,000	52,586,000
Diluted earnings per share	51,507,000	53,142,000	51,245,000	53,028,000
Dividends paid per common share	$ 0.1250	$ 0.1150	$ 0.0450	$ 0.0400

See accompanying notes to consolidated financial statements.

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LANDSTAR SYSTEM, INC. AND SUBSIDIARY
CONSOLIDATED STATEMENTS OF CASH FLOWS
(Dollars in thousands)
(Unaudited)

	Thirty Nine Weeks Ended	
	Sept. 26, 2009	Sept. 27, 2008
OPERATING ACTIVITIES		
Net income	$ 51,613	$ 86,325
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization of operating property and intangible assets	17,414	15,558
Non-cash interest charges	164	130
Provisions for losses on trade and other accounts receivable	6,364	4,684
Losses (gains) on sales/disposals of operating property	(96)	120
Director compensation paid in common stock		634
Deferred income taxes, net	3,756	5,984
Stock-based compensation	3,747	4,994
Changes in operating assets and liabilities:		
Decrease (increase) in trade and other accounts receivable	62,862	(84,527)
Decrease (increase) in other assets	4,736	(7,701)
Increase (decrease) in accounts payable	(12,635)	27,608
Increase (decrease) in other liabilities	(9,609)	1,035
Decrease in insurance claims	(117)	(4,486)
NET CASH PROVIDED BY OPERATING ACTIVITIES	128,199	50,358
INVESTING ACTIVITIES		
Net change in other short-term investments	26,334	(8,866)
Sales and maturities of investments	10,032	10,551
Purchases of investments	(43,559)	(6,921)
Purchases of operating property	(2,276)	(4,903)
Proceeds from sales of operating property	654	25
Consideration paid for acquisitions	(14,888)	
NET CASH USED BY INVESTING ACTIVITIES	(23,703)	(10,114)
FINANCING ACTIVITIES		
Increase (decrease) in cash overdraft	(10,846)	7,137
Dividends paid	(6,419)	(6,056)
Proceeds from exercises of stock options	1,116	12,249
Excess tax benefit on stock option exercises	325	2,185
Borrowings on revolving credit facility	15,000	87,000
Purchases of common stock	(31,660)	(28,519)

Capital contribution from noncontrolling interest	1,375	
Principal payments on long-term debt and capital lease obligations	(103,674)	(97,386)
NET CASH USED BY FINANCING ACTIVITIES	(134,783)	(23,390)
Effect of exchange rate changes on cash and cash equivalents	373	
Increase (decrease) in cash and cash equivalents	(29,914)	16,854
Cash and cash equivalents at beginning of period	98,904	60,750
Cash and cash equivalents at end of period	$ 68,990	$ 77,604

See accompanying notes to consolidated financial statements.

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LANDSTAR SYSTEM, INC. AND SUBSIDIARY
CONSOLIDATED STATEMENT OF CHANGES IN EQUITY
Thirty Nine Weeks Ended September 26, 2009
(Dollars in thousands)
(Unaudited)

	Landstar System, Inc. and Subsidiary Shareholders								
	Common Stock		Additional Paid-In	Retained	Treasury Stock at Cost		Accumulated Other Comprehensive Income	Non-controlling	
	Shares	Amount	Capital	Earnings	Shares	Amount	(Loss)	Interest	Total
Balance December 27, 2008	66,109,547	$661	$154,533	$704,331	14,424,887	$(605,828)	$(561)	$	$253,136
Net income (loss)				51,827				(214)	51,613
Dividends paid ($0.125 per share)				(6,419)					(6,419)
Purchases of common stock					959,704	(31,660)			(31,660)
Stock-based compensation			3,747						3,747
Exercises of stock options and granted non-vested stock, including excess tax benefit	83,220	1	1,440						1,441
Foreign currency translation							373		373
Capital contribution from noncontrolling interest								1,375	1,375
Consideration for acquisition paid in common stock			(139)		(27,323)	1,139			1,000
							439		439

Unrealized gain on available-for-sale investments, net of income taxes									
Balance September 26, 2009	66,192,767	$662	$159,581	$749,739	15,357,268	$(636,349)	$ 251	$1,161	$275,045

See accompanying notes to consolidated financial statements.

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LANDSTAR SYSTEM, INC. AND SUBSIDIARY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)

The consolidated financial statements include the accounts of Landstar System, Inc. and its subsidiary, Landstar System Holdings, Inc., and reflect all adjustments (all of a normal, recurring nature) which are, in the opinion of management, necessary for a fair statement of the results for the periods presented. The preparation of the consolidated financial statements requires the use of management s estimates. Actual results could differ from those estimates. Landstar System, Inc. and its subsidiary are herein referred to as Landstar or the Company. The Company has evaluated the impact of subsequent events through October 28, 2009, the date on which the financial statements were available to be issued, and has determined that all subsequent events have been appropriately reflected in the accompanying financial statements.

Landstar owns, through various subsidiaries, a controlling interest in A3 Integration, LLC (collectively, with its subsidiaries, A3i), a supply chain transportation integration company acquired in the first week of the Company s 2009 fiscal third quarter. Given Landstar s controlling interest in A3i, the accounts of A3i have been consolidated herein and a noncontrolling interest has been recorded for the noncontrolling investor s interests in the net assets and operations of A3i.

(1) Acquisitions

In the first week of the Company s 2009 fiscal third quarter, the Company completed the acquisition of Premier Logistics, Inc. (collectively, with its subsidiaries, Premier) and 75% of the voting interests of A3i. Consideration paid with respect to the acquisitions, net of cash acquired of $2.4 million, was approximately $15.9 million, which included 27,323 shares, or $1.0 million, of common stock of Landstar, subject to certain vesting and other restrictions including restrictions on transfer. Net liabilities acquired were approximately $16.9 million. Identified in the allocation of purchase price was approximately $9.0 million of identifiable intangible assets which are included in other assets on the consolidated balance sheets. The resulting goodwill arising from the acquisitions was approximately $26.2 million, all of which is expected to be deductible for income tax purposes. The results of operations from Premier and A3i (collectively, the Acquired Entities) are presented as part of the Company s transportation logistics segment. The Company expects that Premier and A3i will not have a material effect on its revenue and earnings for the remainder of fiscal year 2009. During 2009, the Company incurred $2,005,000, or $0.02 per common share ($0.02 per diluted share), in one-time costs related to the completion of these acquisitions.

As it relates to the noncontrolling interest of A3i, the Company has the option, during the period commencing on the fourth anniversary of June 29, 2009, the closing date of the acquisition (the Closing Date), and ending on the sixth anniversary of the Closing Date, to purchase at fair value all but not less than all of the noncontrolling interest. The noncontrolling interest is also subject to customary restrictions on transfer, including a right of first refusal in favor of the Company, and drag-along rights. For a specified period following each of the sixth, seventh and eighth anniversaries of the Closing Date, the owner of the noncontrolling interest shall have the right, but not the obligation, to sell at fair value to the Company up to one third annually of the investment then held by such owner. The owner of the noncontrolling interest also has certain preemptive rights and tag-along rights. In addition, as it relates to Premier, the Company may be required to pay additional consideration to the prior owner of Premier contingent on Premier achieving certain levels of earnings through December 2014.

(2) Share-based Payments

The Company s Board of Directors has amended and restated the Company s 2002 Employee Stock Option Plan. As amended and restated, the 2002 Employee Stock Option Plan is now called the Amended and Restated 2002 Employee Stock Option and Stock Incentive Plan (the ESOSIP). The ESOSIP was approved by vote of the Company s shareholders at the Annual Meeting of Stockholders on April 30, 2009. The amendment and restatement of the ESOSIP will, among other things, provide the Compensation Committee of the Company s Board of Directors the power to grant equity and equity-based awards in addition to stock options, including restricted stock, stock appreciation rights, performance shares and other stock-based awards. It also extends the term of the ESOSIP to 10 years after the date it was amended and restated by the Company s Board of Directors for all awards, except for incentive stock options which may not be granted after the tenth anniversary of the date the 2002 Employee Stock

Option Plan was originally adopted by the Board.

In revising the ESOSIP, the Company has not increased the number of shares available for grant under the 2002 Employee Stock Option Plan. As originally adopted, 800,000 shares were authorized for issuance. Through the adjustment provisions of the 2002 Employee Stock Option Plan, to reflect stock splits with respect to the Company s common stock, the number of shares authorized for issuance has been adjusted to be 6,400,000 shares. Awards of restricted stock, performance shares or other stock-based awards now authorized under the ESOSIP would be made from the existing pool of shares available under the 2002 Employee Stock Option Plan. Moreover, to the extent that the awards of restricted stock, performance shares or other stock-based awards provide the recipient with the full value of the shares, and the settlement of an existing obligation is not otherwise payable in cash, each share granted would count as two shares against the share limit in the ESOSIP.

As of September 26, 2009, the Company had an employee stock option plan, the ESOSIP and one stock option plan for members of its Board of Directors (the Plans). No further grants can be made under the employee stock option plan as its term for granting stock options has expired. In addition, no further grants are to be made under the stock option plan for members of the Board of Directors. Amounts recognized in the financial statements with respect to these Plans are as follows (in thousands):

	Thirty Nine Weeks Ended		Thirteen Weeks Ended	
	Sept. 26, 2009	Sept. 27, 2008	Sept. 26, 2009	Sept. 27, 2008
Total cost of the Plans during the period	$ 3,747	$ 4,994	$ 1,177	$ 1,642
Amount of related income tax benefit recognized during the period	923	1,534	273	474
Net cost of the Plans during the period	$ 2,824	$ 3,460	$ 904	$ 1,168

The fair value of each option grant on its grant date was calculated using the Black-Scholes option pricing model with the following weighted average assumptions for grants made in the 2009 and 2008 thirty-nine-week periods:

	2009	2008
Expected volatility	38.0%	33.0%
Expected dividend yield	0.400%	0.375%
Risk-free interest rate	1.50%	3.00%
Expected lives (in years)	4.0	4.1

The Company utilizes historical data, including exercise patterns and employee departure behavior, in estimating the term options will be outstanding. Expected volatility was based on historical volatility and other factors, such as expected changes in volatility arising from planned changes to the Company s business, if any. The risk-free interest rate was based on the yield of zero coupon U.S. Treasury bonds for terms that approximated the terms of the options granted. The weighted average grant date fair value of stock options granted during the thirty-nine-week periods ended September 26, 2009 and September 27, 2008 was $11.75 and $12.60, respectively.

The following table summarizes information regarding the Company s stock options under the Plans:

Number of	Weighted Average Exercise Price	Weighted Average Remaining Contractual	Aggregate Intrinsic

	Options	per Share	Term (years)	Value (000s)						
ing at December 27,										
	2,505,644	$ 35.47								
	362,000	$ 38.24								
	(71,720)	$ 15.57								
	(105,000)	$ 42.76								
ing at September 26,										
	2,690,924	$ 36.09	6.7	102,150		1,022		201,274		
non stock for executive										
	35,914	359	40,180						40,539	
non stock for board of										
sation	10,000	100	8,536						8,636	
non stock for warrants	5,259	53	(53)							
compensation program	281,431	2,814	183,323						186,137	
npensation			259,517						259,517	
							2,271,537		2,271,537	$ 2,271,537
translation					17,287				17,287	17,287
ncome										$ 2,288,824
SEPTEMBER 30, 2009	10,136,550	$ 101,366	$ 29,129,448	$	(66,548)	$	1,978,220	$	31,142,486	

Stock Options We maintain a stock option plan for the benefit of certain eligible employees and our directors. We have authorized 2,000,000 shares for grant under our Amended and Restated 2005 Stock Option Plan, and a total of 253,825 shares of common stock are reserved for additional grants of options at September 30, 2009. Generally, the options outstanding are granted at prices equal to the market value of our stock on the date of grant, generally vest over four years and expire over a period of six or ten years from the date of grant.

For the three and nine months ended September 30, 2009, we recorded stock option compensation expense of $73,400 and $259,500, respectively, compared to $96,800 and $334,400, respectively, for the three and nine months ended September 30, 2008. The compensation expense, net of tax effects, reduced diluted earnings per share by approximately $0.01 and $0.03 for the nine months ended September 30, 2009 and 2008, respectively.

As of September 30, 2009, approximately $451,000 of total unrecognized compensation costs related to non-vested awards is expected to be recognized over a weighted average period of approximately 2.11 years.

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The following table summarizes information about stock options at September 30, 2009:

		Options Outstanding			
				Options Exercisable	
Range of Exercise Prices	Number Outstanding	Weighted Average Remaining Contractual Life In Years	Weighted Average Exercise Price	Number Exercisable	Weighted Average Exercise Price
$0.94 - $1.77	76,000	5.29	$0.28	17,500	$1.20
1.90 - 2.50	83,850	2.35	3.67	58,850	2.41
2.52 - 4.54	278,050	4.30	3.97	266,800	3.97
4.56 - 6.10	637,750	3.78	5.37	360,688	5.42
	1,075,650	3.91	$4.52	703,838	$4.51

We use the Black-Scholes option pricing model using weighted average assumptions for options granted to determine the fair value of options. The fair value of options at date of grant and the assumptions utilized to determine such values are indicated in the following table:

	Three Months Ended September 30,	
	2009	2008
Risk-free interest rate	1.75%	2.99%
Expected volatility	43.9%	37.9%
Expected life (in years)	3.58	3.53
Dividend yield		
Forfeitures	13.0%	0.0%

Option transactions under the 2005 Stock Option Plan during the nine months ended September 30, 2009 are summarized as follows:

	Options	Weighted Average Exercise Price	Aggregate Intrinsic Value	Weighted Average Remaining Term
Outstanding at December 31, 2008	1,055,550	$ 4.43		
Granted	126,000	3.09		
Exercised	(102,150)	1.98		
Canceled/Forfeited	(3,750)	1.90		
Outstanding at September 30, 2009	1,075,650	$ 4.52	$ 1,201,279	3.41
Exercisable at September 30, 2009	703,838	$ 4.51	$ 790,712	3.03

Restricted Stock In connection with our employment agreement dated as of December 1, 2006 with Gregg O. Lehman, Ph.D., our President and Chief Executive Officer, on January 1, 2007 we granted an award of 25,000 shares of restricted common stock to Mr. Lehman, which was valued at a price of $5.30 per share on the date of grant. This restricted common stock vested in three equal installments on the first of the year for each of 2007, 2008 and 2009.

This restricted common stock has the same voting rights as common shares. For both the three and nine months ended September 30, 2009, we recorded stock-based compensation related to this grant of $0 compared to $5,500 and $16,500, respectively, for the three and nine months ended September 30, 2008.

On April 7, 2008, we granted an award of 10,000 shares of restricted stock to Wesley W. Winnekins, our Chief Financial Officer, under the Equity Incentive Plan (as defined below). This restricted common stock vests in two equal installments on December 31, 2008 and 2009. This restricted common stock has the same voting rights as common shares. For the three and nine months ended September 30, 2009, we recorded stock-based compensation related to this grant of $3,300 and $9,900, respectively, compared to $11,000 and $22,000, respectively, for the three and nine months ended September 30, 2008. This grant was valued using a price of $4.60 per share, which was the market value of our common stock on the date of the grant. As of September 30, 2009, $3,300 of unrecognized compensation costs related to the non-vested portion of this award will be recognized through December 31, 2009.

On December 8, 2008, we granted an award of 10,000 shares of restricted stock to J. Mark McConnell, our Senior Vice President of Business Development under the Equity Incentive Plan (as defined below). This restricted common stock vests in three equal installments on December 8 for each of 2009, 2010 and 2011. This restricted common stock has the same voting rights as common shares. For the three and nine months ended September 30, 2009, we recorded stock-based compensation related to this grant of $3,800 and $11,400, respectively. This grant was valued using a price of $2.48 per share, which was the market value of our common stock on the date of grant. As of September 30, 2009, $12,100 of unrecognized compensation costs related to the non-vested portion of this award will be recognized through November 30, 2011.

On February 26, 2009, we granted 35,914 shares of restricted stock to our executives under the Equity Incentive Plan (as defined below). This restricted common stock vests in four equal installments on February 26 of 2010, 2011, 2012, and 2013. This restricted common stock has the same voting rights as common shares. For the three and nine months ended September 30, 2009, we recorded stock-based compensation related to this grant of $8,300 and $19,300, respectively. This grant was valued using a price of $1.77 per share, which was the market value of our common stock on the date of the grant. As of September 30, 2009, $44,200 of unrecognized compensation costs related to the non-vested portion of this award will be recognized through February 26, 2013.

On May 27, 2009, we granted 10,000 shares of restricted stock to Wendy D. Lynch, a board director. This restricted common stock vests in three equal installments on May 27 for each of 2010, 2011 and 2012. This restricted common stock has the same voting rights as common shares. For the three and nine months ended September 30, 2009, we recorded stock-based compensation related to this grant of $6,500 and $8,600, respectively. This grant was valued using a price of $4.24 per share, which was the market value of our common stock on the date of grant. As of September 30, 2009, $33,800 of unrecognized compensation costs related to the non-vested portion of this award will be recognized through May 30, 2012.

Employee Stock Purchase Plan We maintain an Employee Stock Purchase Plan, which allows employees to purchase shares of our common stock at 95% of the fair market value. On May 27, 2009 we increased the total number of shares reserved for issuance under the Employee Stock Purchase Plan by 200,000 shares, thus increasing our total shares of common stock reserved for issuance to 700,000 of which 259,457 shares are unissued and remain available for issuance at September 30, 2009.

Equity Incentive Plan At our Annual Meeting of Shareholders on May 21, 2007, our shareholders approved the implementation of our 2007 Equity Incentive Plan (the Equity Plan). The Equity Plan was developed to provide our executives with restricted stock incentives if certain financial targets are achieved for calendar years 2007 through 2009. In lieu of selecting restricted stock, and at the discretion of our Board of Directors, executives can choose to receive a cash bonus under our 2007 Cash Incentive Plan (the Cash Plan). The performance objectives, and monetary potential of grants under the Cash Plan would be the same as those under the Equity Plan and participants would receive their cash bonuses at the same time as the restricted stock vests under the Equity Plan. Restricted stock granted under the Equity Plan through September 30, 2009, other than the restricted stock granted to our Chief Financial Officer in April 2008 and our Senior Vice President of Business Development in December 2008 as described previously, is earned on an annual basis upon achievement of certain financial objectives for each of 2007, 2008 and 2009. All such shares earned during these years will vest upon completion of our 2009 annual audit. For the three and nine months ended September 30, 2009, we recorded $62,000 and $186,000, respectively, of stock-based compensation related to elections under the Equity Plan, which was valued using a price of $5.56 per share, the market value of our common stock on the grant date. We also accrued $7,100 and $21,300 of bonus expense related to elections under the Cash Plan for both the three and nine months ended September 30, 2009. As of September 30, 2009, $124,100 of unrecognized compensation costs related to the non-vested portion of this program will be recognized through March 2010.

Common Stock Repurchase Plan During 2008, we repurchased 570,680 common shares at an aggregate cost of $2.3 million, including commissions of $34,000. All repurchased shares have been retired. These purchases concluded the common stock repurchase plan, announced on March 24, 2008, authorizing the Company to repurchase up to $2.5 million of its outstanding common stock.

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Reverse Stock Split On October 6, 2008 we completed a one-for-two reverse stock split in order to qualify for listing on the American Stock Exchange, now known as the NYSE AMEX. Except where specifically indicated, all common share information (including information related to stock options and other equity awards) and all per share information related to our common stock in this report has been restated to reflect the one-for-two reverse split. Pursuant to provisions in our stock options agreements and equity plans, the number of common shares available for purchase and issuance under these agreements and plans, and the exercise prices, were automatically adjusted to give proportionate effect to this reverse split.

NOTE 7. CONTINGENCIES

Legal Proceedings We are involved in various claims and lawsuits incidental to the operation of our business. We believe that the outcome of such claims will not have a material adverse effect on our financial condition, results of operation, or cash flows.

Automotive Bankruptcies On April 30, 2009, an automotive customer in our fitness management segment filed for bankruptcy protection under Chapter 11. Our outstanding receivable from this customer was approximately $34,000. The customer has paid the outstanding balance and continues to make timely payments on the continued monthly service billings. In addition, we collected receivable payments of approximately $137,000 from the customer during the 90 days before the bankruptcy filing. Such payments may constitute preferential payments recoverable under the Bankruptcy Code. We believe we have valid defenses to any potential claim for these payments and will not be required to repay the full amount. This customer has assumed our contract as of May 22, 2009. On June 1, 2009, another automotive customer in our fitness management segment filed for bankruptcy protection under Chapter 11. Our outstanding receivable from this customer was approximately $283,000. The customer has paid the outstanding balance and continues to make timely payments on the continued monthly service billings. In addition, we collected receivable payments of approximately $110,000 from the customer during the 90 days before bankruptcy. Such payments may constitute preferential payments recoverable under the Bankruptcy Code. We believe we also have valid defenses to any potential claim for these payments. This customer has assumed our contracts as of July 10, 2009. Our revenue from these customers was approximately $2,909,000 and $1,087,000 for the year ended December 31, 2008 and the nine months ended September 30, 2009, respectively.

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

You should read the following discussion and analysis of our financial condition and results of operations together with our financial statements and the related notes appearing under Item 1 of Part 1. Some of the information contained in this discussion and analysis or set forth elsewhere in this quarterly report, including information with respect to our plans and strategy for our business and expected financial results, includes forward-looking statements that involve risks and uncertainties. You should review the Risk Factors under Item 1A of the Company s Annual Report on Form 10-K for the fiscal year ended December 31, 2008 for a discussion of important factors that could cause actual results to differ materially from the results described in or implied by the forward-looking statements contained in the following discussion and analysis.

CRITICAL ACCOUNTING POLICIES

Our most critical accounting policies, which are those that require significant judgment, include: revenue recognition, trade and other accounts receivable, goodwill, stock-based compensation, income taxes, and self-funded insurance. A more in-depth description of these can be found in Note 3 to the interim consolidated financial statements included in this Quarterly Report and Note 1 of our Annual Report on Form 10-K for the fiscal year ended December 31, 2008.

BUSINESS DESCRIPTION

As a leading provider of population health improvement services and programs to corporations, hospitals, communities and universities located in the United States and Canada, we currently manage 202 corporate fitness center sites, 171 corporate health management sites and 82 unstaffed health management programs.

We provide staffing services as well as a comprehensive menu of programs, products and consulting services within our Health Management and Fitness Management business segments. Our broad suite of services enables our clients employees to live healthier lives, and our clients to control rising healthcare costs, through participation in our assessment, education, coaching, physical activity, weight management and wellness program services, which can be offered as follows: (i) through on-site fitness centers we manage; (ii) remotely via the web; and (iii) through telephonic health coaching.

RESULTS OF OPERATIONS

The following table sets forth our statement of operations data as a percentage of total revenues for the quarter ended September 30, 2009 and 2008:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2009	2008	2009	2008
REVENUE	100.0%	100.0%	100.0%	100.0%
COSTS OF REVENUE	67.4%	67.6%	68.2%	69.9%
GROSS PROFIT	32.6%	32.4%	31.8%	30.1%
OPERATING EXPENSES				
Salaries	15.9%	16.0%	16.0%	16.0%
Other selling, general and administrative	9.0%	8.0%	9.0%	9.1%
Amortization of acquired intangible assets	0.1%	0.2%	0.1%	0.2%
Total operating expenses	25.0%	24.2%	25.1%	25.3%
OPERATING INCOME	7.6%	8.2%	6.7%	4.8%
OTHER INCOME (EXPENSE)	0.0%	-0.1%	0.0%	0.0%
EARNINGS BEFORE INCOME TAXES	7.6%	8.1%	6.7%	4.8%
INCOME TAX EXPENSE	2.9%	3.5%	2.7%	2.1%

NET EARNINGS	4.7%	4.6%	4.0%	2.7%

Results of Operations for the quarter ended September 30, 2009 compared to the quarter ended September 30, 2008.

Revenue. Revenue increased $1,279,000 or 6.9%, to $19,776,000 for the three months ended September 30, 2009, from $18,497,000 for the three months ended September 30, 2008.

Fitness Management

Our Fitness Management segment declined 5.8%, or $595,000, which included a decline in staffing services of $527,000 or 5.4%, and a decline in program services of $68,000, or 11%**.** This overall revenue decline is primarily due to contract terminations we experienced in 2008 and 2009 related to customer reaction to the recessionary business climate. The decline in program services, as compared to last year, was primarily due to contract terminations and lower participation in personal training and specialty classes.

Health Management

Our Health Management segment contributed total revenue growth of 22.9%, or $1,874,000, which included growth from staffing services of $178,000, or 3.9%, and growth from program services of $1,696,000, or 46.8%. Overall, the growth in staffing revenue is attributable to new customers and the expansion of sales to existing customers. The increase in program services, compared to last year, was primarily driven by an increase in health coaching and advising services and biometric screening services.

2009 Customer Commitments and Cancellations

For the three months ended September 30, 2009, the Company received a total of four health management commitments and two fitness management commitments. This commitment activity for 2009 may realize annualized revenue of $5.2 million, to be partially offset by a potential annualized revenue loss of $0.4 million from fitness and health management contract cancellations. These cancellations reflect the continuing weakness in the economy and the financial challenges companies expect to face in the foreseeable future.

Gross Profit. Gross profit increased $453,000 or 7.6%, to $6,441,000 for the three months ended September 30, 2009, from $5,987,000 for the three months ended September 30, 2008. Total gross margin increased to 32.6%, from 32.4% for the same period last year, which is primarily due to Health Management revenue representing a larger percentage of our total revenue.

Fitness Management

Fitness Management gross profit decreased $172,000, which includes a decrease of $182,000 from staffing services, partially offset by an increase of $10,000 from program services. Gross margin for our Fitness Management segment decreased in the three months ended September 30, 2009 to 24.6%, from 24.9% for the same period of 2008. This result is primarily due to a gross margin decrease in staffing services, which decreased from 24.3% for the same period last year, to 23.7%, partially offset by a gross margin increase in program services, which increased from 33.8% for the same period last year, to 39.8%. The margin decrease for staffing services is primarily due to increased wage costs. The margin increase for program services is primarily due to labor efficiencies for personal training and massage services.

Health Management

Health Management gross profit increased $625,000, which includes an increase of $672,000 from program services, reduced by a decrease of $47,000 from staffing services. Gross margin for our Health Management segment decreased in the three months ended September 30, 2009 to 40.3%, from 41.8% for the same period of 2008. This result is

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primarily due to a gross margin decrease in program services, which decreased from 59.1% for the same period last year, to 52.9%, further reduced by a gross margin decrease in staffing services, which decreased from 28.1% for the same period last year, to 26.1%. The margin decrease for staffing services is primarily due to higher costs for employee paid time off and increased wage costs. The margin decrease in program services is primarily due to the mix of programs delivered, the addition of telephonic health coaches during the quarter and higher costs for our eHealth platform.

Operating Expenses and Operating Income. Operating expenses increased $473,000, or 10.6%, to $4,952,000 for the three months ended September 30, 2009, from $4,479,000 for the three months ended September 30, 2008.

The increase is primarily due to higher costs for management incentive programs and higher customer service costs that reflect the growth in health improvement programs. For the three months ended September 30, 2009, operating expenses, as a percent of revenue, were 25.0%, compared to 24.2% for the same period last year.

Operating margin decreased to 7.5% for the three months ended September 30, 2009, from 8.2% for the same period last year. This result reflects the higher operating expenses, as discussed above, reduced by sales growth in our Health Management segment.

Other Income and Expense. Interest expense was inconsequential during the quarters ended September 30, 2009 and 2008.

Income Taxes. Income tax expense decreased $74,000 to $577,000 for the three months ended September 30, 2009, from $651,000 for the three months ended September 30, 2008. The decrease is due primarily to a lower effective tax rate for the quarter ended September 30, 2009, compared to the same period of 2008.

Our effective tax rate was 38.7% of earnings before income taxes for the third quarter of 2009, compared to 43.6% for the same period last year. The lower effective tax rate as compared to the corresponding period of 2008 is primarily due to the lower non-deductible stock based compensation expense in proportion to earnings before income taxes.

Net Earnings. Net earnings increased $71,000 to $912,000 for the three months ended September 30, 2009, from $841,000 for the three months ended September 30, 2008. This increase is primarily due to the sales growth in our Health Management segment and lower income taxes, reduced by higher operating expenses, as discussed above.

Results of Operations for the nine months ended September 30, 2009 compared to the nine months ended September 30, 2008.

Revenue. Revenue increased $1,749,000, or 3.1%, to $57,764,000 for the nine months ended September 30, 2009, from $56,015,000 for the nine months ended September 30, 2008.

Fitness Management

Our Fitness Management segment declined $1,697,000, which included a decline in staffing services of $1,596,000 and a decline in program services of $101,000**.** This revenue decline is primarily due to contract terminations in 2008 and 2009, and lower participation in personal training and specialty classes.

If the economic recession continues for the remainder of 2009, it is possible we could continue to experience a higher level of staffing services revenue loss in our Fitness Management segment. Our most at risk contracts include those in the automotive industry, although we believe the current recession may have an adverse impact on many industries, which could affect our other customers and lead to further revenue loss from contract termination or service reduction. With respect to the automotive industry, we have lost approximately $1.4 million in revenue when comparing the nine month period ended September 30, 2009 to the corresponding period of 2008. During 2009, we expect to realize approximately $1.4 million in revenue from our at risk automotive contracts, and if their financial difficulties continue, we may see additional revenue losses.

It is also possible we could experience further declines in Fitness Management program service revenue during 2009. Program service revenue is derived from fees we charge to members of our managed fitness centers for services such as personal training, massage therapy, weight loss programs and special fitness classes. The revenue decline we experienced in the first half of 2009 is attributed to the effects of the recessionary economy, employment reductions and our members decreasing their spending on discretionary services. We believe this trend will continue during 2009. Because we are the largest provider of fitness management services in the United States, we believe the number of opportunities to bid on new business during 2009 should be consistent with past years. In order to increase our chances of winning new business in 2009 and reverse the historical decline of our fitness management revenue, we also believe that we will need to lower our pricing to be competitive in this market, which may result in lower profitability.

Health Management

Our Health Management segment contributed total growth of $3,446,000, which includes growth of $505,000 from staffing services and growth of $2,941,000 from program services. Overall, the growth in staffing revenue is attributable to new customers and the expansion of sales to existing customers. The increase in program services revenue is primarily due to an increase in our core health programs, including biometric screening services, health coaching and advising services and eHealth platform revenue.

For 2009, we anticipate that the economic recession may have a negative impact on revenue from existing customers. It is possible that many of our health management customers may reduce the scope of, or eliminate their programs during 2009 as a measure to conserve cash and improve profitability. Our health management revenue may also be negatively affected by lower participation rates at some customers due to employee layoffs. At the same time, the recessionary economy has also lengthened the sales cycle for new opportunities. The combination of these events, if they materialize, may challenge our ability to increase 2009 revenue on a basis consistent with past growth.

2009 Customer Commitments and Cancellations

For the nine months ended September 30, 2009, the Company received a total of eleven health management commitments, three expansions of health management services to existing clients, and seven fitness management commitments. This commitment activity for 2009 may realize annualized revenue of $11.2 million, to be partially offset by a projected annualized revenue loss of $2.2 million from fitness and health management contract cancellations. These cancellations reflect the continuing weakness in the economy and the financial challenges companies expect to face in the foreseeable future.

Gross Profit. Gross profit increased $1,478,000, or 8.8%, to $18,344,000 for the nine months ended September 30, 2009, from $16,866,000 for the nine months ended September 30, 2008. Total gross margin in the nine months ended September 30, 2009 increased to 31.8% from 30.1% for the same period last year, which is primarily due to Health Management revenue representing a larger percentage of our total revenue and improved margins for Health Management program services.

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Fitness Management

Fitness Management gross profit decreased $344,000, which includes a decrease of $393,000 from staffing services, partially offset by an increase of $49,000 from program services. Gross margin for our Fitness Management segment increased in the nine months ended September 30, 2009 to 24.3%, from 24.1% for the same period of 2008. This result is primarily due to a gross margin increase in program services, which increased from 36.1% for the same period last year, to 40.9%. Gross margin in staffing services remained flat at 23.3%. The margin increase for program services is primarily due to the mix of programs delivered and labor efficiencies for personal training and massage services.

Health Management

Our Health Management segment contributed gross profit growth of $1,823,000, which includes growth of $1,883,000 from program services and a decline of $60,000 from staffing services. Gross margin for our Health Management segment increased in the nine months ended September 30, 2009 to 39.5%, from 37.6% for the same period of 2008. This result is primarily due to a gross margin increase in program services, which increased from 51.5% for the same period last year, to 54.1%, reduced by a gross margin decrease in staffing services, which decreased from 25.8% for the same period last year, to 24.4%. The margin decrease for staffing services is primarily due to higher costs for employee paid time off, medical benefits, workers compensation and increased wage costs. The margin increase in program services is primarily due to increased margins on health coaching and advising services and biometric screening services.

Operating Expenses and Operating Income. Operating expenses increased $364,000, or 2.6%, to $14,523,000 for the nine months ended September 30, 2009, from $14,159,000 for the nine months ended September 30, 2008. The increase is primarily due to higher costs for management incentive programs and higher customer service costs that reflect the growth in health improvement programs. For the nine months ended September 30, 2009, operating expenses, as a percent of revenue, were 25.1%, compared to 25.3% for the same period last year.

Operating margin increased to 6.6% for the nine months ended September 30, 2009, from 4.8% for the same period in 2008. This result reflects the sales growth in our Health Management segment and cost efficiencies related to Health Management segment program services, reduced by the decrease in Fitness Management segment sales. Since 2009 revenue growth may be challenged by recessionary pressures, our strategies to maximize our operating profitability will focus on closely managing operating expenses and improving business processes.

Other Income and Expense. Interest expense was inconsequential for the nine months ended September 30, 2009 and 2008.

Income Taxes. Income tax expense increased $393,000 to $1,552,000 for the nine months ended September 30, 2009, from $1,159,000 for the nine months ended September 30, 2008. The increase is due to a higher operating income for the first nine months of 2009 as compared to the same period last year.

Our effective tax rate was 40.6% of earnings before income taxes for the nine months ended September 30, 2009, compared to 43.1% for the same period last year. The lower effective tax rate as compared to the corresponding period of 2008 is primarily due to the lower non-deductible stock based compensation expense in proportion to earnings before income taxes.

Net Earnings. Net earnings applicable to common shareholders increased $743,000 to $2,272,000 for the nine months ended September 30, 2009, from $1,529,000 for the nine months ended September 30, 2008. This increase is primarily due to sales growth in our Health Management segment and cost efficiencies related to Health Management segment program services, reduced by the decrease in Fitness Management segment sales.

LIQUIDITY AND CAPITAL RESOURCES

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Our working capital increased $2,921,000 to $13,619,000 for the nine months ended September 30, 2009, from $10,698,000 at December 31, 2008. This increase is largely attributable to our improved operating results and cash accumulation strategy given current economic conditions.

In addition to cash flows generated from operating activities, our other primary source of liquidity and working capital is provided by a $3,500,000 Credit Agreement with Wells Fargo Bank, N.A. (the Wells Loan). Effective with the renewal of the Wells Loan on March 24, 2009, interest will be computed using the daily three month LIBOR rate plus a markup of 2.75% (effective rate of 3.048% and 3.25% at September 30, 2009 and December 31, 2008, respectively). The Wells Loan matures on June 30, 2011, as amended. Working capital advances from the Wells Loan are based upon a percentage of our eligible accounts receivable, less any amounts drawn and outstanding. The facility provided maximum borrowing capacity of $3,250,000 at September 30, 2009 and December 31, 2008, respectively and no debt was outstanding on those dates. There were no borrowings under the line of credit during the nine months ended September 30, 2009. Although we do not anticipate borrowing from the Wells Loan in 2009, we have extended the agreement, as previously discussed, to provide an additional source of funding. All borrowings are collateralized by substantially all of our assets. At September 30, 2009, we were in compliance with all of our financial covenants and expect to remain in compliance with the covenants over the life of the credit agreement.

We believe our short and long-term capital needs will be met with cash flows generated by operations. We anticipate investment activities in 2009 will be near 2008 levels and will be funded through operating cash flows. Capitalized software development costs, as previously discussed, are primarily related to enhancements to our eHealth platform. These enhancements are made to improve efficiencies and/or generate additional revenues and are, thus, discretionary in nature.

We did not see a material change in the payment activities of our customers in 2008 and do not anticipate a material change in 2009. We do, however, expect to realize approximately $2.2 million in revenue from our existing automotive contracts in 2009, including $1.4 million from at risk automotive clients, and will continue to monitor their financial health as it relates to outstanding accounts receivable. On April 30, 2009, an automotive customer in our fitness management segment filed for bankruptcy protection under Chapter 11. Our outstanding receivable from this customer was approximately $34,000. The customer has paid the outstanding balance and continues to make timely payments on the continued monthly service billings. In addition, we collected receivable payments of approximately $137,000 from the customer during the 90 days before the bankruptcy filing. Such payments may constitute preferential payments recoverable under the Bankruptcy Code. We believe we have valid defenses to any potential claim for these payments and will not be required to repay the full amount. This customer has assumed our contract as of May 22, 2009. On June 1, 2009, another automotive customer in our fitness management segment filed for bankruptcy protection under Chapter 11. Our outstanding receivable from this customer was approximately $283,000. The customer has paid the outstanding balance and continues to make timely payments on the continued monthly service billings. In addition, we collected receivable payments of approximately $110,000 from the customer during the 90 days before bankruptcy. Such payments may constitute preferential payments recoverable under the Bankruptcy Code. We believe we also have valid defenses to any potential claim for these payments. This customer has assumed our contracts as of July 10, 2009. Our revenue from these customers was approximately $2,909,000 and $1,087,000 for the year ended December 31, 2008 and the nine months ended September 30, 2009, respectively.

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INFLATION

We do not believe that inflation has significantly impacted our results of operations in any of the last three completed fiscal years.

OFF-BALANCE SHEET ARRANGEMENTS

As of September 30, 2009, the Company had no off-balance sheet arrangements or transactions with unconsolidated, limited purpose entities.

PRIVATE SECURITIES LITIGATION REFORM ACT

The Private Securities Litigation Reform Act of 1995 provides a safe harbor for forward-looking statements. Such forward-looking information is included in this Form 10-K, including this Item 7, as well as in other materials filed or to be filed by the Company with the Securities and Exchange Commission (as well as information included in oral statements or other written statements made or to be made by the Company).

Forward-looking statements include all statements based on future expectations and specifically include, among other things, statements relating to revenue loss in our Fitness Management segment; our belief the current recession may have an adverse impact on many industries, which could affect our customers and lead to further revenue loss from contract termination or service reduction; our belief that revenue decline will continue during 2009 due to the effects of the recessionary economy, employment reductions and our members decreasing their spending on discretionary services; our belief that the number of opportunities to bid on new fitness management business during 2009 should be consistent with past years; our belief that we will need to lower our pricing to be competitive in the fitness management market, which may result lower profitability; our ability to increase 2009 revenue on a basis consistent with past growth; our expectation that we will not borrow from the Wells Loan in 2009 and that we will remain in compliance with all of our financial covenants over the life of the credit agreement; our belief that our short and long-term capital needs will be met with cash flows generated by operations; our anticipation that investment activities in 2009 will be at or below 2008 levels and will be funded through operating cash flows; our anticipation that we will not see a material change in the payment activities of our customers in 2009; statements regarding the potential effects of automotive company bankruptcies on our accounts receivable, contract continuation and prior payments and related claims and defenses regarding repayment of preferential payments, and our belief that inflation has not significantly impacted our results of operations in any of the last three completed fiscal years, as well as statements regarding projections and outlook relating to the industries in which we compete and the economy in general, increasing revenue, improving margins, marketing efforts, competitive conditions, the effect of price competition and changes to the economy, and the sufficiency of our liquidity and capital resources. In addition, the estimated annualized revenue value of our new, lost and existing contracts is a forward looking statement, which is based upon an estimate of the anticipated annualized revenue to be realized or lost. Such information should be used only as an indication of the activity we have recently experienced in our two business segments. These estimates, when considered together, should not be considered an indication of the total net, incremental revenue growth we expect to generate in any year, as actual net growth may differ from these estimates due to actual staffing levels, participation rates and contract duration, in addition to other revenue we may lose in the future due to contract termination. Any statements that are not based upon historical facts, including the outcome of events that have not yet occurred and our expectations for future performance, are forward-looking statements. The words potential, believe, estimate, expect, intend, may, could, will, plan, anticipate, and similar words and expressions are intend forward-looking statements. Such statements are based upon the current beliefs and expectations of our management. Such forward-looking information involves important risks and uncertainties that could significantly affect anticipated results in the future and, accordingly, such results may differ from those expressed in any forward-looking statements made by or on behalf of the Company. These risks and uncertainties include, but are not limited to, our inability to deliver the health management services demanded by major corporations and other clients, our inability to successfully cross-sell health management services to our fitness management clients, our inability to successfully obtain new business opportunities, our failure to have sufficient resources to make investments, our ability to make investments and implement strategies successfully,

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continued delays in obtaining new commitments and implementing services, the continued deterioration of general economic conditions, the actions of automotive customers and bankruptcy courts, and those matters identified and discussed in Item 1A of the 2008 Form 10-K under Risk Factors.

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

We are exposed to market risks related to changes in U.S. and international interest rates. The Company s borrowings under the Wells Loan bear interest at a variable rate. There were no borrowings outstanding under the Wells Loan at September 30, 2009.

We have no history of, nor do we anticipate in the future, investing in derivative financial instruments, derivative commodity instruments or other such financial instruments. We invoice our Canadian customers in their local currency, and such transactions are considered immaterial in relation to our total billings. As a result, the exposure to foreign currency fluctuations and other market risks is not material.

ITEM 4. CONTROLS AND PROCEDURES

Our Chief Executive Officer and Chief Financial Officer, referred to collectively herein as the Certifying Officers, are responsible for establishing and maintaining our disclosure controls and procedures. The Certifying Officers have reviewed and evaluated the effectiveness of the Company s disclosure controls and procedures (as defined in Rules 240.13a-15(e) and 15d-15(e) promulgated under the Securities Exchange Act of 1934) as of September 30, 2009. Based on that review and evaluation, which included inquiries made to certain other employees of the Company, the Certifying Officers have concluded that, as of the end of the period covered by this Report, the Company s disclosure controls and procedures, as designed and implemented, are effective in ensuring that information relating to the Company required to be disclosed in the reports that the Company files or submits under the Securities Exchange Act of 1934 is recorded, processed, summarized and reported within the time periods specified in the Securities and Exchange Commission s rules and forms, including ensuring that such information is accumulated and communicated to the Company s management, including the Chief Executive Officer and the Chief Financial Officer, as appropriate to allow timely decisions regarding required disclosure.

There were no changes in the Company s internal controls over financial reporting during the quarter ended September 30, 2009 that may have materially affected, or are reasonably likely to materially affect, the Company s internal control over financial reporting.

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PART II. OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS

Refer to Item 3 (Legal Proceedings) in the Company s Annual Report on Form 10-K for the year ended December 31, 2008.

ITEM 1A. RISK FACTORS

In addition to the other information set forth in this report, including the important information in Private Securities Litigation Reform Act, you should carefully consider the Risk Factors discussed in our Annual Report on Form 10-K for the year ended December 31, 2008. Those factors, if they were to occur, could cause our actual results to differ materially from those expressed in our forward-looking statements in this report, and materially adversely affect our financial condition or future results. Although we are not aware of any other factors that we currently anticipate will cause our forward-looking statements to differ materially from our future actual results, or materially affect the Company s financial condition or future results, additional risks and uncertainties not currently known to us or that we currently deem to be immaterial might materially adversely affect our actual business, financial condition and/or operating results.

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

None.

ITEM 3. DEFAULTS UPON SENIOR SECURITIES

None.

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

None

ITEM 5. OTHER INFORMATION

None

ITEM 6. EXHIBITS

(a) Exhibits See Exhibit Index on page following signatures

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SIGNATURES

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

Dated: November 12, 2009	HEALTH FITNESS CORPORATION
	By /s/ Gregg O. Lehman Gregg O. Lehman President and Chief Executive Officer (Principal Executive Officer)
	By /s/ Wesley W. Winnekins Wesley W. Winnekins Chief Financial Officer and Treasurer (Principal Financial and Accounting Officer)

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EXHIBIT INDEX
HEALTH FITNESS CORPORATION
FORM 10-Q

Exhibit No.	Description
**11.0	Statement re: Computation of Earnings per Share
**31.1	Certification of President and Chief Executive Officer Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
**31.2	Certification of Chief Financial Officer Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
**32.1	Certification of President and Chief Executive Officer Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002
**32.2	Certification of Chief Financial Officer Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002

** Filed herewith