

MusclePharm Corp
Form 10-Q
August 10, 2015
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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-Q

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

For the quarterly period ended: June 30, 2015

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: 000-53166

MusclePharm Corporation

(Exact name of registrant as specified in its charter)

| | |
|-------------------------------------------------------------|----------------------------|
| Nevada (State or other jurisdiction of | 77-0664193 |
| incorporation or organization) | (I.R.S. Employer |
| 4721 Ironton Street, Building A | Identification No.) |
| Denver, Colorado | 80239 |
| (Address of principal executive offices) | (Zip code) |
| (303) 396-6100 | |
| (Registrant's telephone number, including area code) | |

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 past 12 months, and (2) has been subject to such filing requirements for the past 90 days. Yes No

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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 whether the registrant is a large accelerated filer, an accelerated filer, or 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:

Large accelerated filer Accelerated filer

Non-accelerated filer Smaller reporting company

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

Number of shares of the registrant's common stock outstanding at July 24, 2015: 13,706,929 excludes 875,621 common shares held in treasury.

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NOTE ABOUT FORWARD-LOOKING STATEMENTS

This Quarterly Report on Form 10-Q contains forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995. All statements contained in this Quarterly Report on Form 10-Q other than statements of historical fact, including statements regarding our future results of operations and financial position, our business strategy and plans, and our objectives for future operations, are forward-looking statements. The words believe, may, will, estimate, continue, anticipate, intend, expect, and similar expressions are intended to identify forward-looking statements. We have based these forward-looking statements largely on our current expectations and projections about future events and trends that we believe may affect our financial condition, results of operations, business strategy, short-term and long-term business operations and objectives, and financial needs. These forward-looking statements are subject to a number of risks, uncertainties and assumptions, including those described in Part II, Item 1A, Risk Factors in this Quarterly Report on Form 10-Q. Moreover, we operate in a very competitive and rapidly changing environment. New risks emerge from time to time. It is not possible for our management to predict all risks, nor can we assess the impact of all factors on our business or the extent to which any factor, or combination of factors, may cause actual results to differ materially from those contained in any forward-looking statements we may make. In light of these risks, uncertainties and assumptions, the future events and trends discussed in this Quarterly Report on Form 10-Q may not occur and actual results could differ materially and adversely from those anticipated or implied in the forward-looking statements.

We undertake no obligation to revise or publicly release the results of any revision to these forward-looking statements, except as required by law. Given these risks and uncertainties, readers are cautioned not to place undue reliance on such forward-looking statements.

Table of Contents**PART I FINANCIAL INFORMATION****Item 1. Financial Statements****MusclePharm Corporation****Consolidated Balance Sheets***(In thousands, except share and per share data)*

| | June 30, 2015 (Unaudited) | December 31, 2014 |
|--------------------------------------------------------------------------------------------------------------------------|------------------------------------------|------------------------------|
| ASSETS | | |
| Current assets: | | |
| Cash | \$ 4,170 | \$ 1,020 |
| Accounts receivable, net of allowance for doubtful accounts of \$229 and \$159 as of June 30, 2015 and December 31, 2014 | 24,607 | 16,644 |
| Inventory | 14,850 | 21,069 |
| Prepaid giveaways | 896 | 1,228 |
| Prepaid stock compensation, current portion | 4,573 | 4,476 |
| Prepaid sponsorship and endorsement fees | 448 | 238 |
| Prepaid expenses and other current assets | 3,620 | 1,742 |
| Total current assets | 53,164 | 46,417 |
| Property and equipment, net | 7,632 | 7,805 |
| Long-term investments | 977 | |
| Intangible assets, net | 8,973 | 7,074 |
| Prepaid stock compensation, noncurrent portion | 4,110 | 4,952 |
| Other assets | 235 | 108 |
| TOTAL ASSETS | \$ 75,091 | \$ 66,356 |
| LIABILITIES AND STOCKHOLDERS EQUITY | | |
| Current liabilities: | | |
| Accounts payable | \$ 37,834 | \$ 27,761 |
| Accrued liabilities | 9,121 | 7,023 |
| Line of credit | 6,000 | 8,000 |
| Term loan, current portion | 1,267 | |
| Other debt obligations | 21 | 46 |
| Total current liabilities | 54,243 | 42,830 |
| Term loan, noncurrent portion | 2,318 | |
| Other long-term liabilities | 361 | 146 |
| TOTAL LIABILITIES | 56,922 | 42,976 |

Commitments and contingencies (Note 8)

Stockholders' equity:

| | | |
|--------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|------------------|------------------|
| Common stock, par value of \$0.001 per share; 100,000,000 shares authorized as of June 30, 2015 and December 31, 2014; 14,660,596 and 13,996,007 shares issued as of June 30, 2015 and December 31, 2014; 13,784,975 and 13,120,386 shares outstanding as of June 30, 2015 and December 31, 2014 | 14 | 14 |
| Additional paid-in capital | 138,600 | 129,130 |
| Treasury stock, at cost; 875,621 shares as of June 30, 2015 and December 31, 2014 | (10,039) | (10,039) |
| Accumulated other comprehensive loss | (243) | (66) |
| Accumulated deficit | (110,163) | (95,659) |
| TOTAL STOCKHOLDERS' EQUITY | 18,169 | 23,380 |
| TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY | \$ 75,091 | \$ 66,356 |

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

Table of Contents**MusclePharm Corporation****Consolidated Statements of Operations***(In thousands, except share and per share data)**(Unaudited)*

| | Three Months Ended | | Six Months Ended June 30, | |
|--------------------------------------------------------------------------------|--------------------|------------|---------------------------|------------|
| | 2015 | 2014 | 2015 | 2014 |
| Revenue, net | \$ 50,476 | \$ 46,741 | \$ 91,798 | \$ 96,950 |
| Cost of revenue | 32,978 | 31,094 | 59,916 | 63,430 |
| Gross profit | 17,498 | 15,647 | 31,882 | 33,520 |
| Operating expenses: | | | | |
| Advertising and promotion | 8,285 | 5,920 | 15,510 | 12,248 |
| Salaries and benefits | 7,763 | 5,777 | 14,824 | 11,144 |
| Selling, general and administrative | 5,121 | 2,357 | 10,083 | 4,229 |
| Research and development | 921 | 1,164 | 1,886 | 2,261 |
| Professional fees | 2,064 | 1,292 | 3,519 | 2,077 |
| Total operating expenses | 24,154 | 16,510 | 45,822 | 31,959 |
| (Loss) income from operations | (6,656) | (863) | (13,940) | 1,561 |
| Other (expense) income, net | (348) | (27) | (531) | 317 |
| (Loss) income before provision for income taxes | (7,004) | (890) | (14,471) | 1,878 |
| Provision for income taxes | 21 | 45 | 33 | 77 |
| Net (loss) income | \$ (7,025) | \$ (935) | \$ (14,504) | \$ 1,801 |
| Net (loss) income per share, basic | \$ (0.51) | \$ (0.09) | \$ (1.08) | \$ 0.17 |
| Net (loss) income per share, diluted | \$ (0.51) | \$ (0.09) | \$ (1.08) | \$ 0.15 |
| Weighted-average shares used in computing net (loss) income per share, basic | 13,647,267 | 10,610,022 | 13,491,433 | 10,459,522 |
| Weighted-average shares used in computing net (loss) income per share, diluted | 13,647,267 | 10,610,022 | 13,491,433 | 11,863,882 |

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

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MusclePharm Corporation
Consolidated Statements of Comprehensive (Loss) Income

(In thousands)

(Unaudited)

| | Three Months Ended June 30, | | Six Months Ended June 30, | |
|---------------------------------------------------|------------------------------------|-------------|----------------------------------|-------------|
| | 2015 | 2014 | 2015 | 2014 |
| Net (loss) income | \$ (7,025) | \$ (935) | \$ (14,504) | \$ 1,801 |
| Other comprehensive (loss) income: | | | | |
| Change in foreign currency translation adjustment | (97) | 23 | (177) | 19 |
| Comprehensive (loss) income | \$ (7,122) | \$ (912) | \$ (14,681) | \$ 1,820 |

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

Table of Contents**MusclePharm Corporation****Consolidated Statement of Stockholders Equity***(In thousands, except share data)**(Unaudited)*

| | | Common Stock | | Additional | Treasury | Accumulated Other Comprehensive Income | Accumulated Deficit | Total Stockholders Equity |
|----------------------------------------------------------------------------------------------------------------|-------------------|--------------|--------|-----------------|-------------|-------------------------------------------------|------------------------|---------------------------------|
| | | Shares | Amount | Paid-In Capital | Stock | (Loss) | | |
| Balance | December 31, 2014 | 13,120,386 | \$ 14 | \$ 129,130 | \$ (10,039) | \$ (66) | \$ (95,659) | \$ 23,380 |
| Issuance of common stock warrants to third parties for services | | | | 50 | | | | 50 |
| Stock-based compensation related to issuance of restricted stock awards to employees, executives and directors | | 244,589 | | 6,211 | | | | 6,211 |
| Stock issued in conjunction with product line expansion | | 150,000 | | 1,198 | | | | 1,198 |
| Stock issued in conjunction with MusclePharm apparel rights acquisition | | 170,000 | | 1,394 | | | | 1,394 |
| Stock issued in conjunction with financing agreement | | 50,000 | | 325 | | | | 325 |
| Stock issued in conjunction with non-employee consulting/endorsement agreement | | 50,000 | | 292 | | | | 292 |
| Change in foreign currency translation adjustment | | | | | | (177) | | (177) |
| Net loss | | | | | | | (14,504) | (14,504) |
| Balance | June 30, 2015 | 13,784,975 | \$ 14 | \$ 138,600 | \$ (10,039) | \$ (243) | \$ (110,163) | \$ 18,169 |

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

Table of Contents**MusclePharm Corporation****Consolidated Statements of Cash Flows***(In thousands)**(Unaudited)*

| | Six Months Ended June 30, | |
|--------------------------------------------------------------------------------------|----------------------------------|-------------|
| | 2015 | 2014 |
| CASH FLOWS FROM OPERATING ACTIVITIES | | |
| Net (loss) income | \$ (14,504) | \$ 1,801 |
| Adjustments to reconcile net (loss) income to net cash used in operating activities: | | |
| Depreciation of property and equipment | 838 | 647 |
| Amortization of intangible assets | 498 | 578 |
| Provision for doubtful accounts | 98 | 140 |
| Amortization of prepaid stock compensation | 2,236 | 1,578 |
| Amortization of prepaid sponsorship and endorsement fees | 3,252 | 3,468 |
| Accretion of discount on marketable securities | | (15) |
| Amortization of debt issuance costs | 19 | |
| Stock-based compensation | 6,536 | 4,467 |
| Issuance of common stock warrants to third parties for services | 50 | |
| Gain on settlement of accounts payable | | (31) |
| Loss on disposal of property and equipment | 7 | |
| Change in fair value of derivative liabilities | | (374) |
| Unrealized loss on derivative assets | | 119 |
| Unrealized gain on marketable securities | | (215) |
| Changes in operating assets and liabilities: | | |
| Accounts receivable | (8,061) | (4,790) |
| Inventory | 6,219 | (3,156) |
| Prepaid giveaways | 331 | 202 |
| Prepaid sponsorship and endorsement fees | (3,462) | (2,475) |
| Prepaid expenses and other current assets | (1,857) | (370) |
| Other assets | (127) | (35) |
| Accounts payable | 10,100 | (3,239) |
| Accrued liabilities | 2,016 | 1,971 |
| Net cash provided by operating activities | 4,189 | 271 |
| CASH FLOWS FROM INVESTING ACTIVITIES | | |
| Purchase of property and equipment | (851) | (2,371) |
| Sale proceeds from settlement of marketable securities | | 490 |
| Change in restricted cash balance | | 2,500 |
| Proceeds from disposal of property and equipment | 447 | 2 |
| Purchase of MusclePharm apparel rights | (850) | |
| Purchase of trademarks | (87) | |

| | | |
|------------------------------------------------------------------------------------------------|----------|----------|
| Investment in contract manufacturer | (977) | |
| Net cash (used in) provided by investing activities | (2,318) | 621 |
| CASH FLOWS FROM FINANCING ACTIVITIES | | |
| Proceeds from line of credit | 4,001 | |
| Payments on line of credit | (6,001) | (2,500) |
| Repayments of term loan | (415) | (17) |
| Proceeds from issuance of term loan | 4,000 | |
| Issuance costs of term loan | (40) | |
| Repayments of other debt obligations | (25) | |
| Repayment of capital lease obligations | (64) | (37) |
| Net cash provided by (used in) financing activities | 1,456 | (2,554) |
| Effect of exchange rate changes on cash | (177) | 19 |
| Net increase (decrease) in cash and cash equivalents | 3,150 | (1,643) |
| Cash and cash equivalents, beginning of period | 1,020 | 5,412 |
| Cash and cash equivalents, end of period | \$ 4,170 | \$ 3,769 |
| SUPPLEMENTAL DISCLOSURES OF CASH FLOW INFORMATION | | |
| Cash paid for income taxes | \$ 54 | \$ 77 |
| Cash paid for interest | \$ 270 | \$ 53 |
| SUPPLEMENTAL DISCLOSURES OF NON-CASH INVESTING AND FINANCING INFORMATION | | |
| Stock issued in conjunction with MusclePharm apparel rights acquisition | \$ 1,394 | \$ |
| Stock issued for Biozone asset acquisition | \$ | \$ 9,840 |
| Reclassification of derivative liability to additional paid-in capital and warrant settlements | \$ | \$ 773 |
| Common stock issued for board member compensation | \$ | \$ 115 |
| Capital leases | \$ 359 | \$ 27 |
| Purchase of property and equipment included in accounts payable and accrued liabilities | \$ 283 | \$ 375 |
| Purchase of trademark registration included in accounts payable | \$ 66 | \$ |

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

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MusclePharm Corporation

Notes to Consolidated Financial Statements

(Unaudited)

Note 1: Description of Business and Basis of Presentation

Description of Business

MusclePharm Corporation, or the Company, was incorporated in Nevada in 2006. The Company is a scientifically driven, performance lifestyle company that develops, manufactures, markets and distributes branded nutritional supplements. The Company is headquartered in Denver, Colorado and has the following wholly-owned operating subsidiaries: MusclePharm Canada Enterprises Corp (MusclePharm Canada), BioZone Laboratories, Inc. (BioZone Labs) and MusclePharm Ireland (MusclePharm Ireland).

Basis of Presentation

The accompanying consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America (GAAP).

Reclassifications

Certain amounts in the consolidated statement of cash flows for the six months ended June 30, 2014 were revised to conform to the consolidated statement of cash flows for the year ended December 31, 2014 and the current period presentation. These adjustments resulted in a decrease in net cash provided by operating activities of \$269,000, an increase in net cash provided by investing activities of \$306,000, and an increase in net cash used in financing activities of \$37,000.

Note 2: Summary of Significant Accounting Policies

Principles of Consolidation

The consolidated financial statements include the accounts of MusclePharm Corporation and its wholly-owned subsidiaries. Acquisitions are included in the consolidated financial statements from the date of the acquisition. All significant intercompany balances and transactions have been eliminated in consolidation.

Unaudited Interim Financial Information

The accompanying unaudited interim consolidated financial statements have been prepared in accordance with GAAP. In our opinion, the unaudited interim consolidated financial statements include all adjustments of a normal recurring nature necessary for the fair presentation of our financial position as of June 30, 2015, our results of operations for the three and six months ended June 30, 2015 and 2014, and our cash flows for the six months ended June 30, 2015 and 2014. The results of operations for the three and six months ended June 30, 2015 are not necessarily indicative of the results to be expected for the year ending December 31, 2015.

These unaudited interim consolidated financial statements should be read in conjunction with the consolidated financial statements and related notes included in our Annual Report on Form 10-K for the year ended December 31,

2014, filed with the SEC on March 16, 2015.

Use of Estimates

The preparation of consolidated financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the amounts reported and disclosed in the consolidated financial statements and accompanying notes. Such estimates include, but are not limited to, allowance for doubtful accounts and revenue discounts and allowances, valuations of equity securities and intangible assets, fair value of derivatives, warrants and options, among others. Actual results could differ from those estimates.

Recent Accounting Pronouncements

In April 2015, the Financial Accounting Standards Board (FASB) issued ASU No. 2015-03, Interest Imputation of Interest (Subtopic 835-30) Simplifying the Presentation of Debt Issuance Costs, which provides guidance on simplifying the presentation of debt issuance costs, requiring that debt issuance costs related to a recognized debt liability be presented in the consolidated balance sheets as a direct deduction from the carrying amount of that debt liability, consistent with debt discounts. This standard requires retrospective adoption and will be effective for the Company beginning in its first quarter of 2016. The Company does not expect this standard to have a material impact on its consolidated financial statements.

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In August 2014, the FASB issued ASU No. 2014-15, Disclosure of Uncertainties about an Entity's Ability to Continue as a Going Concern (ASU 2014-15). ASU 2014-15 explicitly requires management to assess an entity's ability to continue as a going concern, and to provide related footnote disclosure in certain circumstances. The new standard will be effective for all entities in the first annual period ending after December 15, 2016. Earlier adoption is permitted. The Company is currently evaluating the impact of the adoption of ASU 2014-15.

In June 2014, the FASB issued ASU No. 2014-12, Accounting for Share-Based Payments When the Terms of an Award Provide That a Performance Target Could Be Achieved after the Requisite Service Period (ASU 2014-12). The amendments in ASU 2014-12 require that a performance target that affects vesting and that could be achieved after the requisite service period be treated as a performance condition. A reporting entity should apply existing guidance in Accounting Standards Codification Topic No. 718, Compensation - Stock Compensation , as it relates to awards with performance conditions that affect vesting to account for such awards. The amendments in ASU 2014-12 are effective for annual periods and interim periods within those annual periods beginning after December 15, 2015. Early adoption is permitted. Entities may apply the amendments in ASU 2014-12 either: (a) prospectively to all awards granted or modified after the effective date; or (b) retrospectively to all awards with performance targets that are outstanding as of the beginning of the earliest annual period presented in the consolidated financial statements and to all new or modified awards thereafter. The adoption of ASU 2014-12 is not expected to have a material effect on the Company's consolidated financial statements or disclosures.

In May 2014, the FASB issued ASU No. 2014-09, Revenue from Contracts with Customers (ASU 2014-09), which provides guidance for revenue recognition. ASU 2014-09 affects any entity that either enters into contracts with customers to transfer goods or services or enters into contracts for the transfer of nonfinancial assets and supersedes the revenue recognition requirements in Topic 605, Revenue Recognition, and most industry-specific guidance. This ASU also supersedes some cost guidance included in Subtopic 605-35, Revenue Recognition- Construction-Type and Production-Type Contracts. ASU 2014-09's core principle is that a company will recognize revenue when it transfers promised goods or services to customers in an amount that reflects the consideration to which a company expects to be entitled in exchange for those goods or services. In doing so, companies will need to use more judgment and make more estimates than under today's guidance, including identifying performance obligations in the contract, estimating the amount of variable consideration to include in the transaction price and allocating the transaction price to each separate performance obligation. ASU 2014-09 is effective for the Company beginning January 1, 2017 and, at that time, the Company may adopt the new standard under the full retrospective approach or the modified retrospective approach. Early adoption is not permitted. The Company has not yet selected a transition method nor determined the effect of ASU 2014-09 on its ongoing financial reporting.

Note 3: Fair Value of Financial Instruments

The Company's financial instruments consisted primarily of accounts receivable, accounts payable, accrued liabilities and debt. The Company's debt approximates fair value based upon current borrowing rates available to the Company for debt with similar maturities.

Note 4: Capstone Nutrition Agreements

Effective March 2, 2015, the Company entered a number of agreements with Capstone Nutrition (Capstone) as follows:

Effective March 2, 2015, the Company and Capstone executed an amendment (the Amendment) to the Manufacturing Agreement dated November 27, 2013. Pursuant to the Amendment, Capstone shall be the Company's nonexclusive manufacturer of dietary supplements and food products sold or intended to be sold by the Company (the Products).

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The Amendment includes amended pricing for Products. The initial term ends January 1, 2022, and will continue thereafter for three successive twenty-four month terms and includes renewal options.

Contribution toward Capstone Facility Build-Out. The Company agreed to pay to Capstone a non-refundable sum of \$2.5 million to be used by Capstone solely in connection with the expansion of its facility necessary to fulfill anticipated Company requirements under the Manufacturing Agreement and Amendment. The Company has paid Capstone \$1.7 million as of June 30, 2015.

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The Company and Capstone entered into a Class B Common Stock Warrant Purchase Agreement (Warrant Agreement) whereby the Company may purchase approximately 19.9% of Capstone's parent company, INI Parent, Inc. (INI), on a fully-diluted basis as of March 2, 2015. Pursuant to the Warrant Agreement, INI issued to the Company a warrant (the Warrant) to purchase shares of INI's Class B common stock, par value \$0.001 per share at an exercise price of \$0.01 per share (the Warrant Shares).

The Company completed an independent valuation of the warrants and recorded an asset of \$977,000, which is included in the caption long-term investments on the consolidated balance sheets as of June 30, 2015. The Company also recorded \$1.5 million of prepaid expenses and other assets on the consolidated balance sheet as of June 30, 2015 and will be amortized over the remaining life of the Manufacturing Agreement.

The Company and INI also entered into an option agreement (the Option Agreement). Subject to additional provisions and conditions set forth in the Option Agreement, at any time on or prior to June 30, 2016, the Company shall have the right to purchase for cash all of the remaining outstanding shares of INI's common stock not already owned by the Company after giving effect to the exercise of the Warrant, based on an aggregate enterprise value, equal to \$200 million. Such purchase is intended to be consummated pursuant to a definitive merger agreement. The fair value of the option was deemed de minimus as of the transaction date.

Note 5: Balance Sheet Components***Inventory***

Inventory consisted of the following as of June 30, 2015 and December 31, 2014 (in thousands):

| | June 30, 2015 | December 31, 2014 |
|-----------------|--------------------------|------------------------------|
| Raw materials | \$ 1,252 | \$ 1,169 |
| Work-in-process | 66 | 101 |
| Finished goods | 13,532 | 19,799 |
| Inventory | \$ 14,850 | \$ 21,069 |

The Company writes down inventory for obsolete and slow moving inventory based on the age of the product as determined by the expiration date. Products within one year of their expiration dates are considered for write-off purposes. Historically, the Company has had minimal returns with established customers, and any damaged packaging is sent back to the manufacturer for replacement. The Company incurred insignificant inventory write-offs during the three and six months ended June 30, 2015 and 2014.

Table of Contents**Property and Equipment**

Property and equipment consisted of the following as of June 30, 2015 and December 31, 2014 (in thousands):

| | June 30, 2015 | December 31, 2014 |
|-------------------------------------------------|--------------------------|------------------------------|
| Furniture and fixtures | \$ 4,052 | \$ 4,041 |
| Leasehold improvements | 3,007 | 2,298 |
| Manufacturing and lab equipment | 1,562 | 1,388 |
| Vehicles | 470 | 470 |
| Displays | 487 | 488 |
| Website | 399 | 241 |
| Office equipment and computers | 229 | |
| Construction in process | 891 | 1,511 |
| Property and equipment, gross | 11,097 | 10,437 |
| Less: accumulated depreciation and amortization | (3,465) | (2,632) |
| Property and equipment, net | \$ 7,632 | \$ 7,805 |

Depreciation and amortization expense related to property and equipment was \$456,000 and \$333,000 for the three months ended June 30, 2015 and 2014, respectively, and \$838,000 and \$647,000 for the six months ended June 30, 2015 and 2014, respectively. These expenses are included in the selling, general and administrative expenses in the consolidated statements of operations.

Intangible Assets

Intangible assets consist of the following (in thousands) and include the acquisition of MusclePharm's apparel rights from Worldwide Apparel disclosed further in Note 10:

| | June 30, 2015 | | | Weighted- Average Useful Lives (Years) |
|------------------------------------|----------------------|-------------------------------------|-------------------------------|-----------------------------------------------------------|
| | Gross Value | Accumulated Amortization | Net Carrying Value | |
| Amortized Intangible Assets | | | | |
| Customer relationships | \$ 3,130 | \$ (313) | \$ 2,817 | 15.0 |
| Non-compete agreements | 69 | (52) | 17 | 2.0 |
| Patents | 2,211 | (434) | 1,777 | 7.9 |
| Trademarks | 671 | (64) | 607 | 6.6 |
| Brand | 4,020 | (303) | 3,717 | 10.5 |
| Domain name | 68 | (30) | 38 | 5.0 |
| Total intangible assets | \$ 10,169 | \$ (1,196) | \$ 8,973 | |

| | December 31, 2014 | | | Weighted- Average Useful Lives (Years) |
|------------------------------------|--------------------------|-------------------------------------|-------------------------------|-----------------------------------------------------------|
| | Gross Value | Accumulated Amortization | Net Carrying Value | |
| Amortized Intangible Assets | | | | |
| Customer relationships | \$ 3,130 | \$ (209) | \$ 2,921 | 15.0 |
| Non-compete agreements | 69 | (35) | 34 | 2.0 |
| Patents | 2,211 | (293) | 1,918 | 7.9 |
| Trademarks | 518 | (20) | 498 | 4.5 |
| Brand | 1,776 | (118) | 1,658 | 15.0 |
| Domain name | 68 | (23) | 45 | 5.0 |
| Total intangible assets | \$ 7,772 | \$ (698) | \$ 7,074 | |

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Intangible assets amortization expense was \$273,000 and \$293,000 for the three months ended June 30, 2015 and 2014, respectively, and \$498,000 and \$578,000 for the six months ended June 30, 2015 and 2014, respectively. These expenses are included in selling, general and administrative expenses in the consolidated statements of operations.

As of June 30, 2015, the estimated future amortization expense of intangible assets is as follows (in thousands):

| Year Ending December 31, | |
|---------------------------------|--------------|
| The remainder of 2015 | \$ 548 |
| 2016 | 1,062 |
| 2017 | 1,043 |
| 2018 | 1,031 |
| 2019 | 999 |
| 2020 | 975 |
| Thereafter | 3,315 |
| Total amortization expense | \$ 8,973 |

Note 6: Other (Expense) Income, net

During the three and six months ended June 30, 2015 and 2014, other (expense) income, net consisted of the following (in thousands):

| | Three Months Ended June 30, | | Six Months Ended June 30, | |
|------------------------------------------------|------------------------------------|-------------|----------------------------------|-------------|
| | 2015 | 2014 | 2015 | 2014 |
| Other (expense) income, net: | | | | |
| Interest income | \$ | \$ | \$ | \$ 223 |
| Interest expense | (133) | (17) | (258) | (56) |
| Change in fair value of derivative liabilities | | (110) | | 374 |
| Gain on settlement of accounts payable | | 26 | | 31 |
| Loss on marketable securities | | | | (386) |
| Foreign currency loss | (197) | (4) | (261) | (34) |
| Other | (18) | 78 | (12) | 165 |
| Total other (expense) income, net | \$ (348) | \$ (27) | \$ (531) | \$ 317 |

Note 7: Debt

In September 2014, the Company entered into a line of credit facility with a banking institution for up to \$8.0 million of borrowings. The line of credit matures in September 2017 and accrues interest at the prime rate plus 2%, currently 5.25%. The line of credit is secured by the Company's inventory, accounts receivable, intangible assets and equipment. As of June 30, 2015, the outstanding borrowings under the line of credit were \$6.0 million. The Company was not in compliance with certain financial covenants under the line of credit as of June 30, 2015 and received a written waiver from the bank until August 31, 2015.

In February 2015, the Company entered into a term loan agreement with the same banking institution for a principal amount of \$4.0 million. The term loan carries a fixed interest rate of 5.25% per annum, is repayable in 36 equal monthly installments of principal and interest, and matures in February 2018. Outstanding borrowings are subject to prepayment penalties of 1.0% of the prepayment amount. The Company also paid debt issuance costs of \$40,000 which were recorded in prepaid expenses in the consolidated balance sheets. As of June 30, 2015, the outstanding borrowings under the term loan were \$3.6 million.

Borrowings on the term loan are secured by the Company's assets and 860,900 shares of common stock held in treasury. The Company is also required to comply with certain negative covenants under the term loan, including restrictions on indebtedness, investments, asset dispositions, mergers or consolidations and other corporate activities. The Company was not in compliance with certain financial covenants under the term loan as of June 30, 2015 and received a written waiver from the bank until August 31, 2015.

Table of Contents**Note 8: Commitments and Contingencies*****Operating Leases and Capital Leases***

The Company leases office and warehouse facilities under operating leases which expire at various dates through 2029. For lease agreements that contain escalating rent provisions, lease expense is recorded on a straight-line basis over the lease term. Rent expense was \$384,000 and \$336,000 for the three months ended June 30, 2015 and 2014, respectively, and \$767,000 and \$633,000 for the six months ended June 30, 2015 and 2014, respectively.

In December 2014, the Company entered into a capital lease agreement providing for approximately \$1.8 million in credit to lease up to 50 vehicles as part of a fleet lease program. As of June 30, 2015, the Company acquired 16 vehicles under the capital lease, which are included in the caption property and equipment, net in the accompanying consolidated balance sheets.

The Company also leases manufacturing and warehouse equipment under capital leases, which expire at various dates through May 2019. As of June 30, 2015 and December 31, 2014, the Company had an outstanding balance on capital leases of \$560,000 and \$265,000, respectively, which were included as a component of accrued liabilities and other long-term liabilities in the consolidated balance sheets. As of June 30, 2015, the Company's future minimum lease payments are as follows (in thousands):

| Year Ending December 31, | |
|-----------------------------------------|--------|
| The remainder of 2015 | \$ 112 |
| 2016 | 216 |
| 2017 | 136 |
| 2018 | 102 |
| 2019 | 42 |
| Total minimum lease payments | 608 |
| Less amounts representing interest | (48) |
| Present value of minimum lease payments | \$ 560 |

Contingencies

In the normal course of business, the Company may become involved in legal proceedings. The Company will accrue a liability for such matters when it is probable that a liability has been incurred and the amount can be reasonably estimated. When only a range of possible losses can be established, the most probable amount in the range is accrued. If no amount within this range is a better estimate than any other amount within the range, the minimum amount in the range is accrued. The accrual for a litigation loss contingency might include, for example, estimates of potential damages, outside legal fees and other directly related costs expected to be incurred. As of June 30, 2015 and December 31, 2014, the Company was not involved in any material legal proceedings, except for the SEC investigation discussed below and routine litigation experienced in the ordinary course of its business.

SEC Investigation

In July 2013, the Company received a formal order of investigation (the Investigation) from the Denver Regional Office of the SEC which is actively investigating various areas of potential violation of the federal securities laws involving the Company and its management. The SEC has issued subpoenas for documents and testimony and has deposed numerous witnesses in connection with the Investigation. As a result of a review undertaken by the Company's personnel in conjunction with the Audit Committee of the Board of Directors during 2014, the Company amended certain prior reports to revise various disclosures concerning executive compensation and disclosure of perquisites, among other things, and filed amendments to the annual reports on Form 10-K for the fiscal years ended December 31, 2013, 2012 and 2011. The Investigation remains ongoing. The Investigation could lead to the SEC seeking fines, penalties, injunctive relief and the adoption of corrective plans to establish reporting and other practices affecting the Company. The Company has reached an agreement in principle with the staff of the Enforcement Division of the SEC Denver Regional Office to resolve the investigation by the SEC, however, such agreement must be approved by the SEC Commissioners. Neither the nature of the relief, the amount of any monetary relief, nor the nature of the corrective actions, whether voluntary or imposed as a result of court proceedings that could be sought by the SEC, can be predicted. The result of any of the foregoing could have a material adverse effect on the Company or its management.

Table of Contents***Insurance Carrier Lawsuit***

In an effort to recover SEC legal defense costs, the Company engaged with outside counsel to review, evaluate and advise on the current Director and Officer policy and corresponding coverages. On February 12, 2015, the Company filed a complaint and jury demand in the District Court, City and County of Denver, Colorado against Liberty Insurance Underwriters, Inc. This action arises from the wrongful and unreasonable denial of coverage by Liberty for the cost and expenses that the Company has incurred and will continue to incur in connection with the SEC investigation under the Company's Directors and Officers Insurance policies.

Product Liability

Additionally, as a manufacturer of nutritional supplements and other consumer products that are ingested by consumers, the Company may be subject to various product liability claims. The Company currently maintains product liability insurance with a deductible/retention of \$10,000 per claim with an aggregate cap on retained loss of \$20.0 million. As of June 30, 2015 and December 31, 2014, the Company had not recorded an accrual for product liability claims. There can be no assurance that insurance coverage will be available for product liability claims or other claims experienced in the ordinary course of the Company's business.

Sponsorship and Endorsement Contract Liabilities

The Company has various non-cancelable endorsement and sponsorship agreements with terms expiring through 2022. The total future contractual payments as of June 30, 2015 are as follows (in thousands):

| | Year Ending December 31, | | | | | | | |
|-------------------------------------|---------------------------------|-------------|-------------|-------------|-------------|-------------|-------------------|--------------|
| | Remainder of 2015 | 2016 | 2017 | 2018 | 2019 | 2020 | Thereafter | Total |
| Future Contractual Payments: | | | | | | | | |
| Endorsement | \$ 4,762 | \$ 8,482 | \$ 9,117 | \$ 6,000 | \$ 4,167 | \$ 5,000 | \$ 6,667 | \$ 44,195 |
| Sponsorship | 3,054 | 4,563 | 3,205 | 2,830 | 985 | | | 14,637 |
| Total future payments | \$ 7,816 | \$ 13,045 | \$ 12,322 | \$ 8,830 | \$ 5,152 | \$ 5,000 | \$ 6,667 | \$ 58,832 |

The following agreements signed during the second quarter 2015 are included in the table above:

In April 2015, the Company entered a partnership with the Cleveland Cavaliers of the National Basketball Association. Under the agreement, MusclePharm Combat Crunch will be the premier partner of the Cleveland Cavaliers and the exclusive presenting partner of the Fourth Quarter Combat Crunch Time in-game feature during select home games at Quicken Loans Arena. The partnership also includes in-arena signage and branding, digital promotions and sweepstakes, and product sampling at designated Cavaliers games. The MusclePharm Combat Crunch partnership and its associated branded elements extend to other Cleveland Cavaliers and Quicken Loans Arena properties, including the Cleveland Gladiators (Arena Football League), the Lake Erie Monsters (American Hockey League) and the Canton Charge (Cavaliers' NBA D-League affiliate). In addition to digital promotions and in-game activation for each of the franchises, the Gladiators will have an official Combat Crunch of the Game presented on the Humongotron, a massive four-sided center-hung scoreboard, during each home game. The total future contractual payments under the agreement at June 30, 2015 are approximately \$2.4 million with additional payments for potential

playoff games.

In May 2015, the Company entered into a multi-year partnership with City Football Group and its four clubs: Manchester City Football Club (including the Continental Cup-winning Manchester City Women's Football Club), Melbourne City Football Club, New York City Football Club, and Yokohama F. Marinos Football Club. The total contractual payments under the agreement at June 30, 2015 are approximately \$8.4 million.

In June 2015, the Company entered into sponsorship and endorsement agreements with bodybuilding pioneer Bill Phillips as Strategic Advisor and Chief Editor of Content. The minimum future contractual payments under the agreements as of June 30, 2015 are approximately \$1.0 million, of which \$250,000 has been paid and \$750,000 is due by December 31, 2015 and serves as advanced royalties.

Table of Contents**Note 9: Stockholders Equity****Common Stock**

For the six months ended June 30, 2015, the Company issued common stock including restricted stock awards, as follows (in thousands, except share and per share data):

| Transaction Type | Quantity (Shares) | Valuation (\$) | Range of Value per Share |
|-------------------------------------------------------------------------|--------------------------|-----------------------|---------------------------------|
| Stock issued to employees, executives and directors | 244,589 | \$ 6,211 | \$3.48 8.60 |
| Stock issued in conjunction with product line expansion | 150,000 | 1,198 | 7.99 |
| Stock issued in conjunction with MusclePharm apparel rights acquisition | 170,000 | 1,394 | 8.20 |
| Stock issued in conjunction with financing agreement | 50,000 | 325 | 6.49 |
| Stock issued in conjunction with consulting/endorsement agreement | 50,000 | 292 | 5.85 |
| Total | 664,589 | \$ 9,420 | \$3.48 8.60 |

For the six months ended June 30, 2014, the Company issued common stock including restricted stock awards, as follows:

| Transaction Type | Quantity (#) | Valuation (\$) | Range of Value per Share |
|--------------------------------------------------------|---------------------|-----------------------|---------------------------------|
| Stock issued to employees, executives and directors | 60,422 | \$ 265 | \$3.48 8.70 |
| BioZone acquisition | 1,200,000 | 9,840 | 8.20 |
| Conversion of series D preferred stock to common stock | 263,000 | 773 | 2.94 |
| Total | 1,523,422 | \$ 10,878 | \$2.94 8.70 |

The fair value of all stock issuances above is based upon either the quoted closing trading price on the date of issuance or the value of derivative instruments at the date of conversion.

Treasury Stock

For the six months ended June 30, 2015, the Company did not repurchase any shares of its common stock and held 875,621 shares in treasury as of June 30, 2015.

Note 10: Stock-Based Compensation

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The Company's stock-based compensation for the three and six months ended June 30, 2015 and 2014 consists primarily of restricted stock awards. The activity of restricted stock awards granted to employees, executives, and board members was as follows:

| | | Number of Shares | Weighted- Average Grant Date Fair Value |
|------------------|-------------------|---------------------------------|--------------------------------------------------------|
| Unvested balance | December 31, 2014 | 2,631,987 | \$ 11.67 |
| Granted | | 201,452 | 4.46 |
| Vested | | (524,246) | 10.15 |
| Unvested balance | June 30, 2015 | 2,309,193 | \$ 11.45 |

The total fair value of restricted stock awards granted to employees and board members was \$825,000 and \$1.1 million for the three months ended June 30, 2015 and 2014, respectively, and \$900,000 and \$1.5 million for the six months ended June 30, 2015 and 2014, respectively. As of June 30, 2015 and December 31, 2014, the total unrecognized expense for unvested restricted stock awards, net of expected forfeitures, was \$14.9 million and \$20.7 million, respectively, which are expected to be amortized over a weighted-average period of 3.0 and 2.6 years, respectively.

Table of Contents***Restricted Stock Awards Related to Energy Drink Agreement***

In January 2015, the Company entered into an energy drink agreement with Langer Juice and Creative Flavor Concepts to expand into a new product line. In connection with the agreement, the Company issued a total of 150,000 shares of its restricted common stock with trade restrictions for a period of three years. Langer Juice and Creative Flavor Concepts may receive additional restricted shares of common stock based upon future revenue and gross margin targets. The restricted stock awards issued have a grant date fair value of approximately \$1.2 million, which are included as a component of prepaid stock compensation and additional paid-in capital in the consolidated balance sheets. The prepaid stock compensation is being amortized over the performance period of ten years.

Agreements with Worldwide Apparel, LLC – Muscle Pharm Apparel Rights

In February 2015, the Company entered into an agreement with Worldwide Apparel, LLC (Worldwide) to terminate Worldwide s right to use MusclePharm s brand images in apparel effective March 28, 2015. The brand rights were originally licensed in May 2011, and amended in March 2014 prior to the termination. The consideration related to the acquisition of the MusclePharm Apparel from Worldwide consists of cash consideration of \$850,000 and 170,000 shares of MusclePharm common stock with an aggregated fair value of \$1.4 million. The total cost of the MusclePharm apparel acquisition of \$2.2 million is included in the caption brand within intangible assets, net, in the accompanying consolidated balance sheet, and is subject to amortization over a period of seven years.

Restricted Stock Awards Issued Related to Financing Agreement

In May 2015, the Company negotiated the termination of a financing agreement with a lending institution and issued 50,000 shares of its common stock. The fair value of the common stock was \$325,000 based upon the closing price of common stock on the date of issuance, and was recorded in selling, general and administrative expense in the accompanying consolidated statement of operations.

Restricted Stock Awards Issued Related to Consulting/Endorsement Agreement

In May 2015, the Company entered into consulting and endorsement agreements with Bill Phillips, a fitness and bodybuilding pioneer, to serve as strategic advisor and Chief Editor of Content of the Company. In connection with the endorsement agreements, the Company agreed to issue a total of 50,000 shares of its restricted common stock. The grant date fair value of the restricted common stock issued was \$292,000, which is included as a component of prepaid stock compensation and additional paid-in capital in the consolidated balance sheets. The prepaid stock compensation is being amortized over the performance period of three years. In connection with the consulting agreement, the Company agreed to issue shares worth \$25,000 within 10 days after each subsequent three month period term. The consulting agreement is for a three year period but may be cancelled with 30 days written notice.

Note 11: Net (Loss) Income per Share

The following table sets forth the computation of the Company s basic and diluted net (loss) income per share for the periods presented (in thousands, except share and per share data):

| Three Months Ended | | Six Months Ended June 30, | |
|---------------------------|-------------|----------------------------------|-------------|
| June 30, | | | |
| 2015 | 2014 | 2015 | 2014 |

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| | | | | |
|---------------------------------------------------------------------------------------------|------------|------------|-------------|------------|
| Net (loss) income | \$ (7,025) | \$ (935) | \$ (14,504) | \$ 1,801 |
| Weighted-average common shares used in computing net (loss) income per share, basic | 13,647,267 | 10,610,022 | 13,491,433 | 10,459,522 |
| Effect of dilutive securities | | | | 1,404,360 |
| Weighted-average common shares used in computing net (loss) income per share, diluted | 13,647,267 | 10,610,022 | 13,491,433 | 11,863,882 |
| Net (loss) income per share, basic | \$ (0.51) | \$ (0.09) | \$ (1.08) | \$ 0.17 |
| Net (loss) income per share, diluted | \$ (0.51) | \$ (0.09) | \$ (1.08) | \$ 0.15 |

The following securities were excluded from the computation of diluted net (loss) income per share for the periods presented because including them would have been antidilutive:

| | As of June 30, | |
|----------------------------------------------|----------------|-----------|
| | 2015 | 2014 |
| Stock options (exercise price - \$425/share) | | 472 |
| Warrants (exercise price - \$1,275/share) | | 89 |
| Unvested restricted stock | 2,309,193 | 1,501,573 |
| Total common stock equivalents | 2,309,193 | 1,502,134 |

Table of Contents**Note 12: Income Taxes**

The Company recorded an income tax provision of \$21,000 and \$45,000 for the three months ended June 30, 2015 and 2014, respectively, and \$33,000 and \$77,000 for the six months ended June 30, 2015 and 2014, respectively, related to foreign income taxes and state minimum taxes.

Income taxes are provided for the tax effects of transactions reported in the consolidated financial statements and consist of taxes currently due. Deferred taxes relate to differences between the basis of assets and liabilities for financial and income tax reporting which will be either taxable or deductible when the assets or liabilities are recovered or settled. In assessing the realizability of deferred tax assets, management considers whether it is more likely than not that some portion or all of the deferred income tax assets will not be realized. The ultimate realization of deferred income tax assets is dependent upon the generation of future taxable income during the periods in which those temporary differences become deductible. Management considers the scheduled reversal of deferred income tax liabilities, projected future taxable income, and tax planning strategies in making this assessment. Based on consideration of these items, management has determined that enough uncertainty exists relative to the realization of the deferred income tax asset balances to warrant the application of a full valuation allowance as of June 30, 2015 and December 31, 2014.

Note 13: Geographical Information

Revenue, net by geography is based on the company addresses of the customers. The following table sets forth revenue, net by geographic area (in thousands):

| | Three Months Ended June 30, | | Six Months Ended June 30, | |
|--------------------|------------------------------------|-------------|----------------------------------|-------------|
| | 2015 | 2014 | 2015 | 2014 |
| Revenue, net: | | | | |
| United States | \$ 36,270 | \$ 27,041 | \$ 67,858 | \$ 60,041 |
| International | 14,206 | 19,700 | 23,940 | 36,909 |
| Total revenue, net | \$ 50,476 | \$ 46,741 | \$ 91,798 | \$ 96,950 |

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Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations

The following discussion and analysis of our financial condition and results of operations should be read in conjunction with our consolidated financial statements and related notes included elsewhere in this Quarterly Report on Form 10-Q, and with our audited consolidated financial statements included in our Annual Report on Form 10-K for the year ended December 31, 2014, as filed with the Securities and Exchange Commission on March 16, 2015. This discussion contains forward-looking statements that involve risks and uncertainties. Our actual results could differ materially from those discussed below. Factors that could cause or contribute to such differences include, but are not limited to, those identified below and those discussed in the section entitled "Risk Factors" included elsewhere in this Form 10-Q.

Overview

We are a scientifically driven, performance lifestyle Company that develops, manufactures, markets and distributes branded nutritional supplements. We offer a broad range of powders, capsules, tablets and gels. Our portfolio of recognized brands, including MusclePharm® Hybrid and Core Series, Arnold Schwarzenegger Series, and FitMiss®, are marketed and sold in more than 120 countries and available in over 45,000 retail outlets globally. These clinically developed scientifically driven nutritional supplements are developed through a six-stage research process that utilizes the expertise of leading nutritional scientists, doctors and universities. We believe we are an innovator in the sports nutrition industry.

Our primary growth strategy is to:

drive innovation, serve the needs of all athletes and fuel the engine of sport through new products and brand extension;

increase our product distribution and sales through increased market penetrations both domestically and internationally;

increase our margins by focusing on streamlining our operations and seeking operating efficiencies in all areas of our operations;

continue to conduct additional testing of the safety and efficacy of our products and formulate new products; and

increase awareness of our products by increasing our marketing and branding opportunities through endorsements, sponsorships and brand extensions.

Our core marketing strategy is to brand MusclePharm as the "must have" fitness brand for workout enthusiasts and elite athletes. We seek to be known as The Athlete's Company®, run by athletes who create their products for other athletes both professional and otherwise. We believe that our marketing mix of endorsers, sponsorships and providing sample products for our retail resellers to use is an optimal strategy to increase sales.

Our annual revenue has consistently increased year-over-year as we continue to grow our brand and develop industry-leading supplemental nutrition and lifestyle products. Revenue for the six months ended June 30, 2015 was \$91.8 million, with a two-year 38.2% compound annual growth rate (CAGR).

Recent Developments

Backlog

As of June 30, 2015 and December 31, 2014, we had product backlog of approximately \$8.5 million and \$5.1 million, respectively. Backlog represents orders confirmed with a purchase order for products to be shipped generally within 90 days to customers with approved credit status. Orders are subject to cancellation, rescheduling by customers and product specification changes by customers. Although we believe that the backlog orders are firm, purchase orders may be cancelled by the customer prior to shipment without significant penalty. For this reason, we believe that our product backlog at any given date is not a reliable indicator of future revenue.

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Components of Results of Operations

Revenue

We derive our revenues through the sales of our various branded nutritional supplements. Revenue is recognized when persuasive evidence of an arrangement exists, delivery has occurred, the price is fixed or determinable and collection is reasonably assured which generally occurs upon shipment or delivery of the products. We record sales discounts as a direct reduction of revenue for various discounts provided to our customers consisting primarily of volume incentive rebates and advertising related credits. We accrue for sales discounts over the period they are earned. Sales discounts are a significant part of our marketing plan to our customers as they help drive increased sales and brand awareness with end users through promotions that we support through our distributors and re-sellers.

During the three months ended June 30, 2015, our two largest customers, Costco and GNC each individually accounted for more than 10% of our net revenue, and in total represented 34% of our net revenue. During the six months ended June 30, 2015, our three largest customers, Costco, Bodybuilding.com and GNC, each individually accounted for more than 10% of our net revenue, and in total represented 44% of our net revenue.

During the three months ended June 30, 2014, our two largest customers, Costco and Bodybuilding.com each individually accounted for more than 10% of our net revenue, and in total represented 28% of our net revenue. During the six months ended June 30, 2014, our two largest customers, Costco and Bodybuilding.com each individually accounted for more than 10% of our revenue, and in total represented 26% of our net revenue.

Cost of Revenue and Gross Margin

Cost of net revenue for MusclePharm products is directly related to the production, manufacturing and freight-in of the related products purchased from third party contract manufacturers. We mainly ship customer orders from our distribution centers in Franklin, Tennessee and Pittsburg, California. The distribution centers are operated with our equipment and employees, and we own the inventory. We also use contract manufacturers to drop ship products directly to our customers.

Additionally, BioZone Laboratories, Inc., (BioZone) which we acquired via an asset acquisition in 2014, manufactures products and, therefore, derives costs of revenue through the costs of raw materials, direct labor, freight-in and other supply and equipment rental expenses. We mainly ship BioZone customer orders from our distribution center in Pittsburg, California.

Our historical experience has been that over the life cycle of a particular product, the cost of revenues as a percentage of total revenue has typically declined as a result of decreases in our product costs. This decrease generally results from an increase in the volume purchased from our suppliers, as well as yield improvements and product testing enhancements.

Our gross profit fluctuates due to several factors, including new product introductions, changes to existing product lines, changes in customer mix and product mix, product demand mix, shipment volumes, product costs, pricing and inventory write downs. We expect cost of revenues to increase in absolute dollars as our revenue continues to increase, however, cost of revenue is expected to decrease as a percentage of revenue due primarily to our ability to efficiently increase our revenue while realizing respective cost efficiencies from volume purchasing and inventory cost reductions related to our Manufacturing Agreement with Capstone.

Operating Expenses

Advertising and Promotion

Our advertising and promotions consists primarily of product giveaways, trade show events, broker fees, athletic endorsements and sponsorship, strategic partnerships, and digital and print advertising. Advertising and promotions are a large part of both our growth strategy and brand awareness. We build strategic partnerships with sports athletes like Tiger Woods and fitness enthusiasts like Arnold Schwarzenegger through endorsements licensing, co-branding agreements and co-developing product lines. We expect our advertising and promotion expenses to increase in absolute dollars in future periods as this is a key strategy for our growth, however, advertising and promotion expense is expected to remain consistent as a percentage of revenue due primarily to our ability to efficiently increase our revenue while realizing respective cost efficiencies associated with such increase.

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Salaries and Benefits

Salaries and benefits consist primarily of salaries, bonuses, commissions, benefits and stock-based compensation. Personnel costs are a significant component of our operating expenses and we expect these expenses to increase in absolute dollars in future periods as we continue to grow our business and add employees, however, salaries and benefits are expected to decrease as a percentage of revenue due primarily to our ability to efficiently increase our revenue leveraging our existing employee base.

Selling, General and Administrative

Our selling, general and administrative expenses consist primarily of office expenses, insurance, depreciation, amortization, sales commissions, travel, freight out, legal settlement costs, director fees, miscellaneous expenses incurred by our board, executive, finance, information technology, legal, human resources, and other administrative functions, and other corporate expenses. We expect our selling, general and administrative expenses to increase in absolute dollars in future periods, however, selling, general and administration expenses are expected to decrease as a percentage of revenue due primarily to our ability to efficiently increase our revenue while realizing respective cost efficiencies associated with such increase.

Research and Development

Research and development expenses primarily consist of salaries, bonuses and benefits, laboratory development of our scientific nutritional supplements, testing and compliance and allocated facilities costs. We expense research and development costs as incurred. Research and development is not the primary driver of our operating expenses but we expect research and development to increase in absolute dollars in future periods, however, research and development expenses are expected to decrease as a percentage of revenue due primarily to our ability to efficiently increase our revenue while realizing respective cost efficiencies associated with such increase.

Professional Fees

Professional fees consist primarily of fees for outside legal, audit, accounting and tax services, investor relations and consulting fees, and we expect these expenses to increase in absolute dollars in future periods as we continue to grow our business and utilize assistance from professional service providers, defend ongoing and new legal matters and expand our global reach. Professional fees are expected to decrease as a percentage of revenue due primarily to the anticipated reduction in activities related to the SEC Investigation.

Other (Expense) Income, net

Other (expense) income, net consists of interest income and expense, gains and losses on foreign currency transactions, settlement of accounts payable, and other miscellaneous expenses.

Provision for Income Taxes

Provision for income taxes consists primarily of federal and state income taxes in the United States and income taxes in foreign jurisdictions in which we conduct business. Due to uncertainty as to the realization of benefits from our deferred tax assets, including net operating loss carry-forwards, research and development and other tax credits, we have a full valuation allowance reserved against such deferred tax assets. We expect to maintain this full valuation allowance at least in the near term.

Table of Contents**Results of Operations**

The following tables present our historical operating results in dollars and as a percentage of revenue, net for the periods presented:

| | Three Months Ended June 30, | | Six Months Ended June 30, | |
|-------------------------------------------------|------------------------------------|-------------|----------------------------------|-------------|
| | 2015 | 2014 | 2015 | 2014 |
| | (In thousands) | | | |
| Revenue, net | \$ 50,476 | \$ 46,741 | \$ 91,798 | \$ 96,950 |
| Cost of revenue | 32,978 | 31,094 | 59,916 | 63,430 |
| Gross profit | 17,498 | 15,647 | 31,882 | 33,520 |
| Operating expenses: | | | | |
| Advertising and promotion | 8,285 | 5,920 | 15,510 | 12,248 |
| Salaries and benefits | 7,763 | 5,777 | 14,824 | 11,144 |
| Selling, general and administrative | 5,121 | 2,357 | 10,083 | 4,229 |
| Research and development | 921 | 1,164 | 1,886 | 2,261 |
| Professional fees | 2,064 | 1,292 | 3,519 | 2,077 |
| Total operating expenses | 24,154 | 16,510 | 45,822 | 31,959 |
| (Loss) income from operations | (6,656) | (863) | (13,940) | 1,561 |
| Other (expense) income, net | (348) | (27) | (531) | 317 |
| (Loss) income before provision for income taxes | (7,004) | (890) | (14,471) | 1,878 |
| Provision for income taxes | 21 | 45 | 33 | 77 |
| Net (loss) income | \$ (7,025) | \$ (935) | \$ (14,504) | \$ 1,801 |

| | Three Months Ended June 30, | | Six Months Ended June 30, | |
|-------------------------------------|------------------------------------|-------------|----------------------------------|-------------|
| | 2015 | 2014 | 2015 | 2014 |
| Revenue, net | 100% | 100% | 100% | 100% |
| Cost of revenue | 65 | 67 | 65 | 65 |
| Gross profit | 35 | 33 | 35 | 35 |
| Operating expenses: | | | | |
| Advertising and promotion | 17 | 13 | 17 | 13 |
| Salaries and benefits | 15 | 12 | 16 | 12 |
| Selling, general and administrative | 10 | 5 | 11 | 4 |
| Research and development | 2 | 2 | 2 | 2 |
| Professional fees | 4 | 3 | 4 | 2 |

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| | | | | |
|-------------------------------------------------|-------|------|-------|----|
| Total operating expenses | 48 | 35 | 50 | 33 |
| (Loss) income from operations | (13) | (2) | (15) | 2 |
| Other (expense) income, net | (1) | | (1) | |
| (Loss) income before provision for income taxes | (14) | (2) | (16) | 2 |
| Provision for income taxes | | | | |
| Net (loss) income | (14)% | (2)% | (16)% | 2% |

Table of Contents**Comparison of the Three Months Ended June 30, 2015 and 2014*****Revenue***

| | Three Months Ended June 30, | | |
|--------------|------------------------------------|-------------|-----------------|
| | 2015 | 2014 | % Change |
| | (In thousands) | | |
| Revenue, net | \$ 50,476 | \$ 46,741 | 8% |

Revenue, net increased \$3.7 million or 8% to \$50.5 million for the three months ended June 30, 2015, compared to \$46.7 million for the three months ended June 30, 2014. Revenue, net for the three months ended June 30, 2015 increased due primarily to an increase in sales to existing and new customers from existing and new product introductions offset by a reduction in international sales related to the strengthening of the US dollar. Discounts and sales allowances increased to \$9.0 million, or 15.1%, of gross revenue for the three months ended June 30, 2015 from \$5.1 million, or 10.0%, of gross revenue for the same period in 2014. The increase in discounts and allowances is mainly related to promotions on new product introductions.

Cost of Revenue and Gross Profit

| | Three Months Ended June 30, | | |
|-----------------|------------------------------------|-------------|-----------------|
| | 2015 | 2014 | % Change |
| | (In thousands) | | |
| Cost of revenue | \$ 32,978 | \$ 31,094 | 6% |

| | Three Months Ended June 30, | | |
|--------------|------------------------------------|-------------|-----------------|
| | 2015 | 2014 | % Change |
| | (In thousands) | | |
| Gross profit | \$ 17,498 | \$ 15,647 | 12% |

Costs of revenue increased 6% to \$33.0 million for the three months ended June 30, 2015, compared to \$31.1 million for the same period in 2014. Accordingly, gross profit for the three months ended June 30, 2015 was \$17.5 million, or 35% of revenue, compared to \$15.6 million, or 33% of revenue for the same period 2014. Our gross profit margin slightly increased due to our continued focus on optimizing product cost partially offset by an increase in discounts and sales allowances.

Operating Expenses

Operating expenses for the three months ended June 30, 2015 were \$24.2 million, compared to \$16.5 million for the same period in 2014. These expenses primarily included costs for advertising and promotions, costs of strategic partnerships with star athletes and strategic advertising agreements to promote our brand, and investing in our staffing needs in order to stay competitive in our industry by developing and testing new products, including stock-based compensation.

Advertising and Promotion

| | Three Months Ended June 30, | | |
|---------------------------|------------------------------------|-------------|-----------------|
| | 2015 | 2014 | % Change |
| | (In thousands) | | |
| Advertising and promotion | \$ 8,285 | \$ 5,920 | 40% |
| Percentage of revenue | 17% | 13% | |

Advertising and promotion expenses increased 40% to \$8.3 million for the three months ended June 30, 2015, or 17% of revenue, compared to \$5.9 million, or 13% of revenue, for the same period in 2014. Advertising and promotion expenses for the three months ended June 30, 2015 included expenses related to strategic partnerships with the UFC, Tiger Woods and other athletes. These new partnerships, along with our Arnold Schwarzenegger Series introduced in 2013, have increased our strategic partnership and endorsements expense by \$1.7 million including stock-based compensation which accounted for 13% of the increase. This expense coupled with an increase in promotional giveaways of \$419,000 and advertising of \$342,000 are the primary drivers for the overall increase.

Table of Contents***Salaries and Benefits***

| | Three Months Ended June 30, | | |
|-----------------------|------------------------------------|-------------|-----------------|
| | 2015 | 2014 | % Change |
| | (In thousands) | | |
| Salaries and benefits | \$ 7,763 | \$ 5,777 | 34% |
| Percentage of revenue | 15% | 12% | |

Salaries and benefits increased 34% to \$7.8 million, or 15% of revenue, for the three months ended June 30, 2015 compared to \$5.8 million, or 12% of revenue, for the same period in 2014. The increase was due primarily to additional resources added to both our domestic and foreign operations as we continue to expand the global reach of our business, and an increase in stock-based compensation charges.

Selling, General and Administrative

| | Three Months Ended June 30, | | |
|-------------------------------------|------------------------------------|-------------|-----------------|
| | 2015 | 2014 | % Change |
| | (In thousands) | | |
| Selling, general and administrative | \$ 5,121 | \$ 2,357 | 117% |
| Percentage of revenue | 10% | 5% | |

Selling, general and administrative expenses increased 117% to \$5.1 million, or 10% of revenue, for the three months ended June 30, 2015 compared to \$2.4 million, or 5% of revenue, for the same period in 2014. The increase was primarily due to costs related to continued development of our existing sales channels and new product distribution channels and related selling expenses of \$1.5 million, increase in stock-based compensation related to a one-time restricted share grant to a financial institution of \$325,000, additional corporate insurance premiums of \$114,000, additional depreciation and amortization on new assets of \$253,000, increased facilities cost as we expand our operations of \$279,000, and a net increase in other expense of \$347,000.

Research and Development

| | Three Months Ended June 30, | | |
|--------------------------|------------------------------------|-------------|-----------------|
| | 2015 | 2014 | % Change |
| | (In thousands) | | |
| Research and development | \$ 921 | \$ 1,164 | (21)% |
| Percentage of revenue | 2% | 2% | |

Research and development expenses decreased 21% to \$0.9 million, or 2% of revenue, for the three months ended June 30, 2015 compared to \$1.2 million, or 2% of revenue, for the same period in 2014. The decrease was due to a \$250,000 decrease in depreciation expense of fixed assets used for research and development, an increase of \$154,000 in customer funded research and development, accounted for as contra research and development, offset by a \$135,000 increase in personal costs including stock-based compensation.

Professional Fees

| | Three Months Ended June 30, | | % |
|-----------------------|------------------------------------|-------------|---------------|
| | 2015 | 2014 | Change |
| | (In thousands) | | |
| Professional fees | \$ 2,064 | \$ 1,292 | 60% |
| Percentage of revenue | 4% | 3% | |

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Professional fees increased 60% to \$2.1 million for the three months ended June 30, 2015, compared to \$1.3 million for the same period in 2014. The primary reason for the increase in professional fees is due to additional accounting and audit fees of \$504,000, related to SOX, audit and international tax planning, additional consulting expenses of \$561,000 offset by a decrease in legal fees of \$368,000 related to the status of the SEC investigation.

Other (Expense) Income, net

| | Three Months Ended June 30, | |
|------------------------------------------------|------------------------------------|-------------|
| | 2015 | 2014 |
| | (In thousands) | |
| Interest expense | \$ (133) | \$ (17) |
| Change in fair value of derivative liabilities | | (110) |
| Gain on settlement of accounts payable | | 26 |
| Foreign currency loss | (197) | (4) |
| Other | (18) | 78 |
| Total other (expense) income, net | \$ (348) | \$ (27) |

Other expense, net for the three months ended June 30, 2015 was \$0.3 million, compared to \$27,000 for the same period in 2014. The significant fluctuations in other (expense) income, net were primarily related to foreign currency transaction gains and losses, and interest expense.

Comparison of the Six Months Ended June 30, 2015 and 2014**Revenue**

| | Six Months Ended June 30, | | |
|--------------|----------------------------------|-------------|-----------------|
| | 2015 | 2014 | % Change |
| | (In thousands) | | |
| Revenue, net | \$ 91,798 | \$ 96,950 | (5)% |

Revenue, net decreased \$5.2 million or 5% to \$91.8 million for the six months ended June 30, 2015, compared to \$97.0 million for the six months ended June 30, 2014. Revenue, net for the six months ended June 30, 2015 decreased due primarily to the strengthening of the US dollar resulting in a decrease in sales to international customers and the launch of the Arnold Schwarzenegger Series introduced late in 2013 resulting in significant initial sales during the first half of 2014. Discounts and sales allowances increased to \$14.1 million, or 13.3% of gross revenue, for the six months ended June 30, 2015 from \$11.6 million, or 11.0% of gross revenue, for the same period in 2014. The increase in discounts and allowances is mainly related to the promotions on new product introductions.

Cost of Revenue and Gross Profit

| | Six Months Ended June 30, | | |
|--|----------------------------------|-------------|-----------------|
| | 2015 | 2014 | % Change |

| | (In thousands) | | |
|-----------------|-----------------------|-----------|------|
| Cost of revenue | \$ 59,916 | \$ 63,430 | (6)% |

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Six Months Ended June 30,
2015 2014 % Change
(In thousands)

| | | | |
|--------------|-----------|-----------|------|
| Gross profit | \$ 31,882 | \$ 33,520 | (5)% |
|--------------|-----------|-----------|------|

Costs of revenue decreased 6% to \$59.9 million for the six months ended June 30, 2015, compared to \$63.4 million for the same period in 2014. Accordingly, gross profit for the six months ended June 30, 2015 was \$31.9 million, or 35% of revenue, compared to \$33.5 million, or 35% of revenue for the same period 2014. Our cost of revenue and gross profit margin were consistent.

Operating Expenses

Operating expenses for the six months ended June 30, 2015 were \$45.8 million, compared to \$32.0 million for the same period in 2014. These expenses primarily included costs for advertising and promotions, specifically tradeshow costs to generate visibility and connect with our customers and end-users, costs of strategic partnerships with star athletes and strategic advertising agreements to promote our brand, and investing in our staffing needs in order to stay competitive in our industry by developing and testing new products, including stock-based compensation.

Advertising and Promotion

Six Months Ended June 30,
2015 2014 % Change
(In thousands)

| | | | |
|---------------------------|-----------|-----------|-----|
| Advertising and promotion | \$ 15,510 | \$ 12,248 | 27% |
| Percentage of revenue | 17% | 13% | |

Advertising and promotion expenses increased 27% to \$15.5 million for the six months ended June 30, 2015, or 17% of revenue, compared to \$12.2 million, or 13% of revenue, for the same period in 2014. Advertising and promotion expenses for the six months ended June 30, 2015 included expenses related to strategic partnerships with the UFC, Tiger Woods and other athletes. These new partnerships, along with our Arnold Schwarzenegger Series introduced in 2013, have increased our strategic partnership and endorsements expense including stock-based compensation by \$2.5 million. This expense coupled with an increase in trade show costs and promotional giveaways of \$1.0 million, offset by a decrease in general advertising of \$364,000, are the primary drivers for the overall increase.

Salaries and Benefits

Six Months Ended June 30,
2015 2014 % Change
(In thousands)

| | | | |
|-----------------------|-----------|-----------|-----|
| Salaries and benefits | \$ 14,824 | \$ 11,144 | 33% |
| Percentage of revenue | 16% | 12% | |

Salaries and benefits increased 33% to \$14.8 million, or 16% of revenue, for the six months ended June 30, 2015 compared to \$11.1 million, or 12% of revenue, for the same period in 2014. The increase was due to additional resources added to both our domestic operations and our foreign subsidiaries and an increase in stock-based compensation charges which represented 41% of the increase.

Selling, General and Administrative

| | Six Months Ended June 30, | | % Change |
|-------------------------------------|----------------------------------|-------------|-----------------|
| | 2015 | 2014 | |
| | (In thousands) | | |
| Selling, general and administrative | \$ 10,083 | \$ 4,229 | 138% |
| Percentage of revenue | 11% | 4% | |

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Selling, general and administrative expenses increased 138% to \$10.1 million, or 11% of revenue, for the six months ended June 30, 2015 compared to \$4.2 million, or 4% of revenue, for the same period in 2014. The increase was primarily due to costs related to continued development of our existing sales channels and new product distribution channels and related selling expenses of \$3.2 million, increased travel related expenses of \$118,000, additional corporate insurance premiums of \$351,000, additional depreciation and amortization on new assets of \$507,000, increased facilities cost as we expand our operations of \$647,000, and increases in general supplies, outside services and communications of \$901,000.

Research and Development

| | Six Months Ended June 30, | | |
|--------------------------|----------------------------------|-------------|-----------------|
| | 2015 | 2014 | % Change |
| | (In thousands) | | |
| Research and development | \$ 1,886 | \$ 2,261 | (17)% |
| Percentage of revenue | 2% | 2% | |

Research and development expenses decreased 17% to \$1.9 million, or 2% of revenue, for the six months ended June 30, 2015 compared to \$2.3 million, or 2% of revenue, for the same period in 2014. The decrease was due to a \$491,000 decrease in depreciation expense of fixed assets used for research and development, a \$140,000 decrease in customer funded research and development, accounted for as contra research and development expense, offset by a \$154,000 increase in personal cost including stock-based compensation and a \$98,000 increase in research and development fees.

Professional Fees

| | Six Months Ended June 30, | | |
|-----------------------|----------------------------------|-------------|-----------------|
| | 2015 | 2014 | % Change |
| | (In thousands) | | |
| Professional fees | \$ 3,519 | \$ 2,077 | 69% |
| Percentage of revenue | 4% | 2% | |

Professional fees increased 69% to \$3.5 million for the six months ended June 30, 2015, compared to \$2.1 million for the same period in 2014. The primary reason for the increase in professional fees is due to additional accounting and audit fees of \$683,000 related to SOX, audit, and international tax planning, additional consulting expenses of \$695,000, and an increase of \$87,000 in other expenses.

Other (Expense) Income, net

| | Six Months Ended June 30, | |
|------------------------------------------------|----------------------------------|-------------|
| | 2015 | 2014 |
| | (In thousands) | |
| Interest income | \$ | \$ 223 |
| Interest expense | (258) | (56) |
| Change in fair value of derivative liabilities | | 374 |

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| | | |
|----------------------------------------|----------|--------|
| Gain on settlement of accounts payable | | 31 |
| Loss on marketable securities | | (386) |
| Foreign currency loss | (261) | (34) |
| Other | (12) | 165 |
| Total other (expense) income, net | \$ (531) | \$ 317 |

Other expense, net for the six months ended June 30, 2015 was an expense of \$531,000 compared to income of \$317,000 for the same period in 2014. The significant fluctuations in other (expense) income, net were primarily related to foreign currency transaction gains and losses and interest expense and interest income related to 2014.

Table of Contents**Non-GAAP Financial Measures**

In addition to disclosing financial results calculated in accordance with U.S. Generally Accepted Accounting Principles (GAAP), our quarterly report on Form 10-Q discloses Non-GAAP financial measures adjusted for: provision for income taxes, depreciation and amortization of property and equipment, amortization of intangible assets, provision for doubtful accounts, amortization of prepaid stock compensation, amortization of prepaid sponsorship fees, stock-based compensation, issuance of common stock warrants and other income and expense. We believe that the non-GAAP measures provide investors with important perspectives into our ongoing business performance. The non-GAAP financial measures should not be considered a substitute for, or superior to, financial measures calculated in accordance with GAAP, and the financial results calculated in accordance with GAAP and reconciliations to those financial statements should be carefully evaluated. The non-GAAP financial measures we used may be calculated differently from, and therefore may not be comparable to, similarly titled measures used by other companies.

The U.S GAAP measure most directly comparable to EBITDA is income (loss) from operations. The non GAAP financial measure of Adjusted EBITDA should not be considered as an alternative to net income (loss). Adjusted EBITDA is not a presentation made in accordance with U.S. GAAP and has important limitations as an analytical tool and should not be considered in isolation or as a substitute for analysis of our results as reported under U.S. GAAP. Because Adjusted EBITDA excludes some, but not all, items that affect net earnings and is defined differently by different companies, our definition of Adjusted EBITDA may not be comparable to similarly titled measures of other companies.

Set forth below are reconciliations of non-GAAP net income (loss) to our reported GAAP net (loss) income:

| | Three Months Ended June 30, | | Six Months Ended June 30, | |
|-----------------------------------------------------------------|-----------------------------|-----------------|---------------------------|------------------|
| | 2015 | 2014 | 2015 | 2014 |
| | (in thousands) | | | |
| Adjusted EBITDA: | | | | |
| Net (loss) income | \$ (7,025) | \$ (935) | \$ (14,504) | \$ 1,801 |
| Non-GAAP adjustments: | | | | |
| Provision for income taxes | 21 | 45 | 33 | 77 |
| Depreciation and amortization of property and equipment | 456 | 333 | 838 | 647 |
| Amortization of intangible assets | 273 | 293 | 498 | 578 |
| Provision for doubtful accounts | 68 | 64 | 98 | 140 |
| Amortization of prepaid stock compensation | 1,127 | 783 | 2,236 | 1,578 |
| Amortization of prepaid sponsorship fees | 1,821 | 1,810 | 3,252 | 3,468 |
| Stock-based compensation | 4,013 | 2,091 | 6,536 | 4,467 |
| Issuance of common stock warrants to third-parties for services | 17 | | 50 | |
| Other expense (income), net | 348 | 27 | 531 | (317) |
| Adjusted EBITDA | \$ 1,119 | \$ 4,511 | \$ (432) | \$ 12,439 |

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| | Six Months Ended Jun 30, 2015 | Three Months Ended | | Year Ended Dec. 31, 2014 | Three Months Ended | | | Year Ended Dec 31, 2013 | Three Months Ended | | | |
|--|-------------------------------|--------------------|--------------|--------------------------|--------------------|--------------|--------------|-------------------------|--------------------|--------------|--------------|--------------|
| | | Jun 30, 2015 | Mar 31, 2015 | | Dec 31, 2014 | Sep 30, 2014 | Jun 30, 2014 | | Mar 31, 2014 | Dec 31, 2013 | Sep 30, 2013 | Jun 30, 2013 |
| | | | | | | | | | | | | |
| | \$ (14,504) | \$ (7,025) | \$ (7,479) | \$ (13,832) | \$ (16,236) | \$ 603 | \$ (935) | \$ 2,736 | \$ (17,718) | \$ (3,988) | \$ (3,946) | \$ (2,422) |
| | | | | | | | | | | | | |
| | 33 | 21 | 12 | 33 | (138) | 94 | 45 | 32 | 115 | 115 | | |
| | | | | | | | | | | | | |
| | 838 | 456 | 382 | 1,285 | 335 | 303 | 333 | 314 | 709 | 198 | 178 | 172 |
| | 498 | 273 | 225 | 698 | 276 | (156) | 293 | 285 | | | | |
| | | | | | | | | | | | | |
| | 98 | 68 | 30 | 201 | 37 | 24 | 64 | 76 | 242 | 83 | 54 | 76 |
| | | | | | | | | | | | | |
| | 2,236 | 1,127 | 1,109 | 3,716 | 1,028 | 1,110 | 783 | 795 | 6,562 | 1,177 | 2,040 | 3,224 |
| | | | | | | | | | | | | |
| | 3,252 | 1,821 | 1,431 | 5,802 | 786 | 1,548 | 1,810 | 1,658 | 4,011 | 1,155 | 1,021 | 1,157 |
| | 6,536 | 4,013 | 2,523 | 10,928 | 4,055 | 2,406 | 2,091 | 2,376 | 3,075 | 1,487 | 1,514 | 37 |
| | | | | | | | | | | | | |
| | 50 | 17 | 33 | 130 | 61 | 69 | | | | | | |
| | | | | | | | | | | | | |
| | 531 | 348 | 183 | (5,577) | (26) | (5,234) | 27 | (344) | 3,306 | (2,089) | (927) | (319) |
| | | | | | | | | | | | | |
| | \$ (432) | \$ 1,119 | \$ (1,551) | \$ 3,384 | \$ (9,822) | \$ 767 | \$ 4,511 | \$ 7,928 | \$ 302 | \$ (1,862) | \$ (66) | \$ 1,925 |

Liquidity and Capital Resources

Since the inception of MusclePharm, other than revenue from product sales, our primary source of operating cash has been from the sale of equity, the issuance of convertible secured promissory notes and other short-term debt as discussed below. As of June 30, 2015, our cash balance was \$4.2 million which consists primarily of cash on deposit with banks.

Our principal use of cash is to purchase inventory, pay for operating expenses and acquire capital assets. As of June 30, 2015, we had a deficit in working capital of \$1.1 million, an accumulated deficit of \$110.2 million and total stockholders' equity of \$18.2 million. As of June 30, 2015, we had outstanding borrowings of \$6.0 million under our line of credit facility. In addition, we entered into a \$4.0 million commercial loan agreement in February 2015 which was fully drawn during the first quarter 2015.

We believe that with increased sales expansion, international sales expansion, along with the additional debt financing obtained in February 2015, and additional debt financing anticipated in the third quarter 2015, there will be opportunities to increase revenue such that our capital resources will be sufficient through at least June 30, 2016; to execute the business plan, which includes more inventory purchases, new product releases and additional advertising, promotions, sponsorships and endorsements. There can be no assurance that such capital will be available on acceptable terms or at all.

Our net consolidated cash flows are as follows:

| | Six Months Ended June 30, | |
|-----------------------------------------------------|----------------------------------|-------------|
| | 2015 | 2014 |
| | (In thousands) | |
| Consolidated Statements of Cash Flows Data: | | |
| Net cash provided by operating activities | \$ 4,189 | \$ 271 |
| Net cash (used in) provided by investing activities | (2,318) | 621 |
| Net cash provided by (used in) financing activities | 1,456 | (2,554) |
| Effect of exchange rate changes on cash | (177) | 19 |
| Net increase (decrease) in cash | \$ 3,150 | \$ (1,643) |

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Operating Activities

Our cash provided by operating activities is driven primarily by sales of our products. Our primary uses of cash from operating activities have been for advertising and promotion expenses, personnel-related expenditures, manufacturing costs, professional fees, and costs related to our facilities. Our cash flows from operating activities will continue to be affected principally by the results of operations and the extent to which we increase spending on personnel expenditures, sales and marketing activities, and our working capital requirements.

During the six months ended June 30, 2015, cash provided by operating activities was \$4.2 million, which differs from our net loss of \$14.5 million primarily because of non-cash charges of \$13.5 million, and a net change in our net operating assets and liabilities of \$5.2 million. The non-cash charges primarily consisted of \$6.5 million for stock-based compensation, \$3.3 million for amortization of prepaid sponsorship and endorsement fees, \$2.2 million for amortization of prepaid stock compensation, and \$1.3 million for depreciation of our property and equipment and amortization of our intangible assets. The primary drivers of the changes in operating assets and liabilities were a \$6.2 million decrease in inventory due to improvement in our supply chain management and promotional sales, decrease in inventory purchase cost and increased sales, a \$10.1 million increase in accounts payable primarily attributable to the timing of payments to vendors, partially offset by a \$8.1 million increase in accounts receivable due to an increase in sales and timing of collections compared to December 31, 2014, and a \$3.5 million increase in prepaid sponsorship and endorsement fees due to an increase in advertising efforts through sponsorships and endorsements.

During the six months ended June 30, 2014, cash provided by operating activities was \$0.3 million, primarily as a result of our net income of \$1.8 million and non-cash charges of \$10.4 million, partially offset by an \$11.9 million net change in our operating assets and liabilities. The non-cash charges primarily consisted of stock-based compensation of \$4.5 million, amortization of prepaid sponsorship and endorsement fees of \$3.5 million and amortization of prepaid stock compensation of \$1.6 million. The net change in our operating assets and liabilities was primarily the result of a \$4.8 million increase in accounts receivable due to increased sales and timing of collections, a \$3.2 million decrease in accounts payable due to the timing of payments to vendors, and a \$2.5 million increase in prepaid sponsorship and endorsement fees due to an increase in advertising efforts through sponsorships and endorsements.

Investing Activities

Cash used in investing activities of \$2.3 million for the six months ended June 30, 2015, was primarily due to cash payment of \$0.9 million related to MusclePharm apparel rights acquisition, investment in contract manufacturer of \$1.0 million related to our opportunity to acquire Capstone and purchase of property and equipment of \$0.9 million, partially offset by proceeds from disposal of property and equipment of \$0.4 million.

Cash provided by investing activities of \$0.6 million for the six months ended June 30, 2014, was primarily due a change in restricted cash of \$2.5 million and \$0.5 million from the proceeds from settlement of marketable securities which was partially offset by \$2.4 million for purchase of property and equipment.

Financing Activities

Cash flows provided by financing activities of \$1.5 million for the six months ended June 30, 2015, was primarily due to proceeds from issuance of our term loan of \$4.0 million and draw down of our line of credit of \$4.0 million, partially offset by repayment of term loan of \$0.4 million and repayment on our line of credit of \$6.0 million.

Cash used in financing activities of \$2.6 million for the six months ended June 30, 2014 was primarily due to repayment on our line of credit of \$2.5 million.

Line of Credit

In September 2014, we entered into a line of credit facility with a banking institution for up to \$8.0 million of borrowings. The line of credit matures in September 2017 and accrues interest at the prime rate plus 2%, currently 5.25%. The line of credit is secured by our inventory, accounts receivable, intangible assets and equipment. As of December 31, 2014, we had drawn down all \$8.0 million under the line of credit and as of June 30, 2015, the outstanding borrowings under the line of credit was \$6.0 million. We were not in compliance with certain financial covenants under this facility as of June 30, 2015 and received a written waiver from the bank until August 31, 2015.

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Term Loan

In February 2015, we entered into a term loan agreement with a banking institution for a principal amount of \$4.0 million. The term loan carries a fixed interest rate of 5.25% per annum, is repayable in 36 equal monthly installments of principal and interest, and matures in February 2018. Borrowings on the term loan are secured by our assets, and 860,900 shares of our common stock held in treasury. We are also required to comply with certain negative covenants under the term loan, including restrictions on indebtedness, investments, asset dispositions, mergers or consolidations and other corporate activities. We were not in compliance with certain financial covenants and received a written waiver from the bank until August 31, 2015.

Contractual Obligations

Our principal commitments consist of obligations under operating leases for office and warehouse facilities, capital leases for manufacturing and warehouse equipment, car fleet, and non-cancelable endorsement and sponsorship agreements.

We presented our contractual obligations in our Annual Report on Form 10-K for the fiscal year ended December 31, 2014. During the six months ended June 30, 2015, we entered into:

Various agreements with Capstone, requiring us to pay \$2.5 million to fund the expansion of manufacturing capabilities of its facility,

In April 2015, the Company entered a partnership with the Cleveland Cavaliers of the National Basketball Association. The total future contractual payments under the agreement at June 30, 2015 are approximately \$2.4 million with additional payments for potential playoff games.

In May 2015, the Company entered into a multi-year partnership with City Football Group and its four clubs: Manchester City Football Club (including the Continental Cup-winning Manchester City Women's Football Club), Melbourne City Football Club, New York City Football Club, and Yokohama F. Marinos football club. The total contractual payments under the agreement at June 30, 2015 are approximately \$8.4 million.

In June 2015, the Company entered into sponsorship and endorsement agreements with bodybuilding pioneer Bill Phillips as Strategic Advisor and Chief Editor of Content. The minimum contractual payments under the agreements as of June 30, 2015 are approximately \$1.0 million of which \$250,000 has been paid as of June 30, 2015.

Off-Balance Sheet Arrangements

We did not have any off-balance sheet arrangements as of June 30, 2015.

Item 3. Quantitative and Qualitative Disclosures About Market Risk

We are exposed to market risks, including changes to foreign currency exchange rates and interest rates.

Foreign Currency Exchange Risk

We have foreign currency risks related to our revenue and operating expenses denominated in currencies other than the U.S. dollar, primarily the Canadian Dollar and more recently the Euro. In general, we are a net receiver of currencies other than the U.S. dollar. Accordingly, changes in exchange rates, and in particular a strengthening of the

U.S. dollar, will negatively affect our revenue and other operating results as expressed in U.S. dollars.

We have experienced and will continue to experience fluctuations in our net income (loss) as a result of transaction gains or losses related to revaluing certain current asset and current liability balances that are denominated in currencies other than the functional currency of the entities in which they are recorded. At this time we have not entered into, but in the future we may enter into, derivatives or other financial instruments in an attempt to hedge our foreign currency exchange risk. It is difficult to predict the effect hedging activities would have on our results of operations. We recognized a loss of \$197,000 and \$261,000 related to fluctuations in foreign currency for the three and six months ended June 30, 2015, respectively.

Interest Rate Sensitivity

Our exposure to market risk for changes in interest rates relates primarily to our indebtedness.

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Our total outstanding borrowings under the line of credit agreement and the term loan agreement were \$9.6 million as of June 30, 2015. Our exposure to interest rates relates to the change in the amounts of interest we must pay on our borrowings. Our borrowing rate is 5.25% as of June 30, 2015. We would not expect a hypothetical 10% impact to our interest rate to have a significant impact on our interest expense.

Item 4. Controls and Procedures

Evaluation of Disclosure Controls and Procedures

Our management, with the participation of our chief executive officer (CEO) and chief financial officer (CFO), has evaluated the effectiveness of our disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934, as amended (Exchange Act)), as of the end of the period covered by this Quarterly Report on Form 10-Q. Based on such evaluation, our CEO and CFO have concluded that as of June 30, 2015, our disclosure controls and procedures are designed at a reasonable assurance level and are effective to provide reasonable assurance that information we are required to disclose in reports that we file or submit under the Exchange Act is recorded, processed, summarized, and reported within the time periods specified in the rules and forms of the Securities and Exchange Commission (SEC), and that such information is accumulated and communicated to our management, including our CEO and CFO, as appropriate, to allow timely decisions regarding required disclosure.

Changes in Internal Control

There were no changes in our internal control over financial reporting identified in management's evaluation pursuant to Rules 13a-15(d) or 15d-15(d) of the Exchange Act during the first quarter of 2015 that materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

Limitations on Effectiveness of Controls and Procedures

In designing and evaluating the disclosure controls and procedures, management recognizes that any controls and procedures, no matter how well designed and operated, can provide only reasonable assurance of achieving the desired control objectives. In addition, the design of disclosure controls and procedures must reflect the fact that there are resource constraints and that management is required to apply judgment in evaluating the benefits of possible controls and procedures relative to their costs.

Table of Contents**PART II OTHER INFORMATION****Item 1. Legal Proceedings**

In the normal course of business, we may become involved in legal proceedings. We will accrue a liability for such matters when it is probable that a liability has been incurred and the amount can be reasonably estimated. When only a range of possible loss can be established, the most probable amount in the range is accrued. If no amount within this range is a better estimate than any other amount within the range, the minimum amount in the range is accrued. The accrual for a litigation loss contingency might include, for example, estimates of potential damages, outside legal fees and other directly related costs expected to be incurred. As of June 30, 2015 and December 31, 2014, we were not involved in any material legal proceedings, except for the SEC investigation discussed below.

SEC Investigation

In July 2013, we received a formal order of investigation (the Investigation) from the Denver Regional Office of the SEC which is actively investigating various areas of potential violation of the federal securities laws involving us and our management. The SEC has issued subpoenas for documents and testimony and has deposed numerous witnesses in connection with the Investigation. As a result of a review undertaken by our personnel in conjunction with the Audit Committee of the Board of Directors during 2014, we amended certain prior reports to revise various disclosures concerning executive compensation and disclosure of perquisites, among other things, and filed amendments to the annual reports on Form 10-K for the fiscal years ended December 31, 2013, 2012 and 2011. The Investigation remains ongoing. The Investigation could lead to the SEC seeking fines, penalties, injunctive relief and the adoption of corrective plans to establish reporting and other practices affecting us. We have reached an agreement in principle with the staff of the Enforcement Division of the SEC Denver Regional Office to resolve the investigation by the SEC, however, such agreement must be approved by the SEC Commissioners. Neither the nature of the relief, the amount of any monetary relief, nor the nature of the corrective actions, whether voluntary or imposed as a result of court proceedings that could be sought by the SEC, can be predicted. The result of any of the foregoing could have a material adverse effect on the Company or our management.

Item 1A. Risk Factors

Except as set forth below, there have been no material changes to the Risk Factors as disclosed in our Annual Report on Form 10-K filed with the Securities and Exchange Commission on March 16, 2015.

Our articles of incorporation, our amended and restated by-laws and Nevada law could deter a change of our management which could discourage or delay offers to acquire us.

Certain provisions of Nevada law and of our articles of incorporation, and by-laws, as amended, could discourage or make it more difficult to accomplish a proxy contest or other change in our management or the acquisition of control by a holder of a substantial amount of our voting stock. It is possible that these provisions could make it more difficult to accomplish, or could deter transactions that stockholders may otherwise consider to be in their best interests or in our best interests. These provisions include:

requiring stockholders who wish to request a special meeting of the stockholders to disclose certain specified information in such request and to deliver such request in a specific way within a certain timeframe, which may inhibit or deter stockholders from requesting special meetings of the stockholders;

requiring that stockholders who wish to act by written consent request a record date from us for such action and such request must include disclosure of certain specified information, which may inhibit or deter stockholders from acting by written consent;

establishing the Board of Directors as the sole entity to fill vacancies of the Board of Directors, which lengthens the time needed to elect a new majority of the board;

establishing a two-thirds majority vote of the stockholders to remove a director from the Board of Directors, as opposed to a simple majority, which lengthens the time needed to elect a new majority of the board;

establishing that any person who acquires equity in us shall be deemed to have notice and consented to the forum selection provision of our Bylaws requiring actions to be brought only in New York, which may inhibit or deter stockholders actions (i) on behalf of us, (ii) asserting claims of breach of fiduciary duty by officers or directors of us, or (iii) arising out of the Nevada Revised Statutes.

establishing more detailed disclosure and in any stockholder's advance notice to nominate a new member of the Board of Directors including specified information regarding such nominee, which may inhibit or deter such nomination and lengthens the time needed to elect a new majority of the board;

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Item 2. Unregistered Sales of Equity Securities and Use of Proceeds

Grants to Employee and Directors

In April 2015, the Company issued 192,784 shares of common stock including restricted stock awards, to its employees, executive officer and directors.

Restricted Stock Awards Related to Energy Drink Agreement

In January 2015, the Company entered into an energy drink agreement with Langer Juice and Creative Flavors. In connection with the agreement, the Company issued a total of 150,000 shares of its restricted common stock which vest monthly over a period of three years.

Agreements with Worldwide Apparel, LLC – Muscle Pharm Apparel Rights

In February 2015, the Company entered into an agreement with Worldwide Apparel, LLC (Worldwide) to terminate Worldwide's right to use MusclePharm's brand images in apparel effective March 28, 2014. The brand rights were originally licensed in May 2011, and amended in March 2014 prior to the termination. The consideration related to the acquisition of the MusclePharm Apparel from Worldwide consists of a cash consideration of \$850,000 and 170,000 shares of MusclePharm common stock with an aggregated fair value of \$1.4 million on issuance date.

Restricted Stock Awards Issued Related to Financing Agreement

In May 2015, the Company terminated a financing agreement with a lending institution and issued 50,000 shares of its common stock.

Restricted Stock Awards Issued Related to Consulting/Endorsement Agreement

In May 2015, the Company entered into consulting and endorsement agreements with Bill Phillips, a fitness and bodybuilding pioneer, to serve as strategic advisor and Chief Editor of Content of the Company. In connection with the endorsement agreements, the Company issued 50,000 shares of its restricted common stock. In connection with the consulting agreement, the Company agreed to issue shares worth \$25,000 within 10 days after each subsequent three month period term. The consulting agreement is for a 3 year period but may be cancelled with 30 days written notice.

The above issuances of these securities were deemed to be exempt from the registration requirements of the Securities Act of 1933, as amended, by virtue of Section 4(a)(2) thereof, as a transaction by an issuer not involving a public offering.

Item 3. Defaults Upon Senior Securities.

Not applicable.

Item 4. Mine Safety Disclosures

Not applicable.

Item 5. Other Information.

None.

Table of Contents**Item 6. Exhibits.**

| Exhibit No. | Description |
|--------------------|-------------------------------------------------------------------------------------------------------------------------|
| 10.1* | Separation Agreement by and between MusclePharm Corporation and Andrew Lupo dated May 21, 2015 |
| 10.2* | Separation Agreement by and between MusclePharm Corporation and Gregory Macosko dated May 21, 2015 |
| 10.3* | Separation Agreement by and between MusclePharm Corporation and Daniel McClory dated May 21, 2015 |
| 10.4* | Executive Employment Agreement by and between MusclePharm Corporation and Brad Pyatt dated June 24, 2015 |
| 10.5* | Executive Employment Agreement by and between MusclePharm Corporation and Richard Estalella dated June 24, 2015 |
| 10.6* | Confidentiality and Non-Disclosure Agreement by and between MusclePharm Corporation and Consac, LLC dated June 23, 2015 |
| 31.1* | Rule 13 (A) 14(A) Certification of Principal Executive Officer |
| 31.2* | Rule 13 (A) 14(A) Certification of Principal Financial Officer |
| 32.1* | Section 1350 Certification of Principal Executive Officer |
| 32.2* | Section 1350 Certification of Principal Financial Officer |
| 101.INS | XBRL Instance Document |
| 101.SCH | XBRL Taxonomy Extension Schema |
| 101.CAL | XBRL Taxonomy Extension Calculation Linkbase |
| 101.DEF | XBRL Taxonomy Extension Definition Linkbase |
| 101.LAB | XBRL Taxonomy Extension Label Linkbase |
| 101.PRE | PRE XBRL Presentation Linkbase Document |

* Filed herewith

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SIGNATURES

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

MUSCLEPHARM CORPORATION

Date: August 10, 2015

By: /s/ Brad J. Pyatt
Name: Brad J. Pyatt
Title: Chief Executive Officer and President

(Principal Executive Officer)

Date: August 10, 2015

By: /s/ John Price
Name: John Price
Title: Chief Financial Officer

(Principal Financial Officer)

(Principal Accounting Officer)