

Health Fitness Corp /MN/
Form 10-K
March 25, 2009

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**UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, DC 20549**

**FORM 10-K
ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF
THE SECURITIES EXCHANGE ACT OF 1934
FOR THE FISCAL YEAR ENDED DECEMBER 31, 2008
Commission File No. 000-25064**

**HEALTH FITNESS CORPORATION
(Exact name of registrant as specified in its charter)**

Minnesota **No. 41-1580506**
(State or Other Jurisdiction of **(IRS Employer**
Incorporation or Organization) **Identification No.)**
1650 West 82nd Street, Bloomington, Minnesota 55431
(Address of Principal Executive Offices)
(952) 831-6830
(Registrant's telephone number, including area code)

Securities registered pursuant to Section 12(b) of the Act: Common Stock, \$.01 Par Value
Securities registered pursuant to Section 12(g) of the Act: None

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act.
Yes No

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act. Yes No

Note: Checking the box above will not relieve any registrant required to file reports pursuant to Section 13 or 15(d) of the Exchange Act from their obligations under those Sections.

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

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

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

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

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Act). Yes No
The aggregate market value of our common stock held by non-affiliates as of June 30, 2008 was approximately \$24,030,000 (based on the closing sale price of \$3.60 per share as reported on the OTC Bulletin Board).

The number of shares outstanding of the registrant's common stock as of March 23, 2009 was: Common Stock, \$0.01 par value, 9,751,920 shares.

DOCUMENTS INCORPORATED BY REFERENCE

Portions of the proxy statement for the registrant's 2009 Annual Meeting of Shareholders are incorporated by reference into Items 10, 11, 12, 13 and 14 of Part III of this report.

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We make available, free of charge, copies of our annual report on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K and amendments to those reports filed or furnished pursuant to Section 13(a) or 15(d) of the Securities Exchange Act on our web site, www.hfit.com, as soon as reasonably practicable after filing such material electronically or otherwise furnishing it to the SEC. We are not including the information on our web site as a part of,

or incorporating it by reference into, our Form 10-K.

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PART I

**ITEM 1. BUSINESS
OVERVIEW**

Health Fitness Corporation, a Minnesota corporation (also referred to as we, us, our, the Company, or Health Fitness), is a leading provider of population health improvement services and programs to corporations, hospitals, communities and universities located in the United States and Canada. We currently manage 215 corporate fitness center sites, 166 corporate health management sites and 99 unstaffed health management programs.

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

You may contact us at our executive offices at 1650 West 82nd Street, Suite 1100, Minneapolis, Minnesota 55431, telephone number (952) 831-6830. We maintain an internet website at www.hfit.com. We were incorporated on March 31, 1987.

BUSINESS MODEL

Major corporations, hospitals and universities invest in fitness centers and health improvement programs for several reasons. First, it is widely understood that healthier employees are more productive, experience reduced levels of stress and are absent from work less often due to illness. At the same time, companies are struggling to deal with the rising cost of employee healthcare, which has historically increased at double-digit rates. According to a recent government report, U.S. spending on prescription drugs, hospital care and other health services is expected to double to \$4.1 trillion over the next decade, up from \$2.1 trillion in 2006. This dramatic increase in expected healthcare costs is primarily attributed to an aging population and poor lifestyle choices relating to diet and exercise. Many companies realize that they may be able to decrease the financial burden of employee healthcare and lost productivity by making health improvement programs a strategic business priority. We believe the services we offer will help employees make better lifestyle behavior choices, thus improving their health, in addition to helping companies decrease the rate of spending on employee healthcare costs.

To capitalize on the growth opportunities within the employer marketplace, we organized our business into two segments: Fitness Management Services and Health Management Services. Within each of these business segments, we provide two types of service: (i) Staffing Services, and (ii) Program Services. Segment reporting is helpful for understanding our business because of the following: (i) the evolution of our Health Management segment and management's belief that the future growth of our Company depends on our Health Management segment; (ii) beginning with the fourth quarter of 2008 total revenue and gross profit from our Health Management segment has begun to outpace the total revenue and gross profit from our legacy Fitness Management segment; (iii) management has invested significant resources to hire additional service and account management staff to handle the growth we have experienced, and expect to experience in the future in the Health Management segment; (iv) management has invested, and expects to continue investing resources to enhance the functionality of our web-based software system to appeal to a wider range of current and new customers for both of our operating segments, and (v) on a monthly, quarterly and annual basis, we manage the performance of our business by reviewing internally-generated financial reports that detail revenue and gross profit results for each segment.

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Following is a description of the services we offer within each segment:

Fitness Management Services

The Fitness Management segment of our business involves the management of fitness centers that have been developed and equipped by corporations and other organizations for their employees. Historically, corporations developed these fitness centers as a way to attract and retain productive employees. More recently, these same corporations have come to realize that a fitness center can play an integral role in modifying unhealthy lifestyle behaviors and improving work productivity.

In terms of size, we believe we are the largest provider of corporate fitness center management services in the United States. Currently, we manage 215 corporate sites, including two sites located in Canada, all of which accounted for approximately 53%, 61%, and 66% of our 2008, 2007 and 2006 revenue, respectively. From a sales perspective, we generally obtain new corporate customers by submitting a proposal, which answers specific questions regarding our management philosophies and pricing structures.

Our Fitness Management segment derives its revenue from the following services:

Staffing Services. We have agreements with corporations and other organizations to staff and manage fitness centers they have developed for use by their employees. We derive revenue from these services through the reimbursement of staff costs, including wages, taxes and benefits, and reimbursement of our costs to provide liability insurance to protect our customers against injury claims. We also receive a management fee to cover the cost of regional and corporate support services. Costs of revenue are comprised of staff wages, employer taxes and employee benefits, in addition to fitness center operating expenses we may contractually agree to pay.

In 2008, 2007 and 2006, revenue from our Fitness Management staffing services accounted for 49.8%, 56.8% and 62.4%, respectively, of total consolidated revenue.

Program Services. At many of our managed fitness centers, we generate additional revenue from members through the delivery of fee-for-service fitness and wellness program services. These services primarily include personal training, weight loss programs, seminars, special classes and massage therapy. Costs of revenue are comprised of commissions we pay our staff for selling and delivering these program services, in addition to the cost of inventory when products are sold in connection with a service.

Within our fitness management consulting practice, companies that are planning new fitness centers may employ us to develop floor plans and interior design plans, select and source fitness equipment and design fitness programs. For companies that desire to develop a commercial fitness center, we can perform a comprehensive analysis of market potential for the center. Services can include demographic analysis, market analysis, and multiple-year financial business plan development.

In 2008, 2007 and 2006, revenue from our Fitness Management program services accounted for 3.2%, 3.8% and 4.0%, respectively, of total consolidated revenue.

Health Management Services

The Health Management segment of our business involves the delivery of services to help corporations and other organizations assess the health characteristics of their employees. We also provide health education services to employees dealing with multiple health risks to improve their lifestyle behaviors.

This segment of our business has experienced the fastest rate of growth, with 2008 revenue growing approximately 33% over 2007, and 2007 revenue growing approximately 29% over 2006. This growth is attributed to our past and recent investments to strategically enhance this segment, which has improved our ability to meet the increasing market demand for health improvement services, as well as meet the increasing needs of our customers. Currently, we manage 166 corporate health management sites and 99 unstaffed health management programs, which accounted for approximately 47%, 39% and 34% of our 2008, 2007 and 2006 revenue, respectively. In this

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segment, we generally obtain new corporate customers by submitting a proposal, which answers specific questions regarding our management philosophies and pricing structures.

Our Health Management segment derives its revenue from the following services:

Staffing Services. We have agreements with corporations and other organizations to staff and manage the delivery of health promotion programs, lifestyle coaching services, and injury prevention and treatment services. These relationships may or may not involve the management of an on-site fitness center. We derive revenue from these services through the reimbursement of staff costs, including wages, taxes and benefits, and reimbursement of our cost to provide liability insurance to protect our customers against injury claims. We also receive a management fee to cover the cost of regional and corporate support services. Costs of revenue are comprised of staff wages, employer taxes and employee benefits, in addition to operating expenses we may contractually agree to pay.

In 2008, 2007 and 2006, revenue from our Health Management staffing services accounted for 23.4%, 22.6% and 21.5%, respectively, of total consolidated revenue.

Program Services. We offer a comprehensive menu of products and services to assess the health risks of our customer s employees, and manage specific health risks by delivering programs to educate and coach participants to improve lifestyle behaviors. We derive program revenue from participant fees we charge for our e-Health platform; paper and web-based health risk assessments; biometric screenings to assess blood profiles and body composition; administering flu shots; and face-to-face, web-based and telephonic health coaching services. We also derive revenue from data collection and reporting services as it relates to the demonstration of program effectiveness. Revenue from these program services are generally paid by our corporate customer, although they may ask their employees to share in the cost. Our costs of revenue for these services are mainly comprised of supply expenses and the direct cost of staff wages, taxes and benefits.

Within our health management consulting practice, we provide corporations and other organizations with a comprehensive analysis of the effectiveness of employee health improvement programs, with a focus on demonstrating a return on investment. We also provide a suite of occupational health consulting services, including injury prevention program design, work-hardening programs, injury treatment, return-to-work programs and regulatory compliance consulting.

In 2008, 2007 and 2006, revenue from our Health Management program services accounted for 23.6%, 16.7% and 12.1%, respectively, of total consolidated revenue.

CONTRACT DURATION

In each of our business segments, the duration of staffing and program service agreements may widely vary, from those that are month-to-month, to those that have a term of five years. A typical staffing services contract carries a term of three years, with revenue recognized upon delivery of service. Contract duration for program services generally ranges from month-to-month up to three years, depending on the scope of services to be delivered. Revenues for these services are recognized upon delivery of service.

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We assess and manage the performance of each business segment by reviewing internally-generated reports that detail revenue and gross profit results for each of our customer sites. This information is used to formulate plans regarding the future prospects of our business, and aids in our determination of how we will invest our resources to ensure we achieve our future revenue and profitability targets.

The following table provides an analysis of business segment revenue and gross profit for each of the years ended December 31, 2008, 2007 and 2006:

| | 2008 | 2007 | 2006 |
|---|---------------|---------------|---------------|
| Revenue | | | |
| <u>Fitness Management Services</u> | | | |
| Staffing Services | \$ 38,698,420 | \$ 39,747,239 | \$ 39,670,546 |
| Program Services | 2,459,854 | 2,679,881 | 2,574,463 |
| | 41,158,274 | 42,427,120 | 42,245,009 |
| <u>Health Management Services</u> | | | |
| Staffing Services | 18,141,690 | 15,819,481 | 13,669,201 |
| Program Services | 18,376,445 | 11,711,450 | 7,664,330 |
| | 36,518,135 | 27,530,931 | 21,333,531 |
| <u>Total Revenue</u> | | | |
| Staffing Services | 56,840,110 | 55,566,720 | 53,339,747 |
| Program Services | 20,836,299 | 14,391,331 | 10,238,793 |
| | \$ 77,676,409 | \$ 69,958,051 | \$ 63,578,540 |
| <u>Gross Profit</u> | | | |
| <u>Fitness Management Services</u> | | | |
| Staffing Services | \$ 8,844,103 | \$ 8,643,280 | \$ 8,861,829 |
| Program Services | 928,455 | 1,155,217 | 1,129,585 |
| | 9,772,558 | 9,798,497 | 9,991,414 |
| <u>Health Management Services</u> | | | |
| Staffing Services | 4,788,484 | 3,974,348 | 3,399,875 |
| Program Services | 9,178,484 | 5,868,032 | 4,239,295 |
| | 13,966,968 | 9,842,380 | 7,639,170 |
| <u>Total Gross Profit</u> | | | |

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| | | | |
|-------------------|---------------|---------------|---------------|
| Staffing Services | 13,632,587 | 12,617,628 | 12,261,704 |
| Program Services | 10,106,939 | 7,023,249 | 5,368,880 |
| | \$ 23,739,526 | \$ 19,640,877 | \$ 17,630,584 |

With respect to segment asset allocation in accordance with FASB Statement No. 131, *Disclosure about Segments of an Enterprise and Related Information*, management believes the Company does not have assets that are related solely to each segment, except for the segmentation of goodwill for annual impairment testing, and thus has not allocated assets to our reportable segments for the following reasons:

- a. The Company is a service business that depends heavily on the joint efforts of our staff to operate and grow each segment of our business.
- b. We do not maintain a large asset infrastructure. The tangible and intangible assets we do own, including the web-based software system we acquired from HealthCalc, are deployed across both segments of our business to generate segment revenue and gross profit results.
- c. Our future growth plans involve a tighter integration between our Fitness and Health Management segments, resulting in opportunities to cross-sell our fitness and health management services to existing customers within each segment. It is difficult to ascertain which assets are responsible for segment results.
- d. We do not separate assets into our reportable segments for internal accounting and reporting purposes. Management believes an arbitrary allocation of assets to each reportable segment would not result in meaningful information about our business.

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GROWTH STRATEGY

In the long-term, we believe that we can enhance our position as the leading integrator of fitness and health management services for corporations and other large organizations. Key elements of our growth strategy include:

Pursue both aggressive organic growth and strategic opportunities in our Health Management business segment. We believe the market for population health management programs will continue to grow.

Pursue new customers in our Fitness Management business segment to expand market share. As the largest provider of corporate fitness management services, we believe we can continue to add new customers, and sell additional fitness services to our current customers. However, this segment operates in a mature market, and price competition is common.

Maximize opportunities to sell our Fitness Management customers on adopting the services we offer in our integrated Health Management model.

Pursue strategic opportunities that provide operational capabilities and long-term financial value.

It has been our practice to continue investing in our Health Management business segment commensurate with the addition of new business, including investments in people, systems and infrastructure in order to enhance our ability to scale, gain greater cost efficiencies and provide a broader base of services. However, we are currently undertaking such investments with caution and due sensitivity to how current macro-economic conditions may affect our business.

OPERATIONS

In our Fitness Management segment, we have one Vice President of Account Services, who has management responsibility for all of our geographical regions in the United States. Each region is managed by a Regional Vice President, who is responsible for fitness center and wellness program staffing, service quality, financial performance, client relationships and the introduction of new service capabilities to our customers.

In our Health Management segment, we have one Vice President of Account Services, who manages all activities related to our health management customers. We also have Regional Vice Presidents who are directly responsible for program implementation, service delivery, financial performance and client relationships.

The Vice President of each segment reports to a Senior Vice President of Account Services, who in turn reports directly to our Chief Operations Officer. These two positions have primary operational management responsibility for our entire business.

Our corporate office provides centralized administrative support, including accounting and finance, human resources and payroll, information technology systems, sales and marketing, and executive management functions, including the offices of the Chief Financial Officer and Chief Executive Officer.

All expenses related to the operating areas noted above are contained in the Operating Expenses section of our Statements of Operations contained in Item 8 of this Form 10-K.

SALES AND MARKETING

We market our services to corporations, members of the fitness centers we manage and to individuals eligible to participate in their corporate health improvement program. Our sales force actively pursues new corporate customers for each segment of our business, which spans a wide variety of industries. Our sales force is primarily responsible for identifying potential corporate customers and sales lead partners, and managing the overall sales process. Our sales team reports to our Senior Vice President, Business and Corporate Development. Our

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corporate marketing department supports the marketing needs of our sales function, in addition to developing point of sale materials for fitness center programs and collateral materials designed to solicit participation in a health improvement program.

SEASONALITY

In our Fitness Management segment, we do not experience any seasonal fluctuations in the realization of new business, or recognition of revenue. In our Health Management business segment, we may experience seasonal fluctuations in the realization of new business, which will generally be timed with the start of a client's benefit plan year. We have also found that the early stage of certain health management engagements result in a higher rate of revenue recognition due to the delivery of on-site biometric screening services. Thereafter, revenue will decrease to a lower level until we deliver a second phase of biometric screening services to assess health improvement, which is generally one year after the initial phase of screenings.

RESEARCH AND DEVELOPMENT

All research and development activities pertaining to the maintenance of our e-Health technology platform, as well as activities leading up to establishing technological feasibility for significant e-Health platform enhancements, are expensed as incurred.

SIGNIFICANT CUSTOMER RELATIONSHIP

We had one customer that provided 9.7%, 9.8% and 10.3% of our total revenue in 2008, 2007 and 2006, respectively. For this customer, we provide fitness center management and employee wellness administration services for more than 50 locations. The agreement with this customer expires on December 31, 2009, and will automatically renew for successive one year periods unless either party delivers written notice at least 90 days prior to termination. We believe that our relationship with this customer is good.

COMPETITION

Within the business-to-business fitness management services industry, there are relatively few national competitors. However, virtually all markets are home to regional providers that manage several sites within their geographic areas. The principal method of competition among fitness management service providers is price, and our target client base has generally been price-sensitive. With our national presence and almost 30 years of history, management believes that we are recognized as a leading provider of corporate fitness management services, that we have a cost-effective business model, and that we are well positioned to compete in this industry.

Within the business-to-business health management services industry, there has been a trend toward consolidation as companies establish a better position to compete for the growth that is expected in this industry. Disease management and managed care companies have made acquisitions of health management companies within the past thirty-six months. To effectively compete with these organizations, which are larger and have access to more resources, we have made considerable investments into the development of our corporate health management business model. Our December 2005 acquisition of HealthCalc.Net, Inc. and the development of our web-based and telephonic health coaching services have enabled us to more effectively compete with these larger companies. With additional strategic investments to augment our current capabilities, we believe we can build a sustainable competitive advantage in order to compete for new business opportunities against these larger competitors.

PROPRIETARY RIGHTS

We have three registered trademarks, Insight®, It Pays To Be Healthy® and Live For Life® that are used in connection with the sale and delivery of our fitness and health management services. We do not have any other significant proprietary rights.

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GOVERNMENT REGULATION

Management believes there is no significant government regulation which materially limits our ability to provide fitness and health management services to our corporate, hospital, community and university-based clients. Although our occupational health, health risk assessment and health coaching services, in addition to the group health plan we sponsor for our employees, are subject to the requirements of the Health Insurance Portability and Accountability Act of 1996, or HIPAA, we do not believe that these regulations have a material impact on our activities.

FOREIGN OPERATIONS

We provide services to companies located in Canada through our wholly-owned subsidiary Health Fitness Corporation of Canada, Inc. Revenue recognized from our Canadian customers totaled approximately \$265,600, \$241,000 and \$259,300 for the years ended December 31, 2008, 2007 and 2006, respectively. Although we invoice these customers in their local currency, we do not believe there is a risk of material loss due to foreign currency translation.

EMPLOYEES

At December 31, 2008, we had 847 full-time and 2,625 part-time and on-call employees, of which 114 were employed at our corporate, divisional and regional offices. The remainder is primarily engaged in providing our staffing and programs services to our Fitness and Health Management customers. Management believes our relationship with employees is good.

AVAILABLE INFORMATION

We file reports with the Securities and Exchange Commission, referred to herein as the SEC, including annual reports on Form 10-K, quarterly reports on Form 10-Q and other reports from time to time. We are an electronic filer and the SEC maintains an Internet site at www.sec.gov that contains the reports, proxy, information statements and other information filed electronically. The public may read and copy any materials filed by us with the SEC at the SEC's Public Reference Room at 100 F Street, NE, Washington, DC 20549. The public may also obtain information from the Public Reference Room by calling the SEC at 1-800-SEC-0330. In addition, we maintain at our website (www.hfit.com), and make available free of charge, our annual report on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K and all amendments to those reports as soon as reasonably practicable after such information is filed electronically with the SEC. The information provided on our website is not a part of this report, and is therefore not incorporated by reference unless such information is otherwise specifically referenced elsewhere in this report.

OUTLOOK AND TRENDS

Within our Health Management business segment, the high cost of employee health care and lost employee productivity has become a key concern for many corporations. According to published reports, annual health care costs are expected to continue to increase at double digit rates for the next several years due to a number of factors, including an aging workforce, unhealthy populations entering the workforce and obesity-related medical conditions due to poor nutrition and a lack of exercise. We believe that, as part of a broader strategy to reduce health care costs and lost productivity, many companies will be interested in addressing the health needs of employees, and their dependents and retirees, and will also desire to implement specific strategies to help at-risk individuals. We believe that we can provide the products, services, expertise and personnel to effectively meet this need.

Within our Fitness Management segment, recessionary pressures have negatively affected the corporate landscape, which has negatively affected the prices we offer to induce renewal of customer agreements, and to obtain new customers. We believe that price competition will continue for the foreseeable future, which may result in lower profitability. In addition, we have customers that operate in industries that are experiencing significant negative financial pressures. Specifically, we experienced a loss of approximately \$2.8 million in potential annualized

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revenue from the termination of fitness management service contracts. Any additional large contract terminations from customers operating in a troubled industry may have a material adverse effect on our results of operation. We are cautious overall in light of the current challenging and unpredictable macro-economic trends, which significantly increase the uncertainties that we face in developing and implementing our business plans.

ITEM 1A. RISK FACTORS

The foregoing discussion in this Item 1A and the other discussion contained in this Form 10-K contain various forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended. Forward-looking statements are based on current expectations or beliefs concerning future events. Such statements can be identified by the use of terminology such as anticipate, believe, estimate, expect, intend, may, could, possible, plan, project, will, forecast, expressions. Our forward-looking statements generally relate to growth strategies, demand for our services, financial results, marketing efforts, competitive conditions and cash requirements. Although it is not possible to foresee all of the factors that may cause actual results to differ from our forward-looking statements, such factors include, among others, the risk factors that follow. However, investors are cautioned that all forward-looking statements involve risks and uncertainties.

Economic conditions may adversely affect our business. Current adverse global economic conditions and trends pose a risk as consumers and businesses may postpone spending, reduce the size of their workforces, and scale back operations in response to tighter credit, negative financial news, declines in income or asset values, and weakened results of operations, which could have a material negative effect on the demand for our services and programs. Economic difficulties in the credit markets and other economic conditions, such as the risk of a prolonged recession, may reduce the demand and/or the timing of purchases for our services and programs from customers and potential customers. A loss of a customer, a reduction in a current customer's business, or reductions in their employee headcounts could have a material adverse effect on our business and results of operations. Other factors that could influence demand from our customers and potential customers include continuing increases in fuel and other energy costs, conditions in the residential real estate and mortgage markets, labor and healthcare costs, other operating costs, access to credit, consumer confidence, and other macroeconomic factors. These and other economic factors could have a material adverse effect on demand for our services and programs and on our financial condition and operating results. The current financial turmoil affecting the banking system and financial markets and the possibility that financial institutions may consolidate or go out of business have resulted in a tightening in the credit markets, a low level of liquidity in many financial markets, and extreme volatility in fixed income, credit, currency and equity markets. There could be a number of follow-on effects from the credit crisis on our business, including insolvency of key suppliers, inability of customers to obtain credit to finance purchases of our services and programs, and/or customer insolvencies. In addition, current economic conditions have created liquidity and credit constraints in the markets. Should the credit markets not improve in the near future, we cannot assure you that we would be able to secure additional financing if needed and, if such funds were available, whether the terms or conditions would be acceptable to us. Uncertainty about current global economic conditions could also continue to increase the volatility of our stock price. .

We may not be able to implement our growth strategy successfully. Our growth strategy is based on becoming the leading integrator of fitness and health management services for corporations and other large organizations. The key elements of our strategy are to pursue growth in our Health Management business segment, pursue new customers in our Fitness Management business segment, sell our Fitness Management customers on adopting the services we offer in our integrated Health Management model, and pursue strategic opportunities that provide operational and financial value. Our ability to implement each of these elements depends largely upon our ability to make strategic investments in our Health Management business segment to fund this growth, and the success of those investments. If we do not have sufficient resources to make the necessary investments, or do not successfully make these investments, our growth strategy will be adversely affected and we may not be able to increase our revenues or profitability. Similarly, if we are unable to implement any of the elements of our growth strategy, our growth may be adversely affected.

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We may experience difficulty managing growth, including attracting qualified staff. We have experienced substantial growth during the past few years, both organically and by acquisition. Our ability to grow in the future will depend on a number of factors, including the ability to obtain new customers, expand existing customer relationships, develop additional fitness and health improvement programs and services and hire and train qualified staff. We may experience difficulty in attracting and retaining qualified staff in various markets to meet growth opportunities. Further, in order to attract qualified staff, we may be required to pay higher salaries and enhance benefits in more competitive markets, which may result in a material adverse effect on our results of operation and financial condition. Sustaining growth may require us to sell our services at lower prices to remain competitive, which may result in a material adverse effect on our results of operation and financial condition. There can be no assurance that we will be able to manage expanding operations effectively or that we will be able to maintain or accelerate our growth, and any failure to do so may result in a material adverse effect on our results of operation and financial condition.

We may not be able to successfully cross-sell our health management programs to our fitness management customers. A part of our growth strategy involves continuing and expanding our efforts to sell health management services to our fitness management customers. Our cross-selling efforts may not be successful since our experience indicates that some current customers have different internal departments involved with procuring fitness management services, on the one hand, and health management services, on the other hand. As a result, we may be required to establish new relationships with personnel within our customers, which will limit the potential benefit of established relationships we have developed. We may also be required to overcome different purchasing requirements and standards to the extent they vary within internal departments of our customers. We may experience similar difficulties in cross-selling all of our services to foreign operations of our domestic customers. If we experience significant limitations as a result of the foregoing circumstances, or any other circumstances, we may not be able to increase our revenues or profitability to the extent we anticipate.

The timing of new and lost staffing service contracts may not be indicative of trends in our business or of future quarterly financial results. We evaluate our business, in part, by reviewing trends in our financial performance. We believe an important indicator of our outlook is revenue to be derived from fitness and health management service contracts we secure with customers. Fitness and health management service contracts are often long-term contracts (i.e., 3 to 5 years), automatically renew on an annual basis and generally require 30 to 60 days notice to terminate in order to avoid the automatic renewal provision. Revenue from new contracts often is not recognized for a period of 90 to 180 days after proposal acceptance due to lead times necessary to execute a contract and hire staff to begin providing services. Since termination notice periods are considerably less than the time it takes to begin servicing new contracts, the revenue lost in a reporting period may significantly exceed the revenue gained from new contracts. Because of these timing differences, management generally does not view changes in quarterly revenue, whether sequential or as compared to prior quarter changes, to be indicative of its outlook or trends in our business or to be reflective of revenue expected in succeeding quarters. Rather, management generally evaluates revenue trends in our fitness and health management services business based upon 12 to 18-month periods since we believe this helps to minimize the timing impact from new and terminated contracts. Management cautions investors not to place undue reliance upon fluctuations in quarterly revenue viewed in isolation from revenue information over longer periods of time (e.g., comparative trailing 12-month information), and to not view quarterly revenue as necessarily being indicative of our outlook or results to be expected in future quarters.

We are dependent on maintaining our relationships with third party partners to provide programs and services. Our growth strategy depends in part upon continuous development and improvement of attractive and effective fitness and health management programs and services. Our failure to anticipate trends or to successfully develop, improve or implement such programs or services may have a material adverse effect on our results of operation and financial condition. We currently contract with certain third party partners to provide a portion of such programs and services and anticipate that this will continue to be the case. If any of such third party partners no longer makes these programs and services available to us, there is no assurance that we would be able to replace such third-party partner programs and services, and if we could not do so, our ability to pursue our growth strategies would be seriously compromised.

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Failure to renew existing customer contracts could have a negative effect on our financial condition and results of operations. The majority of our contracts are with large corporations for the management of on-site fitness centers and corporate wellness programs. While the specific terms of such agreements vary, some contracts are subject to early termination by the corporate customer without cause. Although we have a history of consistent contract renewals, there can be no assurance that future renewals will be secured. The early termination or non-renewal of corporate contracts may have a material adverse effect on our results of operation and financial condition.

Our financial results are subject to discretionary spending of our customers. Our revenue, expenses and net income are subject to general economic conditions. A significant portion of our revenue is derived from companies who historically have reduced their expenditures for our services during economic downturns, such as those in the automotive industry. Should the economy continue to weaken, or experience more significant recessionary pressures, corporate customers may reduce or eliminate their expenditures for on-site fitness center management services and our health management services, and prospective and current customers may not commit resources to such services. Adverse economic conditions are currently causing, and are expected to continue to cause, our customers to reduce their workforces and limit the hiring of new employees, in response to which we must reduce the number of staff assigned to manage a customer's fitness center or assigned to manage health management services. These factors may have a material adverse effect on our results of operation and financial condition.

We operate within a highly competitive market against formidable companies. We compete for new and existing corporate customers in a highly fragmented and competitive market. Management believes that our ability to compete successfully depends on a number of factors, including quality and depth of service, locational convenience and cost. The market for on-site fitness center management services is price-sensitive, and the health management market is dominated by competitors that are larger and have more resources and experience. From time to time, our competitors in either or both of the fitness management and health management markets may put us at a disadvantage by proposing a substantially lower price than us. There can be no assurance that we will be able to compete successfully against current and future competitors, or that competitive pressures faced by us will not have a material adverse effect on our results of operation and financial condition.

We have implemented, on a limited basis, a business model for managing corporate fitness centers on a cost-neutral or for-profit basis. We have, on a limited basis, implemented a model of managing corporate fitness centers on a cost-neutral or for-profit basis. In connection with this business model, we have complete responsibility to generate and account for all fitness center revenues, which are recognized as we provide services. From the revenue we recognize and collect, we pay for all expenses to operate the fitness center. We derive our management fee revenue from the profits of the fitness center. The application of this business model may require us to fund operating losses until enough memberships are sold, and other revenue sources are generated in order to achieve profitability. We believe it may be necessary to fund operating losses from this type of business model for up to twenty-four months before the fitness center achieves profitability. Currently, existing contracts representing this business model do not present a material risk or represent a material contribution to our results of operation. However, there is no assurance that the number and scope of such contracts will not become material in the future or that we will be able to manage such centers profitably or to fund losses for these centers until profitability is achieved.

Failure to identify acquisition opportunities may limit our growth. An important part of our growth has been the acquisition of complementary businesses. We may choose to continue this strategy in the future. Management's identification of suitable acquisition candidates involves risks inherent in assessing the value, strengths, weaknesses, overall risks and profitability of acquisition candidates. Management may be unable to identify suitable acquisition candidates. If we do not make suitable acquisitions, we may find it more difficult to realize growth objectives and to enhance shareholder value.

Future acquisitions may be dilutive to shareholders, cause us to incur additional indebtedness and large one-time expenses or create intangible assets that could result in significant amortization expense. If we spend significant funds or incur additional debt, our ability to obtain necessary financing may decline and we may become

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more vulnerable to economic downturns and competitive pressures. Management cannot guarantee that we will be able to successfully complete any future acquisitions, that we will be able to finance acquisitions or that we will realize any anticipated benefits from completed acquisitions.

We may not realize the anticipated benefits of acquisitions we complete. On December 23, 2005, we acquired HealthCalc.Net, Inc. In the future, we may acquire other businesses. The process of integrating new businesses into our operations poses numerous risks, including:

an inability to assimilate acquired operations, information systems and technology platforms, and internal control systems and products;

diversion of management's attention;

difficulties and uncertainties in transitioning business relationships from the acquired entity to us; and

the loss of key employees of acquired companies.

If we are unsuccessful in integrating other future acquisitions into our operations, we might not realize all of the anticipated benefits of such acquisitions. In such instances, our acquisitions might not be accretive to our earnings, the costs of such acquisitions may otherwise outweigh the benefits and the market price of our common stock might decline.

The loss of any of our key employees could have a material adverse effect on our performance and results of operations. Our success is highly dependent on the efforts, abilities and continued services of our executive officers, including Gregg Lehman, Ph.D., our President and Chief Executive Officer, Wesley Winnekins, our Chief Financial Officer, and other key employees. The loss of any of the executive officers or key employees may have a material adverse effect on our results of operation and financial condition. We also believe that our future success will depend on our ability to attract, motivate and retain highly-skilled corporate, regional and site-based personnel. Although historically we have been successful in retaining the services of our senior management, there can be no assurance that we will be able to do so in the future.

Our results of operations could be adversely impacted by litigation. Because of the nature of our business, we may be subject to claims and litigation alleging negligence or other grounds for liability arising from injuries or other harm alleged by our clients' employees. We have occasionally been named a defendant in claims relating to accidents that occurred in the fitness centers we manage. There can be no assurance that additional claims will not be filed, and that our insurance will be adequate to cover liabilities resulting from any claim.

The indemnification provisions in our management agreements with customers may obligate us to pay claims that arise from our acts or omissions. A majority of our management agreements include a provision that obligates us to indemnify and hold harmless the customer and their employees, officers and directors from any and all claims, actions and/or suits (including attorneys' fees) arising directly or indirectly from any act or omission of the Company or its employees, officers or directors in connection with the operation of our business. A majority of these management contracts also include a provision that obligates the customer to indemnify and hold us harmless against all liabilities arising out of the acts or omissions of the customer, their employees and agents. We can make no assurance that claims by our customers, or their employees, officers or directors, will not be made in the course of operating our business.

Our insurance policies may not provide adequate coverage. We maintain the following types of insurance policies: commercial general liability, professional liability, automobile liability, cyber liability, commercial property, employee dishonesty, employment practices, directors and officers liability, workers compensation and excess umbrella liability. The policies provide for a variety of coverages and are subject to various limitations, exclusions and deductibles. While we believe our insurance policies are sufficient in amount and coverage for our current operations, there can be no assurance that coverage will continue to be available in adequate amounts or at a

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reasonable cost, and there can be no assurance that the insurance proceeds, if any, will cover the full extent of loss resulting from any claims.

We could experience a potential depressive effect on the price of our common stock following the exercise and sale of existing convertible securities. At December 31, 2008, the Company had outstanding stock options and warrants to purchase an aggregate of 1,902,766 shares of common stock. The exercise of such outstanding stock options and warrants, and the sale of the common stock acquired thereby, may have a material adverse effect on the price of our common stock. In addition, the exercise of such outstanding stock options and warrants and sale of such shares of our common stock could occur at a time when we might otherwise be able to obtain additional equity capital on terms and conditions more favorable to us.

Our common stock is thinly traded, and subject to volatility. Our common stock is relatively illiquid, or thinly traded, which can enhance volatility in the share price and make it difficult for investors to buy or sell our common shares without dramatically affecting the quoted price or they may be unable to sell a position at a later date. If limited trading in our stock continues, it may be difficult for investors to sell their shares in the public market at any given time at prevailing prices.

Further declines in our stock price could trigger an impairment of goodwill. The financial markets turmoil appears to be impacting common stock trading prices for nearly all public companies including ours. Our market capitalization dropped below our stockholders' equity during the fourth quarter of 2008 for the first time in recent periods. If we continue to experience profitable operations resulting in increased shareholders' equity value, and if our market price per share does not increase accordingly, it is possible this may trigger an impairment of goodwill in future periods. In addition, our earnings might not maintain or increase at the rate the market expects, or in parity with our competition, which could contribute to a decline in our share price when compared to others in our industry. As a result of these and other factors, we could experience partial or complete goodwill impairment in one or both of our segments or our company as a whole. We have approximately \$14,500,000 of goodwill.

ITEM 1B. UNRESOLVED STAFF COMMENTS

None.

ITEM 2. PROPERTIES

We lease approximately 28,000 square feet of commercial office space for our corporate headquarters in Bloomington, Minnesota, mostly under a lease that expires in December 2012. Our monthly base rent for this office space is approximately \$32,000, plus taxes, insurance and other related operating costs. We also assumed a lease in connection with our 2005 acquisition of HealthCalc for approximately 8,200 square feet of office space in Dallas, Texas, which expires in December 2012. Our minimum monthly base rent for this space is approximately \$15,000.

ITEM 3. LEGAL PROCEEDINGS

We are not currently involved in any material pending legal proceedings. We are, from time to time, subject to claims and suits arising in the ordinary course of business. Such claims have, in the past, generally been covered by insurance. Management believes the resolution of other legal matters will not have a material effect on our financial condition or results of operation, although no assurance can be given with respect to the ultimate outcome of any such actions. Furthermore, there can be no assurance that our insurance will be adequate to cover all liabilities that may arise out of claims brought against us.

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

None.

Table of Contents**EXECUTIVE OFFICERS OF THE REGISTRANT.**

The information required by Item 10 relating to directors, our code of ethics, procedures for shareholder recommendations of director nominees, the audit committee and compliance with Section 16 of the Exchange Act is incorporated herein by reference to the sections entitled Election of Directors , Corporate Governance and Section 16(a) Beneficial Ownership Reporting Compliance, which appear in the Company s definitive proxy statement for its 2009 Annual Meeting.

The names, ages and positions of our executive officers are as follows:

| Name | Age | Position |
|-------------------------|-----|--|
| Gregg O. Lehman, Ph.D. | 61 | President, Chief Executive Officer and Director |
| John E. Griffin | 52 | Chief Operations Officer |
| Wesley W. Winnekins | 47 | Chief Financial Officer and Treasurer |
| Jeanne C. Crawford | 51 | Chief Human Resources Officer and Secretary |
| David T. Hurt | 43 | Vice President Account Services |
| Katherine M. Meacham | 42 | Vice President Account Services |
| Brian J. Gagne | 46 | Senior Vice President-Account Management |
| John F. Ellis | 49 | Chief Information Officer |
| J. Mark McConnell | 44 | Senior Vice President Business and Corporate Development |
| James O. Reynolds, M.D. | 61 | Chief Medical Officer |

Gregg O. Lehman, Ph.D. has been the President and Chief Executive Officer of the Company since January 1, 2007. From March 2006 through December 2006 Mr. Lehman served as Chairman, President and Chief Executive Officer of INSPIRIS Inc., a Nashville-based specialty care management company that provides care to frail Medicare Advantage members in long-term care facilities. From 2003 to 2006, Mr. Lehman was President and Chief Executive Officer of Gordian Health Solutions, Inc., a Nashville company dedicated to improving the health of employees and dependents for employers and health plans. From 1998 to 2003, Mr. Lehman served as President and Chief Executive Officer of the National Business Coalition on Health, a Washington D.C.-based movement of ninety employer-led coalitions seeking better quality and more cost-effective healthcare for employees. Mr. Lehman, who has a Ph.D. and an M.S. from Purdue University in Higher Education Administration, has been a director of the Company since September 22, 2006.

John E. Griffin has been the Company s Chief Operations Officer since February 1, 2008. Mr. Griffin is responsible for overseeing the Company s information technology, account services functions and operations, excluding sales and marketing, finance, human resources and research, development and outcomes. Mr. Griffin has served as President of The Meridian Group, a consulting company he founded that focused on health case financial forecasting, budgeting, strategic planning and operational management, since August 2006 and from September 1995 to April 2003. From July 2007 through January 31, 2008, the Company engaged Mr. Griffin as an operations consultant. From April 2003 to July 2006, Mr. Griffin served as Chief Operating Officer of Gordian Health Solutions, Inc. Mr. Griffin has also served as Chief Operating Officer of eClickMD, Inc. and Computer Sentry Software, Inc. Mr. Griffin holds a Doctor of Jurisprudence from the University of Tennessee College of Law and a Bachelor of Science in Business Administration with a major in accounting. He is a member of the Health Law Section of the Tennessee Bar Association.

Wesley W. Winnekins has been Chief Financial Officer and Treasurer of the Company since February 2001. Prior to joining the Company, Mr. Winnekins served as CFO (from January 2000 to February 2001) of University.com, Inc., a privately held provider of online learning solutions for corporations. From June 1995 to April 1999 he served as CFO and vice president of operations for Reality Interactive, a publicly held developer of CD-ROMs and online training for the corporate market. From June 1993 to May 1995 he served as controller and director of operations for The Marsh, a Minneapolis-based health club, and was controller of the Greenwood Athletic Club in Denver from October 1987 to January 1989. From May 1985 to October 1987, he served in the audit practice at

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Arthur Andersen. Mr. Winnekins received a Bachelor's in Business Administration with a major in Accounting from Iowa State University. He has passed the CPA exam.

Jeanne C. Crawford has been the Company's Chief Human Resources Officer (formerly titled Vice President - Human Resources) since July 1998 and Secretary of the Company since February 2001. From July 1996 through July 1998, Ms. Crawford served as a Human Resource consultant to the Company. From October 1991 through September 1993, Ms. Crawford served as Vice President of Human Resources for RehabClinics, Inc. a publicly held outpatient rehabilitation company. From May 1989 through October 1991, Ms. Crawford served as Director of Human Resources for Greater Atlantic Health Service, an HMO and physicians medical group. From 1979 through 1989, Ms. Crawford served in various human resources management positions in both the retail and publishing industries. Ms. Crawford graduated cum laude from Temple University with a bachelor's degree in business administration, and is a member of the Society for Human Resources Management.

David T. Hurt has served as Vice President Account Services-Fitness Management, where he is responsible for the operation of accounts within the Company's Fitness Management business segment, since April 2001. He directs the overall development and management of Corporate, Hospital, Community and University fitness center operations. Mr. Hurt has been active in the industry for more than 16 years. His experience in health and fitness management began in 1988 with the Valley Wellness Center in Harrisonburg, Virginia. In recent years, he has been involved in the successful development and management of several start-up fitness center projects ranging in size from 45,000 to 150,000 square feet. Mr. Hurt is a graduate of James Madison University, where he received a bachelor's degree in sports management.

Katherine M. Meacham was appointed as the Company's Vice President Account Services-Health Management, in March 2005. In this role, she directs the implementation and management of the Company's Health Management accounts. From December 2003 to March 2005, she served as the Company's Vice President of Marketing. Previously, Ms. Meacham spent 15 years with the Health & Fitness Division of Johnson & Johnson Health Care Systems Inc., a subsidiary of Johnson & Johnson, a business acquired by the Company. Ms. Meacham was the Director of Marketing Services and National Sales leading business expansion in the United States and internationally, while exploring new markets. Ms. Meacham serves on the board for International Council on Active Aging (ICAA). She is a member of the Alliance for Work Life Progress (AWLP), National Business Group on Health (NBGH), American Marketing Association (AMA) and Wellness Councils of America (WELCOA). Ms. Meacham has a bachelor's degree in business with an emphasis in exercise science and sports management from the University of Tennessee and a Master of Business Administration from East Tennessee State University. Additionally, Ms. Meacham has completed advanced studies in organizational theory from Pepperdine University.

Brian J. Gagne has served as the Company's Senior Vice President, Account Management since January 2008 and served as the National Vice President, Health Management from August 2006 to December 2007, and as Vice President, of Programs and Partnerships from December 2003 to August 2006. In his current role, Mr. Gagne oversees the account services team, delivery of health coaching, worksite screenings, customer/technical support and fulfillment services. Mr. Gagne brings more than 21 years of health, fitness and wellness management experience in the corporate, commercial and medical fitness markets. Mr. Gagne joined the Company after the acquisition of the Johnson & Johnson Health Care Systems in December 2003. Prior to HealthFitness, he was the Director, Integrated Behavioral Solutions and was responsible for leading a team of health professionals to develop and deliver patient education programs and tools for the Johnson & Johnson Family of Companies. Prior to his work with Johnson & Johnson, Mr. Gagne served as Executive Director of several medical fitness centers in the Chicago area. Mr. Gagne has a master's degree in exercise physiology and a bachelor's degree in exercise science from the University of Illinois-Chicago.

John F. Ellis has served as the Company's Chief Information Officer since December 2005. Mr. Ellis is formerly a Founder and Chief Executive Officer of HealthCalc.Net, Inc., a company we acquired in December 2005. From January 1995 to August 1999, Mr. Ellis held a position of Senior Specialist with Perot Systems, an information technology consulting group. From November 1989 to January 1995, Mr. Ellis held a position of Vice President of Information Technology at People Karch International, a health and fitness software development services firm. Mr. Ellis holds a B.S. in Physical Education from The Citadel.

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J. Mark McConnell serves as the Company's Senior Vice President Business Development. Mr. McConnell joined the Company in December 2008 and provides leadership to all aspects of the Company's business and corporate development activities, including identifying global sales opportunities for the company's health and productivity solutions as well as working on the development of new client-driven services. From September 2003 to November 2008, he served as senior vice president of the Employer Solutions Group for Healthways. Prior to Healthways, he was the health plan manager of health care initiatives with Kaiser Permanente from September 2001 to September 2003, where he worked in conjunction with General Motors Corp. Mark has a Master of Business Administration from the State University of New York at Buffalo and a Bachelor of Arts in psychology from Muskingum College.

James O. Reynolds, M.D., has been the Company's Chief Medical Officer since February 1, 2008. Dr. Reynolds has oversight of all clinical aspects of the Company's programs and services and the Company's Research, Development and Outcomes division. Dr. Reynolds served from October 2005 to January 2008 as Principal and Senior Healthcare Consultant for Mercer Human Resource Consulting, a global provider of consulting, outsourcing and investment services, where he served as a senior clinical consultant on Mercer's Health and Productivity Management specialty practice. From September 2003 to October 2005, Dr. Reynolds served as Vice President and Medical Director, Integrated Care Solutions, for CorSolutions Medical, Inc., a provider of disease management and related services to employers, health plans and government-sponsored healthcare programs that was acquired by Matria Healthcare, Inc. in 2005. From January 2001 to September 2003, Dr. Reynolds served as Co-Founder, Chief Operating Officer and Executive Vice President of Health and Productivity Corporation of America, which was acquired by CorSolutions in 2003. Prior to these positions, Dr. Reynolds served in various positions in the healthcare industry, was in private practice as an internal medicine physician, and served as an Associate Professor of Medicine at the University of Missouri Hospital and Clinics. Dr. Reynolds has Bachelor's of Science from Drury College, an M.D. degree from the University of Missouri and is board certified in internal medicine. He is an active member of the American College of Physicians, American Medical Association, and the American College of Environmental and Occupational Medicine.

Table of Contents**PART II****ITEM 5. MARKET FOR REGISTRANT'S COMMON EQUITY, RELATED STOCKHOLDER MATTERS AND ISSUER PURCHASES OF EQUITY SECURITIES**

Trading of the Company's common stock is conducted on the NYSE Alternext US under the symbol FIT. Prior to October 22, 2008, trading of the Company's common stock was conducted in the over-the-counter markets (often referred to as pink sheets) or on the OTC Bulletin Board under the symbol HFIT.

The following table sets forth, for the periods indicated, the range of low and high sale prices for the Company's common stock as reported by the NYSE Alternext US, effective October 22, 2008, and the low and high bid prices, as reported by the OTC Bulletin Board, prior to October 22, 2008. Historical prices have been adjusted for the one-for-two reverse stock split completed on October 6, 2008.

| Fiscal Year 2008: | Low | High |
|-------------------|--------|--------|
| Fourth quarter | \$2.00 | \$3.10 |
| Third quarter | 2.22 | 3.60 |
| Second quarter | 3.22 | 4.80 |
| First quarter | 3.90 | 5.40 |