NAUTILUS, INC.
Form 10-Q
May 08, 2014

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

FORM 10-Q

(Mark One)
[x] QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the quarterly period ended March 31, 2014
or
[ ] TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the transition period from to

Commission file number: 001-31321

NAUTILUS, INC.
(Exact name of Registrant as specified in its charter)

| | |
|---|---|
| Washington | 94-3002667 |
| (State or other jurisdiction of incorporation or organization) | (I.R.S. Employer Identification No.) |

17750 S.E. 6th Way
Vancouver, Washington 98683
(Address of principal executive offices, including zip code)
(360) 859-2900
(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 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 [x] No [ ]
Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes [x] No [ ]
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 definition of “large accelerated filer,” “accelerated filer” and “smaller reporting company” in Rule 12b-2 of the Exchange Act:

Large accelerated filer [ ] Accelerated filer [x] 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 Exchange Act). Yes [ ] No [x]

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date:

The number of shares outstanding of the registrant's common stock as of April 30, 2014 was 31,188,133 shares.

NAUTILUS, INC.
FORM 10-Q
FOR THE QUARTERLY PERIOD ENDED MARCH 31, 2014


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PART I. FINANCIAL INFORMATION

Item 1. Financial Statements

NAUTILUS, INC.
CONDENSED CONSOLIDATED BALANCE SHEETS
(Unaudited and in thousands)

| | As of March 31, 2014 | December 31, 2013 |
|---|---|---|
| Assets | | |
| Cash and cash equivalents | $42,035 | $40,979 |
| Marketable securities, current | 12,512 | — |
| Trade receivables, net of allowances of $38 and $53 | 13,394 | 25,336 |
| Inventories | 13,462 | 15,824 |
| Prepaids and other current assets | 4,389 | 6,927 |
| Income taxes receivable | 31 | 80 |
| Deferred income tax assets | 5,237 | 4,441 |
| Total current assets | 91,060 | 93,587 |
| | | |
| Marketable securities, long-term | 1,006 | — |
| Property, plant and equipment, net | 8,670 | 8,499 |
| Goodwill | 2,649 | 2,740 |
| Other intangible assets, net | 12,105 | 12,615 |
| Long-term deferred income tax assets | 22,333 | 25,725 |
| Other assets | 307 | 401 |
| Total assets | $138,130 | $143,567 |
| | | |
| Liabilities and Shareholders' Equity | | |
| Trade payables | $27,320 | $37,192 |
| Accrued liabilities | 7,836 | 9,123 |
| Warranty obligations, current portion | 1,983 | 1,610 |
| Total current liabilities | 37,139 | 47,925 |
| Warranty obligations, non-current | — | 28 |
| Income taxes payable, non-current | 2,664 | 2,577 |
| Other long-term liabilities | 1,359 | 1,472 |
| Total liabilities | 41,162 | 52,002 |
| Commitments and contingencies (Note 12) | | |
| Shareholders' equity: | | |
| Common stock - no par value, 75,000 shares authorized, 31,188 and 31,162 shares issued and outstanding | 6,975 | 6,769 |
| Retained earnings | 89,926 | 84,552 |
| Accumulated other comprehensive income | 67 | 244 |
| Total shareholders' equity | 96,968 | 91,565 |
| Total liabilities and shareholders' equity | $138,130 | $143,567 |

See accompanying Notes to Condensed Consolidated Financial Statements.

NAUTILUS, INC.
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS
(Unaudited and in thousands, except per share amounts)

| | Three months ended March 31, | |
|---|---|---|
| | 2014 | 2013 |
| Net sales | $71,903 | $59,214 |
| Cost of sales | 33,422 | 28,520 |
| Gross profit | 38,481 | 30,694 |
| Operating expenses: | | |
| Selling and marketing | 21,774 | 18,626 |
| General and administrative | 5,803 | 4,947 |
| Research and development | 1,903 | 1,127 |
| Total operating expenses | 29,480 | 24,700 |
| Operating income | 9,001 | 5,994 |
| Other income (expense): | | |
| Interest income | 8 | 1 |
| Interest expense | (7) | (9) |
| Other | (61) | (109) |
| Total other income (expense) | (60) | (117) |
| Income from continuing operations before income taxes | 8,941 | 5,877 |
| Income tax provision | 3,193 | 353 |
| Income from continuing operations | 5,748 | 5,524 |
| Discontinued operations: | | |
| Loss from discontinued operations before income taxes | (512) | (374) |
| Income tax benefit from discontinued operations | (138) | (9) |
| Loss from discontinued operations | (374) | (365) |
| Net income | $5,374 | $5,159 |
| | | |
| Basic income per share from continuing operations | $0.18 | $0.18 |
| Basic loss per share from discontinued operations | (0.01) | (0.01) |
| Basic net income per share | $0.17 | $0.17 |
| | | |
| Diluted income per share from continuing operations | $0.18 | $0.18 |
| Diluted loss per share from discontinued operations | (0.01) | (0.01) |
| Diluted net income per share | $0.17 | $0.17 |
| Shares used in per share calculations: | | |
| Basic | 31,172 | 30,947 |
| Diluted | 31,550 | 31,264 |

See accompanying Notes to Condensed Consolidated Financial Statements.

NAUTILUS, INC.
CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME
(Unaudited and in thousands)

| | Three months ended March 31, | |
|---|---|---|
| | 2014 | 2013 |
| Net income | $5,374 | $5,159 |
| Other comprehensive income (loss): | | |
| Unrealized loss on marketable securities, net of income tax expense of $0 and $0 | (13) | — |
| Foreign currency translation, net of income tax expense of $5 and $8 | (164) | (147) |
| Comprehensive income | $5,197 | $5,012 |

See accompanying Notes to Condensed Consolidated Financial Statements.

NAUTILUS, INC.
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(Unaudited and in thousands)

| | Three months ended March 31, | |
|---|---|---|
| | 2014 | 2013 |
| Cash flows from operating activities: | | |
| Income from continuing operations | $5,748 | $5,524 |
| Loss from discontinued operations | (374) | (365) |
| Net income | 5,374 | 5,159 |
| Adjustments to reconcile net income to cash provided by operating activities: | | |
| Depreciation and amortization | 865 | 818 |
| Bad debt expense | 30 | 169 |
| Inventory lower-of-cost-or-market adjustments | 589 | — |
| Stock-based compensation expense | 265 | 214 |
| Loss on asset dispositions | 1 | 14 |
| Deferred income taxes, net of valuation allowance | 2,321 | 257 |
| Excess tax deficiency related to stock-based awards | 102 | — |
| Changes in operating assets and liabilities: | | |
| Trade receivables, net | 11,752 | 9,280 |
| Inventories | 1,765 | 5,130 |
| Prepaids and other current assets | 2,617 | 1,498 |
| Income taxes payable | 356 | (105) |
| Trade payables | (9,830) | (14,968) |
| Accrued liabilities, including warranty obligations | (1,085) | (1,431) |
| Net cash provided by operating activities | 15,122 | 6,035 |
| | | |
| Cash flows from investing activities: | | |
| Purchase of marketable securities | (13,518) | — |
| Proceeds from sale of assets of discontinued operations | — | 96 |
| Purchases of property, plant and equipment | (521) | (762) |
| Net cash used in investing activities | (14,039) | (666) |
| | | |
| Cash flows from financing activities: | | |
| Proceeds from exercise of stock options | 42 | 147 |
| Excess tax deficiency related to stock-based awards | (102) | — |
| Net cash provided by (used in) financing activities | (60) | 147 |
| | | |
| Effect of exchange rate changes on cash and cash equivalents | 33 | (43) |
| Increase in cash and cash equivalents | 1,056 | 5,473 |
| Cash and cash equivalents: | | |
| Beginning of period | 40,979 | 23,207 |
| End of period | $42,035 | $28,680 |
| Supplemental disclosure of cash flow information: | | |
| Cash paid for interest | $7 | $10 |
| Cash paid for income taxes, net | 95 | 109 |

See accompanying Notes to Condensed Consolidated Financial Statements.

NAUTILUS, INC.
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)
(1) GENERAL INFORMATION

Basis of Consolidation and Presentation

The accompanying condensed consolidated financial statements present the financial position, results of operations and cash flows of Nautilus, Inc. and its subsidiaries, all of which are wholly owned. Intercompany transactions and balances have been eliminated in consolidation.

The accompanying condensed consolidated financial statements have not been audited. We have condensed or omitted certain information and footnote disclosures normally included in financial statements presented in accordance with accounting principles generally accepted in the United States of America (“U.S. GAAP”). Management believes the disclosures contained herein are adequate to make the information presented not misleading. However, these condensed consolidated financial statements should be read in conjunction with our consolidated financial statements and notes thereto included in our Annual Report on Form 10-K for the year ended December 31, 2013 (the “2013 Form 10-K”).

The preparation of financial statements in conformity with U.S. GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities as of the date of the financial statements and the reported amounts of revenue and expenses during the reporting period. Actual results could differ from those estimates. Further information regarding significant estimates can be found in our 2013 Form 10-K.

In the opinion of management, the accompanying condensed consolidated financial statements reflect all adjustments necessary to present fairly our financial position as of March 31, 2014 and December 31, 2013 and our results of operations, comprehensive income and cash flows for the three months ended March 31, 2014 and 2013. Interim results are not necessarily indicative of results for a full year. Our revenues typically vary seasonally and this seasonality can have a significant effect on operating results, inventory levels and working capital needs.

Unless indicated otherwise, all information regarding our operating results pertain to our continuing operations.

New Accounting Pronouncements

ASU 2014-08
In April 2014, the Financial Accounting Standards Board ("FASB") issued Accounting Standards Update ("ASU") No. 2014-08, "Presentation of Financial Statements (Topic 205) and Property, Plant, and Equipment (Topic 360) and Reporting Discontinued Operations and Disclosures of Disposals of Components of an Entity." ASU 2014-08 amends the definition for what types of asset disposals are to be considered discontinued operations, and amends the required disclosures for discontinued operations and assets held for sale. ASU 2014-08 also enhances the convergence of the FASB’s and the International Accounting Standard Board’s reporting requirements for discontinued operations. ASU 2014-08 is effective for annual periods beginning on or after December
15, 2014, and interim periods within annual periods beginning on or after December 15, 2015. We do not expect the adoption of ASU 2014-08 to have a material effect on our financial position, results of operations or cash flows.

ASU 2013-11
In July 2013, the FASB issued ASU No. 2013-11, “Presentation of an Unrecognized Tax Benefit When a Net Operating Loss Carryforward, a Similar Tax Loss, or a Tax Credit Carryforward Exists.” ASU 2013-11 amends the guidance related to the presentation of unrecognized tax benefits and allows for the reduction of a deferred tax asset for a net operating loss (“NOL”) carryforward whenever the NOL or tax credit carryforward would be available to

reduce the additional taxable income or tax due if the tax position is disallowed. ASU 2013-11 is effective for annual and interim periods for fiscal years beginning after December 15, 2013. Since ASU 2013-11 relates only to the presentation of unrecognized tax benefits, our adoption of ASU 2013-11 in January 2014 did not have a material effect on our financial position, results of operations or cash flows.

(2) DISCONTINUED OPERATIONS

On September 25, 2009, in light of continuing operating losses in our Commercial business and in order to focus exclusively on managing our Direct and Retail businesses, we committed to a plan for the complete divestiture of our Commercial business, which qualified for held-for-sale accounting treatment. The Commercial business is presented as Discontinued Operations in our Condensed Consolidated Statements of Operations for all periods.

The disposal of the Commercial business assets was completed in April 2011. We reached substantial completion of asset liquidation at December 2012. However, we continue to have legal and accounting expenses as we work with authorities on final deregistration of certain European entities and product liability expenses associated with product previously sold into the Commercial channel. There was no revenue related to the Commercial business for the year ended December 31, 2013 or the three-month period ended March 31, 2014.

The following table summarizes liabilities for exit costs related to discontinued operations, included in Accrued Liabilities and Other Long-Term Liabilities in our Condensed Consolidated Balance Sheets (in thousands):

| | Facilities Leases |
|---|---|
| Balance, December 31, 2013 | $831 |
| Adjustments | — |
| Payments | (63) |
| Balance, March 31, 2014 | $768 |

We expect the lease obligations to be paid out through 2016.

(3) MARKETABLE SECURITIES

We classify our marketable securities as available-for-sale and, accordingly, record them at fair value. Unrealized holding gains and losses are excluded from earnings and are reported net of tax in other comprehensive income until realized. Dividend and interest income is recognized when earned. Realized gains and losses are included in earnings and are derived using the specific identification method for determining the cost of securities sold.

We periodically evaluate whether declines in fair values of our investments below their cost are "other-than-temporary." This evaluation consists of qualitative and quantitative factors regarding the severity and duration of the unrealized loss, as well as our ability and intent to hold the investment until a forecasted recovery occurs.

(4) INVENTORIES

Inventories consisted of the following (in thousands):

| | As of | |
|---|---|---|
| | March 31, 2014 | December 31, 2013 |
| Finished goods | $12,246 | $14,259 |
| Parts and components | 1,216 | 1,565 |
| Total inventories | $13,462 | $15,824 |

(5) PROPERTY, PLANT AND EQUIPMENT

Property, plant and equipment consisted of the following (in thousands):

| | Estimated Useful Life (in years) | As of March 31, 2014 | December 31, 2013 |
|---|---|---|---|
| Leasehold improvements | 5 to 20 | $2,850 | $2,869 |
| Computer equipment | 3 to 5 | 35,519 | 35,554 |
| Machinery and equipment | 3 to 5 | 5,755 | 5,648 |
| Furniture and fixtures | 5 | 700 | 688 |
| Work in progress [1] | N/A | 4,630 | 4,281 |
| Total cost | | 49,454 | 49,040 |
| Accumulated depreciation | | (40,784) | (40,541) |
| Total property, plant and equipment, net | | $8,670 | $8,499 |

[1] Work in progress includes internal use software development and production tooling construction in progress.

(6) GOODWILL AND OTHER INTANGIBLE ASSETS

Goodwill

All goodwill is assigned to our Direct reporting segment. The rollforward of goodwill was as follows (in thousands):

| | |
|---|---|
| Balance, January 1, 2013 | $2,940 |
| Currency exchange rate adjustment | (200) |
| Balance, December 31, 2013 | 2,740 |
| Currency exchange rate adjustment | (91) |
| Balance, March 31, 2014 | $2,649 |

Other Intangible Assets

Other intangible assets consisted of the following (in thousands):

| | Estimated Useful Life (in years) | As of March 31, 2014 | December 31, 2013 |
|---|---|---|---|
| Other intangible assets: | | | |
| Indefinite-lived trademarks | N/A | $9,052 | $9,052 |
| Patents | 8 to 16 | 18,154 | 18,154 |
| | | 27,206 | 27,206 |
| Accumulated amortization - patents | | (15,101) | (14,591) |
| | | $12,105 | $12,615 |

Amortization expense was as follows (in thousands):

| | Three months ended March 31, | |
|---|---|---|
| | 2014 | 2013 |
| Patent amortization | $510 | $513 |

Future amortization of patents is as follows (in thousands):

| | |
|---|---|
| Remainder of 2014 | $1,530 |
| 2015 | 828 |
| 2016 | 430 |
| 2017 | 143 |
| 2018 | 65 |
| Thereafter | 57 |

$3,053

(7) ACCRUED LIABILITIES

Accrued liabilities consisted of the following (in thousands):

| | As of | |
|---|---|---|
| | March 31, 2014 | December 31, 2013 |
| Payroll and related liabilities | $3,257 | $4,244 |
| Other | 4,579 | 4,879 |
| Total accrued liabilities | $7,836 | $9,123 |

(8) FAIR VALUE MEASUREMENTS

Factors used in determining the fair value of financial assets and liabilities are summarized into three broad categories:

- Level 1 - observable inputs such as quoted prices (unadjusted) in active markets for identical securities as of the reporting date;
- Level 2 - other significant directly or indirectly observable inputs, including quoted prices for similar securities, interest rates, prepayment speeds and credit risk; or observable market prices in markets with insufficient volume and/or infrequent transactions; and
- Level 3 - significant inputs that are generally unobservable inputs for which there is little or no market data available, including our own assumptions in determining fair value.

Assets measured at fair value on a recurring basis were as follows (in thousands):

| | March 31, 2014 | | | |
|---|---|---|---|---|
| | Level 1 | Level 2 | Level 3 | Total |
| Cash Equivalents | | | | |
| Money market funds | $27,975 | $— | $— | $27,975 |
| | | | | |
| Available for Sale Securities | | | | |
| Corporate bonds | — | 5,352 | — | 5,352 |
| Commercial paper | — | 4,495 | — | 4,495 |
| Certificates of deposit | — | 3,671 | — | 3,671 |
| | — | 13,518 | — | 13,518 |
| | $27,975 | $13,518 | $— | $41,493 |

The company recognizes transfers between levels at the actual date of the event or change in circumstance that caused the transfer. There were no transfers between levels during the first quarter of 2014.

We classify our marketable securities as available-for-sale and, accordingly, record them at fair value based on quoted market prices. The factors or methodology used for valuing securities are not necessarily an indication of the risk associated with investing in those securities. Unrealized holding gains and losses are excluded from earnings and are reported net of tax in other comprehensive income until realized. During the first quarter of 2014 and 2013, we did not record any other-than-temporary impairments on our financial assets required to be measured at fair value on a nonrecurring basis.

We recognize or disclose the fair value of certain assets, such as non-financial assets, primarily long-lived assets, goodwill, intangible assets and certain other assets in connection with impairment evaluations. All of our nonrecurring valuations use significant unobservable inputs and therefore fall under Level 3 of the fair value hierarchy. We did not perform any valuations on assets or liabilities that are valued at fair value on a nonrecurring basis during the first

quarter of 2014 or the last quarter of 2013 except for the Goodwill impairment evaluation that was prepared effective October 1, 2013.

The carrying value of Cash and Cash Equivalents, Trade Receivables, Prepaids and Other Current Assets, Trade Payables and Accrued Liabilities approximates their fair values due to the short-term nature of their maturities.

(9) PRODUCT WARRANTIES

Our products carry limited, defined warranties for defects in materials or workmanship which, according to their terms, generally obligate us to pay the costs of supplying and shipping replacement parts to customers and, in certain instances, pay for labor and other costs to service products. Outstanding product warranty periods range from sixty days to, in limited circumstances, the lifetime of certain product components. We record a liability at the time of sale for the estimated costs of fulfilling future warranty claims. If necessary, we adjust the liability for specific warranty-related matters when they become known and are reasonably estimable. Estimated warranty expense is included in Cost of Sales, based on historical warranty claim experience and available product quality data. Warranty expense is affected by the performance of new products, significant manufacturing or design defects not discovered until after the product is delivered to the customer, product failure rates, and higher or lower than expected repair costs. If warranty expense differs from previous estimates, or if circumstances change such that the assumptions inherent in previous estimates are no longer valid, the amount of product warranty obligations is adjusted accordingly.

Changes in our product warranty obligations were as follows (in thousands):

| | Three months ended March 31, | |
|---|---|---|
| | 2014 | 2013 |
| Balance, beginning of period | $1,638 | $2,492 |
| Accruals | 921 | 653 |
| Adjustments | — | — |
| Payments | (576) | (535) |
| Balance, end of period | $1,983 | $2,610 |

(10) INCOME PER SHARE

Basic per share amounts were computed using the weighted average number of common shares outstanding. Diluted per share amounts were calculated using the number of basic weighted average shares outstanding increased by dilutive potential common shares related to stock-based awards, as determined by the treasury stock method. The weighted average numbers of shares outstanding used to compute income per share were as follows (in thousands):

| | Three months ended March 31, | |
|---|---|---|
| | 2014 | 2013 |
| Shares used to calculate basic income per share | 31,172 | 30,947 |
| Dilutive effect of outstanding options, performance stock units and restricted stock units | 378 | 317 |
| Shares used to calculate diluted income per share | 31,550 | 31,264 |

The weighted average numbers of shares outstanding listed in the table below were anti-dilutive and excluded from the computation of diluted income per share, primarily because the average market price did not exceed the exercise price. These shares may be dilutive potential common shares in the future (in thousands):

| | Three months ended March 31, | |
|---|---|---|
| | 2014 | 2013 |
| Stock options | 320 | 340 |
| Performance stock units | 84 | 125 |

(11) SEGMENT AND ENTERPRISE-WIDE INFORMATION

We have two reportable segments - Direct and Retail. Contribution is the measure of profit or loss, defined as net sales less product costs and directly attributable expenses. Directly attributable expenses include Selling and Marketing expenses, General and Administrative expenses, and Research and Development expenses that are directly related to segment operations. Segment assets are those directly assigned to an operating segment's operations, primarily Accounts Receivable, Inventories and Intangible Assets. Unallocated assets primarily include shared information technology infrastructure, distribution centers, corporate headquarters, Prepaids and Other Current Assets, Deferred Income Tax Assets and Other Assets. Capital expenditures directly attributable to the Direct and Retail segments were not significant in any period.

Following is summary information by reportable segment (in thousands):

| | Three months ended March 31, | |
|---|---|---|
| | 2014 | 2013 |
| Net sales: | | |
| Direct | $50,735 | $42,635 |
| Retail | 20,103 | 15,134 |
| Unallocated royalty income | 1,065 | 1,445 |
| Consolidated net sales | $71,903 | $59,214 |
| Contribution: | | |
| Direct | $10,352 | $6,708 |
| Retail | 2,509 | 1,960 |
| Unallocated royalty income | 1,065 | 1,445 |
| Consolidated contribution | $13,926 | $10,113 |
| | | |
| Reconciliation of consolidated contribution to income from continuing operations: | | |
| Consolidated contribution | $13,926 | $10,113 |
| Amounts not directly related to segments: | | |
| Operating expenses | (4,925) | (4,120) |
| Other expense, net | (60) | (116) |
| Income tax expense | (3,193) | (353) |
| Income from continuing operations | $5,748 | $5,524 |

There was no material change in the allocation of assets by segment during the first three months of 2014 and, accordingly, assets by segment are not presented.

No customer represented 10.0% or more of our total Net Sales in the three months ended March 31, 2014 or 2013.

(12) COMMITMENTS AND CONTINGENCIES

Guarantees, Commitments and Off-Balance Sheet Arrangements
As of March 31, 2014, we had approximately $0.4 million in standby letters of credit with certain vendors with expiration dates through August 2014.

We have long lead times for inventory purchases and, therefore, must secure factory capacity from our vendors in advance. As of March 31, 2014, we had approximately $5.7 million in non-cancelable market-based purchase obligations, primarily for inventory purchases expected to be received within the next twelve months. Purchase obligations can vary from quarter-to-quarter and versus the same period in prior years due to a number of factors, including the amount of products that are shipped directly to Retail customer warehouses versus through Nautilus warehouses.

In the ordinary course of business, we enter into agreements that require us to indemnify counterparties against third-party claims. These may include: agreements with vendors and suppliers, under which we may indemnify them against claims arising from use of their products or services; agreements with customers, under which we may indemnify them against claims arising from their use or sale of our products; real estate and equipment leases, under which we may indemnify lessors against third-party claims relating to the use of their property; agreements with licensees or licensors, under which we may indemnify the licensee or licensor against claims arising from their use of our intellectual property or our use of their intellectual property; and agreements with parties to debt arrangements, under which we may indemnify them against claims relating to their participation in the transactions.

The nature and terms of these indemnification obligations vary from contract to contract, and generally a maximum obligation is not stated within the agreements. We hold insurance policies that mitigate potential losses arising from certain types of indemnification obligations. Management does not deem these obligations to be significant to our financial position, results of operations or cash flows and, therefore, no related liabilities were recorded as of March 31, 2014.

Legal Matters

In 2004, we were sued in the Southern District of New York by BioSig Instruments, Inc. for alleged patent infringement in connection with our incorporation of heart rate monitors into certain cardio products. No significant activity in the litigation occurred until 2008. In 2012, the United States District Court granted summary judgment to us on grounds that BioSig's patents were invalid as a matter of law. BioSig appealed the grant of summary judgment and, in April 2013, the United States Court of Appeals for the Federal Circuit reversed the District Court's decision on summary judgment and remanded the case to the District Court for further proceedings. On January 10, 2014, the U.S. Supreme Court granted our petition for a writ of certiorari to address the legal standard applied by the Federal Circuit in determining whether the patents may be valid under applicable law. The case was argued before the Supreme Court on April 28, 2014 and a decision is expected in June 2014. We do not believe that our use of heart rate monitors utilized or purchased from third parties, and otherwise, infringe the BioSig patents.

In addition to the matter described above, from time to time we are subject to litigation, claims and assessments that arise in the ordinary course of business, including disputes that may arise from intellectual property related matters. Management believes that any liability resulting from such additional matters will not have a material adverse effect on our financial position, results of operations or cash flows.

We record expenses for litigation and loss contingencies when it is probable that a liability has been incurred and the amount of the loss can be reasonably estimated. When a loss contingency is not both probable and estimable, we do not establish an accrued liability. However, if the loss (or an additional loss in excess of the accrual) is at least a reasonable possibility and material, then we disclose an estimate of the possible loss or range of loss, if such estimate can be made, or disclose that an estimate cannot be made.

Litigation and jury verdicts are, to some degree, inherently unpredictable, and although we have determined that a loss is not probable in connection with any current legal proceeding at this time, it is reasonably possible that a loss may be incurred in connection with proceedings to which we are a party. Assessment of whether incurrence of a loss is probable, or a reasonable possibility, in connection with a particular proceeding, and estimation of the loss, or a range of loss, involves complex judgments and numerous uncertainties. Management is unable to estimate a range of reasonably possible losses related to litigation in its early stages, especially when the damages sought are indeterminate, or the legal and factual basis for the relevant claims have not been developed with specificity.

We regularly monitor our estimated exposure to these contingencies and, as additional information becomes known, may change our estimates accordingly. We evaluate, on a quarterly basis, developments in legal proceedings, investigations or claims that could affect the amount of any accrual, as well as any developments that would make a loss probable or reasonably possible, and whether the amount of a probable or reasonably possible loss is estimable. Among other factors, we evaluate the advice of internal and external counsel, the outcomes from similar litigation, current status of the lawsuits (including settlement initiatives), legislative developments and other factors. Due to the numerous variables associated with these judgments and assumptions, both the precision and reliability of the resulting estimates of the related loss contingencies are subject to substantial uncertainties.

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

The following discussion and analysis is based upon our financial statements as of the dates and for the periods presented in this section. You should read this discussion and analysis in conjunction with the financial statements and notes thereto found in Part I, Item 1 of this Form 10-Q and our consolidated financial statements and notes thereto included in our Annual Report on Form 10-K for the year ended December 31, 2013 (the "2013 Form 10-K"). All references to the first quarter and first three months of 2014 and 2013 mean the three-month periods ended March 31, 2014 and 2013, respectively. Unless the context otherwise requires, "Nautilus," "we," "us" and "our" refer to Nautilus, Inc. and its subsidiaries. Unless indicated otherwise, all information regarding our operating results pertains to our continuing operations.

Our results of operations may vary significantly from period-to-period. Our revenues typically fluctuate due to the seasonality of our industry, customer buying patterns, product innovation, the nature and level of competition for health and fitness products, our ability to procure products to meet customer demand, the level of spending on, and effectiveness of, our media and advertising programs and our ability to attract new customers and maintain existing sales relationships. In addition, our revenues are highly susceptible to economic factors, including, among other things, the overall condition of the economy and the availability of consumer credit in both the United States and Canada. Our profit margins may vary in response to the aforementioned factors and our ability to manage product costs. Profit margins may also be affected by fluctuations in the costs or availability of materials used to manufacture our products, product warranty costs, the cost of fuel, and changes in costs of other distribution or manufacturing-related services. Our operating profits or losses may also be affected by the efficiency and effectiveness of our organization. Historically, our operating expenses have been influenced by media costs to produce and distribute advertisements of our products on television, the Internet and other media, facility costs, operating costs of our information and communications

systems, product supply chain management, customer support and new product development activities. In addition, our operating expenses have been affected from time-to-time by asset impairment charges, restructuring charges and other significant unusual or infrequent expenses.

As a result of the above and other factors, our period-to-period operating results may not be indicative of future performance. You should not place undue reliance on our operating results and should consider our prospects in light of the risks, expenses and difficulties typically encountered by us and other companies, both within and outside our industry. We may not be able to successfully address these risks and difficulties and, consequently, we cannot assure you any future growth or profitability. For more information, see our discussion of Risk Factors located at Part I, Item 1A of our 2013 Form 10-K.

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. Words such as "plan," "expect," "aim," "believe," "project," "intend," "estimate," "will," "should," "could," and other terms of similar meaning typically identify forward-looking statements. The forward-looking statements in this report include, without limitation: our prospects, resources or capabilities; current or future financial trends; future operating results; future plans for introduction of new products; anticipated demand for our new and existing products; maintenance of appropriate inventory levels; growth in revenues and profits; leverage of operating expenses; future revenues from our licensing initiative; results of increased media investment in the Direct segment; continued improvement in operating margins; expectations for increased Research and Development expenses; the amount expected to be spent on capital projects in 2014; fluctuations in Net Sales due to seasonality; and our ability to continue to fund our operating and capital needs for the following twelve-month period. Forward-looking statements also include any statements related to our expectations regarding future business and financial performance or conditions, anticipated sales growth across markets, distribution channels and product categories, expenses and gross margins, profits or losses, losses from discontinued operation, settlements of warranty obligations, the anticipated outcome of litigation to which we are a party, new product introductions, financing and working capital requirements and resources. These forward-looking statements, and others we make from time-to-time, are subject to a number of risks and uncertainties. Many factors could cause actual results to differ materially from those projected in forward-looking statements, including the risks described in Part I, Item 1A, “Risk Factors,” in our 2013 Form 10-K as supplemented or modified in our quarterly reports on Form 10-Q. We do not undertake any duty to update forward-looking statements after the date they are made or to conform them to actual results or to changes in circumstances or expectations.

Overview

We are committed to providing innovative, quality solutions to help people achieve a fit and healthy lifestyle. Our principal business activities include designing, developing, sourcing and marketing high-quality cardio and strength fitness products and related accessories for consumer use, primarily in the United States and Canada. Our products are sold under some of the most-recognized brand names in the fitness industry: Nautilus®, Bowflex®, Schwinn®, Schwinn Fitness™ and Universal®.

We market our products through two distinct distribution channels, Direct and Retail, which we consider to be separate business segments. Our Direct business offers products directly to consumers through television advertising, catalogs and the Internet. Our Retail business offers our products through a network of independent retail companies with stores and websites located in the United States and internationally. We also derive a portion of our revenue from the licensing of our brands and intellectual property.

Net Sales for the first three months of 2014 were $71.9 million, an increase of $12.7 million, or 21.4%, as compared to Net Sales of $59.2 million for the first three months of 2013. Net sales of our Direct segment increased $8.1

million, or 19.0%, in the first three months of 2014, compared to the first three months of 2013, primarily due to increased consumer demand for our cardio products, especially the Bowflex® Treadclimber®. Net sales of our Retail segment increased by $5.0 million, or 32.8% in the first three months of 2014, compared to the first three months of 2013, primarily due to strong retailer sell-through of our new line up of cardio products.

Gross Profit for the first three months of 2014 was $38.5 million, an increase of $7.8 million, or 25.4%, as compared to Gross Profit of $30.7 million for the first three months of 2013. The increase in Gross Profit dollars and percent was primarily due to the increase in Net Sales and improved product costs. Operating Expenses for the first three months of 2014 were $29.5 million, an increase of $4.8 million, or 19.4%, as compared to Operating Expenses of $24.7 million for the first three months of 2013. The growth in Operating Expenses was primarily related to increases in Sales and Marketing expenses. Operating Income for the first three months of 2014 was $9.0 million, an increase of $3.0 million, or 50.2%, as compared to Operating Income of $6.0 million for the first three months of 2013. The increase was primarily due to higher sales and gross margins. Income from

Continuing Operations was $5.7 million for the first three months of 2014, or $0.18 per diluted share, compared to Income From Continuing Operations of $5.5 million, or $0.18 per diluted share, for the first three months of 2013.

Net income for the first three months of 2014 was $5.4 million, compared to net income of $5.2 million for the first three months of 2013. Net income per diluted share was $0.17 for the first three months of 2014, compared to $0.17 per diluted share for the first three months of 2013.

The improvement in our results of continuing operations for the first three months of 2014 compared to the first three months of 2013 was driven primarily by higher Net Sales and Gross Profit in both the Retail and Direct channels.

Discontinued Operations

Results from discontinued operations relate to the disposal of our former Commercial business, which was completed in April 2011. We reached substantial completion of asset liquidation at December 31, 2012. Although there was no revenue related to the Commercial business in either the 2014 or the 2013 periods, we continue to have legal and accounting expenses as we work with authorities on final deregistration of each entity and product liability expenses associated with product previously sold into the Commercial channel.

Results of Operations

Results of operations information was as follows (in thousands):

| | Three months ended March 31, | | Change | | |
|---|---|---|---|---|---|
| | 2014 | 2013 | $ | % | |
| Net sales | $71,903 | $59,214 | $12,689 | 21.4 | % |
| Cost of sales | 33,422 | 28,520 | 4,902 | 17.2 | % |
| Gross profit | 38,481 | 30,694 | 7,787 | 25.4 | % |
| Operating expenses: | | | | | |
| Selling and marketing | 21,774 | 18,626 | 3,148 | 16.9 | % |
| General and administrative | 5,803 | 4,947 | 856 | 17.3 | % |
| Research and development | 1,903 | 1,127 | 776 | 68.9 | % |
| Total operating expenses | 29,480 | 24,700 | 4,780 | 19.4 | % |
| Operating income | 9,001 | 5,994 | 3,007 | 50.2 | % |
| Other income (expense): | | | | | |
| Interest income | 8 | 1 | 7 | | |
| Interest expense | (7) | (9) | 2 | | |
| Other | (61) | (109) | 48 | | |
| Total other income (expense), net | (60) | (117) | 57 | | |
| Income from continuing operations before income taxes | 8,941 | 5,877 | 3,064 | | |
| Income tax expense | 3,193 | 353 | 2,840 | | |
| Income from continuing operations | 5,748 | 5,524 | 224 | | |
| Loss from discontinued operations, net of income taxes | (374) | (365) | (9) | | |
| Net income | $5,374 | $5,159 | $215 | | |

Results of operations information by segment was as follows (in thousands):

| | Three months ended March 31, | | Change | |
|---|---|---|---|---|
| | 2014 | 2013 | $ | % |
| Net sales: | | | | |
| Direct | $50,735 | $42,635 | $8,100 | 19.0 % |
| Retail | 20,103 | 15,134 | 4,969 | 32.8 % |
| Royalty income | 1,065 | 1,445 | (380) | (26.3)% |
| | $71,903 | $59,214 | $12,689 | 21.4 % |
| Cost of sales: | | | | |
| Direct | $18,417 | $17,158 | $1,259 | 7.3 % |
| Retail | 15,005 | 11,362 | 3,643 | 32.1 % |
| Royalty income | — | — | — | |
| | $33,422 | $28,520 | $4,902 | 17.2 % |
| Gross profit: | | | | |
| Direct | $32,318 | $25,477 | $6,841 | 26.9 % |
| Retail | 5,098 | 3,772 | 1,326 | 35.2 % |
| Royalty income | 1,065 | 1,445 | (380) | (26.3)% |
| | $38,481 | $30,694 | $7,787 | 25.4 % |
| Gross margin: | | | | |
| Direct | 63.7 % | 59.8 % | 390 | basis points |
| Retail | 25.4 % | 24.9 % | 50 | basis points |

The following table compares the Net Sales of our major product lines within each business segment (in thousands):

| | Three months ended March 31, | | Change | |
|---|---|---|---|---|
| | 2014 | 2013 | $ | % |
| Direct net sales: | | | | |
| Cardio products[1] | $45,863 | $35,643 | $10,220 | 28.7 % |
| Strength products[2] | 4,872 | 6,992 | (2,120) | (30.3)% |
| | 50,735 | 42,635 | 8,100 | 19.0 % |
| Retail net sales: | | | | |
| Cardio products[1] | 12,376 | 6,898 | 5,478 | 79.4 % |
| Strength products[2] | 7,727 | 8,236 | (509) | (6.2)% |
| | 20,103 | 15,134 | 4,969 | 32.8 % |
| Royalty income | 1,065 | 1,445 | (380) | (26.3)% |
| | $71,903 | $59,214 | $12,689 | 21.4 % |

[1] Cardio products include: TreadClimber®, MAX Trainer™, treadmills, exercise bikes, ellipticals, CoreBody Reformer®, Bowflex Boost™ and DVDs.
[2] Strength products include: home gyms, selectorized dumbbells, kettlebell weights, UpperCut™ and accessories.

Direct

The 19.0% increase in Direct Net Sales in the three-month period of 2014 compared to the same period of 2013 was primarily related to the increase in sales of our cardio products, especially the Bowflex® Treadclimber®. We believe the sales increase was driven by increased advertising effectiveness, improved call center effectiveness and higher U.S. consumer credit approval rates.

Combined consumer credit approvals by our primary and secondary U.S. third-party financing providers for the three-month period ended March 31, 2014 increased to 41.3% compared to 35.1% in the same period last year, which

we attribute to our media strategy focused on driving quality consumer leads and an expanded lender base.

The increase in Direct Net Sales of cardio products in the three-month period of 2014 compared to the same period of 2013 was partially offset by a decline in Direct Net Sales of strength products, primarily due to lower sales of rod-based home gyms. The decline was attributable, in part, to the reduction of advertising for these products over time, as management determined that television advertising spending on this mature product category was generating suboptimal returns. We continue to market and sell rod-based home gyms through more cost-efficient online media, and sales of these products have cascaded to the Retail segment.

The increase in Cost of Sales of our Direct business in the three-month period of 2014 compared to the same period of 2013 was almost entirely related to growth in Direct Net Sales.

The 390 basis point increase in the gross margin of our Direct business for the three-month period of 2014 compared to the same period of 2013 was primarily due to improved product cost with the higher sales volume.

Retail

The 32.8% increase in Retail Net Sales in the three-month period of 2014 compared to the same period of 2013 was driven by increased sales of the new line up of cardio products launched in September 2013.

The increase in Retail Cost of Sales for the three-month period of 2014 compared to the same period of 2013 was due to the increase in Retail Net Sales.

The 50 basis point improvement in Retail gross margin in the three-month period of 2014 compared to the same period of 2013 was primarily due to greater absorption of fixed supply chain costs with the higher sales volume.

Selling and Marketing

| Dollars in thousands | Three months ended March 31, | | Change | |
|---|---|---|---|---|
| | 2014 | 2013 | $ | % |
| Selling and Marketing | $21,774 | $18,626 | $3,148 | 16.9% |
| As % of Net Sales | 30.3% | 31.5% | | |

The increase in Selling and Marketing expense in the three-month period of 2014 compared to the same period of 2013 was primarily due to higher creative production of $1.0 million, media advertising of $0.7 million and incremental variable selling expenses of $0.8 million.

Selling and Marketing as a percentage of Net Sales is affected by the mix of Direct sales compared to Retail sales. Increasing Retail sales as a percentage of total Net Sales reduces the percentage of Selling and Marketing as a percentage of Net Sales and vice versa.

Media advertising expense of our Direct business is the largest component of Selling and Marketing and was as follows:

| Dollars in thousands | Three months ended March 31, | | Change | |
|---|---|---|---|---|
| | 2014 | 2013 | $ | % |
| Media advertising | $10,667 | $9,963 | $704 | 7.1% |

The increase in media advertising in the three-month period of 2014 compared to the same period of 2013 was primarily to drive incremental sales in the Direct business.

General and Administrative

| Dollars in thousands | Three months ended March 31, | | Change | |
|---|---|---|---|---|
| | 2014 | 2013 | $ | % |

| | | | | |
|---|---|---|---|---|
| General and Administrative | $5,803 | $4,947 | $856 | 17.3% |
| As % of Net Sales | 8.1% | 8.4% | | |

The increase in General and Administrative in the three-month period of 2014 compared to the same period of 2013 was primarily due to higher intellectual property and patent fees in 2014 of $0.2 million. Additionally, incentive compensation and software license fees both increased by $0.2 million in the first quarter of 2014 as compared to the same period of 2013.

The decrease as a percentage of Net Sales in the three-month period of 2014 compared to the same period of 2013 was primarily due to the increase in Net Sales.

Research and Development

| Dollars in thousands | Three months ended March 31, | | Change | |
|---|---|---|---|---|
| | 2014 | 2013 | $ | % |
| Research and Development | $1,903 | $1,127 | $776 | 68.9% |
| As % of Net Sales | 2.6% | 1.9% | | |

The increase in Research and Development in the three-month period of 2014 compared to the same period of 2013 was primarily due to our continued investment in resources required to innovate and broaden our product portfolio.

Other Income (Expense)

Other Income (Expense) primarily relates to the effect of exchange rate fluctuations between the U.S. and Canada.

Income Tax Provision

| Dollars in thousands | Three months ended March 31, | | Change | |
|---|---|---|---|---|
| | 2014 | 2013 | $ | % |
| Income Tax Provision | $3,193 | $353 | $2,840 | n/m |

n/m - Not meaningful

Income Tax Provision for the first three months of 2014 was based on a 35.7% effective tax rate and primarily related to our profitable U.S. and Canadian operations. Income Tax Provision for the first three months of 2013 was primarily related to our profitable Canadian operations, as well as an increase in deferred tax liabilities for indefinite lived tradename intangibles that could not be used to reduce our valuation allowance in the United States.

LIQUIDITY AND CAPITAL RESOURCES

As of March 31, 2014, we had $42.0 million of Cash and Cash Equivalents and $13.5 million of Marketable Securities, compared to $41.0 million of Cash and Cash Equivalents and zero Marketable Securities as of December 31, 2013. Cash provided by operating activities was $15.1 million for the three months ended March 31, 2014, compared to cash provided by operating activities of $6.0 million for the three months ended March 31, 2013. We expect our Cash, Cash Equivalents and Marketable Securities at March 31, 2014, along with cash expected to be generated from operations, to be sufficient to fund our operating and capital requirements for at least twelve months from March 31, 2014.

The increase in cash flows from operating activities was primarily due to the changes in our operating assets and liabilities as discussed below, as well as the decrease in Deferred Income Tax Assets due to the utilization of net operating losses.

Trade Receivables decreased $11.9 million to $13.4 million as of March 31, 2014, compared to $25.3 million as of December 31, 2013, due to a seasonal sequential quarterly decline in Net Sales. Days sales outstanding ("DSO") at March 31, 2014 were 17.9 days compared to 19.9 days as of December 31, 2013 and 22.5 days as of March 31, 2013. The decrease in DSO at March 31, 2014 compared to December 31, 2013 was due to a higher percentage of our Net Sales being derived from our Direct Net Sales, which generally has a lower DSO than Retail Net Sales. The decrease in DSO at March 31, 2014 compared to March 31, 2013 was also due to improved collections from Retail customers.

Inventories decreased $2.3 million to $13.5 million as of March 31, 2014, compared to $15.8 million as of December 31, 2013, due to a seasonal sequential quarterly decline in Net Sales and, accordingly, lower inventory purchases. Inventories as of March 31, 2014 compared to March 31, 2013 decreased by $0.2 million, while sales increased, due to improvements in inventory management.

Trade Payables decreased $9.9 million to $27.3 million as of March 31, 2014, compared to $37.2 million as of December 31, 2013, due to a seasonal sequential quarterly decline in Net Sales and, accordingly, lower inventory purchases.

Accrued Liabilities decreased $1.3 million to $7.8 million as of March 31, 2014 compared to $9.1 million as of December 31, 2013, primarily due to incentive compensation payments made in the first quarter of 2014 that related to 2013 performance.

Cash used in investing activities of $14.0 million for the first three months of 2014 was primarily related to the purchase of $13.5 million of marketable securities during the quarter. Additionally, $0.5 million in capital expenditures was incurred during the quarter for implementation of new software and hardware information system upgrades and new product tooling equipment. We anticipate spending between $3.0 to $3.5 million in 2014 for capital projects.

Financing Arrangements

We have a Credit Agreement (the "Loan Agreement") with Bank of the West that provides for a $15,750,000 maximum revolving secured credit line. The line of credit is available through March 31, 2015 for working capital, standby letters of credit and general corporate purposes. Borrowing availability under the Loan Agreement is subject to our compliance with certain financial and operating covenants at the time borrowings are requested. Standby letters of credit under the Loan Agreement are treated as a reduction of the available borrowing amount and are subject to covenant testing.

The interest rate applicable to borrowings under the Loan Agreement is based on either, at our discretion, Bank of the West's base rate, a floating rate or LIBOR, plus an applicable margin based on certain financial performance metrics. Our borrowing rate was 1.65% as of March 31, 2014. The Loan Agreement contains customary covenants, including minimum fixed charge coverage ratio and leverage ratio, and limitations on capital expenditures, mergers and acquisitions, indebtedness, liens, dispositions, dividends and investments. The Loan Agreement also contains customary events of default. Upon an event of default, the lender has the option of terminating its credit commitment and accelerating all obligations under the Loan Agreement. Borrowings under the Loan Agreement are collateralized by substantially all of our assets, including intellectual property assets.

As of March 31, 2014, we had no outstanding borrowings and $0.4 million in standby letters of credit issued under the Loan Agreement. As of March 31, 2014, we were in compliance with the financial covenants of the Loan Agreement and approximately $15.4 million was available for borrowing.

Commitments and Contingencies

For a description of our commitments and contingencies, refer to Note 12 to our Condensed Consolidated Financial Statements in Item 1 of this Form 10-Q.

Off-Balance Sheet Arrangements

In the ordinary course of business, we enter into agreements that require us to indemnify counterparties against third-party claims. These may include: agreements with vendors and suppliers, under which we may indemnify them against claims arising from our use of their products or services; agreements with customers, under which we may indemnify them against claims arising from their use or sale of our products; real estate and equipment leases, under which we may indemnify lessors against third party claims relating to the use of their property; agreements with licensees or licensors, under which we may indemnify the licensee or licensor against claims arising from their use of our intellectual property or our use of their intellectual property; and agreements with parties to debt arrangements, under which we may indemnify them against claims relating to their participation in the transactions.

The nature and terms of these indemnifications vary from contract to contract, and generally a maximum obligation is not stated. We hold insurance policies that mitigate potential losses arising from certain types of indemnifications. Because we are unable to estimate our potential obligation, and because management does not expect these obligations to have a material adverse effect on our consolidated financial position, results of operations or cash flows, no liabilities are recorded at March 31, 2014.

SEASONALITY

We expect our sales from fitness equipment products to vary seasonally. Sales are typically strongest in the first and fourth quarters, followed by the third quarter, and are generally weakest in the second quarter. We believe that, during the spring and summer months, consumers tend to be involved in outdoor activities, including outdoor exercise, which impacts sales of indoor fitness equipment. This seasonality can have a significant effect on our inventory levels, working capital needs and resource utilization.

CRITICAL ACCOUNTING POLICIES AND ESTIMATES

Our critical accounting policies have not changed from those discussed in our 2013 Form 10-K.

Item 3. Quantitative and Qualitative Disclosures About Market Risk

There have been no material changes in our reported market risks or risk management policies since the filing of our 2013 Form 10-K.

Item 4. Controls and Procedures

Evaluation of Disclosure Controls and Procedures

In accordance with Rule 13a-15 of the Securities Exchange Act of 1934 (the "Exchange Act"), as of the end of the period covered by this Quarterly Report on Form 10-Q, our management evaluated, with the participation of our Chief Executive Officer and our Chief Financial Officer, the effectiveness of our disclosure controls and procedures (as defined in Rule 13a- 15(e) and Rule 15d-15(e) under the Exchange Act). Based upon their evaluation of these disclosure controls and procedures, our management, including the Chief Executive Officer and Chief Financial Officer, have concluded that our disclosure controls and procedures were effective as of the end of the period covered by this report.

Changes in Internal Control over Financial Reporting

There were no changes in our internal control over financial reporting that occurred during the three months ended March 31, 2014, that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

PART II. OTHER INFORMATION

Item 1. Legal Proceedings

In 2004, we were sued in the Southern District of New York by BioSig Instruments, Inc. for alleged patent infringement in connection with our incorporation of heart rate monitors into certain cardio products. No significant activity in the litigation occurred until 2008. In 2012, the United States District Court granted summary judgment to us on grounds that BioSig's patents were invalid as a matter of law. BioSig appealed the grant of summary judgment and, in April 2013, the United States Court of Appeals for the Federal Circuit reversed the District Court's decision on summary judgment and remanded the case to the District Court for further proceedings. On January 10, 2014, the U.S. Supreme Court granted our petition for a writ of certiorari to address the legal standard applied by the Federal Circuit in determining whether the patents may be valid under applicable law. The case was argued before the Supreme Court on April 28, 2014 and a decision is expected in June 2014. We do not believe that our use of heart rate monitors utilized or purchased from third parties, and otherwise, infringe the BioSig patents.

In addition to the matter described above, from time to time we are subject to litigation, claims and assessments that arise in the ordinary course of business, including disputes that may arise from intellectual property related matters. Management believes that any liability resulting from such additional matters will not have a material adverse effect on our financial position, results of operations or cash flows.

Item 1A. Risk Factors

We operate in an environment that involves a number of risks and uncertainties. The risks and uncertainties described in our 2013 Form 10-K are not the only risks and uncertainties that we face. Additional risks and uncertainties that presently are not considered material or are not known to us, and therefore are not mentioned herein, may impair our business operations. If any of the risks described in our 2013 Form 10-K actually occur, our business, operating results and financial position could be adversely affected. There has not been a material change to the risk factors as set forth in our 2013 Form 10-K.

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

Issuer Purchases of Equity Securities

The following table provides information about our repurchases of our equity securities during the first quarter ended March 31, 2014:

| Period | (a) Total Number of Shares (or Units) Purchased [1] | (b) Average Price Paid per Share (or Unit) | (c) Total Number of Shares (or Units) Purchased as Part of Publicly Announced Plans or Programs | (d) Maximum Number (or Approximate Dollar Value) of Shares (or Units) that May Yet Be Purchased Under the Plans or Programs |
|---|---|---|---|---|
| January 1, to January 31, 2014 | 2,017 | $8.52 | — | — |
| February 1 to February 28, 2014 | 1,689 | 8.39 | — | — |
| March 1 to March 31, 2014 | 1,688 | 9.63 | — | — |
| Total | 5,394 | 8.83 | — | — |

[1] Consists of shares withheld from the vesting portion of a restricted stock unit award granted to Bruce M. Cazenave, our Chief Executive Officer. We will withhold from each monthly vesting portion of the award the number of shares sufficient to satisfy Mr. Cazenave's tax withholding obligation incident to such vesting, unless Mr. Cazenave should first elect to satisfy the tax obligation by cash payment to us. We do not have any publicly announced equity securities repurchase plans or programs.

Item 6. Exhibits

| Exhibit No. | Description |
|---|---|
| 10.1 | Employment Agreement, dated as of February 10, 2014, by and between Nautilus, Inc. and Sidharth Nayar.* |
| 10.2 | Stock Unit Award Agreement, dated as of February 28, 2014, by and between Nautilus, Inc. and Sidharth Nayar.* |
| 10.3 | Employment Offer Letter, dated July 26, 2013, between Nautilus, Inc. and Jeffery Collins.* |
| 31.1 | Certification of Chief Executive Officer pursuant to Rule 13a-14(a) of the Securities Exchange Act of 1934, as amended. |
| 31.2 | Certification of Chief Financial Officer pursuant to Rule 13a-14(a) of the Securities Exchange Act of 1934, as amended. |
| 32.1 | Certification of Chief Executive Officer and Chief Financial Officer pursuant to Rule 13a-14(b) of the Securities and Exchange Act of 1934, as amended, and 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002. |
| 101 | The following financial statements from Nautilus, Inc.'s quarterly report on Form 10-Q for the three months ended March 31, 2014, formatted in XBRL (eXtensible Business Reporting Language): (i) Condensed Consolidated Balance Sheets (unaudited), (ii) Condensed Consolidated Statements of Operations (unaudited), (iii) Condensed Consolidated Statements of Comprehensive Income (unaudited), (iv) Condensed Consolidated Statements of Cash Flows (unaudited) and (v) Notes to Condensed Consolidated Financial Statements (unaudited). |

* Indicates management contract, compensatory agreement or arrangement in which our directors or executive officers may participate.

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.

NAUTILUS, INC.

May 8, 2014

By: /S/ Bruce M. Cazenave
Bruce M. Cazenave
Chief Executive Officer
(Principal Executive Officer)

NAUTILUS, INC.

May 8, 2014

By: /S/ Sidharth Nayar
Sidharth Nayar
Chief Financial Officer
(Principal Financial and Accounting Officer)