MEDIFAST INC
Form 10-K/A
September 06, 2007

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, DC 20549

FORM 10-K/A
Amendment No. 1

ANNUAL REPORT UNDER SECTION 13 OR 15(d) OF
THE SECURITIES EXCHANGE ACT OF 1934

For the fiscal year ended December 31, 2005

Commission File No. 000-23016

MEDIFAST, INC.

DELAWARE Incorporation State	13-3714405 Tax Identification number
11445 CRONHILL DRIVE, OWINGS MILLS, MD Principal Office Address	21117

Phone (410) 581-8042

SECURITIES REGISTERED PURSUANT TO SECTION 12(B) OF THE ACT: NONE

SECURITIES REGISTERED PURSUANT TO SECTION 12(G) OF THE ACT:

COMMON STOCK, PAR VALUE $.001 PER SHARE

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

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 o No x

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 o

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. o

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

Large accelerated filer o Accelerated filer o Non-accelerated filer x

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

The aggregate market value of the voting common equity held by non-affiliates of the registrant as of June 30, 2005, based upon the closing price of $3.04 per share on the American Stock Exchange on that date, was $32,985,000.

As of March 14, 2006, the Registrant had 12,786,124 shares of Common Stock outstanding.

DOCUMENTS INCORPORATED BY REFERENCE

Portions of the definitive Proxy Statement for the 2006 Annual Meeting of Stockholders, which will be filed within 120 days after the end of the fiscal year, are incorporated by reference into Part III.

Explanatory Note

This Amendment No. 1 to our Annual Report on Form 10-K for the fiscal year ended December 31, 2005 initially filed with the Securities and Exchange Commission on March 15, 2006 is being filed to reflect restatements of Medifast, Inc.'s Consolidated Balance Sheets as of December 31, 2005 and 2004, and the related Consolidated Statements of Income, Cash Flows, and Stockholders' Equity for each of the three years in the period ended December 31, 2005. These restatements reflect the adjustment detailed in Note R to the Consolidated Financial Statements relating to amortization expense on a customer list acquired in December 2004.

The following sections of this report have been revised to reflect above restatement: Part II – Item 6-Selected Financial Data, Item 7 – Management's Discussion and Analysis of Financial Condition and Results of Operations, Item 8 – Financial Statements and Supplementary Data and Item 9A – Controls and Procedures; and Part IV – Exhibits and Financial Statement Schedules. For the convenience of the reader, this Amendment No. 1 includes, in their entirety, those items in the Original filing not being amended and restated. Except as discussed above, we have not modified or updated the disclosure presented in the Original Annual Report. This Form 10-K/A does not reflect events that have occurred after the filing of the Original Annual Report or modify or update disclosures presented in the Original Annual Report affected by subsequent events. Accordingly, this Form 10-K/A should be read in conjunction with our filings made with the Securities and Exchange Commission ("SEC") subsequent to the date of the filing of the Original Annual Report.

In addition, in accordance with applicable SEC rules, this Form 10-K/A includes updated certifications from our Chief Executive Officer and Chief Financial Officer.

PART I

ITEM 1. BUSINESS.

SUMMARY

Medifast, Inc. (the "Company", or "Medifast") is a Delaware corporation, incorporated in 1980. The Company's operations are primarily conducted through five of its wholly owned subsidiaries, Jason Pharmaceuticals, Inc. ("Jason"), Take Shape for Life, Inc. ("TSFL"), Jason Enterprises, Inc., Jason Properties, LLC and Seven Crondall, LLC. The Company is engaged in the production, distribution, and sale of weight management and disease management products and other consumable health and diet products. Medifast, Inc.'s product lines include weight and disease management, meal replacement and sports nutrition products manufactured in a modern, FDA approved facility in Owings Mills, Maryland.

MARKETS

Over the past 20 years the obesity rates in the United States have increased dramatically. The Centers for Disease Control (CDC) estimate that 64% of the U.S. adult population is overweight, and 30% of these individuals (60 million) are obese which is defined as having a Body Mass Index >30. The amount of overweight adolescents and children ages 6-19 years have more than tripled since 1980. Currently, the CDC estimates that over 30% of adolescents and children are overweight.

The CDC estimates that in the U.S. the associated costs with overweight and obesity reached $117 billion in 2000. The most common health problems associated with obesity are type II diabetes, coronary heart disease, hypertension and stroke, depression and certain forms of cancer. It's also estimated that poor nutrition and physical inactivity account for more than 300,000 premature deaths per year in the U.S.

A 2003 market research study concluded consumers spend about $39 billion per year trying to lose weight or prevent weight gain. This includes consumer spending on diet foods, medically supervised and commercial weight loss programs, diet books, appetite suppressants, fitness clubs, diet sodas, and videos and cassettes.

Distribution Channels

The Medifast Lifestyles Program- The Medifast Lifestyles Program is a medically supported network of health care professionals who support patients on the Medifast program. Patients order products directly from Medifast's website or toll-free number. The Lifestyles medical practitioner ensures that each patient receives personalized attention throughout the weight loss program. Management estimates that more than 15,000 physicians nationwide have prescribed Medifast as a treatment for their overweight patients since 1980, and over an estimated 1 million patients have used its' products to lose and maintain their weight. Direct-to-consumer sales represent approximately 45% of Medifast, Inc.'s total sales.

The Company maintains an in-house Lifestyles support program for customers who have a Medifast physician who does not have the time to provide counseling support. The Company also offers an additional in-house support program to assist customers that are consulting their primary care physician. Customers have access to qualified nutritional counselors for program support and advice via a toll free telephone help line or by e-mail.

Take Shape for Life™ - Take Shape for Life is a physician led network of independent health coaches who are specifically trained to provide emotional support and are conduits to give clients the strategies and skills to successfully reach a healthy weight and then provide a road map to empower the individual to take control of their health. Take Shape for Life is a support program that moves beyond the scope of weight loss to show customers how to achieve optimal health through the balance of body, mind, and finances. Take Shape for Life uses the high quality, medically validated products of Medifast as the platform to launch an integrity based lifelong health optimization program.

Program entrants are encouraged to consult with their primary care physician and a Take Shape for Life Health Advisor to determine the Medifast program that is right for them. Physician directed Health Advisors are supported, educated and qualified by The Health Institute, a training group staffed by Medifast professionals. Health Advisors obtain Medifast qualification based upon testing of their knowledge on Medifast products and programs.

Take Shape for Life accounts for approximately 35% of Medifast, Inc.'s total sales.

Medifast Physicians and Clinics - Many Medifast physicians have chosen to implement the Medifast program within their practice. These physicians carry an inventory of Medifast products and resell them to patients. They also provide appropriate testing, medical support and evaluations for patients on the program. Physicians can also direct their patients to order directly from Medifast, if they do not have space to stock inventory. Physician sales account for approximately 10% of Medifast, Inc.'s total sales.

Hi-Energy Weight Control Centers - In 2003, the Company acquired Hi-Energy Weight Control Centers, a national company specializing in weight management programs, with weight loss centers in over 50 locations. Hi-Energy Weight Control Centers offer a competitive marketing edge through a regional advertising program, exclusive territories and marketing support. The Company continues to seek out qualified licensees to add to its growing number of weight control clinics nationwide. Additionally, the Company is operating 11 corporately owned clinics that serve as models to attract qualified licensees. Hi-Energy clinics account for approximately 7% of Medifast, Inc.'s total sales.

THE MEDIFAST® BRAND

Medifast is a medically supervised weight management program, which specializes in multidisciplinary patient education programs using the highest quality meal replacement supplements. In recent years Medifast's core products and programs have continued to expand over a wellness spectrum to include health management products. Medifast offers products specially formulated for diabetics as well as products for women's health, joint health and coronary health.

In 2003, Medifast began a two-year study with The Johns Hopkins Bloomberg School of Public Health to evaluate the efficacy of its Medifast Plus for Diabetics compared to basic nutrition recommendations by the American Diabetes Association (ADA). Final results showed that participants using Medifast Plus for Diabetics lost twice as much weight and were twice as able to stay on the program as those following the ADA's guidelines. Additionally, two-thirds of those on the Medifast program lost at least 5% of their weight, which is a standard measure of the Food and Drug Administration's (FDA) threshold to indicate clinically significant weight loss, versus one-quarter of those on the ADA diet. In addition to weight loss, the initial study results indicate that Medifast participants sustained an average 9% decrease in blood fasting glucose and an average 19% decrease in insulin levels.

Many Medifast Plus for Diabetics products have earned the coveted Seal of Approval from the Glycemic Research Institute. The line, designated as Low Glycemic, does not overly stimulate blood glucose and insulin and does not stimulate fat-storing enzymes. Products included in the Medifast Plus for Diabetics line consist of three delicious patented shakes, home style chili, apple cinnamon, French vanilla berry oatmeal, maple and brown sugar oatmeal, creamy chicken soup, creamy broccoli soup, chicken noodle soup, minestrone soup and two snack bars.

Most Medifast products qualify to make the FDA's heart healthy claim, "May Reduce the Risk of Heart Disease." In order to make this claim, a product must contain at least 6.25 grams of soy protein per serving and be low in fat, saturated fat, and cholesterol. Unlike popular fad diets and herbal supplements, Medifast products are a safe, nutritionally balanced choice, offering gender specific formulas containing high protein and low carbohydrates, a soy protein source rather than animal protein source, and vitamin and mineral fortification. It is very difficult to meet the minimum recommended nutritional requirements on a low-calorie diet, but a dieter can easily meet these requirements using the nutrient dense Medifast brand of meal replacement food supplements.

Medically supervised, low calorie diets are continuing to gain popularity, as consumers search for a safe and effective solution that provides balanced nutrition, quick weight loss and valuable behavior modification education. In addition, consumers are becoming more aware of chronic diseases such as diabetes and coronary health.

COMPETITION

There are many different kinds of diet products and programs within the weight loss industry. These include a wide variety of commercial weight loss programs, pharmaceutical products, weight loss books, self-help diets, dietary supplements, appetite suppressants and meal replacement shakes and bars.

The Company has proven it can compete in this competitive market because its products have been clinically tested and proven at Johns Hopkins University and have been safely and effectively used by customers for over 20 years. Medifast has been on the cutting edge of product development with soy based nutritional and weight management products since 1989. These products are formulated with high-quality, low-calorie, low-fat ingredients that provide alternatives to fad diets or medicinal weight loss remedies.

The Medifast program has been recommended by physicians for more than 25 years and some Medifast practitioners choose to prescribe appetite suppression diet drugs to patients in conjunction with a Medifast based diet. Diet drug therapies such as those that suppress appetite usually require a restricted calorie diet in order to obtain desired results. Medifast is a dosage/portion controlled weight management solution that is effective in conjunction with drug therapy as prescribed by physicians working within the individual needs of their patients. The Medifast program alone is a mild ketogenic diet that naturally suppresses appetite and eliminates hunger without other therapies for most people.

PRODUCTS

The Company offers a variety of weight and disease management products under the Medifast® brand and for select private label customers. The Medifast line includes Medifast® 55, Medifast® 70, Medifast® Plus for Appetite Suppression, Medifast® Plus for Diabetics, Medifast® Plus for Joint Health, Medifast® Plus for Women's Health, Medifast® Plus for Coronary Health, Medifast® Fit!, Medifast® Take ShapeTM, Medifast® Supplement Bars, Medifast® Creamy Soups, Medifast® Minestrone Soup, Medifast® Hot Cocoa, Medifast® Oatmeals, Medifast® Pro Teas, Medifast® Chicken Noodle Soup, Medifast® Fast Soups, Medifast® Homestyle Chili and Medifast® Multigrain Crackers.

Medifast nutritional products are formulated with high-quality, low-calorie, low-fat ingredients. Many Medifast products are soy based and contain 24 vitamins and minerals, as well as other nutrients essential for good health. The Company uses DuPont Protein Technologies' Supro® brand soy protein, which is a high-quality complete protein derived from soybeans.

Medifast brand awareness continues to expand through the Company's marketing campaigns, product development, line extensions, and the Company's emphasis on quality customer service, technical support and publications developed by the Company's marketing staff. Medifast products have been proven to be effective for weight and disease management in clinical studies conducted by the U.S. government and Johns Hopkins University. The Company has continued to develop its sales and marketing operations with qualified management and innovative programs. The Company's facility in Owings Mills, MD manufactures powders and a portion of its supplement bars and subcontracts the production of its Ready-to-Drink products and additional bars.

NEW PRODUCTS

The Company expanded the Medifast product line in 2005 by introducing Medifast® Banana Crème Shake, Medifast® Peach Oatmeal, Medifast® Beef Vegetable Stew, Medifast® Red Bell Pepper Italian dressing, and Medifast® Ranch dressing. Medifast also introduced a line of diabetic products that includes shakes and bars under the Medifast® Maintain line.

MARKETING

The Company continued to build and leverage its core Medifast brand through multiple marketing strategies to its target audiences. Print advertising, television, and radio were all used to target new customers by stressing Medifast's quick, easy and safe approach to weight management. Also, direct mail has been utilized to encourage and support existing customers.

Online advertising began to be used in 2004 and it included keyword search, banner ads, affiliate programs, and targeted direct email campaigns. The online advertising has been supported by Medifast's well designed, user-friendly website, which provides a wealth of information and customer support for easy ordering functionality.

SALES

The Company's Sales division handles three primary areas:

Physician and Clinic Sales— The sales team is responsible for prospecting larger medical accounts, clinics, hospitals, and HMOs. During 2005, the sales team attended a number of medical professional trade shows, which expanded Medifast's penetration of the clinical business segment.

Hi-Energy Weight Control Centers— During 2005 Hi-Energy provided ongoing support to its licensees as well as to the Company's 11 corporately owned centers which opened at the end of 2004. This support included marketing materials, ads, on-site trainings, fitness programs, nutritional programs and clinical operation materials and forms. Employees attended professional trade shows, prospected new licensees, and partnered with area physicians to provide Hi-Energy programs and services to local hospitals and private practices.

Take Shape for Life— Provides a sales force of independent Health Advisors who support patients and their primary care physicians with a defined support program. Take Shape for Life is a support program that moves beyond the scope of weight loss to show customers how to achieve optimal health through the balance of body, mind, and finances..

MANUFACTURING

Jason Pharmaceuticals, Inc., the Company’s wholly owned manufacturing subsidiary, produces over 80% of the Medifast products in a state-of-the-art food and pharmaceutical-grade facility in Owings Mills, Maryland. Management purchased the plant in July 2002 for $3.4 million.

The manufacturing facility has the capacity for significant increases to its production output with minimal capital expenditures. Adding additional shifts, along with minor capital expenditures for machinery would enable the Company to produce enough products to generate over $200 million in sales.

Manufacturing processes, product labeling, quality control and equipment are subject to regulations and inspections mandated by the Food & Drug Administration (FDA), the Maryland State Department of Health and Hygiene, and the Baltimore County Department of Health. The plant strictly adheres to all GMP practices and has maintained its status as an "OU" (Orthodox Union) kosher-approved facility since 1982.

GOVERNMENTAL REGULATION HISTORY

The formulation, processing, packaging, labeling and advertising of the Company's products are subject to regulation by several federal agencies, but principally by the Food and Drug Administration (the "FDA"). The Company must comply with the standards, labeling and packaging requirements imposed by the FDA for the marketing and sale of medical foods, vitamins, and nutritional products. Applicable regulations prevent the Company from representing in its literature and labeling that its products produce or create medicinal effects or possess drug-related characteristics. The FDA could, in certain circumstances, require the reformulation of certain products to meet new standards, require the recall or discontinuation of certain products not capable of reformulation, or require additional record keeping, expanded documentation of the properties of certain products, expanded or different labeling, and scientific substantiation. If the FDA believes the products are unapproved drugs or food additives, the FDA may initiate similar enforcement proceedings. Any or all such requirements could adversely affect the Company's operations and its financial condition.

The FDA also requires “medical food” labeling to list the name and quantity of each ingredient and identify the product as a “weight management/modified fasting or fasting supplement” in the labeling.

To the extent that sales of vitamins, diet, or nutritional supplements may constitute improper trade practices or endanger the safety of consumers, the operations of the Company may also be subject to the regulations and enforcement powers of the Federal Trade Commission ("FTC"), and the Consumer Product Safety Commission. The Company's activities are also regulated by various agencies of the states and localities in which the Company's products are sold. The Company's products are manufactured and packaged in accordance with customers’ specifications and sold under their private labels both domestically and in foreign countries through independent distribution channels.

PRODUCT LIABILITY AND INSURANCE

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

EMPLOYEES

As of December 31, 2005, the Company employed 164 full-time and contracted employees, of whom 62 were engaged in manufacturing, warehouse management, and shipping, and 102 in marketing, administrative, call center and corporate support functions. None of the employees are subject to a collective bargaining agreement with the Company.

ITEM 2. DESCRIPTION OF PROPERTY

The Company owns a 49,000 square-foot facility in Owings Mills, Maryland, which contains its Corporate Headquarters and manufacturing plant. In 2003, the Company purchased a state-of-the-art 119,000 square-foot distribution facility in Ridgely, Maryland. The facility gives the Company the ability to distribute over $200 million of Medifast product sales per year. In 2004, the Company purchased a 3,000 square foot conference and training facility in Ocean City, Maryland. The facility will be used to conduct corporate training meetings, Board of Director Meetings and employee morale and wellness programs. The Company has 11 leases for its corporately owned Hi-Energy Weight Control clinics throughout Florida, Arkansas, Mississippi and Texas. The leases range in terms from one to five years.

ITEM 3. LEGAL PROCEEDINGS.

There were no material pending legal matters as of 12/31/05.

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

The Medifast Annual Shareholder Meeting was held on September 16, 2005 at the Roland E. Powell Convention Center in Ocean City, Maryland. The shareholders voted Michael C. MacDonald (96%), Mary T. Travis* (98%) and Joseph D. Calderone, O.S.A* (98%) as Class II Directors that will hold office until 2008, and Michael J. McDevitt (97%), and George Lavin, Jr., Esq* (98%) as Class III Directors. Class III Directors will hold office until the next Annual Shareholders Meeting at which time their respective class term expires and their respective successors will be duly elected and qualified. Additionally, the shareholders approved the appointment of Bagell, Josephs & Company, LLC, an independent member of the BDO Seidman Alliance, as the Company’s independent auditors for the fiscal year ending December 31, 2005. Lastly, the shareholders voted to increase the number of authorized shares of common stock by 5 million shares to 20 million shares authorized.

* Independent Director

(a) The following are the Board of Directors:

Name	Age	Position	Date First Became Director
Bradley T. MacDonald	58	Chairman of the Board, Chief Executive Officer and Director	1996
Donald F. Reilly	58	Director	1998
Michael C. MacDonald	52	Director	1998
Mary T. Travis	55	Director	2002
Joseph D. Calderone	57	Director	2003
George Lavin, Jr	76	Director	2005
Michael J. McDevitt	57	Director	2002

BRADLEY T. MACDONALD became Chairman of the Board and Chief Executive Officer of Medifast, Inc. on January 28, 1998. Prior to joining the Company, he was appointed as Program Director of the U.S. Olympic Coin Program of the Atlanta Centennial Olympic Games. Mr. MacDonald was previously employed by the Company as its Chief Executive Officer from September 1996 to August 1997. From 1991 through 1994, Colonel MacDonald returned to active duty to be Deputy Director and Chief Financial Officer of the Retail, Food, Hospitality and Recreation Businesses for the United States Marine Corps. Prior thereto, Mr. MacDonald served as Chief Operating Officer of the Bonneau Sunglass Company, President of Pennsylvania Optical Co., Chairman and CEO of MacDonald and Associates, which had major financial interests in a retail drug, consumer candy, and pilot sunglass companies. Mr. MacDonald was national president of the Marine Corps Reserve Officers Association and retired from the United States Marine Corps Reserve as a Colonel in 1997, after 27 years of service. He has been appointed to the Defense Advisory Board for Employer Support of the Guard and Reserve (ESGR). Mr. MacDonald serves on the Board of Directors of the Wireless Accessories Group (AMEX:XWG). He is also on the Board of Directors of the Marine Corps Reserve Toys for Tots Foundation.

REVEREND DONALD FRANCIS REILLY, O.S.A., a Director, holds a Doctorate in Ministry (Counseling) from New York Theological and an M.A. from Washington Theological Union as well as a B.A. from Villanova University. Reverend Don Reilly was ordained a priest in 1974. His assignments included Associate Pastor, Pastor at St. Denis, Havertown, Pennsylvania, Professor at Villanova University, Personnel Director of the Augustinian Province of St. Thomas of Villanova, Provincial Counselor, Founder of SILOAM Ministries where he ministers and counsels HIV/AIDS patients and caregivers. He is currently on the Board of Directors of Villanova University, is President of the board of "Bird Nest" in Philadelphia, Pennsylvania and is Board Member of Prayer Power. Fr. Reilly was recently elected Provincial of the Augustinian Order at Villanova, PA. He oversees more than 300 Augustinian Friars and their service to the Church, teaching at universities and high schools, ministering to parishes, serving as chaplain in the Armed Forces and hospitals, ministering to AIDS victims, and serving missions in Japan and South America.

MICHAEL C. MACDONALD, a Director, is a corporate officer and President of Global Accounts and Marketing Operations, for the Xerox Corporation. Mr. MacDonald's former positions at Xerox Corporation include executive positions in the sales and marketing areas. He is currently on the Board of Trustees of Rutgers University and a Director of the Jimmy V Foundation. Mr. MacDonald is the brother of Bradley T. MacDonald, the CEO of the Company.

GEORGE LAVIN, JR. ESQ., is a senior partner at Lavin, Oneil, Ricci, Ceprone & Disipio. Mr. Lavin is a 1951 graduate of Bucknell University. He attended the University of Pennsylvania School of Law, receiving an LL.B. in 1956, and then served as a Special Agent, Federal Bureau of Investigation, United States Department of Justice, until 1959. Mr. Lavin is one of the dominant product liability defense attorneys in the nation. He has had regional responsibilities in several automotive specialty areas, and has been called upon to try matters throughout the county on behalf of his clients. Mr. Lavin's present practice and specialty emphasizes his commitment to defending the automotive industry. Mr. Lavin is admitted to practice before the Supreme Court of Pennsylvania, the United States Court of Appeals for the Third Circuit and the United States District Courts for the Eastern and Middle Districts of Pennsylvania. He is a member of the Faculty Advisory Board of the Academy of Advocacy, the Association of Defense Counsel, The Defense Research Institute, The American Board of Trial Advocates, and the Temple University Law School faculty. He has also been elected a fellow of the American College of Trial Lawyers. On March 1, 1994, Mr.Lavin assumed the title of Counsel to The Firm.

MICHAEL J. MCDEVITT, a Director, is a retired FBI Special Agent with over 29 years of government service with the United States Marine Corps and the FBI. He had attained Senior Executive status within the FBI's Investigative Technology Branch and is currently providing consulting services, focusing on physical threat and risk assessments and conducting specialized training for law enforcement and US Government entities.

MARY T. TRAVIS, a Director, is currently employed with Sunset Mortgage Company, L.P. in Pennsylvania as the Senior Vice President of wholesale operations and was formerly the Vice President of operations for the Financial Mortgage Corporation. Mrs. Travis is an expert in mortgage banking with over 36 years of diversified experience. She is an approved instructor of the Mortgage Bankers Association Accredited School of Mortgage Banking. Mrs. Travis was also formally a delegate and 2nd Vice president of the Mortgage Bankers Association of Greater Philadelphia and the Board of Governors of the State of Pennsylvania. She is the key financial executive on the Company’s Audit Committee providing oversight of the Company’s external auditors.

REVEREND JOSEPH D. CALDERONE, O.S.A., a Director, is the Associate Director of Campus Ministry at Villanova University. He formerly spent over eight years with the Loyola University Medical Center as the hospital Chaplain and taught multiple courses including Introduction to the Practice of Medicine and Business Ethics. Rev. Calderone is currently a Captain in the US Navy Reserves and serves as the Wing Chaplain for the 4th Marine Aircraft Wing.

PART II

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

(a) The Company's Common Stock has been quoted under the symbol MED since December 20, 2002. The old symbol, MDFT, had been traded since February 5, 2001. The common stock is traded on the American Stock Exchange. The following is a list of the low and high closing prices by fiscal quarters for 2005 and 2004:

	2005	
	Low	High
Quarter ended March 31, 2005	2.67	3.62
Quarter ended June 30, 2005	2.82	3.30
Quarter ended September 30, 2005	3.01	7.08
Quarter ended December 31, 2005	3.83	5.70

	2004	
	Low	High
Quarter ended March 31, 2004	8.60	14.05
Quarter ended June 30, 2004	4.78	9.33
Quarter ended September 30, 2004	3.05	5.09
Quarter ended December 31, 2004	3.20	5.24

(b) The quotations reflect inter-dealer prices, without retail mark-up, markdown or commissions and may not represent actual transactions.

(c) There were approximately 7,112 record holders of the Company's Common Stock, as of December 31, 2005. The Company had no preferred holders of the Company's stock as of December 31, 2005.

(d) No dividends on common stock were declared by the Company during 2005 or 2004.

ITEM 6. SELECTED FINANCIAL DATA

The selected condensed consolidated financial data set forth below should be read in conjunction with "Management's Discussion and Analysis of Financial Condition and Results of Operations" included as Part II, Item 7 of this Annual Report on Form 10-K, and the consolidated financial statements and notes thereto of the company included in Part II Item 8 of this Annual Report on Form 10-K. The historical results provided below are not necessarily indicative of future results.

	(Restated) 2005	2004	2003	2002	2001
Revenue	40,129,000	27,340,000	25,379,000	12,345,000	5,022,000
Operating income	3,549,000	3,004,000	3,598,000	1,752,000	745,000
Income from continuing operations	3,405,000	2,906,000	3,558,000	1,698,000	566,000
EPS - basic	0.17	0.16	0.25	0.36	0.08
EPS - diluted	0.17	0.14	0.22	0.30	0.07
Total assets	30,120,000	25,968,000	24,230,000	9,888,000	3,357,000
current portion of long-term debt and revolving credit facilities	1,194,000	827,000	819,000	395,000	98,000
Total long-term debt	3,977,000	4,256,000	4,564,000	2,701,000	234,000
Weighted average shares outstanding					
Basic	12,258,734	10,832,360	9,305,731	6,722,505	6,524,969
Diluted	12,780,959	12,413,424	10,952,367	8,737,292	8,069,646

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

FORWARD LOOKING STATEMENTS

This document contains forward-looking statements which may involve known and unknown risks, uncertainties and other factors that may cause Medifast, Inc. actual results and performance in future periods to be materially different from any future results or performance suggested by these statements. Medifast, Inc. cautions investors not to place undue reliance on forward-looking statements, which speak only to management's expectations on this date.

2005 COMPARISON WITH 2004

OPERATING

Consolidated net sales for 2005 were $40,129,000 as compared to 2004 sales of $27,340,000, an increase of $12,789,000, or 47%. A major reason for the revenue increase for the Company is attributed to the continued success of direct sales to consumers as well as the expansion of the Take Shape for Life division. The increase in direct sales was attributed to an expanded direct marketing campaign via print, mail, web and television to drive customers to the call center and website. Through the effectiveness of our online ads and improved web branding a higher percentage of customers ordered on the Company’s website in 2005. In addition, the company expanded it remarketing campaign to drive new customers to the call center and website. The Take Shape for Life division added a Take Shape for Life replicating website option for Health Advisors, an Internet distribution program for their customers, and provided health advisors with additional sponsoring tools to make training and recruiting easier. These have proven to be effective at generating revenues and recruiting Health Advisors into the Take Shape for Life Network. The increased training and recruitment initiatives in 2005 have resulted in the expansion of the sales network into additional locations as well as growth in current locations.

Cost of sales increased from 6,746,000 in 2004 to $10,161,000 in 2005, an increase of $3,415,000. As a percentage of sales, cost of goods sold increased slightly due to increased fuel charges charged by the major shipping companies. Gross margin was 75% at December 31, 2005 and 2004.

Selling, general and administrative (SG&A) expenses of $26,419,000 for 2005 were $8,829,000 more than the $17,590,000 in 2004, due to increased costs associated with the increased scale of the business. The Company increased its advertising and marketing expense by approximately $3.2 million to include additional print and web advertising as well as strategic testing of television advertising. Salaries and benefits increased by approximately $1.1 million, Take Shape for Life commissions increased by $1.4 million due to the sales increase in the network, office expenses increased by approximately $750,000, operating expenses increased by approximately $1 million, and other general and administrative expenses, which included items such as depreciation, amortization, charitable contributions, and property taxes increased by approximately $1.4 million.

In 2005, the Company realized a tax expense of $1,002,000, as compared to a tax expense of $1,159,000 in 2004. The decrease in tax expense is due to timing differences between book and tax purposes for intangible assets, and other temporary and permanent differences. Interest expense increased to $317,000 in 2005, as compared to $245,000 in 2004. This increase was due to a full year of interest expense paid on a new loan acquired in 2004.

The Company reported net income of $2,112,000, or $0.17 per basic share ($0.17 per diluted share), versus $1,729,000 or $0.16 per basic share ($0.14 per diluted share), with a dilution increase of 368,000 shares. Earnings per share were effected by the interest associated with the conversion of the Series “B” preferred stock. This conversion included a $260,000 stock dividend on Series “B” preferred stock and a $19,000 stock dividend on Series “C” preferred stock. As of December 31, 2005 all Series “B” and Series “C” preferred stock have been converted to common stock and included in the weighed average diluted shares. There will be no additional stock dividend payments.

LIQUIDITY AND CAPITAL RESOURCES

At December 31, 2005, the Company had net working capital of $9,996,000, an increase of $2,531,000 from the $7,465,000 net working capital balance at December 31, 2004. Cash and investment securities at December 31, 2005 were $4,184,000. In November 2005, Medifast, Inc.’s wholly owned subsidiary Jason Pharmaceuticals, Inc. renewed its $5,000,000 Secured Line of Credit from Mercantile Safe-Deposit and Trust of Baltimore, Maryland. The line of credit is at LIBOR plus 1.3 percent. The increased line may be used to finance equipment, inventory, and receivables of Medifast, Inc. The Company currently has no off-balance sheet arrangements.

In the year ended December 31, 2005, the Company generated cash flow of $3,213,000 from operations, primarily attributable to higher operating income. This was offset by net changes in operating assets and liabilities that decreased cash flow by $2,065,000. The largest uses of cash were for the purchase of inventory and prepaid expenses, which primarily consisted of prepaid taxes, insurance, and advertising.

In the year ended December 31, 2005, net cash used in investing activities was $2,032,000, which primarily consisted of the purchase of intangible assets and purchases of property and equipment.

In the year ended December 31, 2005, net cash used in financing activities was $309,000, representing the principal repayments of long-term debt and purchase of treasury stock offset by an increase in the line of credit. Medifast, Inc. purchased 110,000 shares of its common stock from October 6, through October 17, 2005 at an average price of $4.03 per share, aggregating $452,000.

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

There are no current plans or discussions in process relating to any material acquisition that is probable in the foreseeable future.

2004 COMPARISON WITH 2003

OPERATING

Consolidated net sales for 2004 were $27,340,000 as compared to 2003 sales of $25,379,000, an increase of $1,961,000, or 8%. A major reason for the revenue increase for the Company is attributed to the continued success from the Take Shape for Life division, national advertising, the Hi-Energy acquisition and the redesigned website. The Take Shape for Life division added a Take Shape for Life replicating website option for Health Advisors, an Internet distribution program for their customers, as well as the new Tasting Party Program. These have proven to be effective at generating revenues and recruiting Health Advisors into the Take Shape for Life Network. The national advertising campaign included print, TV, radio, direct mail and web marketing. The Company increased its Internet sales in 2004 as compared to 2003, by redesigning its website and increasing its web marketing. The redesigned website created an easy to use shopping cart and a more user-friendly interface. The acquisition of Hi-Energy Weight Control Centers contributed to revenues throughout 2004.

Cost of sales decreased from $6,825,000 in 2003 compared to $6,746,000 in 2004, a decrease of $79,000. The decrease is attributed to decreases in costs through economies of scale.

Gross margins increased to 75% in 2004 from 73% in 2003. This was largely due to greater economies of scale as a result of the acquisition of the Company’s 119,000 square foot distribution facility thereby creating higher margins of the Medifast products through purchasing capabilities. The increase is also attributed to the increased margin of Medifast direct and Internet sales directly to patients via the Lifestyles and Take Shape for Life programs. Selling, general and administrative (SG&A) expenses of $17,590,000 for 2004 were $2,634,000 more than the $14,956,000 in 2003, due to increased advertising expenses to include television advertising, celebrity endorsements, expenses involved with starting and operating new corporately owned Hi-Energy Weight Control Clinic locations, the expansion of the Take Shape for Life commissioned sales organization, and overall corporate infrastructure improvements. The Company experienced income from operations for the year 2004 of $3,004,000. This compares with income from operations of $3,598,000 in 2003, a decrease of 17%.

In 2004, the Company realized a tax expense of $1,159,000, as compared to a tax expense of $1,148,000 in 2003 as a result of the elimination of the deferred tax asset and the net operating loss for income tax purposes. Interest expense increased to $245,000 in 2004, as compared to $154,000 in 2003. This increase was due to a complete year of additional debt, which was acquired in 2003.

A preferred stock dividend in the amount of $18,000 was expensed to shareholders in 2004.

LIQUIDITY AND CAPITAL RESOURCES

As of December 31, 2004, the Company had net working capital of $7,465,000, a decrease of $1,933,000 from the $9,398,000 net working capital balance at December 31, 2003. Cash and investment securities at December 31, 2004 were $3,238,000. On November 7, 2003 Medifast, Inc.'s wholly owned subsidiary Jason Pharmaceuticals, Inc. increased its Secured Line of Credit from $1,000,000 to $5,000,000 from Mercantile Safe-Deposit and Trust of Baltimore, Maryland. The line of credit is at LIBOR plus two percent. The increased line may be used to finance equipment, inventory, and receivables of Medifast, Inc. The Company currently has no off-balance sheet arrangements.

In the year ended December 31, 2004, the Company generated cash flow of $1,902,000 from operations, primarily attributable to higher operating income, non-cash expenditures for depreciation and amortization and purchases of inventory and the pay down of accounts payable and accrued expenses.

In the year ended December 31, 2004, net cash used in investing activities was $3,510,000, which primarily consisted of the purchase of intangible assets, purchase of property and equipment, and the purchase of a building.

In the year ended December 31, 2004, net cash used in financing activities was $304,000, representing the principal repayments of long-term debt.

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

There are no current plans or discussions in process relating to any material acquisition that is probable in the foreseeable future

On June 11, 2003 Jason Enterprises, Inc. acquired the assets of Consumers Choice Systems, Inc., a Delaware Corporation. The Company obtained all the assets of the business that support their retail and international business including the distribution rights in 18,000 retail food and drug stores. Jason Enterprises, Inc. acquired the assets for 76,120 shares of Medifast, Inc. restricted common stock and 50,000 five-year warrants at a purchase price of $10.00 per share. The transaction will be accounted for as an asset purchase transaction. The Company is expecting to record limited and selected liabilities that amount to approximately $1.35 million.

On July 25, 2003, the Company announced that it had sold an aggregate of 550,000 shares of common stock and warrants to purchase 82,500 shares of common stock (the "PIPE Shares") to Mainfield Enterprises, Inc. and Portside Growth & Opportunity Fund. The shares of common stock were sold for a cash consideration of $12.40 per share, or a total of $6,820,000, and the warrants, exercisable for a period of five years from the date of issuance, at an exercise price equal to one hundred fifteen percent (115%) of the five-day volume weighted average price (the "PIPE Transaction"), all pursuant to the terms of that certain Securities Purchase Agreement by and between the Company and Mainfield Enterprises, Inc. and Portside Growth & Opportunity Fund dated as of July 24, 2003 (the "Securities Purchase Agreement").

On September 12, 2003 Medifast, Inc.'s wholly owned subsidiary Seven Crondall, LLC purchased a 119,825 sq. foot distribution facility located at 601 Sunrise Ave., Ridgely, Maryland 21660 from New Roads, Inc. for $2,200,000. The Company financed $1,760,000 through Merrill Lynch Capital at the 30 day LIBOR interest rate plus 220 basis points over seven years.

On November 7, 2003 Medifast, Inc.'s wholly owned subsidiary Jason Properties, LLC purchased the assets of Hi-Energy Weight Control Centers, located in Gulf Breeze, Florida. The acquisition includes equipment, inventory, trademarks, and licenses for fifty Hi-Energy clinics. The clinics are located primarily in the southeastern region of the United States. The assets were purchased for $1,500,000 in cash, which included selected liabilities, capital expenditures, costs of assets and miscellaneous fees.

SEASONALITY

The Company's weight management products and programs have historically been subject to seasonality. Traditionally the holiday season in November/December of each year is considered poor for diet control products and services. January and February generally show increases in sales, as these months are considered the commencement of the "diet season." The Company did not experience the same degree of seasonality in 2005. This is largely due to the increase in the consumer's awareness of the overall health and nutritional benefits accompanied with the use of the Company's product line. As consumers continue to increase their association of nutritional weight loss programs with overall health, seasonality will continue to decrease.

INFLATION

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

INFORMATION SYSTEMS INFRASTRUCTURE

In November of 2005, the Company began an IT project to implement an Enterprise Resource Planning solution to upgrade our technology infrastructure and improve manufacturing and business processes. The new IT infrastructure will enable the Company to handle additional business growth and improve the efficiencies across the business platform. In addition, the Company is implementing new software for the Take Shape for Life direct selling network. The software will transform and empower Take Shape for Life's direct sales model by implementing the infrastructure, tools, and support critical to increasing competitive advantage, improving expansion and proliferation of the direct selling channel, facilitating support, success, and growth of the independent Health Advisor network, and meeting the evolving needs of Take Shape for Life's customers.

ITEM 8. FINANCIAL STATEMENTS.

See pages F-1 through F-27.

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

There were no disagreements with the Company's independent auditors, regarding accounting and financial disclosures for the fiscal year ending December 31, 2005.

ITEM 9A. CONTROLS AND PROCEDURES

(a) Evaluation of Disclosure Controls and Procedures

We have established disclosure controls and procedures to ensure that the information required to be disclosed by us in the reports that we file or submit under the Exchange Act is recorded, processed, summarized, evaluated and reported, as applicable, within the time periods specified in the rules and forms of the Securities and Exchange Commission.

In designing and evaluating the disclosure controls and procedures, management recognized that any controls and procedures, no matter how well designed and operated, can provide only reasonable assurance of achieving the desired control objectives, and management necessarily was required to apply its judgment in evaluating the cost-benefit relationship of possible controls and procedures.

In connection with the aforementioned restatement of our financial statements, under the supervision and with the participation of our management, including our principal executive officer and principal financial officer, we reevaluated, as of December 31, 2005, the effectiveness of the design and operation of our disclosure controls and procedures, as defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934, as amended (the "Act"). Based upon that reevaluation, as a result of a material weakness in internal control over financial reporting with respect to amortization expense of a customer list, our principal executive officer and principal financial officer have concluded that our disclosure controls and procedures were not effective to provide reasonable assurance that information required to be disclosed by us in the reports that we file or submit under the Act is (i) recorded, processed, summarized and reported, within the time periods specified in the Securities and Exchange Commission's rules and forms; and (ii) accumulated and communicated to our management, including our principal executive and principal financial officers, as appropriate to allow timely decisions regarding required disclosures. In connection with the Original Filing and prior to our discovery of the error relating to amortization expense on a customer list, our principal executive officer and principal financial officer had concluded that our disclosure controls and procedures were effective as of December 31, 2005 to a reasonable assurance level.

Changes in our Internal Control

There was no change in our internal control over financial reporting during the quarter ended December 31, 2005 that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

Code of Ethics

In September 2002, the Company implemented a Code of Ethics by which directors, officers and employees commit and undertake to personal and corporate growth, dedicate themselves to excellence, integrity and responsiveness to the marketplace, and work together to enhance the value of the Company for the shareholders, vendors, and customers.

Trading Policy

In March 2003, the Company implemented a Trading Policy whereby if a director, officer or employee has material non-public information relating to the Company, neither that person nor any related person may buy or sell securities of the Company or engage in any other action to take advantage of, or pass on to others, that information. Additionally, insiders may purchase or sell MED securities if such purchase or sale is made within 30 business days after an earnings or special announcement to include the 10-K, 10-Q and 8-K in order to insure that investors have available the same information necessary to make investment decisions as insiders.

PART III

ITEM 10. DIRECTORS AND EXECUTIVE DIRECTORS OF REGISTRANT

Information pertaining to directors and executive officers of the Company and the Company’s Code of Conduct are incorporated herein by reference to the Company’s Proxy Statement to be filed with the Securities and Exchange Commission within 120 days after the end of the year covered by this Form 10-K with respect to the Annual Meeting of Stockholders to be held on September 8, 2006.

ITEM 11. EXECUTIVE COMPENSATION.

The following table sets forth information as to the compensation of the Chief Executive Officer of the Company and each other executive officer that received compensation in excess of $100,000 for 2005, 2004, and 2003.

Annual Compensation

Name	Year	Salary ($)	Bonus ($)	Value of Common/ Preferred Stock Issued in Lieu of Cash	Option Awards	Other Annual Compensation
Bradley T. MacDonald	2005	225,000	0	0	40,000	100,000
Chairman of the Board	2004	225,000	0	0	0	0
& CEO	2003	225,000	112,000	0	0	0

Annual Compensation

Name	Year	Salary ($)	Bonus ($)	Value of Common/ Preferred Stock Issued in Lieu of Cash ($)	Option Awards	Other Annual Compensation
Leo V. Williams, III	2005	125,000		12,000	10,000	0
Executive Vice President	2004	118,000	0	0	10,000	0

STOCK OPTIONS

The Company's 1993 Employee Stock Option Plan (the "Plan"), as amended in July 1995, December 1997, June 2002, and again in July 2003 authorizes the issuance of options for 1,250,000 shares of Common Stock. The Plan authorizes the Board of Directors or the Compensation Committee appointed by the Board to grant incentive stock options and non-incentive stock options to officers, key employees, directors, and independent consultants, with directors who are not employees and consultants eligible only to receive non-incentive stock options. Employee stock options are vested over 2 years.

* The following tables set forth pertinent information as of December 31, 2005 with respect to options granted under the Plan since its inception to the persons set forth under the Summary Compensation Table, all current executive officers as a group and all current Directors who are not executive officers as a group of the Company. In addition, a chart listing option holders, grants made in FY 2005, and a list of aggregated options and the value of these options, is provided.

	BRADLEY T. MACDONALD (1)	ALL CURRENT EXECUTIVE OFFICERS AS A GROUP	ALL CURRENT INDEPENDENT DIRECTORS AS A GROUP
Options granted	255,000	210,000	110,000
Average exercise price	$ 0.86	$ 2.20	$ 1.07
Options exercised	228,333	49,999	100,000
Average exercise price	$ 0.97	$ 0.88	$ 0.70
Shares sold	*	*	*
Options unexercised as of 12/31/05	0	160,001	10,000

	FY 05 Grants @ Price & Expiration Month/Year	Approximate 5 YR Potential Realizable Value at 10% Annual Stock Appreciation	Unexercised Options as of 12/31/05	Value of Unexercised Options as of 12/31/05
Current Executive Officers and Directors	135,000@$2.67 2010	$ 4.30	135,000	$ 0
Employees	158,333@$2.69 2010	$ 4.33	71,666	0
Consultants	0		0	0
			206,966	$ 0

20

Nutraceutical Group Industry Comparison of Stock Prices

Company	December 31, 2005 Stock Price	December 31, 2004 Stock Price	$ Change	% Change
Medifast (MED)	$ 5.24	$ 3.52	1.72	48.9%
Natural Alternatives International, Inc. (NAII)	6.48	9.23	(2.75)	(29.8)%
Weider Nutrition (WNI)	5.09	4.35	.74	17.0%
Natures Sunshine Products, Inc. (NATR)	18.08	20.36	(2.28)	(11.2)%

Company	December 31, 2005 Stock Price	December 31, 2000 Stock Price	$ Change	% Change
Medifast (MED)	$ 5.24	$ .14	5.10	3642%
Natural Alternatives International, Inc. (NAII)	6.48	2.19	4.29	196%
Weider Nutrition (WNI)	5.09	2.12	2.97	140%
Natures Sunshine Products, Inc. (NATR)	18.08	6.81	11.27	165%

Index Comparison

$100 invested in 2000 would return:

	2000	2005
Nutraceutical Group Index	$ 100	$ 1,136
Medifast	$ 100	$ 3,740

Factual material is obtained from sources believed to be reliable, but the publisher is not responsible for any errors or omissions contained herein.

COMPENSATION OF DIRECTORS

The Company is authorized to pay a fee of $300 for each meeting attended by its Directors who are not executive officers. It reimburses those who are not employees of the Company for their expenses incurred in attending meetings. Independent Directors claimed a total of $56,400 in Director's fees and/or expenses in 2005. See "Executive Compensation - Stock Options" for stock options granted under the 1993 Plan to the Directors.

ITEM 12. SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT.

The following table sets forth information with respect to the beneficial ownership of shares of Common Stock or voting Preferred Stock as of December 31, 2005 of the Chief Executive Officer, each Director, each nominee for Director, each current executive officer named in the Summary Compensation Table under "Executive Compensation" and all executive officers and Directors as a group. The number of shares beneficially owned is determined under the rules of the Securities and Exchange Commission and the information is not necessarily indicative of beneficial ownership for any other person. Under such rules, "beneficial ownership" includes shares as to which the undersigned has sole or shared voting power or investment power and shares, which the undersigned has the right to acquire within 60 days of March 15, 2006 through the exercise of any stock option or other right. Unless otherwise indicated, the named person has sole investment and voting power with respect to the shares set forth in the table.

NAME AND ADDRESS*	NUMBER OF SHARES	% OF OUTSTANDING
Bradley T. MacDonald	1,304,479 (1)	10.2%
Donald F. Reilly	72,452	0.6%
Michael C. MacDonald	53,419	0.4%
Mary Travis	17,000	0.1%
Michael J. McDevitt	22,900	0.2%
Joseph Calderone	6,500	0.1%
Executive Officers and Directors as a group (9 persons)	1,495,250	11.7%

*The address is c/o Medifast, Inc., 11445 Cronhill Drive, Owings Mills, Maryland 21117

(1) Mr. MacDonald beneficially owns 1,304,479 shares of common stock. Mrs. Shirley D. MacDonald and Ms. Margaret E. MacDonald, wife and daughter of Mr. MacDonald, individually or jointly own 716,332 shares of stock.

22

PART IV

ITEM 14. EXHIBITS AND REPORTS ON FORM 8-K.

(a) Exhibits

3.1	Certificate of Incorporation of the Company and amendments thereto*
3.2	By-Laws of the Company*
10.1	1993 Stock Option Plan of the Company as amended*
10.3	Lease relating to the Company's Owings Mills, Maryland facility**
10.4	Employment agreement with Bradley T. MacDonald***

---

* Filed as an exhibit to and incorporated by reference to the Registration Statement on Form SB-2 of the Company, File No. 33-71284-NY.

** Filed as an exhibit to and incorporated by reference to the Registration Statement on Form S-4 of the Company, File No. 33-81524.

*** Filed as an exhibit to 10KSB, dated April 15, 1999 of the Company, file No. 000-23016.

(b) Reports on Form 8-K

September 21, 2005 to report the Annual Meeting of Shareholders September 16, 2005

October 19, 2005, to report the repurchase of 110,000 shares of common stock

January 17, 2006, to report the sale of Consumer Choice Systems assets, the promotion of Michael S. McDevitt to Chief Financial Officer, and 2006 financial guidance

ITEM 14. ACCOUNTING FEES

In 2005, the Company incurred $90,000 in accounting fees as compared to $70,000 in 2004. These fees include work performed on quarterly audits and the preparation of the Company’s 10-Q’s and 10-K. Tax fees in 2005 and 2004 were $10,000.

SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) 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.

MEDIFAST, INC.
(Registrant)

BRADLEY T. MACDONALD

Bradley T. MacDonald
Chairman, CEO
Dated: September 6, 2007

Pursuant to the requirements of the Securities Exchange Act of 1934, the following persons on behalf of the Registrant and in the capacities and on the dates indicated have signed this Report below.

Name	Title	Date
/s/ BRADLEY T. MACDONALD Bradley T. MacDonald	Chairman of the Board, Director, Chief Executive Officer	September 6, 2007
/s/ GEORGE LAVIN George Lavin	Director	September 6, 2007
/s/ MICHAEL C. MACDONALD Michael C. MacDonald	Director	September 6, 2007
/s/ MARY T. TRAVIS Mary T. Travis	Director	September 6, 2007
/s/ REV. DONALD F. REILLY, OSA Rev. Donald F. Reilly, OSA	Director	September 6, 2007
/s/ MICHAEL J. MCDEVITT Michael J. McDevitt	Director	September 6, 2007
/s/ JOSEPH D. CALDERONE Joseph D. Calderone	Director	September 6, 2007

24

Index to Exhibits

Exhibit Number	Description of Exhibit
31.1	Certification of Chief Executive Officer pursuant to Item 601(b)(31) of Regulation S-K, as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
31.2	Certification of Chief Financial Officer pursuant to Item 601(b)(31) of Regulation S-K, as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
32.1	Certification of Chief Executive Officer and Chief Financial Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002

MEDIFAST, INC. AND SUBSIDIARIES
CONTENTS

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

Board of Directors and Stockholders
Medifast, Inc.
Owings Mills, Maryland

We have audited the accompanying consolidated balance sheets of Medifast, Inc. and subsidiaries as of December 31, 2005 and 2004, and the related consolidated statements of income, stockholders equity and accumulated other comprehensive income, and cash flow for each of the three years in the period ended December 31, 2005. These consolidated financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

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

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the consolidated financial position of Medifast, Inc. and subsidiaries as of December 31, 2005 and 2004, and the consolidated results of their operations and their consolidated cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

As discussed in Note R to the consolidated financial statements, the accompanying consolidated financial statements have been restated to correct the Company’s accounting for amortization expense on a customer list.

Bagell, Josephs, Levine & Company, LLC

Gibbsboro, New Jersey
March 2, 2006, except
for Note R as to which the
date is September 6, 2007

MEDIFAST, INC. AND SUBSIDIARIES
CONSOLIDATED BALANCE SHEETS
As of December 31, 2005 and 2004

	(Restated) 2005	2004
ASSETS		
Current assets:		
Cash	$ 1,484,000	$ 612,000
Accounts receivable-net of allowance for doubtful accounts of $100,000 and $87,000	984,000	1,063,000
Inventory	5,475,000	4,251,000
Investment securities	2,700,000	2,626,000
Deferred compensation	525,000	321,000
Prepaid expenses and other current assets	3,273,000	1,079,000
Current portion of deferred tax asset	-	19,000
Total current assets	**14,441,000**	**9,971,000**
Property, plant and equipment - net	9,535,000	8,698,000
Trademarks and intangibles - net	5,984,000	7,138,000
Deferred tax asset, net of current portion	100,000	91,000
Other assets	60,000	70,000
TOTAL ASSETS	**$ 30,120,000**	**$ 25,968,000**
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current liabilities:		
Accounts payable and accrued expenses	$ 2,263,000	$ 940,000
Income taxes payable	899,000	674,000
Dividends payable	-	65,000
Line of credit	633,000	369,000
Current maturities of long-term debt	561,000	458,000
Deferred tax liability - current	90,000	-
Total current liabilities	**4,446,000**	**2,506,000**
Other liabilities and deferred credits		
Long-term debt, net of current portion	3,977,000	4,256,000
Deferred tax liability - non-current	-	-
Total liabilities	**8,423,000**	**6,762,000**
Stockholders' Equity:		
Series B Convertible Preferred Stock; par value $1.00; 600,000 shares authorized; 0 and 300,614 shares issued and outstanding	-	301,000
Series C Convertible Preferred Stock; stated value $1.00; 1,015,000 shares authorized; 0 and 200,000 shares issued and outstanding	-	200,000
Common stock; par value $.001 per share; 20,000,000 shares authorized; 12,782,791 and 11,001,070 shares issued and outstanding	13,000	11,000
Additional paid-in capital	21,759,000	20,556,000

Accumulated other comprehensive income (loss)		282,000		(39,000)
Retained earnings (deficit)		825,000		(1,287,000)
		22,879,000		**19,742,000**
Less: cost of 210,902 and 78,160 shares of common stock in treasury		(1,075,000)		(536,000)
Less: Unearned compensation		(107,000)		
Total stockholders' equity		**21,697,000**		**19,206,000**
TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY	**$**	**30,120,000**	**$**	**25,968,000**

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

MEDIFAST, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF INCOME
Years Ended December 31,

	(Restated) 2005	2004	2003
Revenue	$ 40,129,000	$ 27,340,000	$ 25,379,000
Cost of sales	(10,161,000)	(6,746,000)	(6,825,000)
Gross profit	**29,968,000**	**20,594,000**	**18,554,000**
Selling, general, and administration	(26,419,000)	(17,590,000)	(14,956,000)
Income from operations	**3,549,000**	**3,004,000**	**3,598,000**
Other income (expense):			
Interest expense	(317,000)	(245,000)	(150,000)
Interest income	158,000	154,000	110,000
Other income (expense)	15,000	(7,000)	-
	(144,000)	(98,000)	(40,000)
Net income before provision for income taxes	**3,405,000**	**2,906,000**	**3,558,000**
Provision for income taxes	(1,002,000)	(1,159,000)	(1,148,000)
Net income	**2,403,000**	**1,747,000**	**2,410,000**
Less: Preferred stock dividend requirement	(291,000)	(18,000)	(58,000)
Net income attributable to common shareholders	**$ 2,112,000**	**$ 1,729,000**	**$ 2,352,000**
Basic earnings per share	$ 0.17	$ 0.16	$ 0.25
Diluted earnings per share	$ 0.17	$ 0.14	$ 0.22
Weighted average shares outstanding -			
Basic	12,258,734	10,832,360	9,305,731
Diluted	12,780,959	12,413,424	10,952,367

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

MEDIFAST, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENT OF CHANGES IN STOCKHOLDERS' EQUITY AND ACCUMULATED OTHER COMPREHENSIVE INCOME (LOSS)
Years Ended December 31, 2005, 2004, and 2003

	Series B Preferred Stock		Series C Preferred Stock		(Restated) Common Stock			
	Number of Shares	Stated Value Amount	Number of Shares	Stated Value Amount	Number of Shares	Par Value $0.00 Amount	Additional Paid-In Capital	Retained Earnings (deficit)
Balance, December 31, 2002	521,290	$ 521,000	985,000	$ 985,000	7,204,693	$ 7,000	$ 9,613,000	$ (5,381,000)
Preferred converted to Common Stock	(117,556)	(117,000)	(718,000)	(718,000)	1,671,108	2,000	833,000	
Options exercised to Common Stock					615,714		590,000	
Warrants Converted to Common Stock					288,724		350,000	
Common Stock issued to Directors, consultants, and acquisitions					665,970	1,000	8,716,000	
Common Stock issued for Series "C" dividend					36,400		18,000	
Dividend paid in stock								(45,000)
Net Income								2,410,000
Balance, December 31, 2003	403,734	404,000	267,000	267,000	10,482,609	10,000	20,120,000	(3,016,000)
Preferred converted to Common Stock	(103,120)	(103,000)	(67,000)	(67,000)	340,240		170,000	
Options exercised to Common Stock					47,221	1,000	34,000	
Warrants Converted to Common Stock					46,700		125,000	
Conversion of debt to equity					55,400		28,000	
Conversion of debt to equity							114,000	

out of Treasury								
Common stock issued to Consultants					15,500		93,000	
Shares issued out of Treasury							(135,000)	
Common Stock issued for Series “C” dividend					13,400		7,000	(7,000)
Dividend paid in stock								(11,000)
Net Income								1,747,000
Balance, December 31, 2004	300,614	301,000	200,000	200,000	11,001,070	11,000	20,556,000	(1,287,000)
Preferred converted to Common Stock	(300,614)	(301,000)	(200,000)	(200,000)	1,001,228	1,100	500,000	
Warrants Converted to Common Stock					2,000	-	2,000	
Options excercised to common stock					138,335	100	190,000	
Common Stock issued for Series “C” dividend					38,000	-	19,000	(19,000)
Dividend paid in stock								(11,000)
Common stock issued for Series “B” dividend					521,158	600	260,000	(261,000)
Common stock issued to Employees					81,000	100	271,000	
Treasury shares issued to employees						100	(39,000)	
Shares issued to officer with two year vesting period								
Treasury shares repurchased								
Net income								2,403,000
Balance, December 31,	0	$ 0	0	$ 0	12,782,791	$ 13,000	$ 21,759,000	$ 825,000

2005

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

MEDIFAST, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CHANGES IN STOCKHOLDERS' EQUITY AND ACCUMULATED OTHER COMPREHENSIVE INCOME (LOSS) – (CONTINUED)
Years Ended December 31, 2005, 2004, and 2003

		Common Stock		
	Accumulated other comprehensive income (loss)	(Restated) Total	Treasury Stock	Unearned Compensation
Balance, December 31, 2002	$ -	$ 5,745,000	$ (167,000)	-
Preferred converted to Common Stock				
Options exercised to Common Stock		590,000	(516,000)	
Warrants Converted to Common Stock		350,000		
Common Stock issued to Directors, consultants and acquisitions	8,717,000			
Common Stock issued for Series "C" dividend		18,000		
Dividend paid in stock		(45,000)		
Net Income	(25,000)	2,385,000		
Balance, December 31, 2003	(25,000)	17,760,000	(683,000)	-
Preferred converted to Common Stock				
Options exercised to Common Stock		35,000	(31,000)	
Warrants Converted to Common Stock		125,000	(123,000)	
Conversion of debt to equity		28,000		
Conversion of debt to equity out of Treasury		114,000	166,000	
Common stock issued to Consultants		93,000	135,000	
Shares issued out of Treasury		(135,000)	135,000	
Common Stock issued for Series "C" dividend				
Dividend paid in stock		(11,000)		
Net Income	(14,000)	1,733,000		
Balance, December 31, 2004	(39,000)	19,742,000	(536,000)	-
Preferred converted to Common Stock			(124,000)	
Warrants Converted to Common Stock		2,000		
Options excercised to common stock		190,000		
Common Stock issued for Series "C" dividend				
Dividend paid in stock		(11,000)		

Common stock issued for Series “B” dividend				
Common stock issued to Employees		271,000		
Treasury shares issued to employees		(39,000)	38,000	
Shares issued to officer with two year vesting period				(122,000)
Vesting of unearned compensation				15,000
Treasury shares repurchased			(453,000)	
Net income	321,000	2,724,000		
Balance, December 31, 2005	$ 282,000	$ 22,879,000	$ (1,075,000)	$ (107,000)

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

MEDIFAST, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CASH FLOW
Years Ended December 31,

	(Restated) 2005	2004	2003
Cash flows from Operating Activities:			
Net income	$ 2,403,000	$ 1,747,000	$ 2,410,000
Adjustments to reconcile net income to net cash provided by operating activities from operations:			
Depreciation and amortization	2,266,000	1,210,000	648,000
Realized (gain) loss on investment securities	10,000	19,000	(1,000)
Common stock issued for services	150,000	93,000	207,000
Vesting of unearned compensation	15,000	-	-
Net change in other accumulated comprehensive income (loss)	321,000	(14,000)	-
Provision for bad debts	13,000	-	-
Deferred income taxes	100,000	486,000	1,138,000
Changes in Assets and Liabilities:			
Decrease (increase) in accounts receivable	65,000	(422,000)	(357,000)
(Increase) in inventory	(1,225,000)	(1,263,000)	(1,729,000)
(Increase) in prepaid expenses and other current assets	(2,194,000)	(143,000)	(687,000)
(Increase) in deferred compensation	(204,000)	-	(321,000)
Decrease (increase) in other assets	10,000	(25,000)	44,000
Increase (decrease) in accounts payable and accrued expenses	1,323,000	(460,000)	525,000
Increase in income taxes payable	160,000	674,000	-
Net cash provided by operating activities	3,213,000	1,902,000	1,877,000
Cash Flows from Investing Activities:			
Sale (purchase) of investment securities, net	(84,000)	1,338,000	(3,564,000)
Purchase of building	-	(566,000)	(1,823,000)
Purchase of property and equipment	(1,672,000)	(1,490,000)	(1,309,000)
Purchase of intangible assets	(276,000)	(2,792,000)	(2,458,000)
Net cash (used in) investing activities	(2,032,000)	(3,510,000)	(9,154,000)
Cash Flows from Financing Activities:			
Issuance of common stock, options and warrants	66,000	7,000	6,722,000
Increase (decrease) in line of credit, net	561,000	314,000	(36,000)
Purchase of treasury stock	(452,000)	-	-
Proceeds from long-term debt	-	475,000	2,669,000
Principal repayments of long-term debt	(473,000)	(1,089,000)	(346,000)
Dividends paid on preferred stock	(11,000)	(11,000)	(45,000)
Net cash provided by (used in) financing activities	(309,000)	(304,000)	8,964,000
NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS	872,000	(1,912,000)	1,687,000

Cash and cash equivalents - beginning of the year		612,000		2,524,000		837,000
Cash and cash equivalents - end of year	$	1,484,000	$	612,000	$	2,524,000
Supplemental disclosure of cash flow information:						
Interest paid	$	317,000	$	245,000	$	154,000
Income taxes	$	1,983,000	$	-	$	-
Supplemental disclosure of non cash activity:						
Conversion of preferred stock B and C to common stock	$	501,000	$	170,000	$	835,000
Common stock for services	$	150,000	$	93,000	$	207,000
Common stock for intangibles and fixed assets	$	-	$	-	$	1,949,000
Conversion of debt to equity	$	-	$	307,000	$	-
Preferred B and C Stock Dividends	$	287,000	$	7,000	$	18,000
Line of credit converted to long-term debt	$	369,000	$	-	$	-
Common stock issued for compensation to be earned upon vesting	$	122,000	$	-	$	-

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

F-7

MEDIFAST, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
DECEMBER 31, 2005, 2004, AND 2003

NOTE A – BUSINESS

Medifast, Inc. (the "Company", or "Medifast") is a Delaware corporation, incorporated in 1980. The Company's operations are primarily conducted through five of its wholly owned subsidiaries, Jason Pharmaceuticals, Inc. ("Jason"), Take Shape for Life, Inc. ("TSFL"), Jason Enterprises, Inc., Jason Properties, LLC and Seven Crondall, LLC. The Company is engaged in the production, distribution, and sale of weight management and disease management products and other consumable health and diet products. Medifast, Inc.'s product lines include weight and disease management, meal replacement and sports nutrition products manufactured in a modern, FDA approved facility in Owings Mills, Maryland.

The Company is engaged in the manufacturing and distribution of Medifastâ and Hi-Energyâ branded and private label weight and disease management products. These products are sold through various channels of distribution, to include web, call center, independent health advisors, medical professionals, weight loss clinics, direct consumer marketing supported via the phone and the web. The processing, formulation, packaging, labeling and advertising of the Company's products are subject to regulation by one or more federal agencies, including the Food and Drug Administration, the Federal Trade Commission, the Consumer Product Safety Commission, the United States Department of Agriculture, and the United States Environmental Protection Agency.

NOTE B - SIGNIFICANT ACCOUNTING POLICIES

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

[1] PRINCIPLES OF CONSOLIDATION AND BASIS OF PRESENTATION:

The consolidated financial statements include the accounts of the Company and its wholly owned subsidiaries, Jason Pharmaceuticals, Inc., Take Shape For Life, Inc., Seven Crondall Associates, LLC, Jason Properties, LLC and Jason Enterprises, Inc. All inter-company accounts have been eliminated.

[2] CASH AND CASH EQUIVALENTS:

For the purposes of the consolidated statements of cash flow, the Company considers all highly liquid debt instruments purchased with maturity of three months or less to be cash equivalents. At December 31, 2005, the Company had $789,000 in a money market account, $365,000 in miscellaneous short-term investments through Merrill Lynch that are considered cash equivalents due to terms of maturity, and $330,000 in operating checking accounts.

At December 31, 2004, the Company had invested in four $100,000 certificates of deposit, of which three were considered cash equivalents. In 2005, all certificates of deposit matured and were rolled into a money market account.

MEDIFAST, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
DECEMBER 31, 2005, 2004, AND 2003

NOTE B - SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

[3] ACCOUNTS RECEIVABLE AND ALLOWANCE FOR DOUBFUL ACCOUNTS

Accounts receivable are recorded net of reserves for sales returns and allowances, and net of provisions for doubtful accounts. Allowances for sales returns and discounts are based on an analysis of historical trends, and allowances for doubtful accounts are based primarily on an analysis of aging accounts receivable balances and on the creditworthiness of the customer as determined by credit checks and analysis, as well as the customer's payment history.

[4] INVENTORY:

Inventory is stated at the lower of cost or market, utilizing the first-in, first-out method. The cost of finished goods includes the cost of raw materials, packaging supplies, direct and indirect labor and other indirect manufacturing costs.

[5] ADVERTISING:

Advertising costs such as preparation, layout, design and production of advertising are deferred. They are expensed when the advertisement is first used, except for the costs of executory contracts, which are amortized as performance under the contract is received. Advertising costs deferred at December 31, 2005 and 2004, were $585,000 and $478,000 respectively. Advertising expense for the years ended December 31, 2005 and 2004 amounted to $3,784,000 and $1,055,000, respectively.

[6] PROPERTY, PLANT AND EQUIPMENT:

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

Building and building improvements	39 years
Equipment and fixtures	3 - 15 years
Vehicles	5 years

The carrying amount of all long-lived assets is evaluated periodically to determine whether adjustment to the useful life or to the unamortized balance is warranted. Such evaluation is based principally on the expected utilization of the long-lived assets and the projected undiscounted cash flows of the operations in which the long-lived assets are used.

In accordance with SFAS No. 144, "Long-Lived Assets", property, plant and equipment and other long-lived assets are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. Recoverability of assets to be held and used is measured by a comparison of the carrying amount of an asset to estimated undiscounted future cash flows expected to be generated by the asset. If the carrying amount of an asset exceeds its estimated future cash flows, an impairment charge is recognized by the amount by which the carrying amount of the asset exceeds the fair value of the asset.

MEDIFAST, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
DECEMBER 31, 2005, 2004, AND 2003

NOTE B - SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

[7] INCOME TAXES:

The Company accounts for income taxes in accordance with Statements of Financial Accounting Standards No. 109, “Accounting for Income Taxes,” which requires an asset and liability approach to financial accounting and reporting for income taxes. Deferred income taxes and liabilities are computed annually for differences between the financial statement and the tax basis of assets and liabilities that will result in taxable or deductible amounts in the future based on enacted tax laws and rates applicable to the periods in which the differences are expected to affect taxable income. Valuation allowances are established when necessary to reduce deferred tax assets to the amount expected to be realized.

[8] EARNINGS PER COMMON SHARE:

Basic earnings per share is calculated by dividing net profit attributable to common stockholders by the weighted average number of outstanding common shares during the year. Basic earnings per share exclude any dilutive effects of options, warrants and other stock-based compensation, which are included in diluted earnings per share.

[9] REVENUE:

Revenue is recognized net of discounts, rebates, promotional adjustments, price adjustments, returns and other potential adjustments upon shipment and passing of risk to the customer and when estimates of are reasonably determinable, collection is reasonably assured, and the Company has no further performance obligations.

MEDIFAST, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
DECEMBER 31, 2005, 2004, AND 2003

NOTE B - SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

[10] ESTIMATES:

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

[11] FAIR VALUE OF FINANCIAL INSTRUMENTS:

The carrying amounts reported in the consolidated balance sheets for cash, certificates of deposit, accounts receivable, accounts payable and accrued liabilities approximate fair value because of the immediate or short-term maturity of the financial instruments.

The Company believes that its indebtedness approximates fair value based on current yields for debt instruments with similar terms.

[12] CONCENTRATION OF CREDIT RISK:

Financial instruments that potentially subject the Company to credit risk consist of cash, certificates of deposit, investment securities and trade receivables. Cash, money markets and investments exceed the federal insurance coverage by $2,248,000 and $3,525,000, respectively. The Company securities at December 31, 2005 and 2004, include amounts deposited with multiple financial institutions markets its products primarily to medical professionals, clinics, and Internet medical sales and has no substantial concentrations of credit risk in its trade receivables.

As of December 31, 2005 and 2004, the Company had two customers that individually represented over 10% of the accounts receivable and in the aggregate, approximately 36% and 49% of the accounts receivable, respectively.

[13] STOCK-BASED COMPENSATION:

The Company has adopted Statement of Financial Accounting Standards No. 123, “Accounting for Stock Based Compensation” (“SFAS 123”). The provisions of SFAS 123 allow companies to either expense the estimated value of stock options or to continue to follow the intrinsic value method set forth in Accounting Principles Bulletin Opinion No. 25, “Accounting for Stock Issued to Employees” (“APB 25”), but disclose the pro forma effects on net income (loss) had the fair value of the options been expensed. The Company has elected to continue to apply APB 25 in accounting for its employee stock option incentive plans. Under APB 25, where the exercise price of the Company’s employee stock options equals the market price of the underlying stock on the date of grant, no compensation is recognized.

MEDIFAST, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
DECEMBER 31, 2005, 2004, AND 2003

NOTE B - SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

STOCK OPTION PLAN

On October 9, 1993 and as amended in May 1995, the Company adopted a stock option plan ("Plan") authorizing the grant of incentive and nonincentive options for an aggregate of 500,000 shares of the Company's common stock to officers, employees, directors and consultants. Incentive options are to be granted at fair market value. Options are to be exercisable as determined by the stock option committee.

In November 1997, June 2002 and July 2004, the Company amended the Plan by increasing the number of shares of the Company's common stock subject to the Plan by an aggregate of 200,000 shares, 300,000 shares and 250,000 shares respectively.

The Company has elected to continue to account for stock option grants in accordance with APB 25 and related interpretations. Under APB 25, where the exercise price of the Company's employee stock options equals the market price of the underlying stock on the date of grant, no compensation is recognized.

If compensation expense for the Company's stock-based compensation plans had been determined consistent with SFAS 123, the Company's net income and net income per share including pro forma results would have been the amounts indicated below:

	Years Ended December 31		
	2005 (Restated)	2004	2003
Net income:			
As reported	2,403,000	1,747,000	2,410,000
Total stock-based employee compensation expense determined under fair value based method for all awards, net of related tax effects	(280,000)	(108,000)	(403,000)
Pro forma	2,123,000	1,639,000	2,007,000
Net income per share:			
as reported:			
Basic	$ 0.17	$ 0.16	$ 0.25
Diluted	$ 0.17	$ 0.14	$ 0.22
Pro forma:			
Basic	$ 0.17	$ 0.15	$ 0.21
Diluted	$ 0.17	$ 0.13	$ 0.18

MEDIFAST, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
DECEMBER 31, 2005, 2004, AND 2003

[13] STOCK-BASED COMPENSATION: (CONTINUED)

The pro forma effect on net income may not be representative of the pro forma effect on net income of future years due to, among other things: (i) the vesting period of the stock options and the (ii) fair value of additional stock options in future years.

For the purpose of the above table, the fair value of each option granted is estimated as of the date of grant using the Black-Scholes option-pricing model with the following assumptions:

	2005	2004	2003
Dividend yield	0.0%	0.0%	0.0%
Expected volatility	0.70	0.40	0.40
Risk-free interest rate	4.50%	4.50%	3% - 5%
Expected life in years	1-5	1-5	1-5

The weighted average fair value at date of grant for options granted during the years 2005, 2004, and 2003 were $2.64, $8.60, and 5.32, respectively, using the above assumptions.

The following summarizes the stock option activity for the years ended December 31:

	2005		2004		2003	
	Shares	Weighted Average Exercise Price	Shares	Weighted Average Exercise Price	Shares	Weighted Average Exercise Price
Outstanding at beginning of year	389,397	1.51	439,455	1.76	891,669	0.69
Options granted	333,333	2.64	30,000	8.60	163,500	5.32
Options reinstated	-	0.00	-	0.00	-	0.00
Options exercised	(138,335)	(1.83)	(47,221)	(1.19)	(615,714)	(1.16)
Options forfeited or expired	(299,668)	(1.17)	(32,837)	(7.01)	0	0.00
Outstanding at end of year	284,727	2.41	389,397	1.51	439,455	1.76
Options exercisable at year end	254,725	3.17	350,336	1.11	302,668	0.76
Options available for grant at end of year	965,273		860,603		810,545	

MEDIFAST, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
DECEMBER 31, 2005, 2004, AND 2003

NOTE B - SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

[13] STOCK-BASED COMPENSATION: (CONTINUED)

The following table summarizes information about stock options outstanding and exercisable at December 31, 2005:

	Options Outstanding			Options Exercisable	
Range of Exercise Prices	Number Outstanding	Weighted Average Contractual Life Remaining (in Years)	Weighted Average Exercise Price	Number Exercisable	Weighted Average Exercise Price
$0.25	6,669	1.0	$ 0.25	6,669	$ 0.25
$0.32	3,334	.40	$ 0.32	3,334	$ 0.32
$0.80	16,666	1.5	$ 0.80	16,666	$ 0.80
$2.67	178,334	4.1	$ 2.67	178,334	$ 2.67
$3.83	40,000	4.8	$ 3.83	13,332	$ 3.83
$4.80	19,724	2.3	$ 4.80	19,724	$ 4.80
$8.60	10,000	3.0	$ 8.60	6,666	$ 8.60
$11.15	10,000	2.5	$ 11.15	10,000	$ 11.15
	284,727		$ 2.41	254,725	$ 3.17

F-14

MEDIFAST, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
DECEMBER 31, 2005, 2004, AND 2003

NOTE B - SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

[15] RECENT ACCOUNTING PRONOUNCEMENTS

In December 2004, the FASB issued Financial Accounting Standards No. 123 (revised 2004) (FAS 123R), "Share-Based Payment, " FAS 123R replaces FAS No. 123, "Accounting for Stock-Based Compensation", and supersedes APB Opinion No. 25, "Accounting for Stock Issued to Employees." FAS 123R requires compensation expense, measured as the fair value at the grant date, related to share-based payment transactions to be recognized in the financial statements over the period that an employee provides service in exchange for the award. The Company intends to adopt FAS 123R using the "modified prospective" transition method as defined in FAS 123R. Under the modified prospective method, companies are required to record compensation cost prospectively for the unvested portion, as of the date of adoption, of previously issued and outstanding awards over the remaining vesting period of such awards. FAS 123R is effective January 1, 2006. The Company is evaluating the impact of FAS 123R on its' results and financial position.

In November 2004, the FASB issued Financial Accounting Standards No. 151 (FAS 151), "Inventory Costs – an amendment of ARB No. 43, Chapter 4". FAS 151 clarifies the accounting for abnormal amounts of idle facility expense, freight, handling costs and spoilage. In addition, FAS 151 requires companies to base the allocation of fixed production overhead to the costs of conversion on the normal capacity of production facilities. FAS 151 is effective for fiscal years beginning after June 15, 2005. FAS 151 did not have a material impact on its results or financial statements.

[16] INVESTMENTS

In accordance with FAS No. 115, "*Accounting for Certain Investments in Debt and EquitySecurities*", securities are classified into three categories: held-to-maturity, available-for-sale and trading. The Company's investments consist of debt and equity securities classified as available-for-sale securities. Accordingly, they are carried at fair value in accordance with FAS No. 115. Further, according to FAS No. 115 the unrealized holding gains and losses for available-for-sales securities are excluded from earnings and reported, net of deferred income taxes, as a separate component of stockholders' equity, unless the loss is classified as other than a temporary decline in market value.

[17] GOODWILL AND OTHER INTANGIBLE ASSETS

In June 2001, the Financial Accounting Standards Board ("FASB") issued Statement No. 142 "Goodwill and Other Intangible Assets". This statement addresses financial accounting and reporting for acquired goodwill and other intangible assets and supersedes APB Opinion No. 17, "Intangible Assets". It addresses how intangible assets that are acquired individually or with a group of other assets (but not those acquired in a business combination) should be accounted for in financial statements upon their acquisition. This Statement also addresses how goodwill and other intangible assets should be accounted for after they have been initially recognized in the financial statements. The Company, in its acquisitions, recognized $893,850 of goodwill. The Company performs its annual impairment test for goodwill at year-end. As of December 31, 2005, the Company has determined that there is no impairment of its goodwill.

MEDIFAST, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
DECEMBER 31, 2005, 2004, AND 2003

NOTE B - SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

In addition, the Company has acquired other intangible assets, which include: customer lists, non-compete agreements, trademarks, and patents. The non-compete agreements are being amortized over the legal life of the agreements ranging between 3 to 7 years. The customer lists are being amortized over a period ranging between 5 and 7 years based on management's best estimate of the expected benefits to be consumed or otherwise used up. The costs of patents are amortized over 5 and 7 years based on their estimated useful life, while trademarks representing brands with an infinite life, are carried at cost and tested annually for impairment as outlined below. Goodwill and other intangible assets are tested annually for impairment in the fourth quarter, and are tested for impairment more frequently if events and circumstances indicate that the asset might be impaired. An impairment loss is recognized to the extent that the carrying amount exceeds the asset's fair value. The Company assesses the recoverability of its goodwill and other intangible assets by comparing the projected undiscounted net cash flows associated with the related asset, over their remaining lives, in comparison to their respective carrying amounts. Impairment, if any, is based on the excess of the carrying amount over the fair value of those assets.

[18] COMPREHENSIVE INCOME (LOSS)

Comprehensive income (loss) is defined as the change in equity of a business enterprise during a period from transactions and other events and circumstances from non-owner sources, including unrealized gains and losses on marketable securities. The Company presents comprehensive income in its consolidated statements of stockholders equity.

[19] RECLASSIFICATIONS

Certain amounts for the years ended December 31, 2004 and 2003 have been reclassified to conform to the presentation of the December 31, 2005 amounts. The reclassifications have no effect on net income for the years ended December 31, 2004 and 2003.

NOTE C - INVENTORY

Inventory consists of the following at December 31, 2005 and 2004:

	2005	2004
Raw materials	$ 1,906,000	$ 1,085,000
Packaging	1,142,000	958,000
Finished goods	2,427,000	2,208,000
	$ 5,475,000	$ 4,251,000

F-16

MEDIFAST, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
DECEMBER 31, 2005, 2004, AND 2003

NOTE D - PREPAID EXPENSES AND OTHER CURRENT ASSETS

Prepaid expense and other current assets as of December 31, 2005 and 2004, consist of the following:

	2005	2004
Marketing and advertising	800,000	478,000
Taxes	779,000	25,000
Commissions	792,000	-
Supplies	393,000	-
Insurance	294,000	273,000
Services	50,000	73,000
Other	165,000	230,000
	3,273,000	1,079,000

NOTE E - PROPERTY, PLANT AND EQUIPMENT

Property, plant and equipment as of December 31, 2005 and 2004, consist of the following:

	2005	2004
Land	$ 650,000	$ 650,000
Building and building improvements	6,871,000	6,728,000
Equipment and fixtures	5,583,000	4,062,000
Vehicle	19,000	11,000
	13,123,000	11,451,000
Less accumulated depreciation and amortization	3,588,000	2,753,000
Property, plant and equipment - net	$ 9,535,000	$ 8,698,000

Substantially all of the Company's property, plant and equipment are pledged as collateral for various loans (see Note J).

Depreciation expense for the years ended December 31, 2005, 2004, and 2003 were $835,000, $804,000 and $421,000, respectively.

MEDIFAST, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
DECEMBER 31, 2005, 2004, AND 2003

NOTE F - TRADEMARKS AND INTANGIBLES

	As of December 31, 2005		As of December 31, 2004	
	(Restated) Gross Carrying Amount	(Restated) Accumulated Amortization	Gross Carrying Amount	Accumulated Amortization
Customer lists	$ 4,356,000	$ 1,398,000	$ 4,355,000	$ 394,000
Non-compete agreements	840,000	566,000	840,000	248,000
Trademarks and patents	1,979,000	121,000	1,703,000	12,000
Goodwill	894,000	-	894,000	-
Total	$ 8,069,000	$ 2,085,000	$ 7,792,000	$ 654,000

Amortization expense for the years ended December 31, 2005, 2004 and 2003 was as follows:

	(Restated) 2005	2004	2003
Customer lists	$ 1,004,000	$ 244,000	$ 127,000
Non-compete agreements	369,000	162,000	86,000
Trademarks and patents	58,000	-	14,000
Total trademarks and intangibles	$ 1,431,000	$ 406,000	$ 227,000

Amortization expense is included in selling, general and administrative expenses.

The estimated future amortization expense of trademarks and intangible assets is as follows:

For the years ending December 31,	Amount
2006	$ 1,125,000
2007	755,000
2008	640,000
2009	462,000
2010	462,000

MEDIFAST, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
DECEMBER 31, 2005, 2004, AND 2003

NOTE G - ACCOUNTS PAYABLE AND ACCRUED EXPENSES

Accounts payable and accrued expenses as of December 31, 2005 and 2004 consist of the following:

	2005	2004
Trade payables	$ 1,695,000	$ 343,000
Accrued expenses and other	-	116,000
Accrued payroll and related taxes	314,000	215,000
Sales commissions payable	254,000	266,000
Total	$ 2,263,000	$ 940,000

NOTE H - OPERATING LEASES

The Company leases office space for its eleven corporately owned Hi-Energy Weight Control Clinics under lease terms ranging from one to five year with leases commencing 2004 and 2005. Monthly payments under the leases range in price from $1,120 to $2,695. The Company is required to pay property taxes, utilities, insurance and other costs relating to the leased facilities.

The following is a schedule by years of future minimum rental payments required under operating lease that have initial or remaining non-cancelable lease terms in excess of one year as of December 31, 2005:

For the Years Ending
December 31,

2006	$ 227,000
2007	191,000
2008	147,000
2009	142,664
2010	53,000
Total minimum payments required	$ 760,664

F-19

MEDIFAST, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
DECEMBER 31, 2005, 2004, AND 2003

NOTE I - INCOME TAXES

Significant components of the income tax benefit for the years ended December 31 are as follows:

	(Restated) 2005	2004	2003
Current:			
Federal	$ 631,000	$ 600,000	$ 973,000
State	181,000	90,000	175,000
Total Current	812,000	690,000	$ 1,148,000
Deferred:			
Federal	$ 157,000	$ 408,000	$ -
State	33,000	61,000	-
Total deferred	190,000	469,000	-
Income tax expense	$ 1,002,000	$ 1,159,000	$ 1,148,000

A reconciliation between the provision for income taxes calculated at the U.S. federal statutory income tax rate and the consolidated income tax benefit in the consolidated statements of income for the years ended December 31 is as follows:

	(Restated) 2005	2004	2003
Provision at the U.S. federal statutory rate	$ 1,102,000	$ 1,087,000	$ 973,000
State taxes, net of federal benefit	170,000	145,000	175,000
Intangible assets	(156,000)	(73,000)	-
Other temporary differences	(98,000)	-	-
Permanent differences	(16,000)	-	-
Income tax expense	$ 1,002,000	$ 1,159,000	$ 1,148,000

MEDIFAST, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
DECEMBER 31, 2005, 2004, AND 2003

NOTE I - INCOME TAXES (CONTINUED)

Medifast, Inc.'s deferred income taxes reflect the net tax effect of temporary differences between the bases of assets and liabilities for financial reporting purposes and their bases for income tax purposes. Significant components of the Company's deferred tax liabilities and assets as of December 31 are as follows:

	(Restated) 2005	2004
Deferred tax assets		
Net operating loss carryforwards	$ -	$ -
Intangible assets	100,000	110,000
Accounts receivable	-	-
Inventory overhead and write downs	-	-
Section 263A	-	-
Total deferred tax assets	$ 100,000	$ 110,000
Deferred Tax Liabilities		
Intangible assets		$ -
Accounts receivable	(37,000)	-
Inventory overhead and write downs	(53,000)	-
Total deferred tax liabilities	$ (90,000)	$ -

The 2005 effective income tax rate of 29.4% differed from the federal statutory rate of 34% due to the amortization of intangible assets, timing differences for other temporary and permanent differences, and state income taxes.

The 2004 effective income tax rate differed from the federal statutory rate due to state taxes, amortization of intangible assets, and for a net operating loss deduction carried forward from 2003.

The 2003 effective income tax rate differed from the federal statutory rate due to state taxes.

MEDIFAST, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
DECEMBER 31, 2005, 2004, AND 2003

NOTE J- LONG-TERM DEBT AND LINE OF CREDIT

Long-term debt as of December 31, 2005 and 2004, consist of the following:

	2005	2004
$2,850,000 fifteen year term loan secured by the building and land at a variable rate which was 7.13% at December 31, 2005	$ 2,201,000	$ 2,391,000
$1,760,000 ten-year reducing revolver line of credit rate at LIBOR plus 220 bps , which was 6.58% on December 31, 2005	1,506,000	1,623,000
$186,976 three-year term loan secured by 20,000 restricted common shares variable rate which was 10.25% at December 31, 2005	59,000	111,000
$200,000 five-year term loan secured by equipment fixed rate was 3% at December 31, 2005	90,000	130,000
$475,000 seven-year loan secured by the building and land at a variable rate at LIBOR plus 250 bps, which was 6.885% on December 31, 2005	428,000	459,000
$366,000 three-year term loan secured by certain assets at LIBOR plus 250 basis points, which was at 6.885% at December 31, 2005	254,000	-
$100,000 unsecured note payable at a fixed rate of 3%, discounted to an incremental borrowing rate of 12%	-	-
Note payable over 3 years secured by vehicle at a fixed rate of 12.25%	-	-
$550,000 agreement three years secured by certain assets of the Company variable rate, which was prime floating at December 31, 2004.	-	-
	4,538,000	4,714,000
Less current portion	561,000	458,000
	$ 3,977,000	$ 4,256,000

Future principal payments on long-term debt for the next 5 years are as follows:

2006	$ 561,000
2007	503,000
2008	356,000
2009	339,000
2010	339,000
Thereafter	2,440,000
	$ 4,538,000

The Company has established a $5 million revolving line of credit at the LIBOR rate plus 1.30% with Mercantile Safe Deposit and Trust Company secured by substantially all of the assets of Jason Pharmaceuticals, Inc. Effective January 17, 2004, $650,000 of the line of credit was converted to a note payable secured by all assets of Jason Pharmaceuticals excluding trademarks at a variable rate at libor plus 250 basis points which was 6.38% on December 31, 2005. The outstanding balance on this line was $633,000 and $369,000 at December 31, 2005 and 2004, respectively.

MEDIFAST, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
DECEMBER 31, 2005, 2004, AND 2003

NOTE K - EMPLOYMENT AGREEMENTS

The CEO of Medifast, Inc., Bradley T. MacDonald, has a two-year employment agreement for an aggregate annual base salary of $225,000 with a bonus potential of 50% of base salary provided the Company makes its profit plan per the Board approved forecast. This contract has been extended to December 31, 2007. Due to the inequities of funding a retirement plan in the 401K, and in recognition of the performance responsible for the turnaround of the Company, the Board of Directors approved a Selective Executive Retirement Compensation Plan funded by the form of deferred compensation. The Deferred Compensation Plan will be funded up to $350,000 by a dollar for dollar match program, having Mr. MacDonald defer $175,000, followed by a Company match of $175,000. In June 2004, the Board of Directors authorized an additional $50,000 to be deferred by Mr. MacDonald followed by a Company match of $50,000. In 2005, the Board of Directors approved the funding of $100,000 into Mr. MacDonald’s Selective Executive Retirement Compensation Plan. This brought the Selective Executive Retirement Compensation Plan total funded value to $550,000. Beginning January 1, 2006 the agreement was modified whereby the deferred compensation will be earned over a 5-year vesting period due January 1, 2011. Mr. MacDonald exercised 13,333 options at $2.67 in July of 2005 and executed 2,000 warrants at $.35 in March 2005.

NOTE L - REDEEMABLE PREFERRED STOCK

In August 1996, the Company sold 432,500 shares of Series “A” nonvoting preferred stock that generated gross proceeds of $865,000, or $2.00 per share. Each share was entitled to a dividend of 8% ($.16) per share. The shares were convertible into the Company's common stock on the basis of one share of common stock for each share of convertible preferred stock. In 2001, 157,000 shares opted to convert to Series “C” Preferred Convertible Stock and 85,000 shares were redeemed under the partial settlement and conversion to Series “C” preferred convertible stock offered to Series “A” preferred stockholders as approved by the Board of Directors. In 2002 the remaining 75,000 shares were redeemed.

NOTE M - SERIES “B” CONVERTIBLE PREFERRED STOCK

In January 2000, the Company was authorized to issue 600,000 Series “B” Convertible Preferred Stock (“Preferred Stock B”) par value $1.00 per share. Each share is entitled to a dividend of 10% of liquidation value $1.00 ($.10) per share and is to be converted on January 15, 2005 unless converted prior thereto. Each holder of Preferred Series “B” stock is entitled to four votes per share in all matters in which holders of the Company’s common stock are entitled to vote. On January 15, 2005, 300,614 shares of Series “B” Convertible Preferred Stock were converted into 601,228 shares of Common Stock. Additionally, a 10% common stock dividend was paid out upon conversion that resulted in 521,158 shares being issued to the Series “B” Convertible Preferred stock investors. As of December 31, 2005 there were no shares of Series “B” Convertible Preferred Stock remaining.

Each share of Preferred Series “B” stock is convertible, at the option of the holder after one year from the issuance date into common stock of the Company. The initial conversion price will be 75% of the market value of the Company’s common stock on the day prior to conversion with a maximum conversion price of $.50 per share subject to adjustment as defined. In March 2002, the Board amended the Series “B” convertible preferred stock terms and conditions as follows (1) a dividend of 10% paid in preferred stock, or (2) cash at the option of the holder. The Board also fixed the conversions of Series

MEDIFAST, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
DECEMBER 31, 2005, 2004, AND 2003

NOTE M - SERIES “B” CONVERTIBLE PREFERRED STOCK (CONTINUED)

“B” preferred at $0.50 per share in common stock and eliminated the spiral conversion provision and reduced voting to 2 votes per share.

NOTE N - SERIES “C” PREFERRED CONVERTIBLE STOCK

In the Fall of 2001, the Company was authorized to issue 1,015,000 shares of Series “C” Preferred Convertible Stock par value (.001), market value $1.00 per share. Each share is entitled to a dividend of 10% of liquidation value $1.00 ($.10) per share and is to be converted on December 31, 2006 unless converted prior thereto. Each Holder of Preferred Series “C” Stock is entitled to one (1) vote per share in all matters in which holders of the Company’s Common Stock are entitled to vote. Each share of Preferred Series “C” Stock is convertible, at the option of the holder, after one year from the issuance date into Common Stock of the Company. The conversion price will be $.50 a share. In 2002, 11,500 warrants issued at $0.35 per share were distributed proportionately to Series “C’ preferred holders.

On August 2, 2005, 200,000 shares of Series “C” Preferred Convertible Stock were converted into 400,000 shares of Common Stock. As of December 31, 2005 there were no shares of Series “C” Preferred Convertible Stock remaining and no additional dividend payments are owed.

NOTE O - WARRANTS

During 2003, the Company issued 200,000 warrants to James Paradis and Anthony Burrascono, both affiliated with Villanova University and 200,000 warrants to Mr. David Scheffler, an investment banker, for advisory and consulting services provided to the Company. The warrants vest in five equal installments of 40,000 warrants per year over a five-year period. These are five-year warrants to purchase common shares at an exercise price of $4.80 per share. These warrants may be cancelled, with a 90-day notice, if the consultants fail to perform to the satisfaction of the Company. During 2005, 120,000 unvested warrants issued to James Paradis and Anthony Burrascono were cancelled. In addition, the Company canceled 120,000 unvested warrants issued to David Scheffler.

During 2003, the Company issued 50,000 warrants to Consumer Choices Systems, Inc. (“CCS”) as part of the payment for the purchase of the assets of CCS. These warrants are three-year warrants to purchase common shares at an exercise price of $10.00 per share. Of this amount, 25,000 warrants were exercised in 2004.

During 2003, the Company issued 63,750 warrants and 18,750 warrants to Mainfield Enterprises, Inc. and Portside Growth & Opportunity Fund. These warrants are five-year warrants to purchase common shares at exercise prices of $16.78 per share, which was equal to one hundred fifteen percent (115%) of the five-day volume weighted average price, all pursuant to the terms of that certain Securities Purchase Agreement by and between the Company and Mainfield Enterprises, Inc. and Portside Growth & Opportunity Fund dated as of July 24, 2003.

During 2005, there were 2,000 warrants exercised at $.35.

MEDIFAST, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
DECEMBER 31, 2005, 2004, AND 2003

NOTE O - WARRANTS (CONTINUED)

The fair value of these warrants were estimated using the Black-Scholes pricing model with the following assumptions: interest rate 4.5%, dividend yield 0%, volatility 0.40 and expected life of five years.

The Company has the following warrants outstanding for the purchase of its common stock:

Exercise Price	Expiration Date	2005	Years Ended December 31, 2004	2003
$0.35	August, 2004	-	-	40,100
$0.35	March, 2005	-	2,000	-
$0.63	September, 2004	-	-	2,500
$4.80	April, 2008	160,000	360,000	400,000
$10.00	June, 2006	25,000	25,000	25,000
$16.78	July, 2008	82,500	82,500	82,500
		267,500	469,500	550,100
	Weighted average exercise price	8.98	$ 7.16	$ 6.49

As of December 31, 2005, 267,500 of the warrants are exercisable.

NOTE P - COMMITMENTS, CONTINGENCIES AND OTHER MATTERS

The Company, like other manufacturers and distributors of products that are ingested, faces an inherent risk of exposure to product liability claims in the event that, among other things, the use of its products results in injury.

NOTE Q - LITIGATION

There was no material pending or threatened litigation against Medifast, Inc. or its subsidiaries as of December 31, 2005.

MEDIFAST, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
DECEMBER 31, 2005, 2004, AND 2003

NOTE R - RESTATEMENTS

The December 31, 2005 financial statements have been restated to recognize an additional $525,000 in amortization expense for a customer list acquired in December 2004. The Company originally assumed an indefinite life on the customer list. Per FASB 142, an estimated useful life for a customer list has to be assigned when the asset is placed into use. As a result, amortization expense should have commenced on January 1, 2005. Pre-tax income decreased by $525,000 from $3,930,000 to $3,405,000 for the year-ended December 31, 2005. Net income for the year ended December 31, 2005 decreased by $324,000 from $2,436,000 to $2,112,000 and retained earnings decreased from $1,149,000 to $825,000.

NOTE S- QUARTERLY RESULTS (Unaudited)

	First Quarter	Second Quarter	Third Quarter	Fourth Quarter
2005				
Revenue	$ 8,326,000	$ 10,555,000	$ 10,985,000	10,263,000
Gross Profit	6,253,000	7,932,000	8,310,000	7,473,000
Operating Income	781,000	1,023,000	1,135,000	610,000
Net Income	426,000	672,000	526,000	488,000
Earnings per common share - diluted (1)	0.03	0.05	0.04	0.04
2004				
Revenue	6,817,000	7,357,000	7,268,000	5,898,000
Gross Profit	5,467,000	5,411,000	5,382,000	4,334,000
Operating Income	919,000	982,000	527,000	576,000
Net Income	647,000	656,000	391,000	35,000
Earnings per common share - diluted (1)	0.05	0.06	0.03	0.00

(1) -Earnings per common share is computed independently for each of the quarters presented; accordingly, in the sum of the quarterly earnings per common share may not equal the total computed for the year.

NOTE T– SUBSEQUENT EVENT- DISPOSAL OF A BUSINESS SEGMENT

On January 17, 2006, Jason Enterprises, Inc., a wholly owned subsidiary of Medifast, Inc. sold certain assets of its Consumer Choice Systems division. Consumer Choice Systems distributes products focused on women's well being to include supplements for menopause relief and urinary tract infections. The sale price was $1.82 million which included $358,000 in inventory, $131,000 in receivables, and $1,337,000 in net intangible assets. Consumer Choice Systems was sold to a former Medifast, Inc. board member. The sale price was $1.8 million and will be recorded as a note receivable by Medifast, Inc. over a 10-year term. The loan is collateralized by 50,000 shares of Medifast, Inc. stock. The following table illustrates segment information from the date Consumer Choice Systems was purchased by Medifast, Inc. on June 11, 2003 through December 31, 2005.

	2005	2004	2003
Revenues, net	$ 958,000	$ 1,498,000	$ 851,000
Cost of Sales	733,000	686,000	343,000
Gross Profit	225,000	812,000	508,000
Compensation and Professional Fees	290,000	213,000	254,000
Selling, General and Adminstrative Expenses	208,000	256,000	212,418
Depreciation and Amortization	209,000	90,000	95,000
Interest (net)	8,000	17,000	8,000
Net income (loss)	(490,000)	236,000	(61,418)
Earnings per share - basic	(0.04)	0.02	(0.01)
Earnings per share - diluted	(0.04)	0.02	(0.01)
Segment Assets	2,216,000	2,625,000	2,497,000
Fixed assets, net of depreciation	54,000	71,000	91,000
Inventory	293,000	391,000	470,000
Prepaid expenses	327,000	-	53,000
Accounts receivable	171,000	629,000	221,000
Intangible assets	443,000	635,000	635,500
Goodwill	893,500	893,500	893,500